Written by **Bruce Walker** on June 6, 2012

Germans Resist Euro Bonds as an Answer to Sovereign Debt Problems

As the European Union struggles with the sovereign debt crisis of its "PIIGS" (Portugal, Ireland, Italy, Greece, and Spain), calls are coming for "euro bonds," which would spread the risk of default among all nations in the eurozone by issuing bonds paid by the eurozone, rather than individual nations. The practical impact would be to allow those nations with serious debt problems to lean upon the better credit rating of Germany. The interest rates on eurozone bonds would be much higher than the current 1.37-percent rate of return on 10-year German government bonds.

Predominant amongst those making the call is Italian Prime Minister Mario Monti, who has stated that he thinks euro bonds will be adopted and that Greece will remain in the single currency of the euro: "I believe we will have euro bonds in one form or another because our union is becoming all the more integrated. However, it must be clear in our minds that issuing euro bonds is not a license to spend and burden others. On the contrary, it is an effort to rebuild Economic and Monetary Union on a more sound and credible basis" and, in reference to the looming problem of Greece electing to drop the euro, Monti said, "I hope Greeks will vote to stay in the euro because this is the best guarantee for a steady future and welfare. I am certain that Greece will stay in the euro zone. The euro zone has made it clear that it will do whatever is necessary to ensure stability and the future of the euro itself."

Germany, which is in much better fiscal shape than the PIIGS, is under pressure to support the euro bond proposal, but the current German government is resisting. Steffen Seibert, of German Chancellor Angela Merkel's office, made this comment several weeks ago: "We are talking about several years [before such bonds should be considered] and certainly not a solution that we are thinking about in the current problematic situation. The federal government believes that euro bonds at the current time are a completely inappropriate means to bring Europe out of the crisis. The chancellor has said many times in public that at the end of a European process — that would take several years — towards a stability union and toward greater political integration in Europe, it is conceivable that at the end of this process, there would be conditions that bring euro bonds closer."

Chancellor Merkel was even blunter last November when she referred to this proposal as "completely impossible," although the Social Democrats in Germany have supported the idea and Green Party leader Jurget Tritten has stated that "joint liability would be limited in both time and scale." France and the European Union bureaucracy also support this idea.

One German official said that a goal of this approach would be this: "We have to get the European Central Bank out of the game of distributing money, and separate fiscal and monetary policy. Germany has only two votes on the ECB Council and no way to control consolidation." There are six members on the European Central Bank Executive Board, which makes decisions for that bank. These six members come from the following nations: Germany (two members), France (one member), Italy (one member), Spain (one member), and Portugal (one member), which means that half of the members are from the PIIGS nations, and France has the swing vote. The new Socialist government of France is likely to be more sympathetic to the PIIGS than the government of Sarkozy.

The European Central Bank has already tried to help the sovereign debt crisis of the PIIGS by purchasing the bonds issued by these nations. As the credit rating of the bonds of the PIIGS grows weaker, the value of those bonds held by the European Central Bank, which have been purchased from those PIIGS nations, lose value as well. Ultimately, it is difficult to see exactly what more the European Central Bank can do to avoid a meltdown of nations like Greece. There has already been some murmuring about possibly letting the ECB have access to the gold reserves of some of these troubled nations. The real crisis — the need of governments to cut spending and reduce debts — remains as politically unpopular in Europe as in America.