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# Eurozone Crisis

*Academic Foresights*

***How do you analyze the present situation of the Eurozone crisis?***



It is now rather well established that the Eurozone crisis should be seen as a particular metamorphosis of the global financial crisis, which developed as a result of contagion from the American subprime mortgage crisis via chains of so-called 'securitisation'. It morphed into a sovereign debt-crisis because inter alia the public purse was used to bail out major banks and because low or negative growth rates reduced tax revenue. Because of the differential capacity of Eurozone member states being able to manage this situation through export-led recovery (pursued rather successfully in Germany, Scandinavia, and perhaps somewhat less so in the Netherlands; but quite the opposite in what would become derogatively known as the so-called PIIGS), the situation became critical when interest-rate spreads generated an acute insolvency crisis that threatened to cause a collapse of the common currency itself. The crisis also revealed the intellectual failure of the so-called 'efficient market hypothesis', whereby it was believed that liberalised financial markets would generate an efficient allocation of savings to investments. According to this line of thinking, the increasingly cavernous gap between current account surpluses in northern Europe and deficits in southern Europe was no cause of concern, because investments in the south would produce the enterprises whereby the accumulated debt would eventually be repaid (e.g. Blanchard & Giavazzi, 2002). The empty office-blocks in cities like Barcelona are particularly telling monuments of this intellectual failure (Charnock et al, 2014). It also has revealed the panglossian nature of assumptions upon which the monetary union was built that was agreed at Maastricht in 1991, ignoring the so-called 'optimum currency area problem' and the need for federal fiscal transfer mechanisms (e.g. de Grauwe, 2013).

This sort of analysis has motivated heterodox economists to critique – in part convincingly - the management of the crisis, which is based, according to them, on a misdiagnosis. Crisis management is based on the assumption that the crisis is one of 'competitiveness'. Through this misdiagnosis, the so-called 'troika' (IMF, ECB, The Commission) is forcing member states requiring financial aid to pursue austerity policies in order to generate balance of payments surpluses. Apart from the watering down of financial regulation in light of the pressure from powerful financial interests (e.g. Soederberg, 2010), this ignores the demand side of the crisis. How are countries such as Spain going to recover a 20 percent competitive disadvantage in relative unit labour costs in relation to an economy with an inflation rate of 1 percent (Germany) without exacerbating the fiscal crisis through a deepening and prolongation of recessionary tendencies? On the basis of this sort of analysis, Engelbert Stockhammer's recessionary tendencies? On the basis of this sort of analysis, Engelbert Stockhammer's (2011) econometric studies suggest that a one-sided adjustment of the deficit countries would require the equivalent of two 1930-style depressions. According to John Grahl (2012), it presupposes the Eurozone running a current account surplus to the rest of the world that is twice the size of that of China with twice the size of the Chinese economy. Where in the world economy would such surplus production be absorbed in the form of a deficit?.

The reason why this sort of analysis is only convincing in part is because, whilst it offers compelling accounts of macroeconomic proportions and the tensions entailed in crisis-management and most certainly the risks, it may be missing the main rationale of crisis management. Given the impossibility of eliminating the external macroeconomic imbalances, we may consider the possibility that this is not the primary objective. An alternative analysis would depart from Naomi Klein's 'shock doctrine' (2009). In this reading, the crisis is used as a lever by powerful interests to shape economic developments through the exertion of further market discipline and above all make common and public assets available for privatisation. It is worth noting in this context that the Excessive Deficit Procedure in the Fiscal Compact now also includes so-called 'structural' policy and the attendant 'Economic Partnership Programmes' are encoded in 'hard' European law. According to the IMF, public, non-financialised assets in real estate and land (including subsoil resources) amount to the equivalent of ¾ of total GDP of developed nation states. A special Briefing of The Economist (2014) reported that the European Stability Mechanism (ESM) is currently employing consultants to work out mechanisms through which such public assets could be brought to market from reluctant debtor member states. It should not be ruled out of hand that this provides the basis of another phase of finance-led growth, provided that the ESM and ECB monetary policy tools such as the Long Term Refinancing Operations (LTRO) and above all the so-called Outright Monetary Transactions (OMT's) help calm the market. And this is indeed the case since September 2012 when the ECB announced that it would intervene in the trading of sovereign bonds to keep yields in check.

Eurozone crisis management will prove 'sustainable'. Furthermore, social protests such as those of The Indignados or in the form of the increased strength of right wing populism, have had little impact on policy so far. However, deeper social-structural factors pertaining to social reproduction may be generating more enduring crisis tendencies for which current policy is very 'unfit for purpose'. Current policy may be ignoring the extent to which the welfare state is a structural necessity for social reproduction in modern societies where extended family networks and conventional partriarchial social norms are being undermined. The so-called 'industrialisation thesis' of the welfare state has produced some rather robust empirical evidence to that effect (Wilensky, 1975; Hort & Kuhnle, 2000). Southern European states did also increase their social expenditure as a proportion of GDP in the first decade of the EMU exactly in response to reproductive needs (Rhodes, 2002: pp. 312-13). As a result of the effect of austerity and higher rates of unemployment, many southern Europeans move back in with their parents and grandparent and rely on highly precarious family networks for their sustenance and management of life-risks. This may trigger more subtle crisis-mechanisms even when macroeconomic management and street-politics have been effectively checked.

***In your opinion, how will the situation likely evolve over the next five years?***

The mechanisms that I invoke do not operate in such short time-scales. The most immediate trigger that makes also more reluctant welfare reformers consider increasing social expenditure is low birth and fertility rates. This has forced the so-called 'Asian Tigers' to embark on ambitious social reform programmes in health, pensions and education that can be compared to the programmes, introduced b conservatives in Europe such as Bismarck, which formed the origin of northern European welfare state development in the 1880s (Briggs, 1969). I am not making the inference that social cutbacks in southern Europe will generate a corresponding drop of fertility, birth and population-growth rates in such as short a timescale as five years. In fact in some southern European states afflicted by the Eurozone crisis, birth, fertility and population growth rates have increased after the crisis (albeit from very low levels). But welfare state research would suggest that in the longer term the problem would be exacerbated. There are also indicators of more immediate effects in other areas. A recent study in The Lancet suggests that the interaction of economic shock, fiscal austerity and social protection systems under threat in the Eurozone crisis and crisis management can be related to dramatic increases in suicide rates, infectious diseases, and HIV as health-systems are put under strain (Karanikolos et. al., 2013).

***What are the structural long-term perspectives?***

The argument presented here can be summarised with reference to this question. Eurozone crisis management does not take into account a core finding of welfare state research, namely that at its essence the welfare state is not primarily a 'generosity', ideological artefact, or 'optional extra'. It is a structural feature of modern society, which serves crucial reproductive functions when extended family networks are attenuated and traditional patriarchial norms are rejected as has increasingly been the case in recent times in southern Europe. Cutbacks in social expenditure run against the grain of structural necessities in such a situation. If this does not result in macroeconomic collapse or effective political protest, more subtle and 'silent' revolutions in everyday life are likely to compel change. Forces behind recent social reform in Asia, compelled by lifestyle changes of families and above all women that lowered the fertility rate (Economist, 2012), may be instructive in that regard.



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