

Europe and America in a Time of Crisis.

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The ongoing world economic crisis highlights the enormous economic differences both within Europe and between European nations and the United States. Europe is not a single political economy but the degree to which Europe remains very diverse set of quite different political economies remains a surprise to many. Whether we look at the difference in levels of economic development, the size and structure of national budgets and deficits, or even the range of different social-economic models found within Europe, it is their diversity that stands out.

First, just consider the large difference in economic development and wealth within the American states and within the EU. For example, the average household income in Mississippi is \$37,000 and over \$70,000 per year in New Jersey - a spread of almost 2 to 1. The differences with the EU are far greater. For example, the average per capita GDP in tiny Luxembourg was nearly \$100,000 per year, but less than \$8,000 per year in Romania.

If one looks at taxing, spending and borrowing, we do not see “A” European model, but many different systems. While some countries tax their citizens very heavily and spend quite generously on social programs, others have substantially lower taxes and lower levels of public spending. In some ways, the most interesting countries in this regard are the Social Democratic welfare states of Northern Europe. Despite the widespread predictions that heavy taxes and large redistributive welfare states should be bad for national economic performance, the Scandinavian countries of northern Europe actually performed remarkably well in the past several years. The key reasons for this is that these countries have invested heavily in their citizens, improving educational systems, social infrastructure, and gender equality. The result has been that these northern countries have managed to build high trust societies in which citizens feel engaged, confident about the future, and fairly treated. The “welfare state,” contrary to many people’s expectations, has strongly contributed to the economic and social success in this part of the world. Today these countries have very high levels of investment and productivity, admirable levels of gender and economic equality and even relatively positive demographic outlooks. All this while they have managed to hold their budgets in line.

The same cannot be said of the countries on Europe’s southern frontier. In the Mediterranean countries, the so called ‘welfare state’ should more accurately be called a ‘pension state.’ The reality in these countries is that young people (and immigrants) are increasingly shut out of the labor market and/or are forced to pay remarkably high taxes and social fees, while their parents and grandparents enjoy remarkably generous social benefits and early pensions. A conspicuous coalition has emerged in

these countries between the aging citizens, the entrenched unions and the political elite. These countries have not only racked up the highest levels of public debt, but also have the lowest levels of trust and confidence in their public authorities. The obvious consequence is that no one trusts the state, few people are willing to take the fiscal burden of having children and these societies becomes more older and more dependent on a underclass of immigrants (both legal and illegal) who have virtually no chance of ever being able to take advantage of the benefits their hard labor is providing those they serve. The economic and social future for these countries appears grim indeed.

The pictures in the middle and eastern parts of Europe are more complex, and quite frankly, more difficult to parse out. On the one hand, the countries in the eastern edge of the European Union have undergone such enormous changes and challenges in the past two decades that it is difficult for anyone outside to understand what direction they headed. At one level, we can see that economic growth in these countries is generally considerably stronger than in western European countries. But, of course, there is a considerable degree of ‘catch-up’ in this fact. It is also the case that precisely because incomes and wages are so low in these countries, that much low-tech investment has gone here in recent years. Moreover, while some of these countries have taken a strongly neo-liberal turn, slashing public spending as well as taxes, others have leaned more towards a the more social-European model. It is certainly too early to predict winners and losers at this point, but it does appear that those that have invested more in their societies are weathering the economic storm better than those who adopted the more radical pro-market policies originally pressed on them by the “Washington consensus.”

In the middle is what former US defense secretary Donald Rumsfeld liked to refer to as “Old Europe.” Even here, we see remarkable diversity. For example, the hugely powerful export machine known as Germany, has benefited massively from its ability to sell more than it buys from its European neighbors. Early in the economic crisis it appeared that Germany would continue to be the “Powerhouse of Europe.” Today, however, as other countries are being forced towards greater fiscal discipline, German manufactures and German banks may be hard pressed to find new customers. The integration of European economies was good for the German economy in the good times, it proves more challenging when times are hard. Moreover, despite their economic power, the Germans have not built the kind of productive social welfare state found to the north and instead relies far to heavily on a social and economic model designed for a 20th century world. France, similarly, seems caught in the tired battles between the “insiders” who are already advantaged by the largess of a generous state and “outsiders” who do an increasingly large share of the nation’s work. As in Germany, there are advocates of a newer economic model favoring social investment in France, but there is little evidence

that they can force those who currently advantaged with long vacations and early retirement in favor of those who have not been able to buy into the system.

Finally, the English speaking countries on Europe's western frontier have pursued yet another political economic model. After a decade of deregulation, tax cutting and impressive economic growth, Ireland and Britain are now mired in economic disarray and caught in what is known as a fiscal trap. With public debt at 57% and 68% respectively, few economist truthfully expect these countries to be able to grow their way out of budget deficit, without raising taxes. But increasing taxes at this point seems likely to snuff out economic growth even before it emerges. Meanwhile servicing that debt eats up an increasing share of tax revenue.

The fiscal health of European nations is also enormously diverse: Norway is running an annual budget *surplus* of 9.9 percent of GDP and has a total budget surplus (that is the opposite of public debt) equaling 143 percent of this oil rich country's GDP. Denmark and Sweden, while doing somewhat less well than their wealthy neighbor, have managed to keep their total government debt to only -1.6% and -13.1% of GDP respectively. This contrasts rather sharply with Greece, which has an accumulated debt of 94% of GDP and deficit of 9.4%, and Italy with a total debt of 100.8% GDP.

The United States sits in a very different position from European nation's, however, because America it by far the largest and economy and military power in the world. Though the USA has a budget deficit of 10.4% of GDP and total accumulated debt of 65.2% in 2010 almost no one questions this country's fiscal stability. This is not only because of the military strength and cultural hegemony of the United States, but also because of the enormous physical and intellectual resources this country has benefited from over the years.

Of course, America and its model of casino capitalism is at the center of the current world economic crisis which grew out of the massive tax cuts, the roll back in the state's regulatory power and the casino capitalism that ensued. The result at first was the massive expansion of consumption by American consumers financed by a willingness take on unheard of debt. The result was not only an economic bubble, but also the rise of enormous inequality and steep declines in citizen trust in their political institutions. In many ways the "Tea Party" is a direct consequence of America's economic model.

Ironically, most economist now believe that, in the short run at least, Americans must to continue consuming radically more than they produce to bring back world the world economy. (This will be as important for Germany as for China.) It should not surprise us then to see that this is the economic model currently being pursued by the Obama administration. While there may well be in the US long term interest to increase taxes, redistribute wealth and rebuild a more egalitarian society. Given the depth of distrust of government found in America today, it seems most unlikely that this will

be the route chosen. Instead, expect to see the US to continue its pattern of low taxes, high borrowing and heavy consumption. American's are addicted to their model. Oddly, so is the rest of the world.