Europe: Prisoner in the euro straitjacket

by Lothar Komp

The new left-wing majorities in Bonn, Paris, and Rome let not a day go by without pulling at least one new proposal for job creation or for fighting the global financial crisis out of their hats. The background of this rhetorical activism of European governments is the self-imposed impotence of trying to act effectively against mass unemployment and other economic disruptions, under the conditions of the European Monetary Union (EMU). At just the time that national sovereignty in economic questions is more urgent than ever, the scheme is to surrender this sovereignty to a supranational institution, whose sole purpose is to secure the stability of currencies. As long as the Schröders, Jospins, and D'Alemas do not summon up the courage to liberate themselves from this euro-compulsion, which they are complicit in bringing about, Europe will plunge further into the depths of economic depression.

For example, the tensions between the new government in Germany and the Bundesbank (German central bank) manifest various levels of insanity. The reduced interest rates now demanded by German politicians, are supposed to bring about a mysterious recovery of the economy, without changing anything in the failed system itself. The central bankers, on the other side, are resisting such moves in a futile attempt to defend the stability of the currency, which is already a pure fiction.

'Multiple personality disorder'

Lyndon LaRouche appropriately characterized the current state of mind of European governments as "multiple personality disorder." That aspect of the psychosis which is immediately related to the euro, the European single currency, leads to fatal miscalculations, the consequences of which can be summarized in six points.

1. The obsession with the euro blocks the fundamental reform of the international financial and monetary system.

The world financial system is at the brink of total collapse. Since the Russian debt moratorium in August and the collapse of the Long-Term Capital Management hedge fund in September, a meltdown in stocks, bonds, and financial derivatives has dramatically worsened the positions of the largest banks and funds. No one knows how many off-balance-sheet corpses have piled up in the cellars of the banks. The next financial catastrophe of significant dimensions could unleash a chain reaction, leading to the implosion of $150 trillion of paper values in the derivatives bubble. In Asia, ever-more governments are turning to resolute measures to regulate the financial markets, in order to protect national economies from the collapsing ruins of the world financial system, and they are demanding a return to a worldwide system of fixed exchange rates. In Japan, such measures are no longer seen as "heretical," as Vice-Minister for Finance Eisuke Sakakibara recently asserted.

But in Europe, heads are still in the euro-clouds. In Germany, it suddenly seems as if it is only strictly loyal Social Democratic Party comrades, indoctrinated by Finance Minister Oskar Lafontaine, who still believe that the euro will have a stabilizing effect on the world financial system. The swings of the euro with respect to the dollar and the yen are supposed to be brought under control with agreements; there ought to be a bit more transparency and supervision of banks and hedge funds, and then everything will come back to an even keel, they imagine.

2. The euro will not protect us from the effects of global financial catastrophes.

The problem for European exporters today is not the fluctuations of exchange rates within the EMU, but the abrupt shifts between European currencies, on the one hand, and with the dollar, as well as the collapse of currencies unleashed by speculators acting against the currencies of countries such as Russia, Indonesia, or South Korea, which results in the sudden loss of entire export markets, on the other. The EMU changes nothing at all about such phenomena.

Should the euro be targetted by currency speculators, one important matter to consider is that the European Central Bank will be equipped with relatively limited reserves of gold and foreign exchange, i.e., some 100 billion deutschemarks (roughly $60 billion), whereas the German Bundesbank today alone accounts for DM 133 billion. Following the successes of international financial speculators in 1992 and 1993 in forcing European central banks to their knees, their war treasuries, due to the financial leverage of financial derivatives, among other factors, have grown immensely.

The conclusion from this fact is: It is not the euro which represents any protection, but only the reliance upon defensive measures such as those available to governments in western Europe until 1958, during the most successful phase of the Bretton Woods system: capital controls and limited convertibility of currencies.

3. The euro significantly exacerbates the danger of a European banking crisis.

On Oct. 12, the *Wall Street Journal* published a warning about "the coming credit crunch," authored by Jean-Michel Paul from Rabobank. Paul pointed out that it is the European banks which hold the lion's share of the outstanding loans in Asia, Russia, eastern Europe, and Latin America, and so these are the banks which will be hardest hit by coming financial shocks. Banks within the territory of the European Union

© 1998 EIR News Service Inc. All Rights Reserved. Reproduction in whole or in part without permission strictly prohibited.

account for 68.5% of these credits, which amounted to $924 billion at the end of 1997, according to reports of the Bank for International Settlements. Paul claimed that it is estimated that 30% of these credits cannot be paid back. Even if 15% of the credits are already written off or are covered by state guarantees, the "optimistic" scenario would entail losses of $140 billion, which would come out of the capital of the banks. Since, on average, $10 of credits are issued for each $1 of capital, this would amount to a forced contraction of the credit volume by some $1.4 trillion. About two-thirds of that contraction would hit European banks.

In addition to a dramatic contraction of credit to the European economies, this also entails a markedly increased potential for the collapse of large banks in Europe. The European Central Bank is not at all prepared for this, precisely because it is almost exclusively oriented to currency policy, and is conceived to have only a limited role in supervision of banks. It lacks the information necessary to recognize risks involving particular banks in advance of a crisis. There is no institution in the context of the Maastricht Treaty which can function as a "lender of last resort," i.e., as a financial fire-brigade capable of providing emergency liquidity. This means that the national central banks—which have been weakened in the meantime—will have to jump into the breach. And what will happen if some bank, which has emerged as a conglomerate of European banks, of uncertain nationality, which will soon be a rather frequent phenomenon, gets in trouble? By the time the proper channels of responsibility are clarified, a chain reaction could well have begun to occur.

How to create jobs

4. Simply lowering interest rates does not create a single job.

Short-term interest rates today are at record lows in all leading industrial countries—the United States, Japan, and Europe. This policy was obviously not very effective in reducing mass unemployment. In view of the nature of the present world financial system, this is not surprising. Additional liquidity, pumped into the system by lowering the discount rates, does not lead to an expansion of credit lines to enterprises in the real economy, which would take the credit to invest and create new jobs. Instead, since summer of 1995, the printing presses of the central banks have been running at full capacity in order to postpone the unavoidable collapse of the worldwide financial pyramids by glutting the system with massive volumes of liquidity. In Japan, with an interest rate of 0.25%, banks can procure liquidity at the central bank and invest the money in high-interest, speculative markets. These volumes are supposed to be stocked up by an additional roughly $500 billion from the taxpayers. As part of the same process, the domestic credit volume of Japanese banks has contracted drastically and unemployment is soaring. This sort of "crisis management," which is hyperinflationary over the short or longer term, is exacerbated by International Monetary Fund "rescue" packages. There is only one solution: a global bankruptcy proceeding for the financial bubble, which cannot be salvaged in any case.

5. The euro prohibits the creation of millions of productive jobs by means of national bank credits.

According to orthodox British economic theory, credit creation can only take place from the central banks via private banks, where the latter see to it, out of their own interest, that the money is invested where it be the most useful for the entire economy, so that no "misallocations" arise. The events of the recent years—from the $2 trillion of bad debts of the Japanese banks, down to the abortive adventures of large European banks with "hedge funds" and financial derivatives—have refuted this nice theory. In times of economic emergency, direct credit creation for infrastructure and technology projects which increase productivity, as outlined in the notion of national banking which goes back to U.S. Treasury Secretary Alexander Hamilton, is indispensable. By means of such credit creation, millions of jobs could be created in Germany and other European countries immediately, for example by building the trans-European railway network, or the far more ambitious plans for the Eurasian Land-Bridge. Maastricht explicitly prohibits such a possibility. Article 104 of the treaty reads:

"Overdraft and other credit facilities at the European Central Bank or the central banks of the member countries (in the following termed 'national central banks') for institutions or authorities of the community, central governments, regional or local governing bodies, or other public institutions, other institutions of public law or public enterprises of the member states are forbidden, including the incurring of titles of debt by these through the European Central Bank or other national banks."

6. Green Keynesian gibberish destroys jobs.

Let us imagine, despite all the constraints imposed by the euro, and despite the lack of willingness to create a new, functioning world financial system, that the German government were to succeed in drumming up a few billion deutschemarks for employment programs. Under the prevailing ecologist/anti-technology policy direction of the new government, it would have no effect at all. What is completely lacking here is a comprehension of how investments in public infrastructure and revolutionary technologies can unleash an increase in productivity, which then, by means of creating new branches of economic activity, leads to the creation of genuinely new jobs. What chemistry and electrical engineering were at the end of the 19th century in this respect, space technology and nuclear technology could be today. Instead, even the Transrapid maglev train is threatened with mothballed, road and rail projects are being blocked for "ecological" reasons, and enterprises are weakened further by the deliberate increase of energy and transportation costs. This policy will actually destroy jobs on a massive scale.