The Debt Crisis in the European Union: Austerity for Life...

Towards a European- style "Brady Plan"

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In July-September 2011 the stock markets were again shaken at international level. The crisis has become deeper in the EU, particularly with respect to debts.

The CADTM interviewed Eric Toussaint about various facets of this new stage in the crisis.

A European Brady deal: austerity for life 1|

CADTM: After the European summit of 21 July 2011 it was announced that the Greek debt was to be reduced by calling upon bankers. Was this a good move?

Eric Toussaint: Not at all. Those decisions do not provide countries facing financial problems with a favourable solution. The decisions taken on 21 July, supposing they are ratified by the parliaments of the member States in September-October 2011, will only slightly loosen the noose that strangles those countries and particularly their populations. Moreover, in the case of Greece (soon followed by other countries), European governments have relied on bankers, who are largely responsible for the disaster, to devise a policy tailored to their own needs. They set up an ad hoc cartel of the major creditor banks under the grand but misleading name of Institute of International Finance (IIF), which has drafted a menu with various options offering four possible scenarios. 2

As recalled by Crédit Agricole, one of the main French banks (it owns a bank in Greece, 'Emporiki,' 3 stuffed full of Greek bonds), the IIF clearly found its inspiration in the Brady Plan that was implemented in the 1980s-90s to face the debt crisis in 18 emerging countries (see below). Heads of State, the EC and bankers, relayed by the media, announced that this would reduce the debt by 21%, which is wrong. Actually, at best, the Greek debt would be reduced by EUR 13.5 billion, i.e. 4% of the current principal, which amounts to EUR 350 billion (which will further increase in the coming years). The 21% figure is the haircut bankers are ready to apply to the value of the Greek bonds they hold. It is just a bookkeeping operation. Indeed it does not affect at all what the Greek government has to pay. Bankers are so pleased that their proposal should have been accepted by the Heads of State and the ECB that several of them announced as early as late July-early August that they provisioned 21% losses on Greek bonds maturing in 2020. For instance, BNP Paribas provisioned EUR 534 million, and Dexia 377 million. 4 By doing that, banks that play a leading part in the IIF hope to get parliaments in the EU countries to ratify the agreements made with the Heads of State and the ECB. Besides, such expected loss provisioning can be offset from their profits to reduce taxation. So far, however, there is one trouble-maker among the bankers, namely the Royal Bank of Scotland (RBS), which withdrew from the IIF and announced that it would apply a 50% haircut instead of 21% and provision losses for GBP 733 million, which shows that the 21% cut is far from sufficient. Moreover, according to the Financial Times and the Belgian financial daily *L'Ėcho* 5 the International Accounting Standards Board (IASB) sent a letter to the European Securities and Markets Authority which regulates the European financial markets, calling into question banks that apply a 21% cut on their Greek bonds when the market to market value is less than 50%.

CADTM: The 21 July 2011 agreement is also said to mean that the Troika's loans to Greece, Ireland and Portugal would be extended over a longer period with lower interest rates. Is this the case?

Eric Toussaint: European governments did announce that they intended to reduce the interest rates they charge Greece, Ireland and Portugal by 2 or 3 points. 6 Announcing a reduction of 3.5% in interest rates for 15 or even 30 year loans amounts to acknowledging that the rates they had demanded so far were prohibitive. The move is motivated by the obvious disaster they have contributed to bring down on those countries and by the risk of the crisis spreading to other countries. The measures announced by European governments on 21 July 2011 are a clear acknowledgement of the 'unjust enrichment' they are responsible for and of the fraudulent nature of their policies.

CADTM: What is unjust enrichment?

Eric Toussaint: Unjust enrichment is abusive enrichment, profit gained through unlawful means. It corresponds to a general principle in international law defined in article 38 of the statutes of the International Court of Justice. |7| States such as Germany, France and Austria borrow at 2% on the markets and lend the same money to Greece at 5% or 5.5%, to Ireland at 6%. Similarly the IMF borrows from its members at low interest rates and lends to Greece, Ireland and Portugal at much higher rates.

CADTM: What is the fraudulent nature of the Troika's policies?

Eric Toussaint: Fraud 8 is an important notion in international law. It refers to an intentional deception made to damage another individual. If a State were led to contract a loan through the fraudulent behaviour of another State or an international organization that is party to the negotiation, it may invoke fraud as grounds for declaring the contract void, since it was agreed to through deceit. Now the Troika uses the plight of Greece, Ireland and Portugal to enforce measures that go against citizens' social and economic rights, challenge collective conventions, contravene the country's sovereignty and in some cases also its constitution. Thanks to some Italian newspapers, we know that in early August 2011 the ECB benefited from speculative attacks against Italy forcing its government to implement the same kind of antisocial measures as Greece, Ireland and Portugal. If the Italian government did not comply, the ECB said it might not help Italy at all.

What the members of the Troika are doing can be compared to the odious behaviour of someone who, while claiming to help a person in a difficult predicament, would actually make it worse and benefit from it. We can also consider that it is a criminal act planned collectively by the IMF, the ECB, the EC, and the governments that are supporting their action. Associating in order to plan and carry out a criminal act increases the responsibility of the aggressors. There is more: the economic policies enforced by the Troika will not allow the affected countries to improve their situation. For three decades this kind of damaging policy has been implemented on behalf of large private companies, the IMF and the governments of industrialized countries, in indebted countries of the South and in a number of countries of the former Soviet bloc. The countries that complied most diligently have had to face terrible times. Those that refused the diktats of international bodies and their neoliberal doxa have fared much better. This has to be recalled for we have to make it known that the results of the policies demanded by the Troika and institutional investors are a foregone conclusion. Neither today nor tomorrow will they ever have the right to claim they did not know what their policies would result in. We can already see what is happening in Greece.

CADTM: For over a year now, the CADTM has been warning against a debt reduction led by creditors, namely the Troika, bankers and other institutional investors. Is this justified?

Eric Toussaint: Of course. The current operation is led by creditors and geared to their own interests. As indicated above, the current plan is a European version of the Brady plan. 9 Let us remember the context in which this plan was implemented at the end of the 1980s.

In the early years of the crisis that broke out in 1982, the IMF and the governments of the US, the UK and other major powers helped private bankers in the North that had taken huge risks as they granted loan after loan to countries of the South, particularly in Latin America (as was to happen later with subprime mortgages and loans to countries such as Greece, Eastern European countries, Ireland, Portugal and Spain). When developing countries, starting with Mexico, were close to defaulting, the IMF and countries of the Paris Club agreed to lend them capital, provided they further repay private banks of the North and implement austerity plans (the notorious structural adjustment policies). Next, as the debt of the South was snowballing, they set up the Brady Plan (after the name of the US Treasury Secretary of the time) that involved a restructuring of the debt of the main indebted countries with bond exchanges. The participating countries were Argentina, Brazil, Bulgaria, Costa Rica, Côte d'Ivoire, the Dominican Republic, Ecuador, Jordan, Mexico, Nigeria, Panama, Peru, the Philippines, Poland, Russia, Uruguay, Venezuela and Vietnam. At the time, Nicolas Brady announced that the amount of the debt would be reduced by 30% (actually, when there was a reduction it was much less than that, and in several major cases the debt even increased, see below) and the new bonds (the Brady bonds) guaranteed a fixed interest rate of about 6%, which was very favourable to bankers. It also ensured that austerity policies would continue under the supervision of the IMF and the World Bank. Today, under other latitudes, the same logic produces the same disasters.

It is most interesting to look at *a posteriori* assessments by two well-known US neoliberal economists, Kenneth Rogoff, former chief economist with the IMF, and Carmen Reinhart, university professor and advisor to the IMF and the WB. Here is what they wrote in 2009 about the Brady bond. They first assert: "Conspicuously absent from the large debt reversal episodes were the well-known Brady restructuring deals of the 1990s." They then base their negative assessment on the following elements: "*In fact, in Argentina and Peru, three years after the Brady deal, the ratio of debt to GDP was higher than it had been in the year prior to the restructuring!*

By the year 2000, seven of the seventeen countries that had undertaken a Brady-type restructuring (Argentina, Brazil, Ecuador, Peru, the Philippines, Poland and Uruguay) had ratios of external debt to GDP that were higher than those they had experienced three years after the restructuring, and by the end of 2000, four of those countries (Argentina, Brazil, Ecuador and Peru) had debt ratios that were higher than those recorded before the deal.

By 2003, four members of the Brady bunch (Argentina, Côte d'Ivoire, Ecuador and Uruguay) had once again defaulted on or rescheduled their external debt. By 2008, less than twenty years after the deal, Ecuador had defaulted twice. A few other members of the Brady group may follow suit." 10 The European version is true to the original Brady Plan down to its finest details. In the context of the plan, participating states had to buy US treasury zero coupon bonds 11| as guarantee in case of defaulting. The European plan devised by the banks, the EC and the ECB (with the full support of the IMF) proposes four options. In the first three, Greece, through the European Financial Stability Facility (EFSF), buys zero coupon euro bonds as a guarantee that it will repay the principal on thirty-year bonds. 12

CADTM: What do you think of this plan?

Eric Toussaint: It will not help Greece to clear its debts for two essential reasons. Firstly, the debt reduction is completely insufficient; and secondly, the economic and social policies implemented by Greece to meet the Troika's demands will further weaken the country. As a consequence the new loans granted to Greece in the context of this plan as well as the former, now restructured, debts can be defined as odious. 13

CADTM: The ECB is said to be against a strong haircut of the Greek debt.

Eric Toussaint: Correct. The ECB is trapped by its own policy: as it bought lots of Greek bonds on the secondary market and agreed to banks, including Greek banks, depositing Greek bonds as guarantee on the loans it grants, the assets in its balance sheet consist of huge amounts of Greek bonds (plus Irish, Portuguese, Italian and Spanish bonds). If a 50 or 60% haircut were to be applied to Greek bonds, its balance sheet would be unbalanced. That being said, it is still quite feasible since this is merely a matter of book-keeping.

The ECB's opposition to a strong haircut coincides once again with the interests of private bankers who do not agree to their assets being devalued either. The ECB has put pressure on EU Heads of State and on the EC for them to strengthen the European Financial Stability Facility so that it can buy high risk bonds. It wants to get this over with as soon as possible.

Translated by Christine Pagnoulle and Vicki Briault in collaboration with Judith Harris

notes articles:

1 See the first part "Greece", the second part "The great Greek bond bazaar" and the third part "The ECB, ever loyal to private interests"

2| They are summed up in an article in *The Financial Times* on 26 July 2011, p. 23, and in the Crédit Agricole's bulletin Perspectives Hebdo 18-22 July 2011.

3 http://www.lesechos.fr/entreprises-... (accessed 26 August 2011).

4 *Financial Times*, 6-7 August 2011

5 *L'Ėcho*, 31 August 2011. See also TF1 "La BNP a-t-elle sous-estimé son risque grec?" http://lci.tf1.fr/economie/entrepri...

6 See the official declaration of the EU Council: http://www.consilium.europa.eu/uedo...

7 It is also mentioned in several national civil codes, for instance in those of Spain (articles 1895ff) and France (articles 1376ff).

|8 Article 49 of the Vienna Convention of 1969 and of the Treaty of Vienna of 1986.

9 See Éric Toussaint, The World Bank : the never-ending coup d'État, Mumbai: Vikas Adhyayan Kendra; (2007), chapter 15.

10 Carmen M. Reinhart, Kenneth S. Rogoff, *This Time is Different: Eight Centuries of Financial Folly*, Princeton University Press, 2009, pp. 84-85. Accessed online as googlebook.

11 These are bonds that do not give a right to periodic interest payments or coupons, hence their name. They are bought at a discount price from their face value, which is paid when the bond reaches maturity. Zero-coupon bonds are usually inflation indexed.

12 See Crédit Agricole, *Perspectives Hebdo* 18 – 22 July 2011, p. 3.

13 On the odious and consequently void nature of debts claimed by the Troika from Greece, Ireland and Portugal (to which we can add debts claimed by the IMF from Romania, Latvia, Bulgaria and Hungary, i.e. countries that are all members of the EU) see Renaud Vivien and Éric Toussaint, '*Greece, Ireland and Portugal: why agreements with the Troika are odious*' http://www.cadtm.org/Greece-Ireland...

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