Greek euro exit no longer unthinkable

By David McHugh
The Associated Press

FRANKFURT, Germany — Let Greece go: It's a possibility that's being considered more and more publicly in Europe.

There have been 2½ years of bailouts, on top of broken promises by Greece to reform. The result: a fifth year of recession and, this week, political chaos. Voters on Sunday favored parties that either oppose the terms of the international bailout or want to renegotiate them. If it can't get more rescue loans, Greece will go bankrupt and likely have to leave the eurozone, the currency union of 17 countries.

The question confronting leaders in Athens, Berlin and other eurozone capitals could soon be: What would happen if Greece left the euro? How much damage would that do to it and other countries in the eurozone? Has Europe insulated itself to a degree that it can cut Greece loose, while keeping its currency alive and its economy upright? Among the possible scenarios are:

» GREEK CHAOS: Economists agree that Greece, where unemployment is 21.7 percent, would suffer even more turmoil and misery if it left the euro. A new drachma currency would fall by 50 percent or more against the euro. So Greeks would try to pull their euros out of their bank accounts — before they could be converted into a new currency worth far less. Owners of Greek stocks would sell for the same reason. As markets plunged and deposits fled, banks would collapse.

To try to limit the financial drain, Athens would probably have to close the banks while the new currency is introduced. It may also try to keep people from moving euros out of the country.

Every Greek company that owes money in euros — to a foreign supplier, say — would see those debts grow much heavier compared with the weaker new drachma. Many would go bankrupt. Greeks with the weaker drachma would have to pay more to travel abroad or buy foreign goods.

The Greek government would still owe $428 billion, mainly to the other eurozone countries that rescued it, the International Monetary Fund and the European Central Bank. Because those debts would remain in euros, it would have little chance of repaying them. Greece would have to try to get its creditors to accept less than full repayments on its loans.

» A BOUNCE-BACK: On the plus side, the weaker drachma would make Greek exports cheaper and more competitive and could help the economy start growing again. Firms outside Greece may be attracted by cheaper labor and real estate, encouraging them to move manufacturing plants there.

Tourism would also get a boost: booking a hotel room on a Greek island, for example, would suddenly become much cheaper for foreigners. As long as Greece uses the euro, it can't benefit from an inexpensive currency. The euro's value reflects the strength of healthier eurozone economies like Germany. Still, Greece isn't a big exporter, so the benefits of a new, weak drachma may not be as great as hoped.

» CONTAGION: The great fear, some economists say, is that if Greece leaves the euro, other troubled eurozone countries might do the same.

"The big danger is financial contagion," said Dennis Snower, president of the Kiel Institute for the World Economy. "The question would be, what stops the Portuguese from doing something similar?"

People might think "just in case, let me get my money out of the bank," he said. "And if enough people think that way, then you're sunk."

Investors who worried that these other countries might also leave the euro bloc would demand higher interest rates to lend to them. If governments couldn't borrow at reasonable rates, they would default on bond payments, hurting the banks that hold such bonds.

The ECB could try to thwart that by issuing unlimited inexpensive loans to banks.

It has done that already, handing out more than $245 trillion in December and February. That calmed the crisis for a few weeks.

The prosperous core of the eurozone — Germany, France, the Netherlands, Finland and Austria — would likely not escape. Their banks own much of the government debt of Spain and Italy.

» POLITICAL EMBARRASSMENT: Ultimately, a Greek exit from the eurozone would be a terrible blow to the prestige of the broader 27-country European Union. The shared currency is a pillar of hopes for a more united continent. Its abandonment would also mean the rescue strategy pursued by leaders such as German Chancellor Angela Merkel of forcing Greece to cut its budgets relentlessly has been a failure.