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Euro Debt Crisis Likely to Be Contained, Bullard Says (Update1)

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(Updates with euro rate in fifth paragraph, comment from Bullard in final paragraph.)

By Kim McLaughlin and Johan Carlstrom

May 27 (Bloomberg) -- Europe's sovereign debt crisis is likely to be contained within the region as the recovery trajectory in the U.S. and Asia protects them from contagion, Federal Reserve Bank of St. Louis President James Bullard said.

"The recovery in the U.S. is strong, Asia is very strong. I just don't see this coming out of Europe," he told reporters in Stockholm today.

Euro-area ministers agreed on May 2 to provide 110 billion euros (\$135 billion) of aid to Greece as the country struggles to control a deficit that reached 13.6 percent of gross domestic product last year, more than four times the European Union limit of 3 percent. When that failed to stop the euro's slide, the EU and International Monetary Fund offered a financial lifeline of almost \$1 trillion to member states. The single currency has lost 14 percent against the dollar this year.

"Many countries have restructured or even defaulted over the years. In most cases, or nearly all cases, that has not resulted in any kind of global implications," Bullard said. "There is no particular reason why a sovereign debt crisis has to mean anything for the global economy."

The euro rose 0.8 percent against the dollar today, appreciating for the first time this week to trade at 1.2273 at 11:28 a.m. in Frankfurt. Against the yen, the euro traded 1.3 percent stronger at 110.94. The gains followed comments by China's foreign exchange regulator that reports suggesting it was reviewing its euro holdings are "groundless."

Debt Restructuring

Nobel Prize winning economist Robert Mundell said yesterday debt restructuring may be "inevitable" in parts of the euro area and Steve Hanke, the architect of currency regimes from Argentina to Estonia, warned a Greek default may become unavoidable.

Mundell, who won the economics prize in 1999, predicted debt restructuring for "one or two" euro nations within five years. Hanke of Johns Hopkins University said Greece's "death spiral" will end in default if debt obligations can't be renegotiated, in an article published on the website of the Cato Institute in Washington on May 25.

"I do not think this is going to derail the global recovery," Bullard said. Of the U.S. economy, he said "real gross domestic product will reach its previous peak here shortly, maybe in the summer or early fall; globally, growth is looking fairly good."

Growth Outlook

The euro area's economy will grow 0.9 percent this year after contracting 4.1 percent in 2009, the European Commission said on May 5. That compares with the commission's estimate for U.S. growth of 2.8 percent this year after last year's 2.4 percent contraction.

It will be "very hard to get the contagion effects to move across borders or around the world because the governments have basically said they're not going to allow the largest institutions to fail," Bullard said. "Because these government guarantees are in place I don't think you get the contraction around the world that you saw in the fall of 2008 and 2009."

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