“It may well be in the interest of the BRIC countries to prop the Euro up”

- Rajesh Chakrabarti, Assistant Professor of Finance at Indian School of Business

“BRIC countries have to initially make sure that Europe can take action to rescue itself before being saved by BRIC”

- Frank M. Song, Professor of Business and Economics at the University of Hong Kong

With the mounting level of economic problems the Eurozone is in dire need of external financial aid. Among the top potential providers of credit analysts highlight the BRIC countries that have accumulated huge foreign currency reserves. In this respect Dukascopy has asked the experts' opinions directly from BRIC countries on the matter.

Rajesh Chakrabarti
Assistant Professor of Finance at Indian School of Business and Columnist at Financial Express

Frank M. Song
Director of Centre for China Financial Research, Professor of Business and Economics at the University of Hong Kong

1) What do you consider to be the main reasons for current Eurozone economic problems?

R.C.: At a fundamental level the problem for the Eurozone is that of monetary union without fiscal union. The primary issue is that of profligacy of some countries financed by bonds that sold primarily because of the reliability of the currency built on the finances of other countries.

F.S.: The main reason is inconsistency of the fiscal policy with the monetary policy. Along with the over borrowing of some countries the Eurozone lacks a unified fiscal policy.

2) How would you assess the statement that by bailing-out Western Europe the BRIC countries are saving their own economies?

R.C.: At first glance this seems a sensible solution since collectively the BRIC countries are witnessing capital account surplus while the Euro area has a capital account deficit. Therefore if the latter uses its reserves to buy the Euro bonds it would save the day for the Euro countries in trouble. To the extent that the Euro problem can snowball into a shut-down of international capital markets and a sudden collapse in the value of the Euro would eat into the value of the Euro-denominated reserves of the BRIC countries. So in all it may well be in the interest of the BRIC countries to prop the euro up.

F.S.: My personal vision is that all the countries are integrated now, namely a huge amount of BRIC countries exports are targeting EU economies. This means that if Europe does not resolve its economic problems, they would bring serious troubles to the rest of the world as well. Logically, BRIC countries have self-interest so that euro does not collapse. It would be very reasonable for BRIC to contribute to the stability of the euro.

3) What do you think might be the conditions for the bail-out if it takes place? Will the BRIC countries manage to use the situation for their benefit in terms of trade conditions, access to technologies?

R.C.: The BRIC countries would probably bargain for market entries and technology access in lieu of their support. Anyway propping the Euro artificially will erode the competitiveness of the Eurozone against the BRIC countries, a condition aggravated by possible trade advantages negotiated by the BRIC countries. Also the solution would have the long-run impact of spreading the problem to the healthier Euro economies through currency overvaluation. A more direct solution of capital reallocation within the Euro zone with a gradual depreciation of the Euro would perhaps be a less distorting, even if politically less palatable, solution.

F.S.: I would say that good bargaining stipulations would be the primary conditions. For instance, for China the required benefits would be high tech products imports to China and opening up European economies for Chinese investments as China has accumulated a lot of foreign exchange reserves. Therefore, a closer relationship between BRIC and European economies would be mutually beneficial.

Beyond that, BRIC countries have to initially make sure that Europe can take action to rescue itself before being saved by BRIC. I would recommend waiting for stronger signals, giving Europe time to cut the budget deficit and to implement more structure changes in the economies. Furthermore, major European economies, specifically, France and Germany have to show their determination to defend the unified euro.