How Europe's debt virus might lead to the Western world catching a common cold

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By Rob Rikoon

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It's mighty cold in Iceland but a deeper chill has descended on the people of Ireland. Do you remember the bad ol' days of 2007 and 2008, when the Icelandic banking system capsized? In order to right that ship, the Icelandic government almost gave the Russians a military base on the southern tip of that island nation. In lieu of that politically unpalatable concession, Iceland declared its financial institution bankrupt and cleared its decks by forcing bondholders and depositors to bear their share of the $US 85 billion in losses.

While still mired in a recession, Iceland's debt is only a small proportion of its economy now and its export industry and employment prospects are looking good for 2011, so much so that Iceland's stock market was the third best performing in Europe this year. Ireland is going down a different path, one sanctioned by the European Union's (EU) leadership and similar to that taken by the USA: it is bailing out its privately owned banks with public money. As a result, Ireland will be running a deficit for years to come, unemployment there will likely rise above its current level of 13.6% and stay high well into the next decade due to the cost of complying with EU dictates. The winners: bankers, investors and politicians; the losers: taxpayers, workers and retirees.

Defaulting on debts seems dishonorable and if you are someone who lends money or if you need to borrow again in the future, it is an awful thing. However, the pain of default does go away, people adjust to their losses, and sometimes they learn from their mistakes of either borrowing or lending too much to the wrong people and life goes on. Those who suffer are those who were directly involved, the slate is wiped clean and new plans and ventures can begin.

Mandating a solution from the outside, which is what bailouts are, puts off the day of reckoning. While it feels good in the short run, as evidenced by the stock market euphoric reaction to bailout news, it creates long term dependences and interferes with the natural process of establishing viable future business opportunities, the kind that creates jobs and gives direction to a vibrant society . Japan is a good example of someplace where the markets have never had a chance to re-establish themselves after the defacto destruction of their real estate, banking and government sectors in the late 1980s and early 1990s.

Allowing Irish banks to go under would severely impact the rest of the banks in Europe and somewhat effect those in the US since there is around half a trillion dollars owed betwixt and between. The European Union might fall apart, but as I have previously written, this reiteration of a pan - continent concept may not be up to the task of creating a true United States of Europe. The Irish people would survive; in fact they would be better off long term through a default than under a bailout. The pain would be severe but relatively short.

Financial and political leaders worldwide believe that their general populaces are ignorant, soft and gullible. Perhaps we are but when people realize that their housing values, retirement benefits and employment prospects are growing consistently dimmer due to ongoing bailout costs, that's when the rubber may hit the road.

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