Greece, the EU and crony capitalism

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Now and again history reaches an inflection point. Statesman and mere politicians, as the case may be, find themselves confronted with fraught circumstances and stark choices. February 2015 is one such moment.

For its part, Greece stands at a fork in the road. Syriza can move aggressively to recover Greece's democratic sovereignty or it can desperately cling to the faltering currency and financial machinery of the Euro zone. But it can't do both.

The bailout agreement expires at month end

So by the time the current onerous bailout agreement expires at month end, Greece must have repudiated its "bailout debt" and be on the off-ramp from the euro. Otherwise, it will have no hope of economic recovery or restoration of self-governance, and Syriza will have betrayed its mandate.

Moreover, the stakes extend far beyond its own borders. If the Greeks do not take a stand for their own dignity and independence at what amounts to a financial Thermopylae, neither will the rest of Europe ever escape from the dysfunctional, autocratic, impoverishing superstate regime that has metastasized in Brussels and Frankfurt under cover of the "European Project".

crony capitalist corruption

Indeed, the crony capitalist corruption and craven appeasement of the banks and financial markets that have become the modus operandi there are inexorably destroying the EU and single currency. By fleeing the euro and ECB with all deliberate speed, therefore, the Greeks will give-up nothing except the opportunity to be lashed to the greatest monetary train wreck ever recorded.

So Greek Finance Minister Yanis Varoufakis has the weight of history on his shoulders as he makes the rounds of European capitals this week. His task in not merely to renounce the ham-handed "austerity" dictated by the Troika. Apparently even the French are prepared to acknowledge that the hideous suffering that has been imposed on Greece's less fortunate citizens must be alleviated. Yet the latter is only a symptom of what's wrong and what stands in the way of a real solution.

The evil started with the bailouts

The true evil started with the bailouts themselves and the resulting usurpation by the EU politicians and apparatchiks of both financial market price discovery and discipline and sovereign democratic prerogatives. Accordingly, the terms of Greece's current servitude can't be tweaked, "restructured" or "swapped" within the Brussels bailout framework.

Instead, Varoufakis must firmly brace his interlocutors on the true history and the condition precedent that stands before them. ***Namely, that the Greek state was effectively bankrupt even***

before the 2010 bailout, and that the massive amounts of debt piled upon it thereafter was essentially a fraudulent conveyance by the EU.

Accordingly, Greece's legitimate debt is perhaps $175 billion based on the pre-crisis euro debt outstanding at today's exchange rate and the haircut that would have occurred in bankruptcy. Greece's new government has every right to repudiate the vast amount beyond that because it arose not from the actions of the Greek people, but from the treachery of EU politicians and the Troika apparatchiks—-along with the unfaithful stooges in the Greek parliament and ministries which executed their fraudulent conveyance.

The purpose was just plain ignoble and corrupt

Indeed, the purpose of the massive EU, ECB and IMF loans to Greece was just plain ignoble and corrupt. The European superstate deployed its vast fiscal and monetary powers to make whole the German, French, and Italian banks and other financial institutions which had gorged on Greece's sovereign debt. For more than a decade, heedless gamblers and lazy money managers and bankers had loaded up on Greek debt bearing yields that superficially bore a premium relative to the German and US treasury benchmarks, but in fact did not remotely compensate for the self-evident credit risk embedded in Greece's budgetary profligacy.

All of this was plainly evident. During the years before the crisis and especially under the oligarchy dominated Karamanlis government, Greece's spending relative to GDP soared. Yet Athens didn't bother to impose the taxes necessary to pay for its public spectacles, such as the 2004 Olympics, or its vast expansion of the state bureaucracy, its wasteful gorging on German defense equipment or the ever-rising subventions to special interest groups.

Greece was sinking into public insolvency

Moreover, it was also plainly evident at the time that even as Greece was sinking into public insolvency, its overall economy was on a fast track to crisis, as measured by a soaring current account deficit. In effect, northern European banks were flooding it with radically mis-priced debt, causing a orgy of unsustainable domestic borrowing and spending.

Indeed, during the 10-year run-up to the crisis, loans to private households and businesses soared by 5X. But in the standard Keynesian fashion, the booming investment and consumption spending financed by this debt eruption was not real or sustainable. It just temporarily flattered the GDP figures, making Greece's actual public debt burden even more onerous than the reported figures—especially after Goldman and other bankers bearing illicit accounting schemes and predatory derivative deals had perfumed the fiscal pig.

The resulting untoward impact of this entire, phony EU financial regime could not be more starkly evident than in the two graphs below. They contrast what was happening to Greece's true, permanent public debt burden—-with the ability of its profligate politicians to access international debt markets at super-cheap rates.

In fact, Greece had been on a steady path toward bankruptcy for 25 years, but as the EU monetary boom accelerated after the turn of the century and the false yields on its euro denominated debt continued to fall, the nation's public debt to GDP ratio was soon in terminal territory. The jig was up on its mad-cap leap into phony euro prosperity.

Saving the rotten regime

But when the crisis came, it was all about saving the rotten regime that had enabled imprudent risk-taking and gross missing pricing of sovereign debt throughout the European financial system. EU apparatchiks never cared a wit about the plight of the Greek people. Their desperate machinations were only for the purpose of appeasing the financial market speculators who would have otherwise caused debt service to soar throughout the EU, thereby generating an existential crisis that would have brought down the failing machinery of the euro and the EU's superstate rulers in Brussels.

So five years of false history needs to be aired and purged. The baleful truth is that widows and children, among others, are starving in Athens today in order that financial speculators would not have a hissy fit and that the apparatchiks of the EU could hang on to their power, privileges and cushy sinecures.

Varoufakis himself recently made this crystal clear:

"Europe in its infinite wisdom decided to deal with this bankruptcy by loading the largest loan in human history on the weakest of shoulders, the Greek taxpayer. What we've been having ever since is a kind of fiscal waterboarding that has turned this nation into a debt colony."

Effectively eliminating credit risk

The real assault on Greece and the common people of every other European country stems from central bank corruption of the sovereign debt market; and from the associated crony capitalist regime of bank bailouts. By effectively eliminating credit risk and by artificially driving the yield on public debt to essentially zero, the European superstate has supplanted old fashioned price discovery, accountability and honesty in the entire multi-trillion market in sovereign European debt with the destructive "whatever it takes" writ of its financial apparatchiks.

Consequently, and as exemplified by today yields of 160 bps, 54 bps and 26 bps, respectively, on the Italian, French and German 10-year bonds, the European government debt market has become a financial freak show. These insane prices have nothing to do with "deflation"; they are pure gifts to front running speculators, who, after five-years of bailouts and ZIRP, have every reason to believe that the craven fools running the European superstate will never permit a dime of losses.

Needless to say, exempting bankers and investors from the consequence of their own folly and greed is fatally inimical to democratic self-governance. As is now so evident in Europe's mounting economic stupor and gathering political fractures, it inexorably leads to unaccountable, centralized rule of fiscal life and financial markets, alike; it is the reason why the Greek people have been stripped of their sovereignty and turned into debt slaves of the EU apparatchiks.

A painful bankruptcy

So the status quo ante must be restored, and it is not hard to imagine how it would have played out. Had the actual parties to Greece's prior spree of fiscal profligacy been allowed to step up to the plate and to shoulder the unpleasant consequences of their previous feckless actions, the outcome would have been a painful bankruptcy—but one which would have cleared the decks of the real culprits and paved the way for a constructive revival of the Greek economy.

First and foremost, the foolish European banks and bond speculators who ignored the self-evident risks of Greece's runaway finances would have taken the deep haircuts needed to put Greece's debt back on a sustainable basis. There would have been no new debt to bailout the culpable financial operators who lured Greece's government into unsustainable borrowing at artificially cheap yields in the first place; and no fraudulent conveyance of losses from these financial institutions to the common folk of Greece. Rather than soaring to its present crushing total of $350 billion, Greece's debt would have actually been rolled back sharply from the $230 billion level it was approaching in 2010.

Moreover, had the crisis been allowed to run its course to bankruptcy when it came to a head in 2010, the resulting massive losses to banks and speculators would have conveyed two essential messages— without which neither political democracy nor honest financial markets can survive.

There was never any mutualization of debt

The first message would have been to mind the financial condition, policies and politics of each and every sovereign issuer within the EU; there was never any mutualization of debt anywhere in the documents and treaties of the EU and no reason to believe that markets could simply command it when it became convenient.

The second, even more crucial message, would have been that there is an inherent, huge risk factor embedded in euro denominated sovereign debt because unless the German army is to occupy Europe, there is no basis, ultimately, for compelling any member country to abide by the fiscal limits of the treaty or even to stay in the EU.

Would that the punters in London and Zurich and the complacent bankers in Munich and Paris have suddenly found that they had been issued new bonds denominated in drachma at 20 cents on the dollar. The current crop of self-serving crony capitalist who run these institutions would have been forced to find a new line of work long ago.

Temptation to issue way too much debt

And let us not mince words. Governments will always be tempted to issue way too much debt. The only way to restrain them is to allow the bankers and investors who buy their paper to face the risk of ruinous losses—both in their financial statements and their career prospects.

Let me tell you something else. Had Greece been allowed to go bust in 2010, then and there real "price discovery" would have commenced in the European sovereign debt markets. And there would have been a two-way therapy as a result. The bankers and investors who bought Greece's junk would have been flushed, and Greece's politicians would have faced their own day of reckoning.

In fact, in the wake of a bankruptcy, it would have been the Greek people and their government—- not the officious bureaucrats of the Troika—-who would have been obliged to formulate and impose the requisite measures of austerity. Needless to say, the calamity and embarrassment of a national bankruptcy five years ago would have caused the Greek electorate to throw-out the corrupt, incumbent politicians and the crony capitalist oligarchs that brought the nation to ruin in the first place.

A new post-bankruptcy government

And notwithstanding the tough choices that would have confronted a new post-bankruptcy government, the resulting period of austerity and fiscal self-discipline would have had a therapeutic purpose. That is, to enable the Greek state to function without new borrowings and to eventually restore its credit in the international capital markets.

Had Greece been forced into bankruptcy and the drachma, it would have been required to endure a brutal regime of "austerity" as it cut its primary deficit to zero; and it would not have had the easy escape option to run the drachma printing presses red hot and monetize its fiscal debt. That would have caused a plunging exchange rate and massive flight of domestic capital and savings.

Stated differently, Greek democracy would have been forced to make tough choices, including deep cuts to pensions, curtailment of subsidies to domestic industries and interest groups, wholesale firings at its bloated public bureaucracies, and painful tax increases on millions of citizens. But the "memorandum" laying out this plan of austerity would not have been written in Brussels and delivered by officious bureaucrats speaking in French, German and English tongues.

Instead, the sacrifices and pain would have been hammered out in the halls of Greece's parliament and its government ministries. Had the politicians and officials who run these institutions attempted to cheat, kick-the-can and otherwise indulge in budgetary self-delusion, they would have been quickly cut short for lack of cash.

Frau Merkel and the faceless bureaucrats

Likewise, any attempt to make ends meet by monetizing the debt would have instantly imposed pain on the Greek citizenry in the form of a plummeting Drachma and prohibitive cost of imports. In short, the public's ire would have been directed where it belongs—-at its own politicians in nearby Athens, not Frau Merkel and the faceless bureaucrats who had been sent to Greece to do her bidding.

So if the task at hand is to turn the clock back to 2009, what is the math involved in repudiating the $175 billion fraudulent conveyance by the EU and how can the new Greek government get it done?

The first part is straight forward

The first part is straight forward. Based on the widely circulated Bruegel numbers, Greece purportedly owes the IMF $35 billion. ***It should repudiate all of its IMF debt because never again should any Greek government go hat-in-hand to the IMF. The latter is a loathsome institution—-a gigantic fount of moral hazard and hand-maiden of the world's crony capitalist bankers.*** During the last four decades it has done little except rescue the soured bets of bankers and bond managers and impose destructive shock therapies on fiscally impaired supplicants, thereby stripping these sovereign nations of the obligation to rectify their own excesses and formulate their own plans of austerity and recovery.

Indeed, the Greeks could do the world an immense favor by not only defaulting on the debts fraudulently conveyed by the IMF, but perhaps it could also threaten to arrest any IMF bureaucrat who crosses its border. Clueless mountebanks like Ms. Lagarde need to understand they are not doing gods work after all; and legislators in Washington, London and Tokyo who keep sending multi-hundred billion blank checks to the IMF need to explain to their constituents why their tax dollars are being squandered bailing out the bad bets of international bankers.

A 50% 'haircut' for Germany in 1953

Likewise, if a 50% haircut was good enough for Germany in 1953, it ought to suffice for the settlement of Greece's obligations to the EU institutions today. According to Bruegel's estimates, the combined amount owed to the Eurozone countries and the ECB is about $230 billion, meaning that $115 billion could be sliced off that total.

Finally, the $25 billion balance of the $175 billion haircut needed to repudiate Greece "bailout debt" would have to come from the approximate $70 billion owed to private banks and bond investors outside of Greece. In practice that would amount to no hair cut at all from the current blown-out market value of these obligations. Indeed, the hedge fund speculators and other punters which scooped up this paper during the illusionary Draghi recovery of the past year would be more than lucky to recover 67 cents on the dollar.

Announcement, not negotiations

So the issue is not the math—its how to get the job done. The answer is that it needs to be done by way of announcement, not negotiations. The debt involved here is not legitimate; it is a fraudulent conveyance foisted upon the Greek people by the bureaucracy and politicians of the European superstate.

In announcing that it is leaving the Euro, therefore, Greece only needs to enumerate how much it intends to pay on its EU/ECB outstandings and over what period of time. About a century ago even the vengeful French were willing to give an impoverished Germany 50 years to make it reparations. Today's prosperous statesman in Berlin should be happy to receive the same.

The chorus of Keynesian apologists

So history is at an inflection point. Hopefully the disparate coalition of leftist politicians and anti-establishment rebels that the Greek people have turned to in sheer desperation will not be bamboozled by the present chorus of Keynesian apologists for the EU's rogue regime of banker bailouts and printing press monetarism.

Greece does not need to borrow new money from any one, and by announcing that it will refuse the next installment of the bailout it has already embraced that cardinal principle. Moreover, after a 2-3 year debt service suspension needed to stabilize its economy and public finances, it can live with a modest primary budget surplus for years to come in order to devote perhaps 4% of GDP to servicing its $175 billion of legitimate external debt. Except this time the required fiscal surpluses would be thrashed out in the democratic forum where the very idea of rule by the people first arose.

Greece can re-establish its own central bank

Likewise, Greece can re-establish its own central bank, currency and international credit if it is willing to abide by a second cardinal rule. Namely, its reconstituted central bank must be constitutionally prohibited from monetizing the debt of the Greek state or receiving government subsidies after its initial capitalization to create a Drachma based monetary system.

Let its central bank own RMB, USD and gold. Under that central banking arrangement, domestic interest rates would be set by market forces. Reckless printing of Drachma to buy any of these global assets would be self-evidently futile—even to central bankers. And a financial system and currency which strictly shackled its central bankers would in no time become a haven for domestic savers and capital inflows, alike.

Greece can restore economic growth and prosperity

Finally, if Greece's new leftist regime actually believes that it can restore economic growth and prosperity through public investment—a belief that does not remotely hold up under the evidence—- it need only adhere to a third cardinal rule. That is, it must find an efficient, equitable and politically sustainable way to raise the money through current taxation.

Greece has been borrowing its way to disaster long enough.