FROM STATES' RIGHTS TO A UNITED STATES OF EUROPE

Easy Credit and Fiscal Fraud, not Socialism, caused the Euro Crisis

By Nick Gier

New Yorkers don't mind transferring money year after year
to Appalachia, but in Europe people do mind.
~Dennis J. Snower, Kiel Institute for the World Economy

For every irresponsible borrower there is a
reckless lender (often a German bank)
~*The Economist* (December 3, 2011)

If Europeans wish to avoid the nuclear option of complete
disintegration, they will have to make the leap toward fiscal union.
~*The Economist* (September 3, 2011)

Beginning as the European Economic Community of six nations in 1958, the European Union (EU) now has 27 members consisting of 502 million people. The Treaty of Rome committed the countries to an "ever closer union," which echoes the "more perfect union" in the U. S. Constitution. The EU motto is "Unity in Diversity," very similar to *e pluribus unum*, out of many states comes one United States of America.

Twelve years ago 17 EU countries adopted a common currency called the euro. When Greece applied for membership in the euro zone in 2001, it assured the other nations that it had sufficient fiscal discipline to meet the budget deficit target of 3 percent and a national debt that is 60 percent of Gross Domestic Product (GDP).

Even though the euro zone budget deficit now averages 4.1 percent, no EU nation—except Finland, Estonia, and Luxemburg—abided by the first requirement. Even Germany was one of seven euro zone countries that busted the 3 percent barrier in 2001. From 2000-2010 twelve other euro economies, including France, stayed below the limit more consistently than Germany did.

Greeks and Italians Fudge their Figures

It is now clear that both Greek Conservative and Socialist governments consistently falsified their economic records. For the week of December 3, 2011, the budget deficit was 8.4 percent, the unemployment rate was 17.5 percent, and 2012 estimate for national debt is whopping 183 percent of GDP. Extreme austerity measures have brought the deficit down from a high of 15.8 percent.

Consultants from Goldman Sachs were quite eager to advise the Greeks how to disguise their mounting debt. As the German magazine *Der Spiegel* reports: "Goldman Sachs helped the Greek government mask the true extent of its deficit with the help of a derivatives deal that legally circumvented the EU Maastricht Treaty deficit rules" (2/8/10).

EU scholars have surmised that euro zone states knew that the Greeks' data were shaky but they chose to admit them anyway. There are at least two reasons why this happened. First, Italy joined the euro with equally suspicious books. As the *Der Spiegel* article states: "Italy used a similar trick to mask its true debt with the help of a different U. S. bank." After allowing Italy in at the beginning, leaders of the original twelve found it difficult to deny entry to Greece.

Second, and more significant, a larger euro zone was a great advantage to strong exporting euro economies such as Germany, Austria, the Netherlands, Finland, and Belgium. About 40 percent of Germany huge export market is in the euro zone. One of greatest dangers of investing in other countries is the possibility of currency devaluation in the recipient nation, and a common currency prevents that.

American and European Banks Eager to Offer Generous Terms

European and American banks were more than willing to give overgenerous terms to businesses and governments in Greece, Ireland, Italy, Portugal, and Spain. America's six largest banks have $50 billion at risk in these countries. Easy credit all over the world has allowed people and governments to go on the greatest borrowing spree in human history. World debt, private and public, has increased from $84 trillion in 2002 to $195 trillion today.

Many Germans complain that they are sick of bailing out lazy Greeks, but the Greeks work more hours a week than the Germans do. How do hard-working Irish and Icelanders fit into this North/South bias? Rich Greeks, just as their American counterparts, are doing well and are notorious for not paying taxes, but it will be the poor and the disappearing middle class that will suffer most from their corrupt politicians and bankers.

Socialism: Neither the Cause nor the Solution

GOP leaders are quick to claim that Europe's problems are due to its "socialist" governments and that, as a fellow traveler, Obama's policies will take the U.S. into an economic abyss. As Republican Congressman Paul Ryan predicts: "What we are seeing is the failure of European socialism and the social welfare states."

The dictionary definition of “socialism” requires that the state own the means of production, and only Cuba and North Korea qualify as socialist states in this sense. In Europe the means of production are in the hands of world-class private companies flourishing in market economies.

The World Economic Forum’s list of competitive economies for 2011 includes seven European welfare states: Switzerland (1st), Sweden (3rd) , Finland (4th), Germany (6th), the Netherlands (7th), Denmark (8th), and the UK (10th). The U.S. is in fifth place. The free market *Economist* has chosen Denmark as the most business friendly and it hailed Finland was the most innovative.

One way to measure the strength of any nation to manage debt is to look at its credit rating. Good credit means that governments are able to issue bonds at low interest rates. Even before it lost its AAA rating, the U.S. did not even make the top ten credit worthy nations, but 8 European welfare states did. The latest ratings from Standard and Poor’s indicate that there are 15 countries with AAA ratings before the U.S. at AA+. Except for Hong Kong all of these countries have higher tax rates than the U.S.

The number of European nations led by Labor, Social Democratic, or Socialist parties has been declining over 20 years and now stands at an all time low. Iceland, Ireland, Italy, and Greece ran up their bills (all over 100 percent of GDP) under center-right governments.

In Ireland, where the Labor Party always ran third, the budget deficit reached 32 percent last year and unemployment is running at 14 percent. By 2007 Ireland’s Anglo-Irish bank has loaned out $91 billion. As a proportion of population this would be the equivalent of an American bank loaning out $3.4 trillion.

Nordic States: Highest Taxes; Low Deficits; and Low Debt

Those European countries with the highest taxes have some of the lowest national debt. This is not the result of socialism, but a common sense financial philosophy that one should balance expenses with sufficient revenue. Congressman Paul Ryan’s budget proposal which dramatically cuts taxes and spending—but wipes out America’s social safety net—will reduce deficits by a paltry $155 billion over ten years. Thirty years out Ryan’s—even assuming normal growth rates—is still not balanced.

Current national debt per GDP in the Nordic countries is 36.7 percent for Sweden, 43.7 percent for Denmark, 48.2 percent for Finland, and 48.9 percent for Norway. Sweden is the fastest growing economy in Europe (4.2%) and Denmark—

thanks to Social Democratic programs in the early 1990s—has had an unemployment rate of 3-4 percent for 20 years. A Social Democratic jobs plan allowed Germany to increase employment during the Great Recession.

Norway is currently running a huge budget surplus (13.1) and Sweden's financial books are balanced. Denmark and Finland have been running very low budget deficits (3.9% and 2.5% respectively). From 2000-2010 Finland has had budget surpluses in 8 of those years. The current budget deficit for the 17-member Eurozone is 4.1 percent, and that includes debt-ridden Greece, Portugal, and Ireland.

Comparable figures for low tax U.S. are 100 percent of GDP for total national debt and a budget deficit of 8.6 percent. The U.S. has run up more than twice as much national debt as Europe. Each person in the EU owes $19,522, but each American is $48,860 in debt. When will the GOP learn that necessary spending must be balanced with new revenue?

Austerity-Driven Economic Expansion is an Illusion

A recent cartoon depicted the Statue of Liberty warning off a boat loaded with euros. She cries out: "We don't want your economic policies!" Actually both American and European governments have very similar austerity plans: dramatic spending cuts (especially in Britain, Portugal, Ireland, Spain, Italy, and Greece), which make it impossible for these economies to grow enough to hire new workers and pay off their huge debts.

There is strong correlation between economic growth under Obama's stimulus plan and the slide towards recession after the money was spent. The GOP's call for austerity driven expansion is a dangerous illusion. It's not working in Europe and it won't work here either.

The European Central Bank must act like the Federal Reserve

At the most recent European summit leaders agreed to put more money in a general rescue fund, but only if all 27 nations agree to tough enforcement of budget deficit rules. Many experts believe that the new infusion of funds is insufficient to bail-out countries such as Italy and Spain, Europe's third and fourth largest economies with trillions of dollars of debt.

One solution is to allow the European Central Bank to act like the U. S. Federal Reserve Bank, which recommends that the Treasury Department issue treasury bills for the entire nation and is able to transfer funds from economically strong areas of the country to weaker regions.

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A recent editorial in the free market *Economist* states: "If Europeans wish to avoid the nuclear option of complete disintegration, they will have to make the leap toward fiscal union." Over 200 years ago the U.S. forged such a union. Over the objections of Thomas Jefferson, Alexander Hamilton ordered the federal government to assume the Revolutionary War debts of the 13 states. Treasury bills were issued and the French eagerly bought them up. Our independence could not have been won without General Gilbert du Motier Lafayette, and French bond buys saved the states from bankruptcy and the U.S. from economic disintegration.

The European Union is still at the stage of our Articles of Confederation, which of course our founders discovered as insufficient for achieving the Common Good. Robert Herold reports that 18 Blue States "receive on average only 87 cents in federal tax dollars for every tax dollar paid. On the other hand, the 18 reddest states average a tidy $1.37 for every dollar mailed off to the IRS" (*The Inlander*, 10/10/10). As a former Blue and a reluctant Red, I at least think this as a small price to pay for making our nation a "more perfect union."

The most recent news from Europe indicates that eurobonds may not yet be necessary. Spain and Italy just received favorable interest rates for their own bonds, 60 percent less than what Greece and Ireland were paying at the depth of the crisis. This is good news for all European countries in financial trouble.

We should all wish Europeans well as they move to an "ever closer union," and we should reject calls for states' rights and recognize proper roles for a strong central government.

Nick Gier of Moscow taught philosophy at the University of Idaho for 31 years. Since 2003 he has received most of his economics education from the free market *Economist*. Most of the data cited are from this journal. Read his other columns on Europe at www.home.roadrunner.com/~nickgier/ThirdWay.htm.