

## EURO HOPES DASHED

Last week Eurozone leaders worked late into the night to produce a package to save Greece from bankruptcy and keep it in the Eurozone. Greek national debt is 160% of its GDP and without that help it would default on its debt and seriously damage the financial institutions that hold that debt. It was agreed to ask those institutions to write off 50% of the debt and to create a bail-out fund of €1 trillion to support Greece and other deeply indebted Eurozone economies. They believed that this was sufficient to convince the markets of their determination to preserve the Euro and went home satisfied.

The Greek Prime Minister, George Papandreou, has now thrown that deal into the melting pot by deciding to hold a referendum on it next January. From a democratic perspective, the idea that the people who will bear the brunt of the austerity measures required of Greece should be asked to give those measures their support is admirable and an example that other European leaders should follow. Politically, Mr Papandreou probably had no other choice than holding a referendum. He leads a coalition Government that appears shaky. There have already been many demonstrations against the austerity measures and further expenditure cuts could lead to a breakdown in public order.

Chancellor Merkel and President Sarkozy almost certainly fear the worst – that the Greek people will reject the conditions of the bail-out plan - and they are livid with Mr Papandreou for the risk he is taking, that could wreck the deal they worked so hard to create. If that is the result of the referendum Greece would probably have to leave the Eurozone and revive the drachma as their currency. Without the bail-out funds Greece would presumably default on its debts, threatening the survival of the banks and others holding that debt.

The markets understand this and the value of the Euro is likely to fall. Economic growth is weak in Europe and this development could push the Eurozone into recession. If Italy and Spain need bailing out next year, the future of the single currency could be in real doubt. There is a G20 meeting this coming weekend, chaired by President Sarkozy, and if he and Angela Merkel use it as an opportunity to assert their determination to preserve the Euro, that might persuade the markets to give them more time to do so. They would need to erect ‘firewalls’ to prevent the Greek contagion from spreading into other member economies and take a tougher line on national policies that could undermine the Euro. In the longer term they will aim to persuade Eurozone countries to integrate their economies more closely, with common fiscal as well as monetary policies. The inherent weakness of the Eurozone is that its members wanted the benefits of a common currency without the obligations of a single economy.

The UK is not a member of the Eurozone and our banks are said to hold very little of the Greek debt. However, Europe is our largest export market and if it goes into recession that will inevitably affect us. The latest statistics reveal that our economy is growing at 0.5%, which is better than some forecasts but hardly enough to make us immune from the impact of a Eurozone recession.

The Eurozone economies integrating with common economic policies will raise serious issues in British politics because of the potential for creating a two tier membership of the European Union. Those nations not in the Euro were absent from last week's meetings about the Greek bail-out, which could be a portent of future EU development. UK membership seems to be returning to the national debate, with increasing pressure for the repatriation of powers from the EU to our own Parliament and Government. It remains to be seen whether the outworking of the present crisis will help or hinder that aspiration. President Sarkozy's sharp words about not wanting Britain's advice about the Euro since we have no part in it could lead to a conclusion that if we want to opt out of so much, perhaps we should opt out completely. That might please some people but not our exporters or those who voted for membership to create an alternative to war as a means of settling our differences.

Martyn Eden

2.11.2011