Written by Charles Scaliger on January 17, 2011

Eurozone Avoids Meltdown — For Now

But, as *Time* magazine observed, the hard balance sheet figures tell a very different story:

> Economists … say Portugal has merely bought itself some time before dipping into the $980 billion (€750 billion) bailout fund set up last year by the European Union and the International Monetary Fund (IMF). "Portugal will have to access the stability fund," says Colin McLean of U.K.-based SVM Asset Management.
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> Closer inspection of [Wednesday's] bond sale suggests as much: the yield, or interest rate Portugal must pay to borrow funds, on the 10-year bond was an average 6.72%, a figure that woefully exacerbates debt in a country whose nominal GDP growth last year was just 1.4%. Portugal's government needs to borrow around $26 billion (€20 billion) from the markets this year; a 6-7% interest rate for this sum would probably bankrupt the country. Indeed, the suspicion amongst market analysts is that the main buyer of these bonds was none other than the European Central Bank, which has an obvious interest in ensuring Portugal's stability.

In other words, the roughly $1.6 billion Portugal managed to raise in this week's auction was just a drop in the bucket as against what it will need to raise over the rest of the year, and the interest rates it is now being charged will make it impossible for Portugal to repay.

Impossible, that is, but for the bailout Portugal is sure to receive as the bankers and their kept politicos continue to postpone the inevitable meltdown and general default. In the short run, the European Central Bank can continue to maintain the fiction of eurozone solvency by purchasing sovereign debt, as it is suspected to have done on Wednesday for Portugal's sake. In the slightly longer run, the EU and IMF (and, if all else fails, the US taxpaying public) can surely afford to underwrite bailouts of a few more inconsequential European economies. But the game changer will be the collapse of Spain and then Italy — economies that no combination of creditors can afford to bail out.

The dread in every eurocrat's breast is that a Spanish default will lead to a breakdown and finally a breakup of the entire eurozone, and with it the fond dreams of continent-wide government as envisioned by the likes of Jean Monnet. The accumulation of unsustainable debt, coupled with the global economic meltdown, have made such an outcome unavoidable.

But what we are witnessing in Europe is but the beginning of a global unwinding and collapse of an entire worldwide financial edifice that for several decades has been built on sand — worthless paper money that has permitted governments and central banks to take on debt and expand the money supply without limit. Now that the rains are falling, the floods surging, and the winds blowing, the fall of this particular house will be very great indeed.