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# Europe Tries to Stave Off a Reckoning

By STEVEN ERLANGER

BRUSSELS — Many around the world are worried that Europe is about to face a [Lehman Brothers](#) moment, a big bankruptcy or sudden default that sets off a new phase of panic in Europe and beyond.

But these days the problem for Europe may be that it has not had — and may not have — its own Lehman Brothers, at least in the sense that Lehman shocked Americans to take divisive and expensive steps to repair the damage. Instead, it has seen a slow-motion leak of confidence and a steady drain on credibility that has extracted a large and growing toll on stock and bond prices and on the livelihoods of its citizens.

Nearly two years after the euro crisis began with concerns about the solvency of [Greece](#), fears have spread to big banks and large countries like Spain and Italy and squashed the gradual recovery from the 2008 [recession](#). But Europe still has not had the all-hands emergency response the Bush administration and the United States Federal Reserve were forced to undertake after the collapse of Lehman on Sept. 15, 2008, and it is unclear if even the intensified market turmoil now is enough to prompt one.

An uncontrolled Greek default or a run on a major European bank could still overturn expectations and compel [France](#), [Germany](#) and the [European Central Bank](#) to act with much greater urgency. But

for now, political and financial leaders are buying time, putting out fires one by one, like propping up Dexia Bank, and making vague promises, as European officials did Wednesday, about scheduling new meetings to discuss the recapitalization of European banks.

“Economists are trained to think about eventual outcomes and work backwards, and that’s the way financial markets function, too,” said Charles Wyplosz, an economist at the Graduate Institute in Geneva. “That’s 180 degrees from how politicians function. They ask themselves about tomorrow or next week or maybe the next election and solve problems as they come. So they’re always behind the markets.”

Despite the fact that economists and bank analysts now widely expect that Greece will have to default on its debt, no European leader will say so, at least for the record. Instead, the countries in the euro zone are continuing to act as if measures agreed to in July to shore up Greek finances, and that slow-moving European parliaments have yet to fully approve, are sufficient to contain the crisis. One sign that Europe is preparing to address the problem might be a sudden outbreak of candor about the real condition of Greece, or an acknowledgement that leading European banks that hold sovereign debt of Greece and other troubled countries in the region will need hundreds of billions in new capital to ensure their stability.

But European leaders, especially in France and Germany, whose own banks are exposed, are reluctant to broach the inevitable. Why? Because they do not yet have in place a big pool of funds to ensure that an orderly Greek default does not lead markets to assume that the much larger economies of Spain and Italy will soon follow it into insolvency. And partly because they do not have the political will to commit those funds.

Without a trillion-plus-dollar “bazooka” in place to shock and awe increasingly skeptical markets and recapitalize banks, Europeans see themselves as having no choice but to temporize, even if that pushes up the cost of an eventual Greek default. And it renders any bad news — even bad news that has been anticipated and published in advance, like Greece’s again missing its deficit reduction targets this week

— enough to send markets into a fresh nose dive.

The incremental approach of European leaders has frustrated their counterparts in the Obama administration and the Federal Reserve, who have repeatedly urged them to commit to a much bolder rescue plan. It has also done little to calm investors, who have already priced in a Greek default and are looking hungrily at Italy. “The markets need clarity,” Mr. Wyplosz said. “They have no reason to believe there’s a floor on public debt, so they fret. Once they have a floor, they can calculate their losses. Markets accept losses and can deal with them, but need a backstop.”

Ultimately, only the European Central Bank can intervene with the firepower necessary to set a floor under the price of the region’s sovereign debt. But its departing chairman, Jean-Claude Trichet, has ruled out the idea of the bank’s acting as the lender of last resort, even if it only guarantees the bond purchases of another fund, the European Financial Stability Facility.

Germany, the Dutch and the Finns, too, are against allowing the bank to make unlimited bond purchases from sovereign states.

The reluctance blocks even obvious moves, like marking down the value of Greek debt to something approaching the market price, which is now only 40 percent of its face value.

There has not yet been a sufficient sense of crisis — no Lehman Brothers moment — that overcomes longstanding European qualms about handing a full range of Fed-style powers to the region’s central bank.

And residents of richer countries in Europe are not yet unnerved enough to agree to write big checks to Europeans elsewhere whom they accuse of spending themselves into a [debt crisis](#).

“Greece is small and its problems can easily be contained,” said Sony Kapoor, managing director of Re-Define, an economic consultancy. “But the inability of officials to deal with this successfully over a year and a half inspires little confidence in their ability to deal with much larger troubled countries such as Italy.”

“The E.C.B. can still stem the panic though a strong intervention,” he continued. “But unless this is done soon, the crisis may spin further out of control.” For now, European leaders are sticking to their talking points.

Many leading economists and bankers now say that major banks in Europe need hefty infusions of capital to weather the inevitable downgrading of the value of European sovereign debt they have on their books. But the banks themselves and their government regulators continue to preach the fiction that the debt is worth more, and in some cases considerably more, than its market value. That only persuades the markets to disregard official statements and continue selling.

The Lehman crisis began when American regulators badly miscalculated, effectively allowing the big investment bank to go bankrupt. But as harmful and unpredictable as that event was at the time, it compelled the Fed to experiment with new forms of intervention in the financial markets and forced a reluctant Democrat-controlled House to approve a huge bailout to shore up the banking system.

Europe’s collective decision making is even more fractious. The countries that use the euro are a collection of sovereign states that all must agree on any painful steps, which may even be harder than getting Congress to do the same. Several European parliaments have yet to approve their shares of a 440 billion euro bailout fund that is now all but officially acknowledged to be too small to grapple with the full scale of the problem.

Moreover, there is already fierce opposition in Germany and at the central banks to American notions of how that fund could increase its financial firepower without formally applying to parliaments for more money.

Lehman Brothers provided the United States, for good or ill, a moment of reckoning. Europe is still trying desperately to avoid one.



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