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## **Ever more austerity: How the European Commission is pushing Europe back into recession**

Increasingly it is becoming clear that reducing public deficits and 'belt-tightening' has become the cornerstone of European economic decision-making.

World leaders agreed in the G20 meeting in Pittsburgh (September 2009) to promote "a strong, balanced and sustained world recovery" setting out a broad strategy for growth and employment through the ILO Global Pact on Jobs (2009). However, today the European Union is putting its economic recovery at risk.

During 2010, restocking and fiscal stimulus were driving the recovery. As both are being phased out, economic growth in Europe is shrinking from an already meagre 1.7% to 1.5% in 2011 (source: IMF). And without the export-led growth of 3.6% in Germany, European growth would have been only 0.6% in 2010. In addition, the turmoil of the sovereign debt crisis, with the Greek and Irish tragedies currently playing out and the increased spreads on the bond markets of a number of euro-area as well as other EU member states, has led to a systemic crisis of the eurozone and added to pre-existing concerns about the sustainability of the recovery.

Despite this economic reality, in October 2010, the Commission adopted a number of measures on the reinforcement of economic governance in the EU (and the euro area) with new enforcement mechanisms for non-compliant member states. Commission President Barroso had hoped to push these proposals rapidly through the European Parliament by summer 2011, negating proper analysis and scrutiny of key pieces of legislation. Meanwhile, the European Semester has already been launched with the publication of the Annual Growth Strategy in January 2011, changing the direction on European policy without democratic consent. As part of the European Semester, member states must start introducing their national reform programmes in mid-2011 following these policy lines.

For the EMF, the proposals of the Commission are of an unprecedented and extremely negative nature. They challenge the decision-making process of democratically-elected governments and intervene in national social dialogue and collective bargaining procedures. (The Commission has already intervened directly in Irish and Greek private sector collective bargaining processes, calling for substantial cuts in minimum wages.) The reinforced Growth and Stability Pact will give the Commission, the finance ministers and DG ECFIN new powers over national budgets and policies, including the power to intervene in policies where they have no direct competences: wage formation, collective bargaining, labour law and labour market policies.

For the EMF it is clear that the Commission considers the further deregulation of labour markets and wage cuts as the major tools to restore the stability of the euro and exit the economic crisis. This directly means the further weakening of workers' bargaining power and a direct reduction in economic security. This is not the way out of the crisis. Undermining income stability and shaking public (economic) confidence by making jobs more precarious, will result in a new contraction in demand and economic growth. For

some regions in Europe, this policy threatens a double-dip recession and significant social damage.

For the EMF the recovery is still too fragile. The process of de-leveraging in the financial sector, private sector and in individual households will take demand out of the economy for many years to come. Therefore fiscal retrenchment should be carried out in an extremely careful manner that is not based on 'slash and burn' policies.

The Commission's current proposals for a strengthened economic governance of the EU are not only undemocratic (direct intervention in national policies) and socially unacceptable, but they also risk pushing the European economy into a prolonged period of weak internal demand, which will generate massively pro-cyclical policies, with industry and jobs moving to other parts of the world where economic perspectives are brighter. Meanwhile, in early February 2011, German Chancellor Merkel and French President Sarkozy proposed a so-called 'Competitiveness Pact' for the eurozone, focused entirely on intergovernmental pressure on unit labour costs and further attacking workers and their collective bargaining autonomy, which is completely unacceptable for the EMF and European trade unionism in general.

Meanwhile, the situation is evolving quickly, with the Merkel/Sarkozy "Competitiveness Pact" redrafted through the proposals of the Barroso and Van Rompuy "EURO PLUS" plan. This latter plan may give the impression of removing some of the harsher elements from the initial Merkel/Sarkozy proposal. But while the attacks on wage indexation have been watered down in the Barroso/Van Rompuy plan, it puts wages in another strait-jacket by linking wage increases in every single member state to the wage developments with its main trading partners. Moreover, the plan urges the decentralisation of collective bargaining procedures (although the Commission has no competency in this area).

The EMF implores European politicians within governments and the EP to take the time to ensure that adopted policies are progressive, effective rather than destructive, and fully respect national and European industrial relations rights and systems underpinning the European social model.

The EMF is deeply concerned that combined fiscal and wage austerity will deflate the fragile recovery and potentially generate a new banking crisis, national defaults and the much-feared double-dip recession. This is not only devastating for individual workers losing their jobs, but makes it even more difficult for member states to reduce national deficits and debt levels.

### **Another way is possible: promoting sustainable recovery**

For the EMF the best way to reduce unemployment and economic deficits are growth-enhancing policies. Therefore, the main challenge for European economic governance today is turning the fragile economic growth into a self-sustaining long-term recovery. This cannot be done by coordinated fiscal contraction or European-wide wage and social dumping. At the same time, the EMF is aware that the financial crisis has exposed a structural problem of the eurozone, which is the imbalance between a centralization of monetary policy at the European level while the economic and fiscal policy instruments have remained at the national level. Greater attention should be paid to rebalancing this policy coordination ensuring effective European economic and fiscal policies. The EMF

insists on concrete and focused steps in the direction of a fiscal and economic union. Moreover, wage coordination must be further promoted, organised by trade unions according to the EMF norm (inflation plus productivity). Fundamental labour rights to free collective bargaining must be guaranteed throughout and by the EU (and beyond).

In order to develop a more balanced approach to economic governance, the EMF launches the following demands:

1. Credible medium-term plans for debt stabilization/reduction are needed but not the short-termist agenda of the Commission's proposals for making the Growth and Stability Pact more rigid. Imposing effectively automatic fines would violate the decision-making processes of democratically-elected governments and is practically unrealistic. In 2003, today's eurozone policemen France and Germany did not comply with the rules but simply refused to pay any sanctions. Moreover, there is a risk that ailing member states may not be able to bear the burden or have to transfer the bill to their population, causing even more hardship. Already now a number of member states are implementing the most extreme austerity programmes since the 1930s. Therefore, the EMF favours a long-term approach of fiscal adjustment, whereby purely mathematical deficit reduction is replaced by a cyclically-adjusted approach, as advocated by the IMF in October 2010<sup>1</sup>.
2. The launch of euro-bonds as a tool to finance sovereign debt while reducing the spreads in public bond markets, thus decreasing the cost of capital by using the creditworthiness of the EU as a whole and attracting domestic and foreign savings. Eurozone countries should be able benefit from lower rates of interest on euro-bonds to a debt ratio of 60% of their GDP to replace national bonds, with surplus countries able to exceed this limit (i.e. offering a means to attract this capital).
3. The launch of a European 'Marshall Plan': a coordinated investment programme which mobilizes savings surpluses in Europe by means of eurobonds, to modernize European infrastructure, develop transnational networks and promote sustainable development. The 3% criterion should be renegotiated. Public spending for investments which in principle pay themselves back could be excluded, while the limit for deficit on public consumption could be reduced towards zero. Policies to leverage greater industrial investment in Europe must be addressed urgently.
4. An industrial policy able to develop new engines of growth and to create new jobs through the promotion of industries, sectors and market niches with activities that contribute to the objectives of sustainable development in sectors such as healthcare, energy efficiency, renewable energies, key enabling technologies, etc. with high technological content and high-quality employment. In this respect, the EMF largely welcomed the Flagship Initiative on 'An Integrated Industrial Policy for the Globalisation Era: Putting Competitiveness and Sustainability at Centre Stage'. The Initiative confirmed the pivotal role of industrial policy in European decision-making. However, an industrial policy can only be successful if it is supported by a macroeconomic policy that also supports growth and jobs. Today this is not the case in Europe.

<sup>1</sup> The IMF stated in its Economic Outlook of October 2010 that "One of the most urgent challenges for advanced economies is to legislate plans that help achieve sustainable fiscal positions before the end of the decade..."

5. The 'relaunched' internal market must be accompanied by a social level-playing field to avoid social and wage dumping (e.g. the respect of core labour standards and setting basic social standards, guidelines on and support for high coverage rates of collective agreements and safeguards for national collective bargaining systems) and halting the deregulation of the labour market to limit the exponential rise in precarious work (e.g. making temporary agency work more expensive, limiting the use of atypical contracts, banning below-standard contracts, etc). 'Improved job quality' should be included as an overall indicator of success for the Europe 2020 strategy.
6. To restore macroeconomic imbalances a focus on direct and indirect labour costs alone cannot rebalance the eurozone. European metalworkers are totally opposed to all wage competition. Moreover, the EMF is totally opposed to deflationary wage policies and pay cuts. These will only intensify the current crisis and depress consumption and social standards in Europe. Wages must increase in line with inflation and productivity. The burden should not only fall on deficit countries but also on surplus countries. Thus both should actively promote internal demand and public investment. The EMF calls for additional social indicators in the scoreboard for the excessive imbalance procedure, for instance on: inequalities, the incidence of low pay, the working poor, the share of labour income in overall GDP and unit profit rates.
7. A better distribution of wealth and income in our societies is essential to achieve sustainable growth as it will increase the propensity to consume and reduce the excessive savings which provoked the original asset bubbles. To achieve this, the lowest incomes have to be addressed on the one hand (where appropriate this can happen through minimum wages, whether statutory or through collective agreement), while stronger policies have to be enforced to fight fiscal fraud and tax evasion, promote progressive taxation policies and shift the tax burden from labour to capital. The EMF calls on the ETUC to launch a substantive campaign tackling low pay and minimum wages in Europe.
8. Proposed changes to pension systems and the automatic increasing of retirement age in line with average life expectancy must be reconsidered. For the EMF, any adjustment of the retirement age should be discussed with social partners and not by automatic mechanisms.
9. Corporate taxation policies must be addressed. A common base and minimum rate for company taxation are also urgently needed in Europe to halt internal fiscal competition for investments.
10. The maintenance of a poorly-regulated and badly-supervised internal market for capital, without harmonisation of taxes on capital, has aggravated the financial crisis in Europe. A banking sector which creates tremendous wealth for a limited few but which brought millions of ordinary people into hardship has no social and political legitimacy. Although much legislative work has already been done to implement de Larosière and G-20 recommendations for financial reform, more has to be done to build a financial system that serves the real economy not vice versa. The EMF particularly insists on:
  - the introduction of a financial transactions tax which will generate revenues for public budget consolidation/investments;
  - tougher policies on tax havens in order to implement the G-20 declaration (London summit, April 2009);

- strict regulation of the non-transparent derivatives markets (e.g. bans on short selling, central clearing facilities) required to shrink the highly speculative shadow banking system;
  - a resolution mechanism for ailing banks to avoid that workers will pay again in the future for the mismanagement and risk-taking in the financial sector;
  - as banks remain unwilling to expand credit, additional measures to promote access to finance are required (guarantee systems, promotion of venture capital);
  - encouragement of long-term investment strategies, e.g. by making voting rights and dividends dependent on the length of the time for which shares are held;
  - a deeper analysis of the high returns in the financial sector and their impact on the real economy (Exaggerated risk taking? Privileged access to information? Anti-competitive market structures?).
11. To complete the internal market, Europe needs the construction of a developed and functioning industrial relations system covering social, health and safety, economic and vocational training policies, including at its core macroeconomic governance structures in which the European social partners play an active role. Negotiated solutions should be promoted at the European level, as well as nationally, to ensure the improvement of living and working conditions.

For the EMF, economic governance should be about promoting growth and not about imposing deflationary adjustments and simultaneously applied austerity policies. It is also about more and better jobs and not about dismantling social protection and welfare states. The EMF deeply regrets that the Commission is abusing the financial crisis to undermine Europe's 'social acquis'. It also regrets that the Commission has put fiscal tightening at the centre of its policies while it is clear that this will jeopardize the economic recovery, prolong the sovereign debt crisis and push the EU back into the recession it has only just left behind. As a result of the multiple failures of the political establishment to tackle the social instability caused by the crisis, there is increasing alienation amongst European citizens towards established political forces in the member states and on European level. Europe needs more joint projects for the future. It needs projects which people can become committed to and be inspired by. The EMF will undertake all efforts to ensure this is realised, including:

- **A call to EMF affiliates to mobilise in order to oppose measures that promote ever greater austerity and undermine collective bargaining in Europe.**

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## **Background information**

### **The Commission's medicine**

The Commission's proposals aim to solve the crisis in the eurozone on the basis of a reinforcement of the Stability and Growth Pact, the introduction of an Excessive Imbalance Procedure, the launch of a European Semester on economic governance and the creation of a permanent bail-out mechanism for indebted states, more specifically:

- The launch of a new concept of 'prudent fiscal policy-making' in good times (by which the expansion of public expenditure should not rise faster than the 10-year average GNP), with increased powers for the Commission to issue warnings in the case of deviation.
- The national debt criterion of 60% of GNP has been put on an equal footing with the deficit criterion. Member states will be required to reduce the gap by 5% of the difference with the 60% threshold. Consequently, those countries with a deficit lower than 3% of GNP may still be put into an 'excessive deficit' procedure if public debt is over 60%.
- Tightening the sanctions regime for the eurozone in case of deviation: from interest-bearing to non-interest bearing deposits (up to 0.2% of GNP), which can be converted into real fines. The sanctions regime will also be almost automatically imposed (the so-called reversed qualified majority rule in the Council - only a qualified majority can stop procedures/sanctions).
- Introduction of an Excessive Imbalance Procedure as a tool for macro-economic surveillance. The procedure consists of an Alert Mechanism based on a scoreboard (with indicators as current account positions, unit labour costs, inflation...). Thresholds will be defined so as to formalize from which level imbalances are potentially harmful. For eurozone countries that are not in line, sanctions can be imposed (yearly fines of up to 0.1% of GNP).
- Introduction of a European Semester – from January 2011 onwards – as a cornerstone of economic policy coordination and to set European-wide fiscal policy. The semester starts in January with the Annual Growth Survey by the Commission. In this document the main challenges facing the EU are identified. The member states will have to integrate the recommendations of the AGS into their national Stability Programmes (on budgetary policy) and National Reform Programmes (on their EU 2020 strategy), which they have to send to the Commission for assessment by April. Finally, the Council will issue policy recommendations by summer which the member states will have to introduce in their budgets and national reform programmes.
- A permanent bail-out mechanism (the European Stability Mechanism) to replace the European financial stability facility (which was set up in May 2010 to deal with the current eurozone crisis and expires in 2013) so as to provide emergency financial assistance to a Member State that cannot service its own debt.

As a result of the new 'European Semester', in January 2011 the Commission published its first Annual Growth Survey. In this document the Commission has set out 10 priority actions. Amongst them:

- Implementation of a rigorous fiscal consolidation: 'Therefore, stronger consolidation is needed and should be implemented on the basis of the reinforced fiscal rules proposed by the Commission'.

- Correcting macro-economic imbalances whereby deficit countries should present corrective measures: 'these could include strict and sustained wage moderation, including the revision of indexation clauses in bargaining systems'.
- Reforming pension systems: "Member states that have not already done so should increase the retirement age and link it with life expectancy" and "MS should reduce early retirement schemes as a priority".
- Getting the unemployed to work: "MS should design benefits to reward return to work ... through time-limited support"
- Balancing security and flexibility: "Such employment protection legislation should be reformed to reduce over-protection of workers with permanent contracts"

While it is true that growth-enhancing measures are also proposed, they are clearly lacking ambition. The proposals under the headings 'Tapping the potential of the Single Market', 'attracting private capital to finance growth' and 'creating cost-effective access to energy' cannot be considered as a comprehensive strategy to promote growth and jobs.

Early in February, the French President and German Chancellor produced an alternative proposal based almost exclusively on unit labour cost developments in the eurozone, and by extension the EU as a whole. This was a highly controversial step, which backfooted the Commission and other member states and totally sidelined the European Parliament. Consequently, at the end of February 2011, the Presidents of the Council and Commission produced their alternative "EURO PLUS" plan, marking acceptance of the Franco-German logic and an attempt to retake the agenda. The key objectives of this pact are defined as follows:

- To foster competitiveness, notably through the alignment of wage and productivity developments
- To foster employment by making work more attractive
- To contribute further to the sustainability of public finances, notably as regards public debt as well as pensions and social security systems
- To reinforce financial stability.

Progress will be assessed on the basis of wage and productivity developments. Unit labour costs (ULC) will be monitored over a period of time, by comparing them with the developments in other euro area countries, and in the main trading partners. Particular attention will then be given to measures to ensure costs developments in line with productivity, such as the review of the wage setting arrangements to enhance decentralization in the bargaining process, improved indexation mechanisms and wage restraint in the public sector. This marks a hardening of the Commission's proposals and goes beyond the Annual Growth Survey.

### **Pushing Europe and workers to the brink of the abyss**

It should be clear that the EMF is in favour of better economic coordination to support monetary union. Indeed, for a monetary union to be successful, it needs to be completed by an economic union. Close coordination of national economic policies has to complement the single currency and the single central bank. However, the question is how the objectives and methods of this coordination are defined.

Furthermore, the EMF does not agree with the strong focus on dramatically reducing public debt to solve the crisis. Indeed, according to the IMF a fiscal consolidation of 1% of GDP tends to reduce real domestic demand by 1% and GDP by 0.5% over 2 years.

The public deficits are the results and not the cause of the financial crisis. It was the fact that the debts and losses of the financial sector were 'socialized' (because bank debts were implicitly guaranteed by governments) and the increase in social spending (the so-called automatic stabilizers) that turned the financial crisis into a Great Recession and not, as in the thirties, a Great Depression.

It is immoral to see that the financial sector, after having been saved by governments and taxpayers (to the tune of € billions), turned against its saviours by speculating on sovereign debt defaults and imposing high interest rates to teach 'bad' governments a lesson, thereby causing a systemic crisis of the eurozone. Due to these exceptional circumstances, it has been impossible for member states to stick to the rules of the Stability and Growth Pact. As a result, fourteen countries are running a debt of more than 60%. The average debt of the EU was 79% of GNP in 2010 (which is 20% higher than in 2007), while the EU average deficit was 6.8%. It must be stated clearly that it was not fiscal irresponsibility that created the current crisis of the eurozone but asset price bubbles, speculation and irresponsible behaviour in the deregulated financial markets.