Comments on

Ireland’s European Crisis: Staying Solvent in the Eurozone
By Colm McCarthy

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The crisis is not explained by profligate public sector. The government accounts were in balance before the crisis and the ratio of debt to GDP was twenty five percent. The crisis resulted from a banking crisis caused by property boom of staggering proportions.

The second reason for the Crisis is that the ECB and Germany/France forced the Irish government to guarantee bank bondholders despite their being no legal obligation to do so and in the teeth of IMF opposition.

His solution is a strengthened European Central Bank and “centralised bank supervision and resolution, centralised deposit insurance and an end to moral hazard and the implicit subsidisation of capital for banks”.
The Housing Boom
Dublin Vs Las Vegas

Figure One Housing Prices in Dublin and Las Vegas 1996-2010

“the costliest mistake ever made by an Irish person”

- The Irish government agreed to bail out bank holders under extraordinary pressure from the ECB and European “It is unprecedented for bondholders in defunct banks to be paid by a country already in an IMF programme”

We are missing parts of the story.

- In terms of percentage of GDP how much did this add to the Irish Debt? Did it add Thirty Billion Euros? Forty?

- Why did the Irish government agree to this. They were under pressure by the ECB and Germany/France. Is this all? Was it a miscalculation? Was it partly due to the commitment of Irish policy makers to the European project behind their willingness to “take a bullet for the team”?
The Solution?

- For Colm, the costs of Leaving the Euro are too high.

- He says solution is not more centralized fiscal supervision.

- His solution for new entrants is a strengthened European Central Bank and "centralised bank supervision and resolution, centralised deposit insurance and an end to moral hazard and the implicit subsidisation of capital for banks".

The Irish experience where Ireland was used as an example to “encourage the others” makes one sceptical about how the new ECB will work in practice. Will it be free of political interference?

It won’t help Ireland much. Ireland is heading towards debt to GDP ratios of 110-120 percent. Debt to income around 1.30 to 1.50.
The Irish Problem

- It appears that Europe is heading towards centralized fiscal supervision. The fact that the German Bundestag got to see the Irish budget before the Irish parliament (the Dáil) shows where we are heading.

- The high debt ratios and European supervision will mean higher direct and indirect taxes on labour. Ultimately, it may also mean the end of the favourable tax treatment for direct foreign investment.

- Higher taxes can spell the end to some unique features of the Irish convergence boom based on foreign direct investment and hours worked closer to the US than Europe.
The Irish Boom after 2000 is partly due to working hours diverging from Europe.
The Irish Minimum Wage (€7.65 = $10 per hour) is very high.

The worst case is probably the most likely case

- Rises in taxes reduce hours per worker towards the European norm.
- Social Benefits and the minimum wage stay at their current levels.
- Ireland is stuck at income levels (not GDP) well below the European average.

To avoid these outcomes will require luck but also good policies. It may also require Irish policy makers to reorient their attitudes towards Europe. Europe and in particular the ECB bailout is part of the problem. The strong commitment by the Irish policy makers to the European Project does not mean that they should put European interests before those of Ireland.
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