Chapter 1: Permanent Cutbacks

It was not supposed to be like this. In the secret conclaves of the European Union, a great effort was made to push through the Fiscal Compact treaty without any say from the people of Europe. The Irish were a special problem because their constitution required a referendum. So a certain tweaking of words was required, as the German Minister for European Affairs, Michael Link, acknowledged, 'We are trying to design everything that is on the table in a way which would be okay in the eyes of the Attorney General and the Irish Constitution so that no referendum is needed.'[1]

But even the best laid plans of Europe's elite can be tripped up. The Attorney General studied the legal arguments and could find no way around it - the Irish had to be given a vote. Once again they would vote on behalf of the people of Europe, giving their verdict on a treaty negotiated by the powerful. A barely concealed irritation spread throughout the halls of power. 'The Irish Again' proclaimed *der Spiegel,* no doubt reflecting the feelings at the highest level in Berlin.[2]

The Fiscal Compact is a hastily conceived document that was agreed between a number of EU governments at a crisis meeting on 9th December, 2011 when the euro appeared on the verge of collapse. The British vetoed it and so it could not become a formal EU treaty. To get around this legal obstacle, it was drafted as an inter- governmental treaty which is designed to later become part of EU law.

The treaty derives from a faulty analysis of the euro crisis and its link to an orgy of financial speculation. The crisis had nothing to do with governments overspending and so a treaty designed to solve this problem was missing the point. The crisis actually began in the financial markets European banks entered the US sub-prime market and provided vast amounts of credit for the property bubbles in Ireland and Spain. When these collapsed, the banks were left with black holes whose scale is still not fully known. Simultaneously, they were also involved in speculation on global food prices, causing huge suffering for 100 million people who starved or

became malnourished as result of price hikes. Sixty percent of the global wheat market, for example, is controlled by finance houses which play the 'commodities futures' market for their private gain. Banks like BNP Paribas and Deutsche Bank are prime examples of institutions engaged in these activities.[3] When their gambling debts came unstuck, the money markets of Europe literally froze up. Yet the new Fiscal Compact does nothing to bring these institutions to heel.

Another source of the crisis was the imbalance at the heart of the euro itself. The Eurozone is a currency union which brings countries of very different strengths together. It deprives each member of the financial instruments – such as control of interest rates – that could be used to manage the specifics of national economies. In the midst of the Celtic Tiger boom, for example, cheap credit at very low interest rates flowed into Ireland when precisely the opposite was required.

None of these issues, however, featured in the discussions of the EU Council of Ministers when they met in December. Instead they diagnosed a different cause as the German Minister of Finance, Wolfgang Schauble explained:

> 'It's actually undisputed among economists worldwide that one of the main causes – if not the main cause- of the turbulence – not just now, but already in 2008 was excessive public debt everywhere in the world'[4]

Schäuble had it completely wrong. Major economists such as Paul Krugman dispute his explanation, claiming that Schäuble was 'just making it up, inventing a crisis that did not happen to avoid dealing with one that did happen.'[5]

There was no evidence to show that 'excessive public spending' was the main problem. Spain and Ireland had low debt levels and in some instances a budget surplus before the crisis. And, strangely, Germany, the country which made the most of sticking to the EU's Growth and Stability Pact (which limits government deficits to 3% and overall debt to 60% of GDP), was in breach of it. The countries with public debt suffered more

and those with 'excessive' public debt suffered least! Table 1 illustrates the contrasting fortunes of Ireland and Germany before the crisis to show the absurdity of Schäuble's argument .

Table 1: Government Deficit and Debt to GDP: Germany and Ireland 2003 -2007

	2003	2004	2005	2006	2007
German Government deficit	-4.0	-3.8	-3.3	-1.6	0.3
German central government debt to GDP	65%	68%	71%	69%	69%
Irish Government deficit	0.4	1.4	1.6	2.9	0.1
Irish central government debt to GDP	34%	33%	33%	29%	29%

Source: OECD-country-statistical-profiles-key-tables.

High public debt did not cause the crisis. Indeed, countries only have high levels of debt *because* of the crisis. But the facts were not allowed to stand in the way of the story the EU elite wanted to spin. European states had, apparently, spent too much and a Fiscal Compact was needed to curb their evil ways.

THE AUSTERITY PACT

The Fiscal Compact, or the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union, has three main provisions.

1. Balanced Budgets

Article 3 of the treaty states that 'the budgetary position of the general government shall be balanced or in surplus'. This is deemed to occur if the 'structural deficit' does not exceed 0.5%. The requirement for a balanced

budget must be transposed into national law, and 'preferably' put into the constitution.

Many people instinctively support the ideal of a balanced budget. When a comparison is made between a country and an individual's finances, 'balance' appears to make sense.

However, countries are not like individuals and there are times when a state needs to stimulate an economy through extra spending. Those who argue this are usually influenced by the writings of John Maynard Keynes.

Keynes was a conventional economist who believed in the economic orthodoxy of his time. But under the impact of the Wall Street Crash of 1929, he challenged the idea that markets should be left to rectify themselves and argued instead for greater state intervention.

Keynes's arguments still make considerable sense today. He suggested that capitalists tend to hold back on investment during a recession because they see the markets for their goods and services shrinking and worry that they will not make a profit.

They also believe that unemployment saps the confidence of workers and so wages will fall. If they hold off investing, they can gain from falling wages and property prices and eventually buy up machinery at a cheaper rate. The result is a dangerous cycle where less investment means fewer jobs; fewer jobs means people can buy less goods and services; and this gives capitalists have even less reason to invest. Recessions, therefore, produce a strange paradox: there is a surfeit of 'savings' – Keynes's polite word for unused capital – while the economy desperately needs investment to get a kick start.

Keynes thought that this vicious cycle could be broken through state intervention. The state was the only force in society that could start spending and so the old, orthodox ideas about 'balanced budgets' should be thrown out. Two other arguments might also be adduced to support Keynes' view.

One is that the state gets more 'bang for its bucks' if it spends during a recession. If it undertakes a major public works programme, it can buy raw materials and machinery much cheaper as it is not competing with private investors for access to these. There is also a 'multiplier effect' from state spending. A worker who receives a wage from a public works programme will spend in their local shop. This allows the shopkeeper to take on extra staff and their spending helps to create even more jobs. So for every €1 invested by the state, many more come back into the economy.

Keynes was no socialist and claimed that his theory 'was moderately conservative in its implications.'[6] He argued that once the state stopped the market destroying itself, there should be no objection to the fact that 'private self interest will determine what in particular is produced, in what proportion the factors of production will be combined to produce it, and how the value of the final product will be distributed between them.'[7] In other words, his plan was to save capitalism – not destroy it.

Keynesianism dominated mainstream economic thinking for nearly fifty years. Yet the Fiscal Compact would effectively outlaw his proposals forever. By insisting on an automatic and permanent budget balance, the state would not be able to mount substantial stimulus programmes. The result would be a victory for those who think the crash should be used to cleanse out the system fully.

They would use it to weaken severely the workers' movement and allow capitalism to resume with lower wages and welfare benefits. The cruelty involved has never concerned the 'deficit hawks'.

2. Punish indebted countries.

Article 4 of the treaty states that where general government debt exceeds 60 % of the Gross Domestic Product the excess must be reduced by one twentieth a year. In the case of Ireland or Greece, for example, they would have to slash their annual spending by 5 % until they reached this threshold.

The current austerity programmes which are conducted under the aus-

pices of the Troika would, therefore, continue for years to come.

Article 5 states that these countries would also be named under the EU's 'excessive debt procedure' and be forced to enter a 'partnership programme' with the EU. This would include 'structural reforms' which 'must be put in place and implemented to ensure an effective and durable correction'. The EU Commission would be charged with monitoring how this is implemented.

'Structural reforms' is a code word for removing social rights which are seen to 'distort' the market. A particular target is any form of state subsidy that prevents 'proper' pricing.

Recently, for example, the IMF demanded that the Irish government remove subsidies that give the elderly cheap electricity, gas and television licences, plus free travel passes and medical cards.[8] This type of 'structural reform' would be part of any partnership programme devised with the EU Commission.

3. Economic governance by experts and technocrats

The treaty gives greater powers to the unelected EU Commission and other 'technocrats' to determine the direction of economic policy.

If a country does not have a balanced budget, it must put in place 'a corrective mechanism' for automatically cutting back spending. Its actions will be directed according to 'common principles to be proposed by the European Commission'. No indications are given about what these 'common principles' are likely to be. The Irish people and the rest of the peoples of Europe are simply asked to take it on trust.

The treaty also demands that states set up 'independent bodies' that are responsible at national level for monitoring its debt-breaker rules. These are the equivalent of Fiscal Councils, which will be drawn from conventional economists who share a right wing outlook.

On top of all that, governments can be brought to the European Court of Justice because of their economic policies. One country can charge an-

other with excessive public spending and the ECB can impose a fine of 0.1% of its Gross Domestic Product.

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1 ‘EU treaty Designed to avoid vote – German Minister’ *Irish Times*, February 22, 2012

2 ‘Schon wieder die Iren!’ *Der Spiegel* On Line 28 February 2012

3 Friends of the Earth, *Farming Money* London, FoE 2012

4 Quoted in Corporate European Observatory, *Austerity Forever*, Brussels, CEO, 2011

5 ‘Fiscalization Watch’, *New York Times* 25 August 2011.

6 Minsky, Hyman, ‘Keynesian Socialism’ 1986, *Hyman P. Minsky Archive.* Paper 16. http://digitalcommons.bard.edu/hm_archive/1.

7 ibid

8 ‘Pensions, Free Travel, Medical Cards on IMF Hit List’ *Irish Independent*, 2 March 2012.