FINANCIAL TIMES

July 15, 2015 6:23 pm

A generous deal that avoids austerity

Lars Feld

Share Author alerts Print Clip Comments

Without these funds, the Greek economy would break down, writes Lars Feld

Some say it was a German-led coup and a humiliation for Greece. But this interpretation of last weekend's summit of eurozone leaders is totally misleading. It blames the fire brigade for putting out the fire.

Since 2009 the financial situation of Greece has been characterised by a lack of funds. Taxpayers did not want to finance their government any more and most of them transferred their money abroad. Greece's creditors did not want to finance another round of excessive spending and withdrew their money. As Margaret Thatcher foresaw, the problem with socialism is that you eventually run out of other people's money.

It was necessary to douse the flames lest they spread elsewhere in the eurozone. So Greece received money from taxpayers in other countries, in exchange for stopping its excessive spending and reforming its economy. This principle has guided International Monetary Fund programmes for a long time. It neither undermines democracy nor erodes sovereignty. Countries that do not want to comply with such programmes need not apply for them.

After almost €200bn of bailout funds and two debt restructurings, the Greek people voted for a government promising to stop the pain without losing market access. Yet now creditors have refused to finance excessive spending.

This time there has been no contagion; interest rates for other eurozone members have remained largely unaffected. Still, the creditors have offered additional funds in exchange for a credible commitment to conduct reforms and transform Greece into a market economy. Against that, the approach of the Athens government has destroyed its credibility. It must now show its willingness to reform and privatise.

This outcome has nothing to do with German stupidity or its supposed reliance on ordoliberalism, an allegedly outdated economic theory from the 1940s. The theory is not outdated — but neither is it one that Berlin has blindly followed. Had it followed the "ordoliberal" way, Germany would not have helped bail out Greece, and then Ireland and Portugal, as well as the Spanish banks. It would not have supported Mario Draghi's promise to do "whatever it takes" to save the eurozone and would not have stayed calm after the president of the European Central Bank announced that it would buy assets with newly minted money. Instead, it would have enforced the liability principle under which people are responsible for the consequences of their decisions.

Monday's agreement provides funds in exchange for collateral, namely the credible promise of reform. Without external funds, the Greek economy would break down even more dramatically than it has. Wages and pensions would not be paid. The deal does not impose austerity. It is the only way of avoiding it.

Should there be another debt restructuring? Not now and not without reforms. In March 2012, private creditors accepted a loss in present value terms of about 70 per cent. In November 2012, eurozone members accepted a loss in present value terms of about 50 per cent. Now it is time for Greece to modernise its economy and its public administration, privatise state-owned enterprises and balance its budget. With interest payments of about 2 per cent of output on public debt, a growth rate of 2 per cent would already help to get out of excessive indebtedness. Sustainable economic growth does not result from another round of excessive deficit spending, but originates from a transformation to a market economy. Wolfgang Schäuble is right.

The writer is a member of the German Council of Economic Experts

Letters in response to this article:

If this is 'generosity', then heaven help us all / From Joseph Zammit-Lucia

Let's stop using the word 'austerity' — what we're talking about is 'reality' / From Ronald Lansdell

RELATED TOPICS Greece Debt Crisis, Greece Politics

Share Author alerts Print Clip Comments