Europe`s Monetary Crisis: Ireland's "Suicide Pact" With the E.U.

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Ireland could be the next Lehman Brothers. That's what has the markets worried. If Irish leaders refuse to accept a bailout from the EU's new European Financial Stability Facility (EFSF), then bondholders will be forced to take haircuts on their investments which will leave banks in Germany and France short of capital. Bonds yields will rise sharply slowing activity in the credit markets. An Irish default will trigger hundreds of billions of dollars in credit default swaps (CDS), which will push weaker counterparties into bankruptcy and domino through the financial system. Contagion will spread to Portugal, Greece, Spain and Italy widening bond yields and forcing governments to increase their borrowing at the ECB. Business activity will sputter, unemployment will rise, and growth will shrink. It will be a second financial meltdown.

But no one believes that will happen. Most people think that Ireland will "take its medicine" and spare bondholders any losses. Irish leaders would rather accept a decade of EU-imposed austerity measures and the loss of sovereignty, then leave the euro and start fresh. It's disappointing. The euro is not designed to meet the needs of the smaller, less industrialized countries like Ireland. They need their own, flexible currency to ease the effects of cyclical downturns. But Irish leaders are still captivated by the idea of a united Europe. So they will cast aside the independence they earned through centuries of struggle for a pipedream and the elusive promise of prosperity.

At present, the Irish government is underwriting the toxic debts of its main banks. Unfortunately, those debts far exceed the revenues of the state. According to BBC's Robert Peston, the liabilities are "equivalent to an oppressive 700% of GDP when banking, public sector and private sector debts are added together." So far, the ECB has helped to keep Irish banks operating by providing 130 billion euros of emergency liquidity. But the wholesale markets no longer accept Irish debt as collateral and bond yields are in nosebleed territory. Irish politicians still maintain they have sufficient funds to get through the middle of next year, but that does not include funding for the banks. In fact, if the ECB stopped lending to the banks today, the system would crash overnight.

So the situation is tense and getting tenser. Even so, everyone expects Ireland's Finance Minister Brian Lenihan to cave in and accept a bailout. That will shift all the losses onto Irish taxpayers.

But what would happen if Lenihan balked and decided to restructure the debt instead of borrowing the money from the EFSF?

Journalist Robert Peston mulls-over that posibility in a recent article for the BBC. Here's an excerpt:

"Anglo Irish Bank and Allied Irish Banks, would probably have to be declared insolvent. And…many billions of euros that Irish taxpayers have already pumped into these banks would have to be written off….

What would then be triggered would be enormous payments by underwriters of credit default swaps (CDSs), the debt insurance contracts taken out by lenders and speculators. These payments would generate enormous losses for the financial institutions, including banks, which provided the CDS cover….

Even without the CDS loss multiplier, the impact of debt haircuts would be painful for British and international banks. According to the Bank for International Settlements, total lending of non-Irish banks to Irish banks is around $170bn, of which British banks provided $42bn, German banks provided $46bn, US banks $25bn and French banks $21bn." ("Ireland: How much punishment for British and international banks?", Robert Peston, BBC)

If Ireland quits the euro, all hell will break loose. The government will have to issue a new currency knowing that their debts will still be denominated in the higher priced euro. That will increase their debt-load. And, they'll be blocked from the raising capital via the bond markets until they've settled old claims. At best, it would take decade or more to dig out and to reestablish their credibility with the markets. On the other hand, they would have shed the euro straitjacket and reestablished their sovereignty. That's got to be worth something, but how much is it really worth?

Journalist Peter Oborne takes a look at the sovereignty issue in a recent article in the Telegraph. Here's an excerpt:

"It cannot be denied that Ireland has lost its status as a sovereign nation. Thanks to its disastrous entanglement with the euro, it has lost any independence in domestic, foreign and above all economic policy. The Irish nation is the creature of Brussels and the European Central Bank. The Irish prime minister has effectively been turned into a pro-consul dispatched to Dublin from Brussels. Brian Lenihan, the finance minister, is like an overseas manager of a Brussels subsidiary. For those of us who love Ireland, this is miserable and demeaning – but it needs to be borne in mind that a similar fate awaits a number of other European countries. Greece already does what it is told by the IMF and the ECB; the same will shortly apply to Portugal and in due course Spain." ("Ireland has lost its sovereignty and is now the creature of Brussels – thanks to the euro", Peter Oborne, Telegraph)

Oborne is not alone in thinking that Ireland is making a mistake by staying in the EU. The Telegraph's Ed West sees things the same way, but describes the EU/Ireland alliance in even darker terms, as a "suicide pact":

"Ireland has a historical attachment to continental Europe, as liberator from British rule, but it perhaps goes even deeper than that, back to its monks' preservation of Western civilization during the Dark Ages. Ireland, more than most countries, feels itself profoundly European and its Catholicism was always a part of that. It is not entirely a coincidence that as Christianity faded Ireland adopted a replacement ideology – the dream of Brussels. Or the world's biggest suicide pact, as I think of it….

Why spend 800 years trying to overthrow the Brits just to come under the sway of the EU? Having said that, almost no one in Ireland goes anywhere as far as UKIP or many Tories in opposing the EU altogether….

The European Project was and is a Utopian idea, based not on practical logic but on an idealistic vision, and it has only one aim in mind – total political union. Along the way its architects have consistently lied to the public about its aims, especially so in the creation of a single currency, which logic suggests requires political unification." ("Ireland's smug, Euro-loving elite has led their country to ruins – 'Little Englanders' saved ours", Ed West, Telegraph)

The financial crisis has stripped away much of the pretense surrounding the 16-country EU. No one is blabbing about ending wars and shared prosperity anymore. The focus has shifted to belt tightening for workers and golden parachutes for bankers and bondholders. In other words, elites are waging the same relentless class war they always have, only this time it's behind the facade of European unity. Does Ireland really want to be a part of that charade?

It's time for Ireland to leave the EU and deliver a blow to the ill-conceived Uberstate. In fact, they should have left years ago.

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