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Will the Euro Survive?

The Greek crisis may well prompt the unravelling of the eurozone, but the European Union should not see this as a threat to its existence

Angela Merkel, the German Chancellor, declared yesterday that "the euro is in danger". She is surely right. It seems increasingly likely that the currency bloc will fracture or shrink, losing at least one of its sixteen members, although the gargantuan €750 billion international rescue this month has bought it time.

Fund managers in London, reckoning that the chances are rising that Greece, Portugal or even Germany will leave the currency, are speculating on how, exactly, a country could do that. Lawyers in Athens have been musing on the possibility of a return to the drachma. Those around George Papandreou, the Greek Prime Minister, say that a return to the old currency is not yet a likelihood, but nor do they dismiss it as an impossibility. The notion of any country leaving the euro was supposed to be unthinkable; now, it is actively being considered across Europe.

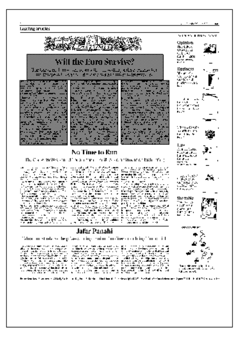
Why is the euro in such trouble? The global financial crisis exposed flaws in Europe's shared currency that were there from the start. The euro is a union between the very different economies of Europe's rich north and poorer south. Helmut Kohl, the former German Chancellor, and "father of the euro", overrode concerns that the Mediterranean nations had not reformed enough to join. Nor did eurozone rules curbing debt and deficits have much effect in prompting change, given that France and Germany were the first to break them.

In the wake of the global financial turmoil, Greece revealed that it might not be able to make repayments on its debts. That sparked a crisis of confidence about government debt across Europe. The panic spread to Portugal, Spain, Ireland and Italy. Next in line after that, traders warned, was Britain. Stemming that crisis has come at huge cost. The rescue package, put together by the EU, the European Central Bank (ECB) and the International Monetary Fund, is more than five times the Union's annual budget.

But the bailout has not solved the crisis. It raises the question of whether Greece, perhaps Portugal or even Germany itself might leave. Greece faces a near-impossible task: to cut its budget deficit from 14 per cent to under 4 per cent in three years. Riots are subsiding, but cuts may trigger a recession that could make debt payments impossible. It is hard to see how Greece can grow without devaluing its currency, to make exports competitive, yet while it is in the euro it cannot do that. While talk of leaving has faded since the bailout, the taboo has been broken. In Germany, by contrast, there is live debate about whether membership is really in the national interest. Germany's share of the bailout is €123 billion, and taxpayers are furious at rescuing profligate southerners. Nor have they welcomed calls for tighter control of the finances of eurozone countries. That would cramp their independence, and threaten to make a habit of transferring their hard-earned surpluses to the south.

How could any country leave? Euro membership is supposed to be a one-way ticket. Yet bankers and lawyers are becoming fluent in the options. One would be to leave overnight to prevent a run on banks. But the lack of warning would enrage the ECB; that option is unattractive unless a bank run started, making it unavoidable. A controlled exit, some muse, might begin by curbing the convertibility of the new currency, perhaps offering it in electronic form.

The euro was always more of a political romance than an economic project. The turmoil of its disintegration would be immense. But the value of shoring up the club dwindles if it may be in the best interests of some members to leave. A threat to the euro is not a threat to Europe, after all. EU members should not confuse defence of the euro with the interests of a successful union of 27 countries with shared values and trade.



L'euro sopravviverà? (pds)