

Grexit? Greece Needs to be Ejected To Save the Euro. Grejection.

It must be clear by now that the Euro doesn't work. Member countries will always disagree on what is an appropriate exchange rate and thus terms of trade with the rest of the world, and worse, with one another. There is no automatic mechanism to link a (further) Greek default to their exiting the Euro. An unceremonious ejection by current Euro members is more likely as Greeks demonstrate intransigence in the face of insolvency.

Austerity is not the answer, but neither is defiance of creditors. And the Euro while central to the problem is not its cause. Had Greece not joined the monetary union, its uncompetitiveness would have led to either a gradually or rapidly declining Drachma. In that parallel reality it would not be a stretch of the imagination to envisage certain experts proposing a D-Mark peg (sort of like joining the Euro.)

Greeks refusing to pay taxes in Euros will refuse to pay taxes in Drachmas.

The time for prevarication and indecision has come and gone. The Euro clearly doesn't work and its time to decide if Europe wants to bear the cost of an irrational construct, or abandon it. In either case, there are orderly and disorderly routes.

If Europe wants to keep the Euro, then Greece must be ejected without mercy. Any mercy shown now will only compound the cost of bailing out Ireland, Portugal, Italy and Spain when they embrace the concept of a country too big to fail.

There is a significant risk that Greece becomes a failed state. Already no single political party commands the confidence of the people. In fact, the desires of the people may be incompatible with international standards of financial rectitude and contract law.

As Europe prepares to eject Greece, it must ringfence the risk to the extent possible and send a message to the rest of peripheral Europe that failure to operate under some semblance of financial responsibility (which is different from blind acceptance of austerity), is a prerequisite for continued inclusion.

Moral hazard must be a concept laid to a violent death. Greece is a free country of free people. It must decide its own course. If it cannot resolve its financial problems and default becomes inevitable, and in the absence of more European forbearance it is, then default it will.

This may not mean automatic exclusion from the Euro. Indeed, any country can use the Euro if you think about it, since no one country can unilaterally print Euros. It will be for the European Union to declare Greece a non Euro member. This would be an empty and symbolic gesture. Greece can still use Euros, to the extent that there are any left in its banking system, and it can still issue Euro denominated bonds, to the extent anyone will buy them.

If Greece printed Drachmas, they would be worth less than the paper or metal they were made of and financial oppression would be required to enforce their legal tender. There would be instant Drachma hyperinflation. The Euro would be the de facto black market currency. The road to anarchy would have been paved.

Once it has been established that failure to engage with other Euro member countries leads to withdrawal of assistance, ejection from the union, default, an unviable independent

currency, hyperinflation and years of depression and isolation, remaining Euro countries can focus and work together towards a more lasting resolution.

The damage of a Greek failure would be massive but it is necessary to hold the rest of the union together. If indeed that was the intention.

How heavy a price this would be for Greece and for Europe. And that would not be all. The sword of austerity would hang over Europe until the level of debt was brought down to more manageable levels. And even then, the vigilance necessary to maintain the Euro and to avoid the accumulation of large imbalances would mean some level of austerity somewhere in the union at most times.

Consider the alternative: a recognition of the inefficiencies of the Euro, preparations for an orderly multi year dismantling of the Euro in a reversal of the process from Maastricht up till the turn of the millennium. The damage would not be small but the source of imbalances would have been addressed.