

# The economists' warning: austerity and the euro

*Financial Times*, September 23, 2013

The European crisis continues to destroy jobs. By the end of 2013 there will be 19 million unemployed in the eurozone alone, over 7 million more than in 2008, an increase unprecedented since the end of World War II and one that will stretch on into 2014. The employment crisis strikes above all the peripheral member countries of the European Monetary Union, where an exceptional rise in bankruptcy is also under way, whereas Germany and the other central countries of the eurozone have instead witnessed growth on the job front. This asymmetry is one of the causes of Europe's present-day political paralysis and the embarrassing succession of summit meetings that result in measures glaringly incapable of halting the processes of divergence under way. While this sluggishness of political response may appear justified in the less severe phases of the cycle and moments of respite on the financial market, it could have the most serious consequences in the long run.

As foreseen by part of the academic community, the crisis is revealing a number of contradictions in the institutions and policies of the European Monetary Union. The European authorities have taken a series of decisions that have in actual fact, contrary to announcements, helped to worsen the recession and widen the gaps between the member countries. In June 2010, when the first signs of the eurozone crisis became apparent, [a letter signed by three hundred economists](#) pointed out the inherent dangers of austerity policies, which would further depress the demand for goods and services as well as employment and incomes, thus making the payment of debts, both public and private, still more difficult. This alarm was, however, unheeded. The European authorities preferred to adopt the fanciful doctrine of "expansive austerity", according to which budget cuts would restore the markets' confidence in the solvency of the EU countries and thus lead to a drop in interest rates and economic recovery. As the International Monetary Fund itself recognises, we know today that the policies of austerity have actually deepened the crisis, causing a collapse of incomes in excess of the most widely-held expectations. Even the champions of "expansive austerity" now acknowledge their errors, but the damage is now largely done.

The European authorities are, however, now making a new mistake. They appear to be convinced that the peripheral member countries can solve their problems by implementing "structural reforms", which will supposedly reduce costs and prices, boost competitiveness, and hence foster export-driven recovery and a reduction of foreign debt. While this view does highlight some real problems, the belief that the solution put forward can safeguard European unity is an illusion. The deflationary policies applied in Germany and elsewhere to build up trade surpluses have worked for years, together with other factors, to create huge imbalances in debt and credit between the eurozone countries. The correction of these imbalances would require concerted action on the part of all the member countries. Expecting the peripheral countries of Union to solve the problem unaided means requiring them to undergo a drop in wages and prices on such a

scale as to cause a still more accentuated collapse of incomes and violent debt deflation with the concrete risk of causing new banking crises and crippling production in entire regions of Europe.

John Maynard Keynes opposed the Treaty of Versailles in 1919 with these far-sighted words: "If we take the view that Germany must be kept impoverished and her children starved and crippled [...] If we aim deliberately at the impoverishment of Central Europe, vengeance, I dare predict, will not limp." Even though the positions are now reversed, with the peripheral countries in dire straits and Germany in a comparatively advantageous position, the current crisis presents more than one similarity with that terrible historical phase, which created the conditions for the rise of Nazism and World War II. All memory of those dreadful years appears to have been lost, however, as the German authorities and the other European governments are repeating the same mistakes as were made then. This short-sightedness is ultimately the primary reason for the waves of irrationalism currently sweeping over Europe, from the naive championing of flexible exchange rates as a cure for all ills to the more disturbing instances of ultra-nationalistic and xenophobic propaganda.

It is essential to realise that if the European authorities continue with policies of austerity and rely on structural reforms alone to restore balance, the fate of the euro will be sealed. The experience of the single currency will come to an end with repercussions on the continued existence of the European single market. In the absence of conditions for a reform of the financial system and a monetary and fiscal policy making it possible to develop a plan to revitalise public and private investment, counter the inequalities of income and between areas, and increase employment in the peripheral countries of the Union, the political decision makers will be left with nothing other than a crucial choice of alternative ways out of the euro.

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