European Economists for an Alternative Economic Policy in Europe

- EuroMemo Group -

European integration at the crossroads:

Democratic deepening for stability, solidarity and social justice

– EuroMemorandum 2012 –

This EuroMemorandum draws on discussions and papers presented at the 17th Workshop on Alternative Economic Policy in Europe, organised by the EuroMemo Group, on 16-18 September 2011 in Vienna, Austria. The text is based on contributions from Joachim Becker, Hermann Bömer, Tanja Cesen, Rolf Czeskleba-Dupont, Judith Dellheim, Trevor Evans, Marica Frangakis, John Grahl, Peter Herrmann, Roland Kulke, Jeremy Leaman, Mahmood Messkoub, Dominique Plihon, Werner Raza, Diana Wehlau and Frieder Otto Wolf.

For more information on the EuroMemo Group, please contact the Steering Committee (details at end of this EuroMemorandum) or look up our website at:

www.euromemo.eu

Summary

The euro area crisis threatens the future of European integration, but instead of challenging the power of the financial institutions which are driving the crisis, the European authorities have imposed austerity programmes on Greece and other peripheral euro area countries, and developed centralised policies for imposing highly restrictive fiscal discipline on all member states which risk undermining the democratic legitimacy of the European Union (EU).

Restrictive fiscal measures have depressed demand in Europe, and economic forecasts for 2012 indicate virtual stagnation, which will exacerbate the difficulties deficit countries face in servicing their debts. A euro area summit at the end of October 2011 decided that Greece's debt should be cut by 50%, but panic selling by bond holders intensified, also affecting larger countries including Italy and Spain.

Austerity programmes in Eastern European countries (Latvia, Romania and Hungary) and the euro area periphery (Greece, Portugal and Ireland), have led to especially serious recessions and major fiscal cuts have been accompanied by demands for privatisation and the deregulation of labour markets.

The EU's South-Eastern neighbours and Turkey, many of which were dependent on capital inflows, have all also been hard hit by the crisis. Like the countries of North Africa, these had all been encouraged strongly by the EU to open their economies.

Growth in several EU countries, in particular Germany, has benefited from the strong rebound in world trade since 2010, but together with the surpluses generated by China and Japan, this is contributing to a dangerous widening of global imbalances. Low interest rates in Europe, and especially the US, have led to destabilising inflows of capital to several middle-income countries, forcing up their exchange rates.

The Fukushima catastrophe has led Germany to reinstate its programme to phase out nuclear energy but this has not triggered a wider European phasing out. Following the failure of the Copenhagen conference, the EU has also failed to develop an adequate response in the area of climate change. European agricultural production, which is based on a failed model of industrialisation, has negative social and environment effects in the EU and undermines the ability of developing countries to feed themselves.

A critique of EU policy

The EU has failed to define an adequate response to the euro area crisis. The proposed reforms to the Growth and Stability Pact are based on the fallacious notion that, provided public deficits are limited, market forces will ensure balanced development. Prior to the crisis Germany had run up a very large current account surpluses, while large deficits in southern Europe were financed by capital inflows. The financial crisis in 2008 led to a sharp decline of private expenditure and necessitated a major expansion of government spending. The EU's new legislation refers to policy co-ordination, but the primary focus is on surveillance and threatens to subject economically weaker states to comprehensive tutelage in every aspect of public policy.

European banks, which face large losses on government bonds, are directly threatened by the euro area crisis. But they have mounted massive lobbying campaigns against financial reforms, and modest proposals affecting derivates and the capital requirements for banks were both successfully diluted. The Commission has proposed introducing a financial transactions tax, but this excludes foreign exchange transactions and is opposed by key states.

The crisis has laid bare the divergent productive structures in the EU. Regional policies have focussed on physical infrastructure and training, but no attention has been given to industrial policy, something which the neo-mercantilist core around Germany has no interest in promoting. EU policies have tended to cement the existing European division of labour, and imposing austerity policies on the peripheral countries will exacerbate this yet further.

The EU's Mediterranean policy has been called into question by the popular uprisings in Tunisia and Egypt; although democratisation has been welcomed, the economic model which led to widespread poverty and unemployment has not been questioned and the EU continues to promote free trade. The EU's neighbourhood and enlargement policy is at an impasse; negotiations with Turkey and countries from former Yugoslavia are making little progress and there is considerable hesitation about further enlargement in many EU member states.

EU trade policy, while paying lip-service to concluding the Doha Round, has shifted decisively towards negotiating bilateral free-trade agreements. The EU is increasing pressure on the African, Caribbean and Pacific group of countries to sign Economic Partnership Agreements, which require wide-ranging commitments to open their countries to EU trade and investment.

The EU has appropriated, wrongly, the military concept of 'security' to designate an illusory way out of dependence on the world market for energy and raw materials. The Commission's new paper on agricultural policy makes an important step towards sustainable policies, but despite recognising the social importance of agrarian labour, payments will not be confined to active farmers.

Alternatives

The ECB must act immediately as lender of last resort in the euro area bond market to break the cycle of falling prices and panic selling. Then the major expansion in the size and power of the financial sector over the last three decades must be dramatically reversed. Commercial and investment banking should be separated; cooperative, public-sector and other non-profit banks should be promoted to provide financing for socially and ecologically desirable investment projects; investment banks, hedge funds and private equity funds should be tightly curtailed. Most derivatives should be banned, and all securities should be traded on public platforms. A financial transactions tax should be introduced on all financial transactions, and a publicly-owned European ratings agency should be established.

The existing level of public debt, especially in Greece, is unsustainable. Debt Audits, as pioneered in Ecuador, should determine which debts are legitimate, and which institutions should bear the write-downs. In countries with very high public debt, a reduction should also be achieved through a wealth tax on the very rich. To prevent speculation against weaker states, euro area countries should swap remaining government bonds for jointly guaranteed euro bonds.

A common monetary policy should be accompanied by a common fiscal policy. This should aim to promote full employment with good work. Austerity programmes will make it even more difficult to repay debt, and governments with primary deficits should be provided with finance to facilitate expansion. A strong programme of public investments is necessary, especially in peripheral euro area countries. Financing should draw on the European Investment Bank, which is already empowered to issue bonds. In place of the one-sided emphasis on cuts in government spending cuts, the long-term reduction in the taxation of higher incomes should be reversed. Constitutional prohibitions on running government deficits are dangerously restrictive and should not be introduced.

A coordinated European wage policy should ensure that the widespread decline of the share of wages in national income is reversed, and that wages in states with lower incomes begin to converge on those with higher incomes. A reduction of normal working time to 30 hours a week should be introduced both to combat unemployment and as a contribution to building a society in which life is not dominated by waged work.

In place of austerity programmes, there is a need for programmes that address fundamental structural problems of capitalism today. Privatisation has been counterproductive, leading to two-tier health systems, and the role of public services should be re-established. Low wage strategies, supposedly aimed at improving competitiveness in developing regions, have failed. Development should instead be based on the adoption of modern technology, and European structural funds should be used to develop advanced productive sectors. To reduce trade imbalances, member states should seek to reduce imports, including through the expansion of renewable energy sources. Co-operatives can play an important role in integrating economic and social goals, promoting local production and consumption. Flexicurity has increased employment insecurity, and to counter this full trade union rights should be re-established and enforced. Measures should be introduced to ensure that enterprises cannot use the argument of 'competitive pressure' from other EU countries to justify lower wages and a deterioration of working conditions.

The EU should address asymmetries in relations with neighbouring countries by adopting asymmetric arrangements, which favour the neighbouring countries, and this should be reflected in a new approach to Association Agreements, which govern such relations. Free trade should be abandoned in favour of sectorally differentiated arrangements with very long transition periods. Neighbouring countries should retain the policy space necessary to strengthen their productive structures, and EU aid should be oriented to promoting industrial development.

In place of its mercantilist export-led strategy, the EU should increase domestic demand so as to absorb more imported goods and services. The prevailing model of WTO-plus bilateral free trade agreements should be abandoned so as to take account of asymmetries between countries. Trade distorting agricultural subsidies should be phased out, and demands for the liberalisation of public services by trade partners should be dropped. Development policies should be reoriented to support the construction of diversified local economies, and the construction of state capacities in less developed countries should be supported.

The EU could make an important contribution to advancing sustainable development if were to coordinate member states' initiatives for Rio II in 2012. These could include transnational green jobs programmes, linking ecological and social concerns with energy saving. The common agricultural policy could also be transformed to achieve a compromise between the political requirements of feeding Europeans with high quality food at low prices; maintaining active farmers who sustain the ecological balance in the countryside; and supporting fair exchange for agricultural products with the rest of the world.

Introduction

The deepening crisis in the eurozone threatens the future of European integration. The European authorities have at each stage of the crisis undertaken the minimum necessary to deal with the immediate situation and completely failed to get on top of the fundamental problems. In place of a major challenge to the power of the financial institutions which are driving the crisis, the European authorities have imposed policies of austerity that have led to hardship for countless citizens across the Union. These policies not only fail to deal with the root causes of the crisis; the authoritarian and highly undemocratic way in which they are being advanced also threatens to undermine the legitimacy of the whole project of European integration.

The crisis was not caused by government deficits. It originated in the US financial system as a result of policies which tried to counter decades of stagnating US wages by allowing working-class and middle-class households to finance increased consumption by borrowing against rising house prices. Policies adopted by the European Commission shortly after the introduction of the euro in 1999 sought to encourage an integrated but less regulated financial system in Europe, very much modeled on the US system, and big European banks eagerly sought the higher returns that appeared to be available in the US. The collapse of the bubble in US house prices set off the financial crisis in 2007 and when the crisis deepened in September 2008 major banks in both the US and Europe were threatened with collapse, and were only rescued by large-scale government intervention. The banking crisis, in turn, led to a collapse of credit and a major slump in output in the final quarter of 2008 and the first quarter of 2009. Output in Europe fell by almost 5% and an even deeper recession was only prevented by government measure to increase spending and cut taxes.

The big jump in government debt is, therefore, not a cause of the crisis but rather a result of measures taken to rescue the banks, expansionary policies to counter the slump, and a sharp decline in tax revenues. But as government debt has risen, the very financial institutions that benefited from the rescue seized on imbalances in the euro area, speculating against the weakest links. Since the end of 2009, a vicious cycle has developed in which financial investors and the opinions of private ratings agencies have interacted to drive up the interest rates of peripheral euro area countries' bonds, and has made it prohibitively expensive for these countries to raise new finance. This began in Greece, whose government deficit was 5% before the crisis (principally due to low tax revenues) but which jumped to 15% in 2009. While the scale of support required by Greece, and other smaller peripheral countries is relatively modest, speculation has since turned against larger countries, including Spain (which actually had a government *surplus* before the crisis), Italy and even France. In fact, government deficits in the euro area are lower than in the US or Britain, but these two countries are able to finance deficits through their central banks, a policy which at German insistence is rejected by the European authorities. As European banks once again pay large bonuses and use the tax payer as insurance, European citizens are being squeezed to pay for the crisis of state financing which, as a result, has been transformed into a deep social and political crisis.

The social crisis is deepest in the countries in Eastern Europe, which were forced to adopt strict austerity programmes as a condition for balance of payments support in 2008 and 2009, and in the peripheral euro area countries which have were obliged to cut wages and government spending as a condition of eurozone support in 2010 and 2011. Austerity policies have led to a widening social cleavage, both within countries and between countries. As governments' strive to assure the financial markets of their soundness by cutting spending, the citizens of one country are being set against those of other, in some cases richer, countries. This is fertile ground for anti-EU populism, which displays worrying signs of strengthening in several member states, including former European stalwarts such as Finland and the Netherlands.

The political crisis is being provoked by the highly undemocratic proposals which the European authorities have advanced in response to the crisis, with a dangerous tendency towards authoritarian solutions. The new fiscal proposals adopted by the European Council in March 2011, while ostensibly about policy coordination are largely concerned with a procedure for ensuring that the European Commission can impose policies on recalcitrant member states. There have been calls for a common European fiscal policy by Jean-Claude Trichet, at the time president of the European Central Bank, and Wolfgang Schauble, the German finance minister, but in both cases this has been directed at ensuring a greater financial discipline, subordinating national policies to a deeply conservative common European policy, rather than moving towards a democratically controlled European approach. In Greece, Portugal and Ireland, which are subject to EU rescue packages, democratic control over economic policy has effectively been suspended for the foreseeable future. And as the crisis in the euro area intensified in October 2011, control of policy making was seized by just two member states – Germany and France – with Germany effectively making the running on the key points. By contrast, a Greek proposal to seek democratic legitimacy for government policies through a referendum was treated with derision.

In place of the anti-social and undemocratic policies which are threatening to undermine the whole basis for European solidarity, there is a need for a fundamentally different approach. The prospect of protracted austerity and a simplistic focus on fiscal discipline will undermine the basis for economic recovery, not only for the debt-stricken countries themselves, but also for all the other states whose prosperity rests on the European market – including Germany. The countries most directly affected by the current debt crisis will only be able to resolve their problems through policies which promote economic growth not austerity. But this raises an even greater challenge. While an exit from the debt crisis calls out for policies that promote growth, environmental sustainability requires the urgent adoption of policies that will ensure a massive reduction in the consumption of non-renewable resources and the emission of green-house gasses and other pollutants.

The political leaders of the European Union and its member states have signally failed to meet these challenges, but there are voices calling for an alternative. While unions have sought to fight against the impact of official policies, new forms of popular protest, such as the *indignados,* who first emerged in Spain, have found an echo in many parts of Europe. Like the *Occupy Wall Street* movement in the US, they have raised fundamental questions about the distribution of wealth and power in our societies.

As in previous years, this EuroMemorandum seeks to set out a critical analysis of recent economic developments in Europe and to present the basis for possible alternative policies. It is intended as a contribution to the critical discussion in intellectual and social movements in Europe, and in solidarity with all those struggling against the impact of the deeply regressive, anti-social policies of the European authorities.

1 The deepening crisis of the European Union

1.1 The euro area faces 'a new and dangerous phase'

The European Union (EU) is set to register a second consecutive year of modest economic growth in 2011, but output for the EU as a whole will remain below its pre-crisis level and countries continue to diverge strongly, as shown in table 1. In Germany, and most other core euro area countries, output is expected to rise slightly above pre-crisis levels in 2011. In the peripheral euro area countries, by contrast, output is still below pre-crisis levels and, most disturbingly, recessions have actually deepened in Greece and Portugal. In Eastern Europe, although countries are set to grow in 2011, with especially strong growth in Poland, output in most other countries is still well below pre-crisis levels, most notably in Rumania and the Baltic region, which remains the worst hit area in the whole EU.

The divergent patterns of growth have been reflected in the 2011 figures for unemployment and income. Unemployment remains high throughout the EU, and although rates fell slightly during the year in around half the member states, they increased in the other half, with the largest increases in Spain, Greece and Cyrus. Real wages fell slightly in many countries in 2011 and were more than 10% below pre-crisis levels in Greece, Hungary, Romania, Lithuania and Latvia.

In the second half of 2011 the economic recovery began to slow, and this looks set to continue into 2012.[1] In Europe, demand is being depressed by the widespread adoption of austerity programmes. These are most marked in Ireland, Portugal and, above all, Greece, which have been forced to slash government spending and wages as a condition of financial support. But wages and spending have also been cut in Spain, and governments throughout the euro area have been adopting programmes designed to meet EU targets for government deficits below 3% of GDP by 2013. The international outlook has also deteriorated. Growth in the United States weakened markedly in 2011 as the impact of expansionary fiscal and expansive monetary policies waned, and the political impasse between Democrats and Republicans in Congress made further expansionary measures – such as the jobs plan announced by President Obama in September – most unlikely.[2] Furthermore, the rapid growth in larger developing countries that has benefited exports, above all from Germany, looks set to slowdown, with increasing concern in both China and Brazil at rising inflation, and the International Monetary Fund (IMF) warning of the possibility of a rapid reversal of capital flows to Asia and Latin America.[3]

The most serious challenge, however, concerns the debt crisis in the euro area which had been temporarily stabilised in 2010 but which re-emerged in spring 2011 and which entered what the IMF described as 'a new and dangerous phase' in the course of the summer. At the European Council meeting in March 2011, EU heads of government agreed on the so-called Euro-Plus Pact, a series of highly undemocratic measures designed to give the European Commission greater control over member states' economic policies, including new rules to enforce stricter fiscal discipline. They also agreed that the €440 billion European Financial

1 In October 2011, the OECD cut its forecast for eurozone growth in 2012 from 2% to only 0.3%.

2 In the face of slowing growth, the Federal Reserve is reputedly considering a third round of pumping money into the economy through large-scale bond purchases (so-called 'quantitative easing').

3 IMF, Global Financial Stability Report, September 2011, pp. 36-37.

Stability Facility (EFSF), which was created in May 2010 but is due to expire in 2013, should be replaced in 2013 by a permanent €700 billion European Stability Mechanism. The new fund will make loans against strict conditions and, despite some initial opposition, will be allowed 'exceptionally' to purchase government bonds. However, at the insistence of a group of countries led by Germany, private investors will be required to bear part of the cost in the event that over-indebted countries are unable to meet debt payments.[4] This measure, which the European Central Bank (ECB) opposed, was one of the factors that contributed to reigniting the euro area crisis. As soon as it became clear that private investors would have to bear part of the cost of future losses, the interest rate for euro area peripheral bonds began to rise significantly. For countries that were considered to be at risk, raising new finance from private investors became prohibitively expensive, and in May Portugal was obliged to turn to the EFSF for €78 billion.

Another important factor that contributed to a deepening of the crisis was the dawning recognition by private investors that the austerity policies imposed on Greece and other countries were leading to deepening recessions which made it even more difficult for countries to meet their debt payments. The Greek government had introduced major spending cuts which significantly reduced its deficit but, as output and employment fell, this led not only to widespread social hardship but also to a fall in tax revenues, making it impossible to meet agreed targets.

Euro area governments responded to the deteriorating situation at the European Council meeting in July 2011. They agreed on a new loan for Greece of €109 billion, although only around €34 billion would actually be for Greece, and the rest was to provide guarantees for a complicated scheme designed to reduce Greece's debt. Greece was to submit to yet further government cuts, together with a privatisation programme overseen by the EU authorities. Recognising that the penal interest rates charged on previous loans had exacerbated countries' problems, the rate was cut from 3% to 1% above the funding costs, and this was applied to loans previously granted to Ireland and Portugal as well. The euro area authorities also proposed a series of revisions to the terms of the EFSF, including increasing its size so that it would be able to lend a full €440 billion and allowing it to be used to buy government bonds and to recapitalise private banks – measures that had to be approved by member states' parliaments.[5]

The new initiative failed to stem the pressure from private investors and in August interest rates increased on bonds issued by Belgium, Italy, Spain and, for the first time albeit to a lesser extent, France. In response, the ECB, which had halted bond purchases in January, resumed intervention in an attempt to stabilise the market, purchasing bonds issued by Spain and Italy (the rule changes which would have allowed the EFSF to purchase government bonds had not yet been approved by member states). At the same time, with huge sums of money now set free, there was a major demand for bonds issued by Germany and the interest rate on its 10 year bonds fell below 2%, the lowest ever recorded by the Federal Republic (the same occurred for US governm. bonds, leading to the lowest rates in 60 years).

4 From 2013, all euro area government bonds will be required to include 'collective actions clauses', which enable a super-majority of bond holders to agree on a partial write-down of values when it is clear governments will not be able to repay the full amount.

5 Approval was completed in October after the Slovakian parliament, which initially voted against the revisions, gave its support.

According to IMF estimates, by August 2011, nearly half of the €6,500 billion stock of euro area government debt showed signs of heightened risk.[6] This has had major implications for European banks, which have extensive cross-holdings of government bonds. As banks faced increasing strains, equity market valuations of European banks began to decline, falling by 55% between January and September.[7] Estimates of how much capital European banks need to raise to compensate for losses vary. In July, the new European Banking Authority (EBA) published the results of stress tests on 91 major European banks, and only 9 failed. Extraordinarily, however, the tests did not consider the possibility that Greek or other government bonds might fail! Preliminary reports of revised EBA stress tests published in October indicated that European banks would need to raise some €90 billion. IMF estimates, made public by Christine Lagarde shortly after becoming the new managing director, claim that the shortfall is around €200 billion.

The authorities' most acute concern is that a Greek debt default could set off a chain of financial failures comparable to that which followed the failure of Lehman Brothers in September 2008. This concern is shared by the US, the G20, the IMF and the World Bank which have all made urgent calls for the euro area to take decisive action. However, action has been hindered by political fragmentation within the EU as well as significant differences between states, most notably between Germany and France who, to the chagrin of smaller countries, dominate the policy process.

At a much awaited European Council meeting at the end of October 2011, euro area governments agreed that, in view of the sharp deterioration in Greek finances, the loan negotiated for the country in July should be raised to €130 billion, and it backed a German call for Greece's outstanding debt to be written down by 50%.[8] In order to confront the risk of the debt crisis spreading, the meeting also agreed that the capacity of the EFSF should be enlarged to around €1,000 billion.[9] Because of a widespread unwillingness to increase contributions to the EFSF, this is to be achieved by 'leveraging' the existing €440 billion, through providing guarantees for the first tranche of losses on bonds (20% to 30% has been considered) rather than making loans. In prior negotiations, France had proposed that the EFSF should be able to borrow from the ECB, but this was blocked by Germany. The heads of government also agreed to back the European Banking Authority's proposal to increase the minimum capital requirements for European banks to 9% of assets. Here too there had been disagreement before the meeting, with France wishing to draw on the EFSF to recapitalise banks and Germany arguing that recourse to the EFSF should be a last resort after private

6 IMF, Global Financial Stability Report, September 2011, p. 16. This is based on credit default swap rates (i.e. insurance) of over 200 basis points for government debt issued by Greece (5% of total), Ireland (1%), Portugal (2%), Spain (9%), Italy (25%) and Belgium (5%).

7 Financial Times, 13 September 2011. The French-Belgium owned Dexia bank, which had large holdings of government bonds, failed in September 2011, leaving €100 billion of bonds to be held in a newly created 'bad bank'.

8 German banks had substantially reduced their holdings of Greek government debt since 2010. The write-down was initially opposed by France, whose banks maintained more substantial holdings of Greek debt, and by the ECB, which was concerned that this could set off wider defaults. In order to avoid the write-down provoking the ratings agencies from declaring a formal default by Greece, banks must 'voluntarily' exchange existing bonds for new bond.

9 The exact amount is unclear due to uncertainty about how much of the funds' resources will be available, and the degree of leveraging. Italy, which is seen as the greatest source of potential risk, has an outstanding government debt of €1,900 billion.

markets and national governments have been tapped. But many of the complicated technical issues about how to implement these proposals had not been resolved and, in the aftermath of the summit, selling in euro area bond markets intensified.

Table 1. Indicators of EU output, unemployment and wage growth

			Euro area core							Euro area periphery				
	EU 27	EA 17	Belgium	Germany	France	Luxemb.	Netherl.	Austria	Finland	Ireland	Greece	Spain	Italy	Portugal
GDP growth 2010-11, %*	1.7	1.4	2.3	2.5	1.7	3.3	1.9	2.3	3.6	0.7	-3.2	0.7	1.9	-2.2
GDP growth peak-2011, %*	-0.8	-1.0	1.7	0.8	0.5	0.5	0.0	0.7	-1.4	-9.6	-10.0	-3.1	-3.4	-3.4
Unemployment rate, 2011, %*	9.5	10.0	7.0	6.1	9.8	4.6	4.1	3.9	7.8	14.4	16.7	21.0	8.0	12.5
Real wage growth 2010-11, %**	-0.3	-0.3	-0.2	0.5	-0.1	-1.0	0.9	-0.3	-0.5	-1.3	-3.5	-1.7	-1.0	-3.6
Real wage growth peak-2011, %**	-0.4	-0.4	-1.5	0.2	-0.1	-1.2	0.3	-0.3	-0.5	-1.3	-11.1	-3.7	-1.0	-3.7

	Other euro area			Northern EU			Eastern EU							
	Cyprus	Slovenia	Slovakia	Denmark	Sweden	United Kingd.	Bulgaria	Czech Rep.	Estonia	Latvia	Lithuania	Hungary	Poland	Romania
GDP growth 2010-11, %*	1.5	1.8	3.5	1.6	4.2	1.6	2.7	2.0	4.2	2.7	4.4	2.6	4.3	1.3
GDP growth peak-2011, %*	0.7	-4.9	2.5	-3.0	4.4	-2.2	-2.7	-0.2	-11.4	-18.1	-9.3	-3.1	9.8	-7.0
Unemployment rate, 2011, %*	7.0	7.9	13.3	7.3	7.4	8.0	11.5	6.8	12.8	16.2	15.6	10.9	9.5	7.3
Real wage growth 2010-11, %**	0.5	-0.2	0.3	-0.8	1.6	-0.1	3.2	0.3	0.8	-1.7	0.2	-1.3	2.0	-4.2
Real wage growth peak-2011, %**	0.5	-0.2	7.1	-0.8	0.8	-1.6	9.5	1.9	-3.8	-22.9	-17.0	-11.8	4.6	-16.9

Source: * Eurostat (October 2011), ** Ameco (May 2011). Peak is highest previous year since 2007.

1.2 'Austerity' as a policy guideline

The European Council set its austerity policies at its March 2011 meeting, as follows: 'Within the new framework of the European semester, the European Council endorsed the priorities for fiscal consolidation and structural reform. It underscored the need to give priority to restoring sound budgets and fiscal sustainability, reducing unemployment through labour market reforms and making new efforts to enhance growth.[10]

Each of the above strands is further elaborated by the European Commission in its report on 'advancing the EU's comprehensive response to the crisis' (COM[2011]11 final), whereby:

- Restoring sound budgets and fiscal sustainability requires annual adjustments of the structural budget in excess of 0.5% of GDP, the conventional benchmark of the Stability and Growth Pact. This is to be achieved by keeping public expenditure growth 'firmly' below the rate of medium term trend GDP growth and increasing taxes, espe-

[10] European Council, 24/25 March 2011, Conclusions, para. 2, p. 2.

cially indirect taxes, considered to be more 'growth-friendly' than direct taxes. Also, fiscal consolidation is to be supported by pension system reforms, such as increasing the age of retirement and providing incentives for complementary private savings.

- In order to reduce unemployment, governments are advised to 'provide incentives to work, avoid benefit dependency and support adaptability to the business cycle' (ibid, p. 6). Also, in order to balance security and flexibility, it is recommended that governments 'reduce over-protection of workers within permanent jobs' (p. 7).
- In relation to growth, 'frontloading' growth enhancing measures are recommended. Such reforms include the elimination of the remaining 'barriers to trade and obstacles to entrepreneurship', the full implementation of the Services Directive, and tax harmonisation, although this is deemed to be a 'sensitive' issue (p.8).

Overall, the main strands of EU economic and social policy constitute a triptych, consisting of 'fiscal consolidation – labour market reform – market liberalisation', where liberalisation includes privatisation of state assets, as well as of social security systems. This triptych is encapsulated in 'austerity', as a defining element of the present neoliberal agenda and a central policy guideline employed not only by the EU, but also by the IMF, as can be seen from the individual EU/IMF Programmes, which come under two headings, the Balance of Payment facility and the newly instituted, albeit of a temporary duration as set out in section 1.1 above, European Financial Stability Facility (EFSF) and the European Financial Stability Mechanism (EFSM). Both the EFSF and the EFSM were based on the loan facility set up for Greece.

The EU/IMF Programmes I: Balance of Payments facility

In the aftermath of the financial crisis, a number of joint EU/IMF balance of payments (BoP) Programmes were put into effect in Hungary, Latvia and Romania. According to Art. 143 of the Treaty of the Union and EC Reg. 332/2002, these programmes are addressed to member-states in balance of payments difficulties and aim to safeguard the functioning of the internal market and/or the implementation of common commercial policy. They entail the provision of medium-term financing on the basis of conditionality. The BoP facility is only open to member-states that do not belong to the eurozone. It has a ceiling of €50 billion.

In particular, the EU acts as a borrower, issuing debt instruments in the capital markets and lending the funds thus raised to the programme countries. On the basis of the Vienna Initiative created in 2009, other international financial institutions, such as the EBRD, EIB and the World Bank also participate in these programmes.

Latvia – In December 2008, Latvia was granted a BoP Programme, expiring in January 2012 and amounting to €20 billion, of which €6.5 billion were from the EU. The conditions of the Programme included the following: fiscal consolidation; fiscal governance reform; financial sector regulation and supervision reform; structural reforms; and absorption of EU structural funds for projects co-financed by the EU.[11] In 2007 Latvia had a current account deficit amounting to 22.3% of GDP, which was reduced to 0.3% by 2011. There was, however, a decline in Latvia's real GDP of more than 20% between 2007 and 2010 while unemployment rose from 6% of the labour force in 2007 to 17.2% by 2011. The low rates of growth forecast for 2011 and 2012 will still leave output more than 10% below the 2007 level and unem-

[11] http://ec.europa.eu/economy_finance/eu_borrower/balance_of_payments/index_en.htm

ployment over 13%. Last but not least, in 2007 its public deficit was only 0.3% of GDP and its public debt 9% of GDP, rising to 4.5% and 48.2% respectively by 2011. These figures underscore the fact that although Latvia did have a problem in the face of the crisis and a severe recession, this was not one of public indebtedness. This raises clear doubts over the EU's emphasis on austerity. These figures point to the fact that, although Latvia did have a problem in the face of the crisis, this was not one of public indebtedness which would have justified the emphasis on austerity.

Romania – Romania was granted two BoP packages: €20 billion, of which €5 billion was from the EU, in May 2009 for 24 months and €5 billion, of which €1.4 billion was from the EU, in March 2011, also for 24 months. The conditions of the BoP programmes were identical with those for Latvia, with the addition of the privatisation of state-owned enterprises, the reform of the public wage system and of the pension system.[12] Like Latvia, Romania had a current account deficit in 2007 (13.6% of GDP), which was reduced to 4.4% by 2011. However, its public finances were within the Stability Pact limits, while it had a high growth rate (6.3% in 2007). In 2007 its public deficit was equal to 2.6% of GDP and its public debt to 12.6% of GDP). By 2011, these increased to, respectively, 4.7% of GDP, primarily due to the country's severe recession (8.3% decline in GDP between 2008-2010), and 33.7% of GDP, well within SGP limits. However, under the impact of the recession, unemployment rose to 8.2% in 2011.

Hungary – The BoP programme for Hungary was the first to be granted, in October 2008, and expired in November 2010. It amounted to €20 billion, of which €6.5 billion was contributed by the EU. The conditions attached to the programme were the same as those for Latvia and Romania. Like these two countries, Hungary's current account improved from a deficit of 7% of GDP in 2007 to a surplus of 1.6% in 2011. Over the same period, the public sector balance improved from a deficit of 5% of GDP to a surplus of 1.6%, while public debt rose from 66% of GDP to 75%. After a severe recession in which real GDP fell by 6.8% in 2009, output is set to increase by 2.7% in 2011, although this is insufficient to restore GDP to 2007 levels. In addition, unemployment deterioriated from 7.4% of the labour force in 2007 to 11% in 2011. The large inflows of capital before the crisis have now become a source of economic fragility as MNCs repatriate profits to their richer home countries.

In all three countries, a brutal correction of the current account balance was brought about through a brutal recession. The austerity demanded by the IMF and the European Commission is in complete contradiction to the needs of these low income countries suffering from mass unemployment and in contrast to their relatively favourable budgetary situation (all three countries have government debt ratios and public sector deficits below the EU average).

The EU/IMF Programmes II: The Greek loan facility, the EFSF and the EFSM

The EU/IMF Programmes under this heading were especially set up as a response to the public debt crisis and, in the case of Ireland and Portugal, as a response to the European banking crisis. The terms of the programmes are similar to those of the Eastern European countries, although the funding differed.

The **Greek loan facility** is a 3-year programme (2010-2013) providing a total of €80 billion in

[12] http://ec.europa.eu/economy_finance/eu_borrower/balance_of_payments/index_en.htm

bilateral loans from euro area countries and €30 billion from a stand-by agreement with the IMF. The European Commission is not acting as a borrower, but as an administrator of the pooled bilateral loans. The programme is conditional on measures taken to enhance fiscal consolidation and pension reform, to promote labour market reforms, to liberalise regulated sectors and to privatise large segments of the economy still in public ownership. The following targets were set for 2014: the public deficit was to be cut from 15.4% in 2009 to at 2.6%; public debt, which stood at 127% in 2009 was to set for 157%. According to the latest review carried out by the so-called Troika (the European Commission, the ECB and the IMF), these targets are unrealistic since they underestimate the implications of the deepening recession. It is estimated that the public deficit will not fall below 3% of GDP until 2020, while the public debt will reach 186% of GDP in 2013 and 152% in 2020. The reasons offered for these divergences are the 'longer and more severe recession' than expected (GDP has declined by more than 10% since the start of the programme and it will continue to decline in 2012) and 'slippages in policy implementation'.[13] The policy recommendations remain unchanged, while Germany and France sort out their differences over the question of the restructuring of the Greek debt. In the meantime, unemployment has risen from 8.3% of the labour force in 2007 to nearly 17% in 2011.

In **Ireland,** which adopted its first austerity programme in 2009, a three-year EU/IMF austerity programme was introduced in 2010. This involved bilateral contributions from the Britain, Sweden and Denmark, from the EFSF and the EFSM, as well as from the IMF and an Irish contribution through the Treasury cash buffer and the national Pension Reserve Funds. It amounts to €85 billion in total, of which €35 billion (41%) is earmarked for the deleveraging and reorganisation of the banking sector. The other objectives of the programme include fiscal adjustment to bring the deficit from 14.3% of GDP in 2009 to below 3% by 2015, together and structural reforms of the labour market. According to the latest Troika review, Ireland is expected to return to positive growth in 2011, estimated at 0.4%, after a decline of more than 10% between 2007 and 2010.[14] The unemployment rate has risen from 4.6% in 2007 to 14.6% in 2011. The large net flows of profits out of Ireland by foreign multinational corporations have not fallen during the crisis (although some of the recorded flows may reflect transfer pricing by MNCs) and, as a result, while GDP declined by 10.2% between 2007 and 2010, GNP registered a fall of 12.1%.

Portugal is also subject to a 3-year programme (2011-2014). Support of €78 billion has been financed by contributions from the EFSM, EFSF and IMF. The programme's objectives include fiscal consolidation to bring the public deficit to below 3% of GDP by 2013, structural reforms to improve competitiveness and deleveraging and recapitalisation of the banks. Portugal's real GDP fell in 2008, 2009 and 2011 and is forecast to fall in 2012, resulting in a cumulative decline of 6%. Unemployment has risen from 8% in 2009 to 12.3% in 2011. In spite of these developments, the Troika remains optimistic that economic recovery will start in 2013, although 'most of the difficult changes still lie ahead'.[15]

Overall, the EU/IMF programmes reiterate the triptych 'fiscal consolidation – labour market reform – market liberalisation', which is evident in the general direction of EU economic and

13 Statement by the European Commission, the ECB and IMF on the Fifth Review Mission to Greece, Memo/11/684, 11 Oct 2011.

14 Statement by the EC, ECB and IMF on the Review Mission to Ireland, Memo/11/720/20 Oct 2011.

15 Memo/11/555/12, August 2011.

social policy. They have also been insisted on by the IMF. One of the most striking elements of the EU/IMF programmes is that they have all resulted in steep declines in output. According to annual AMECO date for GDP data, the fall in output between the pre-crisis peak and the subsequent trough was 20.6% in Latvia, 8.3% in Romania, 5.6% in Hungary, 14.4% in Greece, 10.1% in Ireland, and 6.0% in Portugal.

1.3 The contradictions in EU enlargement and neighbourhood policies

The growth models in the official and potential EU candidate countries in South-East Europe and Turkey have been severely affected by the current crisis. In recent years, growth in these countries was mainly based on capital inflows that were attracted by rigid exchange rates and relatively high interest rates. A significant part of the rising private debt was denominated in foreign currency and, as a result, the indebted middle strata were chained to an overvalued exchange rate. The high exchange rate has had serious drawbacks: It has stunted industrial development, especially in the successor states of former Yugoslavia. In Serbia, industrial production in 2008 was only 51% of the level in 2001.[16] Unemployment is structurally very high – around 30% in Macedonia and Bosnia and Herzegovina, and around 20% in Serbia and Montenegro.

In Turkey, the performance of manufacturing has been more positive than in the former Yugoslav republics, but it was mainly assembly plants that flourished. The exchange rate policies favoured imports over national production and exports. The trade and current account deficits were extremely high in the South-East European candidate countries, in many cases over 10% of GDP. The current account deficit in Turkey was lower, but grew significantly between 2002 and 2007. In spite of high growth rates, employment in Turkey has not grown and real wages have lagged far behind productivity growth under the Justice and Development Party (AKP) governments.

The economies of (non-EU) South-East Europe and Turkey were severely hit by the crisis. Croatia and Montenegro have suffered from a particularly strong and lasting recession. In both countries, GDP declined in both 2009 and 2010. The contraction of GDP was particularly strong in 2009 with a fall of 6.0% and 5.7% respectively. The policy choices of the two countries are severely limited. In Croatia, the level of foreign currency debts is particularly high. In view of the interests of the banking sector and those indebted in foreign exchange, the Croatian government has opted for deflationary policies and is trying to avoid a depreciation of the kuna at any price. In contrast to this strategy, Croatian critical economists have called for a more developmental approach and a conversion of existing domestic foreign-exchange debts into national currency in order to gain policy space. Montenegro has a completely euroised economy and registers the highest current account deficit in the region (26.6% of the GDP in 2010). Serbia, Bosnia and Herzegovina as well as Macedonia all suffered recessions in 2009, but stabilized GDP in 2010. Policies have been pro-cyclical in these countries as well, often under IMF programmes. The Turkish economy suffered from a severe recession in 2009 (a fall in GDP of 4.8%), but experienced a strong rebound in 2010 (+8.9%). However, Turkish growth is extremely reliant on capital inflows, with a current account deficit in 2010 equal to 9% of GDP, and the recovery is therefore extremely vulnerable to a reversal of capital flows.

16 M. Uvalic, *Serbia's Transition - The Thorny Road to a Better Future*, Palgrave, Macmillan, 2008, p. 210

The Eastern neighbour countries have also proved to be very vulnerable, though they possess a stronger industrial base than the economies of former Yugoslavia. Ukrainian pre-crisis growth was heavily reliant on capital inflows and rapidly increasing indebtedness, and Ukrainian GDP fell by 14.8% in 2009 with a limited recovery in 2010. The crisis was milder in more statist Belarus, but the economy is constrained by a severe shortage of foreign exchange.

The crisis years have revealed that the capitalist transformation strategies which were promoted by transnational and local business interests, national governments, the EU and international financial institutions have resulted in unviable production structures in the outer East European periphery of the EU. In the North African countries, the crisis revealed the structural weaknesses of the EU's Mediterranean strategy, the latter being primarily oriented towards liberal economic policies. Contrary to the Eastern European periphery, the economic crisis has translated into revolutionary political processes in Northern Africa.

Neo-liberal policies have likewise produced extremely vulnerable economies and polarised societies in the North African neighbour countries. In the financial press, Tunisia and Egypt had been presented as showcases for neo-liberal policies. These two countries were the pillar of EU Mediterranean policies in Northern Africa. The EU Mediterranean policy has two main goals: access to the energy resources of the region and political stability and, for the EU, political stability had priority over democratisation.

1.4 Radicalizing a neo-mercantilism in trade and development policies

The deepening of the financial crisis in 2008 and 2009 led to a dramatic fall in global trade, and this had a particularly marked impact on export-oriented EU member states like Germany or Austria, but the recovery of trade in 2010 and 2011 fuelled strong growth in Germany and other core EU countries. The recovery of the world economy was strongly influenced by the high growth rates of emerging economies, particularly China. At the same time, although global imbalances were somewhat muted as a result of the impact of the financial crisis, they remain at worrisome levels. While most deficit countries, in particular the US, reduced their imports as a consequence of weak domestic demand, major export nations like Germany and Japan have continued to pursue their export-oriented growth models. This is also true for China, where exports remain the driving force for growth. Although the Chinese government appears to have taken the first steps towards promoting a growth strategy based on stronger domestic demand, this will only have a serious impact, if at all, in the longer term.

A second trend with potentially destabilising effects was the appreciation of the currencies of some emerging economies. This was brought about by inflows of capital from core countries, in particular the US and the Eurozone. Emerging economies like Brazil, whose currency the Real appreciated by more than 30% between early 2009 and mid-2011, implemented measures to halt these inflows, although with limited success. Their governments interpreted the inflows as a consequence of 'beggar thy neighbour' policies resulting from large-scale monetary expansion in the US (so-called quantitative easing) and ineffective crisis management in the Eurozone, and warned of the dangers of a global currency war. While the countries of the Global South largely managed to avoid the worst impact of the global crisis in 2008 and 2009, the turbulence in the Eurozone together with the deep economic and political problems faced in the US are widely seen as a central cause of the slowdown in the global economy in 2011 and the risk of a recession in 2012.

1.5 A deepening complex crisis – the examples of energy and agriculture

The complex crisis of economic, ecological and international relations which has become apparent in recent years, is not being addressed seriously by established policies. The catastrophe of Fukushima, which confirmed all the dangers of nuclear energy, has prompted the German government to reinstate an older, long-term plan to phase out nuclear energy, and this will be followed eventually by Belgium, but it has not triggered a European-wide phasing out. In one area after another, ad hoc measures are being taken, mainly to buy time, in the hope that 'spontaneous' solutions will appear, but with no systematic approach to developing serious long-term proposals. In the case of the loss of biodiversity, for example, the EU has failed to fulfil its promise to develop an adequate policy, although the rampant destruction continues as in previous decades.

Since the Copenhagen summit on climate change failed to achieve an agreement on a post-Kyoto process, the EU has also proved unable to seize the opportunity for forming a 'coalition of the willing' which could go ahead with ambitious measures to control and reduce the emission of greenhouse gases. Instead it has continued to maintain its illusory belief that this can be achieved through technological fixes and market instruments and it seems unlikely that any serious breakthrough will be achieved unless social and political movements are able to generate sufficient pressure.

The problem of limited resources has broadened, even in the more general public perception, from 'peak oil' to 'peak everything'.[17] Nevertheless, the EU has not even begun to develop a sustainable strategy for coping with problems of resource scarcity, a policy that would have to emphasise adapting demand to supply in a socially just way. Instead, the EU continues to pursue a strategy based on 'securing privileged access' to resources for European consumers. This is an approach that is of only short or, at the very best, medium-term relevance, and, most disturbingly, is likely to involve an increasing weight for the military dimension of policy.

The problem is especially marked as regards energy policy: the EU clings to problematic energy sources (nuclear, oil, gas and coal), which are all severely limited, and there is no concerted European effort to develop a strategy that harnesses the almost unlimited potential available from energy saving and the development of sustainable sources of renewable energy. In fact, EU energy policy is set to exacerbate problems in agriculture. It aims to produce up to 20% of the fuel used for transport from agrarian raw materials, and this will have a negative impact on agriculture on a world-wide scale. As an increasing share of agricultural land is used for bio-fuels, land prices will be pushed up. The tendency for transnational corporations to accumulate large, world-wide holdings of land will increase and, especially in Sub-Saharan Africa and Latin America, small farmers will be deprived of the basis for their existence.

There are areas in which scientific understanding is highly contested or not entirely clear. But governments must be criticised when they neglect the knowledge that is available, especially when there are institutions that make it highly accessible, as is the case with the International Panel for Climate Change.[18] Policy has suffered from an uncritical reliance on certain paradigms in economics and other social sciences that have gained ascendency during the years of neo-liberal hegemony. Democratically elected governments should not neglect the

17 L. Brangsch et al., *Den Krisen entkommen. Sozialökologische Transformation*, Berlin, 2011, p. 30ff.

concerns of those affected by policies, and should take full account of the historical experience of public agencies and popular organisations in the fields at stake, and should certainly not overlook past scientific debates.

The EU's Common Agricultural Policy (CAP) offers an instructive example. EU experts appear to overlook the historical experiences related to the emerging food crisis, the milk crisis and the crisis of agrarian mobility, and also ignore the health problems linked to genetically engineered food, the pervasive use of medication in mass animal production, and the resistances induced by a massive use of antibiotics. Instead, supported by powerful lobby groups of the agrarian-industrial complex, these experts go on defending models for action and institutional regulation which have shown themselves to be inappropriate. In its most recent policy paper the European Commission takes it for granted that increased production alone will overcome the present predicament of world-wide hunger.[19] This is, however, quite insufficient: What is at stake in hunger is not only the overall level of production, but also the question of who produces for whom and at what prices; and, of course, how profits are eventually distributed along the chain of provision, from the primary producers to the final consumers.

A necessary first step to overcome this state of affairs would be to acknowledge the dismal state of European agriculture. A failed model of industrialisation in agriculture – often accompanied by genetic engineering technologies without a sustainable perspective of implementation beyond a first round of short-term successes – has led to soil depletion, biodiversity destruction, rural degradation, insecure and globally insufficient food, and reduced rural employment. No profits are made any longer in the sector without state subsidies, while it has become a paradigmatic case for an aggressive nexus between 'mass consumption', 'mass distribution' and 'mass conformity'. This has severely undercut the potential for creating the new figure of the active and aware consumer (cf. the French notion of 'consommacteur' or 'empowered consumer'). The class aspects of agricultural consumption and production seem to have entirely vanished from sight: It is not only a question of the rich versus the poor, where the ecological concerns are unevenly distributed, and the poor are more vulnerable to economic pressures. Globally, the absence of binding regulations and the preference for 'market solutions' based on private property have encouraged the processes of land-grabbing outside of the EU referred to above.

The EU's agricultural policy has created a very critical situation, externally and internally. From the 1980s up to the middle of the first decade of the 2000s, the EU was a prime mover in the process of flooding world food markets with strongly subsidized agricultural products from the industrialized countries, generating a dramatic crash in world market prices for this category of goods. Developing countries have become unable to compete and are still dependent on cheap imported food to feed their growing populations. Many countries import more food than they produce. Yet, in order to achieve sustainable development, countries need to expand their own agricultural production and reduce their dependency on volatile world markets. They therefore need additional agricultural investment, and this should be

---

18 On the negative results of government inaction around climate change see the most recent overview by the International Energy Agency, *World Energy Outlook 2011,* chapter 6, 'Climate change and the 450 scenario', pp. 205-241.

19 Cf. Legal proposals for the CAP after 2013, http://ec.europa.eu/agriculture/cap-post-2013/legal-proposals/index_en.htm, published 12 October 2011.

organised in such a way as to create employment for rural populations and strengthen the broader economic capabilities of small and medium farmers. Even if countries have the political will to promote investment of this type, it is undermined by the kind of trade liberalisation for agricultural products which the EU is supporting on a world-wide scale. This tendency to promote competitiveness at the cost of sustainable development is also reinforced by new technological structures of dependency, as in the case of the introduction of genetically modified seeds which can no longer be reproduced by the farmers who have to use them in their own production processes.

The structural problem underlying this situation is exemplified by the EU's stance on global and European forestry, which has destructive effects on forestry resources, and consequently human livelihoods, outside the EU. The monetary rewards of the EU's Emissions Trading Scheme (ETS) are encouraging big power companies, such as RWE, Vattenfall or DONG, to import huge volumes of wood pellets to generate electricity for European capital cities, such as Berlin, London or Copenhagen This is because within the EU, the incineration of wood is rewarded with CO2 credits earned for spreading the illusion of avoiding CO2 emissions from fossil energy sources, although in fact raising CO2 emissions on a global scale as a result of their operation.[20]

Internally, the subordination of agricultural production and rural development to the demands of the agro-industrial complex has been leading to the destruction of the potential of small farmers to maintain sustainable models of agriculture and regional development. The subordination of agricultural production to the interests of corporate agrarian enterprise tends to destroy the implicit multi-functionality of the agricultural sector. The conservation of biodiversity, and its contribution to climate protection, is not only often overlooked in public debates; it is not even addressed within the context of the renewed CAP which the European Commission now seems to be advocating.[21] This can, again, be specifically exemplified with regard to forestry policy: a strategy of reducing greenhouse gas emissions from agriculture and livestock production is more effective and more important than continuing to support the illusion of climate benefits from a strategy of substituting forest products for fossil fuels. The wood energy option may lead to only a transformation of forests to plantations, a development which would clearly be unsustainable.

A similar problematic has developed in the field of bio- fuels: The EU directive obliging member states to increase the percentage of bio-fuels in the total use of energy to 10% by 2020 can only be implemented by importing 50% of bio-ethanol and 41% of bio-diesel oil to the EU, mostly at the expense of food production capacities in developing countries, increasing the tendencies to land-grabbing and the destruction of primary forests and the habitats of indigenous communities.[22]

---

20 European Environment Agency Scientific Committee, 15 September 2011: Opinion of the EEA Scientific Committee on Greenhouse Gas Accounting in Relation to Bioenergy.

21 The present lack of integration and consistency of the EU policy proposals makes it very difficult to evaluate the specific weight of the proposals coming from the Agrarian commissioner only. It should be looked at, however, as an important stepping stone to be used in advancing the development of a meaningful strategy of EU sustainable development – which does not exist yet.

22 Cf. Bettina Kretschmer, Sophie Bennett, 'Analysing Bioenergy Implementation in EU member states: Results from the Biomass Futures Expert Survey', Institute for European Environmental Policy, London, 27 July 2011, www.ieep.eu/assets/827/IEEP_Biomass_Futures_Expert_Survey.pdf

2 Wrong policies lead to wrong outcomes – A critique of EU policies

2.1 Macroeconomic Policies: towards the surveillance regime

By the autumn of 2011, the complete failure of EU leaders to define a coherent response to the crisis in Greece had not only brought the eurozone to the verge of chaos; it even menaced the world economy with a catastrophic collapse. At the same time, such longer-term 'reforms' in the eurozone as have been formulated by the Commission are not only irrelevant to the current emergency, they threaten to turn the EU into a hegemonic structure in which economically weaker states would lose all political autonomy and be subjected to the permanent tutelage of the stronger states and of the EU institutions under their control. One aspect of the proposed changes was a direct assault on social models and labour standards in the countries of the so-called 'periphery.'

The increasingly self-defeating nature of the EU/IMF interventions in Greece, and the consequent threats to other countries and to the financial system, are dealt with elsewhere in this memorandum. In terms of macroeconomic policy it must be remembered that little or nothing is being done to correct a major source of the imbalances behind the crisis – the export pressure from the stronger economies and from Germany in particular. The Commission itself forecasts that Germany's vast current account surplus in 2011 (4.7% of GDP or €123 billion) will be unchanged in 2012 (4.6% of GDP or €124 billion) while real wages in Germany, in spite of forecast growth of 1% in 2012, will remain below their level in 2000. In these circumstances, balanced recovery in the weaker economies is impossible.

Revisions to the Stability Pact

The rules of the Growth and Stability Pact, supposed to govern the budgetary policies of all EU members and to be obligatory for members of the eurozone, were based on the fallacious notion that, provided public sector deficits were limited, market forces would ensure a balanced development of the economy. In reality, the limited growth achieved over the last decade (the years of the Lisbon strategy) depended on widening imbalances: in 2007, just prior to the outbreak of the financial crisis, Germany posted a current account surplus equal to 7.6% of GDP; the counterpart of this surplus, generated by irresponsible macroeconomic policies in Germany together with a veritable assault on lower-paid German workers, were huge deficits, of over 10%, in such countries as Cyprus, Greece, Portugal and Spain. Far from bringing about balanced development, market forces had permitted an unsustainable loss of competitiveness across the periphery (Ireland's current account deficit, although in single figures at 5.6%, was also unsustainable – figures in Ireland are distorted by massive recorded outflows of profit, partly real, partly the reflection of transfer pricing by the multinationals.)

Until 2008, these growing imbalances were financed by big capital inflows into the countries affected. In Spain and Ireland these were flows into the private sector, especially the commercial banks; in Portugal, and especially Greece where there are serious problems in raising tax revenue, the inflows were mainly absorbed by the public sector. The financial climate, encouraged by the deregulatory stance of the European Commission, the ECB and most national governments, was one of excessive confidence leading to speculation and increasing fragility in the banking system. It should be remembered, however, that without these capital flows the employment performance of the eurozone would have been even worse.

The financial crisis of 2008, which provoked a rapid decline in private sector expenditures, necessitated substantial public sector injections around the world. The Commission had to recognise that much wider public sector deficits were needed temporarily, but by late 2009 it was already demanding an early 'exit' from these more supportive budgetary policies. At the same time it made proposals to make the Stability Pact rules on public sector borrowing and debt much more restrictive and to introduce new rules on macroeconomic 'imbalances.'

The official rationale for these changes is couched in terms of both 'co-ordination' and 'surveillance.' But they do nothing to promote co-ordination. Genuine co-ordination would require firstly the specification of an overall macro policy for the eurozone and then the specification of differentiated national policies compatible with the overall macro stance. There is nothing of this in the proposed amendments. In reality, the primary focus of these measures is on the surveillance of individual member states and, although this is not stated, the concern is only with the weaker member states to whose 'indiscipline' the current crisis is attributed. Thus the whole package neglects the central problem of coordination – the huge imbalances in current accounts.

The legislative package must be seen in the context of a comprehensive attempt to strengthen 'economic governance' in the EU. This term, however, no longer has the same meaning as when it was first used by the European labour movement or even by Jacques Delors who were arguing for the assertion of social control over the European economy. It now signifies reinforced efforts to weaken social controls over labour markets, to reduce expenditure on public services and welfare benefits and to bring errant member states into line with these objectives. Other aspects of the drive for the new 'economic governance' include:

- the *Europe 2020 Strategy*, successor to the Lisbon Strategy, focused on further 'structural reforms' and expressed in the 'integrated policy guidelines';
- the 'EuroPlus Pact', agreed in March 2011, in which the eurozone countries and six others commit themselves to pursue competitiveness, employment, sustainability of public finances and financial stability;
- The Pact will be translated into National Reform and Stability Programmes with implementation monitored by the Commission.

'Economic governance' in all its forms emphasises labour market reforms, including: the review of wage-setting arrangements; decentralisation of wage bargaining; review of indexation mechanisms; subjection of public-sector wages to the needs of competitiveness; reform of employment contracts to promote 'flexicurity'. Other key themes are: raising the pension age; adapting the regulatory framework to the needs of small and medium enterprises; and promoting a business-friendly environment.

The reform of the Growth and Stability Pact consists of six pieces of legislation, which have now passed through the European Parliament with very few changes. The first four tighten the requirements of the existing stability pact and its enforcement through the so-called 'excessive deficit procedure.' The other two introduce an 'excessive imbalance procedure' which introduces similar legal constraints on other aspects of macroeconomic policy; they are obviously inspired by the fact that in Ireland and Spain crisis had nothing to do with public sector deficits but relates to capital inflows into the private sector. The main features of this legislation include the following:

Tightening the Stability Pact:

1. **New definitions** of the stability pact rules emphasise 'excessive' levels of public debt as well as well as annual deficits; 'discretionary' measures have to be taken to correct both and the speed of correction is specified. The only permitted exceptions have a strongly deregulatory character – a member state may run deficits to introduce a funded pension scheme, but not, for example, to finance a social housing programme.[23]
2. **Stronger surveillance** is to take place through the annual submission of stability programmes (including 'structural reforms') which must embody a medium-term budgetary objective to permit the Council to verify 'prudent' fiscal policies. Even countries within the prescribed reference values must not increase public expenditure faster than GDP (thus any move by other countries towards Scandinavian social models becomes illegal).[24]
3. **Reinforced penalties** involve first compulsory deposits and then fines for eurozone members. Sanctions are to become more automatic since at many stages of the 'excessive deficit procedure' a qualified majority in the Council will be needed to block penalties rather than to impose them.[25]
4. Member states must establish a satisfactory **Budgetary Framework**. This covers accounting systems, statistics, fiscal relations with regional and local government, forecasting practices (although the Commission's own forecasting is less than impressive), budgetary procedures and 'fiscal rules.' It is strongly recommended that the latter involve numerical limits, in spite of the repeated difficulties that such rules provoke, most recently with public finance in the US today (and no doubt Germany in the near future).[26]

The Excessive Imbalance Procedure:

5. A **scoreboard** comprising 'a limited number of economic and financial indicators' is to be established. 'Indicative' thresholds will be set for these; if they are crossed investigative procedures may be launched; however there will not be an automatic alert; 'economic judgement should ensure that all pieces of information, whether from the scoreboard or not, are put in perspective and become part of a comprehensive analysis'; this will identify member states to be subject to an 'in-depth' review; this will involve 'enhanced surveillance missions' and additional reporting by the member state concerned.[27]
6. **Penalties** do not follow right away. When excessive imbalances are definitely identified, 'recommendations' will be made to the member state. Its response should be timely; should use 'all available policy instruments' including fiscal and wage policies, labour markets, product and services markets and financial sector regulation. Eventually, however, if the response proves inadequate, sanctions – compulsory deposits and fines – will

---

[23] Amendment of Regulation (EC) No 1466/97 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies.

[24] Amendment of Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure.

[25] Regulation on the effective enforcement of budgetary surveillance in the euro area.

[26] Directive on requirements for budgetary frameworks of the member states.

[27] Regulation on the prevention and correction of macroeconomic imbalances.

be imposed. Equity in penalties is to be assured by expressing these as a percentage of the GDP of the recalcitrant state.[28]

There is, of course, something absurd about this attempt to construct a juridical framework for macroeconomics, as anyone remotely familiar with that discipline will recognise. But the project is also sinister: it threatens to subject economically weaker members – and those alone – to a comprehensive tutelage involving every aspect of public policy. It is clear that the main indicators used will reflect a view of 'competitiveness' which makes it a problem only for the less competitive, not for the more competitive, economies. Criticism in the European Parliament and by some EU governments has led to the removal of explicit reference to wages in the legislation. But the wage levels and social models of the weaker states remain the targets of this project.

Many types of 'imbalance' will be outside the scope of the new procedures. These include: the coexistence of immense private fortunes with public sectors crippled by debt; the failure of wage growth in the EU to match productivity growth over now three decades; the remuneration of financial and corporate leaderships out of all proportion to typical incomes.

The package is embedded in a reinforced set of administrative procedures known as the 'European semester' which will take place in the first half of each year and lead to the definition of two sets of policies, one concerned with macroeconomic policy (the 'stability programmes') and the other (the 'national reform programmes') concerned with 'structural reforms' in the Commission's usual sense of reduced protection for employees, privatisation and the deregulation of business. The first such exercise, which took place in 2011, indicates what is to be expected from these procedures: neither the Commission's recommendations for Germany nor Germany's own programmes recognised any problem with the country's huge trade surplus. The entire process focuses on further fiscal consolidation, labour market 'reforms', and supply-side measures supposedly to promote growth by 'large price and cost adjustments' in the weaker economies – in other words, by deflation.

The consequences of this stance are as would be anticipated by anyone sceptical about the notion of growth-promoting deflation. By September the Commission was compelled to revise downwards its already low predictions for growth in 2011 and 2012. It declared that 'the downward revisions concern all the member states under review, suggesting both a common factor and a re-coupling of growth dynamics.'

One 'common factor' is of course the constant pressure for restrictive policies coming from the Commission and from political leaders in most member states. Another is the looming financial crisis stemming from repeated failures to resolve the crisis in Greece. The rediscovery of 're-coupled dynamics' points to genuine coordination problems neglected by those same leaderships who have preferred to attempt a virtually colonial subordination of the weakest member countries.

2.2 Financial sector reform stymied by extensive lobbying

The deepening of the euro area crisis has led to a crisis for European banks, raising a challenge for the entire European financial architecture. As private financial institutions have sought to profit from massive speculation, politicians have struggled to get on top of the

[28] Regulation on enforcement measures to correct excessive macroeconomic imbalances in the euro area.

immediate effects of the debt and banking crisis, while completely failing to implement the major structural reforms that are needed to control the financial system. Following massive lobbying by the financial sector, reforms have been blocked, watered down or, as in the case of changes to the Market in Financial Instruments Directive (MiFID), postponed. Even when urgent short-term action has been necessary, EU states have been unable to agree, as in August 2011 when some governments refused to participate in a ban on short selling.

In the course of the 2010, attempts to reform the EU financial system were launched for the derivatives market and big banks. In both cases, the EU proposals were even weaker than those that have been introduced in the US.

Derivatives market

In July 2011 the European Parliament voted on a draft legal text for the European Market Infrastructure Regulation (EMIR). EMIR will deal with some of the problems in the derivatives market, in particular over-the-counter (OTC) derivatives, but fails to fundamentally call a halt to this 'financial casino'. EMIR attempts to deal with a major problem that arose before and during the financial crisis in 2007-2008, namely that nobody knew who was trading what kind of risky financial products with whom. This lack of transparency was especially the case for OTC derivatives that were traded in private deals ('over the counter') and not on public exchanges. The main elements of EMIR are that most OTC derivatives should be reported to the authorities to improve transparency, and that more financial speculation should be insured against default. The financial lobby mounted a highly successful campaign to water down the legislation because the OTC derivatives business is an important source of income for big (investment) banks and institutional investors, and related to high bonuses.

The EMIR text has major loopholes. For instance, pension funds can be exempted from clearing their OTC hedging derivatives trade for 3 years or more; similarly, 'non-financial counterparties' do not have an obligation to clear the hedging activities related to their commercial activity. Furthermore, no limits are being imposed on the overall amount of OTC derivatives that may be traded. There is an urgent need to reduce sharply the size of OTC transactions, since most are purely speculative. This is very striking in the case of credit default swaps, which are playing a key role in the euro crisis, since the buyer very often does not hold the bond which is being insured. However, following pressure from the financial lobby, the new regulations fail to establish such limits.

Bank reforms

The lack of major bank reforms in the EU has left banks vulnerable to shocks from the sovereign debt crisis, the euro crisis and stock market volatility. In July 2011, the Commission presented its proposals for a major bank reform. This bank reform, known as the 4th review of the Capital Requirement Directive (CRD IV), should improve banks' capital buffers, bank governance and supervision. The EU Parliament started the discussion of CRD IV in September 2011 and it is supposed to move to a plenary vote in June or July 2012. The CRD IV consists of a set of two different EU laws. The first law deals with the regulation on stricter capital reserves, incorporating the new Basel III standards into EU law. The second piece of legislation is a Directive to improve the supervision and governance of banks and investment firms, especially regarding risk assessment.

The banking sector has again lobbied heavily to reduce the scope of the legislation, arguing that the additional capital requirements will reduce its competitiveness, and will result in banks reducing the supply of credit, especially to small and medium enterprises (SMEs). Supervisors, academics and regulators, including the Commission, have been showing through different impact assessments that these claims are unfounded, and that these problems can be avoided by changing banking business models. Furthermore, many doubts remain as to whether this new EU legislation – which it is not planned to implement fully until 2019! – comprises the appropriate measures to deal with the problematic behaviour and instability of the European banks. The Commission's bank reform proposals can be considered to be far from sufficient not only because the use of capital buffers as a major instrument of banking regulation is problematic, or because the introduction of a leverage ratio and liquidity requirements is being delayed, but also because the Commission's proposals have major weaknesses. The proposals:

- Do not separate retail/commercial banking from investment banking, nor limit their linkages with financial markets since banks can still engage in derivatives trading;
- Fail to limit the size of the total balance-sheet and off-balance-sheet of banks; thus banks and financial conglomerates can still be too big to fail;
- Do not prohibit banks from speculating with their own capital ('proprietary trading' which is forbidden by the 'Volker rule' in the US Dodd-Frank Act of July 2010);
- Do not reform the use by banks of their own risk assessment models, which are frequently based on erroneous assumptions (Greek bonds have a 0% risk!).

The Financial Transactions Tax directive: a breakthrough but not quite a victory

The European Commission presented a draft directive for the implementation of a Financial Transaction Tax (FTT) in September 2011. This is a significant breakthrough for a proposal that has been advocated for many years by civil society, in particular Attac, and which has more recently also gained the support of the French and German governments. The Commission's draft directive has taken up many of the elements that campaigners have sought, including the taxation of over-the-counter (OTC) derivatives, the residence principle to prevent tax avoidance and, above all, the intention not only to generate revenues but also to have a regulatory impact on speculation, in particular on high frequency trades. Nevertheless, the proposal also contains significant limits. Two major criticisms stand out. First, the proposed FTT directive does not primarily aim at fighting speculation and reducing the volume of financial transactions. This can be seen in the tax base, as the Commission proposes to exclude currency trades. The tax rates for derivatives are also much too low. The second limit is that the directive is disturbingly vague on the issue of how the tax revenues should be used. A key feature of the campaign by civil society was that a significant share of the revenues should be deployed in the realms of development and the environment, but neither of these is mentioned in the Commission's proposal. Finally, the marked reluctance of Britain, Sweden and the Netherlands to introduce a FTT could yet prove to be a serious obstacle to its implementation.

2.3 Austerity: The wrong policy for the ills of the EU

Austerity is being pursued by the EU governments, as a general cure-all recipe. Thousands are demonstrating in the streets of an increasing number of European cities protesting against austerity because it is radically reducing their living standards and offering no hope for the future. UNCTAD's *Trade and Development Report 2011* is also highly critical of fiscal tightening and the IMF's policy recommendations, pointing out that fiscal space is not a static variable. In addition, the rush by a number of European countries to pay back high levels of private debt in the crisis will further dampens demand if it is not compensated by increased public sector debt.

In the words of the UNCTAD report, 'from a dynamic macroeconomic perspective, an appropriate expansionary fiscal policy can boost demand when private demand has been paralysed due to uncertainty about future income prospects and an unwillingness or inability on the part of private consumers and investors to incur debt. In such a situation, a restrictive fiscal policy aimed at budget consolidation or reducing the public debt is unlikely to succeed, because a national economy does not function in the same way as an individual firm or household'.[29] This is what is known as the 'fallacy of composition', i.e. believing that what is good for the individual members of a group is by definition good for the group as a whole.

Perhaps more fundamentally, the present crisis has laid bare the divergence of the productive structures in the European Union and the eurozone. The EU is characterised by a division between an export-orientated, neo-mercantilist core, which is grouped around Germany (and includes Benelux, Austria, Czech Republic, Slovakia, Slovenia, Northern Italy, and, to some extent, Poland and Hungary) and an import-dependent European periphery, for whom integration into the EU has led to a partial deindustrialisation (Greece, Spain, Portugal). Further, in some East European countries (especially the Baltic states, Bulgaria and even East-Germany), severe deindustrialisation resulted from the transformation policies, which were not reversed after accession to the EU.

EU regional policies have focused on physical infrastructure development and general-purpose training. But no attention has been given to the key issue of industrial structures. The neo-mercantilist core countries around Germany have had no interest in promoting such policies and the design of EU policies has tended to cement the existing European division of labour. This division of labour has translated into a divide between creditor and debtor countries, whereby import-dependent countries financed their current account deficit by incurring external debt, while the banks in the neo-mercantilist countries facilitated exports to the European periphery by providing such loans. This division of labour is no longer sustainable. Austerity policies not only fail to address such fundamental problems of European integration, they actually exacerbate them further.

Austerity not only fails to attain its economic objectives; it has also had a highly negative social impact. Section 1.2 above, examined the steep declines in output in the EU countries implementing EU/IMF programmes; in this section, we examine the wider social implications of austerity policies for the EU.

The economic crisis is having a heavy toll on society, in terms of declining employment, increasing unemployment, part-time and temporary employment, as well as rising inequality and poverty. In the second quarter of 2011, the EU employment rate for 20-64 year-olds fell to 68.9% from 70.5% at the beginning of the crisis in the second quarter of 2008, diverging further form the *Europe 2020* target of 75%. The employment rate was equal to 75.3% for men and 62.6% for women. Part-time employment increased by 1.3 percentage points, to reach 19.6% (9.1% for men and 32.1% for women), while the share of temporary employ-

[29] UNCTAD, Trade and Development Report, 2011, pp. VI-VII

ment amounted to 14.2% (13.7% for men and 14.8% for women), indicating that employment is becoming ever more precarious.

At the same time, unemployment rose sharply at the onset of the crisis and, after declining very slightly, rose again in 2011. By September 2011, unemployment averaged 10.2% of the labour force in the eurozone (9.9% for men and 10.6% for women) and at 9.7% in the EUY as a whole (9.5% for men, 9.9% women). Especially hit were young people, migrants, the low-skilled and women. In particular, youth unemployment (those under 25) reached 21%, while young people have been especially affected by part-time, including involuntary, and temporary work. In addition, 20% of migrant workers are unemployed, as are 15% of the low-skilled wishing to work. Furthermore, long term unemployment (more than 12 months) accounted for 43% of the total[30].

There are also strong divergences amongst countries, with the highest unemployment rates recorded in Spain (23%) and Greece (18%) and the lowest in Austria (3.9%) and the Netherlands (4.5%). In these circumstances, the EU objective of providing incentives for the unemployed to find work – one of the strands of austerity policy identified in section 1.2 above - appears ironical, to say the least. In 2010, for example, there were 7 times more unemployed people than there were job vacancies in the EU as a whole, 16 more in Greece, 21 more in Spain, 27 more in Portugal, 39 more in Ireland, and 76 times more in Latvia.

The high and increasing unemployment rates in the EU make for social distress, as the number of jobless households and of households with relatively few people in employment ('low work intensity households') is increasing. In 2010 less than one-half of those aged 25-64 lived in households in which either all members or most members had a job (35% and 13% respectively). In these conditions, unemployment leads to widening inequalities amongst and within countries.

In 2009, nine EU countries (Bulgaria, Romania, Latvia, Poland, Estonia, Hungary, Lithuania, Slovakia and the Czech Republic) which accounted for one fifth of the EU population recorded real household income per capita equal to 45% of the EU average. Further, the fifteen countries of the EU which are eligible under the Cohesion Fund (the above nine together with Slovenia, Portugal, Malta, Greece, Cyprus and Spain) together accounted for one third of the EU population and had a real household income per capita equal to 72% of the EU average.

In 2008 the total disposable income of the 20% of the population with the highest income in their country of residence was about 5 times higher than the income of the 20% with the lowest income. The ratio of the income of the top 20% of earners to the bottom 20% was even more pronounced in certain countries, including Greece (5.8), Bulgraria (5.9), Spain and Portugal (6.0), Lithuania (6.3), Romania (6.7) and Latvia (7.3).[31]

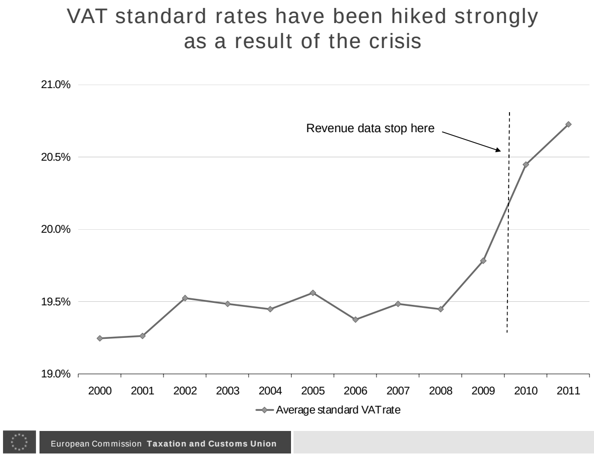
By contrast, in Europe there are 3.1 million individuals considered as 'high net worth individuals' (HNWI), which is defined as owning investible assets of at leat US$1 million. They account for 0.6% of the EU's population, which stands at 502.5 million. In 2010, their wealth

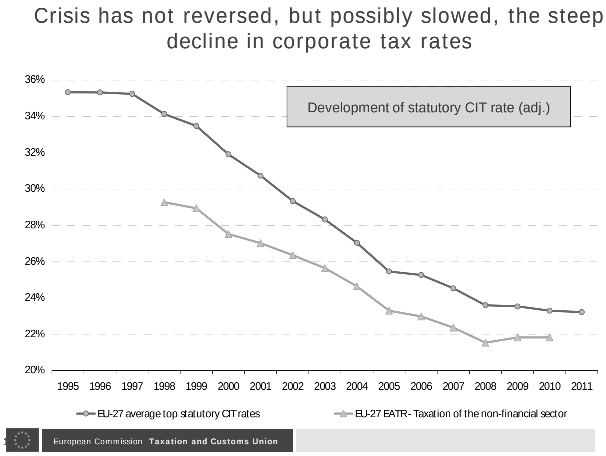
30 Eurostat 160/2011 and Eurostat database, accessed 5/11/11. The unemployment data are seasonally adjusted.

31 Eurostat 16/2011.

totalled US$ 10.2 trillion, which is equal to 24% of the global wealth of HNWIs, while it grew by 7.2% in relation to 2009.[32]

Wealth and income inequalities are however outside the scope of austerity policies which, in reality, tend to exacerbate inequalities. It is argued, for example that indirect, rather than direct taxation, should be raised to deal with the public deficit while, at the same time, it is argued that corporate taxes should be reduced in the name of a more business-friendly environment. This is clearly regressive and there has been a tendency to shift the burden of taxation in the European Union to lower-income wage earners.





Source: M. Fantini, M., 2011, 2011 Edition of the Taxation Trends Report, EC, DG TAXUD

The austerity measures embodied in EU economic and social policy prescriptions and applied by EU/IMF programmes are economically ineffective in producing growth and socially dangerous, impoverishing European societies and leading to greater social polarisation. In accentuating social tensions, already under stress due to the crisis, austerity policies lay the ground for political tensions, if not instability, as right-wing populism grows stronger.

2.4 Enlargement and neighbourhood policies lack a political vision

In 2011, the strategic pillars of the EU Mediterranean policies were called into question. The economic crisis aggravated existing structural problems of the North African countries. Tunisia and Egypt, the two pillars of the EU Mediterranean policy, were the first two countries, which experienced revolutionary processes. These processes were directed not only against the authoritarian regimes, but also against their prevailing economic policies, which had produced high unemployment and social polarisation. They therefore raised a challenge for EU Mediterranean policies in at least two important respects: the collaborative relationship between the EU and the authoritarian regimes and the type of economic order that had been promoted by the EU. In spite of the official pro-democratisation discourse of the European Union, EU officials were visibly disconcerted by the democratisation movement in the Arab world and the removal from power of Ben Ali in Tunesia and Mubarak in Egypt, the EU’s two main allies in the region. Both the EU and member states’ governments were very slow to react to the events. While the initiatives promoting democratisation were finally welcomed, there has been no change to the EU’s economic approach to the region, which continues to be based on neo-liberal principles, in particular free trade. In Libya, EU countries, in particular France and Britain, intervened militarily in the simmering civil war, clearly

32 2011 World Wealth Report, http://www.capgemini.com/insights-and-resources/by-publication/world-wealth-report-2011/?d=BCD137B0-8001-3261-87C2-98873EFF1DF0

acting beyond the bounds of the relevant UN Security Council resolution. There remain nevertheless serious doubts as to whether military interventionism will be conducive to democratisation in the region.

EU enlargement and neighbourhood policies in Europe have also been mired in contradictions and ambiguities. EU enlargement policies are mainly aimed at preparing the ground for the expansion of West European business and making the candidate countries adopt EU norms. Among the candidate countries, Turkey has the longest contractual relationship with the EU. At the same time, it is the most controversial of the candidate countries. EU accession negotiations are continuing with Turkey but they are of a rather token nature. Both sides tacitly behave as though these negotiations will lead nowhere.

In most of former Yugoslavia, where the EU is hoping that the promise of EU integration will contribute to political stability, there are indications of a similar trend to Turkey. While Slovenia joined the EU in 2004 and negotiations with Croatia were concluded in 2011, the prospects of joining the EU are in jeopardy for the other countries of the region. In many EU member states there is an evident hesitation about a further enlargement of the Union and the remaining candidate countries face numerous obstacles, partly resulting from contradictory EU policies. Although the Former Yugoslav Republic of Macedonia (FYRM) signed a Stabilisation and Association Agreement in April 2001, even before Croatia received the official status of a candidate country in 2005, negotiations on FYRM membership of the EU have not commenced because Greece objects to the name of Macedonia. The question of Serbia's EU membership is severely charged by the question of the status of Kosovo. In the 1990s the EU declared that it would only recognise the independence of former Yugoslav republics, but several EU member states supported Kosovo's secession from Serbia, even though Kosovo did not have the status of a republic in Yugoslavia. In all, 22 EU member states have recognised Kosovo's unilateral declaration of independence, while only five EU member states have, like most UN members, not done so. In spite of the divided opinion in the EU, the European Commission is pressuring the Serbian government to take steps towards the recognition of Kosovo. In October 2011, the European Commission announced that it was in favour of granting Serbia and Montenegro candidate status but, in the case of Serbia, it made the beginning of negotiations dependent on improved relations between Serbia and Kosovo. By contrast, the de-facto partition of Cyprus was not resolved before Cypriot EU membership and conflicts about Northern Cyprus are one of the points of contention in EU negotiations with Turkey.

The Eastern Partnership initiative, which was launched in 2008 and supported especially by Poland, is aimed at opening up countries in the post-Soviet region to West European capital and at persuading them to adopt EU norms in key policy fields. For those countries of the EU, which have very cool (or even tense) relations with Russia, the Eastern Partnership is conceived as a means of reducing Russian influence in the region. Eastern Partnership policies are likewise faced with contradictions and conflicts. Ukraine and Belarus belong to the key countries of the initiative. The political relationship between the EU and the governments of the two countries are fraught with tensions. The EU wants to bind the two countries – like the other countries of the Eastern Neighbourhood – closer to the EU. For Poland and the Baltic states, it is a strategic foreign policy aim to reduce the two countries' dependence on Russia. However, there are strong reservations about the governments in Belarus and Ukraine because of their authoritarian tendencies, especially in the case of Belarus. The governments in Belarus and Ukraine follow a 'multi-vectoral' external policy between the EU and Russia. They try to exploit the competition between the EU and Russia to their own advantage. Ukrainian heavy industry, which is backing the present Ukrainian government, has economic interests in the EU and wants better access to EU markets. This constellation has resulted in ups and downs in the EU-Belarus and EU-Ukraine relationships. Since a wave of repression after the last elections in Belarus, the relationship has become tense. Similarly, after the former Ukrainian Prime Minister Julia Tymošenko was sentenced to seven years in prison in October 2011, in what Catherine Ashton, the EU Commissioner for Foreign Affairs, described as an act of 'politically motivated prosecution', it is doubtful whether the association agreement with Ukraine, the core of which consists of a free trade agreement, will be signed. For geo-political reasons, however, some of the East European governments seem to be willing to sign the agreement.

In the EU, attitudes towards the Eastern Partnership initiative are to a significant extent conditioned by attitudes towards Russia. The views on this issue are highly divergent, ranging from the desire for a strategic partnership in German governing circles to fundamental reservations in the Baltic States.

Box 1: EU migration policy and the economic crisis

Before the accession of Eastern European countries and the deepening of the financial crisis in 2008, migration policy at EU level was governed mainly by labour market considerations as part of the single market project which culminated in the right of free movement for EU nationals and the Schengen treaty, which removed border controls between the participating countries. However, matters related to third-country nationals have always been treated at national level and governed by the national laws of EU member states. Migrant workers were not granted a legal status, but demand for them as cheap labourers in the agricultural and service sectors was high and wage dumping and miserable working conditions were widespread among the migrant workforce.

The uprisings in the North African countries of Tunisia, Libya and Egypt brought South-North migration sharply into focus. For decades North Africans have been seeking a better life and supplying labour to the Southern European countries which suffered from a shortage of labour, especially seasonal workers in agriculture. The choice of destinations for the North African migrants was mainly governed by former colonial relationships (between Algeria and France, Morocco and Spain, and Libya and Italy) as well as earlier patterns of migration. Migrants from sub-Saharan African countries have also been moving through North Africa to various EU countries in search of a better life.

These developments have made a mark on EU migration policies and, more importantly, on the member states' approach to migration by both EU and non-EU nationals. At EU level, the freedom of movement within the EU and the Schengen treaty were combined with what has been termed a 'Fortress Europe' policy – raising walls to stem the flow of migration from outside the EU. As part of this policy, the control of migration flows was coordinated with, and to some extent sub-contracted to, North-African countries such as Libya. Under the Gaddafi regime, cooperation on immigration was one of the conditions for Libya's re-admittance to the Western dominated international arena. The setting up of holding camps for illegal immigrants in North Africa was part of the EU's policy of externalising migration management.

The human rights implications of a tighter and 'externalised' migration policy, together with the need for migrant labour and serious problems with human trafficking and smuggling have led the EU to design a more coherent migration policy along the lines of that in the US. This is set out in the *European Pact on Migration and Asylum*, which was adopted by the EU in 2008. The core of the policy is centred on the stabilisation of migrants' status by granting long-term and single/targeted resident permits, integration and the facilitation of long-term migration through the development of a permanent residency Blue Card system (modelled on the US Green Card). As part of the new policy, legislation was also implemented for promoting seasonal migration and facilitating intra-corporate transfers. However, close examination of these initiatives by trade unions, including IG Metal of Germany and the European Trade Union Confederation, and human rights organisations, such as the European Association for the Defense of Human Rights, reveal that the measures fail to meet their objectives since they discriminate among different categories of migrants on the basis of skills, country of origin (EU or third country), and type of migration (temporary/seasonal or long term). This will result in a more fragmented European labour market in which highly-skilled EU or third-country nationals with the highest incomes will be the most privileged among the migrants.

These policies have been combined with anti-immigration measures such as the return of immigrants, cooperation with immigrants' home-country officials and tighter policing of irregular migration. A new strategic policy has also been designed in order to combine 'migration, mobility and security' that would inevitably lead to a further 'securitisation' of migration issues and a marginalisation of the humanitarian and labour-market aspects of migration. It is claimed that these policies would help legal immigrants and protect potential migrants by reducing people smuggling and trafficking. In reality, a more restrictive European immigration policy together with widespread anti-immigrant sentiment tend to reinforce each other and promotes an even more restrictive immigration policy at a national level.

These developments have clearly shifted the migration policy in the EU and in member states towards more control and have undermined the time-honoured principles of cohesion and solidarity enshrined in many of the EU declarations.

The EU is in urgent need of an immigration policy that combines its demand for labour with the social, human and economic rights of immigrants. Discrimination at the workplace, in particular, needs to be ended. Once migration is separated from security issues of crime and terrorism, it will become easier to deal with labour market aspects of migration and create a migrant friendly culture where strict migration rules (like those in the US) could be combined with respect for migrants once they are in the country. On humanitarian grounds any restriction on the access of immigrants, irrespective of their legal status, to basic public services such as health and education should be removed. In the medium to long run attempts should be made to move towards a common immigration policy across the EU based on international justice, solidarity and integration of immigrants, that draws on best practices of the EU national policies on admissions, naturalisation, family reunion and labour market related issues.

2.5 Trade and development policies: Waving the stick and not the carrot

The global financial and economic crisis has been accompanied by a shift in the balance of power in the global economy. This can be clearly seen in the new geopolitical agendas of China in Africa and, to a lesser extent, in South America. The so-called new donors pursue an explicit agenda of access to raw-materials in exchange for quite generous funding for infrastructure and other projects. In contrast to traditional OECD donors, China does not attach strings in the form of political conditionalities to its aid payments. As a consequence, both the EU and the US see their influence in Africa declining. The EU has reacted to this by stepping up pressure on aid recipients to accept unrestricted market opening for EU goods and investments. The Commission's document, *Trade, Growth and World Affairs*, presented in November 2010, is the sequel to its paper *Global Europe,* which appeared in 2006. In the new trade strategy, the EU Commission makes it clear that it intends to pursue an aggressive agenda to open up markets and secure access to raw materials in the interest of EU businesses. Although the document pays lip service to concluding negotiations of the so-called Doha Round at the multilateral World Trade Organisation (WTO), the focus of trade policy has shifted decisively towards negotiating bilateral free-trade agreements with major trading partners.

The EU's negotiations with the African, Caribbean and Pacific group of states (ACP) to conclude Economic Partnership Agreements (EPAs) have made little progress and the Commission has taken steps that will increase the pressure on the African countries to sign such agreements. The Commission has announced that it will phase out a special market access regulation for ACP countries by the end of 2013, and it is also implementing a parallel reform of the EU-Generalized System of Preferences (GSP). Via the GSP-system, less-developed countries are granted unilateral preferential tariff treatment by the EU. Since most of the African ACP countries have received GSP treatment, the incentives for them to enter into EPAs, which would demand from them wide-ranging liberalisation commitments on trade and investment, have been limited. So far, 23 countries in Africa, including Zambia, Nigeria and Senegal, have refused to sign EPAs. The EU is now using the GSP reform as an additional bargaining chip to press African countries into signing EPAs. Before losing market access to the EU under beneficial terms, some vulnerable African countries eventually will have no other choice but to accept such a deal with the EU. However, the geopolitical and economic situation has changed in recent years and stronger African countries, which have profited from increasing commodity prices or privileged relations with China, might simply walk away from the negotiations.

EU trade and development policies with the EUROMED countries have, similarly, also focussed on a one-sided liberalisation agenda over the last 10 years. Negotiations on the liberalisation of investment and services with Morocco, Egypt, Tunisia and Israel have been ongoing since 2008. The revolutionary events during 2011 in Egypt, Tunisia and other countries of the region were, at least in part, motivated by widespread rejection of the prevailing economic model, and this is a clear indication that the EU's trade and development policies must be seriously reconsidered.

2.6 Inadequate and insufficient action: the example of the Common Agricultural Policy

There is a serious mismatch between the declared aims of the EU, and the policies which it actually pursues. Somewhere in the mass of documents published by the EU it is possible to find a reference to a wide range of aims. Some of these are problematic, but others are desirable and the case for them is well argued, even if they are sometimes embedded in problematic overall strategies. A central destructive feature of the EU's prevailing strategies is their over-arching orientation towards promoting competitiveness. This is not only destructive for the potentially positive role of Europe in the world; it also perverts the workings of policies within the EU. Instead of a structure of opaque instruments, which are often supposed to act indirectly through market mechanisms, a set of a set of direct, explicit and transparent policies should be developed at the EU level, taking the imperatives of sustainable development as its explicit and binding basis.

In the global arena, the EU is almost as conspicuous as the US in anticipating a military dimension to its energy and raw materials strategy. The military concept of 'security' has been appropriated, wrongly, to designate an illusory way out of the dependency on the world market for certain raw materials and energy sources. The EU strategy of sustainable development, which doesn't even address major areas of concern, such as external trade, monetary policy, and the common agricultural policy, is largely an example of window dressing, and completely fails to recognise the destructive impact of the integrated European economy.

The problems are, again, well illustrated by the example of the common agricultural policy (CAP). The urgent need for a thoroughgoing reform is acknowledged by (almost) everyone involved. However, the Commission's proposals for reshaping the CAP pre-empt a much needed political debate on the aims of agricultural policy, and how these should be achieved.

The Commission's new paper on agricultural policy makes an important step towards a sustainable conception of agriculture.[33] It recognises the importance of agrarian labour and, as part of its concept of greening agricultural production, it proposes the category of active farmers as central to rural development. The proposal to integrate agrarian labour into the calculation of the bonuses to be paid to producers is, finally, acknowledging agriculture as a potential source of dignified employment. However, this approach is not being pursued in a consistent manner, and it is not proposed to bind all payments under CAP rules to this kind of active social contribution. Defining active farmers as the subjects addressed by European subsidies would have the very beneficial effect of excluding the big corporations involved in the production and distribution of food from payments.

The inclusion of environmental goals as an important feature of agricultural policy should be a powerful lever for promoting the changes that are required to develop sustainability in this sector. It is, however, not sufficient to promise to bind European agricultural subsidies to the ecological and social dimensions of agrarian performance. The European Council and the European Parliament will need to supplement the Commission's proposal so as to ensure that it part of a coherent and overarching strategy of sustainable development. This should recognise the need for developing countries to achieve a sustainable model of rural development, so that they are capable of guaranteeing the right to food. This requires ending the practice of unfair competition by the EU's agrarian sector, and a redirecting of European resources to development co-operation with countries in the Global South and to achieving a sustainable regional development (and employment) in Europe.

[33] European Commission, *The Common Agricultural Policy after 2013,* 12 October 2011.

3 Strengthening democracy and social justice in Europe

3.1 Financial and fiscal alternatives

The market for euro area public debt has been destabilised by massive sales of some countries' bonds by private investors. In order to break the cycle of sales and falling prices, the ECB must act as lender of last resort. In place of the limited and reluctant intervention it has practiced to date, the ECB should announce that it will use all the recourses necessary to ensure that bond prices do not drop below a certain level. A key feature of the lender of last resort function is that, provided it is clear that the central bank stands ready to intervene on the necessary scale, it can stem a wave of panic selling.[34] At the same time, major initiatives should be launched to stem the power of the financial system and to establish the basis for a sustainable recovery.

Downsizing the financial sector

- The major expansion in the size and influence of the financial sector in the last three decades must be dramatically reversed. Financial institutions have appropriated an increasing share of national income and, following a short interlude, have resumed paying large bonuses; they have significantly failed in providing funding that will contribute to the creation of good jobs; and by creating a massive superstructure of derivatives and other complex securities, they have generated massive instability which, only three years after the financial meltdown in 2008, is again threatening the future of the European economy.
- Commercial and investment banking should be separated. Commercial banks should ensure the provision of finance to households for major items of expenditure, and to firms for investments in socially and environmentally desirable investment projects. The expansion of cooperative, municipal and other public and non-profit making commercial banks should be actively encouraged. There should be strict limits on the size of private commercial banks and there must be clear provisions so that they can fail without endangering the stability of the financial system. The regulation of commercial banks should involve direct controls on the expansion of credit, since relying on increased capital requirements reinforces banks' dependence on financial markets.
- Investment banks, together with hedge funds, private equity funds and all other so-called 'shadow banking institutions' should be tightly curtailed. They should not be permitted to operate with borrowed money, and all their activities should be open to public scrutiny.
- Most derivatives do not contribute to macroeconomic stability. They have led to a massive superstructure of instruments which generate profits for financial institutions and which, while they might appear to provide cover for specific risks, have actually led to a major increase in systemic risk. Derivatives should therefore be standardised and tightly controlled and financial investors should not be able to offload the risk of failure – as with credit default swaps – so as to contribute to a greater concentration of systemic risk.

---

[34] For a forceful statement of this see Paul de Grauwe, 'Only a more active ECB can solve the euro crisis', *CEPS Policy Brief,* No. 250, August 2011.

- All securities should be traded on approved public platforms and a financial transactions tax should be levied on all transactions. A publicly-owned European ratings agency should be established.

Towards a sustainable debt

- The existing level of public debt, in particular in Greece, cannot be repaid. Part of the debt will therefore have to be cancelled. In place of an across the board write down, which would hit all financial institutions including employees' pension funds, Debt Audits, as originally pioneered in Ecuador, should be held. Debt Audits provide an innovative means of promoting an open discussion about which parts of the public debt are legitimate and which should be written down. They can also identify which institutions, such as hedge funds that have adopted highly speculative positions in government debt instruments, should bear the brunt of debt write-downs.
- In all member states with high levels of public debt, a reduction should be achieved by a significant transfer of wealth from the very rich through levying a wealth tax.[35]
- The euro area countries should eliminate the possibility of speculating against weaker member states' bonds by issuing euro bonds. The euro area countries should be able to convert government debt into common bonds, perhaps up to a certain limit, and this would be jointly guaranteed by all countries. This would not involve a net issue of bonds, but rather a change in the form in which bonds were held. As a result of the current uncertainty, huge sums have flooded into German government bonds, driving their rate of interest below 2%, the lowest return in 60 years. A common euro bond would ensure that the benefits of low interest rates were shared by all euro area countries, thereby eliminating one of the key problems faced by several peripheral member states.

A European policy for a sustainable recovery

- The common monetary policy must be complemented by a common fiscal policy. This should be based on a European budget of at least 5% of EU GDP, and a coordination of national budgetary policies. The aim of the common fiscal policy should be to promote full employment with good work. The current policy of imposing austerity on Greece and other member states as a condition of receiving financial support is socially unjust and, by driving the countries into deeper recessions, it will make it even more difficult for those countries' governments to reduce their deficits. Austerity will also strength the deflationary pressure facing Europe as a whole. Instead, the European Financial Stability Facility, and the European Stability Mechanism which will replace it in 2013, should provide governments that have primary deficits with the financing necessary to resume growth. At the same time, those countries with strong fiscal and current account positions should strengthen their internal demand so that adjustment is not forced entirely onto deficit countries.
- A strong programme of public investments is necessary to counter the danger of a new recession. Such investments should be part of a long-term strategy to promote social

---

35 In September 2011, euro area households' net worth amounted to €39.3 trillion (ECB, *Monthly Bulletin*, p. S32). This is equal to 420% of euro area GDP, much of it presumably held by the wealthiest households. By comparison, total government debt in the euro area in 2010 was equal to 85% of GDP (p. S57).

solidarity and environmental sustainability, and should be initiated at a European level, including in particular an ambitious plan for promoting investment in those countries which are hardest hit by the crisis, and at a national level. Financing for such programmes could draw on an expanded role for the European Investment Bank, which is already empowered to issue bonds to finance its activities.[36]

- Instead of constantly pushing for cuts in spending, governments should raise the resources available for public investment by reversing the long-term reduction in the taxation of higher incomes. Large incomes (say, over €250,000 a year) should be taxed at a high marginal rate (perhaps 75%). Flat rate income tax should be abolished in those countries where it has been introduced and replaced with graduated tax rates. In addition, a minimum rate of corporate taxation should be introduced in the EU to prevent tax competition between member states.
- Constitutional amendments prohibiting governments from running deficits (so-called 'debt brakes'), first introduced in Germany, but since foisted on other countries seeking to ingratiate themselves with Berlin, are dangerously restrictive. The proposal panders to a common misconception that equates a government budget with that of a private household. It also involves treating the public sector's balance in isolation from the financial balances of the private sector and the foreign sector.[37] If private investment or consumption declines, as in the recent downturn, the state's deficit will rise. In a capitalist economy, private investment is highly volatile and macroeconomic stability requires the public sector to follow an active budgetary policy.

Wages and employment

- A common monetary and fiscal policy must be complemented by a coordinated wage policy. A central aim of this policy should be to reverse the widespread tendency in the EU (as in the US) for the share of wages in national income to decline. In each member state, wages should rise at least in line with national productivity plus an agreed target for inflation. Since productivity has generally been rising more rapidly in member states with lower levels of income, this implies that wages should begin to converge on those in the higher income states.
- To eliminate the imbalances which have accumulated in the last decade, adjustment should not be imposed solely on countries where unit wage costs have risen by more than the eurozone average. Instead a major part of the adjustment should be borne by countries in which unit wages costs have risen below the average for the eurozone. This applies in particular to Germany where unit wage costs remained virtually stagnant between the introduction of the euro in 1999 and the outbreak of the crisis in 2007, and which therefore did not even conform to the ECB's target of 2% inflation, a target which is in any case excessively restrictive. In order to offset the trade advantage which Germany gained over other euro area countries through this mercantilist strategy, wages in

---

36 See the proposals by Stuart Holland, 'Union Bonds, Eurobonds and a New Deal for Europe', July 2011. The proposals distinguish between a conversion of existing national bonds to euro bonds for stabilisation purposes, which would not involve a net issue of new bonds, and the issue of new bonds to finance investments, which would involve a net issue of new bonds.

37 It is an accounting identity that the government's balance (taxation *minus* spending) must equal the private sector's balance (investment *minus* saving) plus the foreign sector's balance (exports *minus* imports).

Germany will need to rise at a higher rate than that given by national productivity growth plus target inflation for a number of years. The wages of workers at subsidiaries of German companies located Poland, Slovakia and other central European countries should also be raised to relieve the downward pressure on the wages of workers in Germany.

- A reduction in normal working time to 30 hours a week remains a major strategic goal for a progressive economic policy. In the short term, this is a key component of a progressive strategy to ensure full employment (the possibilities here are indicated by the way that a reduction in working time helped to stabilise employment in Germany during the recent crisis). In the longer term, shorter working hours is a central feature of creating a society in which life is not dominated by waged work, of creating real free time and the conditions in which households are able to overcome the gender division of labour, particularly in relation to child care.

3.2 Alternatives to austerity urgently needed

The all-encompassing nature of EU/IMF austerity policies means that alternatives are urgently needed. In discussing alternatives, a two level approach is necessary, (i) one concentrating on the 'traditional social policy system', mainly concerned with financial transfers and certain service provisions such as social benefit payments, health care, support of pensioners etc. and (ii) a wider approach from a socio-economic perspective, addressing fundamental and structural aspects of capitalist systems today. Lastly, it is important to regard the following proposals as elements of an integrated whole.

At the centre of the changes that are needed is a strengthened and publicly accountable public sector. Past developments have clearly shown that privatisation policies have been counterproductive. Healthcare has become an exclusive, two-tier system, completely excluding certain sections of the population. For example in Ireland, 22% of the population is not covered by any kind of health insurance, public or private, and is therefore dependent on the basic emergency service.[38] Similarly, transport and communication provisions no longer fulfil their public role of adequately linking distant regions, while inadequate infrastructure often endangers the safety of the public. It is of immediate importance to re-establish the role of public services in order to secure:

- Adequate healthcare services for all, including an increasing number of persons who are falling completely out of the system and those who have only a marginal social insurance. Statutory insurance should be introduced where none exists and measures should be put in place for those who are freelancers or in precarious positions and unable to pay contributions.
- Childcare facilities of a high quality from an early age. These should also provide much needed educational services since, as is well known, the foundation for a qualified workforce is laid in the early pre-school years.
- Financial support for households in need, something which will also contribute to strengthening internal demand.

[38] CSO, Health Status and Health Service Utilisation, Quarterly National Household Survey, 31 August 2010.

The core-periphery division of labour discussed in previous sections means that regional policies need to be radically transformed. Low-wage strategies, supposedly aimed at increasing competitiveness of less-developed regions, have been proven wrong. Recovery and development must be based on promoting the deployment of modern technology and the establishment of sectors of technologically advanced production. The EU has in the past had a partly effective framework of regional funding but under the influence of the Lisbon Agenda, which assumed there would be a trickle down-effect from rich to poor regions, Structural Funds were reduced for the period 2007-2013. This must be reversed and such funds should be substantially expanded, something that will also contribute to a desirable expansion of the EU budget. The main priority for Structural Funds should be to promote advanced, productive economic sectors, rather than providing declining areas with social support.

In order to improve the trade balance of deficit member states, it is necessary to look beyond increasing exports. It is also necessary to find ways of substituting for imports, for example by expanding renewable energy sources, so as to substitute for oil imports, or recruiting qualified engineers in order to avoid the need to import complex technical services. Such a strategy takes time (it will probably take as much as 40 years in the Ruhr area and at least 30 years in Eastern Germany) and public support. But it is measures of this type, rather than austerity, which are required to create the basis for a sustainable economic recovery.

A significant contribution to combating the impact of the current social and economic crisis can also be played by social economy enterprises. There are two features that should be stressed. First, enterprises such as co-operatives should not be seen only as temporary solutions, filling gaps with the support of temporary legal, tax or other measures, with temporary relief from the pressure of the market. Instead, they should be encouraged as long-term initiatives which aim to meet a wide range of objectives, rather than aiming solely at maximising profit as in a traditional enterprise. Second, and the reason why they are able to meet various objects, is that they are, in a number of different respects, integrative organisations:

- They can integrate different entrepreneurial goals such as the provision of goods and services, social integration, and environmental maintenance;
- They can bring together different stages of production from generating raw materials to processing, manufacturing, distribution, exchange and consumption;
- They can encourage local production and consumption;
- They can define their product and service range primarily on the basis of the usefulness of products, rather than on their value as a status symbol, as is the case with 'designer labels', an important feature of a shift to a sustainable model of socio-economic development.

Such an alternative to 'profitable privatisation strategies' implies a strict reorientation in public responsibility. A proposal by the Irish Trade Union Congress puts forward a redefinition of public responsibility. Rather than reducing the role of the public sector to that of framework-setting, i.e. assuming the role of coordination, control and oversight, while leaving the implementation to private enterprise (as in public-private partnerships), there should be a major commitment to promoting the public engagement of citizens (what might be called public-citizen-partnerships).

In the area of labour-market policy, flexicurity has led to increasing employment insecurity and the privatisation of risk, as well as to a restriction of workers' rights. At stake is equally the 'privatisation of rights', not least due to the erosion of collective bargaining. In contrast to what is happening in Ireland and other peripheral area countries as a result of EU policies, the rights of trade unions should be fully re-established and enforced. It is also important to ensure that enterprises are not able to use the argument of competitive pressure from other parts of the EU to push for lower wages, or a deterioration in working conditions. The appropriate legislation should be framed in such a way that it also applies to enterprises from outside of the EU which wish to invest in one of the member states. The EU should also develop a co-ordinated policy for enforcing minimum wages in member states, and ensure that occupational health and safety regulations are strictly enforced—something that has the added advantage of reducing the costs of health care.

3.3 Supporting autonomous domestic development in partner countries

The underlying philosophy of EU enlargement and neighbourhood policy has to change. The EU's current approach based on free trade has simply cemented existing asymmetries. The aim, however, should be to reduce asymmetries and this requires that treaties and forms of cooperation be based on asymmetrical principals so as to favour the partner countries. Both accession and neighbourhood policies must be based on a recognition that existing neoliberal strategies have failed and, instead they should aim to create policy spaces that facilitate industrial development strategies.

Re-industrialisation is of particular urgency in the post-Yugoslav region. However, economic and political conditions here are not favourable for industrial development as, during the war years, a small stratum of 'tajkuni' emerged. These are dominant local business groups with very good political connections, and are mainly active in services, with a clear preference for exploiting monopoly positions. Within the EU, resistance to an inward-looking industrialisation strategy is to be expected from export-orientated businesses in the core countries and the governments of the neo-mercantilist group around Germany. Contrary to existing EU practice, membership candidates should be encouraged to retain the option of controls on capital flows in order to be able to reduce exchange rate instability and prevent currency appreciations. They should, for a time, also retain the option of devaluing their currencies since this is a policy instrument that can play an important role in protecting weak productive sectors while they are in the process of gaining strength.

The relationship with Eastern and Southern neighbours should not be built on free trade agreements, but on mutually advantageous sectoral, political and cultural co-operation. Double standards on democratisation, so evident in EU policy towards North Africa and Eastern Europe, should be discontinued. The relaxation and phasing out of the existing restrictive visa arrangements has been a demand in both Eastern and Southern neighbouring countries. This demand should be met, since it would demonstrate to the citizens of those countries that they are welcome in the EU.

The basic changes required in enlargement and neighbourhood policies can be summarised are as follows:

- To address and correct the existing asymmetries between the EU and neighbouring countries, institutional arrangements should be asymmetric, i.e. in favour of the peripheral countries. This means in particular a distinctively new approach to Association Agreements as the main contractual instrument in governing relations with these countries.

- Free-trade arrangements should be abandoned in favour of sectorally differentiated approaches. Very long transitional arrangements should be granted to candidate countries in sensitive areas.
- Peripheral countries should retain policy space that permits the strengthening of productive structures. EU financial aid to these countries should be oriented towards the promotion of their industrial development.

3.4 Taking responsibility in trade and development policies

The EU has failed to draw the appropriate lessons from the financial and economic crisis. Instead of stimulating internal demand, its policy is based on the belief that growth must come from an increased reliance on exports. As a result, it adheres stubbornly to external strategy that is primarily focused on the pursuit of mercantilist goals. EU policies refuse to take any responsibility for global macroeconomic management. Instead, the EU appears to place its hopes in emerging economies as the driving force of the global economy. This complements the prevailing approach of the EU's surplus countries like Germany, Finland, the Netherlands or Austria, which refuse to abandon their export-oriented growth strategies in favour of an expansion of internal demand. This not only threatens the very existence of the Monetary Union; it also undermines the reputation of the EU as a cooperative force in international relations.

The EU should adopt an approach which tackles prevailing asymmetries between countries by allowing for a more differentiated approach, balancing its commercial interests with the need to safeguard the policy-space of its partners, and using development policies to support democratically-guided economic development strategies. The main features of such an approach include the following:

- An expansive domestic macroeconomic policy should be adopted, thereby leading to a moderately higher absorption of imported goods and services and making a positive contribution to global demand.
- The prevailing model of WTO-Plus bilateral Free Trade Agreements should be abandoned so as to allow for a differentiated approach which takes asymmetries between countries into account and which supports autonomous policy space in partner countries. Trade distorting agricultural subsidies in the EU must be phased out. Demands for liberalisation of public services in partner countries must be dropped.
- Development policies should be reoriented, especially vis-à-vis the (North) African economies, so as to support the construction of diversified local economies. In resource rich countries, the EU should support efforts to avoid Dutch disease phenomena and should contribute to promoting industrial upgrading and economic diversification.
- The construction of state capacities in less developed countries (LDCs) should be fostered by supporting effective tax administrations, which contribute to equitable and sustainable fiscal policies.

Box 2: Taxing matters: The EU as model for Less Developed Countries?

While the relationship between less developed countries (LDCs) and the European Union has been far from unproblematic – colonial legacies, trade inequalities, dependency, chronic indebtedness etc. – the economic prosperity, political stability and extensive and intensive integration of Europe's states continue to be regarded as admirable achievements and worthy, in part, of imitation. The severity of Europe's recent economic crisis has certainly cast doubt on some of the region's economic virtues in the eyes of observers in LDCs, but Europe continues to exert very considerable influence on the course of modernisation in LDCs, both directly, through advisory programmes of material assistance, and indirectly, through the overseas operation of European enterprises. More recently, partly in conjunction with the Economic Partnership Agreements with the African, Caribbean and Pacific (ACP) countries, the EU has provided guidance in relation to 'economic governance', in particular in the field of taxation. In April 2010 the European Commission published a communication to the European Parliament, the Council and the European Economic and Social Committee entitled 'Tax and Development: Cooperating with Developing Countries on Promoting Good Governance in Tax Matters', which sought to assist in building 'effective, efficient, fair and sustainable tax systems' in less developed countries.[39]

The centrality of a well-resourced fiscal system to the success of economic and social modernisation and for reducing income inequalities is undeniable. Advanced states are all characterised by both strong revenue-raising capacities and by high ratios of overall taxation to GDP. Trade liberalisation, promoted by the EU and others within the WTO, has created serious problems for the many LDCs that had hitherto relied heavily on customs duties as a source of state revenues. The EU, along with the IMF, has proposed the introduction of value added taxes (VAT) – the (indirect) taxation of commercial goods and services – as a substitute for customs duties; indirect taxation, however, tends to compound income inequalities: it has a regressive, rather than progressive, effect, especially if basic goods are not exempted, because poorer families spend a higher proportion of their household income on consumption and are able to save less. A more effective, long-term solution, to both fiscal modernisation and to social justice, is the establishment of an efficient and fair system of progressive direct taxation, in which the rate of taxation rises in proportion to the level of income. In this area of direct taxation, the EU and its member states have arguably been very poor examples of both principle and practice. Firstly, the progressive features of EU member states' tax systems have been eroded by both a neo-liberal consensus concerning the need for reducing top marginal rates of income tax and corporation tax and an increasingly dangerous competition between EU-states for inward investment, using tax reductions as inducements. This tax competition accelerated in the wake of enlargement, during which the Commission failed to set minimum standards for either rates of income and corporation tax or fix the rules for defining the 'tax base' nationally and cross-nationally; the toleration of 'flat tax' regimes in seven out of ten Central and Eastern European countries and of significantly lower tax ratios in the transition states has weakened these countries' ability to promote economic modernisation according to national priorities and, above all, to fund effective national crisis-management programmes. All EU states, but particularly the New member states, have in consequence become increasingly reliant on regressive indirect taxation to finance their operations; this in turn has reduced the scope for counteracting the growing inequality of market incomes through state redistribution, with the result that the distribution of real net disposable income has grown significantly less equitable in most EU states.

EU practice therefore presents a very flawed model for less developed states to emulate. The failure, above all, to achieve a common and equitable approach to the taxation of business income has allowed international corporations to continue abusing individual fiscal states, endangering the reve-

39 European Commission, *Tax and Development: Cooperating with Developing Countries on Promoting Good Governance in Tax Matters*, COM (2010) 163 final, 2010.

nue streams of developing states in particular. The lack of transparency in the accounting practices of multinational companies (MNCs), in particular the widespread misuse of transfer-pricing, has denied vital revenue for those LDCs with weaker taxation authorities and lower general levels of compliance. Similarly, the use of secrecy jurisdictions ('tax havens') by both MNCs and some LDC-elites to avoid tax obligations has been identified as a fundamental threat to the development potential of poorer states. Global Financial Integrity states in its updated report, *Illicit financial flows from developing countries*, that, according to its estimates, these flows 'have increased to a range of US$1.26 trillion to US$1.44 trillion in 2008 and that, on average developing countries lost between US$725 billion and US$810 billion per year over the nine-year period 2000-2008'.[40] Christian Aid, in its 2008 report *Death and Taxes*, estimated the annual loss to developing country treasuries through 'transfer mis-pricing' at $160 billion,[41] which is considerably more than the $122 billion received by LDCs in development aid in 2008.[42] The continued toleration by the EU of tax avoidance and the channelling of between 60 and 70 percent of all global trade and investment flows through tax havens remains the greatest obstacle to establishing fiscal health in LDCs. There is an urgent need to support the efforts of the Tax Justice Network and other organisations to introduce country-by-country reporting of corporate turnover and profits as a precondition for the promotion of effective and fair tax systems in LDCs and the rest of the world.

3.5 Sustainable development and the Common Agricultural Policy

In place of the neo-mercantilist obsession with 'competitiveness' that dominates present EU policy, there is a need for forms of regulation which ensure that economic, social, ecological and political goals are imposed on the spontaneous, unregulated working of the market. This might not be an immediate, concrete possibility given the political and institutional situation in the EU, but it is important that the policies that are adopted are not unilateralist and isolated but rather part of a comprehensive response. It is also important that the short-term responses to the immediate crisis do not undermine the longer term challenge of achieving sustainable solutions.

For Europe, such a perspective would not imply an inward-looking stance. Rather it would lead to a positive de-linking from automatic globalisation, making Europe (and specifically the EU) one partner among many others who are presently linked to globalized circuits in a more or less dependent way. The EU may find a constructive role in such a process of change by participating in the creation of a more plural economic world, in which Europe ceases to exploit historical advantages and assists other countries to achieve a democratic control of their economic development in their own specific ways.

As an active participant in the multilateral search for models of de-centralized sustainable development, Europe could overcome its Euro-centric heritage and play a significant role in a multi-polar world. If the EU, and especially the countries of the eurozone, could find appropriate ways of addressing the multi-dimensional crisis of sustainability, it could provide important support for countries and regional groups of countries in the Global South.

---

40 Dev Kar & Karly Curcio, *Illicit Financial Flows from Developing Countries: 2000-2009*, Washington, 2011, p. vii,: www.gfip.org/storage/gfip/documents/reports/IFF2010/gfi_iff_update_report-web.pdf

41 Christian Aid, *Death and Taxes. The True Toll of Tax-Dodging*, London, 2008, p. 49.

42 Jens Martens & Wolfgang Obenland, *UmSteuern. Folgen von Kapitalflucht und Steuerhinterziehung für die Länder des Südens – und was dagegen zu tun ist*, Misereor, Global Policy Forum Europe, Terre des Hommes, Aachen/Bonn/Osnabrück, 2011, p. 31.

The EU could make an important contribution to advancing strategies of sustainable development on a world-wide scale if it were able to co-ordinate its member states' initiatives before the Rio II summit in spring 2012. However, given the present set of priorities and institutional structure this is unlikely to occur. The EU could develop credible demands for Rio II by proposing trans-national green job programs, linking ecology and social concerns for example, in the ecologically central field of energy saving. It could also strengthen both its internal effectiveness and its external credibility by reshaping European structural policies – not only in the field of agriculture – so that they will serve to promote a transition towards forms of sustainable development.

The CAP could serve as a crucial field for such a transformation of the EU by achieving a sustainable compromise between the political requirements of feeding Europeans with high quality foodstuffs at moderate prices; of maintaining a stratum of active farmers who are able to sustain the delicate ecological balance in many European landscapes; and of purchasing agricultural products from the Global South at prices that are fair and which enable the countries of the South to develop sustainable patterns of production.

The CAP should be transformed into a European instrument for assuring the food sovereignty of the EU's member states, while at the same time supporting relations of fair exchange for agrarian resources and products with the 'rest of the world'. Transformed in this way, it could also provide a model for the areas of raw materials and of sustainable renewable energy sources. The CAP should at the same time develop new models for valuing and compensating the environmental and climate services of agrarian production; it could contribute decisively to the maintenance and development of traditional cultured landscapes and natural reserves as the two most prominent cornerstones of cultural and natural diversity. By defining a binding framework for agrarian production units the CAP would define the cornerstones of long-term rural development. In order to improve the EU's ability to achieve this, the CAP should be structured as one coherent pillar, with all the relevant expenditure brought together in the EU budget, and with the competence to make decisions brought together in one institution.

Contact information of the Steering Committee of the EuroMemo Group:

Wlodzimierz Dymarski, Poznan (wlodzimierz.dymarski@ue.poznan.pl) Miren Etxezarreta, Barcelona (miren.etxezarreta@uab.es); Trevor Evans, Berlin (evans@hwr-berlin.de); Marica Frangakis, Athens (frangaki@otenet.gr); John Grahl, London (j.grahl@mdx.ac.uk); Jacques Mazier, Paris (mazier@univ-paris13.fr); Mahmood Messkoub, De Hague (messkoub@iss.nl); Werner Raza, Vienna (w.raza@oefse.at); Catherine Sifakis, Grenoble (catherine.sifakis@upmf-grenoble.fr); Diana Wehlau, Bremen (euromemo@uni-bremen.de); Frieder Otto Wolf, Berlin (fow@snafu.de).

Declaration of support

I support the general direction, main arguments and alternative proposals in the

EuroMemorandum 2012

European integration at the crossroads:

Democratic deepening for stability, solidarity and social justice

______Yes ______ No

First Name, Last Name:

Institution:

Address:

Phone:

e-mail:

Signature:

I would like to be informed about the regular work of the working group and be invited to their meetings. Please add my email-address to the mailing list of the EuroMemo Group.

______Yes ______ No

I would like to support the EuroMemo Group financially with a donation. Please send me further information on how to support the EuroMemo Group financially.

______Yes ______ No

Please return this form to the EuroMemo Group by 7 December 2011

- by e-mail to euromemo@uni-bremen.de
- or by fax to: ++49-(0)69-4305-1764.

European Economists for an Alternative Economic Policy in Europe

www.euromemo.eu