

Missing Chances for Change

This is part of our round table on [Against the Troika: Crisis and Austerity in the Eurozone](#).

Heiner Flassbeck and Costas Lapavitsas have written a book that is designed to serve at least three purposes. In the first instance, it is a thoughtful and grounded critique of orthodox economic thinking at the heart of Europe's single currency architecture, the decisions and actions it takes as a result, and the impact it has on the resilience of the single currency as a whole. Second, it examines German behaviour within the single currency, seeking to substantiate the argument that instead of working as an anchor stabilising the rest of the eurozone, it has acted in mercantilistic and free-riding ways that destabilise it. Third, it outlines what Greece would have to do to break free of these outside restrictions and reclaim its own sovereignty from eurozone. There are other points made within the book, but these are the core ones.

This book is organized into two sections. Section 1 deals with the first and second goals outlined above. It is a welcome alternative to the approach taken to currency areas found in most economic textbooks that start with orthodox / neoclassical economic assumptions and then work out models of desirable economic benchmarks and adjustment strategies based upon them.

Instead of focusing on stable prices as the benchmark of a working monetary union, Flassbeck and Lapavitsas argue for coordination of unit labour costs instead, following observations of how economic growth in Europe closely follows wage growth. This implies that instead of focusing on the budget deficits of national governments, and on the debt levels that they have, EMU rules should focus on a golden rule in which national governments commit to ensuring that unit labor costs increase at a steady pace of approximately 2% per year. This would mean that countries would do what is required to ensure economic growth and employment, and at the same time ensure that no country can undercut the economic chances of the other states by engaging in competitive internal devaluation.

In short, EMU's first failing was not in setting a golden rule, but setting it in the wrong place. With a focus on budget deficits and public debt, nothing could be done to ensure economic growth and development. Indeed, GDP and budget retrenchment would shift into a contractionary, pro-cyclical spiral during periods of economic stress, undermining the currency area's resilience against economic shocks. But even more problematic, EMU has no tools to manage or punish a state that defects from the commitment to act as a good member in the single currency area. Germany, the authors contend, did precisely this by insisting on debt, deficit and inflation criteria as part of EMU's membership rule set, and then engaging in an aggressive domestic campaign to drive prices and consumption well below those targets. This amounted to a mercantilist exercise in competitive deflation, placing other member states at a disadvantage by making their own products more competitive than those of their neighbors in the single currency. And yet there is nothing that those other countries can do to retaliate and hence change that countries behavior. They are only able to compete on terms that Germany effectively sets. Alternatives left to other states to retaliate remain unavailable due to the free flow of goods, services and capital in the single market as a whole.

This is intelligent, concise and empirically-grounded work that primarily serves to show what has gone wrong, and what in theory could be done to rectify it with a different policy direction. The implications of those choices for institutional design are not truly followed up on, though one can imagine that they would lead to a mirror image of the existing European Semester system, in which the existing goals of budget and debt sustainability are substituted with wage growth. It remains, as one would expect, far removed from any chance of adoption in the EU. It is the basis for a radical institutional re-engineering of EMU, rather than the kind of compromise that could be considered realistic. It also, in the introduction and in section 2, drifts off into why, because change is not realistic, why national governments should withdraw from the euro. This is the book's major lost

chance—it could and should have dealt with how that would look, and why it is realistic. There are real reasons to be critical about the authors not taking on this task.

Section 2, however, takes a shot at the how part of that question with regard to one country. It deals with the strategies and tactics that a leftist government in Greece should employ to regain economic growth and employment. It comes to the conclusion that it is impossible for Greece to achieve economic growth and employment with an economic and monetary union as a result it sets out a path for doing so in an autarkic fashion. The proposals are indeed radical and revolutionary, even for Greece. The country would have to set up its own scrip, and then its own currency to keep the country running, use it to recapitalise the country's banks, accept that the country would have to significantly devalue the currency, be shunned by international capital and consequentially impose capital controls. It would then have to nationalise the banks to direct capital to needed sectors, raise employment and wages and return to growth and employment through domestic consumption.

If reading Section 1 starts out very reasonably and then ends with something impractical, reading Section 2 starts out as surreal, were it not for the negotiations between Greece and the eurozone that were taking place as the book was being published. We know that the Greek Finance Ministry under Varoufakis undertook at least some of the contingency plans outlined by Flassbeck and Lapavitsas (the preparations for scrip and currency), and it is no far reach to assume that control over the banking sector, capital controls and an Keynesian-style program of fiscal expansion with a New Drachma were part of the plans. It is a way for readers to get inside the mind of what the Greek government, or rather then Finance Minister saw as a realistic second path to internal devaluation in the eurozone in return for keeping the single currency. As we also know, the Syriza government eventually chose the latter.

This is therefore a worthwhile and fascinating read, if someone impractical. It also suffers from periodic inconsistencies that occur when more than one author is writing on a tight schedule. Whereas the introduction of the book and the first section indicates that all EMU states should go back to their own currencies, the second part of the book sees this as really only necessary for Greece, though others might benefit from its example. Had Greece ever set it.

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[Against the Troika: Crisis and Austerity in the Eurozone](#)

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