CEPS COMMENTARY
Thinking ahead for Europe

China's assistance could do more harm than good in the eurozone

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3 November 2011

Does Europe need 'assistance' from China? Not at all, if it gets its own act together. Unlike the US, the eurozone does not have an external deficit that needs to be financed. Its current account is balanced, so there are enough savings within the monetary union to finance all public deficits. The problem is one of distribution. There is an excess of savings north of the Alps, but northern European savers do not want to finance the southern countries such as Italy, Spain and Greece.

Why should China buy Italian or other peripheral debt if German savers and banks do not want to do it? The answer might be that China will be asking for an implicit guarantee from Germany for any 'euro' bond it buys. But this does not make sense for Germany. Why should it pay a political price for something – guaranteeing the debt of other countries – that it has consistently refused to consider even for its own banks?

A large inflow of funds from China and other 'investors' could in fact do more harm than good. The incoming capital would strengthen the euro and thus make a recovery in the periphery even more difficult. Germany's exports are much less price sensitive than those of countries on the periphery. Germany can thus get by with a stronger euro, but countries such as Italy and Greece, which must compete on price, would be even further weakened. Why should Europe pay any political price for assistance that is not really needed and that might actually be counterproductive?

Moreover, there is the important difference in the composition of the eurozone (the 17 member states of the EU that have adopted the euro) and the full 27 members of the European Union. Any political concessions would have to be agreed by all 27. The non-euro members of the EU have little reason to agree to political concessions just because the eurozone is not capable of managing its own internal problems.

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