

DEEPENING EUROPEAN BANKING CRISIS: G7 holds emergency meeting

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Global Research, June 06, 2012

[World Socialist Web Site](#) 6 June 2012

Region: [Europe](#)

Theme: [Global Economy](#)

Finance ministers of the Group of Seven (G7) industrialized countries held emergency talks yesterday, amid signs of a renewed economic slump worldwide and an intensifying crisis in Europe—notably the Spanish banking crisis and fears of a Greek exit from the euro.

European bank stocks closed mostly higher on news that all the G7 powers had agreed to the meeting. Japanese Finance Minister Jun Azumi reported that the G7 countries had stated they would cooperate in dealing with the Spanish banking crisis. They reportedly did not discuss the possibility of a Greek exit from the euro.

The financial press reported that investors would closely follow statements today by the European Central Bank (ECB). The ECB's decision to reject a bailout request from Spanish bank Bankia played a major role in late May in provoking the current panic, amid the collapse of the Spanish real estate market.

The meeting came amid increasing discussions in European capitals of plans to respond to the escalating European debt crisis by pooling resources.

Experts estimate that Spanish banks need a total of 100 billion euros to cover their losses. Bankia, taken over by the state at the beginning of May, urgently needs 23 billion euros alone. Because of this, the Spanish government is no longer able to raise international bonds. The financial markets were virtually closed for his country, Finance Minister Cristobal Montoro had to admit on Tuesday.

If Spain, like Ireland, Portugal and Greece, applies for support from the European bailout fund, the fund's resources would be quickly exhausted. As the fourth largest economy in the euro zone, Spain provides guarantees for some 12 percent of the fund, which would shrink accordingly. The spread of the crisis to Italy, the third largest economy in the euro zone, would also become more likely.

While the Spanish banking crisis is currently considered the biggest threat to the euro, governments and financial markets continue to look nervously to the Greek elections of June 17. The Coalition of the Radical Left (SYRIZA) has announced that in the event of an electoral victory it would unilaterally cancel the austerity measures agreed with the troika—the European Union, European Central Bank and International Monetary Fund.

Although SYRIZA leader Alexis Tsipras insists that his party wants to remain in the euro zone, work with the Troika and repay Greece's debts in the long term, there is little evidence so far that the troika is ready to engage in a renegotiation of the financial packages for Greece. This would create a precedent that would make it difficult to dictate austerity

measures to other countries. If they cut off credit to Greece, a default and exit from the euro zone would be almost inevitable.

The rating agency Standard & Poor's now estimates the probability that Greece will leave the euro zone at one in three. All euro zone governments, as well as Beijing, are preparing contingency plans for such an eventuality.

Experts are arguing about the consequences of such developments. While some assume that Greece would plunge the whole euro zone into the abyss, others think the effects would be manageable.

In the *Financial Times*, the former head of UK investment banking at Lehman Brothers, Michael Tory, advocates a Greek bankruptcy because it would be a salutary shock to Europe. Just as the Lehman's bankruptcy in 2008 provided governments "a good stare into the abyss" and "mobilized the political will" to support the banks with hundreds of billions of dollars, a Greek bankruptcy would generate the political will in Europe "to institute jointly guaranteed euro zone bonds underpinned by ironclad and enforceable centralised fiscal discipline".

Neither in Europe nor internationally has a common approach been found so far how the imminent collapse of the euro could be prevented. Above all, the German government has previously insisted on strict austerity and rejected providing any additional financial support, whether in the form of euro bonds, or by the European Central Bank printing money.

Berlin is now increasingly isolated, however. Most European governments, along with the US, are pushing for a policy of quantitative easing and the issuing of common European bonds to provide the banking system with sufficient funds.

Now the German position has started to shift. The main reason is that Germany itself is increasingly affected by the crisis. About 40 percent of German exports go to the euro zone, where many countries are in recession. Growth has also slumped in China, India and other emerging countries where German export figures saw their biggest increases in recent years.

As a result, economic indicators in Germany have declined sharply. The DAX, Germany's most important stock index, lost 16 percent of its value in the last ten weeks. Meanwhile, the calls are mounting urging the federal government to change course.

Under the headline, "The end of the German illusion", *Spiegel Online* wrote: "Now the new economic downturn and the slump in the stock market are showing that Germany is quite vulnerable—and therefore must make sacrifices".

In the *Süddeutsche Zeitung*, former Foreign Minister Joschka Fischer (Green Party) warned in dramatic terms that the European house was in flames. In the coming months, the country will fall into the abyss, "unless Germany and France jointly change course", he wrote.

Chancellor Merkel has now signaled her willingness to make concessions. But there is no longer any talk of "growth", economic stimulus or the like. Rather, the German government is willing to bear a larger share of the burden of rescuing the European banks, if, in return, the governments concerned cede fiscal sovereignty to Brussels (and thus indirectly to Berlin).

On Monday, Merkel discussed a European banking union with Jose Manuel Barroso, President of the EU Commission. This would put major European banks under EU regulation and introduce mutual deposit insurance. Under these conditions, the banks would then receive capital injections from European funds, and not as previously from national funds.

Another model that is currently being discussed is a so-called debt repayment fund. All countries would place their debts that lie above the Maastricht limit of 60 percent of Gross Domestic Product (GDP) into such a fund. This fund would then issue joint bonds at a relatively low interest rate and pay off the debt within 25 years.

As a condition for all such proposals, the German government is demanding further steps towards a fiscal and political union. This would mean that European institutions would get more control over the developments inside the nation states.

What Merkel means by this is transferring the type of social cuts that have devastated Greece to Europe as a whole. The EU would support indebted countries by repaying their debts and saving their banks; in return, it would dictate their budget, employment and social policies.

Such plans are not only meeting opposition in Britain, which rejects any interference by the EU in its financial sector, but also in Italy and France. "Neither wants to find itself in the position of answering to fiscal and banking authorities that, fairly or not, will almost inevitably be deemed an arm of the German government", commented the *New York Times*.

The victim of all the plans being discussed is the European working class, which faces a new round of social cuts.

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