TRANSCRIPT

"Change of Direction," IG Metall Conference – Berlin, Germany

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[Begin]

My friends, it is a pleasure and honor to be asked to speak to you this morning. And I want to begin by congratulating you for taking up a theme that I think is a common theme around the world – the idea of the good life.

I suppose I first encountered this theme a year or so ago at a meeting to discuss the future of development in Ecuador. And it reflects a little bit of the concerns my father had late in his life when he wrote a book entitled, "The Good Society."

I think it is a right and resonant theme for the future as we grapple with the problems that we face today. But first we must indeed deal with these problems —with the dark matters and imminent dangers that are before us now. And so I will focus my remarks on the first two words in the title of this conference, the question of changing course.

Five years ago when the great financial crisis broke into public view, those who claimed falsely that no one could have predicted it also claimed that our economies would recover. Standard forecasts foretold rapid growth and high employment within five years. Banks in America would start lending again. Confidence would return in Europe. Those of us who said no, that there would be no return to normal, were for the most part ignored. Yesterday we heard Professor Nouriel Roubini give a magisterial and very high speed tour of the world situation making it clear of course that the promised recovery has not occurred. But if Nouriel is Sir Isaiah Berlin's fox, who knows many things, let me try this morning to be the hedgehog who knows one big thing, and that one big thing is that what we are experiencing is a single, unified, global crisis of the economy and of the financial system. It is not a cluster of distinct and separated events; a subprime crisis in the United States; a public debt crisis in Greece; a bank crisis in Iceland; a real estate bust in Ireland and Spain; nor are there distinct U.S. and European crises, nor can the financial be separated from the real, nor is Germany a country to which crisis has not yet come with the suggestion that there might be some separate way out. There is one crisis, only one crisis, a deeply interconnected crisis of the world system. This crisis has, I think, three deep sources going back not twenty years but forty years to the early 1970s and the end of what we sometimes call the "golden age," the "glorious thirty" years in the immediate aftermath of the second World War.

The first of the three deep sources is, I think, the rising real cost of the resources that we use, of energy and of everything that we use energy for. This was a problem that emerged in the 1970s and was then submerged again; it was deferred by new discoveries, by the geopolitical situation, and by the financial power of the western countries, which because of the debt crisis in much of the rest of the world had the effect of suppressing demand for these core resources. But this is a problems that can no longer be avoided or deferred. The cost of energy is roughly twice of what it was a decade ago and the future is far more uncertain. Both of these factors, cost and uncertainty, place a squeeze on the surplus or profitability in regions, continents, and countries that are importers of these resources. And as we confront, as we must, the problem of climate change and as we begin, as we must, to pay the price of climate change this problem is going to become more difficult. That's just an economic reality that we have to cope with as we face the imperative before us.

The second great underlying issue it seems to me is technical change, the particular character of which in our time is quite different from what is was before. If you take the digital revolution together with globalization, the ease of transnational manufacturing and also to some degree the outsourcing of services, we find we live in an era where technology is radically labor-saving. It supplants workers. One thing that we can say without too much exaggeration is that the computer and the many associated technologies that have derived from it are now doing to the office worker what a century ago the internal combustion engine did to the horse.

And the third great source of our problem is ideological. It is the neo-liberal idea that has given us deregulation and de-supervision; that has given us the notion that markets can function on their own without breaking down or blowing up. It is this notion as applied especially to finance. This is the great illusion of the last generation, and it fostered a form of economic growth that was intrinsically unstable and unsustainable. Why? Because it was based on declining standards for loans and on lax accounting of the proceeds of those loans. Or to put it in simple terms, it was based upon financial fraud, on the most massive wave of financial fraud that the world has ever seen. And the world has seen a lot of financial fraud. It was known to be such to the lenders at the time. This was true of housing loans in the United States made by the tens of millions that were known to the lenders as "liar's loans," as "ninja loans," no income, no job, no assets; as “neutron loans” destined to explode leaving the building intact but destroying the people. This was known at the time. These were loans that had to be refinanced or they would default.

It was also true of loans to the public sector, for example Greece. The fact that Greece had a weak public sector and a weak tax system was not a state secret before the crisis. It was something that was known on both sides of these transactions. This was equally true of commercial real estate in Ireland and of housing in Spain. You simply had to go and observe what was going on. Not to mention the acquisitions of the Icelandic Banks. It’s a fundamental fact, I think, that’s visible everywhere you look but not spoken of in polite society especially when economists address audiences of bankers. I trust you will indulge me since I am addressing an audience of unionists and friends and speaking this frankly to you, as I think it is very important.

Rising inequality is often linked to these phenomena. But I think we should be clear about what the linkage is. It is not the case that inequality rose and people compensated for it by borrowing more so they could have a higher standard of consumption. This is not what happened. It certainly did not happen in the United States. What happened was, is that the lenders went out to find new markets often fostering fraudulent loans on low-information borrowers, poor borrowers, inner city home owners, for example, forcing those loans to be refinanced so that the recipient only saw a fraction of the debt with which they were ultimately saddled. And the inequality arose from the booking of fees on those loans. This is how bankers get rich. They make their money in this way. And you can see this in their tax statements and you can see it in the geographical distribution of income gains in the United States.

And when the extent of the fraud could no longer be concealed then there was panic and collapse. This happened both in the United States and Europe and it did damage to the financial structure that was, let me suggest to you, essentially irreversible. It destroyed the underlying basis for economic growth that had sustained us for some time. That is to say it destroyed the housing finance market in the U.S. and it destroyed the sovereign credit market in Europe. And because in Europe it destroyed the sovereign credit market, the effects fell on public services and on dependent populations. Millions of jobs of course were also lost in both continents. That was the collateral damage.

These matters have not gone away. And if you wish to ask why we did not experience the predicted recovery over the last five years, I think the answer is because they didn't go away and will not go away.

So we need to ask, how do we deal with them? And the basic choice is between two principles. It's between all-in-it-together or everyone-for-themselves. That's the choice. So while all of the wealthy resource-using, computerized finance-capitalist economies have been hit by the same forces, they have not all been hurt in the same way. The institutions that are available do matter, they have an effect. Here I want to say something you may find surprising, which is that actually my country, the United States, has enjoyed a certain advantage.

And what was it? People have often said that the U.S. has a flexible labor market. This was not it at all. In the United States real wages did not fall in the crisis, actually in the first year they went up. Labor markets did not adjust. We did not restore employment. The employment population ratio was five percentage points lower than it was a decade ago. No, what happened in the U.S. was something quite different.

This is actually my real voice, I'm not sure water will do any good. [Laughter]

What happened in the United States was that we had a very flexible and effective system of public transfer payments which rose rapidly in the crisis. Unemployment insurance, early retirement under social security, disability, lower tax collections, and then on top of that, the expansion package, the stimulus package, the Keynesian policy that came into effect very quickly. And these things broke the fall in incomes and preserved living standards to a very substantial degree.

Now this was also true in parts of Europe as it was I'm sure here. The automatic stabilizers came into effect. It was true in northern Europe. I was in Finland two days ago and they said basically they had a large fall in output but no fall in income. But it was not true everywhere in Europe.

And the second key fact lies in the difference in the underlying debts. In the United States these were largely private debts. And private debts are either paid down -- mortgages are amortized – or they are defaulted, in which case people have to leave their homes but they leave their debts with their homes. They are not pursued afterwards by and large. In one way or another, those debt problems are resolved over time—painfully—but over time they tend to diminish. But with public debt, with sovereign debt, it's not so easy and that of course is the issue here in Europe. Sovereign debts are perpetual until they are forgiven and written off, that is to say, until there is a meeting of minds between the debtors and the creditors on what has to be done. And we've had this experience in the United States with Latin America. It's not news to us.

It is fashionable to say that the U.S. is a free market economy with practically no welfare state. I am sure you have heard that many times, but the facts are actually otherwise. If you look at the numbers, we spend about six percent of our personal income on public pensions. I guess it's about seven percent on public healthcare and another ten or so, on the private side. Overall in 2008, public transfer payments were about fifteen percent of personal income and they went up rapidly in the crisis. So my point is that in this respect the United States, which is a very large continental economy, is as an economy not entirely like Germany but more like Germany than like Greece or Spain.

We do have a system that can sustain and that we can finance. Notwithstanding all you hear about budget deficits, that's obvious. The United States government does not have a financing problem. The simplest evidence for this is the long-term interest rate which is at an historic low in spite of the size of the deficit and the public debt. And again that worked to break the shock of the crisis. We did not recover but we did not fall apart. Why not? Because fundamentally we are working with national institutions that were built a long time ago in the New Deal and the Great Society, and fundamentally those institutions are still there. Deposit insurance, social security, Medicare, Medicaid, and grants-in-aid from the federal government to the states and cities. It's a tested model and it works.

Now what is the situation in Europe? In Europe of course you have national institutions that were built, very strong ones, on essentially the same tradition of social solidarity and social insurance, and that of course is especially true in northern Europe. It is the critical tradition of any successful society in the modern world—of the ability to react to stress. But it's not the case for your continental institutions which were built later in a different time. Those institutions are neo-liberal. I regret to say they are built on ideas that were exported from the United States to a large degree. I apologize to you for that. Your problem was that you accepted the exports and you're paying for them now. You impose arbitrary budget and debt ceilings. You gave your central bank a monetarist price stability charter straight out of the University of Chicago, very different from the one, the dual mandate for full employment and price stability, which is in the legal statutes governing the U.S. Federal Reserve. I mention that all the time because I was a very young member of the staff of the House Committee on Banking when that statute was written and I was actually the person who drafted it.

And you also allowed your banks to over-leverage under the disastrous Basel II arrangements, relying on alleged capital buffers to provide stability. What's wrong with that? Straightforwardly, if the capital buffers are not backed by accurate accounting, they don't exist. And if you aren't supervising the accounting you don't know what's there and what's not.

But most of all, your politics imposes a dysfunctional austerity on the debtors who cannot pay and cannot escape their debts. And your leaders, Europe's leaders, justify this by confusing surpluses with virtue and deficits with vice, an easy transfer to economics from religion, pretending that one can exist without the other, which actually if you were Catholic you would know is not the case. In fact, in economics deficit and surplus are simply the accounting counterparts of each other and you cannot erase the deficits without also erasing the surpluses.

In Germany, you, even a few years ago wrote the so-called “debt brake” into your constitution—a balanced budget except in times of severe economic crisis. What is that? It's a constitutional provision that you will always have a severe economic crisis. What a foolish thing to have done, I have to say.

[Applause]

I was going to say I was sorry to have to be harsh in those remarks but I can see that’s not necessary.

Now in the U.S., as well, these core social institutions are under threat. They have been under threat for years and that threat is acute at the moment. We have the so-called fiscal cliff, a contrived crisis, a reactionary device to force cuts in the programs that have so far survived thirty years of Reaganism-- cuts in Social Security, Medicare and Medicaid, as well as other public spending. But it has not happened yet and there is actually some good political news. I think the re-election of the President by a decisive margin and the results in the Senate were a defeat delivered by the American public to the neo-liberal vulture capitalist ethos. And the President, who was perhaps not as brave as some of us would have liked in his first term – okay that is a very kind remark – has already moved to assert some moral leadership in these matters which he had not done before. The battle is a matter of defense; the case is very clear cut; the people have spoken. I will not predict victory but the position is much better on these core issues than it was a month ago.

But you in Europe, and especially you my friends in Germany, have a much harder task. Europe is moving from stop gap to stop gap, from hypocritical half measure to hypocritical half measure, from false assurance to false assurance as the situation gets worse. Eventually the debtors-turned-victims will rebel but they lack moral standing, political power, and the economic capacity to save Europe. That can only come from here. Solidarity is the prerogative of the strong.

In 1919 in a book entitled, "The Economic Consequences of Peace," John Maynard Keynes addressed his countrymen. He wrote, "If the European civil war is to end with France and Italy abusing their momentary victorious power to destroy Germany, and Austria Hungary now prostrate, they invite their own destruction also being so deeply and inextricably intertwined with their victims by hidden psychic and economic bonds." And again much later in the book, "The policy of reducing Germany to servitude for a generation of degrading the lives of millions of human beings and of depriving a whole nation of happiness should be abhorrent and detestable. Abhorrent and detestable, even if it were possible, even if it enriched ourselves, even if it did not sow the decay of the whole civilized life of Europe."

I make no defense of the government in Greece, nor of the property speculators in Spain, Ireland, or the banks in Iceland or anything else you might name. But the flaws and follies at these agencies as I said before were not secret. They were known to those who lent to them just as the fraudulence of the housing loans were known in America to those who were making them. It was common currency. Responsibility is joint, mutual and sustained.

And we know because we have seen it elsewhere, everywhere from 19th century Germany to 20th century American to post-war Europe and the 21st century in China, that economic integration concentrates economic activity, particularly high income activity. Successful banks, advanced technology, machinery making, don't occupy all that much space. This is the principle of increasing returns. Germany is a big beneficiary of this principle inside Europe and indeed in the whole world. You yourself are representative of the world's most successful industrial activity. You're the architects of that. But we also know that relations between a wealthy exporter and a less wealthy importer cannot be regulated on commercial banking terms indefinitely. Nor can surpluses be maintained while deficits are exorcised. It's a mathematically impossibility. The rules of double entry bookkeeping are known to every shopkeeper and cannot be ignored by political leaders.

So what is the alternative? It must first involve a comprehensive restructuring of the debts. There is the Yanis Varoufakis-Stuart Holland "Modest Proposal" which I think is a very good starting place. It insists on three elements. They are: first, a common pool of Maastricht-compliant bonds; second, an European Investment Bank- funded New Deal program—an investment program—a reconstruction program, let us call it a Green New Deal and marry the challenge of economic reconstruction to the challenge of dealing with our larger energy and climate problems; and third a common, an independent banking authority with the authority to supervise and the authority to restructure, as required, including to downsize and rationalize the financial sector. This is something that we should have done in the United States when we had the political opportunity in 2009.

Now, these matters are necessary but I don't think they go all the way to addressing the needs.

I think that the statement made by the Executive Board of IG Metal on the 9^{th} of October, "Change of Course in European Solidarity," is a marvelous document that sets out basic principles that are required for going further to develop a sustainable architecture. So you already know the answer on how to change course, but let me give you some ideas.

Professor Rubery yesterday offered an excellent proposal: A common unemployment insurance fund for Europe. That would support those people who specifically are the most damaged victims of the crisis. Why not?

Let me add to this another idea. A pension union—a European Pension Union to ensure that people who have worked their entire lives, retire decently on the standard of Europe as a whole and not on the past productivity of their own impoverished countries. Perhaps, later on, there could be a topping up scheme for wages on the model of the earned income tax credit in the United States; maybe a continental minimum wage. These are low-impact, easy-to-administer, old-fashioned devices, and they bypass weak and ineffective governments in the periphery. They stabilize incomes, employment, and purchasing power. They can work to save your markets even as they save the countries in which they have their most important effects.

Your document shows that you, as unionists, understand how the principle of solidarity works. It states in general terms what reforms are required and that you are ready to act on the great challenges of inequality, energy, and climate that face and plague us all.

Let's look at this problem with a very hard eye. What will happen if we do not succeed? I think there is a model. It's not so long ago; it's not so very far away. It's Yugoslavia, which was in its day, a very successful middle income country. My brother, as it happens, served as the first United States Ambassador to Croatia from 1993-1998. He told me early on this was not age old ethnic conflict, but new crimes committed for political and economic reasons. That's what kicked off those wars. And when the violence starts in an advanced, in a developed country, it moves quickly and the fractures are not clean. And I can assure you that if you talk to people in certain parts of Europe, and Greece particularly, you can hear already the anxieties that you could have heard in Yugoslavia in the early 1990s.

If you don't like that model, and of course none of us can possibly stand to see this happen, well there's another one also not far away, not long ago, that's the Czechoslovak model-- a civilized, orderly, negotiated divorce. It would be better. But I have to ask, does any country anywhere in the world enjoy the sane, secure, farsighted moral leadership that Czechoslovakia happened to have had at that time?

So I think you came to the right judgment in this document. You came to the right judgment that Europe must be saved.

Let me thank you again for inviting me and for your patience in listening to my remarks. I make them to you again as leaders of one of the world's great unions because the union movement rests on solidarity and courage. And I do so in the spirit of remarks made by Abraham Lincoln to the United States Congress in December of 1862, when he wrote, “I trust you will perceive no want of respect yourselves in any undue earnestness I may seem to prescribe.”

Lincoln went on, by the way, to close with what is one of the great texts of American political history. So if you will permit me I’ll read just a little more of it. He wrote, “We can succeed only by concert. The dogmas of the quiet past are inadequate to the stormy present. As our case is new, so we must think anew and act anew. We must disenthrall ourselves, and then we shall save our country...

“Fellow-citizens, we cannot escape history. We will be remembered in spite of ourselves. No personal significance or insignificance can spare one or another of us. The ...trial through which we pass, will light us down, in honor or dishonor, to the latest generation... We say we are for the Union. The world will not forget that we say this. We know how to save the Union. The world knows that we do know how to save it. We—even we here—hold the power, and bear the responsibility. The way is plain, peaceful, generous, just—a way which, if followed, the world will forever applaud.”

It is your Union of course that is at issue today, but it is yours, you created it. It may be lost. It will not be saved on its own. I congratulate you again on the leadership you are showing and will continue to show. And I wish you well and I thank you again.

[End]