The (so-called) crisis of the Euro

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The role of crises within capitalism

- Destroy excess capital; forcibly adjust credit magnitudes back into line with production
- Impose restructuring on firms, branches and international position of national economies
- Strengthen subordination of working class: relatively limited in recent crisis until so-called crisis of the euro in May 2010

Key phases of crisis in Euro area

Financial crisis

- broke August 2007, deepened September 2008
- Europe banks made big losses due to large-scale investments in toxic US securities
- financial collapse prevented by state injections of capital & loan guarantees

Economic crisis

- slump in output Q4 2008 & Q1 2009
- impact in Europe due to (a) slump in trade, and (b) collapse of credit
- depth and duration of slump cushioned by expansive (national) fiscal programmes
- large decline in tax revenue
- big increase in fiscal deficits and government debt

Sovereign debt crisis

- triggered in May 2010 by Greek difficulties in refinancing public debt
- failure of European Union to respond rapidly (German reluctance) led to speculation against euro
- Euro area governments eventually agreed to provide €110 billion funding for Greek debt; despite ECB resistance IMF involved
- Speculation against euro continued; fed by concerns about Spain and Portugal’s external liabilities (largely private)
- Euro area governments (strongly pushed by US) agreed to create $440 billion European Financial Stability Facility; complemented by €60 billion for balance of payments support from EU and €250 billion from IMF
- ECB began to purchase Greek, Spanish & Portuguese government debt (largely sterilised)

Social crisis

- major cuts in wages & public spending forced on Greece, Spain & Portugal
- cuts already introduced in Ireland
- plans for fiscal contraction announced in other countries

Policy issues

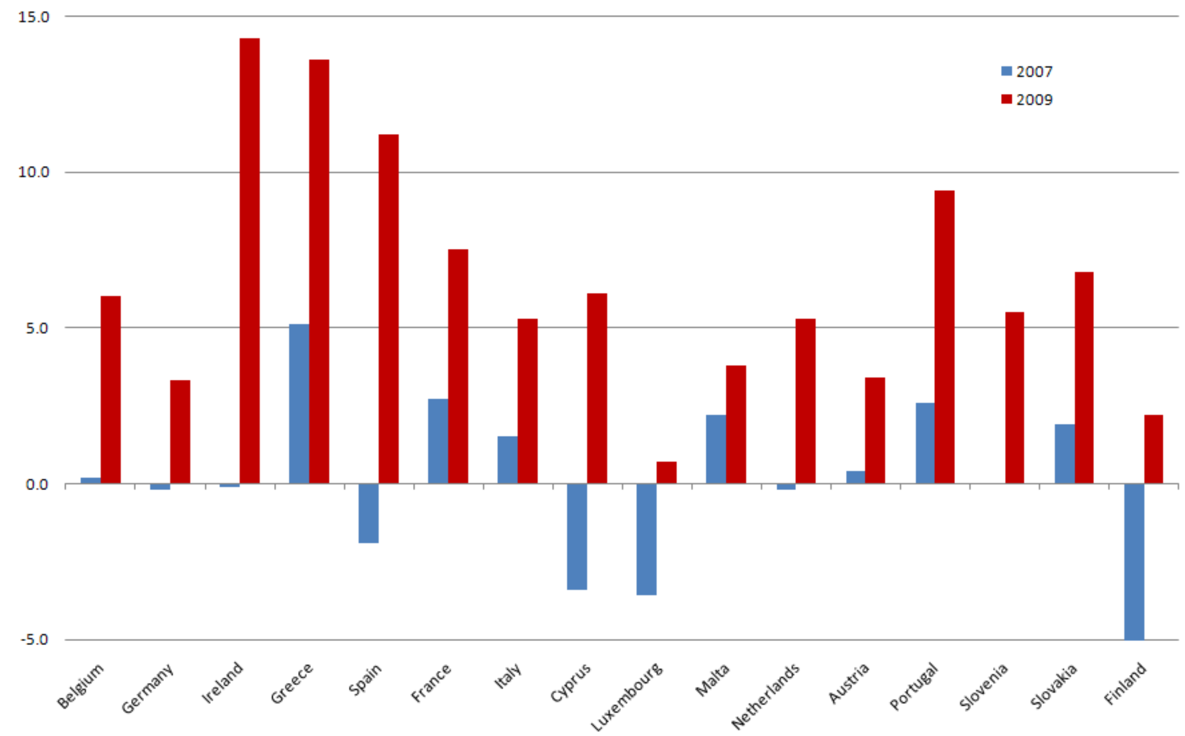
Polarisation in Euro area

- Greek fiscal deficit stems from low revenues rather than high spending; but Greece only weakest link in chain of imbalances in Euro area
- Germany: real wages risen less than productivity; falling unit labour costs; growth dependent on export surplus
- Southern Europe: real wages risen by more than productivity; rising unit labour costs; stronger growth of domestic demand; current account deficits
- Significant financing of southern European deficits (government & private) by banks in northern Europe
- ECB 'stress tests' of banks not considered convincing
- Need for coordinated European policy; not so-called 'independent' fiscal council (*a la* ECB) to impose fiscal retrenchment

Currency rivalry

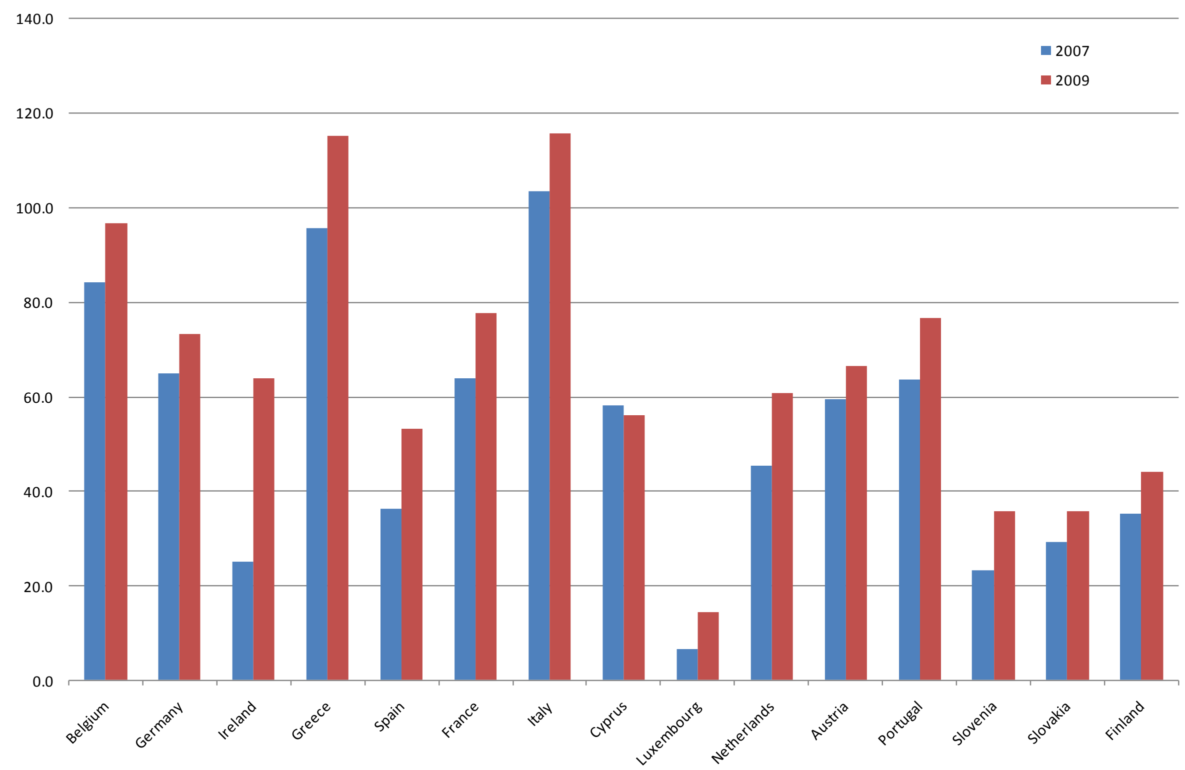
- Abrupt shift in Euro area fiscal stance partly due to political delay in responding to debt issue; but dramatic edge imparted by highly unstable international monetary relations
- Depreciation of dollar re. euro 2002-2008 (interest rate differential); improvement in US trade balance 2007; but potentially dangerous strategy (1979!)
- Challenges to lead role of dollar: China (Chou), UN (Stiglitz Commission), Japan (Hatoyama)
- Threat to global financial stability 2008 → 'flight to safety' (US govt securities); euro depreciated 20%
- As threat of global collapse receded, euro recovered 2009 (interest rates!)
- Uncertainty about Greek debt → extensive forward selling of euro → pressure on euro governments to respond
- Euro area countries relatively protected from x-rate crises (cf. Eastern Europe); but crisis highlights need to supersede international system based on dollar and private capital

Euro area fiscal deficits   (% GDP)



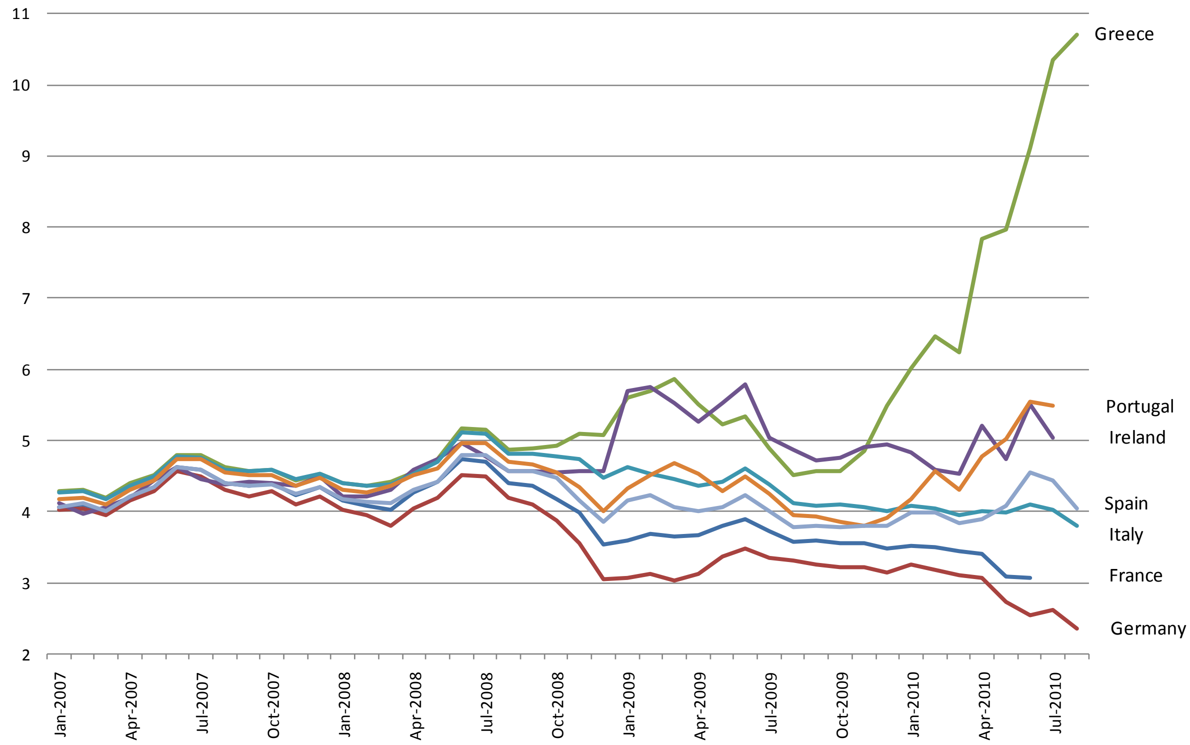
Source: Eurostat

Euro area government debt (% GDP)



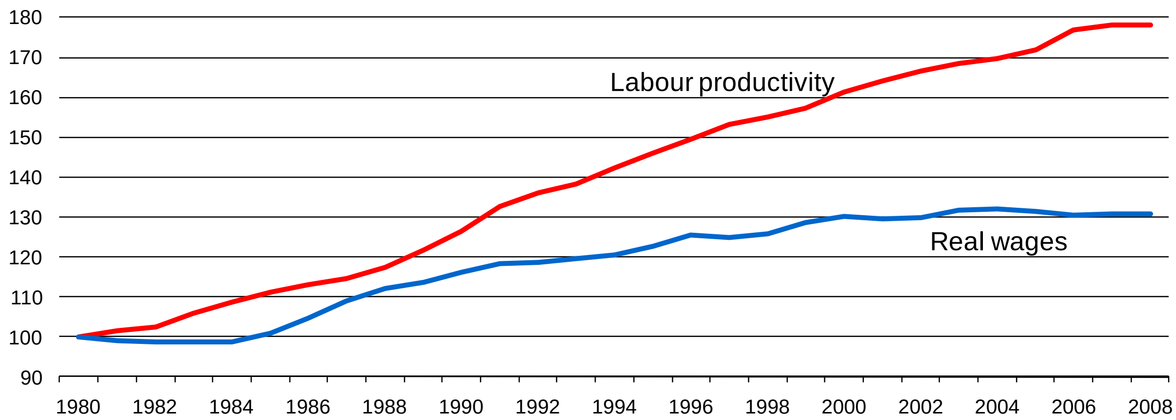
Source: Eurostat

Euro area 10 year government bond yields (%)



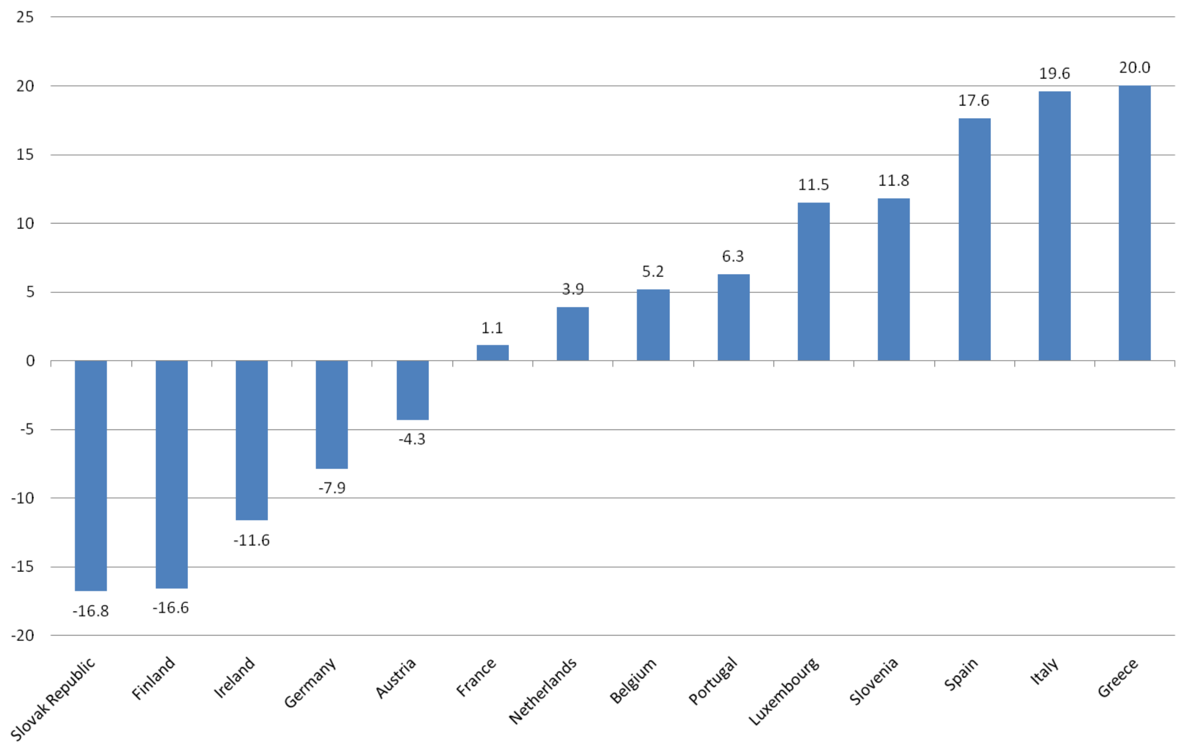
Source: OECD

Germany: Index of labour productivity and real wages (1980 = 100)



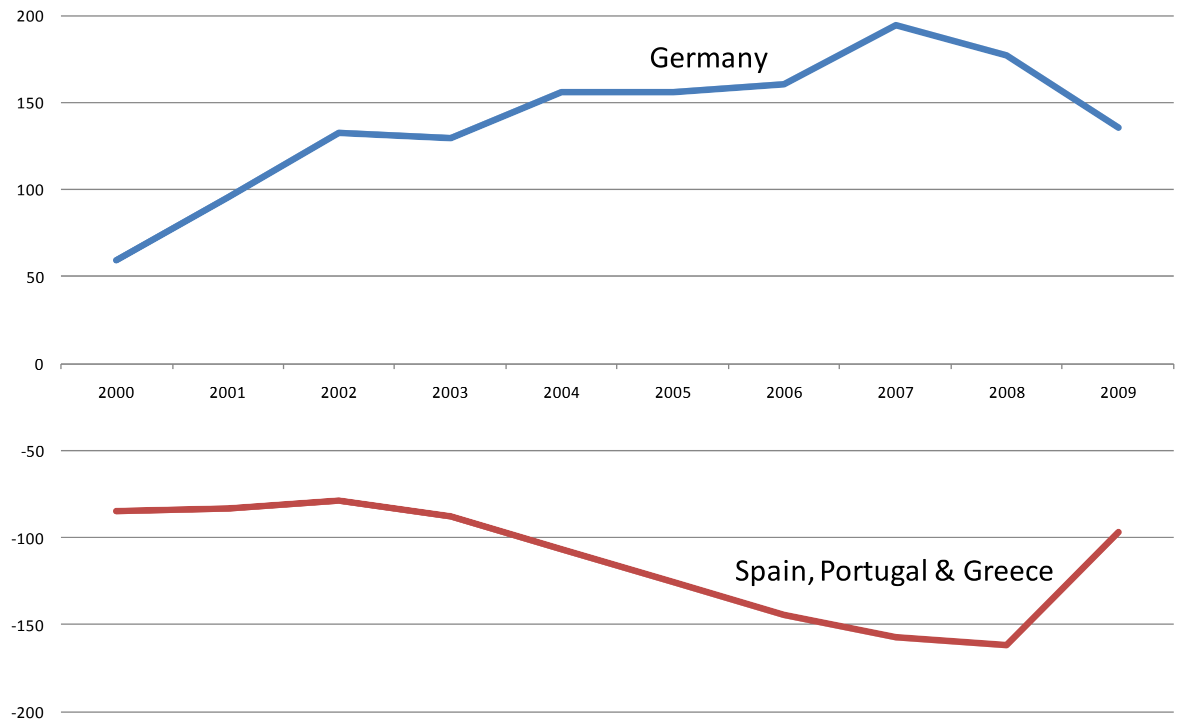
Source: OECD

Euro area: Change in unit labour costs, 2000 – 2007 (%)



Source: OECD

Trade balance, 2000 – 2009 (€ billions)



Source: Eurostat

Bank exposure to Greece, Ireland, Portugal and Spain (End Q1 2010, $ billions)

		Bank nationality									
		DE	ES	FR	IT	OEA	GB	JP	US	ROW	Total
Greece	Public sector	23.1	0.9	27.0	3.3	22.9	3.6	4.3	5.4	2.0	92.5
	Total	51.0	1.6	111.6	8.8	47.9	16.5	5.9	41.2	12.7	297.2
Ireland	Public sector	3.4	0.2	8.7	0.9	3.8	7.3	1.8	1.9	1.8	29.7
	Total	205.8	16.2	85.7	28.6	92.5	222.4	22.9	113.9	55.8	843.8
Portugal	Public sector	9.9	10.6	20.4	2.2	11.5	2.6	2.3	1.6	1.7	62.9
	Total	46.6	108.0	49.7	9.4	29.1	32.4	4.0	37.3	6.0	322.4
Spain	Public sector	30.0		46.9	2.3	19.1	7.6	12.5	4.9	4.4	127.6
	Total	217.9		244.2	42.5	200.6	141.7	30.0	186.4	39.3	1,102.6
Total	Public sector	66.4	11.7	103.0	8.7	57.3	21.1	20.9	13.8	9.9	312.7
	Total	521.3	125.8	491.2	89.3	370.1	413.0	62.8	378.8	113.8	2,566.0

Source: BIS Quarterly Review, September 2010

Euro – dollar exchange rate

Source: European Central Bank

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