European Trade Union Confederation (ETUC)
Confédération européenne des syndicats (CES)

URGENTLY WANTED: EUROPEAN LEADERSHIP TO FIGHT THE NEW DEPRESSION

ETUC Declaration to the European Spring Summit of March 2009

PART I: What we are facing: A Recession turning into a Depression

1. Economic forecasts are bad and even getting worse. Whereas the January Commission forecast expected the European economy to shrink by 2% in 2009, most recent forecasts refer to a recession of minus 2,7% (ECB) or even a collapse in economic activity up to minus 5% in the case of individual member countries. Unemployment will rise fast in coming quarters and will reach more than 10% by 2010.

2. The economy is caught in a downwards tailspin and things will continue to deteriorate if policy makers do not act adequately to halt this tailspin. Here are the seven downwards spirals at work to turn the recession into a new Great Depression:

    a. **Economic recovery plans**: Too little to prevent mass redundancies. With the impact of the fiscal expansion on 2009 growth limited to 0,5%, and compared to a deficit in aggregate demand of 4%, the Recovery plan falls substantially short of the policy response that is required. The European Recovery plan will therefore not prevent the recession from hitting the core work force of companies in coming months. Massive restructuring will feed back in the economy and strike another blow to demand and economic activity.

    b. **A second wave of financial meltdown could be in the pipeline.** The economic recession will lead to an increase in default rates on mortgages and corporate loans. International accounting standards will force banks to adjust downwards the rating of these loans in their books. As a result, a new imbalance between banking assets and banking capital will appear. Banks squeeze credit even further and finance to support economic activity will become even more rare: The scenario of Autumn 2008, where banks squeezed credit in reaction to the losses on securitised bonds, may be about to repeat itself.

c. **The Stability Pact all over again.** Public deficits are exploding and the 3% threshold will be breached. If fiscal consolidation strategies are set up from 2010 onwards, public deficits would be cut at the exact moment the economy is in this still in the doldrums and cooping with the fall out from the second wave of credit contraction (see above). The consequences of fiscal contraction for an economy that is already weakened will be disastrous.

d. **Europe being torn apart by financial markets….** Many Central and Eastern European countries face difficulties in accessing capital markets. In the process of rebalancing assets with capital, Western European bank headquarters are cutting credit flows to their bank subsidiaries in Central and Eastern Europe at a time the region is estimated to renew finance at a rate of 200 billion a year. On top of this, financial markets are specifically targeting government bond markets and even euro area members are now confronted with soaring interest rate spreads with German bonds. The perverse self fulfilling prophecy of financial markets is back at work: High interest rates undermine public finances, thereby seriously limiting member states' leeway to stabilize the economy and in the end actually triggering the default the market fears.

e. **…with the IMF, being backed by European funds, destroying the Social Model in Eastern Europe.** If Europe leaves more vulnerable member states outside the euro area exposed to the vagaries of financial markets, then those member states will have no other choice but to turn to international financial institutions, in particular the IMF. However, the track record of the IMF is well known: In exchange for foreign currency loans, countries are forced to cut anything that is social: wages, social spending, workers' rights, public services. Moreover, access to the Commission's 25 billion euro balance of payment fund is conditional upon respecting the IMF adjustment program. European funds are being used to help the IMF to cut down the social dimension in Europe. For the moment, IMF lending to European member states is limited to Hungary and Latvia but the risk is that the usual herd behaviour of financial markets would spread contagion throughout the region.

f. **Protectionism and the internal market.** A return to protectionism will certainly not solve the crisis and the ETUC opposes such a course of action. The ETUC therefore regrets that some decisions, taken under pressure from the business lobby, risk creating de facto internal market distortions. By allowing credit guarantees to companies up to the entire wage bill of the company, the level playing field between member states with higher margins of fiscal action or access to capital markets (see above) may be distorted and there is the danger that not all member states can help their industrial basis to survive the credit squeeze. Moreover, whereas these measures improve business' access to finance, there is no guarantee that business will not use this finance to cut the core work force while continuing the culture of corporate greed (pay out super dividends or CEO bonuses) instead of investing.

g. **Wage cuts: Be careful what you wish for.** A collapse of wage dynamics would be another contribution to the making of the New Depression. Contrary to the idea that wage formation in Europe is rigid, the risk is that wages actually react too forcefully and in too flexible a way. A recession of minus 2% will seriously weaken the bargaining position of workers and drag wage dynamics down. If the relationship of the past between wage dynamics and economic crisis holds, a collapse of wage dynamics to a rate of growth close to zero cannot be excluded. The danger is that this would tip over low inflation into zero inflation or even deflation, thereby causing a rise in real interest rates. Rising real interest rates in the midst of a recession and against a background of excessive private sector debt loads will trigger yet another round of the downward spiral. Debt deflation, similar to the 1930's, is on the cards.

Part II: European leadership to guide the markets and fight the New Depression

3. To avoid the New Depression from unfolding, we urgently need real European leadership. We need European leadership to organise a European answer to the collapse of employment and economic activity instead of leaving member states to face this on their own. We need European leadership to provide member states with the financial means to fight the crisis and its social consequences. We need European leadership to fight financial markets' liberal bias and to prevent financial market speculation from turning into a self fulfilling prophecy. We need European leadership to stop rigid rules (international accounting standards, Basle II capital requirements, stability pact rules) from continuing to inflict serious damage on our economies. We need European leadership to level the playing field for the internal market and avoid protectionism and social dumping.

4. To halt and reverse the downward tailspin of the European economy, the ETUC urges the Commission and the European Spring Council to develop European leadership by deciding on the following lines of action:

5. **Invest in Social Europe**: The European Labour Market is flexible but not secure. Workers are suffering mass redundancies while their rights to robust unemployment benefits have been hollowed out by years of structural reforms and widespread precarious jobs practices. The ETUC demands a New Social Deal, designed by social dialogue and appealing to employers, member states and the Commission to take up their responsibilities in order :

    a. To strengthen and broaden unemployment benefit systems, accessible to all, in particular to workers in precarious contracts.
    b. To invest massively in skills and lifelong learning as well as in direct job creation in the social sector.
    c. To offer young people entering the labour market in 2009 a guarantee on a job or training.
    d. To change the governance of companies in order to rebalance the position of workers and the social dimension in the strategic choices of companies.

6. **Invest in an expanded recovery programme**: The downturn is structural. The private sector will not spend or invest much in coming years but will be driving down its excessive debt loads instead. The economy needs a new driver for growth and jobs: Public sector led investments in the greening of the European economy. The ETUC demands the Commission and the Council to launch a new program of European investment projects with a value of 1% of European GDP. This new investment program is to focus on areas of renewable energies, clean technologies, European infrastructure and networks, modern cars and cleaner transportation systems. To avoid 'free riding' or 'window dressing' from national members, to focus efforts and to develop possible cross border synergies, the European level itself needs to undertake this investment effort.

7. **Public money for public investment**. With the public sector called upon to rescue the economy from the meltdown of banks and businesses, governments need to mobilise the financial means to do so. The ETUC demands:

   a. the Central Banks in Europe (to the extent they are not already doing so) to buy up public debts backing up public investments, thereby proving low cost and stable finance for governments. It is necessary to do so because central banks have almost reached the zero bound on interest rates and now need to start using the weapon of quantitative easing of monetary policy. It is also possible to revert to a policy of printing money because it is the spectre of deflation, not inflation, that is looming.

   b. the European Central Bank (ECB) to fight financial markets speculating against euro area members and to privilege the buying of those bonds showing excessive spreads with the German bond. In addition, issuance of a eurozone bond needs to be examined.

   c. to attach strict conditions making sure excessive dividend pay outs, capital buy backs and CEO golden parachutes can never again undermine companies' balance sheets in those cases where public money is used to bail out private companies.

   d. to stop tax competition to undermine the revenue basis of public finances. We need a European agenda to attack tax havens, zero or near zero taxes, flat tax regimes and to work closer on corporate profit tax, capital gain tax, taxes on high fortunes. A financial transaction tax should be given serious consideration.

8. **European solidarity to protect all of us against the irrationality of financial markets.** Financial markets were dead wrong when providing triple A rating to US toxic assets. We should not trust these same financial markets to speculate against governments and currencies and thereby ripping the European economy apart. The ETUC demands:

   a. To give a strong signal to financial markets keen on betting against Central and Eastern European currencies by immediately raising the Commission's balance of payment fund from 25 to 100 billion euros.
   b. To ban the IMF and its structural (mis)adjustment programs from Europe and link instead financial support of member states with European Social Model principles including the principle of distributive justice with robust workers' rights and fair tax systems in which the 'strongest shoulders carry the strongest burden'.
   c. To increase European social spending in order to enlarge the activities of the European Social Funds and the European Globalisation Fund, implying a substantial increase in the European budget itself as well as the introduction of the European level taxes, for example by developing a tax on financial speculation or a tax on super dividend pay outs.

9. **Flexibilising rigid rules.** The mixture of international accounting rules, Basle II capital requirements for banks and on top of this a Stability Pact constraining public investment at a time the public sector is the only actor able to go against the tide of debt de-leveraging provides for a lethal combination. It is urgent to stop this cycle of pro-cyclical madness and to stop it in time before even more serious damage is done to the jobs and the economy. The ETUC demands:

   a. To amend or apply the European Directive on banking capital requirements in order to allow banks to use accounting standards based on 'long term fundamental value' rather than on short term market value.

b. To use the full flexibility provided by the reformed Stability Pact: Decide that investing in recovery and a greening of the economy is a structural measure allowing a temporarily higher deficit. Make clear that public finances need to be consolidated from the moment the level of economic activity reaches its potential again and not a moment sooner. Europe can not cut its way out of debt deflation, Europe needs to grow out of debt.

10. **Common principles for wage policy in a time of depression.** Wage moderation is part of the problem. Wage moderation caused economic policy to rely on excessive debt loads to keep the economy going despite rising inequalities and a systematic redistribution of the benefits of growth from labour to capital. We can no longer continue with this perverse logic: If workers in Europe are forced to continue to undercut each others' wages, low inflation will turn into deflation, real interest rates will rise and the recession will intensify. The ETUC demands:

    a. A European framework for 'fair and decent' wages. In the context of the European Employment Strategy, Member states, together with the national social partners, should be invited to conduct policies and collective bargaining establishing a strong downwards floor in wage dynamics in order to avoid deflationary wage developments and obtain higher wages instead. This implies wage floors at the bottom of the labour market as well as respecting the 'going wage rate' and wage increases as set by collective bargaining agreements.

    b. European action to ensure 'equal treatment and equal pay for equal work for posted workers. Market freedoms can no longer be allowed to take priority over fundamental rights and collective agreements. This implies an overhaul of the posted workers' directive as well as a Social Protocol to be attached to the European Treaty.

    c. A European wide crackdown on excessive CEO bonuses, remuneration, stock options and golden parachutes as well as on super dividend pay outs and capital buy-back operations.