“The debt sovereign crisis is a community problem which can only be solved by all members moving from preconceived conditions. It means that Ireland saves the banks, the Greeks get their tax collection system in order, the Spaniards do something about persistent underemployment, the Germans something about unwillingness to allow a softening of the currency; in return for which everybody wins.”

- Brian Lucey

Dukascopy has interviewed Brian Lucey, Professor of Finance at the prestigious School of Business in Trinity College Dublin, to discover how Ireland is doing in light of the debt crisis in Europe. Professor Lucey gives his view on the troika ruling, Germany’s behaviour in the Eurozone and provides advice on how to rectify the turmoil.

Brian Lucey

Professor of Finance at the School of Business in Trinity College Dublin
and Editor of Research In International Business and Finance

1) What is the most effective way for the government to endure negative impact of the Greek debt contagion?

The government plan is to attempt to get Ireland to the situation where we are back within the Maastricht criteria of a 3% budget deficit. I think we should move to a primary budget surplus, that is, to my mind, a better approach.

However, the Irish government has two interlinked problems. One is a problem with our domestic finances – we are spending more than we have. Regardless of anything that happens in the Eurozone, our current budget deficit it has to be closed and the government is doing pretty significant changes to tax and to government expenditure on both capital and current side in order to breach that gap.

The previous government has taken on the debts of the banks and in particular they took debt in a number of banks which are now bankrupt. They are acting as a significant drag; they have tipped us over in two, the IMF, EU, and ECB – troika, being our real economic masters. So the government needs some way of getting out from under that set of debts before they crush the country as they are the straws that are breaking the camel’s back. The government is trying hard with relatively little success in getting the ECB to accept that this burden now needs to be shared with the European side of the House. So that is what they need to keep doing more rigidly and rapidly.

2) How would you assess the situation with the mounting unemployment in Ireland?

The problem with Irish unemployment is that like in the most countries it is a function ultimately of domestic demand. We are in a deep recession and until domestic demand picks up that unemployment is not going to start to be eroded. In general, a lot of the unemployment is coming from people who had been working in construction and construction related industries. As a consequence of the bursting of the housing and the construction bubble, the people are finding it difficult to get back into work. The unemployment figures would be significantly worse did we not have a large amount of people emigrating from the country. The obstacle is that the government needs to do something, but it does not have any money.

3) What are the prospects that the budget targets and GDP forecasts for the next year will be achieved?

> I believe the government now has a reasonable handle on the figures. Historically we have very good quality data in Ireland. We are not in a Greek situation where they are ending up with figures being simply unbelievable.

So the government will be much on track with whatever they say they are going to be on track with. The issue is the speed of adjustment. One could argue that there should be some degree of front-loading of whatever adjustments they are going to make because the external environment is every day more uncertain.

I do not think that we are going to miss our targets, if we do, it is not going to be by much and it certainly won't be because people and the government have not been trying to deal with the fiscal side of the problem.

Yet, I must go back to the distinction between the national debt that the government borrowed to run the country. That is what we have to repay and the tens of billions that the previous government took on as the consequence of the banking guarantee which was done at least in part on behalf of the European Central Bank. For this, however, we have got very little in the way of, shall we say, "Thanks" from the ECB.

4) What could be the scenarios for further economic developments in the Eurozone? For instance, if Greece abandons the euro how will particularly your country be affected?

I think the Irish government would see Irish national interests best served by staying as close to a core, hard currency Euro zone, as possible. I believe that if we end up with the situation where there is dissolution or partial dissolution of the Eurozone, the government will try and position us. And if we look again, absent of banks, where we are in terms of our growth prospects economically and in terms of our ability to adjust the fiscal discipline when required, then we are certainly more akin to that tier then we are to the southern tier. The issue is whether or not we will have time to plan that.

My concern would be that once the Eurozone, if it starts to unravel, might just fly apart. If that is the case, then the problem is where the money goes. There will be massive flights to safety from all peripheral countries and there will be a question raised whether the bund is safe. We now see the situation where UK government gilts are seen safer in the short-term than the bund. It is uncertain if it will spread into a strong Swiss franc while the Swiss are trying to preserve what is left from the Swiss industrial and service activities.

5) In general, are you optimistic about the current European situation?

I think the situation in the Eurozone is entirely down to whether or not Madam Merkel accepts that it is a Euro zone, not a German zone.

> If Germany wants to have a currency zone where there is zero inflation, strong currency and absolutely independent Central Bank, then it is about their previous currency, Deutsche Mark, which they signed away for, basically, for the opportunity to export more to the Eurozone. That is the price.

EU and ECB it is “E” which stands for European, not some kind of version of “D” for Deutschland. And that needs to be realised. The debt sovereign crisis is a community problem which can only be solved by all members moving from preconceived conditions. It means that Ireland saves the banks, the Greeks get their tax collection system in order, the Spaniards do something about persistent underemployment, the Germans something about unwillingness to allow a softening of the currency; in return for which everybody wins.

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