Merkel, Sarkozy want to give the banks more capital

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French President Nicolas Sarkozy and German Chancellor Angela Merkel met in Berlin on Sunday against a background of sombre warnings of new bank failures, an impending bankruptcy of Greece and an imminent collapse of the euro.

After the meeting they both declared their willingness to aid banks in the euro area with fresh infusions of public funds. They also promised to present a convincing and comprehensive package to resolve the crisis by the end of the month.

Merkel declared that Germany and France were aware of their shared responsibility for the euro zone, the European Union (EU) and the world economy. They would work together and do whatever necessary to ensure a recapitalization of the banks in Europe.

Sarkozy expressed his “complete agreement” with Merkel: “Sustainable, global and fast solutions” for the euro crisis must be found for the G20 summit on November 3-4 in Cannes. Germany and France wanted to propose “significant changes” to EU treaties, to allow for “binding co-operation on financial and economic policies for the euro member states.”

Merkel and Sarkozy, however, refused to give any specific details. Their ostentatious display of unity was principally directed at calming panicky stock exchanges and financial markets.

On Monday, EU Council President Herman Van Rompuy announced that the EU summit scheduled for October 17-18 would be postponed for one week. Suspicions emerged that fundamental differences between Merkel and Sarkozy were behind the decision to shift this complex event involving 27 heads of government. Merkel and Sarkozy both denied this was the case.

The agreement between Merkel and Sarkozy to recapitalize European banks came following massive international pressure.

In the columns of the *Financial Times*, the prime minister of Britain, which does not belong to the euro zone, called on Germany and France to resolve their differences and tackle the euro crisis with the use of a “bazooka.”

“Time is short, the situation is precarious,” David Cameron warned, writing that the very existence of the monetary union was threatened.

Cameron demanded an action plan to recapitalize the banks, a massive expansion of the Euro-bailout European Financial Stability Facility (EFSF), a clear future strategy for highly indebted Greece and more involvement by the International Monetary Fund.

Earlier, US President Barack Obama had urged the EU to take more far-reaching measures to tackle the debt crisis. “They’ve got to act fast,” he told a press conference, demanding a “very clear, concrete plan of action that is sufficient to the task.”

Over the weekend, the Belgian-French bank Dexia collapsed—the latest victim of the crisis. After a joint meeting on Monday night, the governments of Belgium, France and Luxembourg announced the break-up of the ailing bank. The Belgian government is to take over the Belgian part of the bank for €4 billion. Dexia’s risky securities are to be swapped into a “bad bank,” with the three states providing guarantees totalling €90 billion.

Dexia was rescued in 2008 with €150 billion in public funds. At that time, the bank had invested heavily in US real estate. Now, the collapse of European government bonds, in particular Italian and Greek bonds, under the impact of the European sovereign debt crisis has once again created problems for the bank.

The increase in equity for European banks, agreed in principle by Merkel and Sarkozy, sets the stage for the

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bankruptcy of Greece. European banks are to be provided with sufficient capital to cope with large losses on the value of Greek bonds.

There are, however, profound disagreements over how to finance the recapitalization of the banks. French banks are especially heavily exposed in Greece, and Sarkozy wants to use the EFSF to bail them out. The German government, which contributes the largest share to the EFSF, rejects such a course and wants to encourage banks to obtain the necessary capital before national governments intervene—with the EFSF coming into play only in an extreme emergency.

The German and French administrations also have conflicting views regarding future dealings with Greece. According to media reports, the German Finance Ministry is working on plans to provide for a debt haircut of up to 60 percent, which would technically amount to a bankruptcy. The Greek government would be insolvent and would have to dramatically slash its public expenditure. Creditors would be required to write off a large portion of their bonds, an event that would hit French banks particularly hard. Paris, therefore, wants to postpone a bankruptcy as long as possible and gain time.

Both governments also know that a policy involving donating further billions of public money to the banks is highly unpopular, at a time when public spending is being massively cut and Greece will be driven into bankruptcy. Media and politicians fear that hostility to the banks will continue to grow and develop into a broad, uncontrollable social movement.

German Social Democratic Party (SPD) chairman Sigmar Gabriel warned the Merkel government not to give the banks any more money without imposing stricter rules or temporarily nationalizing them. “We cannot save the banks for the second time without pruning them back,” he told the *FAZ* newspaper. “The motto must be: ‘not a cent from the state to bail out the banks without fundamental changes’.”

Die Zeit said it was a mistake to focus on recapitalizing the banks in order to rescue the euro: “The message this sends is that when we have secured the banks we can let the states go.”

A commentary in the *Sueddeutsche Zeitung* even called for “civil protest in the streets” against the power of the financial industry. “Whoever wants to protest against this naked redistribution in favour of finance capital will find no place inside the German parties, the paper wrote. “The major parties seem like playthings of the markets.”

This newspaper, which is notoriously conservative in economic issues, is obviously not about to launch a movement against capitalism. Rather, it is seeking to establish a pressure valve before popular anger gets out of control and really threatens capitalism. “It’s time for people to take to the streets in Germany and force the parties to rethink,” the newspaper stated, declaring at the end of its comment: “Not to abolish capitalism but to reform it.”

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