

Greece's Economic Woes are Systemic

Keith Rankin, 24 June 2015

In *The Daily Blog* on 13 June, I wrote ([Greece and all that – Unpacking Austerity in Europe](#)) about Greece's resistance to the ongoing attempts within Europe to make Greece a scapegoat for the systemic problems of the Eurozone (Euro Area) of the European Union (EU). And I likened Greece's debt situation with that of Germany in the late 1920s, noting the irony that it is now Germany which is most insistent on making Greece pay for the wider systemic problem. It was interesting then to come across Jeffrey Sachs' article [The Endgame in Greece](#) for ([Project Syndicate](#)) which makes many of the same points as mine, including references to the global financial situation of the 1920s. His is an urgent plea for the ruling classes in Europe to see the bigger picture.

In the 1920s the debt problem was remarkably similar to the Euro problem today, with its systemic problems relating to the gold standard being equivalent to the Euro problems today. I will add here that another analogue country for Greece may be the United Kingdom. It was the British exit ('Brexitee') from the gold standard that triggered the ultimate downfall of the interwar gold standard, and there will be many people aware in Europe today just how significant a Grexit could be for the Euro Area as a whole. Interestingly, the 1931 Brexitee, arguably the most significant global financial event of the twentieth century, immediately restored economic health to the United Kingdom, as if a huge boil had been successfully lanced. Europe, still committed to an untenable gold standard, continued to languish with huge political consequences.

Some of my comments in the discussion from my 13 June essay.

"The debt that accumulated in Portugal, Ireland, Greece and Spain in the first decade of the Euro was essentially 'vendor finance'. In particular, Germany's export machine cranked up and made all these sales to the southern countries. In trade you get paid (for your exports), directly or indirectly, in imports. Germany did not want to accept imports as payments. Instead, Germany and other mainly northern countries became creditors, meaning that the south should pay later (in the form of exports from the south to the north). That 'later' is now, so the northern countries need to accept payment in the form of imports. The southern countries (and Ireland) are now running current account surpluses. They are meeting their trade obligations as best as they can, under extremely difficult circumstances. But they are exporting to countries outside of the Euro area. ***The problem that is accentuating the crisis is the failure of the northern countries to accept payment in the form of imports.*** Yes, in Greece, due to lax fiscal systems, the government took on much of what would otherwise have been private debt. Further, the Greek government itself had been a good customer of German businesses. The major reason why public debt stands out much more in Greece, however, is the Olympic Games of 2004, awarded to Athens in 1997, before the Euro currency was created. This was an international event, and it was appropriate that infrastructure in Greece was improved for such an event."

The whole Euro crisis from the outset has been misframed as a 'sovereign debt crisis', when it is really a crisis of unbalanced trade, which itself largely emanates from the "tribal" (Sachs' word) mercantilism pursued by the Germans, Dutch and others. These countries took advantage of the Euro area as a means to notch up huge and ongoing trade surpluses, believing somehow that such 'vendor finance' strategies (export more, import less, receive IOUs in lieu of imports) represented economic success. By definition, the countries they exported to racked up huge debts. Repayment of these debts can only take place if the tribal northern countries completely reverse their mercantilist strategies.

Sachs mentions the issue of perceived 'moral hazard' as being central to the issue. Here are my words:

"I think there's no technical issue [forcing Greece out of the Euro Area, if the Greek government defaults]. In practice, it would be a negotiated default on part of the public debt. Actually, I understand that already happened, around 2012. Certainly the Greek public debt to GDP ratio has not gone up by as much as it should have, given the size of the Greek government's ongoing deficits. To forgive all Greece's public debt would be seen as an extreme case of moral hazard.

We have to remember that, from the European creditors (bond-holders') point of view, this is not really about Greece. It's about Spain, Italy and France. The creditors would want a punishment meted out that is at least proportionate to the size of the crime as they see it. Also it's political. The Euro conservatives and centrists do not want to be forced to even contemplate the Syriza analysis of the systemic crisis that Europe faces. Instead, the Euro Area as a whole is trying to worm its way out by running increasing trade surpluses with the rest of the world. That means, in time, a globalisation of the Euro crisis."

On the matters of the role of agricultural trade crises before the 1930s' Great Depression, and the role of government austerity measures to restrict imports, I commented:

"Thanks for raising this issue [of falling agricultural prices]. You are right in that falling agricultural prices and import-aversion were significant forces in bringing about the Great Depression. But the main means to reduce imports in the 1920s were deflationary policies, not protectionist policies. The causes of the Great Depression lie in the global economy of the 1920s, and the eventual cure lay in the (eventual) individual sub-global (national and imperial) responses in the 1930s. The 1920s was about countries trying to run trade surpluses through policies of 'internal devaluation', known then as 'deflation'. The goal was to reduce imports and to increase exports. This made some sense to the deficit countries with dwindling gold reserves, including the UK and of course Germany. The worst offenders were the money hoarders, USA and France. It is true that the US Smoot-Hawley tariff of 1930 substantially aggravated the extreme global imbalance. This is because the US was the country that had been running trade surpluses for a decade; the world economy then needed the US to become its biggest spender. Instead, the US did the very opposite, substantially reducing its imports. One of the most important events bringing the UK out of depression, and eventually much of the rest of the world was the (intended temporary) abandonment of free trade (in 1931). It gave Britain the freedom to adopt expansionary policies which could be assured to boost the British domestic economy. Britain's imports soon revived, despite tariffs, as British incomes recovered. Important here to NZ was the negotiated 'imperial preference', through which growth in British imports would boost empire exports. In return, NZ switched to buying a significantly greater proportion of its imports from the UK (eg British instead of American cars). Through the late 1930s, a revival of the empire economy facilitated a revival of the global economy, though too late to bring Germany back into the global trading system."

On the matter of the future of the European Union and the Euro Area, I commented:

"I sense that the EU nations not in the Euro Area will eventually have to make a choice: join the Euro Area or leave the European Union. The coming referendum in the UK confirms English ambivalence towards the EU, signaling an eventual exit, even if the referendum favours staying in. The interesting subtext is, I understand, that Scottish independence may be facilitated. Scotland would like to join Ireland as a full member of the EU and the Euro Area."

The so-called 'Greek crisis' will not go away if Syriza does come to an accommodation with the Greek government's creditors. It's a systemic crisis that still has quite a long way to run. As I noted above, the logic of the tribal European financial establishment "means, in time, a globalisation of the Euro crisis".

What gives me hope is the youth and intellectual capacity of Syriza. Young Greek intellectuals are providing, through practical adversity, the leadership that is required to address global systemic problems. I sense, in the making, a global revolution in political economy not unlike the mid-nineteenth century Darwinian revolution in biology. Intellectual revolutions are generally generational revolutions. Eventually the resistant older generation passes on, rather than conceding intellectual defeat.
