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SNAPSHOT

## Austerity and the End of the European Model

How Neoliberals Captured the Continent

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*A May Day demonstration in central Madrid. (Susana Vera / Courtesy Reuters)*

Since the onset of the European sovereign debt crisis in 2010, countries across the continent have responded by imposing fiscal austerity. From Greece to Ireland, governments have cut spending by double digits. Spain, which is in the midst of a recession and has an unemployment rate nearing 25 percent, slashed its budget by eight percent and plans to shrink its deficit by an additional 27 billion euros this year. Even Germany, whose economy is considered the healthiest in Europe, has pledged to eliminate 80 billion euros in spending by 2014. These national austerity policies will be reinforced across the continent by the EU fiscal compact, a treaty slated to go into effect next year that will require European countries to maintain balanced budgets. Tea Party loyalists in the United States should be green with envy.

It is unclear if these efforts will quell market contagion or stabilize European economies in the short term. What

is clear is that austerity will transform Europe's political economy in the long term, lending credence to neoliberal ideas of limited government and loosely regulated markets. The irony of this transformation is that it reinvigorates the very ideas that helped cause the financial crisis in the first place; after all, it was the unyielding faith in markets and weak regulation that allowed the financial bubble to swell. At the same time, a response to the sovereign debt crisis based on austerity precludes any alternative social-democratic framework that would emphasize growth and protect citizens from the vagaries of the market.

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In the mid-2000s, during the heyday of the financial boom, the benefits of light-touch regulation and market-based solutions seemed indisputable. Self-regulation by firms, the argument went, would reduce the burden of slow moving, bureaucratic oversight, and competition in markets would spur new innovation and drive down costs across industries. European social democrats had to play defense not only on financial regulation but on labor and education policies, consumer protection, and even the environment.

At first, the global financial crisis seemed like a turning point; it made clear that markets do not always efficiently distribute goods and services. Banks had taken advantage of limited regulation to repackage bad investments and sell them to unwitting customers. Policymakers, particularly in Europe, seized on the turmoil to push back against neoliberal policies that had dominated since the turn of the millennium. They also championed their own social-market model, which had cushioned workers from the initial blow of the financial crisis. In 2008, German Finance Minister Peer Steinbrück declared that "the cause of the crisis was the irresponsible exaggeration of the principle of a free, unrestrained market."

The sovereign debt crisis, however, has recast the debate once again. Europe's recent economic troubles have taken three different forms. Some countries, such as Greece, face an old-fashioned debt crisis: Governments borrowed too much money during the boom and have no viable means of repaying it. In other countries, such as Ireland, the financial crisis forced governments to bail out the banking sector and absorb its debts. Still other countries, such as Spain, suffered a crisis of liquidity after bond purchasers demanded higher interest rates on government debt. In the latter two, markets, not governments, were the primary culprits. But that has not stopped politicians in Germany and the Netherlands from singling out government -- inefficient, bloated, and profligate -- as the problem. The government in Athens has become the poster child of the austerity movement, but it only speaks to one of the causes of Europe's current woes.

To be sure, it is high time to rein in government's excesses, particularly in Greece, where state employees notoriously receive 13th- and 14th-month "bonus" salaries. But austerity pushes too far in the other direction, squelching alternative policies that would favor a mixed economy. Given the need to conserve public sector resources, proponents of austerity argue, firms and individuals are required to step in to provide core services, as is the case with the Big Society initiative in the United Kingdom. At the same time, governments are increasingly forced to privatize segments of their economies; Spain and Ireland have put everything from electricity to airports up for auction. What's more, in the name of labor productivity, workers are asked to bear the burden of economic recovery through cuts to wages, pensions, and other benefits. German Chancellor Angela Merkel's

focus on structural reform in her 2012 speech at Davos typifies this trend. Austerity politics, then, necessarily reinforces the belief that in the wake of the crisis only markets can determine the contours of the European economy.

This new political landscape bears negative consequences for Europe and the world. Across Europe, the image of the EU as an advocate of smaller government and less-regulated markets is politically unpopular and threatens to undermine support for cooperation and integration. Opposition to such policies was the rallying cry that brought down the ill-fated European constitution in Dutch and French referenda in 2005. The anti-austerity protests that have rocked Athens and Madrid touch on a deep uneasiness among EU citizens concerning regional cooperation. The success of extreme parties, including the National Front in France, the UK Independence Party, and the Pirate Party in Germany, suggests that mainstream politicians struggle to channel voter frustration. Austerity threatens to embolden these forces and weaken European commitments to openness. For the EU to retain its popular legitimacy, it must be more than just an engine of free trade and deregulation.

Meanwhile, on the global stage, the politics of austerity prevents Europe from offering an alternative vision of capitalism and globalization to that put forward by the United States. At recent international economic meetings, for example, European officials have agreed to international rules about how much capital banks need to hold that are even more trusting of markets than U.S. regulations. For a middle-class worker in India worried about corruption, or an Indonesian farmer fearing the shock waves of financial crisis, European austerity offers little hope. Gone is the idea of Europe leading a global third way between laissez-faire capitalism and managed socialism.

Austerity politics in Europe is not simply a short-term fight between the surplus countries in the center and the deficit countries on the periphery. It is a long-term political agenda that privileges lenders over debtors and capital over labor and, as such, should be seen through the lens of partisan politics. Center-right governments in Germany, the Netherlands, and Spain have been among the most vocal proponents of austerity. If the French and Dutch elections bring new parties to power, however, there will be a window of opportunity for Europe to chart a different course to recovery.

Reviving an alternative agenda for the political economy of Europe would first require social democrats to convince voters that the crisis is not just a story of profligate governments but also of reckless markets. Addressing the failures of the market requires solidarity among European countries. Creditor governments should support the European Central Bank's role as lender of last resort and allow for the creation of Eurobonds, which would help solve the liquidity problems in Spain, Italy, and elsewhere. European voters and leaders must also demand that governments mobilize to promote growth by stopping further severe cuts and expanding consumption, particularly in the creditor countries. For if austerity is allowed to run its course, and Berlin and Brussels continue to starve the beast, Europe could quickly become a hotbed of widespread social unrest.

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