



Written by [Bob Adelman](#) on October 27, 2011

The Euro “Deal” — More Questions Than Answers

First, the holders of Greek sovereign debt have voluntarily agreed to accept a write-down of their holdings by 50 percent which would be sufficient, he said, to bring down Greece’s debt-to-GDP ratio from its current level of 150 percent to 120 percent by the year 2012.

Second, in exchange for additional austerity measures, Greece will receive another \$140 billion from the IMF by the end of the year.

Third, the “rescue fund,” or European Financial Stability Facility (EFSF), will be leveraged so that it will have available approximately \$1.4 trillion to loan to countries that get into financial trouble in the future.



Next, the banks affected by the write-downs will be required to raise their net capital ratios from the current five percent to nine percent by next summer, and further austerity measures will be applied to those states applying for financial help in order to qualify for it.

Van Rompuy concluded: “We lay the foundations for our future. All members of the Euro Summit are determined to follow this path.”

There are endless questions about all of this, not the least of which is what trade-offs the banks taking the 50 percent haircut made as part of their “voluntary” agreement. If they aren’t able to raise the required capital from private market sources, would they be able to borrow from the EFSF? Would they be funded by additional government support? In other words, would the ultimate backstop be the taxpayer once again?

Will the insertion of an additional \$140 billion into Greek government coffers provide assurance that Greece won’t need further assistance later on? If their debt-to-GDP ratio doesn’t come down to 120 percent by 2012, what happens then? And is 120 percent manageable? Does this give them room to avoid continuing annual deficits and begin to whittle away at the total debt over time? If the present and proposed austerity measures continue to drag that economy further down, does that reduce the likelihood of managing even that reduced debt service? What’s magical about 120 percent anyway?

The rescue fund is now allowed to be leveraged by some four- to five-to-one to enable it to offer assistance to other countries like Italy and Spain. But isn’t this simply more debt? Why just four- or five-to-one? Why not 10-to-one, just to be safe? Isn’t debt what got these countries into trouble in the first place? And by the way, where did the initial funding for the EFSF come from? [It turns out](#) that it’s all funny money, with the EFSF being initially funded by contributions from the various nations who are seeking financial assistance from the fund. But the EFSF can issue bonds, using “guarantees given by the euro area member states in proportion to their share in ... the European Central Bank.” The EFSF can also use the European Union’s budget as collateral for those bonds. If this is beginning to sound like



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a papier-mâché labyrinth one wouldn't be too far wrong.

What if the austerity measures being imposed on Greece (and about to be amped-up in order to qualify for the next check from the IMF) continue to fail to work? It reminds one of the saying on a slave-ship: "Beatings will continue until morale improves."

In her analysis of the so-called "deal," *Marketwatch*'s Sarah Turner [noted that](#) the trade group representing the banks taking the haircuts, the Institute of International Finance, "would work with Greece, euro-zone authorities and the International Monetary Fund to develop a concrete, voluntary agreement that should set the basis for a decline in Greece's debt to GDP ratio to 120% by 2012.... The specific terms and conditions of the voluntary [private-sector involvement] will be agreed by all relevant parties in the coming period and implemented with immediacy and force." In other words, there isn't anything in writing yet, just a general idea that sometime in the future, the Institute "would work with Greece ... to develop ... an agreement ... that should set the basis."

Observers were quick to point out the flimsy ethereal nature of the agreement so laboriously birthed in Brussels. Jonathan Loynes, chief European economist for Capital Economics, noted drily that "the plans announced by euro-zone policy makers overnight look more like a pea shooter than the 'bazooka' promised [earlier] to tackle the region's problems." To Ambrose Evans-Pritchard, [writing in](#) the *UK Telegraph*, "The unpleasant truth is that [these] proposals are idiotic, the worst sort of financial engineering, legerdemain, and trickery."

At bottom, these phony and chimeral agreements reflect the reality of using paper money to solve the problems created by paper money. As an anonymous author has said:

The world will soon wake up to the reality that everyone is broke and can collect nothing from the bankrupt, who are owed unlimited amounts by the insolvent, who are attempting to make late payments on a bank holiday in the wrong country, with an unacceptable currency, against defaulted collateral, of which nobody is sure who holds title.

Photo of Herman Van Rompuy: AP Images



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