Greek sovereign debt needs to be restructured now

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By now there is no doubt that Greece needs a radical restructuring and reduction of its debt. Greece has reached the point where it cannot pay even the interest of its sovereign debt. Interest alone reaches 20-28% of the state revenues, and this percentage will grow as long as Greece is in a recession. Greece needs to reduce its debt immediately. Without this reduction, it will be driven to an uncontrolled bankruptcy.

Greece society, citizens and political parties need to see beyond today. Receiving larger new loans to pay off the smaller old ones and simultaneously increasing the debt does not solve the problem for Greece. It simply indebts even deeper future Greek generations. The short term borrowing "solutions" do not solve the debt problem. They are convenient for the politicians, but catastrophic for Greece. They are the same practices that since the 1980s lead Greece to the edge of the abyss. Greece needs a real solution to its debt problem that will work in the short run, and will also work in the long run too.

Seeing the long term impasse, the Greek government must have the courage to tell openly the truth to the EU and the IMF, that is, that Greece is unable to pay the total amount of its debt, and not even the full interest on its debt. The fact that Greece cannot pay the total amount of its debt is well known to analysts, as well as to Greek and European politicians and bankers. But despite that, politicians and bankers pretend they do not know this fact. On the one hand, politicians are thinking only for the very short term of the next three or six months, and it is convenient for them to cover up reality. On the other hand, bankers cover up their terrible position and rely on the favor and corruption of the politicians essentially asking them to transfer the bank losses to the general public. However, the tough reality is shown clearly from the prices of the Greek bonds in the market (66,50% interest rate for the two-year Greek sovereign bonds this week). Unfortunately, many of the Greek mass media and the Greek government have demonized the markets, and thus, they cannot make good use of the information that the markets provide.

Facing the truth that everyone knows that Greece is unable to pay even the interest of its loans, it falls on the Greek government to say clearly and publicly the truth. Greece should ask a debt restructuring and erasing of at least 50% of its debt both from private lenders and from the EU lenders. After this part of the debt is erased, Greece will finally have a manageable debt level, approximately 80% of its GNP. If Greece does the necessary reforms, it will be easy for it to find again growth and prosperity.

Greece must coordinate the deletion of at least 50% of its private lenders' debt with the exchange of its old bonds with new ones that would have as a collateral of their face value high quality bonds (such as the German ones) that Greece can buy or the face value of the new Greek bonds can be guaranteed by the EU stability mechanism ESM/EFSF. For the bilateral loans of the EU support packages, Greece must ask for forgiveness and deletion of a part of the debt. The 50%

“haircut” and the exchange with higher quality bonds will solve once and for all the problem. The new high quality (because of the guarantees or collateral) Greek bonds will have low interest that Greece will be able to pay. The total cost of the haircut for the European countries and the IMF will be €55 billion and €100-120 billion for the private sector. These amounts are small, and I would say minimal, in relation to the cost to Europe of a long Greek crisis. If it proves politically impossible to impose a haircut on the bilateral loans from EU and the IMF, Greece could pay these in full and impose a larger haircut of 60% to the private lenders.

But why should the European states and the private lenders agree to this solution? First, because they will not have another choice. The vast majority of Greek sovereign bonds are issued under Greek law that implies that the Greek parliament can pass a law that imposes the haircut. Second, because the European will also see that the total cost of this solution is small relative to the cost of the daily long run Greek crisis that threatens to “contaminate” large European countries, such as Italy and Spain.

The 50% haircut and the exchange with higher quality bonds must happen now, before the proposed exchange of Greek bonds held by banks with a 10-20% haircut. If the exchange with a 10-20% haircut goes forward, the new Greek bonds may not be ruled by Greek law, and that may make it more difficult to make the necessary future additional haircut of 30-40% on them.

Some may say that the 50% haircut that is necessary for Greece will make the Greek banks collapse. First, we should see that this haircut has already occurred – it is just not reflected yet in the accounting books of the banks. The prices of bank equities already reflect the haircut, and the ECB and the bank of Greece have put money aside to provide liquidity to the banks. In any case, Greek and EU banks have to urgently raise more capital.

Others may see the restructuring as an opportunity not to implement the structural reforms. That would be quite wrong. The structural reforms are necessary to improve the competitiveness of the Greek economy, and for Greece to achieve a public sector surplus.

Does the haircut and the exchange of bonds imply a departure for Greece from the Euro? Not at all. On the contrary, the haircut and the exchange of bonds will bring Greece for the first time to a sustainable growth orbit closer to the central axis of the European Union.

This article suggests the absolutely necessary solution at the last moment. Does Mr. Venizelos (Greek finance minister) have the courage to propose it and implement it? Does Mr. Samaras (largest opposition party leader) and the other opposition parties have the courage to support it, even if it costs them votes? All Greeks must, even at this last moment, put first the national (and long term) interest of Greece.

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