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## To Really Save the Euro, Europe Needs to Take an Ax to Its Tangle of Red Tape

- By IRWIN STELZER



Phase One of the save-the-euro campaign is completed. After a lot of huffing and puffing, the euro-zone countries, the International Monetary Fund and the European Central Bank have cobbled together a bailout that might see Greece and other members of Club Med through this year and part of next. You might term this a success—if you don't count the facts that it might threaten German Chancellor Angela Merkel's political career, that the ECB has lost its reputation for political independence and that the bailout has reduced the penalty for improvident bank lending.

Phase Two is under way. Its creators have always yearned for central control of the fiscal policies of euro-zone members, and are on a path to getting it. No longer will Brussels and the richer North turn a blind eye to the spending and shenanigans of the poorer South. Instead, they will impose fines, a loss of voting rights, or some other form of Germanic sanction on the persistently profligate.

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Robert Zoellick says the EU should pursue 'tax policies that encourage work.'

The markets remain skeptical. The promised austerity measures are not certain to succeed. After all, Greece has just fired as many as 234 finance ministry officials for their failure to pay taxes since at least 2007. Some 60 lesser civil servants can't be axed, and will be reassigned to other jobs. I mention this not to amuse but to point out that government promises of austerity have to be weighed alongside the history of the officials charged with honoring them.

Still, there is progress. Spain, in the gun sights of the bond vigilantes, could not avoid being shorn of Fitch's triple-A rating, although parliament approved the government's austerity program—by one vote. The Zapatero government has finally begun to force consolidation of the banking system, forcing troubled regional cajas to merge. It is doubtful that combining two or more failing banks without cleaning up their balance sheets will accomplish very much, but let's not quibble: at least the problem of banks that have loaned too much to property developers is being attacked.

Both Spain and Portugal are cutting and freezing the salaries of civil servants, and following Ireland in reining in the most generous portions of their welfare states. Italy, its new austerity program put in place last week, has a bit of room for maneuver because its debt-to-GDP ratio is far lower than Greece's.

But none of this will matter unless there is a Phase Three. Even if some taxes are raised, and some outlays cut, Europe cannot grow at a rate sufficient to restore its finances (even France has an unsustainable deficit of 7% of GDP) without basic policy changes. The Organization for Economic Cooperation and Development predicts the euro zone will be the world's growth laggard, growing at 1.2% this year and 1.8% in 2011, while the U.S. racks up growth of 3.2% in both years, and Japan records 3% and 2% growth rates in 2010 and 2011, respectively. And those projections might be overly optimistic: retail sales in the euro zone have declined for five consecutive months.

Which brings us to Robert Zoellick, CEO of the World Bank. Mr. Zoellick knows a thing or two about what drives economic growth, and although I don't always agree with the policies of international

funding institutions—be wary of policy makers bearing gifts of other people's money—I do think Mr. Zoellick has got it right.

In an exchange of correspondence, which he has given me permission to reference, the World Bank boss points out that the way out of Europe's problems involves a lot more than austerity, or Keynesian pump-priming.

"To enable Europe to grow at a rate that will contribute deficit-reducing remedies to its Treasuries and create jobs," says Mr. Zoellick, "the EU should look at cutting red tape that holds back new businesses, at increasing competition, and pursuing tax policies that encourage work and private investment." It is the adoption of these policies in several developing countries that Mr. Zoellick argues is helping them to grow at more than twice the rate of Western economies.

My own view is that only an exquisite combination of well-timed policies can avoid a financial panic. First: a dose of austerity now to signal that the bond market's message has been received. Second: a credible plan for future reductions in the scale of state spending. Third: a bout of quantitative easing by the ECB, which means continuing to buy Greek and other sovereign debt, and, to use a term clearer than "quantitative easing", printing money. Fourth: serious growth-oriented structural reforms that favor job-creating small businesses, reduce the burden of state pensions, encourage hiring by making firing easier, and stabilize the financial system. Remember: Spain's debt was downgraded because austerity measures "materially" reduce its growth prospects.

That only partial list of what needs to be done indicates the massive exercise of wisdom and will required of policy makers. Past experience does not suggest that either virtue is in over-supply in the eurocracy.

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