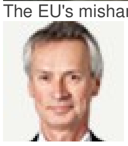
The Telegraph

Greek candidate willing to call European leaders’ bluff

Alexis Tsipras told Greek voters as recently as last week that his government would cease to enforce the bail-out demands

The EU's mishandling of Greece has been calamitous Photo: Getty Images



By **Ambrose Evans-Pritchard**

9:55PM GMT 10 Dec 2014

350 Comments

Events have rudely exposed the illusion that Greece's people will submit quietly to a decade of colonial treatment and debt servitude.

As matters stand, it is more likely than not that a defiant Alexis Tsipras will be the elected prime minister of Greece by late January. His Syriza alliance has vowed publicly and persistently that it will overthrow the EU-IMF Troika regime, refusing to implement the key demands.

A view has taken hold in EU capitals and the City of London that Mr Tsipras has resiled from these positions and will ultimately stick to the Troika Memorandum, a text of economic vandalism that pushed Greece into seven years of depression, with a 25.9pc fall in GDP, longer and deeper than Europe's worst episodes in the 1930s.

Mr Tsipras is a polished performer on the EU circuit. He can no longer be caricatured as motorbike Maoist. But the fact remains that he told Greek voters as recently as last week that his government would cease to enforce the bail-out demands "from its first day in office".

The logical implication is that Greece will be forced out of the euro in short order, unless the EU institutions capitulate. Syriza's deputy, Panagiotis Lafazanis, is plainly willing to take this risk, warning in October that the movement must "be ready to implement its progressive programme outside the eurozone" if need be. His Aristeri Platforma holds 30pc of the votes on Syriza's central committee.

Mr Tsipras also knows it. He is gambling that EU leaders - meaning Germany's Angela Merkel and Wolfgang Schauble - will yield. His calculation is that they will not dare to blow up monetary union at this late stage, and over a relative pittance,

Too much political capital has been invested. The EU-IMF loans have already reached €245bn, the biggest indenture package in history. To let it fall apart now would reveal the failings of their EMU crisis management.

The clock is already ticking. Greece must repay €6.7bn to the European Central Bank in July and August. The ECB will not roll the debts over because that would be monetary financing of a government. The capital markets are shut.

Mr Tsipras is expecting to receive a call from the ECB within weeks of taking office reminding him that Greece owes some €40bn in support for the banking system. This will be a veiled threat to pull the plug, as it threatened to do in Ireland, and came close to doing in Cyprus.

I am reliably informed that his answer to any such call will be: "do your worst". Mr Tsipras wishes to keep Greece in the euro but not at any price.

"We are not going to crumble at the first hurdle," said one of his close advisers. "A freshly elected government cannot allow itself to be intimidated by threats of Armageddon. The ECB bought these bonds to stem the eurozone crisis, not to help Greece."

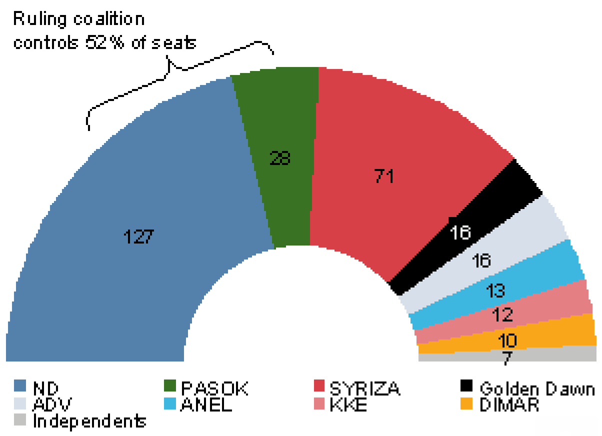
Needless to say, markets are taking fright. The Athens bourse fell 13pc on Tuesday, the biggest one-day drop since the 1987 crash.

Yields curve on three-year Greek debt have exploded by almost 300 basis points to 9.52pc in two days. They are now 90 points higher than 10-year yields, a violent inversion of the yield curve unseen since default scares of the EMU crisis. Italian and Portuguese yields have been ratcheting too, early evidence of where contagion risk still lies.

The Syriza road show in the City last month went horribly wrong. "Everybody coming out of the meeting wants to sell everything Greek," said a leaked memo by Capital Group's Joerg Sponer.
The reported shopping list was: a haircut for creditors; free electricity, food, shelter, and health care for all who need it; tax cuts for all but the rich; a rise in the minimum wage and pensions to €750 a month; a moritorium on private debt payments to banks above 20pc of disposable income; €5bn more in EU subsidies; and demands for 62pc debt forgiveness on the grounds that this is what Germany received in 1952. "The programme is worse than communism (at least they had a plan). This will be total chaos," said Mr Sponer.
"It was a disaster," said Professor Yanis Varoufakis from Athens University, a man tipped to play a key economic role in any Syriza-led government. The reality is more prosaic. "We are not going to go on a spending spree. We will aim to achieve a modest primary surplus, and we will liberalize the labour market," he said.
"Greece faces a humanitarian crisis and we will spend €1.3bn to alleviate abject poverty. There will be US-style food stamps and we will reconnect electricity to homes where it has been cut off," he said.
"There will have to be debt relief because it is simply unpayable. We will ask Germany to renegotiate," he said. Most of the remaining debt is owed to EU bodies, which replaced private creditors long ago.
The proposal is based on "Bisque bonds" floated by John Maynard Keynes in the 1930s. The idea was explored by Nobel laureate Joseph Stiglitz and Daniel Heymann in their book "Life After Debt".
The bonds would be new issues with payments linked to the rate of GDP growth. Greece has already issued such bonds under its 2012 restructuring. Mr Tsipras wants this extended to all the debt, and on better terms. If EMU leaders believe their own tale that Greece can grow its way out of debt at rates of 3.5pc or 4pc, they should have no fear agreeing to such terms.
This is the Tsipras plan. It is high stakes poker. We know from kiss-and-tell books - such as "Morire di Austerità" by ex-ECB board member Lorenzo Bini-Smaghi - that Chancellor Merkel came within a whisker of ejecting Greece from the euro in 2012. She relented only when it became clear that Italy and Spain were going up in flames.
The eurozone now has firewalls in place. There are - in theory - back-stop mechanisms to bolster confidence. Richard McGuire from Rabobank says the prospect of QE may embolden some to think they can cope with the systemic fall-out if Greece were "allowed to go it alone", in other words if it were kicked out.

It may not come to this. Premier Antonis Samaras may yet find 25 opposition MPs to support his candidate for the Greek presidency in parliamentary votes this month. Only if he fails to win a 60pc super-majority will there be a snap general election.

Composition of the Greek Parliament



Source: RBS Credit Strategy, Wikipedia

The latest Alco poll gives Syriza 31pc support, with Mr Samara's New Democracy holding at 25.7pc. This lead has been stable for months. The winner gets an extra 50 seats under the electoral law. Syriza will need a coalition partner - probably the pro-EU Potami party - but its ascendancy looks clear.

The EU's mishandling of Greece has been calamitous. Investment has fallen by 63.5pc. Public debt has spiralled to 177pc of GDP, even after two sets of haircuts on private creditors.

Unemployment has dropped slightly to 25.9pc, or 49.3pc for youth, but only because of a mass exodus, a brain-drain to the US, Canada, Australia, Germany, and the UK. The work force has shed over a million jobs, dropping to 3.5m.

The economy has stabilized. It grew 0.7pc in the third quarter on pent-up demand. But this should not be confused with recovery or a return to viability within the EMU fixed-exchange system. Exports were lower in 2013 (€51.6) than in 2007 (€56.6bn). The current account deficit has narrowed because imports have collapsed.

For all the talk of EU-led reform, Greece's ranking on the World Economic Forum's competitiveness index has dropped from 67 to 81 over the last six years, below Ukraine, Guatemala, and Algeria.

"The concept of reform has been gradually discredited during the current crisis," was the acid verdict of the Athens think-tank IOBE in its latest report. Any marginal gains from EU reforms have been overwhelmed in any case by the hysteresis damage of lost labour skills, which lowers Greece's future growth trajectory.

Stripped bare, it has been brute austerity, imposed by powerful foreign creditors in their own interest. My view is that Greece would have recovered long ago if it had left EMU at the outset of the crisis, turning to the IMF for a classic bail-out package. It received the IMF's austerity medicine, but not IMF's the cure of debt forgiveness and devaluation. The fiscal multiplier did its worst with nothing to offset it.

Debt relief was blocked. The Troika imposed yet more debt onto a country that was already bankrupt, allowing foreign banks and investment funds to dump their bonds onto Greek taxpayers through the mechanism of EU "bail-outs". These were not in fact bail-outs. They were loans. The burden remains entirely on the shoulders of the Greek state, though you would not know that from reading the North European press.

The IMF admits in its mea culpa that Greece needed debt relief from the start. Normal rules were violated, under EU pressure, because the primary goal was to hold EMU together. The assumption was that any hint of debt restructuring for Greece risked setting off an uncontrollable chain-reaction through southern Europe.

“Debt restructuring should have been on the table,” said Brazil's member of the IMF board, in leaked minutes from a meeting in May 2010. The loans “may be seen not as a rescue of Greece, which will have to undergo a wrenching adjustment, but as a bailout of Greece’s private debt holders, mainly European financial institutions”.

The Troika's fear of contagion was justified, as the unfolding drama would later show. The deformed construction of EMU amplified the stress, and the dangers. It is easy to forget how close we were to a systemic blow-up at that moment, in the white heat of the crisis, before the ECB had begun to fulfil its primary duty as a lender of last resort, and before any EMU rescue machinery was in place.

Greece was sacrificed to buy time for the alliance, like the Spartans at Thermopylae. It was subjected to an unworkable economic experiment, in defiance of known economic science and principles. Given what has happened, Europe’s leaders have a special duty of care to Greece. They have betrayed it.

Europe's contractionary policies have failed on every level. The region has not regain "escape velocity" since the Lehman crisis, and is now sliding into deflation. Output is still below 2008 levels and has performed worse over the last six years than from 1929 to 1935. Debt ratios are rising across the South.

The centre-Left has proved unable to articulate any critique because of EMU's political code of Omerta. The once great parties of European social democracy have become grim enforcers of reactionary policies, apologists for mass unemployment.

So it falls to rebels to catalyze the simmering rage. Europe's leaders may have met their match at last in the ice-cold Mr Tsipras.