LEFT-WING STRATEGIES TO SOLVE THE EURO CRISIS

What answers can the left provide to the euro-zone crisis and the world economic crisis? The Left Party has begun analysing this important question in light of the continued growth of euro-scepticism. In order to further the debate, the Rosa Luxemburg Foundation has published a study by the economists Heiner Flassbeck and Costas Lapavitsas on the causes of the crisis and possible solutions. This study is summarised in the following, but can be found in full at: http://www.rosalux.de/publication/39478.

HEINER FLASSBECK

THE EURO AT A CROSSROADS

THE CONCLUSIONS OF THE STUDY BY FLASSBECK AND LAPAVITSAS

Let’s use our last chance!

The study by Heiner Flassbeck and Costas Lapavitsas, *The Systemic Crisis of the Euro – True Causes and Effective Therapies*, which has been published by the Rosa Luxemburg Foundation, clearly demonstrates that the common European currency is seriously under threat. This situation has come about because the basic conditions needed for successful monetary union have been disregarded since the very beginning. Consequently, European Economic and Monetary Union (EMU) has been managed according to principles that fail to grasp its complexity, and EMU policy, which is blinded by the ideology of its main actors, has continually focused on fiscal issues.

Since the beginning of the European crisis, which occurred at the same time as the world economic crisis, attempts to prevent the dissolution of European monetary union have been marred by serious mistakes. Once again, fiscal issues – in this case, the sovereign debt crisis – have become the focus of policy, and this has hindered the development of a comprehensive and targeted therapy package that could solve the problems currently faced by EMU. Moreover, the one-sided and clearly false accusations directed at debtor countries, as well as the austerity policies that have been demanded from them, have caused an economic crisis. Importantly, this crisis will negatively impact on people’s lives, on democracy, and on the peaceful coexistence of citizens in Europe for decades to come.

However, it is not too late to change direction. If Germany, as the most important creditor country, were to show a greater understanding of the crisis and radically change its position, as well as develop a new strategy together with other countries, it should be possible for the euro-zone to overcome its severe recession and the economic crisis. Nevertheless, the chances of creating a successful turnaround dwindle with every day that we remain attached to the old, failed strategy. A new strategy would need to include the following crucial elements: a reduction of the gap in competitiveness, particularly by increasing wages in Germany; an immediate end to fiscal austerity; and providing European Central Bank (ECB) credit, Eurobonds or largely unconditional support through the European Stability Mechanism to bridge the difficult transition period for debtor countries. Yet even these solutions would need time: it would take at least ten years for the debtor countries to return to a situation in which they are economically self-reliant, and able to generate growth and jobs.

Yet as fundamental policy change remains highly unlikely, other policy options need to be considered. This is imperative as we are faced with a situation in which the costs associated with change in the worst-affected countries would be extremely difficult to manage politically and could seriously endanger democracy. Flassbeck and Lapavitas demonstrate that the benefits of EMU could have gone far beyond political considerations. Common monetary policy over a large part of Europe represented an incredible chance; yet this chance has been left untapped. In light of the fact that debtor countries are imposing extremely costly processes of change, and that there is no guarantee that these processes will soon enable debtor countries to return to a path of sustainable growth, politics is being pushed to its limits: it is essential that this be recognised.

Democratically elected governments can only impose a limited amount of suffering on their citizens. This is especially the case during a crisis in which it is difficult to explain why one country must continue to suffer while other countries or institutions have taken de facto control. It is unlikely that citizens in affected countries will accept this situation for long. History foreshadows the inherent potential within economic crises for conflict, rebellion and chaos. Nonetheless, in the majority of historical cases, political damage was limited by currency devaluation, which provided a relatively fast method of bringing about economic turnaround, and improved the outlook for the economy. EMU currently lacks such a mechanism. In fact none of the economic policies that have been forced on countries by the troika has the potential to bring about positive economic change. Wage reductions are clearly counter-productive as they harm the domestic economy, which, with the exception of Ireland, is quantitatively far more important in Europe than the export sector. Moreover, so-called supply policies cannot help overcome the current weakness in demand as they tend to exacerbate the demand-side crisis.

Exit must be an option

Sooner or later, and in the case of the euro-zone this point is not far off, democratically elected governments will have to demonstrate their ability to tackle the crisis. It is essential that economic confidence be strengthened and that people, especially young people, gain hope for a better future. If this does not occur, support will rise for the margins of the democratic spectrum. Accordingly, continued crisis throughout the region – both in creditor and debtor countries – is likely to boost support for political parties that question EMU, blame it for the suffering caused by adjustment policies, and propose a national exit. In the early stages of EMU, many supporters of the European idea naively assumed that an irreversible step had been taken. However, all social regulations that people make can and must be changed if they fail: blocking debate about an exit from EMU because of an unwillingness to question the value of Europe as a political entity is irresponsible and only serves to play into the hands of the euro-sceptics.

Nonetheless, if we were to act sensibly and consider exit as an option, we would still have to develop a means of countering centrifugal nationalist powers without destroying the idea of a political Europe. Apart from the many minor technical problems that might arise during an exit scenario, two main hurdles would have to be overcome. First, strict controls on the movement of capital would be essential if capital flight and a run on the banks were to be avoided in the case that exit was being considered in one or more countries at the same time. Cypress provides a precedent: on the one hand it demonstrates that exiting EMU can be brought in line with European treaties and agreements; but it also proves that controls can be put in place quickly enough to prevent chaos from developing after it has become clear that an exit is being considered. Second, during the transition to a new national currency there is a risk that leaving a currency's value to the market might lead the currency to collapse, which would make transition a very painful and expensive process.

All deficit countries need currency devaluation of the order of 25 to 40 per cent; further devaluation would seriously harm European trade, while implementing a new currency would severely reduce the income (in real terms) of countries that are heavily dependent on imports; paradoxically, this could then develop into the next political bombshell. Consequently, the most important current challenges facing European politics are: preventing excessive currency devaluation; enabling countries that want to remain part of the EU to do so (probably the vast majority); and protecting the European single market by ensuring the transition process is as painless as possible. The study by Flassbeck and Lapavitsas has shown that implementing these measures would revive the European monetary system by protecting the countries that choose to exit EMU from uncontrolled devaluation. This would enable them to regain their competitiveness without facing the collapse of their domestic economy.

Germany's economy would undoubtedly be hit hard by a euro exit, and would be subjected to a harsh process of adjustment even if countries (including southern European countries and France) exited EMU in an orderly manner. This is because Germany's production structure, which was built up during the years of monetary union, is extremely heavily geared towards exports: exports amount to more than 50 per cent of German GDP. A euro exit would lead the export sector to shrink significantly, although this would also be dependent on the type of adjustment undertaken and whether it could be at least partly offset by expansion of the domestic market. However, if Germany were to attempt to counter its reduced competitiveness with further pay cuts, a deep and prolonged recession with high unemployment would be unavoidable. Once again, it is crucial that Germany understands and accepts the causes of the crisis, and this includes acknowledging its own mistakes and acting accordingly. A renewed struggle for competitiveness and market share would threaten the livelihoods of large sections of the German population, and this could threaten the country's political stability.

Europe is more than just the euro

Many people who have good reason to associate Europe with historical peace have great difficulty accepting the dissolution of monetary union or an exit of some states from EMU. Despite this, we need to remain realistic. Monetary union appears to have taken place too early, and to have gone too far. Although rescuing the euro would be a great achievement, if the euro cannot by saved in every country, all available political energy should be used to protect a politically united Europe from the collapsing ruins of part of its monetary union.

The study clearly shows that the decision to take on the euro can be based upon sound economic arguments; however, since the beginning, these arguments have been ignored and politically discredited by dominant economic theory. Even major institutions such as the ECB and the European Commission have attempted to implement monetary union in accordance with dominant neo-classical theories: their experiment has completely failed. A form of monetary union that is built upon the monetarism of the ECB and the Commission, as well as on a crude belief in competition between nations, a view that is held by the largest EU member state, can and could never work in practice.

We cannot allow Europe to call itself into question because of strong ideological views on the economy. Everyone who wants to save Europe as a political idea – and that must be the overriding aim – needs to realise that this can only be accomplished with an economic theory that is both realistic and progressive. We need to understand that everyone is entitled to benefit from economic progress under all circumstances, and that the idea of competition between nations is absurd; then and only then can we hope to build a new Europe out of the old ruins.

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Heiner Flassbeck is an economist and founder of Flassbeck-Economics. In 1998 and 1999 he was secretary of state in the Federal Ministry of Finance. From 2003 to 2012 he was chief economist at the United Nations Conference on Trade and Development (UNCTAD); www.flassbeck-economics.de.

The Rosa Luxembourg Foundation is one of six party-affiliated political foundations in the Federal Republic of Germany. The Foundation's primary aim is to provide political education. The Foundation is affiliated with the Left Party (DIE LINKE).