

# A few days left to solve out-of-reach crisis



Hannelore Foerster/Bloomberg

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[Tim Shufelt](#) Oct 21, 2011 – 6:54 PM ET

In its effort to catch up to a crisis perpetually beyond its reach, the eurozone's political framework has proven incapable of mustering the necessary urgency.

The required consensus of 17 separate legislatures (17!) have weakened attempts to quell contagion through long delays between proposal and enactment.

Imbalances requiring bold and timely action have worsened over the past two years. Meanwhile, time ticks away before some sort of escalation tests global stability.

So, that markets seem to expect something different to come out of this weekend's much-hyped summit is itself a testament to the resilience of optimism, however misplaced.

"We're going to be talking about this for years," said Alex Jurshevski, founder of Toronto-based Recovery Partners and an expert in sovereign restructuring. "This is just another chapter in a very long process, a process that's not being managed well, because there is no management framework. These guys are making it up as they go along."

On Sunday, the European Council will gather for discussions on another round of rescue planning, with new signs of distress in Europe's state finances and banking sector. The talks will be followed up on Wednesday.

In anticipation, global bond yields rose from crisis lows, commodities moved higher, the U.S. dollar weakened and key equity benchmarks for the Toronto and New York exchanges gained 1% to 2% on Friday.

The renewed appetite for risk came amid speculation of an audacious European plan, including an increase to the writeoff of Greek debt by the country's private debtholders, a boost to the bailout fund, and a recapitalization plan for distressed banks.

"The markets seem remarkably sanguine about the ability of policymakers to save the day," said Jonathan Loynes, chief European economist at Capital Economics.

Many analysts wonder why, given the eurozone's recent record.

Since Greece sparked the sovereign debt crisis in March 2010, global markets have been locked in a cycle of fluctuating sentiment, said Craig Alexander, chief economist at Toronto-Dominion Bank.

Periodically it goes like this: investors get deeply worried about the sovereign debt crisis; markets then put pressure on politicians to act; followed by a wave of hope that decisive action is on the way; a plan of attack is announced; markets initially respond favourably; then, the prompt realization that the root causes remain unaddressed.

Rinse, panic and repeat.

The fallout from a plan announced in July — which formulated a second bailout for Greece, an expanded role for the European Financial Stability Facility to purchase toxic debt, and a 21% voluntary haircut for those holding Greek bonds — followed this now-familiar pattern.

The ensuing market relief lasted all of one day, before the reality of European politics dawned on investors, Mr. Alexander said.

"You make the proposal but then it needs legislation to be passed and it needs every single country to agree," he explained.

That process took three months to complete, ending in the Slovakian legislature just last week. "This tells the entire problem of the political system not being capable of moving quickly enough," Mr. Alexander said.

While that plan moved through Europe's slow-moving gears, the sovereign debt crisis gained momentum.

With its economy in contraction, Greece's finances worsened, Mr. Jurshevski said. "It became totally obvious that the 21% haircut is far too little," he said.

Now, reports have eurozone authorities acknowledging that fact and considering a writedown of 60%. But ever one step behind, Greece may ultimately require a haircut of up to 75%, Mr. Jurshevski argued.

“So far, the solutions put forward are not solutions, they’re patches,” he said.

In the leadup to Sunday’s summit, the signals coming from European leaders have been contradictory and the rumours have run rampant.

Much of the optimism now evident in markets for an extensive European plan may largely be a function of the building pressure.

Language coming from the G20 urging the eurozone to take comprehensive action has taken on an uncharacteristically blunt tone.

Additionally, the growing severity of the crisis has many convinced that the region’s leadership has no choice but to react sharply.

“We’ve already seen the first financial institution fail,” Mr. Alexander said, referring to the rescue of French-Belgian bank Dexia SA. “We are having a banking crisis in Europe.”

And Moody’s Investors Service downgraded Spain’s rating by two notches this week, while warning France of a possible review of its AAA rating.

“The question is going to be whether the politicians respond to the pressure,” Mr. Alexander said. “A rational outcome is that they will. The sad thing is that a rational outcome may not be what occurs.”