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The Greek Crisis: Immediate Collateral Damage

di Sandro Leipold

Europe's attention these days is totally devoted to Greece – and understandably so, given the critical stakes at hand. Quite aside from how this latest installment of the euro crisis will end, the concentration of attention on Athens has however immediate costs for everyone, in three ways: it undermines confidence, perpetuates a misread of the crisis, and distracts from the required growth initiatives.

At first glance, it may seem that euro-wide confidence has held up relatively well in the face of the Greek flare-up. Market volatility has clearly increased, but there has been no meltdown. On the contrary, equity markets reached new peaks, clinging to any faint hint of a possible agreement on Greece. Spreads on government bonds have remained narrow, at all-time lows. It is however reasonable to presume that the flywheel of increased confidence would now be turning with greater vigor were it not for the concerns emanating from Athens. There has been an unexpected confluence of positive factors, with the simultaneous decline in oil prices, the depreciation of the euro, and the advent of ECB quantitative easing. This clearly favorable constellation has been eclipsed however by Greece's shadow. The most ominous cloud is the one hanging over the ECB's QE. It is generally recognized that the instrument's effectiveness in Europe is stymied by a variety of structural factors, and its impact on growth was expected to derive mainly from its hoped-for confidence effect.

While contagion risks are certainly reduced compared to 2010-11, uncertainty – inimical to entrepreneurship and investment – remains high. The assurances that stronger firewalls are now in place are moreover unconvincing. The only new bulwark is provided by the ECB's Outright Monetary Transactions (OMTs), which managed to calm the markets from the instant of their announcement in the summer of 2012. But these are now inoperative, relegated to a legal limbo between Karlsruhe and Strasbourg, beyond the reach of even as brave a policymaker as Mario Draghi. Even if their legal uncertainty were to be dispelled, their use would require agreement on a program by any potential beneficiary. This would need to take the form of a precautionary program, by the unfortunate name of an “enhanced conditions credit line,” that all potential candidates (Ireland, Portugal, Spain) have so far spurned. Such lack of demand has not however prompted any rethink of its modalities by the ESM or its governors (the Eurogroup ministers).

A second lamentable effect of the return of Greece to center stage is that it perpetuates a misleading narrative of the euro crisis. This reading it that the crisis is primarily due to the profligacy of peripheral countries, accustomed to living beyond their means, at the expense of the virtuous north. Part of this vignette are early retirements, lengthy holidays, public sector patronage, extensive tax evasion, and so forth. In this regard Greece is a “perfect culprit” in the eyes of the northern European voter. This interpretation of the crisis is however clearly shallow; it certainly does not fit the reality of Ireland or Spain, nor very well that of Portugal. However, it remains the dominant one in the core of the euro zone, also because irresponsibly nourished by political leaders. It is now back in full force, hardening prejudices and further tearing at Europe's socio-political fabric. As noted by Jean Pisani Ferry and others, the narrative of the crisis, and probably also its evolution, would have been quite different had the first country to ask for support been Ireland rather than Greece.

Finally, the return to prominence of the Greek crisis is distracting attention from what really remains to be done: the long-awaited policies for growth. The Juncker investment plan has yet to attract a single euro in contributions from member countries, and its full entry into operation remains in a distant future.

Furthermore, whatever happened to the absolute “policy priority” launched with much fanfare at the September 2014 informal Council meeting in Milan? It was an excellent proposal, which would have represented a first real coordination of structural reforms - in this case, a collective reduction of the tax wedge in 11 euro area countries. There has been no further mention of the initiative, and it seems to have fallen by the wayside.

The return of the Greek crisis should at least induce a self-critical reflection within the euro area. The distressing fact, however, is that the eurozone is bereft of any means of self-assessment from which to draw lessons from the past, learn from its mistakes, and adjust accordingly. In this regard, it could usefully look at the practices of the International Monetary Fund, which has well-established procedures to review its work, criticize it if necessary (as it did on Greece in June 2013), and to adapt its approach. Without these procedures, the euro area seems destined to persevere in its errors. The euro crisis continues to be, as from its start, a crisis of governance, and so it will remain as long an intergovernmental approach prevails. That is, one may legitimately fear, sine die.

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