The Crisis of Europe: Elements of a Political Strategy

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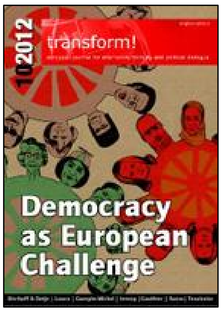

Many of our friends have been asking the following question over the past few months: What if Portugal was to leave the Eurozone? Should I withdraw my savings, should I look for a foreign bank to deposit them, should I anticipate the payback of the house loan to the bank, should I sell the house, should I make provisions for private pension funds, should I take out health insurance, should I emigrate, what should I do?

Instead of answering simply by giving a prescription for individual actions to protect ourselves from uncertainty, we prefer to offer readers another solution: the one of choosing to learn, to think and to discuss in order to be able to decide. Our proposal is to respond collectively to the difficulties, rather than having everybody be on his/her own. This article is about this collective choice. It proposes decision-making and mobilisation while facing the emergency: to come up with the necessary force to renegotiate and restructure the debt, to cancel the debt share, which results from imposition and abuse, to reorganise the country according to social priorities, to democratise the economy, to save Europe by remodelling it in the direction of social responsibility and overcoming financial capital.

Who determines an exit from the Eurozone?

Let us begin by anticipating what an exit from the Eurozone would be like, which is the major concern of our friends and correspondents. The proposal for leaving the Eurozone has been persistently defended by two types of currents: the economists who reject the straitjacket of the Euro and cannot find another solution, and those who prefer nationalism to the protraction of the European crisis (or have always been nationalists). They come from different sectors, with distinct ideas and proposals.

Among the economists who advocate leaving the Euro, one can find the usual opponents, such as Paul Krugman and Nouriel Roubini from the United States. For them, the exit of Greece and Portugal from the Eurozone is no longer a choice. It is, or is beginning to be, simply unavoidable. According to them, the recessive spiral of fiscal adjustment measures will make governance impossible, with tax increases which no longer create more revenue, with the economy at a standstill and the exhaustion of policies. Therefore, they argue that the only way is to leave the Eurozone so that a new currency can be devalued and the economy balances out by increasing exports and reducing wages. It is important to note that none of them supports the repudiation of debt, or they are indeed very discreet when it comes to a renegotiation; instead they hope to gain some time to pay the debt in another way, through an increase in exports. And both agree that all workers should bear the costs of the adjustment in the form of reduction of wages and pensions.

At this point there are good and bad arguments. But, above all, it is a response which proposes a permanent wage austerity, often indifferent to the immediate effect on people's lives. In this context, there are other economists who suggest that one could ask the European Union to finance an exit out of the Eurozone or that one might even expect the financial markets to maintain an attitude of neutrality towards the newly created currency (let us imagine that it would be called "escudo"). And there are those who come up with a curious proposal: The country should threaten to leave the Eurozone only if and when it receives a compensation for the damages its economy has suffered from the loss of market shares and competitiveness. It would be a kind of ultimatum: if you do not pay us, we stay.

We disagree with these positions. We prefer the more realistic test, asking ourselves what would happen if the government's economic choice were an exit from the Eurozone. But before proceeding, let us avoid the ambiguity of romanticism: if a government were to decide that Portugal should leave the Eurozone, it would be the government of Germany, which is at this point commanding the European Union. There is no other social force or political dominance that has the ability to make this decision. There are no imaginable combinations in Portugal between the PSD, CDS and PS, the signatory parties of the agreement with the troika – IMF, ECB and European Commission –, that would indicate such an alternative. In addition, even if this were to happen, one should not expect that the alternative political force would seek to protect workers. In fact, this option simply does not exist in the policy of alternation of power that has been ruling Portugal.

If Portugal were to leave the Eurozone, it would be only be due to the diktat of Germany and the imposition of a new model of governance of the European Union. The Ultimatum of 1892 and the ensuing imposed bankruptcy is remembered because it triggered social upheaval and paved the way for the overthrow of the monarchy, with Britain imposing its will and taking possession of the African colonies. But now it concerns the social regime in which we have lived in over thirty-five years of democracy.

Does Germany want the end of the Euro?

There will only be an end to the Euro, if this is the interest of Germany. But will Germany want it? Nobody knows enough to answer this question with any certainty. The twisted path of German's right wing leadership, and in particular Chancellor Merkel's, is too contorted to be clearly understood. Germany's right wing, which might lose the power to govern to a coalition between the Social Democrats and Greens in the upcoming parliamentary elections, has been trying to compensate its exhaustion by employing the demagogy of nationalist arrogance against Greece, but even with this policy, it has lost all regional elections. And, for the first time in recent history, the government was forced to interrupt the issuing of its public debt in late 2011, because it was not getting the interest rate that had first set as a goal. The same happened in early 2012. The President resigned in February 2012 and the coalition of right-wing parties showed signs of weakness. All of this indicates that the German political leadership has notable difficulties controlling the country. Thus it is not reasonable to make definitive predictions about what is likely to happen in 2012 and 2013.

Conversely, there are solid structural elements: the German economy would suffer a lot with a break-up of the Eurozone, as we shall see below. The return of all European countries to their own currencies would create a risk of disorder that would not be beneficial to Germany, which as the strongest economy in Europe would have more to lose from the resulting trade conflicts. The reason is obvious: if the first and foremost objective of all countries were the increase of exports and the reduction of imports by means of creating a new national currency, seeking thus to impose a neo-mercantilist policy to their own advantage, the result would be a disaster, as the exports of some countries are the imports of others. One thing is certain: they cannot all simultaneously sell more and buy less.

This neo-mercantilist policy was the one used by Germany, forcing other European states to accept it – it was the only country that could do it and did it on such a large scale. Nonetheless, in order to increase competitiveness, the German economy subjected its workers and employees to drastic wage reductions. But it is not enough just to suppress wages in order to expand exports: it is also crucial to keep the borders of European countries open.

For this reason, Germany has counteracted the pressures which could lead to a general breakdown of the Euro. It has so far avoided the pressure on Greece to exit, even acknowledging a hitherto unthinkable restructuring with the partial cancellation of their debt. Even if a domino effect of Greece (or Portugal) quitting the Euro is unlikely, the uncertainty about the future of the Euro would be a fact.

On the other hand, the first months of 2012 made it clear that the problem in Europe is neither Portugal nor Greece. It is the pressure of financial capital, especially on Italy, Spain and other economies strongly affected by speculation and recession. The massive three-year program of cheap financing of private banks, approved by the ECB at the end of 2011, notwithstanding its previous doctrine, demonstrates how institutions subordinated to the German government fear the consequences of a widespread financial meltdown. No German government will want the end of the Euro if it takes the economic implications into account.

Nevertheless, does Germany want, on the pretext of protecting the Euro, some or all of the peripheral countries to be excluded from it? This point will be answered further below. Let us focus first on how this could work in practice. Let us see how Portugal quitting the Euro would affect workers' lives.

After all, there may be a new holiday

First things first. Let us start with the decision to create the new currency, which would use the name of the previous currency "escudo". The scenario is the following: the government, facing the economic difficulties, decides to accept Germany's ultimatum, declares that it is quitting the Euro and wants to switch its national currency to the escudo.

Secretly it starts to print escudo banknotes and prepares to announce the big news on a Friday night, during news broadcasts, when banks are already closed (or it might even decree several bank holidays). On this weekend, all banks work overtime to deliver the notes to all ATMs, in order to put the new currency into circulation immediately.

There are other alternatives: some suggest that the government could simply reprint the Euro banknotes with the brand of the new "escudo", until it manages to circulate the new notes. But these are hypotheses that require some level of imagination, because it is not certain that the Euro authorities would accept this stratagem without retaliation.

What is going to happen, in any case, is that everyone will find out about the plans for a new currency. This release operation of the new "escudo" involves thousands of people who transport and distribute the notes, and they will surely tell their families. In any case, everyone will have heard the declarations of ministers over the weeks before, explaining that the situation is very bad and that it requires extraordinary measures to save the home country. Everyone would be aware of the European emergency summit and would realise what was happening. There are secrets that simply cannot be kept.

What are people going to do? It is evident, isn't it? They are going to collect all their savings from banks and save their Euro banknotes. If they do not do this, all their savings will be turned into "escudos", at a nominal value which will fall in the course of the sharp depreciation which is, after all, the whole purpose of this operation. In other words, the saving accounts will lose as much value as the currency in which they are registered. All the workers who deposited their wages and pension money will be the first victims of the new policy. Therefore, they will try to rescue whatever they can.

And not only workers. There will be a massive flight of capital. The companies, the financial funds, all institutions which have money deposited in banks operating in Portugal, will want to move it to where they perceive that their deposits are protected from devaluation.

Now, banks do not want to pay their customers their whole bank balances, because this would ruin them. They neither want to nor can, as they simply do not have the money for it – and there are not enough banknotes in the banks to pay all their debt to all depositors at once. The banks will therefore close their doors when the alarm sounds everywhere, and the government will have to call in the army to protect the buildings. This is what happened in Argentina or Russia or in all cases where large devaluations were announced (and it was not even about changing currency and creating another one, something which has never happened in the history of the European Union, with the aggravating circumstance that the circulating currency is removed to be replaced by another, strongly undervalued one).

By then, those who advocated leaving the Eurozone as an immediate alternative, begin to face the first difficulty. The fact is that the army and the banks will act against the population. And the first victims are the depositors. If the depreciation were about 50%, as some economists that advocate such an alternative estimate, the savings of workers will lose half of their value.

However, what is very likely to occur is that for some time the Euro and the "escudo" banknotes will circulate alongside each other and these double price references will have a strong inflationary effect, apart from leading to an excessive devaluation of the "escudo". It can also lead to uneasiness in markets as a result of hoarded products, due to fear of the ensuing economic development. At this point, there will be a race to the supermarkets and there will be fewer products on the shelves, until the new economic situation has settled down. Life will not be easy after the Euro.

How much do we owe the bank?

And then there is the second shock. Half of Portuguese families owe long-term money to the bank that lent them money to buy a house, which will be paid back in the course of many years. These loans were taken out in Euros. On the day of quitting the Euro, the government has two options: 1) accept what the banks want, meaning that the families' debts will continue at the previous value in Euros, or 2) decree that, in order to protect debtors, the debts will be converted into escudos. In practice, there is only the latter alternative, because otherwise the social upheaval, intensified by the debt increase, would be unacceptable.

In fact, if the government were to allow them to keep the credits in Euros (as originally stipulated in the contracts), people would be more chained to their debt. Let us imagine someone's debt of 100,000 Euros would be converted into the devalued escudos, and thus total 30,000,000 escudos. If the salary of the debtor before the devaluation was 1,000 Euros (which in the new currency would be 200,000 escudos or 200 "contos"), later on, with the devaluation, that sum would be worth only about 670 Euros, half of which was used to pay the bank. He would initially have needed about seventeen years, and that with great difficulty, to pay his whole debt. Now, he will need twenty-five years with the same difficulties, giving the same half of his salary to the bank. At the end, he will have lost eight years.

In the second case, in which the government decrees the conversion of debts into escudos, as it should, those who had a debt of 100,000 Euros before the devaluation, will turn out to have a debt of 20,000 "contos" or 20,000,000 escudos, which would total about 67,000 Euros. In that case, the bank would lose. The problem is that in the course of such a process of devaluation of debt, the bank goes bankrupt, because all of a sudden there is a giant hole in its balance sheet, and its debt to international banks remains in Euros. In no way can the bank pay its foreign debts.

That is why the advocates of an exit from the Eurozone explain, honestly, that it will be necessary to nationalise all banks, not necessarily in order to socialise the financial capital, but to save it. Now, to save a bank can be very costly, as we know from the case of the fraudulent bankruptcy and ruinous salvation of BPNLBW. Because when a bank is nationalised, one gets its assets, but also its debts. Those are usually debts to the depositors and debts to those who lent money, usually foreign banks. This debt is in Euros, but the bankrupt and nationalised bank will begin to receive its revenue and deposits in devalued "escudos", in order to continue to make its payments abroad in Euros. The public debt on the other hand, has suddenly soared, as the state has taken over the 175 billion bank debt. Saving banks costs dearly: bank debts, which were once private, become public when they are being nationalised. It is this way when banks are the debtors, but not when banks have more to receive than to pay – which is not the case of Portuguese banks (and the foreign banks in Portugal).

Tax increase

Having come at this point, we know what is going to happen: in order to pay the debts that resulted from the nationalisation of the bank sector, there will have to be another tax increase, this time to finance the international banking system. The worker, whose personal debt was protected, must pay through other means, in this case through new taxes. Of course, one can hypothesise that the government can simply refuse to pay the international debts of nationalised private banks. But then this whole operation of the new currency devaluation may be questionable, because its purpose was to increase exports to open markets, so that increased sales of Portuguese products would save the economy.

On the other hand, this decision would make it even more difficult for the economy to access external financing. Unable to borrow directly from other countries or financial markets, the Portuguese government would have two options left. The first is to keep the primary balance positive: i.e. the government can never spend more than what it receives in taxes. This in turn means to charge more taxes to workers and invest less, both being recessive measures that are even more inadvisable in this situation, apart from being socially wrong and unjust. The second option is to use its new resources, as the Bank of Portugal could print more and more "escudos" to make state payments, which on the other hand would accentuate devaluation and inflation.

Let us now turn back to the problems that the government is facing, because it has decided to leave the Euro or accept the imaginary ultimatum of Germany. It already has a rather large opposition: namely those who will pay more taxes or who saw their debts multiply, who pay more for food, transport and medication and those who lost part of their savings and deposits. Considering this situation, workers will quickly figure out that they lost part of their salary (or their pension), that the budgetary effort has not decreased (on the contrary, it has become worse, since the debt will be paid in Euros, but the taxes that the state collects are paid in escudos, and therefore we will need more and more escudos for each Euro) and there will be further cuts in health and education. For all these reasons, the workers will fight in order to recover their wages.

The government will argue that this might void all efforts. Exports are cheaper now, either because the escudo is worth less and goods have become cheaper, or because companies pay lower wages in escudos. If wages rise, competitiveness will again be undermined. What will the government do if faced with the workers' protests? The country gets caught up in turmoil, because there will have been riots at the banks' doors, because depositors will have realised what they were going to lose, taxes and prices are going up and wages down. The government has two options now: the solution of the Argentine presidents, who fled the palace in a helicopter, or the solution of repression.

In other words, leaving the Eurozone we will find ourselves with our backs to the walls. The economists who wanted to prevent the continuation of austerity measures, and rightly so, will thus in the end have proposed a system of even more austerity, oriented mainly towards the benefit of one single economic sector, the export industry, accepting lower wages due to the devaluation of the escudo. New difficulties would be created and it would take time before any advantage caused by the devaluation would appear. In the meantime it is obvious that the government is going to lose the respect of its workers, because they are the ones who suffer.

Saving the economy through exports

Thus, the second shock is over. But there is more and worse to come. The escudo will have lost 50% compared to the Euro. The government, and those who defend the devaluation of the currency as a solution to recover the economy, expect the beneficial effect to be the following: exports are likely to increase, because they will have become cheaper (calculating that their prices in foreign currency become cheaper and also because of the reduction in wages), while imports are likely to decrease, because they will have become more expensive in escudos. Consequently, there would be a shift of capital to the exporting industries and services and, simultaneously, a reduction in consumption and imports. All this would improve the balance of payments considerably. The rule is: if things get better for exporting companies, they will also get better for the entire economy.

It seems positive, but it has an enormous flaw. The fact is that in the course of the devaluation, the price of imported products would increase on the same day. Fuel would cost one and a half times what it did previously, and so would the entire transportation system: imagine a litre of gasoline at 480 escudos (or currently 2.4 Euros). The same applies to imported food products or medicine, among many other bare necessities. In supermarkets, there would be a lack of goods, but those for sale would become more expensive immediately.

As two-thirds of Portuguese incomes are spent on consumption, one can easily imagine the effect of these two price increases. That impact alone would account for a decrease in the value of wages.

As to exports, it is obvious that they may increase. But many economists perceive society as a laboratory and all too often forget at what time decisions are made and at what time policies take effect. Timing will be crucial in this case, for one simple reason: import prices will rise immediately, but the effects of the possible increase in exports will take time, maybe a great deal of time.

Even so, certain conditions need to coincide so that exports can grow. It is necessary that the foreign buyers of Portuguese products want to buy more due to the price reduction, as long as there is no recession abroad and the Portuguese products are tailored to markets with a growing demand and their qualities meet the standards demanded by foreign consumers.

Even if exports increase, it will happen slowly: sales revenues will only start to come in after sales have been made and therefore one must wait during the whole time of production and even the time that it takes to increase the productive capacity: To increase production, it is necessary to invest; to invest one must have the necessary capital, hire more workers, pay them and only after receiving the returns on exports. In order to have exports leading the process of economic growth, it will be necessary to reverse decades of deindustrialisation in Portugal, and also the specialisation of the economy in non-tradable sectors. It is certainly desirable, but time-consuming and difficult to implement in the short term.

Furthermore, one must take into consideration the cost of raw materials and other resources that are imported to determine the price of the products that the Portuguese economy exports. As half of the total value of exports depends on imported products, and those will have become more expensive with the currency devaluation, at the end the competitive gain from exports is reduced. Therefore, export revenues will increase only slightly, slowly and late. At the same time, the cost of living will have become more expensive, with savings badly shaken by the devaluation, whereas the increase of the employment rate and of exports takes time and is uncertain.

The economic recovery through exports is an unknown quantity and the fall of wages is a certainty. The socialist policy, which we propose, has a principle, and that is to defend the working class. This policy does not seek to sacrifice the workers' salary, which is their legitimate part of the domestic product. The authoritarian solution of exit out of the Eurozone is a proposal that does not avoid austerity measures – on the contrary. And therefore there is no reason to defend it as a viable alternative. It reduces wages and creates more debt.

Let us state it clearly: in the present context, leaving the Euro is the worst of all solutions and can only be imposed by the will of the European directorate. One can then only accept the worst solution if there simply is no other, or when all alternatives have been exhausted, when it is required in order to survive. There is only one condition that can make it necessary for the Portuguese to leave the Eurozone, and this situation cannot be excluded: If the European institutions and regulations were to collapse, Portugal's independence might be at stake and there would be no other solution than to leave the European Union and, consequently the Euro, in order to recover its decision-making capacity. The risk of transition from one system of creditors to a colonial protectorate implies such a threat. Obviously, the majority of the Portuguese population must be involved in this reaction, so that the strength of popular movements and the protection of labour interests shape and determine it.