

Greece dependent on the patience of German taxpayers

SO THE world breathes a sigh of relief that Greece has elected a government committed to the bailout program. This means that European authorities will finance the restructure of Greek debt and keep Greece in the euro for now. But that only buys time. If Greece is going to continue to access finance and, more importantly, pay the interest cost on its borrowing, it will have to make its real economy a whole lot more competitive.

Greeks have been paying themselves pensions and wages that they can't afford. Tax collection is hopelessly inefficient. And business is well below international competitiveness.

In the old days, when Greece got into this situation it would devalue its currency. As a result, the Greek people would reduce their standard of living against international standards and



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In the debate over the euro, only one nation's voice really counts.

industry would become more competitive. But after it went into the euro, Greece lost the ability to use the currency to adjust its economy. What's more, once inside the euro it found that lenders asked for lower interest rates since they thought there was now no currency risk on government bonds, and they

assumed that if Greece got into trouble Europe would bail it out and look after the lenders. Which it has. So money became plentiful and cheap. And Greece borrowed more, up until the point that lenders began to lose confidence and turned off the tap.

Devaluation would be the fastest way for Greece to restructure its economy. Without it the path to competitiveness is going to be a whole lot harder. The bailout package requires the government to cut pensions, reduce the number of public servants and get costs under control. This is known as the "austerity" option.

There are some who say there is an easier way. They say that there should be a program to stimulate growth and boost revenue, which might even involve more spending. This is known as the "growth" option. German Chancellor Angela Merkel is in

the austerity camp and French President Francois Hollande wants the "growth" option.

In this debate only the Germans really count because they are the ones that are going to stump up the money. They can afford to help because, unlike most of Europe, they practise austerity and thrift. And if German taxpayers are going to have to pay higher taxes, they think their European brothers and sisters should share some of the pain.

The proponents of austerity and growth have different temperaments and different time frames, too. A boost in spending might help in the short term, but in the longer term getting costs down and productivity up will pay off. The question is whether the Greek voters will wait that long.

Short-term decision-making is how Europe got into this

problem in the first place. All through the 1990s and 2000s the countries that are now in trouble continued to run large budget deficits in the name of stimulation and expansion. They found it was always a good time to spend. They never seemed to think it was the right time to cut spending and get debt under control.

Which brings us to another interesting participant in this debate. At the recent Camp David G8 summit, President Barack Obama clashed with Chancellor Merkel over her plans to deal with the euro crisis. The White House wants more expansionary policy. Obama has since claimed that the European crisis is "starting to cast a shadow on our own economy". At present, US unemployment is at 8.3 per cent. The conventional political wisdom in the United States is that the President needs a seven

in front of that number to guarantee re-election. The shadow he is seeing is the newly competitive Mitt Romney rising in the opinion polls.

So the US will advocate its recipe for the European crisis from the sidelines. It's weird to see America urging Europe to spend more. They hardly need encouragement. The US would have some influence if it was putting money on the table to pay for it. But its own deficit and debt problems are of European proportions, and because of those problems it is in no position to underwrite Europe's.

Which brings us back to Chancellor Merkel. Ultimately the people who will decide this are the people who will pay for it. And her country is pretty much on its own when it comes to that.

Peter Costello was federal treasurer in the Howard government.