



Containing Greece's Travails in Europe

Michael Mussa assesses the threat of a default by Greece and the misgivings and constraints felt by Germany in trying to avert a crisis.

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Steve Weisman: The turmoil in Europe continues over whether to bail out Greece in its hour of financial trial. Mike Mussa, senior fellow at the Peterson Institute for International Economics, is here to talk about what is going on in Europe and its impact on the United States and the rest of the world.

This is Steve Weisman at the Institute. Mike, thanks very much for joining us.

Michael Mussa: My pleasure once again.

Steve Weisman: Mike, what is at the core of Greece's problems and how much do these problems exist in other parts of Europe?

Michael Mussa: The core of the problem is that Greece now has a very large government deficit, the largest in Europe—12 percent of GDP [is] the reported figure, and perhaps bigger than that. And they have a very poor record of dealing with their fiscal problems. They've fudged the figures on a couple of occasions in the past decade, so there's a lot of distrust of them in the market and in the official sector as well, and they have a substantial volume of their debt, which they need to roll over this year. They're not going to repay it but they need to re-borrow it as it matures this year. That's mainly in the spring. So, there's a lot of pressure in the market on their interest rates.

Steve Weisman: Who owns the debt?

Michael Mussa: It's spread around. Mainly, it's held in Europe and probably mainly by institutions—financial institutions, including banks. Some of it is held domestically in Greece, but a lot of it is spread around to various financial institutions in Europe. We hold a little bit of it.

Steve Weisman: What if Greece fails to roll over its debt and defaults?

Michael Mussa: Well, it's going to have the biggest the impact on Greece, which is going to mean basically they're cut off from any borrowing. Since they're continuing to run a deficit beyond the level of what they need to borrow in the form of interest, it's going to put a sudden very sharp constraint on government spending. They're going to have to cut wages very severely and so forth.

One of the big concerns is the spillover effects that it would likely have because there are other European countries—Portugal, Ireland, Spain in particular, also Italy—that have also very large deficits and large outstanding debts. And if Greece went into default, then it would raise the questions about these other countries as well.

Steve Weisman: Are the French, the Germans especially, prepared to bail them out or roll over the debts or supply new financing in order to give Greece enough time to get its house in order?

Michael Mussa: Well, enough time is probably going too far. I think they are in fact, at this stage, really locked in to providing at least short-term support in order to enable the Greek government to roll over the debt that is maturing in the next few months. There's been sufficient indication that they're prepared to do something along that line. If they suddenly came out and said, "No, we're not going to do it," it would then force default.

So, I think they're locked in. What's at issue is the discussion of the terms and conditions, which the Greek government would need to satisfy in terms of their budget policies or promises about their budget policies in order to secure that financial support. But at this stage, it would be very difficult for the others to back away.

Steve Weisman: Do the Germans feel any responsibility on their own for this problem that afflicts a country like Greece? I mean, German exports and efficiency in productivity in general have put a lot of the other economies in Europe on the defensive and they feel a little blame toward Germany. Do you think that's fair?

Michael Mussa: Well, I don't think the Germans feel much responsibility that their virtue, in their view, should not be the excuse for others' relative vice. So, if the Greeks have a problem, it's because they haven't been as virtuous as the Germans have been. And I think they rather resent the notion that their money might be put at risk in order to bail out the Greeks, who have not maintained a reasonable fiscal policy for a number of years. And part of the problem I think for the German government, the chancellor and others, is that public opinion in Germany is not very sympathetic to bailing out the Greeks and possibly a longer list of countries.

Steve Weisman: What is the form of the rescue if it takes place?

Michael Mussa: My guess—I think what's been discussed—is providing some form of guarantee of the rollover debt that the Greeks will be issuing, possibly involving purchases of a significant part of that debt by various quasi-public institutions such as the Caisse des Depots in France and a couple of the Landesbanks in Germany, which are financial institutions that are connected to the government but are not the central banks. The European Central Bank's constitution really prohibits providing direct support.

Steve Weisman: What concerns should Americans have about the lack of resolution of this problem?

Michael Mussa: Right now, and I think for this episode, it's going to be largely a European responsibility. At some point, if the problem is not resolved in the present round, it may come to the IMF, which also has sources of financing involving the United States, as well as the Europeans. I don't think that we'll see them come to the IMF on this occasion.

But if the Greeks don't solve their problem beyond the nearer term and they have to come back for another round of support in a year or two, by that stage the Europeans may say: "Enough. You have to go to the big bad Fund in order to get any additional support." But I think that's a year or two off.

Steve Weisman: And the IMF presumably would be tougher on Greece than the Europeans can be right now?

Michael Mussa: That would certainly be the perception. I think the threat of pushing the Greeks to go to the IMF is one of the things the other Europeans are going to hold over them, now and in the future.

Steve Weisman: Does the United States have any role to say to the Europeans, “You need to resolve this?” After all, the United States’ own house is not in the best of shape.

Michael Mussa: I think this is a situation where we should keep our mouth shut. It’s like refereeing an argument in another family. It’s generally not a good idea.

Steve Weisman: Okay, Mike. But let’s keep watching it. And thanks very much.

Michael Mussa: Right.

