CREDO WEALTH

The Final Act?

The architects of ancient Greece used a technique called entasis – whereby all major vertical and horizontal lines are slightly curved – to create the illusion of a perfect geometry. Likewise, in order to sell the bailout terms to the Greek parliament, Tsipras may have to resort to political entasis and make the crooked seem straight.

In a bid to save the Greek banking system from collapse, Tsipras caved to the demands of his creditors. The next few days may prove crucial. Given the explicit rejection of the economic reform programme by the Greek people in early July, one may justifiably wonder how Mr Tsipras hopes to pass the package through an increasingly restive Greek parliament. To quote his own party's newspaper: "Germany is not entitled to destroy Europe for the third time in a hundred years". While the rhetoric is overblown, the message is clear: the fragile accord between Greece and her creditors hides deep divisions.

Yet beyond the troublesome Hellenic state, the conduct of the crisis provides ample fuel to Eurosceptic fires. Bagehot wrote that to stem a banking crisis the central bank should lend against solid collateral. In Greece, the people wanted cash, but the banks were lacking. Under normal circumstances, the central bank would extend loans, with the banks' investments pledged as security. In flagrant defiance of its treaty obligation to support the general economic policy of the Eurozone – which includes a requirement to separate the health of the banking system from the solvency of sovereigns – the European Central Bank (ECB) forced a shutdown of the Greek banking system, and made it clear that business would only resume after a deal had been struck. The unedifying conclusion is that the ECB's independence is conditional.

Even if Athens accepts the terms of the bailout, Greece's ability to pay its debts remains unclear. The IMF's latest Debt Sustainability Analysis makes clear that the debt burden is unsustainable without further concessional loans and an extension of existing debt maturities. It even goes so far as to suggest a possible write-off of some €50bn of debt. But even these figures are dubious, based on a presumed primary budget surplus of 4.5% (before interest). During a brief interlude in austerity in 2014, Greece's budget surplus peaked at 1%, not even close to the IMF's base case assumption. Yet the often overlooked reality of Greece is that the Greeks can, quite literally, walk away from their debt. The European Union promises unhindered migration. If remaining in Greece means living in a country where taxes must exceed public expenditures, many may do just that.

For now, a Greek exit has been averted but the bailout package, filled as it is with tax hikes, spending cuts, and pension cuts, leaves little scope for growth. If this comes to pass, Greece may once again return to the negotiating table, but given that German exporters rely on the less productive members of the Eurozone for an artificially depressed currency, an exit will likely remain unpalatable to all parties. For now, resolution of the crisis depends on Tsipras' abiity to present the bailout package as bitter medicine, not hemlock.

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