Why debt relief could save Greece but would destroy the Eurozone

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Should Greece now be granted more favourable terms by its creditors following the 'no' vote in the country's referendum? **Michiel van Hulten** *writes that while most economists view some form of debt restructuring as necessary for Greece to recover, it would be exceptionally difficult politically to sell the principle of debt relief in other Eurozone countries. He argues that by voting 'no' Greece has effectively closed the door on the rest of Europe and that although the Eurozone may be able to cope with a Grexit, it could never survive an electoral revolt among its citizens.*

So the Greeks have said no. The way the referendum was called and organised fell well short of international standards, but given the margin of victory for the 'no' camp there can be little doubt that a majority of Greeks supported the hardline position taken by its left-wing government in recent weeks.

The Greek government says the referendum result means Europe must adjust the terms of its bailout terms, which Finance Minister Varoufakis (who just resigned), calls "terrorism". It wants debt relief and an end to austerity. From an economic perspective this makes sense. Most experts agree that without a debt restructuring Greece stands little hope of getting back on its feet, although it is worth noting that the point has been made most forcefully by commentators in the UK and US – two countries outside the Eurozone without direct taxpayer exposure to the Greek crisis.

Credit: Adolfo Lujan (CC-BY-SA-3.0)

But calls for immediate debt relief ignore the impact such a move would have on the internal politics of other Eurozone countries. While most UK voters could not care less about what happens to Greece's debt or Eurozone membership (they see the whole project as one gigantic failure which they are happy not to be a part of), citizens of Eurozone countries are deeply concerned. They believe, rightly, that the Eurozone can only function if its members stick to its rules (which is probably why France, which has flouted the Eurozone's rules for years, is the Greek government's only real friend in the current crisis). If Greece doesn't like the rules, it is free to leave.

In previously bailed out nations (Cyprus, Ireland, Spain and Portugal), debt relief would be seen as grossly unfair given the hardship these countries have had to go through – and are still going through – to get their economies back on track. Cancelling part of the Greek debt would be adding insult to injury. In creditor nations, voters have been told for the last five years that their billions of euros in loans to Greece would ultimately be repaid. While creditor nations have not suffered from the crisis in the same way that debtor nations have, Finland is in a deep economic crisis itself, the Netherlands is only just emerging from recession, France is in permanent stagnation and Germany alone is keeping the Eurozone afloat.

In those countries, like in Greece, left-wing and right-wing populists are ready to pounce on centrist governments which are seen not to protect the national interest. Le Pen, Farage et al have welcomed the Greek referendum result as a slap in the face of EU governments. But they will be the first to condemn any new bailout deal – no matter on what terms. In fact it is a small political miracle, given the aftermath of the 2008 crisis, that it has been possible to provide Greece with any bailout money at all. Voters in creditor nations see Greece as a failed state (Greece ranks bottom of the EU league in Transparency International's Corruption Perceptions Index); a black hole into which their hard-earned money is disappearing. Greece's 'no' vote sends a signal that this is not about to change.

Greece has not been helped by the fact that its new government has spent much of its first few months in office going around Europe insulting and offending potential allies. To throw the second world war back in the face of its largest creditor wasn't exactly smart politics. Mr Varoufakis calling Italian debt "unsustainable" probably helps explain Prime Minister Renzi's current tough line on Greece. And each time Mr Tsipras goes to Moscow to shake hands with Putin, Dutch voters are reminded of the Russian President's ultimately responsibility for the downing of flight MH17 in which almost 200 of their citizens were killed. The Greek government has also proved itself to be an unreliable interlocutor. These are not in themselves reasons for not helping the Greek people. But they help explain many voters' reluctance to do so. As Philip Stephens wrote in the FT: "Mr. Tsipras has never quite grasped that other nations too have democracies".

Citizens in other Eurozone countries are clearly not indifferent to the plight of the Greek people. A vocal minority already support immediate debt relief. But for the vast majority, a debt restructuring can only take place once Greece puts its house in order politically and economically – not through socially harmful budget cuts, but by modernising its adminstration, improving tax collection, tackling nepotism, rooting out corruption and freeing closed sectors of the economy up to competition, to name but a few of the measures that would be required. By voting 'no', Greece has effectively closed the door on the rest of Europe. So be it. The rest of the Eurozone may be able to cope with Grexit, but it could never survive an electoral revolt among its citizens.

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