

Eurozone's quack solutions will be no cure



Wolfgang Münchau

I was uncharacteristically optimistic last week, and had planned to end my informal series on eurozone crisis resolution with a benign scenario. The eurozone would survive in one piece; there would be no blood on the streets, just a once-and-for-all, albeit reluctant, bail-out, accompanied by a limited fiscal union. But as several readers have pointed out, my scenario is prone to a very large accident. I accept that point. Last week, we caught a glimpse of how such an accident may come about. My benign scenario looks a lot less certain today than it did a week ago.

The week began with the strong showing of two parties in the Finnish election, which are advocating a partial Portuguese debt default as a condition for a rescue package. The results triggered a renewed outbreak of the financial crisis, as eurozone spreads rose to near record levels once again.

The most disturbing news, however,

was a revolt within Angela Merkel's increasingly fragile coalition. It looks as though the German chancellor is on the verge of losing her majority over the domestic legislation of the European Stability Mechanism (ESM), the long-term financial umbrella for the eurozone. She may have to rely on the opposition to ratify the ESM, which may come at a heavy political cost. The Bundestag already postponed the vote on the ESM until the autumn, hoping to keep it clear from the controversial decision to pass the Portuguese rescue programme in May.

As opposition to the ESM mounted, German officials fell over themselves to be quoted by various newspapers pronouncing that a Greek restructuring was inevitable. Even Wolfgang Schäuble, finance minister, talked about the possibility of default. Some wily speculators unleashed the rumour that Greece would spring a surprise debt restructuring. The rumours prompted a criminal investigation. Another week in the eurozone's debt crisis!

A monetary union is at a natural disadvantage when it comes to the handling of crises. There is no central government that takes decisions, which makes communications hard to control. What is less forgivable is the serial

incompetence of the eurozone's decision-makers, as exemplified by the perpetual eagerness to declare the crisis over the very second financial market pressure subsides. Not only do they know little about financial markets, they have surrounded themselves with policy advisers who know little too.

Their ignorance is an ideal breeding ground for quack solutions. One such is immediate default.

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German Christian Democrats and Finnish isolationists spent the last week trying to convince themselves that a Greek debt-restructuring would save them a lot of money.

That belief is premised on two false assumptions. The first is that a voluntary restructuring could solve the Greek debt problem. It can work in limited cases, but not when countries are insolvent. Greece, however, faces no short-term liquidity squeeze, because it is supported

by the European Union and the International Monetary Fund. There is no need for any restructuring, voluntary or involuntary, right now. But Greece may need to impose a "haircut" in the future to ensure debt-sustainability. The ideal moment would be when the country achieves a primary surplus, probably in 2013.

The second wrong assumption is that the Greek banking sector would survive a restructuring unscathed. This is a conditional error. If you believe that a voluntary restructuring would be sufficient, then the Greek banking sector would indeed survive. But it would surely not survive a large and involuntary haircut. The European Central Bank would face a haircut on its direct investments of Greek government bonds, and, more importantly, much of the collateral posted by Greek banks would vanish. On my calculation, the cost of a Greek default to the German taxpayer alone would be at least €40bn (\$58bn), including recapitalisation of the ECB. A bail-out would be cheaper.

A premature Greek default would change everything. As would the failure by the EU and Portugal to agree a rescue package in time; or an escalation in the EU's dispute with Ireland over corporate taxes; or

a ratification failure of the ESM in the German, Finnish or Dutch parliaments; or a German veto for a top-up loan for Greece in 2012; or the refusal by the Greek parliament to accept the new austerity measures; or a realisation that the Spanish *cajas* are in much worse shape than recognised, and that Spain cannot raise sufficient capital.

Then there is the downgrade threat for French sovereign bonds. I recall asking a French official about this, and getting the smug answer that the rating agencies could hardly downgrade France if they maintained a triple A rating for the US. That was before last week. By extension, France must also now be in danger. A downgrade would destroy the logic of the European financial stability facility. It is built on guarantees by the triple-A countries. Without France, the lending ceiling of the EFSF would melt down further.

The list of potential accidents is long, but they share a joint theme – serial political crisis mismanagement. We saw another glimpse of that last week. If we go down the route of premature default, and allow the True Finns and the true Germans to run the show, the eurozone as we know it will be finished.

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To win the cyberwar we have to reinforce the cloud

Mike McConnell

Many challenged my grim assessment early last year, when I called for America to develop a new strategy to address the kinds of cyberattacks that could cripple our nation's infrastructure. If there were a cyberwar, I told Congress, we would lose. The unfortunate truth is that, a year later, we are no better prepared – and the stakes have risen.

Since then more details have emerged on the early 2010 attacks on Google and two dozen other companies, connecting them to China. Alongside the revelations about the Stuxnet attack on Iran and the WikiLeaks saga, the question today is no longer whether the cyberthreat is real – that was last year's discussion. The challenge now is what to do about it, while balancing security, privacy, openness and innovation.

We should immediately focus on protecting critical infrastructure – the power grid, financial networks, air traffic control and other transport infrastructure – by realigning their use of the internet. To do this we must create new "protected lanes" inside the global superhighway. I call this potential area "dot.secure": a series of highly protected lanes for those operating vital infrastructure, within the free and open world of the .com global network.

The WikiLeaks saga has generated intense debate about whether the release of classified government information is in the public interest. To be clear, I am not an advocate of doing away with the freedom of our citizens and their use of the internet. But I would also argue that we are a nation of laws, and everyone is entitled to privacy – individuals, businesses and, yes, government.

We must create new protected lanes inside the global superhighway for those operating vital infrastructure

To do its business effectively the government must be able to exchange information with other governments in private. Businesses must be able to protect innovation and patented information; individuals must be able to keep the ownership of their new ideas.

There also need to be defined areas of the internet where that can take place – where individuals can post to blogs, create videos, comment on the news and be completely anonymous – and other places where access to specific data is restricted. Equally, we must develop access systems for sensitive business where an individual is limited to data essential to his or her task.

Highly secure and open areas of the internet do exist today. The defence department runs "mil," a domain with limited gateways, military grade encryption, perimeter security and support from the National Security community to identify foreign threats. The government's "gov" domain has a similar goal of limited gateways, but will also benefit from high-grade encryption.

On the other side of the information highway, the .com lanes are open with easy movement and access, requiring only the level of security that an individual or business requires for themselves. These open lanes are less costly to maintain, and will benefit even more from the economies of cloud-computing, a powerful, cost-efficient shared computing environment.

What's missing is the middle ground: dot.secure. The nation's finance, electric, power, water, land transport, air traffic control, industrial control systems must be protected within the security of the restricted lanes. Each month, we understand more about how to heighten security in the "cloud", and our technicians develop more nuanced approaches to security architecture. Beyond that, cloud operators can focus on network intrusion prevention and response to protect information and its users.

We need to apply the evolving knowledge of cloud-security to our infrastructure through a new government/private partnership. The administration and Congress know the seriousness of cyberthreats, but they are not moving fast enough to address them.

We must remember that cyberspace is more than just the internet. It is a domain itself. For America to protect our economy and way of life as we have in the other domains, we cannot wait for the next big attack to shock us into action.

The writer was director of the National Security Agency in the Clinton administration and director of national intelligence in George W. Bush's second term. He is executive vice-president of Booz Allen Hamilton

Missing in action: Republican champ



Clive Crook

At this rate, the US presidential election of 2012 promises to be a titanic struggle between a failed incumbent and an unelectable challenger. With the election bearing down – less than two years to go – Mr Obama hit the campaign trail last week, ostensibly talking about the budget but in reality market-testing his anti-Republican message. Republicans have been slower off the mark and will need to get a move on, but the delay is understandable. They have so many weak candidates to choose from.

Conventional wisdom holds that incumbent presidents are hard to beat. Certainly, they have advantages. While out rousing the base and grubbing for votes, it helps to have Air Force One and a rollaway presidential podium at your disposal. But incumbents do in fact lose. Jimmy Carter lost. The first George Bush lost. Mr Obama's approval rating is not yet disastrously low, but his policies are less popular than he is. If the economy is still struggling next year, he is at risk.

And it might be. Unemployment is high and falling only slowly. The housing market is still on its knees, leaving many mortgage borrowers with negative net worth. Consumer confidence has dropped lately, not risen. The fiscal stimulus is fading – and if Republicans continue to outmanoeuvre the administration on budget policy, it may fade more abruptly than the economy can withstand. The Federal Reserve is starting to divide on whether monetary policy needs tightening.

Additional monetary stimulus now looks unlikely unless the recovery goes into reverse. Mere sluggish growth – less than Mr Obama may require – will not move the Fed to act. A strong Republican's chances in 2012 might therefore be fair to good. All the party needs is a strong Republican.

Last week, a poll for the New York Times and CBS asked Republicans to say whether they were enthusiastic about any of their likely presidential candidates and, if so, which. Perhaps suspecting a trick question, 56 per



cent declined to name anyone.

Sarah Palin, arousing the enthusiasm of just 4 per cent, seems out of favour. Mike Huckabee, formerly governor of Arkansas, now an amiable cable-TV host, topped the poll with just 9 per cent. Mitt Romney, former governor of Massachusetts, presidential contender in 2008 and ex officio frontrunner for the 2012 nomination, came second with 8 per cent. Almost tying that score was Donald Trump – attention addict, avowed billionaire, reality-TV blusterer and valiant denier of male-pattern baldness ("I refute it thus").

Mr Huckabee may choose not to run. Let us suppose – let us hope – that Mr Trump is only joking. How strong a candidate would Mr Romney be? One does not wish to seem overly negative, but it has to be a drawback that as governor of Massachusetts he pioneered a close variant of Mr Obama's healthcare reform, a policy that every self-respecting Republican voter loathes like no other. Mr Obama delights in

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needing him, thanking him for leading the way on the Democrats' signature achievement.

Mr Romney's answer is that he favours letting each state decide for itself how to do healthcare reform. Substantively, there is actually something to be said for that, but it does not help him much politically. He cannot attack Obamacare as savagely as the party requires when he gave his own state much the same system. The fact that his record as a Rino (Republican In Name Only) governor did not prove instantly fatal to his candidacy proves the weakness of the field.

To talk of weakness, by the way, is not to say that the Republicans lack candidates who might be good

presidents. Mr Romney might be a good president. The issue is electability. The party must choose a nominee and the country must then vote that person into office. The Republicans' problem is that the party's energised electorate has drifted so far from the middle that one kind of electability may rule out the other.

Tim Pawlenty, the successful two-term governor of Minnesota, is much touted. He is an impressive man and by ordinary standards a staunch conservative – but not staunch enough for the Tea Party. He had to retract his earlier support for a carbon cap-and-trade law. He is emphasising his religion (Catholic-turned-evangelical) and playing up the social conservatism. The party faithful are unconvinced, sensing Romney-like fluidity. On the enthusiasm question, he was named by 1 per cent.

Mitch Daniels, governor of Indiana, might also be a fine president. But he too is impaired in the eyes of

many Republican activists. He called for a "truce" on issues such as abortion – a deeply suspect position. He has been a successful and popular governor. As a former federal budget director and fiscal-policy nerd, he is a man for these times. As a social liberal (comparatively speaking) and fiscal conservative, he has been given an easy ride by the press. But none of this will get him the nomination. How many Republicans declared their enthusiasm for Mr Daniels in that recent poll? Again, a resounding 1 per cent.

In last November's elections, the Republican rank and file threw control of the Senate away by ejecting strong candidates and nominating duds they knew might lose. They did it with pride: they had a point to make. Will they adopt the same approach in 2012 and proudly hand victory to a beatable Mr Obama? They are thinking about it.

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Fund Egypt's future to save the Arab uprising

Ahmed Zewail

As I was leaving Cairo after Hosni Mubarak stepped down, I asked Esraa, a young woman who was one of the leaders of the revolution: "What was your objective?" She said, "taghier al nezam", a change of the system. The Egyptians brought down the head of the system, but not the system itself. That is the challenge now.

Egypt's revolution, like Tunisia's, represents a model for change in the Middle East. These societies are not fragmented by tribal or sectarian conflicts. Despite differences of faith or even the occasional collisions between them, Egypt is united. In contrast, the second model for revolutions is that of Yemen, Libya and others in the making. In these cases, unfortunately, tribal and sectarian conflicts may lead to chaos and civil war, ultimately dragging the Middle East backward into conflict and fanaticism, not forward.

To avert this, the revolutions in Egypt and Tunisia cannot be allowed

to fail. Egypt is the key. With 85m people, it is the largest country in the region and the heart of the Arab world. Making sure it succeeds is essential for the spread of democracy and stability of the world's energy supply as well as for peace in the region. What can be done?

From my experience pushing for reform over two decades and as a negotiator with the youth and government leaders during the revolution, I know what in the long term is needed most – a decent education system. The so-called "children of Facebook" who fomented the revolution know Egypt was once ahead of South Korea in scientific research and development. They know that in the 30 years Mr Mubarak sat in his palace and Egypt deteriorated, China has lifted hundreds of millions out of poverty, sent astronauts into space, built megacities and high-speed trains, and brought its students up to world standards. They ask why Egypt cannot do the same thing.

This will, of course, take time but it is imperative to begin now. Of Egypt's many problems the

three most urgent to address are governance, economy and education. The army's Supreme Council, now the ruling political entity, has to ensure swift political changes. Egypt badly needs national unity and reconciliation. But to take the critical long-term steps to transform society it needs financial support.

Like Tunisia, Egypt is in flux as a range of groups contend over the future. An education fund would point it the right way

While Egyptians themselves must fashion the new nation, they need help in rebuilding sustainable institutions. The place to start is with the pivotal project, "renaissance in education and development", whose acronym is the first command of the Koran – read.

For years the west supported Mubarak and gave aid for what it hoped was stability – but was

actually stagnation – in the Middle East. What Egypt needs now is a global partnership of private and government organisations to establish a fund to finance a revolution in education. This should be directed by a board of trustees from renowned Egyptians and world leaders in co-operation with the Egyptian government.

Such an effort would need an initial \$1bn from private and government sources. Further funds then could come from other nations and be deployed by the World Bank, the Arab Bank and the Islamic Development Fund. Repudiation of debt will redirect national resources to this and other vital projects. Egypt does not possess rich natural resources. Its agricultural area is relatively small – less than 10 per cent of the total land. Its growth relies on tourism, Suez Canal tariffs and foreign investment. Yet Egypt is rich with human capital. According to the United Nations, Egypt's population will grow to 114m before it stabilises in the year 2065.

The psychological influence of launching such a fund at this

moment cannot be underestimated. Like Tunisia, Egypt today is in flux, as a range of interest groups contend over the direction of the future. By showing that effective, and youth-based, institutions can be built, this project would point Egypt in the right direction.

In Egypt, every family is suffering from the deteriorated schooling and university system of the Mubarak regime. What families want most of all is to secure a good education for their children.

It is in the best interests of everyone – the Chinese, the Americans, the Europeans and the other Arab states – who wants long-term stability in the Middle East that the peaceful democratic revolutions in Egypt and elsewhere succeed. Time is of the essence!

The writer was awarded the Nobel Prize for chemistry in 1999. Currently he is a professor at the California Institute of Technology, serves on President Barack Obama's Council of Advisors on Science and Technology, and is involved in Egypt's transition to democracy