**Will there be a viable deal?**

Ashoka Mody

April 1, 2015

To be viable, the deal must create a realistic prospect that in some reasonable timeframe Greece will manage its own affairs. By this criterion, a viable deal is most unlikely.

Berlin-Brussels-Frankfurt-Washington—BBFW—have a view on how economies emerge from financial distress: fiscal austerity to reduce public debt and structural reforms to induce growth.

But that will not work for Greece. Indeed, there is probably no historical instance where this strategy has worked.

On fiscal austerity, the evidence is now overwhelming. Persistent austerity hurts growth, which raises the public debt-to-GDP ratio, which leads to calls for more austerity, which further reduces growth.

Structural reforms enjoy wide support. But the evidence for this elixir is missing. Quantitative studies that claim to demonstrate the virtues of structural reforms almost always assume those virtues. The German authorities like to sell their Hartz reforms as evidence; but they are being disingenuous. Germany's growth has everything to do with its historically strong technological capacity and unique relationship between businesses and employees. These rather than lower wage growth keeps Germany competitive.

And if structural reforms are mainly code for lower wages, some gains may accrue in the long-run through improved competitiveness. But the immediate effect is to further reduce purchasing power and growth.

Bottom line: the BBFW framework cannot in short order redress the problems that have accumulated for decades. And holding a country under tutelage never works.

There is an alternative that keeps Greece within the eurozone. This requires stretching all out debt repayments—including to the IMF and the ECB—over a very long time. With that, BBFW must disengage from specifying the policies that Greece should follow. Let the Greeks manage their own affairs. They can do so only if their effective debt burden is so low that private markets are once again willing to take Greek risk.

So that Greece does not become a burden on European taxpayers, future Greek debt contracts with private creditors must carry provisions for standstills in repayments at pre-agreed triggers. Greek authorities will pay for such provisions, be forced to limit borrowing, and have no need for European help.

Over time, Greeks will determine their own destiny. Wages may eventually need to go below Polish levels for Greece to be competitive again. But the Greeks will have time to think about that.

The present course will only be an endless replay of the saga since February 11. The acrimonious exchange that has followed the premature declaration of triumph on February 20 is not accidental. It affirms the André Szász axiom. Szász, a former Dutch central banker, has explained: Europeans agree on the words but act on completely different interpretations of the agreement.

BBFW apparently hold the cards and are wedded to their position. Some of their ideas are sensible. But because their framework is fundamentally unsound, the Greeks will not be able to deliver. There is little common ground. The impasse will divide and hurt Europe.