



A Big Move by the EU and the IMF

Anders Åslund favorably assesses the latest steps to insulate the rest of Europe from the financial crisis in Greece.

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Steve Weisman: The reviews and the markets have reacted favorably to the latest action by the European Union and the International Monetary Fund to protect Europe from instability resulting from the problems in Greece. Anders Åslund, senior fellow at the Peterson Institute for International Economics, is here with me, Steve Weisman, at the Institute to talk about the latest development. Thanks, Anders.

Anders Åslund: My pleasure.

Steve Weisman: First, what did the European Union and the IMF do that was different this weekend?

Anders Åslund: Essentially they did everything that they should do. They put up enough money on the table. They abandoned this bizarre no-bailout clause and read another clause in the European treaty that allows you to bail out countries. And they imposed strict fiscal action against Portugal and Spain because their problem is mainly too large budget deficits and not too large public debt. They also allowed the European Central Bank to do quantitative easing—to buy government bonds, and not only government bonds but also private bonds, exactly what the Fed has already done. And in order to improve fiscal standards, they have imposed IMF discipline. So essentially, they have done everything that people asked them to do.

Steve Weisman: What does Greece have to do?

Anders Åslund: You can say that the Greek problem remains but it has been isolated. The big question that remains is if Greece doesn't need to write off half of its debts, \$200 billion. But we don't need to deal with that for now because the EU-IMF program for Greece has taken care of it so that Greece doesn't need to go out for any market financing for at least two years.

Steve Weisman: So Greece is still going to struggle with this austerity program and there are still doubts in your mind and the minds of others that it can do that without a debt restructuring, but you're saying this can be now insulated.

Anders Åslund: Yes. The important issue was to avoid contagion to Portugal and Spain or other countries, and that was essentially taken care of.

Steve Weisman: Let's talk about a few of these one by one. There's been talk for the last month or two that the European Union treaty forbids bailing out governments from financial difficulties, but you just said that they found a clause in the European Union treaty that is sort of an escape hatch on that. How did they do that? Why did it take so long?

Anders Åslund: I don't understand why they haven't referred to this article before. It's Article 122.2 in the revised EU treaty and it reads like this: where a member state is in difficulties or is seriously threatened with severe difficulties caused by natural disaster or exceptional occurrences beyond its control, the council on a proposal from the commission may grant, under certain conditions, union financial assistance to the member state concerned. To me, this sounds totally obvious that Portugal and Spain are now in trouble because of Greece and not because of themselves and that should comply with this article.

Steve Weisman: So Greece is sort of like Hurricane Katrina here.

Anders Åslund: Indeed.

Steve Weisman: For Spain and Portugal, who've had a virtuous more or less conduct in the fiscal area. But they still need to take some further steps, according to what was agreed this weekend.

Anders Åslund: Yes, you can say that their problem is big budget deficits, which are beyond the Maastricht criterion, far beyond it. But the public debt is far below the Maastricht ceiling of 60 percent of GDP in public debt.

Steve Weisman: So Spain and Portugal can get there without too much trouble?

Anders Åslund: Yes. They need to cut their public deficits very substantially, and that's what the European Union now says very promptly. And it should also bear interest, of course, as a deflationary policy, but that is difficult to get away from.

Steve Weisman: Other countries have had to do that, including countries in Eastern Europe.

Anders Åslund: Yes. If you look up on the EU members in the Baltic states, Latvia will probably take a decline in GDP of a total of 25 percent during three years; Lithuania and Estonia, which have managed without any IMF or EU program, have taken each a decline in GDP of 17 percent.

Steve Weisman: That's tough, though.

Anders Åslund: Yeah. But this is reality. You can't live beyond your means and this is what Southern Europe and the European Union are now facing up to.

Steve Weisman: Another step that you mentioned that's a dramatic change in policy is that the ECB, the European Central Bank, is going to actually buy bonds of what? Private companies? Governments? How is that different from what it had earlier said it would do?

Anders Åslund: Previously, they have just refused to do this. They have taken government bonds as collateral for repo operations, for repurchasing operations. But now they are actually intent on buying bonds and essentially adopting the policy that the Fed has pursued—

Steve Weisman: Since 2008.

Anders Åslund: Yes, and quite successfully, I would say, in the United States. So all of a sudden, the European Union has adopted the things that were necessary for it to function.

Steve Weisman: Speaking of the Fed, how much do you think the Fed and the US Treasury were involved in the discussions over the weekend? There are some reports of Vice President Biden and President Obama making public statements. I think the Fed also announced some swap arrangements over the weekend as well.

Anders Åslund: Yes, the swap arrangements are quite substantial and important. And clearly for the last week, US government officials in a broad range have been deeply involved in the European crisis.

Steve Weisman: Anders, do you think this crisis response reflects a recognition that if the European situation continued as it was going, it really did threaten the global economy the way that Lehman Brothers did in 2008?

Anders Åslund: It did. I think that this was a Lehman Brother collapse that was underway for the last week. And now it looks as if it could have been stopped.

Steve Weisman: What are the risks that it won't be enough?

Anders Åslund: I don't think that the risk is that it won't be enough but that for some reason, one legal reason or the other, the action that has been announced cannot be carried out. So it's up to the lawyers to cause the trouble now.

Steve Weisman: There will be a constitutional challenge, but it sounds like they found a basis for the action.

Anders Åslund: Yes, as a layman when you read this Article 122.2, it sounds totally obvious with regard to the other EU countries that they are hit by what Greece has done.

Steve Weisman: Based on your understanding of European politics, do you think there's some sort of European version of the Tea Party movement that's going to try and block this?

Anders Åslund: I doubt that.

Steve Weisman: Okay, Anders. Thanks very much.

Anders Åslund: Thank you.

