The Euro Tragedy

— Raj Nair

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By **Mr. Raj Nair,** Chairman of Avalon Consulting

Some call the crisis that is unfolding, a Greek tragedy. I would prefer to name it by one of the root causes. Greece would have faced tough times even if it had its own currency but would have had room to manoeuvre like many nations around the world have, other than those in Euro zone and it may not have come to such a sorry pass as now. The key short term tools that countries facing difficulties use are devaluation when the economy has become uncompetitive and inflation when they overladen with debt. By virtue of having a common currency across 19 countries, the Eurozone is like a man with his head in the oven and legs in the freezer, trying to pretend that on an average he is O Kay. None of them are O Kay. Countries which are doing relatively well feel that the poor performers are dragging them down whereas the ones in trouble feel that the better-off nations have imposed too many restrictions on free movement of trade, labour, etc. This is the Euro Tragedy. Puerto Rico, the dollar economy which is part of the US Commonwealth, better known as the home of Bacardi, is another case in point; it threw up its hands over this weekend to say that it is broke and cannot honour its debt. Neither Greece nor Puerto Rico can devalue its currency. Euro and the US Dollar are in some sense 'pegged' to the productivity of the Mainland and Germany/ Northern Europe, leaving the laggards with limited options to recalibrate their currency against its economic situation. Greece and Puerto Rico have endured long period of recession with no end in sight, as a result.

It is nobody's case that there is no North-south divide in Europe in terms of productivity, economic performance and risk. It is even reflected in the yields of 10 year Government paper. The yield in Greece is 14.46% whereas, at the other end of the spectrum in the Netherlands, it is only 1.02%. In proudly independent nations which are more dominant that the European Union politically, each country with its own culture and attitude towards economics and productivity, each with its own fiscal policy, labour laws, etc., it is difficult to avoid the perils of a common currency which was created more out of hope and political convenience than out of economic conviction.

Therefore Greece is where it is. Where will it go? The referendum on July 5 could go either way. If the question posed is biased (extreme example: Would you prefer to cave in to the demands of the European Union instead of upholding your nation's honour?) or the people who protested last night on the streets reflect the country's real mood, the results are obvious. The consequences would be worth debating. The EU is hoping that it will go the 'good' way in which case, they have their work cut out for them.

If it goes the other way, will Greece insist on an exit or the EU force it to exit? Both are unlikely. The EU, worried about setting a precedent, (there being a few more weak economies in line for a Greece-like situation), is more than likely to impose some form of suspension. Since the EU politicians have a penchant for avoiding difficult decisions there could many shades of suspension. If Grexit is unlikely, what will Greece do in the mean while? That is the next article.

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