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The Debt Crisis in the Euro Zone

A tug-of-war between the political and the economic sphere

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Section II: Economics, Politics, Law

Europeanisation and Social Transformation: Legal vs. Cognitive Aspects of Change¹

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Introduction

The Greek fiscal crisis that erupted in the autumn 2009 in the wake of the international financial crisis 2008-2009 shaped a real challenge to the governance of the EU project in general and of its crown jewel, the EMU project, in specific. Obviously not only the international financial markets were at risk. This could also, according to numerous expert comments within the field, soon be the case for the whole EMU project as such.

The political discourse vocabulary was soon very much about austerity measures, haircuts, stress tests, necessary reforms, state bankruptcy, defaults, lack of confidence, and crisis of capitalism and so on. In 2010 the acronym PIIGS was coined and commonly used, referring to the same kind of problems with too high budget deficits and state debts in Portugal, Ireland, Italy, Greece, and Spain.

The crisis meetings between interested parties have since followed one another and not surprisingly the crisis in terms of market turmoil and political wrangling has during the whole process received intensive worldwide attention in the media as well as among politicians and economists, and in public opinion in Europe.²

The overall purpose of this paper is to approach the problematique of the euro zone crisis 2009-2012 by putting “a basic underlying tension in the political-economic configuration in advanced capitalist societies” (Streeck 2011: 5) to the fore.³ Disequilibrium and instability, according to Streeck, is the rule rather than the exception, and this fact has found expression in a historical succession of disturbances, of which the crisis referred to is just one. With the crash of privatized Keynesianism in 2008, the crisis of post-war democratic capitalism entered its fourth and latest stage after the successive eras of inflation, public deficits and private indebtedness according to Streeck. He argues that the distributional conflict since 2008 has turned into “a complicated tug-of-war between global financial investors and sovereign nation-states” (Streeck 2011: 20-21). At the same time as “markets must avoid pushing states into declaring sovereign bankruptcy, always an option for governments if market pressures become too strong [...] financial markets may be looking forward to a promising fight against political interference, once and for all reinstating market discipline and putting an attempt to all political attempts to subvert it” (ibid. p. 22). Governments for its parts have different reasons, often in the interests of investors, to act in solidarity, among other things in order to protect themselves from a general increase in interest rates on government bonds.

The more narrow aim of the paper is to describe and explore the current euro crisis through the lenses of a “tug-of-war” (Streeck 2011) between the political and the economic sphere, on the one hand EU institutions as well as member states, on the other hand the financial market. The empirical data from the political sphere consists of decisions from relevant actors within the EU system like the ECB, the Commission, the European Council, the Council as well as comments, conclusions, and statements from ministers, commissioners and the like at some critical junctures. Data from “the other side” is mainly based on the ratings from the three leading rating agencies in the world: Standard & Poor’s, Moody’s, and Fitch Ratings.

¹ This paper was originally intended for “Diversity in Economics” (Chair: Dietmar Meyer).

² See Kevin Featherstone, “The Greek Sovereign Debt Crisis and EMU: A Failing State in a Skewed Regime”, *JCMS 2011, Volume 49, Number 2*, pp. 193-217, for interesting comments and references on economic governance in the euro area as well as EUs “somewhat mixed record” in responding to the banking crisis after the collapse of Lehman Brothers in September 2008.

³ See Wolfgang Streeck, “The Crisis of Democratic Capitalism”, *New Left Review 71, September-October 2011*, pp. 5-29. See also Wolfgang Streeck, “Markets and Peoples”, *New Left Review 73, January-February 2012*, pp. 63-71.

It is something of a truism saying that the rating agencies have an extremely influential position in the international economy. Volcker⁴ argues that the role and structure “need further review” and according to Sinclair (1994) it is about “governance without government”. They exert power over sovereign states, raising issues of accountability, Featherstone (2011) argues. The importance, however, on the international scene is relatively new, and probably a consequence of globalisation and market deregulation one could argue. Not surprisingly the role of the rating agencies has in many cases resulted in sharp criticism during the first decade of the 21st century, even so during the so called euro crisis.

An underlying assumption in this paper is that rating agencies can be seen as markers or bearers of concerns of the financial market vis-à-vis the political sphere. The starting point is to analyze the so called tug-of-war as a kind of ping pong game including an open question regarding who is acting and who is reacting in this game, or in other words: who is in charge of the process? Is there a game on equal terms (‘giving and taking’) or has any of the players a more ‘hegemonic position’ in this interactive game? In what ways did the tension between the political actors and the financial markets during the crisis referred to express itself?

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In what follows I will first present an analytical framework and then turn to the sequence of events that has taken place since late autumn 2009 until March 2012. My short empirical focus though will be on some critical junctures during this crisis. Finally I will give some concluding remarks.

Disturbances within the political and economic order

With the crash of privatized Keynesianism in 2008, the crisis of post-war democratic capitalism entered its fourth and latest stage after the successive eras of inflation, public deficits and private indebtedness Streeck argues. According to him the distributional conflict since 2008 has turned into “a complicated tug-of-war between global financial investors and sovereign nation-states” (Streeck 2011: 20-21).

⁴ See Paul A. Volcker, “Financial Reform: Unfinished Business”, *The New York Review of Books*, November 24, 2011, Volume LVIII, Nr 18.

According to Streeck the important leap in public indebtedness after 2008 reflected that no democratic state dared to impose on its society another economic crisis of the dimension of the 1930s as punishment for the excesses of a deregulated financial sector. Even though the governments took upon themselves a significant share of the new debt in order to reassure private-sector creditors, “it could not prevent rising suspicions on the part of the same financial markets that, in the process of rescuing them, national governments might have over-extended themselves” (Streeck 2011: 20). In other words, creditors began to demand turning back to sound money “through fiscal austerity, in search for reassurance that their vastly increased investment in government debt would not be lost” (Streeck 2011: 21).

At the same time as “markets must avoid pushing states into declaring sovereign bankruptcy, always an option for governments if market pressures become too strong [...] financial markets may be looking forward to a promising fight against political interference, once and for all reinstating market discipline and putting an attempt to all political attempts to subvert it” (Streeck 2011: 22). Governments for its parts have different reasons, often in the interests of investors, to act in solidarity, among other things in order to protect themselves from a general increase in interest rates on government bonds.

What we experience now is nothing less than the financial markets fighting with the very states, or with the words of Streeck “the complex contests currently taking place between financial institutions and electorates, governments, states and international organizations [...] Now the issue is how far states can go imposing [...] the profit expectations of the markets on their citizens, while avoiding having to declare bankruptcy and protecting what may still remain of their democratic legitimacy” (Streeck 2011: 24). In a lightly updated version of the earlier article from 2011 Streeck (2012: 64) concludes that it is obvious that the democratic states of the capitalist world have two sovereigns, not one: “their people, below, and the international markets above. Globalization, financialization and European integration have weakened the former, and strengthened the latter”. ‘Capital whisperers’ have succeeded ‘people whisperers’, and ‘investor confidence’ is more important than ‘voter confidence’. Consequently, it is the money of the banks that is at stake, not ours, and a rescue package is not about genuine solidarity with the people of different member states but with the financial markets.

Governance without government

It is something of a truism saying that the rating agencies have an extremely influential position in the international economy. Their influence is worldwide, even though not uncontroversial. Volcker (2011) argues that the role and structure “need further review” and according to Sinclair (1994)⁵ it is about “governance without government”. They exert power over sovereign states, raising issues of accountability, Featherstone (2011) argues. The importance, however, on the international scene is relatively new, and probably a consequence of globalisation and market deregulation one could argue.

Crouch (2009)⁶ argues that during the so called privatised Keynesianism vast quantities of totally factious cake were produced, and on basis of the notional values of which even vaster quantities of such cake were leveraged: “Bad debts were funding bad debts, and so on in an exponentially growing mountain” (Crouch 2009: 393). According to her the financial institutions of Wall Street, the City of London or elsewhere developed forms of knowledge that encouraged destructive decisions, and this is what she calls “the Achilles’ heel of the model”. While the information technology was supposed to provide the market traders with updated information on a global basis, it paradoxically raised the opportunity cost of any detailed searches for complex information, like the composition of risks. According to Crouch the rating agencies, the markets own solution to certifying the quality of financial institutions as well as national economies, followed the same path. Referring to the Icelandic banks that were accorded the highest possible rating just before they collapsed, she concludes that “the agencies were not inquiring deeply into the quality of their assets. Aware that the traders in the markets who were using the ratings were not interested in such knowledge, they also ceased to look for it” (Crouch 2009: 394).

Not surprisingly the role of the rating agencies has not only resulted in sharp criticism during the first decade of the 21st century, but even more so during the so called euro crisis. With reference to the financial crisis in 2008 Paul Krugman, Nobel Prize Laureate in Economics, voiced serious critique against the agencies. In an article in *The New York Times* (“Berating

⁵ Sinclair, T.J. (1994), “Passing Judgement: Credit Rating Processes as Regulatory Mechanisms of Governance in the Emerging World Order”, *Review of International Political Economy*, Vol 1, No 1, pp. 133-159.

⁶ See Colin Crouch, “Privatised Keynesianism: An Unacknowledged Policy Regime, *The British Journal of Politics and International Relations (BJPIR)*: 2009, Vol 11, pp. 382-399.

the Raters”, www.nytimes.com, April 26, 2010) Krugman called the whole system “corrupted”, even though the system “looked dignified and respectable on the surface”. The US Congress was in 2010 considering new legislation in order to increase the regulation of the agencies, among other things criticising them for contributing to the sub-prime mortgage crisis and more generally for offering poor forecasts.

At the same time a renowned German economist, Thomas Straubhaar, went out in *Der Spiegel* (“Warum Rating-Agenturen verramscht werden müssen”, www.spiegel.de, *Spiegel Online*: 2010-05-15,) and demanded the three leading agencies to be sold off. According to him they have no instruments predicting a crisis. Rather, they are likely to react when a crisis is a fact, and Straubhaar argued that the crisis in Greece was the proof that rating agencies worsen crisis instead of prohibiting them. Straubhaar was also very critical of the strong dominance of the US-based agencies and was of the opinion that European agencies would provide more competition.⁷

Myriam Fernández de Heredia, head of the Sovereign and Public Finance (IPF) group in EMEA (Europe, Middle East, and Africa) at Standard & Poor’s, clarified sovereign ratings in an article in *World Finance* (“Regaining focus on sovereign credit ratings”, March 30th, 2012, www.worldfinance.com) due to the debate on the downgrading of nine euro-zone countries in January 2012, and the US downgrade in August 2011. One point that she is stressing is that credit ratings “are not assessments of investments merit, they are assessments of creditworthiness”. S&P’s rating reflects the agency’s view “on both capacity and, importantly, the willingness of the borrower to meet its financial commitments in full and on time [...] while credit quality may be a factor in investment decisions, there are numerous other factors investors may consider prior to deciding whether to buy, sell, or hold”. Furthermore, she discusses among other things credit ratings and default probability; the relevance of sovereign credit ratings; credit rating agencies, political risks, and the political agenda; ratings and the market prices; and ratings and market behaviour”.

⁷ Even the European Commission, the European Central Bank as well as many prominent ministers from member states of the EU have on different occasions during the current period of the euro crisis expressed strong dissatisfaction of the rating agencies’ influence.

When more than twenty Italian banks were downgraded by Moody's in May 2012, Italian bankers condemned the move as "an assault on Italy", that should be ignored: "Once more rating agencies turn out to be a destabilizing factor for financial markets with their partial and contradictory statements", the Italian Banking Association declared (IHT, 2012-05-22). In an article in International Herald Tribune Harvey Morris asks whether the latest moves to put the rating agencies under the spotlight are "a case of seeking to curb the overweening power of unaccountable private institutions or are the Europeans just out to shoot the messenger?" According to Harvey it seems to be a bit of bot: Proposed reforms are geared to making investors less reliant on judgments of "the big three" at the same time as ending their near monopoly in the sector" ("Europe Hits Back at Rating Agencies", IHT, 2012-05-22).⁸ In 2009 Standard & Poor's took action to help restore confidence in ratings by among others publishing detailed information designed to help market participants better understand what Standard & Poor credit ratings means. It says further: "Standard & Poor's are designed primarily to provide relative rankings among issuers and obligations of overall credit-worthiness; the ratings are not measures of absolute default probability. Creditworthiness encompasses likelihood of default, and also includes (i) payment priority, (ii) recovery, and (iii) credit stability."⁹

The technical details regarding the rating procedure are quite complex and it makes no sense for the purpose of this paper to go into detail on this, just some brief remarks using S&P as an example. Big letters from 'AAA' to 'D' are used. An obligation rated 'AAA' has the highest rating, better than AA, better than A, better than BBB and so on. The obligor's capacity when rated 'AAA' to meet its financial commitment on the obligation is extremely strong. An obligation rated 'D' is in payment default. The ratings from 'AA' to 'CCC' may be modified by the addition of a plus (+) or minus (-) sign to show relative standing within the major rating categories.¹⁰

⁸ For interesting discussions on the role of rating agencies, the regulation of them, as well as references, see for instance Nicolas Véron (2009), Rating Agencies: "An Information Privilege Whose Time Has Passed", *Bruegel Policy Contribution (2009:01)*; Jonathan Katz, Emanuel Salinas, and Constantinos Stephanou (2009), "Credit Rating Agencies", *Public Policy for the Private Sector, October 2009*.

⁹ Standard & Poor's (2009), "Understanding Standard & Poor's Rating Definitions", June 03 (www.standardandpoors.com/ratingsdirect)

¹⁰ Standard & Poor's (2011), "Sovereign Government Rating Methodology and Assumptions", June 30 (www.standardandpoors.com/ratingsdirect). See also Standard & Poor's (2011), "Standard & Poor's Ratings Definitions", April 27(www.standardandpoors.com/ratingsdirect)

The S&P sovereign rating methodology focuses on factors that affect a “sovereign government's willingness and ability to service its debt on time and in full”. The analysis concentrates “on a sovereign's performance over past economic and political cycles, as well as factors indicating greater or lesser fiscal and monetary flexibility over the course of future economic cycles”. The five key factors that form the foundation of the analysis are:

1. Institutional effectiveness and political risks, reflected in the political score.
2. Economic structure and growth prospects, reflected in the economic score.
3. External liquidity and international investment position, reflected in the external score.
4. Fiscal performance and flexibility, as well as debt burden, reflected in the fiscal score.
5. Monetary flexibility, reflected in the monetary score.

Needless to say the analysis of each of the five key factors embodies a combination of quantitative and qualitative elements. Some factors, such as the robustness of political institutions, are primarily qualitative, while others, such as the economy, debt, and external liquidity are mostly quantitative indicators.

* * *

Greek data makes the financial markets concerned

George A. Papandreou became prime minister of Greece in October 2009. A lifelong socialist, his time in office should become dominated by the debt crisis left behind by his conservative predecessor. In November 2011, two years after he set off the long-running European debt crisis by revealing that his predecessor had covered up a huge budget deficit, Papandreou agreed to step down as part of a deal that created a unity government in return for support for a debt relief plan negotiated by European leaders.

During that period Papandreou had kept Greece at least technically solvent, but at the cost of crushing the unity of his own party and seeing his own popularity drop as austerity measures demanded by the rest of Europe he drove the country into a deep recession. And most of his energies ended up being devoted to the dismantling of large parts of the welfare state created by his father and grandfather when they were prime ministers. In November 2011, Lucas Papademos, a respected economist was appointed prime minister.

In late October 2009, some weeks after the election, Papandreou announced that the country's budget deficit had expanded to almost 13 per cent of GDP, far more than former PM Karamanlis's government had said, and that the economic situation was "a catastrophe". S&P downgraded Greece's long-term credit rating on 16 December 2009 because of the weakening in the country's finances, one week after Fitch having downgraded Greece to the same credit quality (BBB+). The agency said it cut its rating on Greece to BBB+ (close to speculative or non-investment grade) from A- and left the country on Credit Watch negative, meaning it could be lowered further:

"The downgrade reflects our opinion that the measures the Greek authorities have recently announced to reduce the high fiscal deficit are unlikely, on their own, to lead to a sustainable reduction in the public debt burden," it said in a statement. "Moreover, we believe that the government's efforts to reform the public finances face domestic obstacles that would likely require sustained efforts over a number of years to overcome [...] The Credit Watch placement reflects our view that the ratings could be further lowered if the government is unable to gain sufficient political support to implement a credible medium-term fiscal consolidation program."¹¹

Standard & Poor's (S&P) said that because it now expects overall debt and public deficit levels to rise, which will cost the government more to fund, "we see Greece's fiscal flexibility diminishing more than we had previously expected" and total debt as a percentage of Greek GDP will hit 126 percent of GDP in 2010 and around 138 percent of GDP in 2012: "In our view, the increasing debt-service burden narrows the scope for debt stabilization, particularly against the background of what we expect will be a significantly weaker near-term economic growth environment," it said. The agency said it should resolve its Credit Watch stance in the next three to four months and this depends on whether the government can find "sufficient political support to implement a credible medium-term fiscal consolidation program." If political considerations and social pressures hamper progress in establishing a framework for containing the debt burden, "we could lower the ratings further," it warned.

¹¹ "Standard and Poor's downgrades Greek sovereign rating", AFP 16 December 2009 (<http://www.france24.com/en/node/4950029>)

PM Papandreou began a desperate work to find ways to cover payments on Greece's \$400 billion in debt, as bond investors drove interest rates ever higher. He repeatedly insisted that the Socialists should not cut wages and would protect poorer citizens, but hardline Communist-led unions rejected a "social dialogue" initiated by the government. The political and economic reality though forced Papandreou almost immediately to promise reduces on public sector hiring and pay, a ten percent cut in civil servant benefits and a reduction in military spending. He also called for a 90-percent tax on bonuses at banks and an overhaul of the fiscal system in measures due to come into force from early 2010. However, both markets and the European Commission wanted more, with the commissioner Joaquin Almunia saying that EU awaited "concrete measures that will strengthen fiscal adjustment in 2010 and ensure a fast consolidation of public finances."¹²

The dark clouds on the horizon, however, were approaching. As Featherstone (2009: 204) has shown, successive Greek governments had sustained high level of public debt, fluctuating around 100 per cent of GDP since early nineties. The real concern regarding Greece's fiscal position came on 20 October 2009, when the Greek finance minister announced almost a tripling of the level of government debt to 12.8 per cent of GDP, increased further to 13.6 per cent after further calculations in early 2010. Not surprisingly Greek data became a major issue for the international financial markets and as if that was not enough all three leading rating agencies further downgraded Greece's status and almost immediately "the sequence of downgrades greatly exacerbated its position [...] and brought into sharp relief their highly influential position in a changing international economy" (Featherstone 2009: 200).

* * *

On April 23, 2010, Mr Papandreou declared his country's economy "a sinking ship" and formally requested the lower-interest loans promised by the European Union and the International Monetary Fund. The bailout, worked out over weeks of negotiations, called for 110 billion euros in loans over the next three years, intended to avoid a debt default. Shortly thereafter two institutions were set up by the EU in order to manage further rescue loans: the European Financial Stability Mechanism (EFSM), and the European Financial Stability Facility (EFSF), both of them with borrowing guarantees from the European Commission.

¹² AFP, 16 December 2009 (<http://www.france24.com/en/20091217-unions-strike-against-government-austerity-plan>)

Not surprisingly S&P declared Greek debt “junk status” (April 27) and also downgraded Portugal, as investors worried political pressures could block the euro bailout of Greece. S&P cut its rating of Greek government debt to BB-, the first level of speculative status. The downgrade put Greece on par with Romania and below Kazakhstan among others. The agency referred to the “political, economic, and budgetary challenges that the Greek government faces in its efforts to put the public debt burden onto a sustained downward trajectory.”¹³

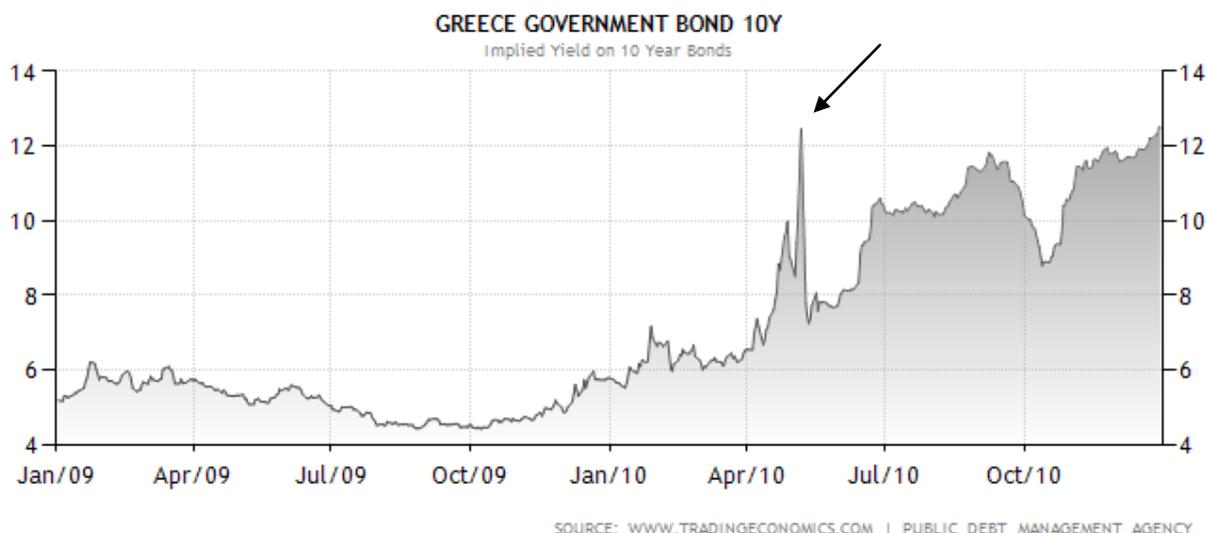
The international comments from the financial sector were talking about “Greek crisis which has spiralled out of control”, “it is like coconuts falling from the tree”, “outright panic among investors”; “Greece has entered a death spiral of government insolvency”.¹⁴ Probably as a consequence of the downgrading of Greece’s credit worthiness to junk status Greek government bond yields skyrocketed in late April to more than 12 % and thereby setting the scene for the first rescue agreement with the EU and IMF in May. Even though the yield curve then fell sharply, it was only temporary. The message from the financial market was that the bail-out did not sufficiently address the underlying issues of the crisis. It makes sense to interpret the configuration of the yield curve as an indicator of financial stress. Bonds issued by national governments in foreign currencies are normally referred to as sovereign bonds and “the yield required by investors to loan funds to governments reflects [...] the likelihood that the debt will be repaid”.¹⁵

Figure 1 Greek Government Bond Yield (10 Year)

¹³ <http://www.reuters.com/article/2010/04/27/us-greece-idUSLDE63P0LU20100427>. Fitch had on 9 April 2010 downgraded Greece to BBB-.

¹⁴ Ibid.

¹⁵ <http://www.tradingeconomics.com/greece/government-bond-yield>



Not surprisingly the EU response to the Greek crisis in late 2009 and early 2010 was rather passive. As can be seen in Figure 1 the yield on Greek government bonds (10 year) were still in line with the yield during January-April, even though increasing in November and December. Greece was not even present in the text in the conclusions from the European Council Summit in October and December 2009. Nor did the the policy makers seem to have a premonition of the forthcoming financial turmoil. On the contrary it was said that the economic decline “is coming to a halt, with a stabilization of financial markets and an improvement in confidence”.¹⁶ The leading politicians seems to have been more concerned about the consequences of the global financial downturn in 2008-2009 from a general perspective and they called “for rapid progress to be made on the strengthening of the regulatory framework for the prevention, management and resolution of financial crises and on the development of a comprehensive EU-wide framework for closer policy coordination on financial stability”.¹⁷

The EU Summit in December 2009 was also focused in more general terms on what to do in order to prevent global financial crisis in the future, and one gets a feeling that the leaders had not yet realized the deep consequences of the upcoming Greek crisis. The language was typically technical and bureaucratic: “the financial crisis has clearly demonstrated the weaknesses of the current regulatory framework and supervisory arrangements for financial institutions” or “the European Council welcomes the rapid and determined action taken by the Council which has agreed a fundamentally new structure for financial supervision in

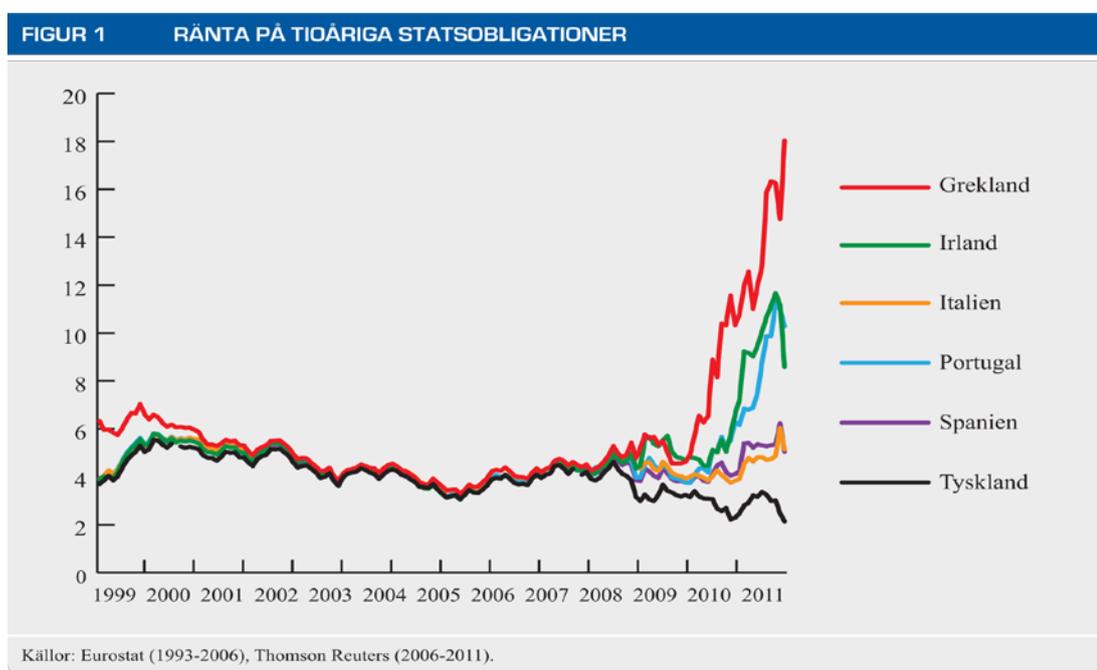
¹⁶ Presidency Conclusions, European Council 29-30 October 2009 (15265/1/09 REV 1, CONCL 3)

Europe”.¹⁸ Regarding the decision in May 2010 to bailout Greece The European Council promises that it would be “unique and exceptional”.¹⁹

The financial markets increase its pressure

The market increased its pressure on the political sphere during 2011 and the summits followed one another. Even though the political activity was extremely high in 2011 in order to get back the lost confidence from the financial markets, the sequence of downgrades continued, followed by increased bond yields regarding Greece, Ireland and Portugal. A general lesson is that the positive effects of announcements by policymakers of new measures intended to address the sovereign debt crisis were mostly of very short duration, as is clearly shown in the bond yield curves (Figure 1-4). Obviously credit investors’ longer-term worries remained high and the view of the financial markets was that measures taken did not sufficiently address the underlying issues. Consequently the fall in bond yields turned after some time in an upturn again, thereby forcing policymakers to focus on the need for new measures. To be continued and concluded...

Figure 2 Government Bond Yields (10 Year): Greece, Ireland, Italy, Portugal, Spain, Germany (Tyskland)
Source: Calmfors (2011)



¹⁷ Ibid.

¹⁸ Conclusions, European Council 10-11 December 2009 (EUCO 6/09, CO EUR 6, CONCL 4)

Figure 3 Greece Government Bond Yields (10 Year)

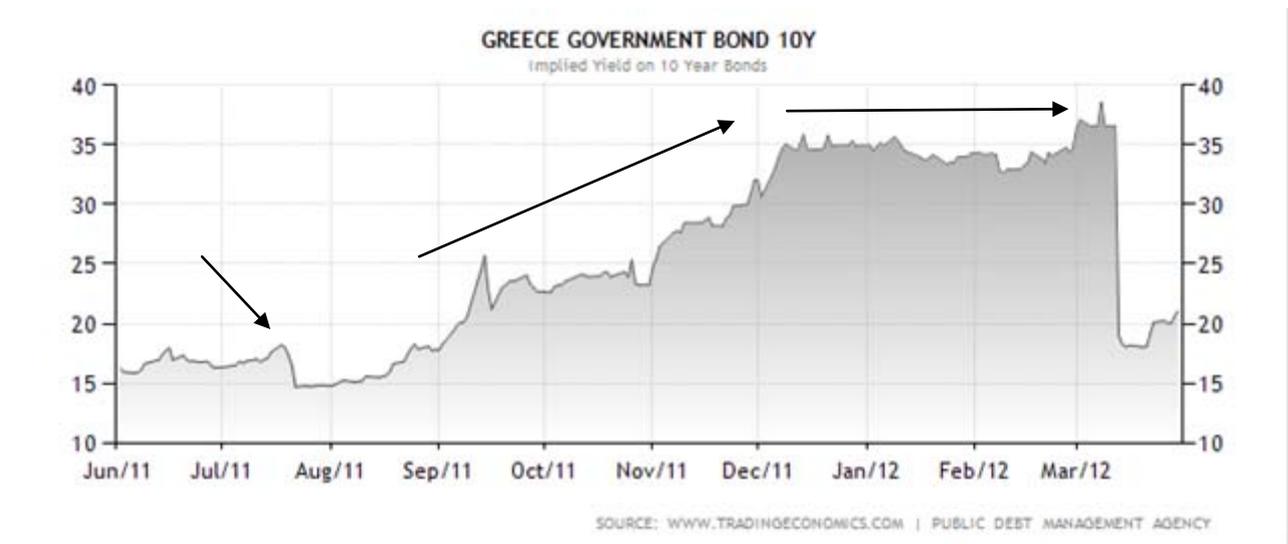
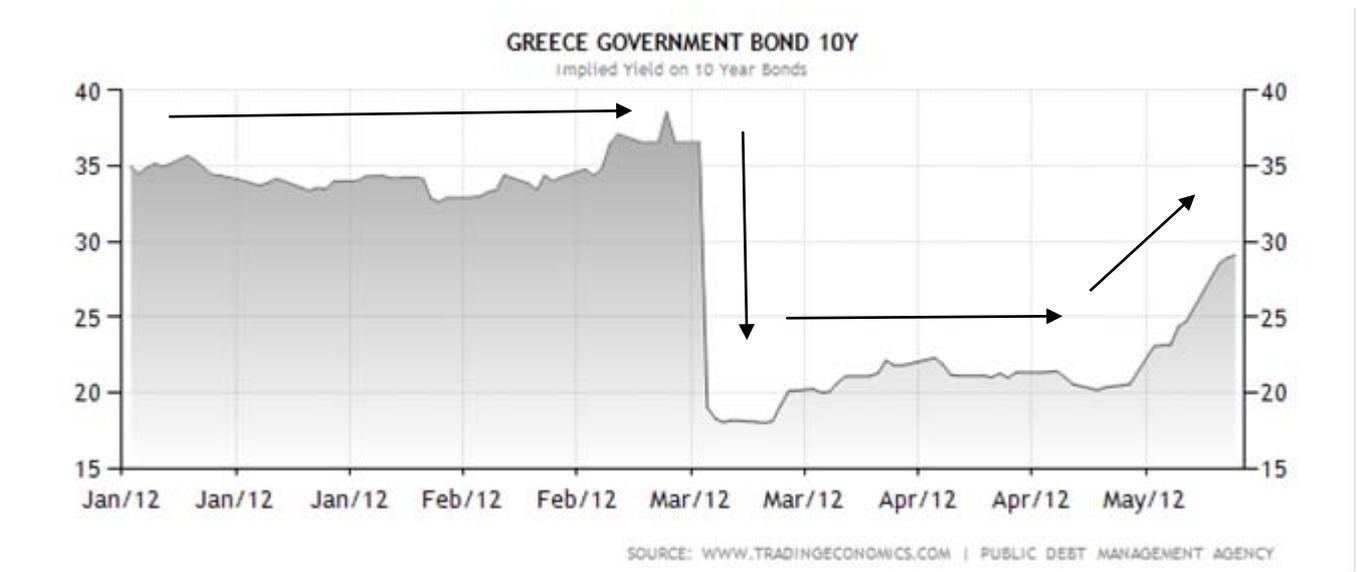


Figure 4 Greece Government Bond Yields (10 Year)



Time is running out and Europe is holding its breath

¹⁹ Conclusions, European Council, 17 May 2010, (ec.europa.eu)

During the second half of 2011 the crisis meetings continued to follow one another and not surprisingly the crisis received even more intensive attention. The events can easily be framed in terms of a lengthy tension or a tug-of-war between the political and financial sphere. In August Italian bond yields reached six per cent, probably closely related to lack of confidence due to PM Berlusconi's personal scandals. In September S&P downgraded Italy's credit rating, depicting its outlook as "negative". Even though the political side at certain occasions voiced heavy criticism against the downgrading from the rating institutes, they were also very outspoken regarding actions needed to meet the message of the markets and rebuild confidence and trust. In his speech to the European Parliament in September 2011 Barroso, President of the EU, was very clear in his message:

To be continued and concluded...

Conclusions

An underlying assumption in this paper was that rating agencies can be seen as markers or bearers of concerns of the financial markets vis-à-vis the political sphere. The starting point has been to analyse the so called tug-of-war as a kind of ping pong game including an open question regarding who was acting and who was reacting in this game, or in other words: who was in charge of the process? Was there a game on equal terms ('giving and taking') or had any of the players a more 'hegemonic position' in this inter-active game? In what ways did the tension between the political actors and the financial markets during the crisis referred to express itself?

Here follows some very preliminary results:

The euro crisis explored in this paper can in a fruitful way be understood and systematically illuminated through the lenses of Steeck's conceptual framework in terms of a "tug-of-war". It is of course difficult to prove causality, and this has not been my ambition. Even though it is now and then like a chicken-and-egg debate, it should not be an over-statement to say that the financial markets have been the driving actor during this process and consequently they have been in a more hegemonic position in what might be called an inter-active ping pong game. By taking the initiative they forced the opponent to react, thus always a step ahead.

The rating institutes, even though from time to time heavily criticised, have during this period carefully monitored the development, evaluating and scrutinizing all the measures adopted by political actors and at every moment ready to rate. The downgrades almost always forced the policy makers to agree on more far-reaching decisions to calm financial markets, decisions which in turn were closely examined and sooner or later rated again in a never ending process. In other words, the ball was always in the return as measures enacted were mostly judged as inadequate to the task. Very often the politicians got a very short respite as the financial markets were quite impatient and wanted quick results, not only promises.

Of course one should neither over-estimate, neither under-estimate, the role of the rating agencies – sometimes initiating the process, but mostly confirming what has already happened in the financial markets. Without any doubts they had power and influence during this period, even though one gets a feeling a few months into the new year (2012) that there was a tiredness of their messages in the media. The fluctuations with reference to the sovereign bond yields have probably been as important as the ratings when it comes to finding a financial weather thermometer of the issues at stake. Moreover, both factors were at the same time embedded in an overall process defending the core values of the financial markets vis-à-vis the political market.

No doubts the political as well as the economic sphere had imperfections, both of them reacting too late in the beginning of this crisis. With hindsight one could say that the agencies for a long time made a bad job, responding too late to facts that were since long obvious. On the other hand politicians came late on track, and early in the process they were obviously unaware of the magnitude of the crisis and thus unwilling to act and make decisions. Later on during the process policy makers often communicated conflicting statements on whether and how a sustainable solution should be provided. It is maybe a truism saying that these spheres had different logics – the politicians, with a quite different and longer time frame compared to the actors within the economic sphere, were forced into a balancing act to satisfy both the voters and the financial market needs.

The investors within the financial markets on the other hand had an easier task. Not surprisingly their time perspective was short as they were very eager to see results. It should be underlined that the financial markets probably did not have any political preferences vis a

vis the Euro project in a narrow sense. Rather, they followed the logic of the market and made calculations according to these principles. The consequence of this was that the more concerned the financial actors were lending money to the sovereigns, the higher risk premium the sovereigns had to pay. The latter were so to speak trapped in a vicious circle that in turn led to a self-fulfilling prophecy.

The so called tug-of-war took place through a very sophisticated system of signals that were very well known for the actors involved. It can be exemplified by the intensified political and economic turmoil autumn 2011, finally ending up with with new prime ministers on place in Greece, Italy, Spain, and Belgium respectively in November and December of that year. But the calm did not last long as there were still many issues to resolve. Many questions were left with no clear answers: Should the Greek parliament say yes to the hard conditions for the second bail-out? Should it prove possible with a debt swap or should Greece default? Should the finance ministers in the euro zone, as well as the IMF, finally agree to implement the rescue package and pay out the promised loan. What should happen to the fiscal pact already decided upon?

A well-known fact is that financial markets do not like situations with unknown outcome at all. Stability and predictability are important factors for them and consequently they jittered rather immediately late 2011 as well as early 2012 by downgradings, warnings, and negative outlooks, which in turn led to increased government bond yields and greater uncertainty. Only when all the pieces in the so called bond swap were in place in March 2012 the financial markets were happy and the game was over for now. Europe could take a breather for a while, even though many insightful experts said that this was just a break in the Greek and European drama.

However, the market's calm would prove deceptive. Not surprisingly the ping pong game was to be continued after some time, now with a special focus on Spain and its banks, the further development in Greece and the Greek election June 17 and its aftermath, as well as the economic situation in Cyprus. But that is another paper to be written...

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