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## Schäuble has killed off the Grexit fairytale

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### **Abstract**

After the 11-12 July Greek-End Schäuble has been harshly criticised for putting the possibility of a temporary Grexit on the negotiating table of the Eurogroup. In this piece I develop a counter-factual argument. I argue that intentionally or otherwise, with his strategy Schäuble has finally killed off the Grexit fairytale told so many times by Krugman, Stiglitz, Sinn, O'Rourke et al.



The years long Greek drama produced this summer the greatest twist in the plot. Although his manners were teutonically rude, the German Minister of Finance Wolfgang Schäuble's much criticised Grexit strategy has achieved something miraculous. Intentionally or not – only he knows – it killed the Grexit fairy tale told for so long by well-known US, UK and German academic economists.

From the start of the race back in January 2015, it was clear that the game of chicken between Syriza and Germany would always be won by the side able to convince their opponent that they were ready to jump into the abyss of Grexit. Alexis Tsipras, the Greek Prime Minister, was close with the referendum on 5 July. But Schäuble did not blink. On the contrary, he stamped on the accelerator, and once Tsipras had taken a good look into the black hole of Grexit, he pulled the hand-break and made a U-turn.

Tsipras' volte-face demonstrates that the economists (and some political economists) who call for Grexit might have their economics right (a devaluation could potentially benefit the country) but they have their politics and sociology awfully wrong. There is a reason why 70 per cent of Greeks want to stay in the euro. They know their country well. This is why they have accepted Tsipras' capitulation in Brussels and encouraged their Parliament to vote, for the first time with an overwhelming majority, in favour of the ongoing harsh third rescue package.

Until now many in Greece, both on the far left and the far right, dreamed of a better life with the Drachma. Schauble's Grexit plan, and Tsipras' reaction to it, have brought them back to reality. Living standards will fall in Greece over the coming years, but Grexit would be much worse. More than any other European leader, over the past eight months Tsipras has weighed up the pros and cons of an exit. His determination to stay is a strong message for anyone who will be at the same juncture in the future.

Although the Greek people are not the most Europeanised citizens of the Eurozone, even today, despite their hardship, most Greeks associate membership to the inner club of the EU with progress, modernity and high living standards. They look to their neighbours – Turkey, Bulgaria, Macedonia and Albania – and know they are better off. Leaving the euro would be a national humiliation much larger than the one experienced by Tsipras in Brussels.

Another element of the fairy tale is that a transition to the Drachma could be done smoothly. This is wishful thinking. Most Greeks oppose leaving the club. They will fight Grexit; even violently. Thus, if it happened, Greece would be mired in political instability: the worst possible environment to introduce a new currency. 'Euroisation', Montenegro-style, would be the most likely scenario.

As Tsipras has pointed out, the losers of Grexit would be the poorer and lower-middle classes. By contrast, the winners would be the conservative elites, who have stashed their savings abroad and are eagerly waiting for the introduction of the ever-devaluating New Drachma in order to use their hard euros to buy assets on the cheap. This would only increase the wealth gap between rich and poor in a country that is already highly unequal.

Schäuble's in-your-face-Grexit therapy and Tsipras' U-turn have achieved two outcomes hardly anyone envisioned at the beginning of the chicken game race. First, the German Bundestag has agreed another rescue package for Greece, making many Germans grudgingly accept that we are de facto in a transfer union. Second, most of the radical left in the South of Europe has now realised that leaving the euro is not an option. The structural constraints and potential risks are too huge.

People in the South want to stick to the core of the Eurozone, not because they want, or are forced, to become German, as is often stated by Anglo-American commentators, but because they aspire to have the same capitalist and democratic institutional frameworks (more meritocracy and less clientelism and corruption) found in central and northern Europe.

Now that the Grexit fairy tale has been killed off and the social-democratic and hard left, including the anti-establishment Spanish party Podemos, seem to have acknowledged the structural constraints of leaving the euro, perhaps they will focus their efforts on changing the structural conditions of the Eurozone. It is clear that Merkel cannot permanently decide the fate of the Union. She has no legitimacy to do so. The Eurozone needs to move towards a fiscal and political union to survive, but to get there Europe's social-democracy and France need to play a more active role.

In this regard, it is positive to see Hollande both stand firm against Grexit – if Paris says no it will not happen; forcing Berlin to eventually agree on a debt restructuring – and call for the creation of a European Finance Minister and a Eurozone Parliament. The only way to test whether Schäuble and the German public are true Europeans, as they constantly claim, is to match their bet and force them to show their cards.