Threatening to leave the eurozone may be Ireland's only way to break the link between its sovereign and bank debt.

by Blog Admin

Ireland faces a heavy fiscal and structural adjustment programme imposed by the Troika at the same time as some EU countries insist that it continues to pay the debt of its failed banks. With Spain now getting assistance for its banks under the European Stability Mechanism, **Aidan Regan** *argues that there are different rules for different eurozone countries. He writes that the only way that Ireland may be able to achieve its objective of separating sovereign from bank debt is to threaten to leave the monetary union.*

If Germany, the Netherlands and Finland insist that Ireland continues to pay the debt of its failed banks (and refuse to allow the European Stability Mechanism (ESM) to retrospectively take on this responsibility) there can probably only be one rational response by the Irish: threaten to bring down the house and pull out of the eurozone.

Without getting into the nuances of European level decision making there are four reasons why this is the case. Firstly, if these countries are unwilling to accept the decision of the European Council on June 29th that Europe needs to break the link between sovereign and bank debt in individual member-states, they have violated the rules of the game (or implicit social contract that emerged from this meeting). These rules are not written into hard legislation but they are premised on a gentleman's agreement that Europe, as a collective club, must help individual member-states, such as Ireland, to separate sovereign and bank debt. This is absolutely necessary if member-states are to develop the conditions for economic and employment recovery (which is good for all Europeans).

Secondly, if these countries – or more precisely their Finance Ministries – insist that 4.5 million people continue to shoulder the burden of private bank debt (which amounts to over €60bn and originates in a complex web of banking transactions within the EMU) without collective support from Europe, then no amount of pampering by the Irish government will fix the problem. The Irish approach of pampering stronger states has failed to change their position. Machiavelli in his excellent empirical study of power games in Europe during the 14th century (it is the 500 year anniversary of the *Prince* this year) famously stated that there are only two ways for political leaders to deal with potential enemies: pamper them or destroy them. The first has failed. Threatening (and being willing) to pull out of the euro might force a bit of self-enlightenment among European leaders.

Thirdly, regardless of whether Ireland gets a deal on its bank debt it will still require financial assistance from the ESM when the current round of funding expires. Ireland, whilst being a member of the Eurozone, cannot access financial markets. Therefore it will remain a non-sovereign economic country pursuing a fiscal and structural adjustment programme that is imposed by the Troika (the European Commission, European Central Bank and the International Monetary Fund). This is difficult for the government to sell to the electorate as it is. It will be impossible for any government to sell a Troika adjustment programme to citizens if these same actors refuse to cut the link between sovereign and bank debt. Furthermore, as long as the banking and sovereign debt is connected in Ireland, the prospect of the fiscal adjustment programme working declines. It is totally within the self-interest of all Europeans to relieve Ireland of its banking debt. In recognition of this, the IMF and ECB are probably furious with the bargaining position of the Dutch, Finnish and German governments.

Finally, and perhaps most importantly, it is completely inequitable to enable the ESM to take on the bank debt of Spain (and all European countries in the future) without retrospectively applying the same conditions for countries who took on their own bank debt at the beginning of the crisis. The most basic rule for any society, association or club is that its members are guaranteed equal rights and conditions. An association, such as the eurozone, that applies different rules for different countries is not politically sustainable. It will feed into the rise of populist political parties. Double standards are illegitimate and violate all common sense notions of social justice. It is for all of these reasons that it would be perfectly legitimate for Ireland to change strategy and drive a hard bargain.

There is nothing rational in accepting unwarranted pain, inequality, injustice or a violation of the rules. It is perfectly rational to strike back at those who are inflicting it. One would be forgiven therefore if the Irish confronted the Dutch, Finnish and German governments with a strategy that will potentially destroy them electorally. In the absence of European solidarity a bit of *realpolitik* is probably the only way the Irish government will achieve their objective of separating sovereign from bank debt, while simultaneously forcing Northern European governments to recognise what is really in their own interest.

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Note: This article gives the views of the author, and not the position of EUROPP – European Politics and Policy, nor of the London School of Economics.

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