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Economic Crisis

A left strategy for Europe

- IV Online magazine - 2011 - IV435 - April 2011 -

Publication date: Wednesday 13 April 2011

Michel Husson's article, A European strategy for the left was published by International Viewpoint on January 2011. In the article Husson argues that "the radical left must not get locked into the impossible choice and start the risky adventure of leaving the euro and a utopian idea of currency harmonisation." In this response Costas Lapavitsas argues that the euro is irreformable and advances an alternative strategy. A fuller version of this article will appear in Socialist Register, 2012, The Crisis and the Left, in a forum discussion with Elmar Altvater and Michel Husson.

Crisis and Austerity

The roots of the turmoil in Europe lie in the world crisis that commenced in 2007. Briefly put, the bankruptcy of Lehman Brothers in September 2008 led to a banking crisis, which ushered in a global recession. European economies were hit by collapsing exports and contracting credit. The worst was averted through state intervention, partly to support banks, partly to sustain aggregate demand. But state intervention led to the next and more severe stage of the crisis, that of public debt. And as the public debt crisis got deeper, it threatened to reignite the banking crisis.

It cannot be overemphasised, however, that the specific character and ferocity of the European turmoil are due to the monetary union. The euro has acted as the mediator of the world crisis in Europe. From the perspective of Marxist theory, this is hardly a surprise since the euro is a form of world money and not just a common currency. The euro is designed to act as means of payment and hoarding in the world market or, in the language of mainstream economics, as a reserve currency. It serves the interests of the major states that command it as well as of the large financial and industrial enterprises that deploy it internationally. But, by the same token, the euro has crystallised the tensions and imbalances of European capitalism, acting as the epicentre of crisis. This has been a classic feature of world money since gold played that role and dictated the pace of crises through its hoarding, inflows and outflows.

The euro is an unusual form of world money created afresh by an alliance of states, with Germany at its core. It contrasts sharply with the dominant form of world money, the dollar, which is a national money catapulted into its world role due to the imperial power of its unitary state and economy. For the euro to be able to act as world money it has been necessary to create institutional machinery suited to an alliance led by Germany, a nation state considerably weaker than the USA. Three elements have been instrumental to it: first, an independent central bank in full command of monetary policy and presiding over a homogeneous money market for banks; second, fiscal stringency imposed through the Growth and Stability Pact; third, relentless pressure on labour wages and conditions to ensure competitiveness for European capital.

The institutional machinery of the euro has catalysed the crisis in Europe. Pressure on labour has been most relentless at the core of the eurozone, resulting in rising competitiveness, primarily for Germany. The result was an entrenched gap between core and periphery, reflected in current account surpluses for the former and deficits for the latter. The gap was bridged by huge capital flows from core to periphery which took the form mostly of bank loans. [1] In the periphery, furthermore, banks engaged in rapid expansion thus adding further to debt. By the end of the 2000s, the periphery had become enormously indebted – domestically and abroad, privately and publicly.

When the world crisis hit Europe, leading to recession and state intervention, it inevitably turned into a crisis of peripheral debt in all its dimensions. In turn the debt crisis threatened to become a banking crisis that could potentially destroy the euro. The response to the crisis by the European ruling classes – of both core and periphery – has cast a harsh light on the entire European â€˜project’. Their paramount concern has been to rescue the euro. To achieve this aim, policy has focused on saving the banks exposed to peripheral debt. Thus, the ECB has advanced abundant and cheap liquidity to banks; in contrast, miserly liquidity at high interest rates was made available to states. At the same time, unprecedented austerity was imposed on peripheral countries, while welfare provision was cut and labour conditions were worsened. The costs of the crisis were thus shifted onto the shoulders of working people as far as possible. By early 2011 the class content of the policy to rescue the euro had become crystal clear: first, to defend the interests of financial capital by protecting bondholders and other lenders, second, to promote the interests of industrial capital by crushing labour costs.

These policies have been dictated by Germany, the main beneficiary of the euro. German ascendancy is now stronger than at any time in the history of the European Union. By the same token, the imperial interests at the heart of the eurozone have become transparent. If the current policy to rescue the euro succeeds – and there are grave doubts that it will – Germany will emerge as the undisputed master of the eurozone and the dominant force across Europe. The periphery, meanwhile, will stagnate with high rates of unemployment and worsening income distribution. Even so, a thin layer of financial and industrial capital within the periphery will probably continue to do well.

The crisis has been a momentous event for Europe. It has forced through rapid social change in favour of capital and against labour. It has also encouraged geopolitical change, turning the eurozone into a German backyard. At the same time, it has put paid to the hackneyed ideas of European partnership and federalism that have provided the ideological cover of the eurozone. The crisis should have thus provided an opportunity for the Left to recover its poise putting forth anti-capitalist proposals to take Europe in a socialist direction. Unfortunately this has not yet happened. Much of the continental Left is still in the grip of Europeanism, and is concerned to develop strategies that have a European rather than a socialist character. Above all, it is in fear of disrupting the monetary union. The result has been the absence of effective Left opposition to the social and imperial transformation currently taking place in Europe.

A â€˜good euro’?

The Europeanist Left clings to the notion that the eurozone could be reformed in the interests of working people, creating a â€˜good euro’. Advocates of the â€˜good euro’ can be split into two currents, both of which are prominent within the newly formed Party of the European Left but also more broadly across Europe. [2] One current are ardent Europeanists who generally downplay the class and imperial interests at the heart of monetary union. The other current are reluctant Europeanists who, despite stressing class interests, do not fully appreciate the implications of creating a new world money. Both are terrified of the dangers of nationalism and isolationism, should the eurozone collapse. The monetary union might have been ill-conceived, but now that it has become a reality, it would not be advisable to break out of it. [3]

For reluctant Europeanists this position also leads to what might be called â€˜revolutionary Europeanism’, overthrowing capitalism on the supposedly privileged terrain of European integration. Logically this should also entail creating a unitary (and revolutionary) European state, but this demand is not often stated explicitly. Whether ardent or reluctant, â€˜good euro’ proposals demonstrate considerable convergence. There is, for instance, general agreement that austerity and liberalisation ought to be resisted, and that Europe needs major redistribution of income and wealth. There is also agreement that a coordinated investment policy would be desirable to raise productivity in the periphery and to restructure the European economy.

These are creditable ideas and much of the Left - Europeanist or not – would probably concur with them. The trouble is that they do not deal with the pressing nature of the crisis. By far the most acute aspect of the crisis is the debt of the periphery. It has eventually become accepted across the Left that the burden of debt on several peripheral countries must be lifted for economies to recover. Beyond this point, however, agreement is hard to find. Ardent Europeanists, such as those within the Party of the European Left, tend to favour consensual restructuring of debt (in effect, creditor-led default) which would lower the level of peripheral debt without upsetting the mechanisms of the eurozone unduly. The trouble is that creditor-led default is unlikely significantly to reduce peripheral debt. Lenders are not generally known to welcome losses. Reluctant Europeanists, consequently, tend to favour radical restructuring of debt, often at the initiative of the borrower. But they propose to write debt off unilaterally while remaining within the framework of the eurozone, the main powers of which will have to take the losses. Quite how this will be achieved has not yet been explained.

Against this background, Europeanists have put forth a variety of specific proposals regarding debt. Here the ground becomes treacherous because it leads to the outer reaches of actual policy-making by the governments of Europe. The proposals have typically revolved around lending by the ECB and issuing Eurobonds, aspects of which are already present within the current policies of the eurozone.

Summarising ruthlessly and across a variety of suggestions, the general idea appears to be that the ECB should expand its current practice of purchasing public debt in secondary markets (and lending against collateral of peripheral public debt.) The ECB should acquire much of the existing debt of peripheral countries and it should also finance the fresh borrowing of eurozone states in the future. It is further suggested that the issuing of Eurobonds – which is already undertaken by the European Financial Stabilisation Facility to obtain funds for lending to countries in difficulties – should be expanded to meet the regular lending needs of eurozone states. [4]

Nothing precludes crossbreeding between these suggestions, including the notion that the ECB should be financing itself by issuing Eurobonds. Such proposals appear as the analogue of the operations of Federal Reserve in the USA, and thus as an important step toward creating fiscal as well as monetary homogeneity within the eurozone. Unfortunately, there are major problems with these proposals, which help explain why they have generally been given short shrift by the eurozone establishment. One problem relates to the losses from bad peripheral debt. If, for instance, the ECB were to acquire existing peripheral debt at a deep discount, the capital of banks would have to be replenished to prevent failure; if debt was acquired at face value, there would probably be substantial eventual losses for the ECB which would have to be made good. There is a prevalent confusion among much of the Left as to what a central bank can do. The ECB indeed possesses an enormous ability to act as lender of last resort, i.e., to advance liquidity to banks and states. But lender of last resort has nothing to do with handling bad debts, i.e. solvency. Guaranteeing solvency is a matter for the Ministry of Finance which must mobilise tax income to make good the losses represented by bad debts. In the context of Europe this means drawing on the tax income of core countries, and therefore imposing burdens on working people. The ECB has no power to make good the foolish lending that European banks indulged in during the 2000s. Recapitalising the banks means committing tax revenues, a step that would have profound class and power implications

Furthermore, the suggestion that the ECB should systematically acquire peripheral debt and, even more, that it should have an open commitment to finance the future borrowing of eurozone countries would pose a threat to the euro as world money. If the ECB were, for instance, to begin financing the regular borrowing of all eurozone countries, there would be heightened risks of inflation which would lower the credibility of the euro in world markets. There is no comparison with the dollar in this respect. The dollar is the incumbent form of world money that draws on established institutional and customary mechanisms for its acceptability. The euro is a competitor that has not yet developed a firm framework of acceptability for itself in the world market. The German ruling class is unlikely to accept state borrowing arrangements that might jeopardise the global acceptability of the euro.

Similar considerations apply to issuing Eurobonds in order to replace existing peripheral debt. The borrowing difficulties of peripheral states can certainly be managed through Eurobonds, though this would be a slower method than the ECB providing liquidity directly. But confronting the likely losses from bad debts is an entirely different matter, which requires committing capital from tax income. And that is without even mentioning the additional cost to core countries from borrowing at higher interest rates, if they were to issue Eurobonds jointly with peripheral countries.

Finally, there is a further problem which is often not appreciated. â€˜Good euro’ proposals essentially aim at overcoming the contradiction between fiscal heterogeneity and monetary homogeneity within the institutional machinery of the eurozone. Presumably, if a common fiscal space was created across the eurozone, either through loans by the ECB, or by issuing Eurobonds, the functioning of the euro would become smoother and crises would be eliminated. But the problem is that the financial sphere of the eurozone is not nearly as homogeneous as is often imagined. There is indeed a homogeneous money market, which regularises the terms of bank borrowing across the eurozone, but the ownership of banks remains resolutely national. Similarly, there is no homogeneity in supervising and regulating bank activities, both of which are largely left to each nation state. Consequently, if bank solvency became problematic, banks would only be able to seek recourse to their own state, as happened in Ireland in 2009-10 and Belgium in 2008-9. There are no European mechanisms to handle the losses that European banks would inevitably make if peripheral debt was written off. And nor is there any obvious way in which German or French workers could be made to accept higher taxes to rescue, say, Italian banks. Each state would have to deal with the losses of its national banks. The euro remains a creation of nation states in this regard, and its implications for workers have a clear national aspect.

A radical left strategy

A radical alternative to the policies currently adopted across the eurozone should offer a resolution of the crisis that would shift the balance of social forces toward labour and push Europe in a socialist direction. For the Left to develop a distinctive position, it would have to challenge the strategic choices of the rulers of Europe instead of merely focusing on malfunctioning institutional arrangements. The first step would be to acknowledge the class and imperial relations at the heart of the eurozone. Working people in both core and periphery have no stake in the success of the European Monetary Union. On the contrary, the attempt to create a world money that serves the interests of European capital has meant worsening labour conditions at the core and major crisis in the periphery.

A radical alternative should also recognise that the current policy of imposing austerity and promoting German ascendancy has a high probability of failure. The main reason is that austerity leads to recession which worsens the problem of debt. Even worse, the long term prognosis for the periphery is for low growth. Greece, Ireland and Portugal will find it increasingly difficult to service their public debt and will probably have to restructure, or even default. The inevitable losses would impact upon core countries, and the sums are likely to be large. Greece alone, if it is to have decisive relief, would require a reduction of public debt by perhaps 50%-60%, approaching 200 bn euro. Should this eventuality materialise, continued membership of the eurozone would be put on the table, partly by core countries, and partly by defaulting peripheral countries themselves. The rickety structures of the eurozone would then come under even greater pressure. The Left ought to be preparing for such a turn of events, instead of recoiling from it in horror.

The division between core and periphery implies that a radical left alternative would necessarily differ across the eurozone. For workers at the core, particularly Germany, it would be vital to break the relentless pressure on wages imposed by monetary union. But note that it is fallacy to think of higher wages as a means of rescuing the euro on the grounds that they would, presumably, rebalance competitiveness across the eurozone and boost domestic consumption in the core. There is no capitalist class that would systematically aim at raising the wages of its own workers, since it would then be ruined in competition. If wage restraint was broken in Germany, the monetary union would become a lot less attractive for the German ruling class, raising the issue of its own continued euro membership. After all, Germany has long experience in deploying the Deutschmark strategically to improve its share of world production and trade.

A radical strategy in core countries ought to include further steps that could complement the reversal of wage restraint while preparing for the failure of monetary union. An important element would be control over the financial system. Tax and other impositions to rescue banks from their reckless exposure to the eurozone periphery ought to be resisted. Indeed, the Left ought to be making the case for bank nationalisation that could act as lever to rebalance core economies, assuming that the mechanisms of control over banks would also be changed to reflect broader social interests. Above all, the weight of the German economy ought to be shifted away from exports and toward improving domestic consumption, public provision, and infrastructure. For this, it would be necessary to recapture command over monetary policy from the ECB and to impose controls on capital flows.

In the periphery, on the other hand, the immediate focus of a radical alternative must be to confront the burden of public and private debt. Public debt, in particular, has to be renegotiated with the aim of writing off its greater part. To this purpose there should be debtor-led default drawing on grassroots participation. There are certainly costs to defaulting and unilaterally writing off debt, including being shut out of financial markets for a period and paying higher interest rates in the future. But even mainstream literature points out that – to its surprise – these costs do not seem to be very substantial. [5]

Debtor-led default would be immeasurably strengthened by establishing independent Audit Commissions on public debt across peripheral countries. They would facilitate workers' participation in confronting the problem of debt, not least by allowing for independent knowledge of the causes and terms of indebtedness. The Commissions could make appropriate recommendations for dealing with debt, including debt that is shown to be illegal, illegitimate, odious, or simply not sustainable.

Debtor-led default in the periphery would immediately raise the issue of eurozone membership, given that the lenders are the core countries. Exit is an important component of a radical Left strategy that could annul austerity while restructuring economies in the interests of labour. But changing the monetary standard is a major shock that would require a broad programme of economic and social change. The most important concern would be to prevent the monetary shock from becoming a banking crisis, for then the repercussions on the economy would be severe. It follows that banks would have to be placed under public ownership and control, protecting depositors, avoiding bank runs, and creating a framework to restructure the economy. Needless to say, it would also be necessary immediately to impose capital controls.

The new currency would depreciate thus putting added pressure on banks borrowing abroad, but also removing the shackles from the productive sector and boosting exports. Regaining command over monetary policy while defaulting on the debt would also immediately remove the stranglehold of austerity on the productive sector. On the other hand, rising import prices would put pressure on workers' incomes, thus necessitating redistributive measures through tax and wage policy. Finally, industrial policy would be introduced to restore productive capacity in the periphery and to create employment. A concerted effort could then be made to raise the productivity of labour allowing peripheral countries to improve their position in the international division of labour. Naturally, such a dramatic shift in the balance of social forces in favour of labour would require democratic restructuring of the state improving tax collection and dealing with corruption.

A radical left strategy for both core and periphery would comprise transitional measures in the most profound sense of the term. Its precise character would depend on the social forces that would be mobilised to support it and on the types of struggle that would emerge. But the great merit of the strategy is that it could change the balance of forces against capital, creating better conditions to resolve issues of distribution, growth and employment. In this respect, a radical left alternative would create a favourable environment for socialist change by improving the social and economic conditions of workers.

There is no need for such a strategy to lead to isolationism and nationalism provided that the European Left regained a modicum of confidence in itself and in its historic arsenal of socialist ideas. Indeed, the danger of a nationalist backlash is likely to become worse as long as the Left continues to disappoint working people. â€˜Good euro' proposals offer no means of stopping the ruthless re-assertion of class and imperial interests in the eurozone. A strategy that confidently detached itself from the failing project of monetary union would provide a basis for solidarity among European people. For that, the Left would have to abandon Europeanism, the official ideology that has for long haunted its collective mind.

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Both this article and the Husson article to which it responds were originally published by *Socialist Resistance*

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[1] As is fully established in RMF (2010).

[2] Both were very much in evidence at the conference â€˜Public Debt and Austerity Policies in Europe" The Response of the European Left', held in Athens in March 2011 http://athensdebtconference.wordpress.com/about/

[3] Witness, for instance, ATTAC-Germany (2011) and Husson (2010).

[4] The idea of systematically issuing Eurobonds gained considerable influence when proposed by the official voices of Juncker and Tremonti (2010). But it had already been circulating among left currents for some time.

[5] As is repeatedly noted by, for instance, Sturzenegger and Zettelmeyer (2007).

