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*Business & Innovation*

Michel Santi

# Capitalism without Conscience

P.I.E. Peter Lang

In this striking new book it is argued that the outraged attitudes of neoliberals and many of those who work in financial institutions with regard to the size of public deficits are far from being genuine and merely mask a desire to dismantle social programs and reduce the size of government.

The author makes a persuasive case that neoliberals actively seek the deepening of the financial crisis to support their ideological demands for the shrinking of government expenditure. Indeed, he argues that neoliberals have an interest in encouraging a psychosis about public deficits in the general population to justify the cuts to public spending that will deny services to those same citizens.

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P.I.E. Peter Lang  
Bruxelles





# **Capitalism without Conscience**



P.I.E. Peter Lang

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**Michel SANTI**

# **Capitalism without Conscience**

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## A Sisyphus Myth for Modern Times

How could one not remember *The Prisoner* – the cult British 60s series in which a giant bubble frantically chased the hero played by Patrick McGoochan? These days, our world is in a similar situation – each and every one of us are hostages of bubbles because the world is full of them, and not just from the speculative bubbles that plague our markets. Indeed, there is nothing easier than differentiating the bubble that imprisons and isolates our politicians, the salary and bonuses bubble for the executive managers of large companies and in the finance world, the youth unemployment bubble, and finally the inequality bubble. Just like the bubble that tirelessly chased the prisoner of our TV series, it would seem that our financial system has been affected by a similar curse because the collapse of a bubble displaces like clockwork the speculative fever of another instrument or another market, which then blows up to make another speculative bubble! Indeed, financially we are progressively losing control of our lives. It wasn't for any reason that Joseph Stiglitz, the Nobel prize winner in Economics, questioned whether or not a person's life nowadays depends on "their income or the education provided by their parents".

Financial deregulation has given rise to almost twenty-five years of banking and stock-market crises. This *laissez-faire*, having spread throughout the English-speaking world to Continental Europe and reaching Latin America and Asia, is the culmination of a planet that has been progressively plagued by speculative bubbles, which have blown up to some devastating financial, economic and of course human, effects. A non-exhaustive list covering modern times would go from the resounding failure in 1984 of what was then the seventh largest American bank – "The Continental Illinois National Bank and Trust" – to the Wall Street Crash in October 1987, to Japan's Lost Decade, starting in 1990. It would further include the banking crisis in the Scandinavian countries between 1987 and 1991, the violent financial shake-up in Mexico in 1994, the 1997 Asian debacle, the 1998 Russian crash, the implosion of technology stocks from the year 2000, with the grand finale of the current crisis that started with subprime mortgages in the Spring of 2007. The latter remains more persistent than the others in the sense that the brief lull periods have been followed by ever more serious developments since 2007, and in different locations. The current up-

heaval is also vastly more complex than those that came before it, probably due to the liquefaction of financial products, whose sophistication can in no way be compared to the products wielded in the nineties. Nevertheless, the first stage was punctuated by significant crashes, like those of Northern Rock in Great Britain (Fall 2007) and Bear Stearns in the United States (March 2008), existential threats to American mortgage giants (Fannie Mae et Freddie Mac ending up nationalized) and to AIG, the largest insurance company, ending with one of the most dramatic exits of its kind with Lehman Brothers. These last ones created unparalleled effects given that they all occurred in Fall 2008.

If the orthodox economists and conservative political directors agreed today on austerity being the only remedy to the crisis of the European periphery countries, the streaks of bad luck in countries such as Greece and Spain must therefore be analyzed from a different angle, with the neoliberal circle of influence being greatly less favorable. The diagnostic arising from current public deficits, accused of being responsible for all of our sorrows, deliberately avoids the pending questions by only engaging organizational aspects and the consequences of actions being settled with massive public debts. We forget, for example, that even in 2008 Spain respected the Maastricht criteria (the utmost accolade of financial orthodox) and that it was considered as an excellent student of the Euro Zone. We also tend to ignore that the Greek crisis was part of a sequence set off by the liberalization of the world-wide financial system, of which the establishing of the Euro Zone formed a supplementary stage. This persistence in laying down the budgetary rigor does nothing more than mask the immense labyrinth of financial innovation. High finance had indeed managed during the 2000s to completely separate the decision to grant loans to households and businesses on the one hand, from the latent risks and creditworthiness from their debtors on the other hand. In this respect, let us make no mistake, the public deficits are in no way the cause of our current troubles, which are to be found through the immense generosity of the suppliers of loans dispensed to entire sectors of the population, regardless of whether or not they qualify for them. It has likewise made use of a leverage effect, in a completely indifferent way, by a totally unrestrained system by financial instruments that promote schizophrenia and irresponsibility. This hypercomplexity of new financial products and sophistication of securitizations have ended up in an explosion out of all proportion to demand (especially in the United States and in Great Britain). Really, finance has forced the hand of the consumer by literally inundating him with loans through an increasingly inventive financial engineering. This generalized euphoria takes place through financial and prudential corruptions and of a general laxity of our economic and political leaders, desensitized by and financial system which they were convinced would

have become optimum. Disguised by the financial products' complexity, ordinary citizens were thus preyed upon, becoming speculators, similar to those of a Ponzi scheme, convinced that the value of their real estate would hit a breathtakingly high summit.

How could one resist such a whirlwind when the U.S. retail price index was apprising around 15% each year between 2001 and 2006? This unprecedented, easy profit pyramid was nonetheless easily knocked down in 2007 shelling the brushed-aside financial heavyweights in Wall Street with a disconcerting ease and, more importantly, with devastating consequences for the American, and therefore global, economy. It is thus the Anglo-Saxon events in 2007 and 2008 – rooted in the speculative euphoria of private lending – which provided the decisive impetus to a crisis that consequently spread throughout Europe. It is the gradual infection of the global banking system, the collapse of international commerce and toxic financial products and other “zombie” debt held by private lenders who have lit a match that still consumes us to this day. These are not public debts. Certain countries harshly affected by the crisis today benefit from the sizeable budget surpluses, such as Spain, thanks to their tax revenue from their real estate bubble. It is thus absurd to hue and cry about the States adopting a budgetary rigor which is supposed to correct the inequalities that their responsibility is in no way invested in.

The international financial community demanded no less from the Western nations than a return to budgetary balances. However the States almost lost all power over their economic policies because they gave up on influencing the financial variables. Isn't progressive deregulation effectively expressed by determining the exchange rates by the sole exchange market? By continuous market speculation (where shares may be listed night and day), minute by minute establishing the capitalization of a business? By a bond market handling enormous – or even reduced – amounts on loan to private debtors or indeed the States? It is thus an environment in which structured financial products where derivatives and other so-called “exotic” instruments have confiscated the very substance of the States' financial and economic power – even the most powerful ones like the United States of America – with the financial community demanding a fiscal consolidation that they no longer have the means to carry out well. The power of our States has also insidiously been diluted by the liberal globalization, insofar as our companies are totally dependent on globalization.

The European Union has, in addition, glaringly highlighted this process whereby the States give up the majority of their competences and prerogatives so as to be in a position to weigh in and be relevant (regarding Asia and the U.S.) in this global battle of capitalism. The relin-

quishing of powers yet again to the States has been completely lost to the international crisis. The result today is one of financial ruin in which politicians can no longer do anything as they have been stripped of almost all of their leverages. This is why today's emperors have resorted to "normal" clothes, which fit them all too well! Additionally, not happy with being saved and bailed out by their respective supervisory governments, the establishments and finance world today blame the States for their deficits... the very ones who have been worsened by saving the financial markets from the money pit they had thrown themselves head-first into. It is a comical situation, albeit immoral, in which the States are baffled by a power placed in the hands of the financial markets, and unbalanced by steep amounts injected into the balance sheets of the flowerets of this globalized financial world and are required to clean up their public accounts. The wide range of final demands from creditors who bear a strong weight on the States to be reimbursed, at the risk of speeding up the generalized financial collapse of which they themselves (the creditors and the financial system) would be the first ones to suffer from! There is nothing but incoherence for this financial community that has not stopped demanding rigor and austerity from the States all the while bemoaning a growth that is too weak to allow the repayment of public debts! When will the markets, and with them the caste of orthodox policies that slavishly monitor them, realize that budget economies are not a credible strategy to reduce public deficits?

Rigor is but a sedative – albeit a temporary one – slowing down the creditors and a bitter pill to be swallowed by the population. Or even worse, given that it is the countries that have implemented a tough austerity and who are the most punished by the financial markets, ones that have gotten out of control by a growth that naturally undermines them. Is it not strange to consider a State's deficit in the same light as a household budget or a company's balance sheet? It is most certainly not reassuring for a creditor to learn that its debtor is having payment problems or that he or she runs the risk of losing their job. Because of all this, this type of comparison can in no way be applied to the public debt of a sovereign nation for the sole reason that a state has a duty to stabilize the economic and financial conditions of the area it is responsible for. It is unacceptable to wallow in deceitful reasoning and suspect demonstrations of rationality that confuse the necessary budgetary rigor of a household or a company with the responsibilities of a state as a last resource to revive their activity and economic make-up. Who will take the reins and who will fill in the gaps if the private sector is paralyzed in its expenditures, in its production, and in its investments? Without the regulatory intervention of the state, unemployment is condemned to get worse and the economy to recant, together with an unavoidable deterioration of public accounts. In times of crisis, austerity most certainly does

not go well will fiscal consolidation, even if this technical debate masks another, even more fundamental debate.

Indeed, it is the State's role in the economy, which is at the heart of these diametrically opposed (or even antagonistic) solutions – between those in favor of budgetary rigor, with an additional setback for the state, and those who tolerate public deficits, considered as the price to pay for a state taking on its duty as arbitrator and regulator. Accepting budgetary economies doesn't just mean going back to a financial and accounting orthodox that is both unjustified and counter-productive in times of crisis. It means resigning oneself to yet again and even more cut back the rights of the state, and by extension, ours. It means accepting the verdict of the markets and leaving the overwhelming majority of our citizens defenseless. A real trench warfare is unveiled to this effect by the tenants of this strict orthodox, who don't hesitate in employing "budgetary fear tactics" (to use Paul Krugman's expression) in order to their final goal consisting in an almost total eclipse of political powers. To do this, a specious argument is developed to cover all defenses, which deliberately and happily mixes individual solvency and the solvency of the state, against a public that is bombarded with cataclysmic images, the sole goal of which is to put pressure on their government to adopt slimming measures. At the same time, we put up with the cynicism of our leaders who, without asking too many questions, accept the dictates of the markets and impose the rigor. Such cynicism is believed by a citizen who accepts all the sacrifices under the false pretense that the debts must one day be paid back. Paradoxically, the current financial crisis in itself serves as an argument for the tenants of this orthodox who argue in favor of further constricting public powers. So it is clearly the European countries in which the state again as some importance (such as Scandinavian countries and, to a lesser extent, France) who have best endured the ordeals.

Does austerity, then, aim to reduce the deficits, or is it but a pretext to move the state backwards, demolishing in the process what remains of social programs? In a situation in which the profits of large companies and financial establishments are beating records, in which access to low-cost capitals allows them to increase leverages and investment possibilities, how can one not be troubled by these incessant calls for austerity that are nothing but smoke screens designed to confuse? Let us remember the premonitory words of Aldous Huxley in "Brave New World": "Sixty-two thousand four hundred repetitions make one truth". The real objective evidently being a complete anorexia of the state, which, like clockwork shall translate as a bulimia of the private sector, starting with the finance sector. It would now be a good time recall Keynes again who (in 1936) concluded his "General Theory" with a call



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for the “socialization” of investment – a business too serious to be left in the hands of the financial markets.

## **Money – Monopoly of the State and the Solution to the Crisis**

Despite all the attempts of economists to reduce its importance, money is not neutral. It has systematically refused to allow itself to be categorized or boxed into a rule that such school of thought or such theory of economics has assigned it. One this is for sure – it is absolutely essential during periods of great weakness as shown by the expansionist policies and other cash injections implemented in the United States and China furthering the current crisis. The latest example being the massive emergency stimulus put in place in January 2013 by the new Japanese government. In the same way we may note, implicitly, the devastating European effects caused by the absence (and fear) of exploiting the benefits of money. Money effectively absorbs the cash crisis that paralyses the economy and avoids deflation that slowly kills it. Karl Marx (1818-1883) and John Maynard Keynes (1883-1946) agreed that money is the goal of all production and all services rendered. Production begins and ends with money. Did Keynes get it wrong with the “monetary theory of production”? Even Milton Friedman (1912-2006), champion of the monetarist school, ardent defender of ultra-liberalism and Winner of the Nobel Economy Prize, joined Mark and Keynes in their appreciation of the crucial role of money. It was not just that he believed money is the source of inflation and depressions given that it allows it to be manipulated by the state who assumes the monopoly and who prints too much of it. According to Friedman, the state acting as printer en masse of notes, puts into questions the efficiency of companies and markets are supposedly regulate themselves. In fact, the success of the monetary theory and its *laissez-faire* policy should have been accompanied from the end of the seventies with a loss of power for the central banks, which were asked to do no more than monitor and maintain the inflationary threat by using one weapon only – that of the monetary policy consisting in raising or lowering their interest rates in a humdrum way. These trends (and monetarists) likewise managed to demand from the state, and actually get it to control its lifestyle, in order to balance its accounts. This restriction of public power was, at the same time, compensated by a hyperbolic expansion of the financial sector that would be able to regulate itself as the excesses and embezzlements were by no

means in its interest, according to the very same theorists. Financial stability would naturally be the meeting point, together with its prize of financial prosperity and its generalized material comfort, in which the most deserving of citizens could have a slice of this “deregulation cake”. This inevitable logic was further hindered within the framework of the European Union set-up. Strict quotas on public spending were effectively halted, thus furthering Member States from any possibility and from any temptation of making use of money’s virtues. To do this, the Central European Bank was implemented according to a model of total disconnection with the budgetary and fiscal policies of the Members. With accomplished, and one could say, statutory, autism, the CEB would also ensure the monetary supply of EU Member nations without getting involved in their public accounts. The founders of this ultra-liberal Europe considered (further to Friedman) that money is so suspect that its use must be strictly monitored by a body in which the States have no special authority. Money was this box of matches snatched away by a child, but not without being punished. This European counter-example is today particularly eloquent as we realize that, in doing this, all the ingredients of an even worse conflagration than the Great Depression were voluntarily put in place.

Money, however, is not to be taken lightly. It is not some type of food or dough that can be molded according to our needs at that time. Nor is it a lubricant. Money is very likely the most decisive institution of our capitalist system. Being the only measuring instrument for work carried out, for anything produced or exchanged, it is at the heart of our social machine. As is normal for such a monetary policy to be in the hands of the state – a sign of the good operation of public affairs – all the separation attempts between the creation of money and the real economy are doomed to failure. Indeed, it is impossible to separate economic life from political life because the transmission belt between these two worlds is money, itself exclusive to the state, and thus to politics. The only definition of an objective or of an inflation channel by a central bank is, in itself, a political act, in the sense that it responds to the demands, or serves the interests of a group. It is, at the same time, natural and legitimate that the state uses money as a lever in relation to economic activity, to fulfill the needs of certain social groups, to make others pay (or contribute) or to monopolize resources. This important and fundamental act for “monetization” is thus omnipresent in the expression of the state. It is effectively in terms of money that social contributions and government subsidies are set or that the fines and even the sentences are formulated. As it is the state that benefits from the monopoly of printing money, it is likewise the state that sets the game rules and the conditions it agrees to be assigned it. Furthermore, our companies have fully assimilated this power that they recognize as

exclusive to the jurisdiction of the state, accepting to pay taxes, running into debt, or agreeing to loans – as much actions expressed in one sole unit of account, the creation of which is the responsibility of the state. Even so, the very serious sentences inflicted in France to counterfeiters – scalding in the Middle Ages and the guillotine up until 1832 – correctly reflects the way in which those who got in the way of this absolute privilege of the state were punished. A crime of *lèse-majesté* back then and against the Republic today, is still punishable by death in 2012 in certain countries!

The fundamental problems of our companies in relation to money are, at the heart of it, due to the lack of money, that is, default payments. Monetarists, such as Friedman and his peers, have further been embarrassed by the function they attributed to money because they have systematically dismissed – or forgot about – the only assumption of bankruptcy of a financial establishment, and even more, of a sovereign country. However, a crisis is still accompanied by a rush towards the most secure assets, the first of them being money, knowing that this intensive search for money increases its subjective value while it (mechanically) decreases the other assets. In times of crisis, only the state therefore can swim against the current while sticking up several defense lines. Its central bank may also remember the unlimited loans to financial establishments that suffer a devaluing of their investments and heavy withdrawals of their deposits. Additionally, the central bank acts on another level consisting in buying up assets at risk and those which nobody wants anymore, until then held by banks and companies. The goal being to avoid the absolute evil that is the “debt deflation” described by Irving Fisher (1867-1947). The use by the central bank of its money anticipates the general sale of assets, equity and other securities from the operators short on cash. Sales which could lead to a downward spiral affecting all sort of investments. The central bank may well provide the Government with the money to ensure the reflation of the aggregated demand, with a beneficial impact on growth. Only this “dance of the dollar” to recall the important expression of Fisher, would be the only way to ensure economic recovery.

Within the framework of the current crisis, the central banks are not, however, rising to the occasion as they, like the governments, have let the recession take place and let unemployment get worse. As regards countries like the United States, who have implemented stimuli, they have failed due to a lack of ambition because these measures were not as consequential or sufficiently generous to become decisive in guaranteeing a long-lasting revival of economic activity. Whatever they were before the crisis or brought about by the same crisis, public deficits have been powerful impediment having significantly curbed public policy.

The States having been persuaded by the economists and experts that they can no longer allow themselves to spend more. The founders of this ultra-liberal Europe considered (further to Friedman) that money is so suspect that its use must be strictly monitored by a body in which the States have no special authority. While the economies were weakening and the governments were handcuffed by their deficits, against all expectation and despite common sense, the interventions of central banks were limited therefore to their strictest expression (except in the United States). That is why, in the context of depressive episodes where the private sector is forced to repay its debts (the famous “deleveraging”), the central bank needs to flood the economy for which it is responsible with cash. Faced with a situation where finance must digest its excesses, and businesses such as the private ones are reluctant to invest and spend, the central bank has indeed no other choice but this expansionist policy. Even if it drops bundles of banknotes by helicopter, to use the famous phrase of Milton Friedman when he spoke about Japanese deflation. These stimuli can certainly not be properly calibrated, and appropriately targeted, it remains that spending – even seemingly less useful – are likely to enjoy the workings of the economy. In a depressed context in the presence of a notorious slowdown, monetary officials must be deflected exclusively toward this economic resurrection and should therefore not skimp on resources. Since a too timid and stingy stimulus would have almost no effect, and would amount to “a sword slicing water”. Caution is certainly a virtue, but in the presence of such fundamentals, it can be a real vice for economic actors in the private sector that must be rescued by the central bank. A state that refuses to call on its central bank cannot therefore call upon any legitimate pretext preventing it from straightening out its economic activity and improving the unemployment situation. This is why it is crucial to understand how this monopoly of money-creation operates and how it can – and must – serve the general interest.

The existential questions on the powers of the state and the reports of exhausting its fire power taking place nowadays – with equal amounts of concerns never even taking place – in actuality mask a substantial debate on its role in our economic life. A state that avails its citizens and businesses of its monetary system considers money as an instrument that favors its prosperity. Without this determination, the State’s action is useless or nothing more than a minority. This deteriorates into “poverty in the midst of plenty”, to use the words of Keynes, which perfectly illustrates its aim by describing a context “a condition where there is a shortage of houses, but where nevertheless no one can afford to live in the houses that there are”! The state must therefore avail its nation of all of its resources and possibilities – including monetary ones! In doing so, public deficits must not run into any obstacle or any limit (although isn’t

this the very *raison d'être* of any state?) in the restoration of full employment and price stability. A system exists allowing the restoration and reconciliation of these two, on the surface antimonial, fundamental components of our economic life. On the other hand, it lacks the political willpower and ardor to implement it.



## **Public Deficits – A Stick Shift to Revive Economic Activity**

The explosion of public deficits, a spectrum of default payments of one or several countries or restructuring of their sovereign debt, are in no way specific to the crisis that has been sweeping through our western nations since 2007. Since the French Revolution, it has been possible to count four major phases marked by an uncontrollable escalade in national debts. The first period goes back to the Napoleonic wars in 1848 in which half of the countries, States and kingdoms at the time were successively declared bankrupt. The second period really got going after the foundation of the German Empire in 1870 and lasted about twenty or so years. The Great Depression, of course, clearly originated in the stock market crash in 1929 and lasted until the end of the 1940s. Finally, a fourth crisis, limited to the emerging markets, had devastating effects throughout the 1980s and 1990s. Japan, an industrialized country with an integrated economy, was also affected by this crisis, having suffered the implosion of several bubbles since the start of the nineties. Modern day is thus marked out by crises linked to debts which last on average two decades... or indeed longer, Japan for example still hasn't escaped its "lost decade" which has been going on now for more than twenty years! The monstrous deficits preceding and accompanying the Great Depression were decreased in due form by the bankruptcies of certain States, while hyperinflation vehemently took on the role of eradicating the debts of several others (Weimar's Germany naturally comes to mind). We also call to mind the fact that all of the countries allied with the United States during the First World War defaulted against this company – with the sole and well-known exception of Finland. None of the nations that defeated Germany at the time were in a position to repay the United States for their engagements, which worsened the declining economic conditions disguising the Great Depression. The colossal deficits of the First World War and the Great Depression – never paid back – ended up in default payments or restructurings consisting in partial repayments or in sudden rises in inflations. A bit closer to home, the crisis in the emerging countries was also regulated by a combination of restructurings topped with hyperinflation. This also allowed the cleaning up of debts and speculative bubbles to come to an end. Debts



also form an integral part of a State's operation and its way of life. They likewise form the pattern of our own daily life.

The current crisis has nevertheless highlighted the deficiencies of our economic models where the debts' variable is strangely absent despite the controlling and active role it plays in them. Our current economic system naturally includes salary and price variables. It is further determined by the central bank that, through its traditional inflation control instrument – namely, interest rates – has a fantastic lever to measure out our prosperity. It is because of all this that the essential ingredient of debt seems painfully to be to default on our current economic models to which nobody has had the guts to incorporate the credit variable. The body of economists, and with the credit rating agencies that parasite the system, are in this way late in globalization and seem stuck at the previous stage of closed economies in which all debts must be necessarily offset by debts of equal amounts. If we find ourselves today in a world where the credit rating agencies can dictate their law and where the debts of a country (or a region) are susceptible to collapsing an amazing human venture (the European Union), it is purely because of the deficiencies in our economic models, which do not include the debt and which, perhaps more importantly, overlook its effects. Our financial stability and prosperity depends nevertheless just as much on monetary policy (that is on interest rate setting) as on non-conventional tools and levers (such as injections of cash, and thus debts). And yet, our political leaders and our economists confine themselves to academic ponderings in which deficits are completely forgotten about. The balance of measures and approaches is at once slanted and the imbalances are systematically accentuated by decisions and positions that brush aside the (often beneficial) effects of the debt. The central banks, the ministries for Treasury and Budgets, the regulating bodies such as universities and academic research departments must therefore understand and include the active (and often “straightening”) role of debt in the economic grid. With economic framework no longer being able to be defined as a circuit (and a closed one at that), a great rethinking must occur based around these questions: What is the nature of our debts and how are they shared out between private debts, company debts and public debts? When does debt become excessive? When does investment make the economic growth of a country indebted to foreign funds? Are loans and bond issues the only mechanisms allowing the redistribution of funds? Why aren't the risks fairly divided out between the various stakeholders? Is it not logical for the credit providers to assume a certain degree of non-repayment risk for their loans given the interest charged?

Furthermore, the responses to these questions must include a certain amount of evidence too often denied by economists and leaders. Indeed, resorting to loans allows households and individuals to stabilize their consumption and their daily life when their income fluctuates or is actually uncertain in times of crisis. In the same way, it allows businesses facing erratic turnovers to regulate their investments and their production. Credit allows the state to continue on with its public spending without taxing its citizens too much all the while providing it with important levers to revive entire sections of its economy. All in all, public debt offers liquidity to economic agents by greasing up the wheels with inevitably positive consequences on private and company investments. The citizen's lifestyle and the improvement of economic conditions are thus tightly correlated to the debts of its state, because the volatility and macroeconomic uncertainties are exacerbated by the refusal to seek sufficient credit. In short: no public debts, no growth! This is because it is the debt that will allow our societies to become more modern, to build themselves, to enrich themselves and be confident that better days will come. Our material comfort, the development of our mentalities and even the blossoming of our democracies are indeed due to this capacity of becoming indebted, and this willingness and ability to live on credit, at least in part. Without debts and without this transmission belt of financial tools, we would still be poor, our Western world would not have been able to play its role as an engine of global growth and modernism, the average citizen would certainly not have been able to consume, to become owner of his home, or even just buy his cell phone, and companies would not have been able to invest and develop.

A country's economy, like an individual's budget, is condemned to restrict itself as soon as the credit tap dries because of, for example, a financial crisis. A painful deleveraging process is thus implemented consisting in repaying, at least in part, these debts, combined with default payments from debtors unable to fulfill the requirements of their creditors. Consequently, the States logically employ drastic reductions in their spending while the affected households stop any unnecessary consumption. The creditors, whoever they may be, are in no way tempted to take the helm by increasing their spending because of the inactive general climate and their losses for those that haven't been repaid. Such a convergence is liable to paralyze an economy, or indeed global activity, within a general self-feeding deflationary spiral framework. The decrease in consumption and public spending translates therefore into stagnation, or indeed cuts, in salaries having in turn a negative impact on prices. The latter are indeed restricted for trying to conform to a half-mast request, with a disastrous cascading effect on revenues for all the stakeholders. Put otherwise, these essential debts do not impoverish the

world because the commitments of a household, of a business, or of a state evidently constitute assets for their creditors. In fact, the never-ending arguments created by the neoliberals in which our States can no longer get themselves into more debt and in which this crisis would have been worsened by the excessive debt, are truncated. This is because a quick and easy answer justifies the debt reflation in times of crisis. The size and extent of global debt has no effect on the level of world wealth, because the debt of an individual or a state is the debt of another, or indeed, several others. Moreover, it is essential to introduce a decisive qualitative distinction in this approach and in this analysis of the debt because all debts are not valued. Indeed, the profit of the debtor is crucial because one may remain solvent while another becomes liable to default in their payments. In addition, it is what explains the size of our current crisis and it is what allows us to come to the conclusion that the new debts taken out nowadays by solvent economic agents or by States (who may freely print the money) contribute to considerably relieving the excess of debts of the others. Spending and investment made by a state will have a necessarily positive impact on the employment and unemployment of unexploited resources. Companies and individual liable for debts will be in a position to progressively pay back. The growth will thus be the meeting point... if only the private sector – at least partially relieved of its debts and having new-found confidence – took the reins. The private sector would most certainly get into debt again, which would allow the state to take a breather in reducing its deficits, but the debtors' profile will have changed and cleaned up. Indeed, these are solvent and strong debtors, in the sense that they fulfill their obligations, who will have taken the place of weak links who had a devastating effect on the economy. The global debt level will not have decreased, but the confidence and investment will be re-established by this simple debt-transfer to credible operators. Debt, thus, may well remedy debt, whilst conversely, breaking the chain of debt leading fatally to economic depression.

Excessive debt creates certain weaknesses, none of which highlight the fateful landing of 90% deficits (decreasing the GDP of the country in question), above and beyond which national debt strongly damages growth. Its excessive accumulation is obviously not devoid of risks. Common sense and intuition tells us that the ability of the States (much like the ability of households and companies) to pay their interest and their debts is seriously put into question by the sharp drop in their revenue. These situations, in the extreme, lead to a default payment for the state, or in individual bankruptcy for the debtors whose debts are becoming progressively more vulnerable to bumps. It is at this moment that consumption stagnates, that investment takes a step back, that unemployment gets worse, that creditors stop giving out loans – in short,

when confidence collapses. Indeed, the causal link is shown between excessive debts, the collapse of economic environment, the volatility of the situation and the bankruptcy of financial stakeholders. Because of all this, confidence is vital and its revival must be the absolute priority of the States, especially in stormy climates. In times of crisis, the State's duty is to fill the gaps left by the collapse of the private sector. Furthermore, only the force of a public kick is able to get a growth, dangerously hypothecated by the increase in deficits (whatever their nature or their origin may be) and by the aging of populations, back on track. Let us remember by counterexample the USA, which upon the election of Franklin D. Roosevelt in 1936 and while it (and the whole world) was still in a depression, reduced public spending so as to stop its debts. These austerity measures decreed at the time by the Roosevelt Administration to please the financial sector caused unemployment to jump to 19% of the working population and forced the aim of the American public power to create jobs in order to compensate for the massive layoffs in the private sector. Indeed, it is close in this context to the big uncertainties that Keynes suggested to the state to pay people in order to dig holes to bury bank notes in. Boutade however highlighted the crucial role of the state Regulator, revealing the pressing necessity to maintain employment at a level permitting consumption and keeping confidence. For that matter, hasn't the British Empire's public debt, throughout the course of its history (more exactly, since the start of the 18<sup>th</sup> century) reached unbelievable levels, at times exceeding 250% of its GDP? In effect, it is the gradual but irreparable decline that would have had to strike this country, in any case according to the standards wanting the landing of 90% debts in relation to the GDP trigger a restricting and volatile poverty cycle. However it is not its massive debt level that prevented the British Empire from taking down Napoleon and from jettisoning it in the Industrial Revolution taking place in the world. It is probably thanks to this lever of its debt that this empire prospered and got a relatively stable growth throughout the 19<sup>th</sup> century until the First World War.

To put it another way, if our political and economics leaders wish to avoid the return of the "Great Depression", they shouldn't deceive themselves about its reasons, at the risk of having to suffer a new one in the near future. Because the both dramatic and long period from the 1930s was not so much provoked by the financial collapse (which was no doubt striking and memorable) than by the irreparable increase in unemployment. So when it was of course inconvenient to let the banks go bankrupt one after the other, the main tragedy was taking being played out elsewhere – that is, in the employment market, which was unfortunately threatened by the American Federal Government's inability to react forcefully. This was reduced thanks to an economic adjust-

ment due entirely to the preparation of the Second World War. Waiting for this impressive revival initiated by the war industry, a Keynesian showcase, the USA nonetheless suffered (worse than the Depression) combined deficits reaching 25% of their GDP at the time, equivalent to \$4000 billion in today's money. Why did the Federal Government manage to get into such advantageous spending at the end of the 1930s and going into the 1940, given that they could have done it in 1931 and thus avoid a decade of superfluous suffering for a country? Put simply, for similar reasons to those that nowadays create tension between believers of growth and believers in austerity – that is for reasons of principle and ideology. In fact, the obsession with deficits – as prevalent in politicians then as it is now – was leading to counterproductive decisions. Indeed, public spending and other New Deal stimuli was substantially restrained in 1937 with the already known harmful effects, taking place while the economy was giving encouraging signs and unemployment was decreasing to 10%. Nowadays, rigor leads inevitably and in the same way to a similar debacle to that of the second half of the thirties in the general context of a stagnant employment market. Because the obsession with deficits eclipses the fight against unemployment which must be the priority. It goes without saying that it is not the decrease in deficits – as important as it is – that presides over the affected confidence of the general public. In this respect, the politicians have proved time and time again that they are bad economists given that the deficits in no way constitute a source to revive consumption, which takes the lion's share in aggregate demand. In addition, it is the very anemic employment market that is at the same time responsible for a consumption that remains at levels that are unable to have a domino effect on the economy and salaries that are reaching their limits. An evil combination that translates into a decrease in demand. Current perspectives, which are hardly brilliant, risk therefore of being worsened by the return of a new “Great Depression”, due entirely to rigor.

Why was this austerity policy imposed on peripheral European nations? Has the deterioration of economics 101 been inevitable? Or is austerity the result of the panic that seized hold of the markets which, in turn, has paralyzed political leaders? In this respect, the correlation between the soaring cost of financing the sovereign debt of these countries and the increase in austerity implemented is eloquent. Effectively it is the countries which have suffered the highest “spreads” – i.e., those which the markets were gradually squeezing for more and costly financing – which also implemented austerity measures and the most drastic hardships. The intuition according to which it is the financial markets and their threats of excesses which applied intense pressure on the European Union and on its leaders with respect to intense budgetary economies is therefore? Knowing that, conversely, austerity was not

implemented among the countries where the spreads remained stable. Since then, where does that leave us? That markets are “simply” in the end messengers, bearers of bad news? Namely that the deterioration of the public debt and the competitiveness of nations mechanically translated into a surge in their financing costs, which could only be controlled through all-round savings? Or that it is fear and collective panic which had a disastrous impact on the hollowing out of these spreads which are irrevocably far away from the fundamentals... a little like the surge in stock markets is regularly totally incompatible with the state of the real economy? Since the response to this dilemma is not obvious, you may doubt and opt for a second hypothesis. Nevertheless, it is crucial that a central bank be involved in this type of situation. Indeed, it is only its determination and action to provide liquidity is able to calm things down. It means accepting the verdict of the markets and leaving the overwhelming majority of our citizens defenseless. The ultimate objective of its intervention is to appease the markets and other stakeholders in order that the fundamentals are analyzed for those they are, and not through the prism of collective panic. And, indeed, the decision of the European Central Bank in 2012 and its governor, Mario Draghi to support the Euro “whatever happens” was spectacularly decisive. By agreeing to assume its role as lender of last resort, the ECB has calmed markets and eased the affected countries that have gradually seen a significant improvement of these spreads. Rather than consolidate public accounts of peripheral European nations, the ECB confined itself to having its presence felt, with a resulting collapse of financing costs in these countries. Thus, it is the countries where these spreads were the most degraded (Greece and Portugal) which benefited from the sharpest decline. As economic data did not naturally improve with the wave of a magic wand, it is thus easy to deduce that the financing costs fell at the same time as the “fear” factor. Moreover, it is in the countries where this fear had been the most intense that ECB intervention proved to be the most effective, since it is there that the spreads had fallen the most. It is even possible to push this reasoning even further. And to assert that the soaring cost of financing sovereign debt of these peripheral countries had no correlation whatsoever with economic fundamentals! Otherwise: how do you explain that these spreads are at reasonable levels today – far from their records in mid-2012 – whereas the debt ratios/GDP likely worsened in all the countries in the spotlight? Should the erosion in these statistics relative to their public accounts and their growth not have been “mechanically” translated by new records on the financing of their debt? Yes, but in the meantime the ECB had appeared suddenly confirming the intuition that it is the market panic – not economic fundamentals! – which had initiated the surge in these spreads. Austerity is therefore only the result of intense panic which seized our politicians,

themselves, under pressure by the financial markets, in the absence of lender of last resort. Let us push this reasoning one last time, since it is now very easy to make this statement: it is countries which implemented the most extreme measures of austerity which today have suffered the biggest decline in their growth. In short, there are nations which suffered an unprecedented austerity by panicked markets and European leaders, knowing that these sacrifices did not in any way produce the expected results. Indeed, they deteriorated more the foundations of these countries, including their ability to pay their debt. As such, the cash crisis degenerated into an insolvent crisis! This is the cost of listening religiously to financial markets which, far from being the messengers, are confined to sending bad signals all the time. Signs very wrongly interpreted by European leaders who are woefully ignorant in matters of finance and who embarked lightheartedly into a crossfire against public deficits. Meanwhile, for its part, the ECB was complacent in its splendid isolation until the situation became truly untenable, whereas its more precocious intervention would have avoided so much human suffering. To paraphrase Paul Krugman who uses the significant metaphor of “ducks”, the determination of our politicians and the economic and financial elite to impose austerity won’t get rid of the vermin or the bad taste in our mouths! It always returns despite all possible treatments, like the rigorous madness that persists to reduce public deficits that it is on the contrary essential to use wisely during a recession.

The paying back of debts is thus practically inefficient as soon as it takes place in a general situation of stagnant revenues. We will never repeat it as much: growth will only be brought back with public policies aimed at promoting full employment and improving revenues. Once returned, this growth will only be maintained under cover of a legal and equitable redistribution, crucial to re-establish the link between a growing productivity and increasing salaries. Without the progression of revenue, no long-term growth will take place. That is unless our politicians and economists have deliberately made the choice to transform our nation into one of leisure... Only “reflation”, a term borrowed from Fisher – will break the current infernal spiral.

## **Cleaning up the Financial System – A Prerequisite to Reducing Deficits**

In times of crisis, a recurring phenomenon wants private debt to progressively fall into the public's lap, or out otherwise, that they become debts owed by the public. The worsening of the crisis mechanically cuts into the ability of companies and households to pay back debts taken out with the banking sector. And this is where the state takes an increasing cut of the debts of its financial sector as the credit crunch intensifies. And this is why banking crises almost always precede sovereign debt crises. The escalate in private debt (of both companies and households) is cleared – in light of the crisis and using the banking transmission belt – by an explosion of public debt. To put it another way, the state resolves to call into question its own solvency by assuming the debts of the private sector. The States that have absorbed the losses and assets of financial establishments haven't done it so much as in collusion with, or out of kindness to, the banks, but rather in order to spare the economies of the potentially devastating consequences of bankruptcies. Nonetheless, the nationalizations and the losses – a far from saving the root problem – have transformed the banking crisis into one of sovereign debt. This is because our current crisis likewise tells the story of successive rescue plans, with a permanent characteristic being that both are as Paranoiac as each other. The billions injected in 2008 into Royal Bank of Scotland, Lloyds, AIG or again into Fannie Mae and Freddie Mac, like those allowing the bailout in 2009 of establishments that were sinking in the Dubai real estate market, certainly authorized placing the financial institutions under artificial breathing. Because of all this, this deferment – or this administered electro-shock therapy – agreed to by the financial establishments was but the inflation price of state debts. In this way, and although in appearance, the drama in the peripheral European countries had been initiated by its growing difficulties in assuring its market financing, the exposure of European banks to these countries was, in reality, what detonated this crisis. It is thus undeniable that the European banking system, which was in a risky situation, to say the least, played a central role in the financial liquefaction of the peripheral states of the EU.



This undeniable interaction between public and private debts must thus be translated as an involvement of each citizen in the fight against deficits. In other words, this tendency (or this plague) of debt is characteristic of our developing countries, which have cultivated since about 30 years ago, an almost chronic tendency for cycle of booms in debt followed by implosions. Indeed, we could estimate that the private sector debts of OECD countries have advanced at an annual average rate of 4-5% during these last thirty years! The deficits have, in this way, formed an integral part in the daily lives of our populations and of our States since the start of the 1980s, knowing that a hyperbolic increase occurred when the crisis started in 2007. It is this dramatic drop in market, real estate and, in general, assets valuations, that gave the decisive impetus to this financial crisis triggered in the spring of 2007. Indeed, it is in the countries encouraging property ownership – or rather real estate speculation – with the extremely lax rules in granting mortgages that the real estate market met its greatest slump. Among these countries are the USA (with the most threatened states, such as Florida, whose market dropped 60%), Great Britain, and even “new” countries but addicted to leveraging such as Dubai. The collapse of these valuations being the object of bank loans thus froze all the loans granted to companies and individuals by the financial establishments, leading to an understandable stagnation in economic activity and a worsening of the financial crisis. This growing scarcity of credit to the real economy since 2007 is thus responsible for an economic tightening, while it was the previously and very generously granted credit (between 2001 and 2004) that was responsible for the real estate bubble. Put another way, without debt our economies cannot develop and prosper, with the knowledge that economic activity always ends up dearly paying the price for too much debt.

Public deficits are therefore what result from this decrease, the immediate translation of which is the decrease in the State’s tax revenue and the increase in unemployment compensation payments and other social security provisions, directly linked to the difficult economic situation. It is also in this way that at least half of the public deficits of the peripheral EU countries in 2012 are due to the fall in tax collections and the unbearable increase in their debt interest. It is useless and counterproductive to reduce public spending in such a situation because these represent less than 10% of their deficits. When will we finally realize that the deterioration of public deficits is due only to the increase in unemployment? These days, our politicians are at a crossroads and must fight – and show a real obsession – by the “passive” deficit, which is mechanically created, because the increased unemployment prevents the state from offsetting its spending. The key priority being employment, those who are unemployed evidently will not be put back to work due to

reductions in public spending or the increase in taxes. The state on the other hand must consider the “active” side of deficits that consists in creating new employment and ensuring all welfare payments for its citizens. The only solution to reduce the public deficits brought about by unemployment is, obviously, to eradicate the unemployment. Passive deficits must be transformed into active deficits, that is, into deficits that are of use to the public which take over a depressed financial system to finance and re-establish all economic sectors. To put it another way, the path that will allow public deficits to be decreased is the one that will settle the financial crisis because the role of the state is evidently not to finance the economy forever. This reconstruction of the banking system must necessarily be carried out based on new rules. After having ridding the banks’ balance sheets of the toxic assets and having cleaned up their accounts, enforcement personnel must necessarily monitor the practices, supervise the payments and rethink in depth the training of bankers. At the same time, a restructuring of private debts must occur which, through a rationalization, or indeed wiping out, of a portion of their debts, shall re-establish their consumption and saving capacity. Public deficits must thus cease to be examined with fear by both politicians and central banks because to this day, they remain the only lever to recreate employment. Provided that the deficits are advisedly utilized, that is as passive one, they shall become active. In the absence of private financing, unemployment can only be reduced by public deficits in the knowledge that the private and banking sector must again fulfill their duty as liquidity providers whilst the financial crisis fades out.

Moreover, one after the other, all the arguments – or pretexts? – in favor of austerity fall like nine pins. Would deficits be an extra charge to be borne by future generations? Those who claim so have not always understood that increasing the debt today is not in any way an inter-generational transfer, but an intra-generational one. Since it is the debtors – tomorrow – who should in fact reimburse tomorrow’s creditors. Do deficits harm investment? So in times of a depressed private sector, the state must specifically step in rapidly to pour cash into its economy. Would these deficits lead to soaring interest rates? Indeed, to the contrary, in any case in heavily indebted countries, which nevertheless have their own “sovereign” currency, namely the United States and Japan... In short, the state should instead take on more debt and bigger deficits in order to restore full employment, even if our current leaders flatly refuse to use debt to stimulate economic activity. Their single and only objective – or obsession? – thus being to balance their budget. Is tax consolidation a policy? While the ambition of our leaders (men and women) should instead be to stimulate investment and reduce inequalities! How can they continue to defend austerity – and therefore the acceleration of unemployment – when they can use tax as a leverage wisely and fairly

at the same time, while putting pressure on the European Central Bank, which is completely uninterested in growth. Public spending is drastically revised downwards while efforts and energies should be focused on increasing the taxation of the wealthier classes, and the active contribution of the ECB to growth recovery. Unless the fallacious argument behind which lurk the proponents of orthodoxy which are being used to divert attention from their real motivation. Who would have the state take a step backward time and time again, exactly as the current British model and the admission of the Prime Minister who just stigmatized the poor and unemployed, according to him, had “made a choice lifestyle”... It is therefore in the name of “structural reforms” and “there is no other alternative to stringency” that we blithely saber social spending, and we oppose any veto contemptuous of any job creation that would call for state stimulus. Like the President of MEDEF professed, as “life is fragile, love is precarious, why would work not be insecure?” Thus, the ardent defenders of finance and healthy accounts require that the employment level be dependent on only the degree of confidence prevailing in the business community. While it has been repeatedly documented in the last twenty years that the stock market and financial speculation was the main reason for the deterioration of economic conditions. Under the guise of an economic argument, this diehard obstinacy which fights fiercely against the doctrine of full employment yet masks less and less its true political, even ideological, motives. Narrowing public spending strictly to income earned by the state is in fact nothing more than a moral tale told by those who set themselves up as lecturers in liability 101. Behind their storytelling which abuse ordinary people who are made to believe it is necessary to manage the budget of a state in the same way as the purse strings of a household, these destroyers of deficits preserve very prosaically the interests of the dominant class. The very one who, seeing everything through the prism of material accumulation and enrichment, saw itself described by Keynes as “semi criminal” and “semi pathological”... All the while supportive of the dominance of annuitants on our economies, this dictate of austerity also reveals a ruling intellectual class that definitely fails to address the economic fundamentals from the right angle. Why not indeed integrate this debt equation into parameters as compelling as the level of interest rates and inflation? And why continue to insist that a healthy economy must necessarily be balanced (budgetary and accounting) when an economic activity – by essence dynamic, i.e. unstable – occasionally requires the soothing injection of public funds? It is therefore important not to confuse economy with morality, for those who need support have committed no sin. Before – well before – the state seeks to balance its books, its only concern should be getting its citizens back to work.

## **Spend more to Earn more**

France in Consequently, we better understand why austerity measures and other cuts in public spending are instantly doomed to fail in times when the economy is in desperate need of oxygen. Economic activity is thus condemned to fall back and public deficits to worsen with it, in the absence of sufficient loans granted by the financial system to economic actors, and in a situation when the government reduces its spending or increases tax rates. It is also in this way that 25 billion Euros worth of French taxes in 2012, with 33 billion Euros to be added to them in 2013, just like the latest Spanish austerity plan (to only mention this country) consisting in new efforts of 65 billion Euros, will inevitably and logically translate into an economic recession, becoming totally counterproductive. In particular, who has undertaken to “find” 100 billion Euros in order to balance out its budget in 2017, must quickly choose its side. It is undeniably half-way between the inner core and periphery of Europe, which likes to flaunt a “Norwegian” tax system, risks finding itself in the short term in an unsupportable position in which its competitiveness decreases even more due to an overvalued currency. In fact, by wanting to be a part at all costs of the inner European core, (on the same level as Germany), France shall be cruelly left (by rejection) on the periphery. In fact, isn’t France Europe’s runner up in terms of taxation of capital? Does she not try to discourage investment from the top of her implicit tax rates (capital) which is (according to 2010 statistics) 37.2%, just behind Denmark’s current rate of 39%? In 2013, the taxation of the return on corporate capital, the increase in tax on profits, the tax surcharge on households should, for once, put France at the top of this classification. Knowing that it occupies already second place in Europe – and therefore the world! – regarding the taxation of property, just behind Britain. Indeed, it is in the countries encouraging property ownership – or rather real estate speculation – with the extremely lax rules in the excise duty of mortgages that the real estate market met its greatest slump. Gripped by a vice between their European commitments and market demands, our European nations thus get us into a terrifying circle in which withdrawals – worsened by the goal of trying to respect their commitments in terms of limiting deficits – slows economic activity down even more. Not only does it ask us to suffer the costs of this slowing down of activity but our want to consume and

invest is definitively disturbed by the reduction in our revenues. So then, because of the decline suffered by the Euro Zone in 2012, these are quite the opposite of the public support measures that would need to be implemented in a general context, in which the global investment, consumption and commerce engines are broken down. The austerity imposed on weakened nations in the midst of an economic downturn is turning out to be harmful. This is in addition to the knowledge that this same austerity becomes totally useless insofar as the financial sector gets better and starts to take on its role as a lender again. Consequently, public deficits and their ratios (reducing the GDP) are a necessary and unavoidable evil until the financial sector restores itself. In reality, these public deficits are the only engine that economic activity can avail of... the only lifeline for growth. They will naturally be inclined to take a step backwards, or indeed be completely diminished, as soon as the private sector takes the helm of the action and public funds. But let us not skimp past social spending in times of crisis because it is not these economies that will reduce our deficits but rather it is these economies that will weaken and worsen the citizen. Cuts in public spending, decreases in unemployment budgets and minimum salaries such as the reduction in the State's lifestyle will have little long-term effect on our public accounts while they kill of the economy in the short term. We can see an increase of these deficits because of the additional decrease in the State's tax revenues. But let us get one thing clear – these are not debts that damage growth. Rather, this causal link should be inversed: deficits are mechanically created by the step-back in growth. This is fortunate because we can but congratulate the state for being there to inject its cash that will prevent the paralysis of our economy. It is imperative that we consider this inversed causality and accept that economic crises are not induced by public deficits so as to no longer adopt bad measures that will only worsen the situation. This is why the appropriate responses within the framework of a recession initially caused by a drastic weakening of banks and the financial circuit – supposed to clean up the economy – consisting in more public spending, combined with tax reductions in order to revive activity. The revival, which will inevitably be the meeting point, will bring back the growth that will in turn allow the decrease, or indeed disappearance, of public deficits. It is thus, to paraphrase Keynes, in times of luxury that are the ideal times to use austerity and not times of economic crisis. With the spending of one being income for the other, these are the revenues of all of the consumers, stakeholders and business owners that are also condemned to drop if they reduce their spending at the same time in order to repay their debts. That being said, the problem with debt only worsens because, as Fisher put it “the more the debtors pay the more they owe)” in describing this calamity that is the “debt deflation”. It is precisely in this kind of set-up

– when the private sector is only worried with repaying its debts – that the public sector must do exactly the opposite, i.e. spend!

The improvement of my personal financial situation is necessarily dependent on the increase of my income or the decrease of my spending. Nonetheless, the problems that I am personally faced with are not similar to those that society must manage. If I reduce my spending in order to improve my own financial situation, the global income of society that will decrease due to an individual's decision to spend less! In the same way, if I wish to increase my spending without resorting to loans, I must inevitably call on my savings. The logic is thus unappeasable: if society's consumption has to increase without worsening the loan situation, it's savings that must be called for. One this is for sure, the post-crisis economy will necessarily have to be restructured based on healthy values such as savings. Today, these saving however hinder the resolution of our immediate problem by slowing down the increase of aggregate demand at the heart of our economies. Keynes had very cleverly identified this paradox of frugality: to promote saving in present conditions will only increase the recession. The challenges for society are thus not equivalent to my own challenges, just like the long-term measure to clean up and consolidate our economy are not similar to the actions that are undertaken today so that this recession does not turn into a depression. In fact, certain decisions liable to improve our conditions in the long term do nothing else but worsen it today! Consequently, all of our efforts must go towards increasing the aggregate demand and, in this perspective, the States must strongly contribute to increase their debts in order to promote demand and consumption. These growth engines shall be subsequently replaced by exports and by the investment of businesses, which will allow States to reduce their debts, due to a reduction in their spending, together with tax revenue stimulated by the recovery.

On paper, the discipline consisting in limiting public debts in relation to the GDP works well because it provides reassurance by placing a guardrail up against the spending madness of politicians. The very fact of reassuring the markets allows borrowing at reasonable interest rates according to a supposed undeniable logic in which state spending is proportional to taxes. And this is why this concept of deficits reducing the GDP shows its limits insofar as the country concerned is hit by a recession needing large additional expenditure by the state in order to try to sustain the demand. This is why – in theory and in a perfect world – the prolonged prosperous periods of growth must be built on in order to balance out the public accounts, or indeed to gather up excesses. Meanwhile, it is understandable that deficits accumulate when public funds are used with the goal of reviving the economy. They are the

result of a recession but allow us to fight the spiral threatening the economy's lifelines. To put it another way, the deficits are acceptable as long as they allow us to block this slippage in which companies considerably decrease, or indeed totally stop, new employment (when they are not simply fired), because they forecast a decrease in their production and services. At the same time, the consumer is led to become withdrawn because of fear of unemployment and uncertainty. It is there that the state must intervene in assuming its duty to regain confidence by injecting stimuli. It is thus in such an economic situation that hollowing of public deficits in no way constitutes a catastrophe because it allows the economy to be kept on a drip. The deficit in this way transforms into positive energy which benefits all economic actors.

Moreover, deficits form whenever consumption goes beyond production capacity of the country in question. This is when we become dependent on foreign capital to finance a more or less substantial part of our lifestyle. We immediately think on Chinese capital which inundates the United States in the hope that in return, it buys Chinese products. We should also think about the French and German capital that has been poured into countries such as Greece and Spain since the launch of the Euro, who in turn bought French and German products. This massive influx of capital towards the European periphery is reversed as soon as financiers and investors have been gradually convinced of these countries' weak repayment capacity. Likewise, China would be forced to withdraw from the United States if it one day lost confidence in them. This type of deficits similarly leads to a negative dynamic which can only be fixed by re-establishing the production capacities of the country in question, with an inevitably positive impact on employment. Whatever their nature and origin may be, public deficits must be turned against the recession that hit the country and they must be considered as a weapon to revive aggregate demand. Only voluntary policies to intensify public spending and advisedly reduce taxes will allow this vicious cycle, fed by half-mast consumption and production and by the escalade in unemployment, the effect of which in turn is to damage demand, can be broken. Only state intervention can clean up, revive and regulate economic activity. The austerity advocated by orthodox believers turns out to be contrary to nature because the state proves to be essential and unique in this breath that it breathes into its national economy. The state mustn't therefore come across resistance in its path or any limitation to its stimulation of the economy – its only limit and horizon being the restoration of employment. After all, it is possible to decree growth!

## **Deficits Created by Under-exploited Resources**

We thus find ourselves today in a world of reversed values in which the majority of the specialists prevent the state from undertaking new spending while at the same time being aware that only these injections of cash can save the economy. For these champions of budgetary economies, it is unthinkable to further widen public deficits to save our economies today whilst at the same time the recession can only be fought off by stimulating activity by the agency of an increase in public spending. This is why an almost generalized consensus prevails according to which the Western States, already virtually bankrupt, wouldn't know how to face any more spending. This is at the same time as the latter offers the only exit door out of the recession and stagnation. This tyranny of rigor – this dictum of frugality of public action – further disguises itself as moralistic with the opinion that future generations shouldn't have to pay the price for today's excesses. Deceitful reasoning according to which the loans taken out today will mortgage the future, which is unacceptable for the citizen to live in and for the state to spend beyond their respective means. And which justifies this collective suicide by a strange argument according to which the stimuli applied today would in reality be the loans to pay back tomorrow. However, the arguments on public spending allow the immediate use of all resources and all production tools at our disposal. It stands to reason that the intensive exploitation of resources creates wealth and that the cash injections from the state generate revenue. The stimuli and public spending are a self-fulfilling prophecy that mobilizes the economy's production capacity whilst allowing new employment. Public spending exudes therefore wealth and material comfort because it is the utilization of our production capacities and all of our resources – including human resources – that galvanizes our economies. The stimuli are not thus a responsibility that must be assumed by future generations and they do not steal tomorrow's jobs. On the contrary, they allow current activity to develop via the exploitation of resources that couldn't be built on without this public spending. Public deficits are an authentic instrument to resurrect the economy which efficiently replaces private investment in times of crisis. Indeed, public spending also creates wealth and revenue. And this is why with the only perspective of private companies being profit, they are completely indifferent to the exploitation of resources



and to the increase in national wealth. The company and the system cannot thus bank on a private sector in times of crisis that will certainly not pay out with the goal of creating revenue for others.

To increase loans today in no way clouds the perspectives of solvency of future generations. In fact, the loans initiated today create the wealth of tomorrow! The debts taken out today, together with the stimuli injected bring back a transfer of resources. It is in effect in the future, within the framework of repayments, that the debtor clears all or part of its debt to the creditor. This debt service constitutes therefore an intra-generational transfer – not intergenerational – of wealth. To take out new debt today will not clear a net expense and pay all the bills of future generations. To support this reverse theory – that is to claim that loans mortgage the future – goes back to implicitly recognize that today's production prevents and damages tomorrow's production. This is evidently not the case as it is not because we produce more vehicles, more computers or because we modernize such industry or such company today that we will stop producing or working in this way tomorrow. According to this same intra-generational transfer logic, the agents that have to pay our debts will form an integral part of a cycle – by nature a closed circuit one – where they will be the carriers of a redistribution of resources in favor of creditors who will be their contemporaries. This circuit is purely intra-generational therefore, following the example of the current public deficit which will have to be offset by taxes (and other payments such as VAT) which the future generations will have to pay off because of the debts taken out today by the state. These liquid assets will thus return tomorrow to the state. This analysis of current debt which does not represent a handicap for the future is moreover implicitly accepted by the traditional economists who recognize that public debts are not an inextricable problem or even an unbearable burden on growth. The only proviso rightly issued with public deficits is that they lead to an increase of interest rates that evidently has repercussions on the private sector, which in turn decreases or even cancels its investments.

Whatever it may be, the solution exists in order to keep these interest rates low, even within the framework of major public deficits. The key to controlling costs linked to financing debts consists in the optimal utilization of all resources and an intensification of the production of the economy's acting companies. Indeed, it is nonsensical that interest rates increase – that is that the money's rent is more expensive or that there is a scarcity of capital, so long as the situation in which resources are not exploited lasts, production still hasn't reached its limits and under-employment persists. The extent of resources still available, maintaining unemployment and the amount of services to assure and products to

manufacture that is still physically possible to pour into the economic circuits should, on the contrary, mechanically implement tax decreases, whatever may be the background of the public deficits, which or no more than an epiphenomenon. In order to corroborate these assertions, we must try to understand the cause and effect relationship between the unexploited resources, unemployment and revenue. It is undeniable that the additional demand in capital (that is, the injection of stimuli or the acceleration of credit) favors spending which, in turn, stimulates revenue so long as the original shortage in which resources are under-exploited exists, factories do not operate at full capacity and unemployment persists. Indeed, so long as the consumer – whatever the commodity or service required may be – won't be satisfied, its demand will automatically create an increase in revenue and savings on the other side of the chain. Revenues will only cease to be influenced by this law of offer and demand whenever a balanced situation is established and all capacities of the economy are built on. It is at this stage that credit will no longer be necessary or even useful and the revenues will logically be able to stagnate because the gap between unexploited resources and the demands of economic actors will have been filled. The variable of revenues is in this way like mercury that reaches its point of equilibrium. It is crucial to understand and accept the fact that these unexploited resources (which reflect the deficiencies of an economy) must be translated as an increase in revenues, essential to fill this gap. The equilibrium between loans and credits materializes when it is no longer essential to take out new loans, that is from the moment where all of these resources are taken advantage of and as soon as full employment is established. This likewise signifies that it is not the interest rates that must increase when the situation is unbalanced and that the economy shows malfunctions as it is at this point that it most needs capital.

Rather, it is the salaries and revenues that must be increased in order to play their domino effect on the economy, in the knowledge that, additionally, the rent of the money benefits only a miniscule number of actors. Let us inform our Finance Ministers and CEOs that the salary variable is fundamental in relative strength of the economies. Our lessors (who of course are keen to lend at a higher rate) must accept that our economic activity – and thus our public deficits – will greatly improve by increasing the salaries variable rather than the incidental interest rates variable. It is wrong to think that interest rates increase because of an increased demand in loans and capital. Indeed, more credits lead to more spending and thus to more revenues and more savings. It is consequently this new savings that becomes new finances. These new available liquid assets will meet the new needs of creditors, in such a way as an increase in interest rates will not be necessary given that it is the initial credit that in part feeds the savings, which in turn

becomes new loans. Furthering the knowledge that the proportion of credit not turned into savings profits the economy by having a positive influence on revenue through the famous multiplier effect anyway, this great benefactor of economic activity single-handedly justifies the spending and credit. It is in this way that 100 Euros spent in Shop A accordingly increases the revenue of A knowing that this process is quickly stopped if A chooses to save all of this sum, which will nonetheless be used for new credits and will benefit the system, in any case in an optimal world and cycle managed entirely to benefit the cycle. If A only saves 50 Euros and spends 50 Euros in B, it is thus B's turn to benefit from an increase of its revenues, which will in turn benefit one or several others if B decides to thus extend the process. The multiplier effect continues until all of the initial 100 Euros is placed into savings, or to put it otherwise, until what no longer becomes spending for one and savings for the other is completely placed in savings. It should be noted that, if only this circle is dedicated to the good operation of the economy, that is provided that all the stakeholders "play the game", the credit, the stimuli and the spending benefits either the revenues or the savings, shall be recycled into credit.

The consequence being that the interest rates variable really is nothing more than an epiphenomenon, a sort of useless parasite that only benefits those who refuse to ensure the economy's liquidity, those who continually increase the stakes for their own personal profit all the while looking down on the rest. It is this same logic that allows us to conclude that public deficits – however high they may be – are not prevented from affecting the interest rate and, moreover, there is no lacking in examples to illustrate this point. It goes without saying that this lack of correlation between massive public deficits and the soaring of the fees to finance this debt by way of punishment by the markets is evident in the United States – a fine example of great financial clout and an undeniable government. How do you explain the rise in interest rates since the end of the nineties to the end of Clinton's Presidency, at the same time as the American Federal State's budget was exceeded for the first time in decades? And how can we understand their decrease since the accession of his successor, George W. Bush, given that the latter had to irreparably increase the deficits? The best example however is that of our current crisis – strongly marked by debts – and which is nonetheless characterized by practically zero American interest rates! Interest rates are not therefore exuded by high deficits, but they are what results from an inadequate monetary policy or from investors having unilaterally decreed a punitive raid against a country, that is to say and in all cases, from an arbitrary decision to increase interest rates.

## **Public Deficits and Redistribution of Resources within Society**

What is the real impact on the States' spending deficit and other stimuli applied in favor of the economy? To put it another way, is one Euro spent or one Euro of tax deductions one more Euro of extra deficit for public accounts? After all, the subsidies agreed to by the state lead to revenue, greasing up the economic wheels, which increase the State's tax revenue. This is why the ayatollahs of the deficit, who haven't stopped vilifying public spending and condemning the stimulant measures from the state, are wrong in calling on the burden that they will make up for future generations. Because the debt taken out today by the state, that which is injected into the economy and in favor of its actors, certainly represents a tax to be paid back tomorrow but it likewise constitutes a transfer of wealth. By indebting ourselves today, we understand the wealth of creditors all the while instantly lightening the burden carried by the debtors. Public debts, of which the object is to stimulate the economy, to exploit resources and to reduce unemployment, do not therefore lead to a genuine responsibility for stakeholders but must rather be considered as a simple transfer of wealth and assets of the crediting group which is limited to placing its available liquid assets in the right place and for the biggest benefit of the real economy. In the same way, this transfer carries with it a redistribution of the future production to benefit companies who will have been able to get these investments. In other words, those who flip out over the state taking control of its economy in times of crisis and those who violently and persistently critique public deficits are not moved by an altruistic vision or by a will to instill a tax regime... their vehemence is understandable. It is this transfer of wealth that is so feared, that deprives the person of leisure in favor of those who truly profit the economy by their work, by their inventions and by their aptitudes. Moreover, this concept of debts being something to be assumed by the people of tomorrow must be again modified. Indeed, the stimuli injected into the economy will not fully translate into immediate growth, but will likewise positively affect long-term growth. Investment, the modernization of our enterprises, the development of technologies, training for those at all salary levels thus increases the production potential in the mid-term and short-term with

naturally favorable consequences to those who, tomorrow, will have to repay our debts – not to mention the multiplier factor associated with this type of stimuli which largely surpasses the unit. Investment, the modernization of our enterprises, the development of technologies, training for those at all salary levels thus increases the production potential in the mid-term and short-term with naturally favorable consequences to those who, tomorrow, will have to repay our debts – not to mention the multiplier factor associated with this type of stimuli which largely surpasses the unit. This brings us back to say that those investments, such as those previously stated will translate, for the economy and stakeholders, into profits and production savings largely exceeding the amounts injected. And what can we say about future tax collections from the state that are greatly improved? This is why the public deficit must be considered as an investment in the future. This is why a given and well-targeted stimulus of 1 or 100 billion Euros will not lead to a clear increase of 1 or 100 billion Euros.

These wealth transfers further act to the detriment of this very small proportion of the population having the chance to save and which thus benefit from high revenues. Moreover, let us not forget that the proportion of men and women who live off their work in our Western nations decreases little by little compared to persons of independent means and pensioners. The state must thus issue national loans, mainly aimed at well-off citizens, with the aim of actively and intentionally carrying out a redistribution that will affect the best-off. Apart from the fact that this loan will not be confiscatory – given that it will be remunerative and must be paid back in time – the economic revival will clearly benefit these privileged classes, which will be largely made up for in their solidarity. The state must thus issue national loans, mainly aimed at well-off citizens, with the aim of actively and intentionally carrying out a redistribution that will affect the best-off. Apart from the fact that this loan will not be confiscatory – given that it will be remunerative and must be paid back in time – the economic revival will clearly benefit these privileged classes, which will be largely made up for in their solidarity. The reasoning is identical in relation to the tax increases which will today affect the well-off and wealthy classes, who will benefit at the start of the economic activity reboot. After, won't these stimuli be injected into the economic cycles in which these privileged actors play a specified role? Indeed, the state has the advantage of operating a progressive taxation scheme which will allow a better stimulation of the economy. Because it makes no sense whatsoever to impose more heavily upon the poor and middle class because of their relative low incomes. As they are unable to save, they spend the product of their wages, and this product would be more useful to the economy if it were used for consumption instead of taxes. Whereas the progressive

and significant increase of taxes on the well-off class – which is able to save – is economically beneficial because these amounts collected by the state (and which otherwise would be hoarded) flow back into the cycle to benefit a larger number. Given that the wealthy consume a large amount less as a percentage of their income, the increase in their tax rate thus allows a stimulation of economic activity which would not have been able to otherwise profit their savings. Whilst taxing the poor and middle classes doesn't unduly benefit the economy because these amounts will be recycled into the consumption cycle anyway, this withdraw from the wealthy turns out to be highly beneficial to the mass as it injects amounts aimed at saving into the economy. In times of crisis, it is thus recommended to establish a relatively strong progressive taxation in order to better divide out the wealth, to reduce inequalities and, finally, to avoid depression. The ultimate objective is obviously to redistribute the wealth at the top of the pyramid down to the bottom in order to stimulate the consumption of those who live from the product of their work. It is thus an inversed "tax shield" in the sense that it is imperative to put a limit to the tax rate of the middle classes and the poor with the aim of maintaining their purchasing power. It goes without saying that this tax system – which must be stressed on the well-off classes in times of crisis – must be lightened at the start of the economic revival or in times of inflation. We must therefore reverse the logic and the prevailing arguments and realize that the presence of unexploited and neglected resources, combined with an unemployment, the main reason of which being the often gaps in employee training, necessitate the implementation of wide-scale programs that allow this vitality to return to our economy. Society as a whole will moreover only be able to benefit from stimuli that allow unemployment to decisively step back, all the while improving all incomes. Consequently, the concerns, or indeed the anguish, in relation to our public deficits are very clearly exaggerated and force us to superfluous restrictions because of deceitful or self-serving reasons. After all, wasn't it Hyman Minsky (1919-1996) who suggested not thinking of balancing our deficits unless full employment was re-established?



## **National Currency – The Supreme Weapon against Deficits**

All public debts are not worth the same. In this respect, it is crucial to have a clear distinction according to the monetary system adopted by the country with which we analyze public debt. Indeed, a country benefitting from a fluctuating exchange rate, that is one in which the currency isn't able to be exchanged into another currency over a certain period of time at a fixed rate, or indeed into a precious metal as was the case with gold standard, never risks going into bankruptcy. A sovereign country that freely issues currency-denominated loans does not have to face the potential consequences or usual measures of market retaliation or pressure whenever they engage in spending that greatly exceeds their budgetary capacities. To jump into programs allowing it to stimulate its economy and to guarantee its citizens their social benefits, this country – which enjoys the absolute monopoly in the issuance of its national currency – avails of a solution that allows it not to increase taxation and stop sinking amidst the mass of markets to be financed. Indeed, it is sufficient to credit bank accounts with the currency that it alone has the power to issue. Contrary to a country having abdicated its monetary sovereignty by indexing its currency to another one and which is thus naturally limited in its capacities to print, and even more so, to spend its own currency. The example of countries having correlated their national currency to the American Dollar shows beyond a doubt that they can only issue their currency in amounts that allow them to maintain the level or the fluctuation range defined in relation to the dollar. Their freedom to print their own currency is also restricted by the compatibility with this indexation, which instantly renders their currency non-sovereign and extremely subjected to market waves that do not hesitate to launch into speculative attacks against a currency that would have been issued in too large of amounts and forced to leave this indexation – in other words, default payment. Their freedom to print their own currency is also restricted by the compatibility with this indexation, which instantly renders their currency non-sovereign and extremely subjected to market waves that do not hesitate to launch into speculative attacks against a currency that would have been issued in too large of amounts and forced to leave this indexation – in other words, default



payment. Their freedom to print their own currency is also restricted by the compatibility with this indexation, which instantly renders their currency non-sovereign and extremely subjected to market waves that do not hesitate to launch into speculative attacks against a currency that would have been issued in too large of amounts and forced to leave this indexation – in other words, default payment. Drawing up public debt in a foreign currency – an option chosen by certain companies – also represents a potential danger that cannot be ignored because this very same public debt can represent a threat for the state in question, which is unable to print this foreign currency in order to fulfill its obligations. The only source of foreign currencies being that of exports which, in times of global financial crisis, or loss of competitiveness of companies of the debtor the country are likely to fall and thus have a disastrous impact on the inflows of foreign currencies. Not to mention the risk of a sharp appreciation of the foreign currency in which the state borrows which, combined with a fall in exports, could expand losses and extol deficits. A state which borrows in a foreign currency, believed to be reliable and safe for its creditors, thus leads to the opposite effect to what was initially sought.

Let's digress a little to note also the known risk that the private sector takes by borrowing in a currency other than its own, thereby placing it in an extremely fragile situation, for the same reasons as those likely to affect its own state. This brings to mind the acute crisis of certain Eastern European countries (such as the Czech Republic or Latvia) whose households and businesses had borrowed in Swiss Francs prior to the 2007 crisis, persuaded by their banker that the interest rates of that currency would remain low, with promised savings on their substantial financing costs *vis-à-vis* their own currency or that of the Euro. Logic pushed so far that the private sector of certain emerging European nations had even borrowed up to 90% in foreign currencies, the regional European average being 50% of private credit arrangements contracted in foreign currencies, of which 20% on average only in the Swiss Franc. If the interest rates of the Swiss Franc were indeed maintained at insignificant levels as the bankers of these emerging Eastern European nations had thought, its safe haven status had to, however, catapult it to more than 30%! The consequences proved catastrophic for those debtors who did not normally have any revenue in Swiss Francs and nonetheless were forced to make repayments of 30% higher on their debt. Let's also think about the number of French municipalities and towns which had, under the impetus of a (sadly famous) European bank, decided to index their borrowings to the exchange rate of this same Swiss Franc, convinced by their banker that they would maintain their financing costs under pressure with respect to the "high stability" of this currency. French towns which today find themselves in an inextricable situation,

near bankruptcy, since this massive appreciation of the Swiss Franc forced them (by the series of ratchets under their contracts) to have to pay interest rates of almost 25% per annum on their debts! In conclusion, no one – neither state nor the private sector – should venture into debt in a currency that is not its own without risking default if a single parameter goes wrong.

In addition, the decision for a country to correlate its currency – or even abandon it altogether – in favor of another therefore amounts to giving up fully its monetary policy, and sometimes tax, which provides yet an immense privilege. In these times of European turbulence, we think obviously about the members of the EU handing over the reins of this privilege to the supranational institution known as the European Central Bank. As these countries only use, and not issue, Euros, they are able to finance their lifestyle with tax levers and bond issues. From this point of view, an emerging country that has a sovereign currency clearly has more flexibility in determining its public policies than Germany! Hyperinflation is certainly a threat – it remains the only one! – able to limit the enthusiasm of those nations which are still fully sovereign in their ability to print their currency in virtually unlimited quantities to fulfill their duty to their citizens. Of course, we think about the textbook case of Zimbabwe or Weimar... However, a country that was even a few years ago the second most important economic power in the world, and today is the third, strongly credits bank accounts and prints money en masse – Japan –, without any hyperinflation and even without incurring the slightest surge in its financing costs. It is precisely because Japan has a monopoly on issuing yens and its public debt is denominated in this currency that it does not suffer the fate of Greece despite a reduced ratio of debt to GDP even less enviable than that of this same Greece. And the argument of a few according to which the Japanese public debt is only quasi held by its citizens is not welcome. A sovereign country remedies its sovereign debt and honors its creditors by crediting their accounts, that its public debt be held by strangers or by its own citizens.

Hence the reason for a fundamental ingredient which is always at fault with the Euro, which is far from being a “sovereign” currency unlike, for example, a country like the U.S. which has its own sovereign currency. In fact, for the members of the Euro zone, everything happens as if they had opted for a foreign currency, somewhat like how certain “dollarized” countries indexed their currency to a standard. Indeed, certain mechanisms of assistance to members in need are already acting as shock absorbers and even the presence of the ECB instills some flexibility. Nevertheless, the countries united under the Euro banner are not recipients of considerable advantages that are conferred on nations

issuing a sovereign currency. In this regard, the Greek creditors unveil this structural weakness intrinsic to European nations which use a de facto non-sovereign currency. In fact, a country which issues its own sovereign and freely convertible currency can never go bankrupt since there are no limits as to how much of its own money it can print in order to settle its debts and operating expenses. There are no restrictions stopping it from borrowing on markets and, in absolute terms, it can issue its currency in sufficient quantities to pay interest and its debts so as to finance its multiple deficits... Thus, this country is not, in theory, subjected to any spending limitations since it benefits from the sovereign privilege of crediting several bank accounts in its own national currency without worrying about the surge of interest rates on its bonds. Indeed, it does not issue its borrowings under the restriction knowing that, whatever happens, it can pay the interest by printing even more of its national currency... This is precisely why a country such as Japan, whose debt ratio/GDP is double that of the PIIGS, pays modest interest on its Treasury bonds: it issues a sovereign currency. However, a country which borrows in a currency that is not its own or whose national currency is indexed to a foreign currency (or to gold) risks defaulting on payment in case of a grave financial crisis. That is why certain European nations must be faced with an increased spiral on the financing of their debts even when their ratios are less spectacular than those of Japan, or even the U.S. From the point of view of member nations of the European Union, the Euro remains somewhat like a foreign currency. It is little like if the member nations had indexed their former national currency – even underlying – to the European currency, and a little as if they had permanently incurred debt in a foreign currency where they do not benefit from the privilege of issuing it as it would seem proper for them. Thus, the different central banks of countries which adopted the Euro and all have accounts with the ECB – only to issue these same Euros – benefit only from limited monetary reserves: the funds provided to these nations by the ECB are effectively proportional to their Treasury bills subscribed by the markets and investors. A country like Spain is therefore restricted in this arena and forced to borrow at impossible rates since it does not have the advantage of printing its own bills or the possibility of unlimited support from the ECB. Today, European leaders are still ignoring this weakness in the system. Indeed, they act as though they do not understand the concept of monetary sovereignty whereas the implementation of the Euro presented since its introduction a “congenital” defect?

In such a context where the Euro presents this original sin heavy to assume, it is strictly impossible for a number of these member nations to reboot via a massive depreciation of their national currency. Incapable of reestablishing their captivity in favor of boosting their exports, these

countries thus find themselves in a catch-22 system of deflation and buried under the weight of their ever worsening indebted situation. As their citizens are only – after all – human beings, who for the most part have very largely punctured their threshold of tolerance, default payment remains therefore the only honorable solution. With, at the helm, financial and economic chaos This is why we in Europe are currently living an authentic revolution of mentalities which are forcing us to mourn an illusion that comfortably cradled us. With, at the helm, financial and economic chaos. This is why we in Europe are currently living an authentic revolution of mentalities which are forcing us to mourn an illusion that comfortably cradled us. The myth of the state as protector and ultimate refuge has officially given up the ghost, since we know now that our – non sovereign – state can go bankrupt. The myth of the state as protector and ultimate refuge has officially given up the ghost, since we know now that our – non sovereign – state can go bankrupt. Well before the creation of the Euro, the Canadian, Robert Mundell (born in 1932) specified the conditions for a successful monetary union. These works garnered him the Nobel Prize in 1999, i.e. precisely the year in which the single currency was launched. According to Mundell, a shared currency by a geographic region would only be viable in the case of mobility of capital and labor, flexibility in salaries and prices, similar economic cycles and tax transfers within the zone. In other words, money and workers should be able (and want) to travel and establish themselves in different parts of the EU. Prices should even decrease if necessary and not only increase. The members of this Union should benefit both from economic expansion or suffer economic contraction together. Finally, a solidarity (ideally automated) should allow some regions in turmoil receive financial support from an agency created for this purpose or by a federal government. Today, the European Union does not have any of these advantages, making it an unsustainable Union, at least according to the Mundell criteria, unlike the United States whose structure allows it to absorb economic shocks. Of course, an unemployed person in South Carolina can move to Texas where he has just found work while a Greek would find it very difficult to establish himself in Sweden and vice versa. Apart from the language barrier and mindset, a European country, devastated from, or undergoing, a sharp economic slowdown would, in addition, receive no subsidy from its central administration allowing it to stay the course and successfully fight the recession. Thus, the union in effect in the U.S. only functions because its workforce can move freely from state to state, where constant interzonal capital flows and institutionalized automatic mechanisms cushion financial shocks. Indeed, not content with these congenital defects, the European Union turns out to be even a machine producing bubbles – that is to say, imbalances – due to a single interest

rate divided by regions and nations which are thus subject to actual divergent exchange rates between them. In the actual European context, the Euro actually acts as a gold standard, whereby the adjustments and essential readjustments – which cannot be achieved through the relief valve of appreciation and devaluation – are done exclusively by the transmission belt of prices and salaries. The Euro clearly cannot be converted into gold, but – in the absence of the characteristics described by Mundell and in the presence of a uniform rate of interest for all members – it compresses economies and produces recession. Since the prevailing gold standard is reflected in adjustments to support systematically weak economies and currencies while sparing the strong countries. Is this not the peripheral Europe which suffered and cashed in all imbalances within the framework of the actual European crisis? Remember the purpose of the gold standard which exerted a downward pressure on some fragile currencies of nations undergoing economic contraction and therefore high unemployment, unable to make the necessary domestic adjustments. The Euro – as the gold standard – makes the situation worse for countries in recession by creating deflation. Let us never forget that maintaining the gold standard which effectively had to hinder fighting – even prevent – the Great Depression. Let us also remember that it is the countries which were not members – or which quickly exited it at the time – which first reestablished themselves or pulled themselves out of it with limited damage. It is more or less understood that speculation and the financial world were launched with heads lowered, since the beginning of the 1990s, into the delightful game of playing Greek, Italian or Portuguese interest rates against German rates. Thus, giddy profits were recorded by investing in peripheral nations or the Southern countries which were not supposed to go bankrupt thanks to the umbrella of the Euro. As such, the financial system neglected a fundamental point, i.e. in the absence of a currency that may be devaluated if necessary, this devaluation thus takes another form: default payment... Therefore, the actual European disappointments – which are not the result of fiscal indiscipline – are amplified by this single currency which is not used as a lever to lessen the pain of economic and social recovery for Europeans.

## Currency War or Attempts at Reflation?

Lenin asserted almost a century ago that “the surest way to destroy a nation was to circumvent its currency”. The Weekly Standard of February 9, 2013 published an article about him where Irwin Seltzer harangued that “Lenin would welcome the [current] currency war”, in that it would (according to him) help destroy capitalism... Would we have spent a century for nothing? Have we therefore not learned anything in a hundred years? Because it is vital to overcome the stifling orthodoxy of today, as of this unique mind-numbing thought, which never tires from teaching us that the policy of quantitative rate cuts undertaken by some central banks lead straight to universal monetary conflict. In addition, without being able to explain to us this alleged relation of cause and effect between the expansionist policy of a central bank and the weakening of its national currency. But it is true that those who use this warlike terminology still do not understand the process of money creation put at the service of an economy that they stubbornly refer to as “manipulation” or “hazardous experimentation” undertaken by the central bank. Whereas it should instead be leaning toward the dynamism and innovative spirit of some central banks whose efforts are entirely oriented towards restoring economic activity and reducing unemployment. For example, how not to endorse wholeheartedly the second wave of quantitative rate cuts (QE2) of \$600 billion set up in November 2010 by the U.S. Federal Reserve? Let us remember this very troubled period of a stagnant U.S. economy despite excessively low short-term interest rates accompanied by an intense fragility in the European banking system. Did the Fed not wisely then turned on its printing press to compress its long-term rates, critical to any recovery, while providing valuable support to European banks? It was, however, largely taxed at the time of seeking to weaken its currency (by printing generously) through leveraging monetary creation, that thus would allow a recovery by exports. For the advocates of neo-liberalism (and a shrinking state), the Federal Reserve openly plotted with the clear intention to devalue the dollar and unfairly boost its economy. Does the drop in the green back negatively affect the unemployment rate in Brazil or the backlog of orders of Chinese companies, as the leaders of these countries continue to claim? All this makes it possible to relativize considerably the fluctuations in interest rates, the success of issuing bonds, the identity of those which

hold the Treasury bills and even the threats of insolvency. Is the strengthening of the currency of these countries not simply the result of their accession to the status of industrial and commercial power? So why all this anxiety and fuss around these issues of public deficits that are really not so? Why not consider the effect of currency appreciation at the same time as the cause and the consequence of the enrichment of a nation? Probably because economists and leaders confuse their pockets with that of the state! All mechanisms ignored by almost all analysts – as leaders – opting instead for a vocabulary and a cataclysmic description while monetary creation reduces unemployment in the “integrated” savings while accelerating industrialization of the emerging countries. In fact, a country’s debt differs altogether from private debt. In this regard, there is debt and debt and it would be completely counter-productive not to distinguish them since, by doing so, we contribute actively to penalizing the state, therefore ourselves. Do the United States and Japan have warlike intentions when they try to reverse their unemployment and fight deflation through monetary creation? First, let’s note that when it generates deficit, that is to say, when it creates money, the state issues simultaneously an asset in favor of the private sector but without the latter having to offset this debt by a bond or constraint of any kind. Since, far from being the sought after goal, the depreciation of their respective currencies is only the collateral effect of their expansionist policy. Thus, public debt represents a net gain for the private sector and therefore for the economy. Contrary to the Chinese position which used and abused monetary manipulation, the policies put in place in the U.S. and Japan can effectively provoke a devaluation of their currency but not similar in any way to manipulation, much less so to any “war”. And this, contrary to the private sector which, not having the ability to print money, and not being capable of crediting accounts at will, cannot be indebted beyond a certain threshold. Unlike war, which is obviously a negative sum game (I destroy you, you destroy me), an expansionist monetary policy is a “win-win” process, most often followed by benefits for the country which puts it into place, and by extension to its trading partners. The private sector can thus easily switch to a Ponzi scheme. Must the British decision to leave the gold standard in 1931, gradually followed by the United States and France, not precede the restoration of their growth? This term is, on the other hand, not found in the vocabulary of a state which has its own sovereign currency, and therefore which is not obliged to borrow. Is it not by abandoning gold and its corollary, namely the expansion of the monetary base, which finally turned the page of the Great Depression? As a result, the obligation of governments – and which markets impose on them – to balance their budgets and public accounts can be revisited under another perspective. And those looking to rewrite history must review their copy because it is

not the German hyper inflation of the early 1920s which ascended Hitler to power, but the deflationary Brüning policy a decade later. It becomes obsolete. Within this same Germany which today dictates austerity and contraction throughout Europe, as if – it neither – retained the teachings of the past... After all, the first use of currency is not so much to buy other currencies than, especially, to use it in the exchange of goods and products! Indeed, as we have seen before, however little a country has an independent monetary scheme, the mass of its debts and the limits of its deficits as the pace of issuing its bonds fall within its own decision, because no one would in theory be able to impose them on it. That is why the loss in value of any given currency encourages the consumer to acquire more durables, and the company to invest in its equipment and production. Contrary to the gold standard regime and the indexation of a national currency to another referenced currency, the floating exchange rate system therefore gives a nation latitude and freedom to act potentially fully and completely. Isn't the depreciation of a currency reflected in the value of these goods and products which become mechanically more expensive? Is this not peculiar to a sovereign nation? The increase in prices and tariff – and in other words: inflation! An extremely tough and generally widespread urban legend demands, however, that the state be “respectable and responsible” by balancing its budget – or at the very least that it gets close to balancing it – with the objective of not exhausting its national resources and not “spiraling” out of control. Does it not motivate companies to produce more goods for sale at the best price, and consumers to buy today in anticipation of a further increase in these prices? That is why the expansionist policy of the industrialized countries in integrated economies can have a widespread ripple effect on all their exports. He sees this as an exemplary value for the whole of society which should not let its expenses spiral out of control. Some nations are certainly not in a position to improve substantially their foreign trade. According to him, the state should be present to lead citizens to the way to discipline to get them back on track... If this is the case, it is necessary to note that today we are witnessing a radical shift in paradigm since it is the turn of modern and evolved but extremely deficit States who need to get back on track! The fact remains that the overall level of world exports will improve vastly since Japan will sell more cars, the U.S. more aircraft, the European Union more machines... In short, the creation of money and the consecutive loss in value of certain major currencies will lead to falling unemployment and higher incomes. That does not matter: that this logic of reversal of values is pushed further and therefore we use to dismantle the myth of the frugal state. In what amounts to a much more globalized economic recovery than a war. In fact, the state – with a monopoly on printing money – is able to credit accounts, including those of its creditors. Competitive devaluations are



not a zero-sum game which allows the country that practices them to boost its exports at the expense of those who have decided (for reasons of aberrant principle) not to enter into the arena of this monetary multiplication. As such, it does not have to leave it to the markets to determine its financial costs, and even less its public policies. Instead, they are a great tool for economic resurrection, especially if the country in question falls within its objectives in terms of inflation, due to imported goods necessarily made more expensive by the loss in value of its national currency. Ceding to market pressure by having to publicly borrow thanks to the bond instrument is therefore strictly voluntary for a state. You can actually only remain appreciative of the explicit target of 2% inflation set by the Japanese government, which will be launched through multiple acquisitions of securities and other assets to provide the means to achieve doubling its monetary base over the same period! This state believes in playing the game. Quantitative rate cuts are therefore amplified and expanded. In reality, it only plays the game of investors whose sole preoccupation is to grow their savings. Emphasis will be placed at the same time on the quantity and quality of these interventions which will take place at an annual rate of 60-70 trillion yen, i.e. about \$600 to \$700 billion, which represents the accumulated “QE1” and “QE2” programs in the United States. That is why a country such as Spain, which abdicated its monetary policy (to the EDB), has today been reduced to borrowing from the markets at astoundingly high interest rates to finance itself. Like the U.S. Federal Reserve in its “QE2” program, the Bank of Japan will purchase long-term Treasury bonds, but it will buy also shares on the stock market and real estate properties. The Greek or Spanish cataclysmic experience further demonstrates the cruelty of markets and rating agencies which have completely taken control. The stated and ultimate purpose is to instill valuable reflation, only able to fight and defeat the rampant depression that has plagued this country for many years. Public deficits will continue to persist so long as the growth rate remains lower than the rate of return on the State’s bonds. Make no mistake: this new Japanese “experience” is certainly the most important business – and worthwhile – from a central bank, which, since the days of Paul Volcker in the U.S. and the large means put in place to fight against inflation in the late 1970s and early 1980s! In this regard, it is necessary to understand that the European Union is not really confronted with a debt crisis, but with a problem of sluggish growth, the effects of which naturally spill over into its public deficits. If the Bank of Japan manages to revive subdued inflationary pressures, it will manage to lessen the debt burden of the country while presiding over a return to job-creating growth. Weren’t the rates of refinancing Spain’s debt consistently between 5.4 and 5.9% between

January 2000 through May 2002 without anyone worrying about it or predicting cataclysm?

To this end, the recent example of Japan – which is to create money and promote inflation – is clearly to be followed and replicated within the so indecisive European Union. Robust growth would in fact allow the State to offset this charge while providing opportunities and confidence to financial players. Far from being a zero-sum game, competitive devaluation supported by an inflationary ambition is there an irreplaceable lever in reviving an anemic, even deflationary, economic activity. This is precisely why it is now vital to focus exclusively on the growth rate of our economies, while relegating this obsession with deficit reduction to the background having the perverse effect of stopping the activity. Besides, the Nikkei is not the only stock exchange to have applauded the tough decisions of the new Japanese government, since all global financial markets have understood the benefits of such a monetary creation on global recovery. Finally, as it is strange to note today that they are the same ones who did not see the financial crisis coming who persist on the path of austerity, orthodoxy and who set themselves up as great defenders of the public purse and large deficit slayers. At a time when the “core” European countries begin to falter: France with 1997 industrial production levels and its German counterpart to 2007 levels and retail sales at an unprecedented decline of 4.7% for the same country. Now when Indeed, they were the same one who yesterday indulged in – and with – the financial markets fully delivered to themselves, and who often drew juicy profits, which have now – against all expectations – become fanatical, even fetish, about limiting public spending. The European Central Bank should be proactive and deign, in turn, to get its “hands dirty” from its printing press, instead of, like the European leaders, continuing to whine and stigmatize the Japanese initiative. While it and many nations within the heart of Europe are obsessed with the financing costs of their sovereign debt, they seem still unable to grasp that a country issuing its own floating currency does not have to undergo the retaliatory measures of financial markets. In this regard, the case of Japan which is financed by abysmally low rates despite tremendous public debt is once again illuminating. It suffices that the last-resort lender, i.e. the central bank, transfers cash into the Treasury’s account knowing that the other side of the coin is inflation. A sovereign nation with a sovereign currency can therefore be fiscally irresponsible without the soaring cost of financing its public debt encumbering its growth. But have the ECB, Germany and the other exemplary nations of the EU only understood that the cost of financing their public debt close to zero – or zero – is precisely the best reflection of stagnant economies, even on the edge of the precipice? As higher financing costs of the public debt can also be a signal for a state to redi-

rect its liquidity in favor of future investments and at high added value, and to interrupt its “Keynesian” expenses in view of the recovery ahead. Therefore, that Germany (or Switzerland) derive no pride in their negative rates because it really is not the ability to obtain financing at low prices that will advance their economic recovery. Therefore it is only when the economy is working at full capacity that extra public spending – but also businesses and households – induces inflation. In the same vein, the austerity policies and contraction necessarily and inevitably lead to... more economic contraction. Under this assumption of full capacity, inflation can be further avoided by a gradual reduction in public spending which would, at any rate, be counterbalanced by increased investment by the private sector within a framework of a booming economy. Because only an activist policy mixing monetary creation and pressure on their currencies will enable European citizens to see the light at the end of the tunnel. The acceleration in public spending is therefore not likely to generate inflationary pressures by causing a run on consumption and aggregate demand in the context of an activity that is slowing down, no more so than it would threaten (as was seen above) the solvency of the sovereign state in question. It is then that the cost of financing the European sovereign debt will increase: a clear signal of the great return to economic growth. Let’s therefore stop pretending that the creation of money and the monetization of debt lead to insolvency and inflation. When will Europeans finally understand that there is nothing to fear than fear itself? Rather let’s try to qualify and put into perspective by understanding that a given economic context is able to “cash in” extremely liquidity injections and support a widening of its deficits while being able to bounce back.

## **Public Debt: Reflection of a Sovereign Nation**

Therefore, we do not understand – or at any rate very little – what public debt really is. A sovereign nation as described above does not have any obligation to create bonds and other Treasury bills to finance itself. Do countries which ask markets and investors for money, at sometimes prohibitive interest rates, know or are they aware that such a transaction is entirely voluntary? Indeed, it is a strategy – questionable or definable according to the circumstances – which means that the state in question decree that credit accounts deposited into its central bank would turn into revenue by converting them into bonds and other instruments of credit. Therefore, deliberate choice, on the part of a country which grants investors, private funds or other countries outright a say in its monetary policy and public spending. Entering the arena of financial markets for a country seeking funding amounts in effect to accepting – even promoting – a transfer of wealth, but also of power to and in favor of its creditors. This is why a state should identify those who purchase its Treasury bills, when it should simply not be selected prior to their issuance. This is an essential issue, even existential, for an independent country eager to maintain its sovereignty. The contemporary example that immediately comes to mind is the dependence of the United States *vis-à-vis* their first bondholder, namely China. After all, and this has already been seen since the European crisis with Western and modern countries, markets are very capable of paralyzing an economy, not when a country fails to meet its commitments, but simply whether markets are no longer convinced of its financial virtue. Issuing bonds is therefore a voluntary process on the part of a state which could just as easily have the same liquidities by requesting its central bank to credit its account and those of its service providers. Money has no smell or color, economic actors are very indifferent toward whether their stimuli, tax cuts, income and social benefits come from international investors or printing money. All this makes it possible to relativize considerably the fluctuations in interest rates, the success of issuing bonds, the identity of those which hold the Treasury bills and even the threats of insolvency.

So why all this anxiety and fuss around these issues of public deficits that are really not so? Probably because economists and leaders confuse

their pockets with that of the state! In fact, a country's debt differs altogether from private debt. In this regard, there is debt and debt and it would be completely counter-productive not to distinguish them since, by doing so, we contribute actively to penalizing the state, therefore ourselves. In fact, a country's debt differs altogether from private debt. In this regard, there is debt and debt and it would be completely counter-productive not to distinguish them since, by doing so, we contribute actively to penalizing the state, therefore ourselves. First, let's note that when it generates deficit, that is to say, when it creates money, the state issues simultaneously an asset in favor of the private sector but without the latter having to offset this debt by a bond or constraint of any kind. Thus, public debt represents a net gain for the private sector and therefore for the economy. And this, contrary to the private sector which, not having the ability to print money, and not being capable of crediting accounts at will, cannot be indebted beyond a certain threshold. The private sector can thus easily switch to a Ponzi scheme. This term is, on the other hand, not found in the vocabulary of a state which has its own sovereign currency, and therefore which is not obliged to borrow. As a result, the obligation of governments – and which markets impose on them – to balance their budgets and public accounts can be revisited under another perspective. It becomes obsolete. Indeed, as we have seen before, however little a country has an independent monetary scheme, the mass of its debts and the limits of its deficits as the pace of issuing its bonds fall within its own decision, because no one would in theory be able to impose them on it. Contrary to the gold standard regime and the indexation of a national currency to another referenced currency, the floating exchange rate system therefore gives a nation latitude and freedom to act potentially fully and completely. Is this not peculiar to a sovereign nation? An extremely tough and generally widespread urban legend demands, however, that the state be “respectable and responsible” by balancing its budget – or at the very least that it gets close to balancing it – with the objective of not exhausting its national resources and not “spiraling” out of control. Paul Samuelson, born in 1915 and recipient of the Nobel Economics Prize in 1970, goes even further by calling this rule “superstitious” – foolish but globally a dogma – to maintain national budgets close to balanced accounts. He sees this as an exemplary value for the whole of society which should not let its expenses spiral out of control. According to him, the state should be present to lead citizens to the way to discipline to get them back on track... If this is the case, it is necessary to note that today we are witnessing a radical shift in paradigm since it is the turn of modern and evolved but extremely deficit States who need to get back on track! That does not matter: that this logic of reversal of values is pushed further and therefore we use to dismantle the myth of the frugal state. In fact,

the state – with a monopoly on printing money – is able to credit accounts, including those of its creditors. As such, it does not have to leave it to the markets to determine its financial costs, and even less its public policies. Ceding to market pressure by having to publicly borrow thanks to the bond instrument is therefore strictly voluntary for a state. This state believes in playing the game. In reality, it only plays the game of investors whose sole preoccupation is to grow their savings. That is why a country such as Spain, which abdicated its monetary policy (to the EDB), has today been reduced to borrowing from the markets at astoundingly high interest rates to finance itself. The Greek or Spanish cataclysmic experience further demonstrates the cruelty of markets and rating agencies which have completely taken control. Public deficits will continue to persist so long as the growth rate remains lower than the rate of return on the State's bonds. In this regard, it is necessary to understand that the European Union is not really confronted with a debt crisis, but with a problem of sluggish growth, the effects of which naturally spill over into its public deficits. Weren't the rates of refinancing Spain's debt consistently between 5.4 and 5.9% between January 2000 through May 2002 without anyone worrying about it or predicting cataclysm? Robust growth would in fact allow the State to offset this charge while providing opportunities and confidence to financial players. This is precisely why it is now vital to focus exclusively on the growth rate of our economies, while relegating this obsession with deficit reduction to the background having the perverse effect of stopping the activity. Finally, as it is strange to note today that they are the same ones who did not see the financial crisis coming who persist on the path of austerity, orthodoxy and who set themselves up as great defenders of the public purse and large deficit slayers. Indeed, they were the same one who yesterday indulged in – and with – the financial markets fully delivered to themselves, and who often drew juicy profits, which have now – against all expectations – become fanatical, even fetish, about limiting public spending.

It suffices that the last-resort lender, i.e. the central bank, transfers cash into the Treasury's account knowing that the other side of the coin is inflation. But is inflation really dangerous or, rather, when does inflation become dangerous? Almost all economists fear in fact – and with legitimate reasons – that that excessive money creation results in a surge in inflationary pressures. However, a State's stimuli in favor of its economic actors, the reduction income tax and other increases in public spending never risk incurring inflation if the economy performs well below its abilities and as long as the government exercises price control. Therefore it is only when the economy is working at full capacity that extra public spending – but also businesses and households – induces inflation. Under this assumption of full capacity, inflation can be further

avoided by a gradual reduction in public spending which would, at any rate, be counterbalanced by increased investment by the private sector within a framework of a booming economy. The acceleration in public spending is therefore not likely to generate inflationary pressures by causing a run on consumption and aggregate demand in the context of an activity that is slowing down, no more so than it would threaten (as was seen above) the solvency of the sovereign state in question. Let's therefore stop pretending that the creation of money and the monetization of debt lead to insolvency and inflation. Rather let's try to qualify and put into perspective by understanding that a given economic context is able to "cash in" extremely liquidity injections and support a widening of its deficits while being able to bounce back. And let's moderate our obsession with the ratios of our debts *vis-à-vis* our GDP which are only very reliable and worthy of interest in a system of fixed exchange rates or indexed to a metal. Indeed, these ratios and measures are from providing irremovable benchmarks within our globalized economies. Informed governments, advised by informed experts, would be better to analyze dynamically since there is no level of debts or deficits which would automatically or mechanically set off crises and which would reduce growth. The budget of a modern state with the so-called "integrated" economy is the result of inherently endogenous variables. It is narrowly related to the performance of the private sector, since it becomes deficit in nature when households decide not to spend and businesses increase their imports. If there are indeed limits to which a country can spend, they must not in any case be defined in terms of solvency. These limitations are rather functions of resources that the state intends to mobilize since deficits would be logically much more massive than the state commits to exploiting the abilities of its economy and putting its citizens to work.

Deficits and economic activity on the one hand, jobs and savings on the other hand, are the two facets of the same puzzle. Thus persistent unemployment (as it has been for decades in our Western countries) means that our deficits are too low and that the state should increase its spending or lower taxes! Stimuli would gradually be withdrawn in case of sustainable regression of unemployment or if the economy was no longer able to absorb investments, which would therefore lead to inflation. In other words, the only limit on public spending is not the lack of funding or the overflow of debts which would be too massive *vis-à-vis* GDP. The only obstacle to public spending is inflation. But therefore: Would Germany be correct in opposing all its forces to more stimuli to help peripheral Europe? The big problem with its approach is that it lacks total inventiveness, flexibility and that the Germans are barricaded behind a full theoretical and academic argument. The ridiculously low returns on the German Treasury bills indeed indicate that this country

inspires total confidence and therefore benefits from a massive influx of liquidities which compresses its rates. But they also mean that the least inflationary threat is to be totally excluded. Germany should therefore never fear the 1923 hyperinflationary nightmare of Weimar (against which our central banks today have the tools to defend themselves) but rather the cataclysmic scenario of 1932 when the U.S. unemployment rates was over 30% of the U.S. population... Germany's absolute priority – as the economic engine and Europe's poster child – and good governance by the ECB should therefore lead to rebalancing the capital flows in the Union for better distribution. The misfortunes of Greece, Spain and the other fragile countries come from a scarcity in cash at their disposal while Germany, for its part, abounds in it, as reflected through the insignificant, or even negative, return on its treasury bills. It should therefore reduce its surplus, stimulate its consumption, and encourage a minimum level of inflationary pressure so as to induce an inverse movement with peripheral European countries. German deficits – or at least the reduction in surplus – would mechanically translate within the same monetary Union into a significant reabsorbance of the deficits of needy countries.

Let's therefore once and for all get rid of these prejudices which surround us – even stifle us – and which raises a precondition to economic recovery to reduce deficits. The reality is totally different since the public purse can resuscitate – or at least invigorate – the private sector by boosting its revenues and savings. In time of crises, on the state is able – and has the duty – to protect the weakest and most needy and to make society prosper by guaranteeing it its social assistance and by making employment for all a priority. So long as there is unemployment, so long as our economy is not modernized, so long as our plants do not operate at full capacity, so long as our businesses cannot compete and citizens do not produce, a sovereign state can and must continue to stimulate the economy and create money. Letting deficits slip thus remains the only means of recovery for the private sector during a recession while helping to restore savings. Thus it is only thanks to the massive stimulus packages injected successively by the Bush and Obama administrations (respectively) that the U.S. economy did not plunge into depression despite a totally infected financial system and a crisis almost as severe as the Great Depression. It is also the massive program implemented by China in 2009 which maintained its growth rate despite the collapse of global economic activity which severely undermined its exports. Austerity and budgetary economies devastated European growth and plunged it into recession since the third quarter of 2011. For those who vilify money creation by invoking the aspect of “artificial” recovery it creates, my response is that if there is recovery, a reduction in unemployment and recovery of purchase power, the objec-



tive has been achieved. If printing money reestablishes confidence – and it does! –, I can hardly ask for more. There is therefore proof that, as long as the state is sovereign and it prints a floating currency, it is possible to build growth – and therefore ensure the comfort of citizens – with credit, when turbulent and instable periods depress the private sector. It is up to the state to support these stimuli by implementing essential measures and regulations aimed at stabilizing the private sector and forcing it to settle its debts. There is therefore proof that, as long as the state is sovereign and it prints a floating currency, it is possible to build growth – and therefore ensure the comfort of citizens – with credit, when turbulent and instable periods depress the private sector. It is up to the state to support these stimuli by implementing essential measures and regulations aimed at stabilizing the private sector and forcing it to settle its debts. It is up to the state to regulate activity to avoid speculative bubbles and excesses. However, its single and only limitation in terms of deficits is able to absorb its own economy, for injected money must only be considered as a tool to reestablish purchasing power and investment. Continuing to shrink deficits during times of crisis is tantamount to accepting high unemployment and a notorious decrease in the standard of living of all citizens, including those who kept their jobs. Let's not sacralize money which is only a vehicle to move our economy forward more leniently and for our ship to arrive safely. It is not actually the means of transport which count, but the passengers. In the same vein, let us trivialize the action of raising or lowering interest rates, which is nothing sacred or difficult to understand or comprehend. Indeed, the central bank simply buys bonds in the markets (with the money it has already created) when it decides to lower its rates. It performs the reverse operation since it must go back, that is to say, it sells Treasury bills and removes the money received in return... In other words, as money is not a value, let's use it sparingly and scrupulously since it allows us to achieve our objective.

## **Central Banks, the Ultimate Safeguards against Depression**

*A cash crisis is the worst scenario for the banking system. Without the “last-resort lender”, without the ultimate support of a central bank that is able to guarantee savers’ deposits, this is the flight of capital from this weakened bank and from the entire system which restricts financial establishments from selling their assets to pay panicked depositors. An insidious spiral of falling asset prices occurs when banks come under pressure and attempt to recover cash to honor their commitments. This downward spiral is likely to reach the critical stage when banks need more than what is still carried as an asset on their balance sheet, and so a cash crisis turns into a solvency crisis. It is also at this point that depositors realize that their intuition and fear were after all justified... Such a rush would not, however, take place if a credible central bank guaranteed bank deposits and if these investors were confident of recovering their assets. Hence the crucial role – at least psychologically – of the central bank, guardian angel or last line of defense which assumes this vital role of purveyor of cash to the banking network. Did it not raise its interest rates in July 2008 during the subprime turmoil, i.e. a few weeks after Bear Stearns declared bankruptcy and a few weeks before Lehman’s own demise? Its mere presence in the background is to simply reassure and prevents banks from failing in a domino effect. This is a similar process that reaches the bond debt of a member country of a monetary union in case of a grave crisis. Fears about the solvency of a country (such as Greece) leads investors (markets, as they are generically referred to) to divest themselves of their Treasury bills of some other member nations of the union for fear of a cash crisis that would spread. Unless a solid central bank, worthy of this name intervenes to reassure investors who, after all, are only human beings! Without the determined presence – and determining – of a lender of the last resort, the cash crisis naturally degenerates into a solvency crisis, and the country in the spotlight then has to pay always more (interest) to persuade these investors to continue lending it. If the central bank is not on the radar, this country does not have any other cash source than that provided by the markets, which will make it pay dearly to fight without the benefit of support from a central bank. These hyperbolic financing costs contami-*

nate the rest and soon enough, the other member nations of this union which assist will be powerless to withdraw cash from their Treasury bills and should in turn raise the stakes (interest rates) to continue to glean cash.

This escalate in financing costs obviously exerts perverse effects on the budget of the country and, in this regard, no country – not even Germany – is able to keep up with interest rates growing steadily on financing its public debt. Each country faces its breaking point at some stage – the one where servicing its debt leads it directly to insolvency. Except if a central bank – whose only presence has the effect of a scarecrow – lowers tension by several notches. Tension which, in reality, would not even have been raised to such extreme levels if this central bank had clearly shown its intention to support this country's bond market. The European Central Bank would have been able to save Greece, Ireland, Spain and the European banking system from so much misery if it had only shown strong support and a willingness to provide these failing players with a cash injection. Because we must realize that this severe European crisis is only a game of cat and mouse that has turned out badly for a Europe that now threatens to sink from the mere fact of the absence of a lender of last resort. Investors seeking all naturally to preserve their assets in the bond debts of these member nations, the only vigorous affirmation on the part of the ECB showing its determination to flood these weakened countries with liquidity would have avoided such an escalation in the costs of debt financing and also banished the specter of the chain reaction bank failures. The slow pace of the ECB and the inertia of European leaders – unless it was their total ignorance of financial mechanisms? – were thus balanced by a devastating escalate in the debt charge of a number of European countries. Finally an indisputable surcharge for the ECB itself which, after much procrastination, is still committed to assisting the European banking system. “Lost battles are summed up in two words”, asserted General MacArthur, “... too late”. Indeed, the commitments of the important banks being clearly more massive than those of the states, it would have been less costly (for everyone) that the ECB support early states – crowned with popular legitimacy – than belatedly banks in private hands. Besides the symbolic, yet essential relief paid timely by the ECB to a European state. Does it not make sense that such assistance would otherwise be less onerous since the average public European debt *vis-à-vis* the GDP average of the Union is 80% when the debt of European banks is nearly 25% of GDP of the European Union? And the arguments according to which such bond purchases by the ECB would exacerbate inflation do not hold since, as Milton Friedman himself says however little suspected of collusion with Keynesian practices (as seen later), an argument of monetary mass does not systematically lead to inflation. On

the contrary, as Anna Schwartz and himself, in their monumental work titled “A Monetary History of the U.S.”, attribute the intensity of the Great Depression to the U.S. Federal Reserve at the time, having utterly failed to fulfill its duty as lender of last resort. Moreover, isn’t it Friedman in person to whom we owe the famous quip that encourages the monetary authorities of a country in deflation to drop bundles of banknotes, if necessary “by helicopter”? The guarantee and certainty of support by a central bank are certainly likely to encourage risk attitudes, even all kinds of abuses, among banks, financial players and even country leaders. Under its budgetary management, a government may indeed be tempted to go the route of public spending for purely demagogic reasons if it knows it is covered by cash from its central bank... However, a central bank that would not intervene on behalf of a state for fear of encouraging this “moral hazard” would be committing an unpardonable error. Moreover, why would you feel obliged to come to the assistance of private financial establishments – except to push them into the arms of risky behavior – and hesitate to support a state, and therefore populations? The obligation of a central bank is therefore to inject liquidity, whenever necessary, into both banks and countries, knowing that rules may be enacted in return for assisting states, as conditions are imposed on financial establishments drawing on public funds. Indeed, it is much healthier to make a clear separation between the intervention of a central bank (which responds to urgent needs of liquidity) and regulations for needy states and banks in peril. Thus there must be an organization designed specifically for this purpose upon which the monitoring the financial governance of European States (and their banks) should rest whereas the appeal for liquidity must be the only and singular preoccupation of their central bank, which must not in any way be incumbent upon moral considerations. Why would an approach similar to the one in effect for banks (which benefit from ECB support and which are accountable to a regulatory body) not be implemented for states? So it is the ECB which would assume its responsibilities of lender of last resort and great stabilizer of bond markets while a Pan European organization would be in charge of monitoring and regulating the issue of bonds of each member country.

Moreover, a number of orthodox experts assert that, if a state is forced to seek assistance when it is faced with a liquidity crisis, the central bank must abstain when the crisis becomes a solvency problem. The reasoning is the same for banks. However, how do you make a clear and unequivocal distinction between a liquidity crisis and that of solvency? If today – and rare are those who question it – Greece is *de facto* insolvent, are Spain and Ireland also insolvent or can their woes be simply attributed to liquidity problems? How would markets (basic, primitive, impulsive, short-term) be able to assess the financial situation

of a state – and therefore to lend at a more or less high rate – when our best economists are incapable of clearly diagnosing the creditworthiness of an European state against undeniable transparency yet replete with abundant economic statistics? In reality, a sovereign debt crisis affecting one or several member states of a monetary union is characterized by an inextricable mix of problems implying both their solvency and their immense difficulties in sourcing cash. While the cash crisis is translated into escalating financing costs for a State to conclude logically that a crisis is affecting its solvency, this State exacerbates its liquidity worries with a key intensification of threats on its insolvency. In practice, it is extremely complicated to distinguish whether a nation's problems are linked to its solvency or its liquidity. A central bank must therefore be generous and not skimp on infusing cash with a view to restoring its liquidity to quash any inclination to see it as insolvent.

A central bank cannot thus afford to indulge in its cozy isolation, since it must constantly “do its job”, i.e. confront the ever changing or steadily deteriorating realities on the ground. And contrary to what Friedman claimed (which will be analyzed later), a central bank's monetary policy should not be disconnected from the budgetary and fiscal realities of the countries or regions which are its responsibility. Although decisive, the definition of interest rates must not be the only reason why central banks exist, which, despite wanting to pass for elders and characters beyond the reach of political power, end up performing their measurement work of the business cycle mechanically. This shock, brutal but predictable, is forced to question the supposed independence or neutrality of central banks which is perceived – and rightly so – as goodwill *vis-à-vis* the financial markets. If at least one piece of evidence is revealed in favor of this crisis, it is that the central banker can no longer adorn itself with its well accommodating garb of independence *vis-à-vis* political power, since its acts are fundamentally and intrinsically clad with political connotations, and even its refusal to take action! That it prevents a financial institution going bankrupt or that, on the other hand, it does not lift its little finger to prevent another from collapsing. That it issues its caution in favor of commitments undertaken by such a sector of economic activity. That it fights hard against any inflationary pressure or, on the contrary, tolerates a certain degree of it, favoring or penalizing either the holders of Treasury bills or the debtors. A central banker, whose every decision is highly political – who is up to his neck in the ring –, cannot continue to pride himself on this independence which is only a myth. Moreover, as it is no longer plausible to leave such power in the hands of individuals not elected by the people, one of the major battles which to be delivered out of this crisis will lie in redefining the job of the central banker, his powers his duty of accountability and the possibility of removing him, if and when applicable. The

framework in effect since the 1990s until 2007 of low inflation and almost uninterrupted growth should not actually be misleading. If central bankers ascribe merit to it, they must in turn be responsible for the creation of multiple speculative bubbles, who poorly understood the risks of a sprawling financial sector and who completely missed out on monitoring and regulating gargantuan inequalities in cross-border and continental capital flows.

They seem as paralyzed by ideological prejudices according to which financial markets always end up regaining their stability and according to which international movements of capital generate an optimal distribution of wealth. Indeed, the overwhelming majority of our central bankers belong to the generation of economists blinded by the teachings of Milton Friedman, who espoused that the Great Depression and the speculative boom of the 1920s which preceded it had no correlation. Our monetary managers have indeed only contempt for economic unorthodox economic theories as difficult to equate. In this troubled and constant imbalanced world, the job of the central banker requires, however, continuous finesse and anticipation. That's why; the lack of a true central bank worthy of this name, the actual European architecture irrevocably transforms solvent countries into insolvent countries. It is important to realize that its absolutist quest for a hardline orthodoxy led the ECB – and, as such, European economies – straight into the wall. Did it not raise its interest rates in July 2008 during the subprime turmoil, i.e. a few weeks after Bear Stearns declared bankruptcy and a few weeks before Lehman's own demise? Did it not raise its rates twice – so unlikely – during the European tempest, in 2011? That is also why – to borrow from Martin Wolf – the ECB will be remembered as the “magnificently orthodox central bank of a failed currency union”.

When will we finally understand that the current European woes are in no way due to public debts? Why do orthodoxy, mainstream thinking, the overwhelming majority of economists and political leaders (who do not understand much), persist in considering this crisis as that of European “sovereign debts”? A little history is illuminating in this regard. And that it is regrettable for all of us that they do not look back to 1931 – tragic for all – from which to draw parallels and precious information for today... From the bankruptcy of the very large Austrian bank, *Österreichische Kredit Anstalt*, over-exposed in East and Central Europe. On the History of France in this case because it is a French law in the early 1970s that would focus this financial orthodoxy – and write in stone the sacrosanct independence of the central bank – responsible for the current devastation of European Union! To the general financial instability of Europe under threat from currency implosion due to unpaid German reparations. On January 3, 1973 the new status of the

Banque de France were indeed adopted that would revolutionize the job of a central banker, turning it into a sort of “teflon” character – totally non-stick – not having to be accountable to the executive of the country or its citizens. To the U.S. intervention in the sense of debt restructuring for a Germany that was tied to a gold standard, yet one of the main reasons for the Great Depression. It’s actually to 1973 and to French law that we can trace the beginning of the irresponsibility of the central banks, particularly in its Article 25 which states that “the Treasury cannot be the nominator of its own effects at the discount of the Bank of France”. Only countries which abandon the first gold standards (Great Britain followed by the Scandinavian countries) are the first to pull themselves out of this terrible crisis without incurring too much damage. Therefore turning crucial in the management of public finances of Western nations which followed in the footsteps of France. The unexpected rise in U.S. interest rates in 1928 was certainly the first sign of this crisis. States being henceforth – and de facto – permanently at the mercy of the banking system, since their Treasury no longer had the right to borrow from its central bank. As well, the deflationary global calamity, linked to a global economic contraction, is rooted in the gold standard, particularly due to the attitude... of France, presented by a number of experts as mainly responsible for the intensification of the Great Depression! Historic step on the path to international financial liberalization, crossed and initiated by France, which now prohibited recourse to the printing of money of its central bank if needed. It is actually the substantial increase in France’s gold reserves (from 7 to 27% between 1927 and 1932!), which, in creating scarcity for this metal, would undoubtedly contribute to an enormous deflationary spiral for all developed nations at that time. A burning topical issue in the European context today! With deflation as the distinctive sign of the Great Depression, it could have been avoided if the central banks at that time (and the French one in the first place) had maintained their 1928 gold bearing ratios... Indeed, it is this frenetic accumulation of the yellow metal by eminent central banks which fueled global deflationary pressure. Moreover, the adoption of this law left nothing to chance at a time when France was headed by a former banker, namely Georges Pompidou. However, maintaining gold reserves at their levels prior to the Great Depression would not have altered the historical correlation between consumer and production pricing and the quantities of gold held by central banks. The dollar was no longer convertible into gold which was part of the decision of U.S. President Nixon in 1971 to suspend all purchases and sales of gold. It was Léon Blum, Prime Minister, who finally took France out of the gold standard in 1936, but the damage was done. And in an atmosphere of international financial stress where the U.S. hoped to prosper, illustrated by the famous repar-

tee of the Treasury Secretary John Connally at the time: “The dollar is our currency but your problem”! Isn’t the parallel obvious in today’s Europe where austerity is the new gold standard? In short, the collapse of the Bretton Woods system established in 1944 (under the influence of Keynes) ushered in a new era where the risks were expected to be borne by investors, now facing the vagaries of currency fluctuations. What a pity that policies are not a little like historians since the conjuncture of the 1930s strangely resemble our situation today, except that at that time it was only Germany which was in the same situation as peripheral Europe finds itself today. The abandonment of this convertibility also had a fundamental impact on the financial actors who obviously did not fail to seize the opportunities offered by speculation on the volatility of emerging market currencies. Entirely dependent on foreign capital, it had been steam rolled by unrealistic reparations stipulated in the Treaty of Versailles within a general framework of grossly under-capitalized national banks. Deregulation and liberalization of the financial sector was therefore the essential prerequisite that would allow its players to take advantage of these new market fluctuations. Indeed, this is the whole problem relative to the reparations imposed on Germany, and their disastrous consequences, which have today been removed from the debate to make room for deficit obsession. It is in this environment from which emerged the concept of central banks independence whose objective was to sterilize monetary policy. The ardent defenders of austerity actually impose an absolute diktat on the media, opinions, public policy and academia by imbuing a climate of disaster where only hyperinflationary trauma seems worthy of interest. And to avoid any interference from politicians too often inclined to use it for economic recovery, at the risk of fueling inflation. It is as if the disaster from the reparations imposed on Germany had been waned before the imaginary disease of deficits. Is it because Germans are perfectly aware of the multiple Treaties of Versailles that they dictate today to Greece, Spain, Portugal and other nations forced to pay much more than their abilities and means allow? It turned into a sort of cardinal – or gray eminence – immured in a permanent conclave and quick to distil the black smoke to prevent any attempt to monetize its debt by the executive of its country. Indeed, this is violent and unprecedented austerity that Germany had to implement at the beginning of the 1930s in favor of the drying up its international funding, which resulted in an unemployment rate that at one time was higher than 35% France – which at that time was the Germany of today – was doing well. Here is the central banker – reporting to no one – who therefore had the power to sanction *vis-à-vis* the elected. It was one of the most prosperous and solid economies in the world at that time. As a result, monetary policy – i.e., the crucial definition of interest rates – was becoming passive. It was content to pass on



and echo the wishes and dictates of high finance. In a position to transform itself into a financial engine for the rest of Europe from the end of the 1920s and beginning of the 1930s, instead, France preferred to withdraw behind a wall of selfishness by refusing to adopt a conciliatory and expansionist monetary and economic policy, opting instead to ignore the plight of its neighbors. This French law of 1973 was subsequently repealed... only to be replaced in 1992 by the Treaty of Maastricht and in 2009 by that of Lisbon jealously defending the same orthodoxy. The financial collapse of Europe owes a lot to this navel gazing by France at that time. Namely to prevent any overdraft facility or credit granted by the European Central Bank to governments, regions or local communities members of the Union. Just as the peripheral European nations can today, with reason, blame German intransigence for their intolerable end that they reached. As our states could no longer call on their central bank to finance their accounts and public spending should they needed to, therefore we have all become dependent on the commercial banking system which, itself, was indeed able to create liquidity privately from nothing to lend to our states through interests. From what remains, France could not escape this crisis which had rudely contaminated it since 1932. Practice initiated in 1973 by France but almost everywhere since an IMF study actually reveals that two-thirds of the 152 central banks around the globe restrict considerably – when they do not prevent a short – all ready or make central banks available to their government. How is it that we fail to recognize that the France of so many years ago is today's Germany, mired in missteps and which revels in mistakes that it will end up by paying – it also – a heavy price? On behalf of the venerable and untouchable “price stability”. Since if there is one country which, amongst all, is worried about retaining the teachings of the past, that country is Germany. So, in defiance of macroeconomic stability. why do we accord so much importance to the 1923 hyperinflation when we should instead be deeply concerned about avoiding 1933, the year which saw the extinction of democracy? And too bad if the cost of financing their debt by our states attain untenable sums, and for public finances, growth and the purchasing power of the citizen... This essential German shift will, however only see the light when this country recognizes its financial debt toward the European Union that it will clearly never leave. In an environment of absolute European depression weathered with the collapse in tax revenues, shrinking welfare and soaring unemployment. Since such a possibility would immediately translate into a strengthening of the rediscovered national currency – the Deutsche Mark – and an inevitable deterioration of the standard of living of its citizens in favor of a dramatic decrease in its exports. With states to finance their lifestyle – so we did! Indeed it is the advent of the single currency which allowed Germany to more than

double its exports from 469 billion Euros in 1999 to more than one trillion Euros in 2010, during which its economy grew twice faster than the European average during the same period. This impressive rise in German exports is undoubtedly inseparable from the quality of its manufactured products. Simply because it is impossible for us to be financed by our central bankers who wrap themselves in their robes of independence. There remains no doubt that its competitiveness was undeniably favored by a relatively weak currency. Independence which in reality is only a smoke screen intended to mask their allegiance to the banking system. So this country benefits on several levels from the woes of hyper weak nations of the EU.



## **Europe: How many Divisions?**

The introduction of the single currency was at the origin of major distortions since capital flows could thus move from one member nation of the EU to another without regulation or control. It goes without saying that these liquidities seeking attractive returns gradually left the nations of the North with limited potential (Benelux, Germany and also France) to take up residence in the booming nations of the South and therefore thirsty for capital. Investors therefore did join in the auction and the returns in the economies of Southern Europe transformed into whirlpool projects under which these incessant capital flows would have been, in different circumstances, moderated by readjustments to the national currencies of these nations. However, the exchange rate could not play its essential role as regulator since all these countries shared a single currency. The masses of liquidities could therefore leave the rich countries to colonize the “emerging” member nations of the EU without the parity of the Euro being lowered for countries that invested or increased for those who benefited from these capital flows. These distortions also led to notorious inflation in the booming nations of the South which was royally ignored by Germany (only to cite it) which was thus happy to be able to invest in, and export to, these countries with great potential. As disastrous as these disparities in the inflation rate within the same zone were in the medium-term, they were not, however, fought since interest rates (like currency) were the same throughout this zone. These interest rates were maintained at an artificially low level for several years so as to support a lackluster German economy at the beginning of the 2000s with, for immediate and inevitable consequences, an overheating of peripheral economies. Indeed, these booming nations – that should have been contained by higher interest rates – were dropped as fodder for speculators who helped to inflate all kinds of bubbles which could have been partially avoided or lessened by an adapted monetary policy.

The famous excess of the PIIGS are therefore largely due to lax European interest rates sanctioned by the ECB and imposed by a Germany which then needed it! It was therefore Germany which dictated this policy to the ECB and not Greece, Portugal, Ireland or Spain... So many countries that were abandoned to their fate, and to their multiple speculative bubbles, as soon as these funds dried up in the aftermath of the

financial crisis. After largely investing in, and benefiting from, speculative development in peripheral Europe, Northern Europe thus did a turnabout and began to accuse the “grasshoppers”, yet once generously maintained by the Northern ants. It is certainly not a question of exonerating the irresponsible behavior of the national leaders of Ireland or Spain who closed their eyes to the excess of their countries, as it is important to condemn the Greek messengers. Just as it should deplore the guilty refusals or delays of the successive governments of these countries in vitally reforming their taxation systems and labor market. For all that, the lure of profit from businesses and finance from the northern countries, the tolerance of their authorities in the face of unjustified interest rates and their convenience *vis-à-vis* a circulation in capital which flooded the countries to the South were so many factors which helped to rush the PIIGS into the abyss.

The German position – which now pushes toward diametrically opposed excess consisting of imposing blind austerity on these highly affected countries – is even less understandable that budget deficits are not the roots of the financial crisis. Indeed, it is the advent of this crisis that breathed deficits into budgets of the states and not the reverse: Were not Spain and Ireland in surplus prior to the crisis? It makes sense also that all countries – a fortiori of a single currency group – cannot simultaneously benefit from surplus budgets. As it is evident that funds could not be invested in a balanced way among the members of the European Union. One of the priority EU projects should thus consist of monitoring and regulating capital flows among its members, a notorious sauce for imbalances in the balance of payments of each member within a framework of a common currency for all these nations. The collapse of Greece (citing only this country) is therefore entirely due to inconsistencies and gaps in the European construction. The members certainly benefited from a precious stabilization of their exchange rate in favor of introducing the Euro. In the same way they benefited greatly from the convergence of real interest rates (for cheap financing) which tended more and more toward those in Germany. They nevertheless forever lost the ability to define their monetary policy, that is to say, fixing their key interest rates. As such, they no longer have the privilege of a flexible currency which they could have possibly appreciated or devalued according to actual needs.

Today, these same peripheral European nations, which formerly masked their poor competitiveness and their high levels of public spending thanks to modest financing costs (due to this convergence which now firmly belongs in the past), are faced with an austerity which will certainly not allow their productive apparatus to recover. The increase in this competitiveness would of course likely bring them growth with the

key being a gradual repayment of their debts. Nevertheless, as measures aimed at improving this competitiveness are only effective in the long-term, only investment is immediately likely to feed growth. Austerity is therefore not an adequate solution when a country is hit by a financial crisis and that its private sector is depressed by debt, a fortiori if its banking sector is hyper weakened by the implosion of a property bubble as in Spain. The interdependence of European countries contributes further to exacerbating the depression, sentenced to spreading like wild fire due to this integration. The prerequisite for recovery – and of course to any lull – is introducing new common credible and realistic regulations, a sine qua non condition for rebooting the private sector. That is why the myth according to which a formula proven to work in one country would necessarily work in another – all the more reason in several others – will end up running through the EU. It is therefore necessary to diagnose separately each member country so as to implement different remedies to each one, or the same remedy according to a different degree. It is in this spirit of nuance, yet necessary if the goal is to significantly reduce deficits and reboot growth, which is sorely needed.

Since the German example is not easy to reproduce, despite the scorn of the German Chancellor Merkel deploring the “mediocrity” which had become the Euro “standard”! However, Germany could boost exports to such an extent only because it has depleted its poor ones! In any case it is what the employees in the Euro of the hour and the workers who earn EUR400 a month scream very loudly about... With its top priority of a long-term austerity policy, Germany can of course boast of unquestionable results in terms of putting its finances back in order. It would indeed react with determination in the face of its colossal reunification cost and in the wake of the very poor competitiveness of the factories in the former East Germany. As such, it followed Keynesian concepts and implemented a sound counter-cyclical measure, namely increasing VAT from 16 to 19% in 2007, i.e. after three prosperous economic years. If the collection of these new revenues necessarily paved the way for rehabilitating its finances, it is evidently much easier to undertake fiscal consolidation at a time of prosperity than during an economic and financial crisis. This increase in VAT was of course one of the milestones of a voluntary domestic devaluation policy whose most obvious manifestation was strict austerity in wages. The trade surpluses were somehow the natural secretion of this German that also resulted in a sharp surplus in the balance of payments. Indeed, impressed by these performances and always in search of solid investments, global investors rushed toward German Treasury bills, which mechanically contributed to establishing extremely low real interest rates in the country in a

general way – and permanently – without any impact whatsoever in favor of an increased in domestic consumption.

It remains no less than the ultimate example to follow was there: the country in difficulty had to prescribe strictly to a regime of halved wages and unemployment contributions, accompanied by substantially higher indirect fiscal pressure. Such was the magic formula that the peripheral European countries had to implement to boost their exports by adopting a recovery model of export-led growth. All in an effort to emulate the German model that was the poster child of perfection, not unreasonably as seen from the first European exporter. If only a country's surpluses are simply for the deficits of others and the German dynamic was successful – by achieving substantial trade surpluses – due to European (and global) consumption of Germany's manufactured products. German prosperity is actually wholly constructed on the economic activities of importing countries. So Germany feeds its own growth from the growth of other countries, somewhat parasitically. Therefore this serves nothing, and it would even be completely counter-productive if all European nations adopt these austere measures all at once to boost productivity in order to reboot their economies through exports. The one and only condition for success of such a business would be that Europe ceases consumption and that the rest of the world rushes to consume European products, which is hardly likely. In summary, how and why is Germany persuaded that its model can be implemented by all of its European partners which are ordered, in other words, to no longer buy its own goods? Germany, whose exports within the EU amount to 60% of its overall figure in 2011? Is it really convinced that the European Union will morph under its influence into a briskly gigantic export machine to the rest of the world? If a country alone can – of the same size and importance of Germany – implement domestic devaluations with a view to improving its competitiveness, an umbrella economy like the European Union having the largest GDP in the world, could not undertake such a revolution in its consumer and export habits without provoking a global disaster. This German attitude of imposing its standardized model of rebuilding reserves and inflating surpluses thanks to exports is therefore aberrant... and also totally unrealistic (in another registry of course) that unbearable reparations had been dictated to it after the First World War.

It is a pity that policies are not a little bit like historians! And that it is regrettable for all of us that they do not look back to 1931 – tragic for all – from which to draw parallels and precious information for today... From the bankruptcy of the very large Austrian bank, *Österreichische Kredit Anstalt*, over-exposed in East and Central Europe. To the general financial instability of Europe under threat from currency implosion due

to unpaid German reparations. To the U.S. intervention in the sense of debt restructuring for a Germany that was tied to a gold standard, yet one of the main reasons for the Great Depression. Only countries which abandon the first gold standards (Great Britain followed by the Scandinavian countries) are the first to pull themselves out of this terrible crisis without incurring too much damage. The unexpected rise in U.S. interest rates in 1928 was certainly the first sign of this crisis. As well, the deflationary global calamity, linked to a global economic contraction, is rooted in the gold standard, particularly due to the attitude... of France, presented by a number of experts as mainly responsible for the intensification of the Great Depression! It is actually the substantial increase in France's gold reserves (from 7 to 27% between 1927 and 1932!), which, in creating scarcity for this metal, would undoubtedly contribute to an enormous deflationary spiral for all developed nations at that time. It is actually the substantial increase in France's gold reserves (from 7 to 27% between 1927 and 1932!), which, in creating scarcity for this metal, would undoubtedly contribute to an enormous deflationary spiral for all developed nations at that time. With deflation as the distinctive sign of the Great Depression, it could have been avoided if the central banks at that time (and the French one in the first place) had maintained their 1928 gold bearing ratios... Indeed, it is this frenetic accumulation of the yellow metal by eminent central banks which fueled global deflationary pressure. However, maintaining gold reserves at their levels prior to the Great Depression would not have altered the historical correlation between consumer and production pricing and the quantities of gold held by central banks. It was Léon Blum, Prime Minister, who finally took France out of the gold standard in 1936, but the damage was done. Isn't the parallel obvious in today's Europe where austerity is the new gold standard? What a pity that policies are not a little like historians since the conjuncture of the 1930s strangely resemble our situation today, except that at that time it was only Germany which was in the same situation as peripheral Europe finds itself today. Entirely dependent on foreign capital, it had been steam rolled by unrealistic reparations stipulated in the Treaty of Versailles within a general framework of grossly under-capitalized national banks. Indeed, this is the whole problem relative to the reparations imposed on Germany, and their disastrous consequences, which have today been removed from the debate to make room for deficit obsession. The ardent defenders of austerity actually impose an absolute diktat on the media, opinions, public policy and academia by imbuing a climate of disaster where only hyperinflationary trauma seems worthy of interest. It is as if the disaster from the reparations imposed on Germany had been waned before the imaginary disease of deficits. Is it because Germans are perfectly aware of the multiple Treaties of Versailles that they dictate today to Greece,



Spain, Portugal and other nations forced to pay much more than their abilities and means allow?

Indeed, this is violent and unprecedented austerity that Germany had to implement at the beginning of the 1930s in favor of the drying up its international funding, which resulted in an unemployment rate that at one time was higher than 35% France – which at that time was the Germany of today – was doing well. Indeed, this is violent and unprecedented austerity that Germany had to implement at the beginning of the 1930s in favor of the drying up its international funding, which resulted in an unemployment rate that at one time was higher than 35% France – which at that time was the Germany of today – was doing well. It was one of the most prosperous and solid economies in the world at that time. It navigated these troubled waters by maintaining a single digit unemployment rate and enviable accounting surpluses. In a position to transform itself into a financial engine for the rest of Europe from the end of the 1920s and beginning of the 1930s, instead, France preferred to withdraw behind a wall of selfishness by refusing to adopt a conciliatory and expansionist monetary and economic policy, opting instead to ignore the plight of its neighbors. The financial collapse of Europe owes a lot to this navel gazing by France at that time. Just as the peripheral European nations can today, with reason, blame German intransigence for their intolerable end that they reached. From what remains, France could not escape this crisis which had rudely contaminated it since 1932. How is it that we fail to recognize that the France of so many years ago is today's Germany, mired in missteps and which revels in mistakes that it will end up by paying – it also – a heavy price? Since if there is one country which, amongst all, is worried about retaining the teachings of the past, that country is Germany. So, why do we accord so much importance to the 1923 hyperinflation when we should instead be deeply concerned about avoiding 1933, the year which saw the extinction of democracy? That German leaders therefore return to school to relearn how a European bank crisis that set off in 1933 propelled their country – and Europe – into the horrors of 1933. It is no longer tolerable that leaders from this country declare (as the spokesperson for the German Ministry of Finance did in April 2010): “Just because we have extinguishers it doesn't mean that we'll use them to put out fires”. Gailbraith had understood well that “there are few areas where history counts so little as in the world of finance”... That is why it is no longer tolerable that political leaders declare (as the spokesperson for the German Ministry of Finance did in April 2010): “Just because we have extinguishers it doesn't mean that we'll use them to put out fires”. Identical instinct – or fears – which are at work in the face of its fear *vis-à-vis* inflation. The big – even single – European problem and the huge chip in its armor is the dichotomy between congenital monetary power

and budgetary authority of the respective members. For indeed only those who save – and who, therefore, fear or dread the future – is haunted by inflation, which has the effect of reducing the value of their savings. Each of these countries abdicated its monetary sovereignty (in favor of the ECB) while it could retain the power to levy taxes... without being in a position to stimulate its economy in the traditional way, like the U.S. did.

This essential German shift will, however only see the light when this country recognizes its financial debt toward the European Union that it will clearly never leave. Since such a possibility would immediately translate into a strengthening of the rediscovered national currency – the Deutsche Mark – and an inevitable deterioration of the standard of living of its citizens in favor of a dramatic decrease in its exports. Indeed it is the advent of the single currency which allowed Germany to more than double its exports from 469 billion Euros in 1999 to more than one trillion Euros in 2010, during which its economy grew twice faster than the European average during the same period. This impressive rise in German exports is undoubtedly inseparable from the quality of its manufactured products. There remains no doubt that its competitiveness was undeniably favored by a relatively weak currency. So this country benefits on several levels from the woes of hyper weak nations of the EU. By exporting more to these other member countries which, suffering from an endemic decline in their own competitiveness, end up with German imports less expensive than their own national products! By exporting more, of course, to the rest of the world due to a weakened Euro because it comprises nations like Greece, Portugal, Italy or Spain... Germany does not need to manipulate its currency to make its exports attractive: it is simply a bystander watching the fire engulf peripheral Europe and the South. In this regard, an interesting and revealing study from the Swiss bank, UBS, concluded that an exit from the Euro would cost Germany between 20 to 25% of its GDP, i.e. between EUR6,000 and EUR8,000 per capita the first year, which should reduce to EUR3,000 to EUR4,000 the following years. The same study indicating that the German citizen should only have to pay EUR1,000 in total if the European Union were to integrate half of the debts of Greece, Ireland and Portugal... the only reason for the much higher price to pay when exiting or breaking the EU is to be sought in its currency, which would suffer a simultaneous and lasting appreciation penalizing its exports. The ING Group estimates that a scission in the European Union would result in the Germany's GDP falling by 9.2% with unemployment at around 9.3%, the price to pay for the surge in its regained currency which would translate into a substantial collapse of the German export engine. In a sense, the German leaders are today faced with a tough choice since it would mean having to support financially an integrated

Europe by pooling the debts of member countries. The alternative, hardly more appealing, is to assume the potentially devastating social and financial costs of exiting the EU to which the massive recapitalization of German banks will be linked, heavily involved in the sovereign debt of the peripheral nations. In other words, the Germans are completely interested in remaining in the Euro zone, as they have everything to gain if the Euro remains at current levels. As a last resort, they will therefore do whatever is necessary to support “weak” nations like Greece within the EU.

## A Mercantile Europe

Intensive fiscal consolidation implemented in peripheral Europe and France actually acts as a scorched earth in the sense that it literally smothers the tiny growth prospects still alive. Knowing that, in addition, the economic recovery will be more painful than the downturn will have lasted a long time... It will only do so thanks to a re-balancing from within even the Union and will necessarily be substantial. The nations which must now undergo austerity will indeed have to intensify their exports to the EU countries whose growth is (more or less) intact. In fact, this re-balancing is already underway, but remains largely inadequate. If German imports certainly increased by 2% between July 2011 and July 2012, the trade surplus of the country has also increased, making sure to neutralize this stronger domestic demand... Moreover, why do Greece, Portugal and Spain continue to suffer huge trade deficits despite rising exports combined with a deceleration in imports? The answer is to be sought in the German labor costs which have experienced a nominal drop of 18% between 2000 and 2009 compared to the European average income. It is actually to a real killing game that Germany was delivered and particularly toward the peripheral European countries which, themselves, saw their wages rise significantly over the same period. Eurostat statistics show us that income gaps have widened by more than 40% in less than ten years between Germany and countries like Greece and Spain. Obviously totally to the detriment of Greek and Spanish companies which have suffered a de facto forfeiture of their competitiveness *vis-à-vis* a competitor who also has qualitatively superior products. Today, the situation is gradually changing in favor of the improvement of Greek competitiveness (for example) because the employees in this country have seen their income reduced by 19% since 2009. However, the slowness of this intra-European re-balancing – and the continued suffering of the Greek people – are entirely attributable to the timidity of Germans who have raised their wages by 2% between 2009 and 2012. The Euro zone would love to address these acute problems in differences in competitiveness within Europe by exporting more to the United States, to China and to emerging markets. It knows, however, that it cannot build on this hope of salvation in a context where the U.S. is struggling to recover their own business by dint of cash injections, and while China – which seems to be slowing – tries to satisfy

their consumers with products manufactured domestically to limit the bill of its imports. Therefore, the solution will necessarily come from within the EU, and it is unique because it is summed up in higher German (and Nordic) consumption. In other words, it is vital for the entire Union that this intra-European competitiveness “gap” be quickly filled by peripheral European nations increasing their exports. Therefore, Germany will have to stimulate its growth, probably (but not only) by reducing taxation, to actively participate in this intra-European re-balancing. The entire Euro zone desperately needs to revive its domestic consumption. And this will necessarily entail a rebound in German consumption. If the Germans assume that no country can live beyond its means, the same logic should also dictate that no country should live below its means! The radical change in German wage policy is an integral part of the solution to European woes.

The advent of the single European currency has exacerbated the dependence of EU economies on exports while denying them any means to protect themselves against default in payment. The introduction of the euro in its current form operated indeed a clear distinction between the monetary sovereignty and the fiscal policy of each member nation. The dichotomy to restrict the public deficits of each member and to curb near-natural inclinations of politicians to spend. Moreover, everyone was perfectly aware that fiscal indiscipline and the lack of fiscal rigor would be sanctioned by the markets, which would question – until their solvency – any potential “short-sightedness”... Thus, this congenital defect – the lack of monetary sovereignty – undermined the entire European construction by propelling to the issue the forefront, yet relatively, benign public deficits. It is as if the entire immune system of the Union was suddenly switched off. In the absence of a central bank free to inject cash into the public finances of needy members and in the absence of a federal budget on the back of the firepower of the European Central Bank. The European debt crisis and fiscal woes of peripheral countries must therefore be put into context... that shows us that the narrative according to which it is the spendthrift and lax nations which are allegedly responsible is clearly wrong. This sophistication with financial tools is being knowingly developed by a financial sector concerned with evading the law. Let us well understand that, in the globalized financial world, fraud is not an anomaly: it is an integral part of the system, it is one of its undisputable components. Suffice it to say that we need only look at the jargon being used in the mid-2000s to understand – thanks to vocabulary! – that the financial stakeholders knew perfectly well that they were distributing suspect and unsavory financial products. They were “neutron credits” intended to crumble without causing their downfall in the housing market. They were “ninja credits” whose poor beneficiaries had no income, no job or assets (No

Income, No Job or Assets). Moreover, the currency sovereignty of members of the EU would have allowed them to deal with the crisis as an emerging economy would have. However, short of having the advantages granted by a fund transfer institution or a central bank worthy of this name, the affected European peripheral nations were subjected to attacks on their sovereign bonds whose yields soared. The markets made them pay dearly that they found themselves boxed in – even bastardly – where their solvency was suddenly called into question. A textbook example, Ireland saw its consumption and growth record lightning levels and growth as a result of the sentiment of wealth induced by the expansion of its real estate market through the transmission belt of credit. Powered by the euphoria of the real estate loans, did the Irish banking system not swell – like the frog of La Fontaine – to reach a volume five times the country's economy, and the Irish foreign debt 400% of the GDP in 2010? Did not the crisis imported as a result of the United States and Great Britain end in a panic on the Irish banking system whose rescue cost 20 points of GDP to little Ireland, whose budget deficit would widen to 32% of GDP in 2010? Untenable pressure exerted on a country which since then suffered capital flight, due to a lack of an intra-European compensation mechanism. Another case in point, namely Spain, whose banking system was overrun by a storm and not being able to devalue its currency on the foreign exchange market... due to there being no market to quote the Spanish currency that no longer existed. Thus, unlike the Asian financial crisis, the European financial crisis could not benefit from the currency valve supposed to offset (at least partially) the terrible internal devaluations.

In short, the EU founders certainly imposed very specific safeguards to reduce the extreme risk of default of a member nation. The fundamental objective of the Stability and Growth Agreement is certainly to confine the excessive accumulation of public debt. Yet – and very probably obsessed by the German obsession with deficits – the founding fathers of Maastricht also neglected the existential threat of an overflow of private debt. This explains why and how the total lack of monetary sovereignty of the member countries of the Euro zone is the very foundations of the crisis. And also that is why austerity which weighs on public budgets is ineffective. Because unlike the forecasts of orthodox economists (i.e., almost all of the profession!), reductions in public spending in Spain, Greece and elsewhere have certainly not been offset by an increase in investment by the private sector. In fact, the private sector – still heavily indebted – began instead to save through fear (justified) of a further decline in economic activity, which would be naturally induced by fiscal discipline. An IMF study (dating from the very beginning of 2013) shows that a dollar reduction in public spending does not remove 50 cents from an economy, as the current dominant

thought and economic research imagined it would, but rather...\$1.70! This crisis would have no place in the European Union if it was a genuine monetary union like the United States, operating fiscal transfers between their states if needed when it comes to offsetting the adverse cyclical effects on the budget of one of their 50 stars. The European episode is therefore not a history of public indebtedness, or balance of payments deficit, and therefore requires no solution using fiscal austerity or sobriety on its members. It is this statutory schizophrenia established between fiscal policy and currency on the one hand and the absence of other intra-EU transfer mechanisms to reduce the imbalances that have shaped an unnecessary and completely avoidable crisis.

The European Union still has an arsenal of stopgap measures at its disposal to easily out the fire which ravages its weakest members. As they have accounts with the ECB, why would the ECB not provide Greece with enough credit so that it can, not embark on a spending spree, but only borrow three quarters of the sums due after its forthcoming bond deadline? European authorities would naturally implement adequate monitoring measures so as to protect their collective interest, and this country would continue its measures of financial restructuring and rationalization. It should be simple enough to borrow an amount progressively lower than 25% *vis-à-vis* its needs by the grace of the European printing press. Suddenly, the markets would demand lower interest rates on residual financing agreed to by Greece, bolstered firstly because its debt would have been reduced by 25% and reassured secondly because this intervention would attest to European cohesion. The benefits of this injection – purely technical – of liquidities would gradually be felt on the Greek economy since tension would drop significantly because a state would be less dependent on market severity. As such, and as growth is restored in Greece which would be mechanically reflected in its tax revenues, the ECB would slowly recoup its loans, either by debiting Greece's account or by another more inventive means crafted by our sound central bankers.

Since this is only this condition – namely, solidarity – capable of returning Europe to prosperity. Indeed it is against nature that such shocking differences in the compensation of their respective Treasury bills prevail among married couples, having vowed to remain together for better or worse. How can the wealthier European nations themselves and, a fortiori, this supranational pseudo-institution that is the ECB, accept that Greece, Portugal or a country like Spain pay 3, 4 or 10 times more for their debt than Germany or Luxembourg? Is it acceptable, as pointed out on August 1, 2012 by the German daily Bild, that “Germany earns money thanks to the Euro crisis?” According to Bild, the country would have saved EUR60 billion in the last thirty months in refinancing

its debt. It is that simple, and Bild trumpets it: “Germany even earns money while being in debt”!

Forgiveness would have been possible if the pitfalls had been insurmountable. As it happens, the cure for this great evil which ravages Europe is childlike simplicity since it suffices that the ECB credit certain accounts, of course subject to safeguards. Does the actual European strategy – imposed by Germany and its central bank – not remind us of the U.S. bombardment of Vietnam which destroyed a rebel village while claiming to save it? Did Germany, the Bundesbank (the German central bank) and the ECB not destroy the European Union which believing it was saving it? A possible decision of total and unlimited support by the ECB would obviously be highly political, but politics in Europe is, as we know all too well, is slow and complex. The European construction was however carried out since the beginning thanks to a prominently political objective which was to make Europe forget the war and to erase dictators, communism and therefore rifts from Europe. It is regrettable that it is this radical shift, toward a Europe entirely based on trade and finance, which made it lose its political horizon, and which is now on the verge of damnation. In the same vein of ideas, how do we accept that the necessary fiscal and social harmonization in the EU brings unanimity? For intra-European fiscal and social competition – i.e. within the same Europe – is even harsher than *vis-à-vis* the outside, and under the pressure of Anglo-Saxon neoliberalism in its purest version it has been introduced into the EU! Today, the sole issue remains the economic government of the EU with the qualified majority, at the risk of seeing Great Britain depart. The tendency should be toward solid federal governance (with fiscal and social coordination) rather than punitive governance currently in place. Europe will therefore turn into a vacuum, coming to a complete stop – totally exhausted – if it does not take the bull by the horns for a total sharing of resources. The ultimate instrument for sharing its wealth is its central bank. It is obviously not the only one and there are several other ways of showing solidarity, but the quickest way to appease the present woes of the European population is to outdo the markets and restore growth. Moreover, is there anything to question when our jobs, our standard of living, our social peace and our comfort are threatened? Is this only because of their bad management and speculative bubbles that certain European nations are living through an existential crisis? For the construction of the EU deprived them of their financial sovereignty by placing them in a position of absolute dependence *vis-à-vis* the ECB, while making them singularly and solely responsible for their growth. Greece, Portugal and even Germany are thus comparable to the U.S. states without even the benefit of a federal government which spends (and borrows) to stimulate their economy. For, we are under no illusions, only public spending



reestablishes growth when everything else has been lost or suspended. The only honorable solution for Europe is a formal federation which would suddenly provide each of its member countries with its currency sovereignty and replace the EU as a club of countries benefiting from the privilege of printing money at will, if need be, so as to lend assistance to its states in need. Beyond that, we are actually witnessing a pitiful tragedy where the ECB and the rich countries wallow in their autism while other members of the family are slowly dying. Only raising the problem and resolving it at a federal level are likely to save the European Union. Such a happy event would see creditors “line up” to lend Greece which would no longer, in the absolute, need them since it benefits from the ultimate assistance of the ECB (which would therefore deserve its name of “lender of last resort”) or other European mechanisms. The risk of a European country defaulting in payment would immediately evaporate.

Beyond that, Germany and the other countries in its bosom are constantly bemoaning the lack of competitiveness among the peripheral European nations where labor costs would be too high in comparison to the frugal Northern “ants”, disciplined and controlling as though it is owed the costs associated with their payroll. This permanent stigmatization passes, however, under the silence of a phenomenon that specifically allowed the salaries of the PIIGS to gradually increase since the 1980s to join the current salary levels of industrialized nations, well integrated in the North. It is therefore due to this “convergence” that the labor cost increased in Spain, Portugal and in the countries to the South, and not following the bad habits of their employees presented as lazy and yet demanding... It is now difficult to deny that the salaries of workers in the South do not differ markedly from those in the North per unit of goods produced. German, French, Spanish, Portuguese and Irish workers indeed earn their living equivalently to similar product or equal service. In reality, the workers in the South are even generally less well paid than their Northern counterparts since they produce goods and ensure services either in lesser quantities or of inferior quality. In this regard, competitiveness, labor cost and even the mentality are definitely not the central problems of the PIIGS. There are several and daily examples of workers from the South who migrated to the North revealing their talents, skills, discipline and diligence. The deficiencies of the nations to the South are instead to be found in the level of public and private investment in key sectors as their infrastructure, equipment and governance.

Therefore, it is not only the level of wages in these countries that must be questioned but also the paltry allocation of their assets which clearly makes them incapable of being competitive – in quantity and

quality of the goods produced – with their neighbors to the North. Indeed, the wages perceived by the workers to the South *vis-à-vis* their production only makes them lower. In other words, the sharp increase in the prices of their goods does not reflect only their revenues, which are little appreciated, but also the harmonization of the tariffs of their goods and commodities *vis-à-vis* those of the North. For the PIIGS, the European convergence is transformed into a sizable increase in prices in the face of relatively stagnant wages. These accusations according to which the Mediterranean worker would have abused the influx of capital in his country by always demanding a higher salary, obliterating the competitiveness of its economy, are therefore only stuff of urban legend. Indeed, labor costs per unit or service produced has hardly increased proportionally with the selling price of that same product that the Southern worker received less pay per unit in 2007 than in 1980! Labor costs therefore converged between the Centre, the North and the periphery of the European Union due only to the convergence of prices between these regions, and through no fault of employees to the South who would have won a larger share. The real reasons for the lack of competitiveness of the PIIGs may therefore be found elsewhere, namely in the high compensation of huge masses of capital which were invested there at that time. The investors actually demanded always increasing returns on capital as the price for their cash investments. So much money which was therefore cruelly lacking that was needed for the vital structural improvements to bring them in line with that of the North. These southern nations were therefore more victims than beneficiaries of these capital flows.



## **An Unnecessary Crisis and Completely Avoidable in Europe**

In conclusion, the days of the Euro are today threatened, not through the fault of abysmal deficits of certain European states, but simply because of the European policy skids leading to a cacophony of unacceptable dithering. European leaders do not always consider that it is the dissolution of the Union – in any case as is already known for more than a decade – which is on the menu if they finally decide to address seriously the issue of fiscal union! A European Treasury should thus be created, a logical conclusion to fiscal harmonization for all members of the EU, which will act as a shock absorber necessarily produced by nations with often divergent business cycles and essential diagnoses. To even raise funds through the issuance of bonds, this European Ministry of Finance will, at the same time, function as an agency for transfer payments from the wealthiest nations to the least wealthy. For, without a good and solid fiscal union, the European massive and endemic imbalances will eventually be due to the Euro zone. Either by the gradual and inevitable exit of its weakest members, or by the comprehensive and sudden implosion of its entire structure! It would be much more advantageous for all EU member states to pass through the necessary “fiscal union” case/box than to have to endure the throes of a broken currency which would accompany bank failures, default payments of sovereign debt, even the reestablishment of exchange control and freezing bond markets... Political decision – in the noble sense of the term – through excellence, this fiscal union seems, however, impossible to realize in the current prevalent political landscape in the various EU countries. Indeed, it is not only Germany which will veto, it is not exclusively the voter and the taxpayer of this country who will refuse to participate financially in saving the European project... As a “fiscal union” is necessarily accompanied by extra sacrifices, the weaker countries themselves will also use their veto because their citizens have become completely disenchanted – even disgusted – with what was once for them the European “dream”.

The failure of the European Concept – according to which a country in difficulty can appeal to the monetary policy or benefit from budget transfers to settle its domestic problems – is therefore likely to lead to a

major, economic and, indeed, financial, but also political crisis, since these nations realize that they receive no support in exchange for giving up their sovereignty. It goes without saying though that only mechanisms of cash transfers toward these fragile nations are likely to overcome their loss of solvency, while reversing the unemployment and income curves which change unfavorably and indeed inversely. Even worse since the attempts by these weakened countries to reboot their domestic consumption were sharply swept a backhand by “exemplary” countries. These righteous nations systematically imposed stringency everywhere causing these affected economies to dry up. An elementary reminder of fundamental differences between sovereign countries and nations which, abdicating all control over their currency policy, would have otherwise avoided the European implosion. The insolvency of peripheral European countries would never have actually been challenged if they had been clearly supported by an ECB which has the privilege of printing money at will that it is able to inject into its needy members. A group of countries benefiting from this option to create a currency, covering such a geographic zone and reflecting such clout can never go bankrupt, except of its own doing as the recent U.S. episode demonstrates where Congress balked at raising the debt ceiling. In reality, there is no European debt crisis. There is, however, a Euro crisis. The debt is simply a symptom of the single currency crisis and a defective central bank which, furthermore, takes pleasure in navigating in troubled waters. A more important start-up in the world history of investment funds of up to \$1 trillion, does not LTCM count among its prestigious staff two future Nobel Economics Prize winners? It is therefore the Euro in its present form which creates the conditions for the crisis lined with bad choices. Austerity being one of these bad choices. Since economic recovery is well worth, after all, the temporary worsening of deficits... Indeed, given that EU members cannot print their tickets, as the refusal by the ECB and European institutions to flood them with cash, transforms each European nation... into a bank! Spain, Italy or Greece have therefore become banks and are subject – exactly how a bank would be subject to it – to flights of capital and massive cash withdrawals, until the final collapse.

The big – even single – European problem and the huge chip in its armor is the dichotomy between congenital monetary power and budgetary authority of the respective members. Each of these countries abdicated its monetary sovereignty (in favor of the ECB) while it could retain the power to levy taxes... without being in a position to stimulate its economy in the traditional way, like the U.S. did. This very restrictive mobility of EU members in rebooting their economic activity and encouraging their growth comes from two flaws. First, the inability to print their own currency and therefore to inject liquidities into their

economy. Second, the Maastricht criteria strictly governing public deficits considerably restrain states in their maneuvers to consent to an attractive tax system, as well as to public spending (to hire bureaucrats or to initiate substantial public works projects. It should be noted that the European structure did not give priority to jobs which were sacrificed on the altar of economic orthodoxy and stringency. For the fathers of Maastricht, it was, in fact, better to restrain spending public spending and focus only on growth to reduce unemployment... that is if the employment was part of their concerns. It is this congenital defect that is responsible for triggering the crisis suffered by the Union for three years. And it is this European superstructure, tax and fiscally decentralized, which is the source of its amplification. As the peripheral European nations are deprived of the monopoly of issuing currency with which they go into debt, lenders consider when they borrow in a foreign currency. In addition, this lack of fiscal and budgetary integration of members of the Union exacerbates financial strains since setbacks from national banks permanently contaminate their trusteeship country. Indeed, the financial system and states interact very differently depending on whether monetary union is centralized or based on some sort of federal system. Indeed, the financial system and states interact very differently depending on whether monetary union is centralized or based on some sort of federal system. The solvency of a member state of the United States of America is never called into question by the failure of a bank incorporated and domiciled in the State in question. However, for those who argue (correctly), the United States was not made in a day. And others, such as Germany and the Nordic ants, try to bring to the Southern cicadas the culture of rigor and discipline, essential prerequisites for the European fiscal and budgetary integration. It is necessary to oppose even the chronology of the formation of the European Union. The sequence requiring balanced budgets and debt limit and deficit was in fact the starting point from which all should flow. This is the form that was privileged at the expense of substance and contempt of solidarity. In doing so, this decentralized structure grossly underestimated the vulnerability of countries with a natural inclination to deficits, or simply faced with specific difficulties. Countries particularly dependent on the influx of private capital, in a context where they had no latitude to beat their currencies. In other words, the original sin was to establish the Euro before the federal union and in the absence of duly formed organically integrated institutions. How did the founders of the single currency hope to hold a fragile building together whose foundation consisted of economically, politically and institutionally nations so divergent for which there existed no mechanism for compensation and support? Solely by virtue of a balanced budget? Indeed, by giving up this precious flexibility granted by a sovereign currency (and therefore free to

print), by abdicating their currency policy (i.e., the definition of their interest rates), by forcing the convergence of economies into notoriously dissimilar competitiveness. The Euro weakened core European countries. And it brought about the inevitability of speculative bubbles in the peripheral countries, that could only now count on these bubbles to maintain and sustain their economic activity. In reality, the financial turmoil of the EU is only the deep symptom of endemic evil of European integration overshadowing growth and employment.

However, growth is not challenged by social assistance programs. Indeed, nowhere was it proven that there was the direct and systematic correlation between public spending in favor of its citizens and a regression/decrease in growth. In other words, let us not sacrifice wellbeing, safety and harmonious expansion of the population on the pretext that economic growth would win here since this is not true. Indeed, only poorly targeted social programs affect growth, insofar as monetary policy or inappropriate taxes. For it is not European nations which spend more on their citizens which today find themselves on the brink, as, on the contrary, public spending on social programs by the peripheral European countries did not weaken them. For it is not European nations which spend more on their citizens which today find themselves on the brink, as, on the contrary, public spending on social programs by the peripheral European countries did not weaken them. In reality, the spending by the PIIGS on social programs are less than that by the so-called “Northern” European countries such as Germany, Austria, the Netherlands, Belgium or Finland, which can be more generous thanks to their ability to borrow from the markets at negligible costs. The same can be said for non EU European countries (such as Switzerland and the Scandinavian countries) which – benefiting from the huge asset of very low cost financing, even negative – which also spend a lot more on social programs than European countries such as Italy or Spain. In what kind of world would we like to live? In a world where certain countries may provide largesse to their population because they benefit from zero percent interest rates on loans from the financial markets? While others, who carry large deficit accounts, are victims of punitive means from “investors” who, suddenly, exert unacceptable and outrageous blackmail on vulnerable people. In so doing, Europe is floundering in an authentic “liquidity trap” described by Keynes, although of a new and modern kind. These negative rates paid by certain privileged nations on their bond debt are in fact a veritable liquidity trap, in the sense where they are captured by the wealthy countries and thus subtracted from the affected countries that yet need them greatly. A fractured line therefore divides Europe, a sort of financial iron curtain which operates a methodical triage between the club of countries with negative rates and others. Obviously no one has an interest in maintaining or fueling this polariza-

tion, but are the rich countries in surplus even aware of this? Will the European Union – this piece of work by Monnet, Schuman and Adenauer –, this economic and financial powerhouse with the world's highest GDP, passively adapt to seeing certain of its members finance freely their standard of living while others must borrow at 5 or 7%, when it is not even more...? Is it not amazing, for example, to hear the Portuguese Prime Minister urge (in August 2012) the youth of his country to leave to seek work elsewhere? It is actually our youth who are the first to pay the price for this crisis. More than half of those under 25 years old are unemployed in Greece and Spain, knowing that youth unemployment is also higher than 50% in certain regions of Southern Italy! Indeed, under the pretext of conforming to orthodoxy, how can we tolerate sacrificing our youth at the altar of liberalism? How do we remain unmoved in the face of intergenerational conflict which is occurring inside our Union, where those in charge seem obsessed by stock market fluctuations and by the verdict of rating agencies? How do we tolerate hundreds of millions of European citizens – today, in the second decade of the 2000s – still being kept hostage to financial markets which freely possess the powerful tool to reward or otherwise sack? Does the European civilization not deserve better than to be summed up in terms such as “returns” or “state bonds”? It is imperative to redirect radically Europe's construction, when Milton Friedman asserted that it would not last more than fifteen years!

Dogmas – like prejudices – wreak havoc on society and, one might add, on economies. Are not austerity and fiscal orthodoxy considered like truths unveiled by the same ones who depart from the – untouchable – principle according to which recessions and high unemployment are the price to be paid for achieving the sacrosanct balanced public accounts? Comforted by the great majority of economists and the small academic world, almost all our political and economic leaders only have eyes for this neo-liberal doctrine. And have nothing but contempt for the neo-Keynesians and other progressives who clearly distinguish between the budget of a sovereign state... and the purse strings of a household. Applied stupidly and to the letter, dogmas are often cruel and destructive. That does not matter: our politicians, like our intellectual elites, impose rigor with the same lightness that apothecaries of yore practiced bloodletting. O tempora, O mores: our new charlatans continue to prescribe today more austerity for citizens already stifled by the recession! It is all the more remarkable that these fanatics have consolidated more their grip on our system, whereas it is their neo-liberal belief that precipitated our economies into the abyss. While devoting corruption and unbridled capitalism to the rank of deities. Is not it sad that even those who supported, yesterday, growth and employment are driven today as ardent defenders of “blood and tears”? From the creed of the



golden rule, tirelessly and religiously recited by the current “socialist” executive. To the dramatic consequences of the reductions in budget expenditures on the French economy inevitably doomed to contract. Through the act of contrition, pathetic servility, agreed to the government (“It is our duty to reverse the trend”, according to Pierre Moscovici, French Minister of Economy and Finance, referring to, on December 27, 2012 in the German *Handelsblatt*, the French commitment to reduce the deficit to 3% in 2013). The brainwashing done by the neo-liberal cult has proven successful – globally – as even the French left followed suit. Since even the most powerful man on the planet – the U.S. president – caves in to its demands: he gradually ceded nearly all of his positions to the Republicans in the resolution of the fiscal cliff. Haven’t President Obama and his administration now been reduced to finding insane tricks to fund social programs? Thus the U.S. Treasury has discussed putting nearly \$1,000 billion in platinum coins into circulation, which would allow to legally circumvent the U.S. debt ceiling! As such, today, everything has been accomplished. Indeed, like religious fanatics, neo-liberals refuse categorically to submit to the evidence that a sovereign nation, which issues a sovereign currency (i.e., freely exchangeable in markets), is in no way subject to creditors that would put the ante on its financing costs. A sovereign nation and so-called leaders can – and must – spend more than their income allow for, if their objective is to stamp out the recession. The battered citizen only knows that a central bank could simply press a button to credit accounts, create money, and this, with the dual aim of reviving the economy and protecting its people from the throes of financial markets. Who took the trouble to explain to the unemployed at the end of the day that a country which has a sovereign currency can maintain budget deficits over extremely long periods of time without the negative impact on economic growth? The employee struggling daily to provide for his family would be outraged to learn that austerity (he is the first to suffer) only exacerbated the economic downturn. A nation and a household must apply diametrically opposed strategies when their incomes collapse: while the decrease in spending of the individual has a negligible effect on the economy of the country, reducing the lifestyle of the public sector has a disastrous impact on both the private sector and consumption. Any other strategy is doomed to failure, despite the imprinted statements of pity from the neo-liberal theorists who argue that the economy of the European Union worsens for not having opted for more rigor and for not having prescribed it early enough! So two worldviews clash: bleed a more or less moribund patient even more or send the neo-liberals away who show an almost morbid obstinacy to want to balance the budget of a country. No: the U.S., Great Britain and Japan – which have a currency that they can print when and how they feel like it – did not suffer from escalating cost

of financing public debt. No: the unemployment level in the U.S., which implemented several stimulus packages, did not quite reach the average catastrophic levels of the EU. Yes: the U.S. economic recovery and unemployment reduction would have been more dramatic if these stimuli had been more generous, as advocated by the neo-Keynesians. And finally yes: in spite of these cash injections and despite the massive amounts of money that were printed (with the QE1, QE2 and QE3 programs combined with operation “Twist”), the U.S. fiscal deficit was reduced over these past three years at an unprecedented rate since the end of the Second World War! The budgetary savings signed by President Obama will drastically reduce the U.S. federal debt which is expected to fall to 83% of GDP by 2022! After swelling multiple speculative bubbles since the mid-1980s, the neo-liberal ideology so ravaged Europe today, imposing across the continent the fire of austerity and destructive madness of balanced budgets. We must reject all these senseless net savings programs, as it is imperative to oppose any cuts in social spending, the effectiveness of which is systematically denied by reality. Because the state should instead be generous and invest in the economy – ie increase its deficits! – so long as this recessionary environment persists. In fact, behind this technical debate, hides a much more significant battle: a real societal choice. The economy must become a social system serving the citizen. And money a simple tool made available to the system, must be measured out for collective prosperity, that being its only concern. That is why, today, neo-liberalism is nothing more than a “barbaric relic”!



## **Cyprus, or the Supreme Contradictions of Neoliberalism**

The Cypriot adventures ended up demonstrating the new reality prevailing in the European Union. Namely, in this world dominated by national egoism, careerism and the Brussels technocracy, nothing advances and it is strictly impossible to progress without crisis. Bureaucracy and European inertia, coupled with petty calculations of the respective leaders of each member country can indeed only be moved under the ax of financial markets and under intense media pressure. Never mind that unnecessary crises may have to be created. As everyone now knows, the EU will not be dismembered and it will be preserved, the main actors (i.e., Germany) skillfully exploit these structural defects while using the lever of threat – or blackmail – to achieve their ends. Hence the categorical refusal to support small Cyprus without confiscation of bank deposits. Indeed only the spectra of a rise in power of the financial crisis with its lot of market liquefaction, bank failures and at the end of it all, the worsening of an already unsustainable unemployment, are proving quite effective. Because only these threats can be conveyed to the affected populations as the very bitter pill of austerity. In this respect, the Cypriot narrative perfectly illustrates this operation. This storytelling masks a hardly blameless reality for European citizens. However, the official history of blood and tears, the announced implosion of markets where we are told that it ravaged the real economy, the cataclysmic demise of the single currency, gradually badly hide the all-powerful lobby of nations which pull the strings and is obviously led by Germany. And that we stop hearing the eternal refrain of the “clash of two European models”. From this Mediterranean Europe which consumed endlessly (including German products) to Northern Europe which is ageing and which therefore is logically obsessed with preserving their savings. No! The continent is moving now to the Wagnerian score that seeks to transform us into global export machine. Which steamroller – whose ultimate goal is to unify Europe – can only move forward decisively under the pressure of dramatic events. That’s why a turn of events in the smaller European countries (representing less than 1% of EU GDP) turns into melodrama rocking the very foundations of the Euro. Which explains why a molehill becomes a mountain. If I were

the European Minister of finances, I would for sure jump on the bandwagon of this psychodrama and declare invariably serious events if you do not persevere with the rigor that is our only way out. After Cyprus, isn't there... Slovenia which is likely to sweep us away? We owe the unprecedented intensity of "sovereign debt crises" like its past and future relics to the "Made in Germany" factory of crises. It is thanks to it that the poorly-named European Central Bank looks away while unemployment affects more than one in two young people in some of the "Club Med" countries, which are inadvertently inspired by the cicada. By stifling solidarity and stoking egos, German imperium lays the groundwork for social and identity conflagrations in Europe.

How was the European Union able to tolerate in its midst – or at its level – nations which favored such banking and financial growths? And why did it not seek to contain – when there was still time – this development, all the more morbid as the relevant countries were tiny in size? Indeed, Iceland, Ireland and Cyprus owed their meteoric prosperity to the sprawling development of their banking "refuge", which would make so much profit that it eventually became incommensurate with respect to the size of the economy that housed it. Too massive to be saved or "too big to save"... Thus the bank deposits in the Icelandic financial institutions culminated in 980% of this small island's GDP, i.e., proportionally ten times the bank loans in the United States. While Ireland had a large banking system, 440% of its GDP and Cyprus 800%! Iceland, however, was able to pull out of it more honorably than Ireland who suffers always from having its citizens absorb the losses of its banking system. Having actually declared default toward its foreign depositors and on its offshore accounts, Iceland was also able to benefit from a flexible currency whose fall led to the devaluation of the deposits of its investors. It is therefore only due to a financial repression in good and due form – coupled with a temporary control on capital – that Iceland was able to recover. Knowing that losses on deposits in Iceland were much more substantial than those that would be imposed on the Cypriot bank accounts, which would receive more lenient treatment. Yet Cyprus found itself at a crossroads, faced with a fundamental choice. Look fully and finally to Europe, or continue to maintain a banking system sheltering very questionable fortunes. If its past banking excesses – and its some 20 billion Euros in Russian funds deposited in its banks – enabled it up until then to tax its citizens at lower rates and avoid investing in a sustainable economy. It now became intolerable – after soon six years of financial crises – that a nation leaves its banks to metastasize, without being able to support them in case of need, let alone correct their abuse. But let's not only stigmatize small Cyprus. Doesn't asset under management in Singapore attain 7.7 times its GDP?

Did only the balance sheets of UBS and Credit Suisse rise to three times the Swiss GDP, whose bank balances are 6.8 times GDP?

So many statistics indicated that there was decidedly something rotten in the kingdom of the global financial architecture. Did not the absolute freedom of movement of capital, established in the 1970s, began at the same time an era of repeated financial crises and speculative bubbles? Are the successive crises in Latin America and Asia – which were the prelude to the big implosion of Western countries which started in 2007 – not directly attributable to an abuse of leverage as a result of the free movement of capital? Both made possible due to poor banking and financial regulation? While it is clear today that the reestablishment – at least in some form – of control of international capital flows would only be effective if adopted on a global scale, or at least by the G20 countries to start. The Cypriot episode confronts a reality that should finally allow the right questions to be asked: should not the full liberalization of movement of capital be amended? If globalization was – in theory – full of hope and prosperity for some nations and regions of the world, it has also proved disastrous for the countries unable to regulate a sprawling and uncontrollable banking system designed to make profits worldwide. Ditto for the European construction: great project and ideal on the verge of sinking due to no centralization, common banking regulator and shared taxes. Birth defects with immediate consequence that a Cypriot Euro is not worth a Luxembourg Euro, because of no common deposit insurance, which cannot be agreed to without a common regulatory banking authority. As each member of the European Union has, in reality, a qualitatively different currency, despite a cosmetic or synthetic Euro which no longer deceives anyone. This European monetary union meant to stabilize material comforts to promote harmony among peoples has now been transformed into a precarious factory. Hope, however, does not seem lost, and in this respect, to pay depositors – creditors – is a giant step and a notorious intellectual effort in the right direction. If it is fundamentally unfair and unacceptable to help small savers. If it is absurd to implement such a tax for the sole purpose of balancing public accounts in order to sink your teeth into a stupid orthodoxy. To tax the wealthy – or to collect a certain portion of it – gives states an alternative that they cannot afford to overlook in a European context where the ECB refuses to use its printing press. By the end of 2011, the very influential Boston Consulting Group had predicted that nearly 30% of global wealth would gradually be absorbed by the states themselves under pressure to absorb their losses by the financial markets and the orthodoxy requiring the balance of public accounts. According to the institute, it is indeed no less than \$21 trillion in debt that our Western countries should absorb by monop-

olizing 28.7% of the wealth of the affluent western classes, which amount to \$74 trillion!

All countries will obviously not be housed in the same boat. The Handelsblatt cites the case of Italy where the average private wealth is 164,000 Euros, compared to Austria where it is 76,000, to deduce therefrom that – on paper – this country suffers from no debt crisis. Indeed, while the Italian individual assets (again according to the BBG) reach 173% of the GDP of this country (compared to 124% in Germany), would not it be tempting (and understandable) for the Italian authorities to take 15% of this wealth to get their public debt below the level of 100% of GDP? In an environment where austerity and lack of endemic competitiveness cripple the majority of European countries. While it is very difficult to restructure debts due to a fragile banking sector. And as it is impossible to convince Germany and the ECB to reduce further real interest rates through quantitative rate cuts. The only lifeline available to states, the only path allowing them to invest in their economies and increase their money supply to boost inflation expectations – and thus promote growth – will be confiscated, or taken by force, available cash in bank accounts. Whatever the outcome, the Cypriot case in this regard is a clear signal of this paradigm shift induced by the dominance of neo-liberalism. Thus it is tripping over its own contradictions: it is indeed a flat rejection of printing money, it is also its stubbornness to establish rigor mainly for ideological reasons that are forcing states to take money from where it is, i.e., from the wealthy. At the very ones who are the most ardent supporters – even developers – of neo-liberalism!

## Is Financial Innovation a Curse?

This omnipotent finance achieved its absolute domination from computers which prevail today on stock market fluctuations, and therefore on the capitalization of our businesses. How else can one explain that large cap securities such as Société Générale or the Italian bank, Intesa Sanpaolo (and several other well-known institutions) can sell 15% in a single session? What is behind the collapse of Bank of America's shares by 20% in a single day? Or behind a Dow Jones index which can fluctuate by more than 400 points upward and then downward over the course of several days? They are in reality robots which, with the assistance of algorithms, issue buy and sell indications since 55% of the volumes dealt with today (as opposed to 20% in 2005) on all U.S. financial markets are the sole responsibility of machines! Everywhere, grey matter seems to have disappeared since everyone – banks, speculative funds and even pension funds – is now addicted to this “trading algorithm” which makes the Dow Jones lose 1,000 points in the space of a few minutes (the famous “flash crash” on May 6, 2010). The economist Heilbroner (1919-2005) maliciously said at the end of his life that mathematics had breathed stringency into economic science before killing it! These algorithms that control this “high frequency trading” further allow their instigators to reap huge profits daily. Or losses when the system catches a cold, such as Knights Capital losing \$440 million in 45 minutes in the summer of 2012! In reality, this algorithm trading enables its originator to intervene prosaically between a buyer and a seller to pocket a small margin... except that it is about a commission charged on thousands – even on millions – of transaction. It is the entire profession which must now recognize that it erred in its assessment of a highly complex system... that it did not always understand it! Indeed, these flagrant technological advances are exploited by the financial world precisely with the objective to go around – even breach – regulations. As John K. Galbraith (1908-2006) suggested, it is vital to gauge and dissect financial technology within a legal framework so as to understand the most complex instruments. This sophistication with financial tools is being knowingly developed by a financial sector concerned with evading the law. Let us well understand that, in the globalized financial world, fraud is not an anomaly: it is an integral part of the system, it is one of its undisputable components. Suffice it to say



that we need only look at the jargon being used in the mid-2000s to understand – thanks to vocabulary! – that the financial stakeholders knew perfectly well that they were distributing suspect and unsavory financial products. They were “neutron credits” intended to crumble without causing their downfall in the housing market. They were “ninja credits” whose poor beneficiaries had no income, no job or assets (No Income, No Job or Assets). They were “liars’ loans” since everyone knew that the person applying for credit had lied on his application... So many instruments directly led to the “subprime” disaster and showed that the financial world was perfectly aware of the explosive matter that it manipulated.

Will economic “science” one day have the same fate as anthropology and phrenology? In other words, will economic science ever become a fossil science, vaguely respected for what it will have brought but completely out of date? Leverage, derivatives, derivatives, also known as “exotic” products, options, knock-out, knock-in, one touch, futures, futures markets, securitizations... Must we destruct all these financial innovations? Should financial science be regarded with suspicion when it innovates? It is indeed impossible to tolerate more sophisticated – even decadent – financial products whose only objective is very often to enrich a certain class. Does it make sense to devote much public contempt to all financial inventions which bring marked improvement to our standard of living? After all, no one thinks to condemn the Internet, the basis of the collapse of the bubble of the technology stocks? Furthermore, had not the principle of a limited company and stock market capitalization been confronted with great distrust during the 19<sup>th</sup> Century by those who were persuaded that it would allow it would allow the emergence of entrepreneurs eager to shirk their obligations? Unlimited personal liability was in place at that era. Can you imagine today’s economic and business world functioning without limited liability companies and the stock markets? As well, excessive credit is certainly the origin of the property frenzy whose decay (since 2007 with the crumbling of sub-primes) led to today’s crisis, but did credit expansion systematically degenerate into a speculative bubble?

Instead, is it not from the moment when a security is converted into a security of securities and is cut into tranches to be resold to several stakeholders that from that point the banker believes himself invincible and that all hope begins to be vain? Indeed, all financial innovations do not apply: easy and traditional access to credit undeniably makes society advance when it is used to purchase one’s home or finance one’s studies. However, this same credit spent on refined products becomes disastrous if used for market speculation or to adopt irrational behavior and devoid of any economic justification. Thus, while finance can actually

make our world better whereby our huge middle class as well as the most needy can legitimately improve their standard of living, it can become a weapon of mass destruction when a few among us use it for unsavory purposes. Therefore, is this financial innovation or its specific applications, at the behest of greed and immorality of a business minority, which are harmful to the system and society? Sub-question: what is the overall balance sheet of the value of financial innovation on the real economy? If financial techniques only marginally benefit society during good times, its ability to harm is, however, disastrous when the train derails! It is therefore imperative that we – even – this world of finance which saw spectacular expansion and whose contribution to the GDP of our developed countries steadily climbed for 150 years. What, therefore, is really the added value of finance and how does it benefit economic productivity? Should we, after Paul Volcker, former Chairman of the Federal Reserve Bank and advisor to the Obama administration, assert that the only tangible asset of finance is the automatic distributor of bank bills?

The answer is still pending and doubts are allowed since yesterday's prosperity was the pretext for all sorts of predatory behavior on the part of individuals and entities that ruined the system, with the blessing of our politicians. So, it had been explained to us that profit should be the only horizon, that it was legitimate that this sole purpose – “worthy of respect” – underpin and feed our energy and thirst for success. It is clear today that this quest for profit destroys our lives and our planet. Worse yet, that it threaten our individual freedoms! The devotion of the Anglo-Saxon social model, having excessively boosted trade and consolidated all types of businesses into massive conglomerates, proved to be a failure for long-term growth and harmful to society. This philosophy turned us into psychotics (“sociopaths” in the words of Nassim Taleb), which vie with imagination to destroy value and – even more serious – values. This dogmatic eagerness to “laissez-faire” finally resulted in tyranny, when it was, however, so much healthier to have the largest number participate in leading business and businesses. The markets accelerated the advent of macro-management – that is to say, oligarchy – whereas only micro-management leads to stability and production of individuals. The academic world, that of business such as our economic authorities all depart from the principle that it is better to promote large organizations and banks when (and even if) they are known to have lost almost all sense of collective responsibility. In so doing, these cartels and concentrations of power, which instill foul air on all economic activity, slowly kills private initiative while compromising our individual rights. That is why it serves no purpose to believe today in the illusions of those who pretend to “reinvent” capitalism since – and it is Marx himself who recognized it – capitalism is always reinventing

*Capitalism without Conscience*

itself. Indeed, constantly changing, it is eternally in search of new artifices, new techniques and sophistication, sometimes extreme, with the single objective of optimizing its profits and satisfying the instinct of accumulation. Moreover, each stage of its metamorphosis throughout its history was systematically punctuated with corruption and outrageous exploitation.

## **The Moral of History or Immoral History?**

The name of protagonists, the signs of financial establishments as the dates are followed and certainly do not resemble each other. The story told, however, is always the same, punctuated by personal interests, greed, accidents on the financial markets described as “unpredictable”... so many episodes that marked the life of the past twenty-five years as “the more things change the more they stay the same”, as the Anglo-Saxons would say. A list – which does not claim to be exhaustive – of the scams and fraud of the world of finance and revealed only during a part of 2012 would indeed be eloquent. Let us begin with a case which lasted just as long as the Madoff scam, namely that committed by the owner of “Peregrine Financial Group”, who stole altogether the assets of his depositors. To build offices for \$18 million or to pay fines handed down by regulatory authorities... whereby only \$5 million remained in the accounts of his clients, which were supposed to amount to \$200 million! A scam comparable with the best of them, made public in the Fall 2011, called “MF Global”, except that it was some \$1,600 billion that went missing. Now let us talk about the illegitimate losses of \$9 billion deposited during this period of 2012 by a JP Morgan Chase trader nicknamed “London Whale”... Or the shocking example of one of the premier banking institutions in the world, HSBC, which had to disclose that it was a repeat offender of money laundering. Indeed, despite the steps taken in 2003 and 2007 by U.S. authorities, this bank continued its relationships with drug traffickers and businesses suspected of having links with terrorists. Until the U.S. Congress marked the end of the festivities in the summer of 2012. Let us not forget to mention also the program of spring of 2012 the scam by the credit card company Capital One, forced to reimburse \$210 million for having abusively distributed its products to U.S. consumers.

Let us round off this list by the mother of all manipulations, called the “Libor”. Indeed, threatened by legal proceedings by the both the Justice Departments in Great Britain and the U.S. for falsifying the reference interest rate called the “London Interbank Offered Rate”, Barclays Bank had to pay in July 2012 close to \$500 million to these two countries in settlement of this litigation. Despite this arrangement, let us make no mistake here, this wrongdoing is not just another act of embezzlement along the already very tortuous paths of finance. As one

of the most important rate indicators in the world, the Libor influences actually the interest rates of the majority of key currencies since almost all of the loans granted to businesses around the world is indexed to it. The (presumed) fraud focused on mortgages, credit card loans and other transactions agreed to in favor of businesses and private individuals for a total amount including between \$500,000 and \$800,00 billion! The amounts involved by this wrongdoing are astonishing since all credit agreed to – from mortgages to student loans or that granted to businesses through credit card overdraft – are more or less related to this Libor. Thus, according to the Federal Reserve Bank in Cleveland, more than half of the mortgages at variable rates in the U.S. are affected by Libor fluctuations. As well, and despite mass resignations of the highest level executives at Barclays, the scandal does not stop there since these manipulations were discovered at two levels. Barclays knowingly disclosed a wrong rate to its regulatory authority which itself used to borrow on the markets with dual first: first, to realize profits on derivatives and second, improve its public image by showing that it managed to borrow at attractive rates. In doing so, this bank – in cahoots with other satellite offices – masked the reality of its financial situation with its regulatory agencies, its clients and its creditors by posting falsely attractive rates on its own borrowings. The chain of manipulation of this interest rate would have infected some forty financial companies and more traditional businesses, dozens of traders, more or less involved at various levels in this new financial scam unmasked in the summer of 2012.

How do you continue to have confidence in a banking and financial system engulfed in so many scandals, scams and concealments? Bankers – who can only blame themselves for their total loss of credibility – are responsible for the entire capitalist financial system running a great risk which relies wholly on trust. Indeed, without this precious trust, the entire edifice will crumble, money in circulation (or “fiduciary” currency) loses all its value and all financial instruments will be auctioned off. How is it possible – and even less tolerated – that one of the key financial institutions for many years manipulated the most determining interest rate on financial markets? Indeed, without this precious trust, the entire edifice will crumble, money in circulation (or “fiduciary” currency) loses all its value and all financial instruments will be auctioned off. How is it possible – and even less tolerated – that one of the key financial institutions for many years manipulated the most determining interest rate on financial markets? How can we not be outraged by these three international banks – JP Morgan, Barclays and HSBC – having survived the tough crisis of 2008 by the grace of tax contributions, nonetheless persevere in their wrongdoings with the objective of taking more from this same citizen who uses their services? How can an

institution like Goldman Sachs justify using the most important leverage in all of its history in full turmoil in 2009? The year when, according to the Wall Street Journal, Wall Street salaries and bonuses reached amounts comparable to those of 2004 and 2005, i.e. at the height of the speculative bubble... In reality, those from the financial institutions who survived the 2007-2009 crisis are today even more powerful than prior to the collapse of the subprime bubble. Slight competition due to a certain number of banks which were absorbed or went bankrupt, but also to weakened states in debt – therefore the striking force lessened – are today transformed by a world of finance that it is very difficult to fight.

Another step – massive and which concerns us all – is, itself also, “likely from manipulation or distortion”, according to a recent G20 report, namely that of oil tariffs. At the height of the Libor scandal, it would seem that the integrity of companies is challenged within a context where the setting of their price depends (such as the Libor) voluntary declarations from a certain number of institutions, funds and traders who disclose the prices paid on their acquisitions. Oil tariffs – which are therefore the result or the weighting of the system based on trust – would themselves also be subjected to attempts of manipulation from operators seeking to make money from knowingly induced distortions. All in a market of thousands of billions of dollars and which very closely affects our daily life and our purchasing power. This financial universe has now become so imbued with its prerogatives and its power on our lives that it measures its success only in terms of profits. Persuaded actually that more it inflates its profits and more its public utility is comforted, it is mired in a before schizophrenic escape, whose only advantage is that it leads directly to self-destruction. That is why scandals and scams – even widen – five years after the setting off of the most acute financial crisis in a century. As such, trickery and deviant behavior are now so much part of normal life that no one is any longer surprised or outraged when another fraud is discovered. That is why advertising the Libor scandal – however major – only attracted a shrug from observers who had reason... A survey conducted in 2012 by a U.S. law firm, Labaton Sucharow, at 500 banks and financial companies in the U.S. and Great Britain, was amazing/astounding/staggering. As such, 24% of those in charge who were questioned admit the existence of fraud as a condition for success. As well, 70% of the people surveyed estimate that the regulatory authorities are totally incompetent. In other words, there would be several reasons for not committing fraud. The fear of “getting caught” would not, however, be sufficient reason for not lying or not stealing, since punishment is almost nonexistent.

However, this latest scandal with the Libor seems sadly familiar, as it has now become routine for financial establishments to try to manipulate rates or profit from unethical situations. Financial abuses have now become part of our morals. Indeed, honest bankers and financiers are no longer big enough to compete with their fraudster colleagues. So a bank which does not hide its losses, or sells rotten assets, or launders money, or influence the rate of a derivative or another instrument... would no longer be competitive and would eventually go bankrupt, or suffer a severe drop in its stock price. In real life as in nature, the Darwinian selection teaches us that on the strongest survive. In the financial universe – which unfortunately rubbed off on our daily lives –, it is the dishonest ones who remain, even prosper, while those who play by the rules are damned. This steamroller of scams and wrongdoings has a name, the “Gresham” dynamic, which was described by George Akerlof, born in 1940 and Nobel Prize Winner for Economics in 2001. “Dishonest dealings tend to drive honest dealings out of the market. The cost of dishonesty, therefore, lies not only in the amount by which the purchaser is cheated; the cost also must include the loss incurred from driving legitimate business out of existence”. This Gresham dynamic – dominant in today’s financial markets – there causes volatility in ethics for the benefit of fraud which is becoming more endemic. Those who respect the law and morality are therefore becoming scarce whereas their unscrupulous rivals remain thanks to the tricks and manipulations which compromise their costs, or inflate their profits. In other words, it is becoming “too expensive” to be honest these days.

Would justice – or rather the lack thereof – be on the verge of destabilizing the economic and financial system? Have you not noticed how managers of small businesses are relentlessly pursued – sometimes even harassed – while the criminal justice system struggles to find justifications and legal grounds, since it must deal with the case of “too big to fail”? This is, however, not the qualifications required by our lawyers, analysts and other experts that are lacking. The French Financial Markets Authority and specialists of the Monetary and Financial Code in France, like the “United States Attorney’s Office” in the U.S. have indeed often husked, unraveled and successfully investigated many complex cases when it is about crucifying the “small fry”. A certainty, an observation: we are not all equal in the eyes of the law, and public authorities do not treat us all alike. Enough to discourage future entrepreneurs and other small investors as a biased – even arbitrary – legal system fundamentally harm the economy. The cement of our society, equality before the law is nevertheless a prerequisite for a healthy and balanced economic and financial environment. Once the prison is reserved only for small fish and for those who, well, have “bad luck”, when the causal link between crime and punishment is broken or even

weakened, evil and vice are raised to the level of standards. Why be honest and why prescribe the rules of the game if the chances of being sidelined are dwindling? Is it not understandable – or simply human – that those who are tempted by crime take this route if the penalty is not always the appointment? With devastating consequences for those who prescribe to the law are clearly disadvantaged and weakened in an economy where fierce competition prevails. Is it any wonder that in such a context stakeholders and actors in the system gradually change their behavior because of the shift of the “risk-reward” ratio? Is this imbalance of justice not a boon for those who violate the rules are still yearning for moral justification? Society as a whole must therefore adapt to this new paradigm that teaches that it is “acceptable” to break the law. According to the same compelling logic, the “too big to fail” are considered “too big to jail” or too important to be jailed... Does this very disturbing constant that undermines confidence in the system not also demonstrate – hollow – that the protection of money and interests comes before the protection of citizens and society? Real exhortation launched towards institutions (financial and other) and from their directions to form cartels, manipulate share prices and prices, and defraud, in defiance of the stability of our economies. Even if this clemency is often invoked precisely on behalf of this economic and financial stability, as our leaders are haunted by the possible consequences that the bankruptcy of a bank could have, or the court appearance of a prominent (economic or political) individual. What good is it to obey the laws and regulations if only the weakest and least protected are tried? When crime is legitimized, it is the state that naturally loses all legitimacy. And it becomes impossible to reconstruct the financial system on the only basis that counts and on which it can prosper: trust.





## God's Work?

In fact, political leaders and regulatory authorities have given in to all the demands of the financial world regarding deregulation in all directions, under the pretext of establishing universal prosperity. Thus, the advisor to President Reagan and end analyst of his environment, Francis Fukuyama was surprised at the incestuous relationship between the largest financial institutions and partisan economists of efficient markets. He noted the collusion of this beautiful world with the world of power: "Wall Street seduced the economics profession not through overt corruption, but by aligning the incentives of economists with its own. It very easy for academic economists to moved from universities to central banks to hedge funds – a tightly knit world in which everyone shared the same views about the self-regulating and beneficial effects of open capital markets. It very easy for academic economists to moved from universities to central banks to hedge funds – a tightly knit world in which everyone shared the same views about the self-regulating and beneficial effects of open capital markets. The alliance was enormously profitable for everyone: The academics got big consulting fees, and Wall Street got legitimacy". It is therefore understandable that no one has stumbled upon the 1998 collapse of the funds of Long Term Capital Management ("LTCM"), the dress rehearsal for the 2007 subprime mortgages. A more important start-up in the world history of investment funds of up to \$1 trillion, does not LTCM count among its prestigious staff two future Nobel Economics Prize winners? The interconnection between an institution such as Goldman Sachs and two Treasury Secretaries (Robert Rubin and Henry Paulson) was only the final proof – indeed, anecdotal – but in addition to this policy which was nothing more than ex-financial growth, too content to render service at the slightest opportunity. The closeness between regulators, politicians and economists completed the compromise of a few for the benefit of finance which then occupied the public forum. Lobbying thousands of politicians by the financial world was no longer necessary since the eagerness for deregulation was unanimously shared between these two worlds. The policy officially attained the Stockholm Syndrome status: it was in love with finance which had gradually deprived it of most of its powers. With the essential firewall between politics and finance having been deliberately disabled, is it no wonder that certain blatant types of

deregulation directly led to these crises, such as compensation of rating agencies by banking establishments or the hiring by banks of former regulatory agency bureaucrats..., unless it was the reverse? The rest, like Mario Draghi and Mario Monti, respectively presidents of the European Central Bank and the Italian Council, are they not the products of Goldman Sachs where they held responsible positions? As noted, the “Sachs government” is in no way restricted in the Anglo-Saxon world. In summary, if it is true that collusion between governments and oligarchies is ongoing which leads to a systematic confiscation of profits and a sharing of losses, our democratic western nations borrowed from the banana republics and accommodated very well the systematic defense and preservation of certain private interests with public funds.

Strengthened by deposits amounting to approximately \$800 billion, Citibank reigned supreme and almost absolute before the crisis. Robert Rubin, the U.S. Treasury Secretary from 1995 to 1999, had stifled a bill from his own Democratic administration which was to divide and clearly distinguish commercial financial institutions from investment banks. Citibank could then proceed legally at a juncture to combine traditional commercial banking with massive speculation on Wall Street and global financial markets. In reality, this firm was not only one “too big to fail”, it was also a much too massive business to be sanely and rationally managed. Its size made it ungovernable and uncontrollable. In fact and from 2002, Citigroup was embroiled in all the financial scandals, from Enron to Worldcom through insider trading and other conflicts of interest involving some of its managers or analysts... so much so that it was also one of the financial institutions most affected by the subprime crisis since it only survived at the price of capital injections of hundreds of billions of dollars taken from the taxpayers of its country. Strange derives from a megabank whose management and board of directors were regularly adored by the press and their alter ego, since considered one of the most brilliant management teams in the financial world. Who could forget Chuck Prince, its arrogant chairman of the board who, however, was dismissed in 2007 due to monumental losses suffered by his establishment. Or the inevitable Robert Rubin, former Treasury Secretary, appointed member of the board of directors and executive director until shown the door in 2009, under pressure from critics and the quasi-collapse of his bank? Prominent figures who, interviewed by the committee of U.S. Congress charged with investigating the reasons for the subprime crisis, asserted, “like a great many others”, not having “anticipated the unprecedented collapse of the market” (according to Prince) despite structured products and systematic securitizations of toxic assets held in commercial quantities for their balance sheets. “C’est l’ensemble de la profession qui n’a pas perçu le potentiel négatif de cette crise”, as Robert Rubin would say to this

committee by completely ignoring his responsibilities *vis-à-vis* the staggering failures of this once top bank in the world that he co-managed. He, who was supposed to monitor risk management due to his leading position as president of Goldman Sachs which he held before becoming the U.S. Treasury Secretary...!

Goldman Sachs – iconic group among all –, which, in 2006, distributed subprime shares to its clients while it anticipated the debacle of the U.S. property market on which it speculated downward for its own equity. Goldman had understood all too well since, far from leaving itself open risk on one-directional bets like Lehman, Bear Stearns, Merrill Lynch or Citigroup –, this institution played with velvet gloves on and earned on both fronts. That of commissions on sales (for its clients) of putrid assets while making off with the placing on markets which gradually realized the excess in property valuations. Thus, while almost all the Wall Street institutions persisted in ignoring the warning signs of the subprime disaster, Goldman Sachs – inducted/crowned the most profitable institution in U.S. financial history – created and distributed CDOs (collateralized debt obligations), financial derivatives linked to real estate, to its main clients... while one of its most important managers (Paulson & Co) was betting on the collapse of these assets, and one of its executives (the Frenchman Fabrice Tourre) acknowledged in February 2007 in an e-mail to a friend that “the business of CDO had died”! Such are therefore the record profits recorded by the collapse of the subprime and the success of Lloyd Blankfein, Chairman of Goldman Sachs, who, having replaced Henry Paulson in 2006, himself called nominated to be Treasury Secretary by Bush, earned in 2007 – the year the U.S. property market collapsed – the largest bonus in the history of U.S. finance, i.e. \$70 million! According to Blankfein, interviewed by a London newspaper, Goldman performed more or less “God’s work”. In other words and in the words of Fabrice Tourre in the January 2007 e-mail: “The entire building is about to collapse at any moment now. Only potential survivor, the fabulous Fab, standing in the middle of all these complex transactions, highly leveraged, exotic, that it created without necessarily understanding all the implications of those monstrosities!”

From the megalomaniac boss of Goldman Sachs entrusted with a mission that he qualified as “divine” to the rest of the sprawling U.S. financial system which continually relied on its contribution to the enrichment of society, Wall Street had therefore definitely lost all sense of reality. The disclosed figures were from the rest vastly out of step with the daily life of the average citizen: \$26 million for the Blankfein’s apartment, \$2 billion, the estimated value of the Goldman Sachs headquarters in Manhattan or even \$550 million paid by this same institution in settlement of its litigation with the SEC (Securities and Exchange

Commission), the U.S. regulator. This number of zeros in a world where virtual reigns sucked the life out of the real economy without bringing the slightest added value to society in return. Who could curb or contain a world of finance in spectacular expansion and whose contribution to economic activity continued to gain in importance since roughly 150 years? Equivalent increases in salaries in the financial world, since they were within a range of 60 to 70% above the salaries of the average employee in the “real” economy. However, how did the dizzying growth of the finance profit from the long-term productivity and prosperity of the economy? Paul Volcker – always him – had wished that “someone would give (him) one shred of neutral evidence that financial innovation has led to economic growth”.

## **Who do the Rating Agencies Work for?**

In an ideal world where markets and prices are supposed to reflect all economic and financial data, countries that have lived beyond their means – the “cicadas” – are punished for their excesses. Therefore, markets hold themselves out as the grand moralizers depriving these countries of their ability, yet sovereign, to finance rates compatible with maintaining a stable economy. And for good reason: these markets or, as it is fashionable to say in refined language, “the investors” brew/brainstorm such amounts that a country, even large and important, could not overcome their guardianship and free themselves from tyranny. On the world scale, only a group of solid and determined nations would even dictate the new rules of the game which would free them from the yoke of this ogre (the market) whose only objective, whose only justification and whose sole *raison d’être* were to earn always more. Therefore, let us start with the postulate according to which important economic and financial countries would join forces to impose a new order. This alliance allowed them to regain their autonomy and establish stable growth in their region, because not related to the vagaries and whims of financial players. Two years of European crisis would have been enough to teach a basic citizen, not necessarily benefiting from economic training, how markets punish certain countries deemed frivolous. They always demand more and more compensation, in exchange for funding that they grant to these countries whose insolvency is ordered almost overnight. In this regard, rating agencies have happily participated in this system, when they have not thrown oil on fire by transforming the deficits of certain defenseless countries into psychodrama. However, it is not so much the debt of these nations than the soaring interest which they must pay on this debt which precipitated the debacle of these defenseless nations faced with sprawling markets. Let us remember in this regard that Greece’s debt was more than 105.8% of GDP in 2008 and that of a country such as Italy was 97.6% that same year, figures not so far from the 90% level considered as unacceptable by traditionalists (source: Eurostat). And let us compare these figures with Greece and Italy’s deficits which amount to 165.35 and 120.1%, respectively, at the end of 2011, due to punitive actions led by markets and their stooge, the rating agencies. Vigorous growth would have certainly been able to help decisively curb these deficits, but only how

do you restore stable and calm growth while escalating interest rates is pulling the entire economy down? What were the role and responsibilities of these rating agencies in the debacle?

The world financial slump was set off following the U.S. property crisis referred to as “subprime”, from 2007. This genuine rush toward U.S. property was in reality and basically a purely financial phenomenon, because mortgages before the Second World War were a rarely known instrument. Our grandparents were actually accustomed to paying cash for their property purchases, hence the small number of property owners (as compared with today) until the 1950s. Indeed, it is only the foundation for the U.S. (just before the Second World War) of agencies whose mission was to buy mortgages held by the local banks that the property sector gradually becoming more powerful until hitting its high note in 2000 and its disintegrating in 2007. And for good reason, since the creation of the Federal National Mortgage Association – the sadly famous “Fannie Mae” – allowed local and national financial institutions to be flooded with liquidities from the sale of their mortgages and in return offering other mortgages to prospective homebuyers... This purely financial arrangement contributed to the obvious and decisive expansion of the property market which made significant progress since 62% of Americans had become homeowners in 1960, in comparison with a figure of hardly 40% in 1940. This substantial expansion of this truly financial engineering exclusively dedicate to real estate was understandably linked to a need to distinguish solvent debtors from those who were more likely to default on debt repayments. Thus, the U.S. authorities naturally turned toward the three agencies which were active in rating bonds, namely, Moody’s, Standard and Poor and Fitch, already known at the time for the prestigious AAA or their feared BBB...

These rating agencies completely failed in their mission of rating these mortgage securitizations, which were from the outset coated with a favorable rating since backed because of the “stone”... This labeling which was practically risk free thus gave financial institutions carte blanche which gradually provided larger and larger sums to house mortgages by causing the bubble that we know today. This transfer of wealth and investments – U.S. and worldwide – into securities classified as risk free was interrupted by mid-2006 from the moment when, house prices reached dizzying heights, the market began to decline. Indeed, soaring default payments on these mortgages forced investors, banks and regulatory authorities to return to the reality of facts, that is to say to realize that favorable ratings given to these securities by the all-powerful agencies were in reality false... Hence the bubble burst and a financial system which was stuffed with real estate securitizations. U.S. authori-

ties, nonetheless, are also partially to blame since the U.S. regulator – the Securities and Exchange Commission or the SEC – had ruled, first, that banks did not have the right to purchase securities whose rating was lower than BBB and, second, that the rankings assigned to these securities had to be the responsibility of competent rating agencies known for this. In so doing, the SEC was duly promoting a true cartel which continues to serve today and which – even worse – is not obliged to disclose its methodology for calculating scores! Having actually intelligently pleaded its case by explaining to the authorities that its operational techniques must remain confidential to remain effective, this pressure group was thus able to navigate in murky waters with impunity where the lack of transparency was guaranteed by the law. Furthermore, and just like any cartel, which actively discourages any competition – that is to say any newcomer likely to cut/limit market share –, this rating mission proved to be the exclusive domain of a few companies already in place without, as is the obvious consequence, any corrective mechanism, questions asked or readjustment which could have been the result of a new company with new methods. Finally, not satisfied with reigning supreme in the world market, these agencies could also wallow at will in the clear conflict of interest was to be paid... by firms whose rates they ensured! How can the reliability and impartiality of points awarded to companies naturally driven to adopt all sorts of charming offensives to persuade these rating agencies of their financial health be accepted? So, did the three rating agencies not maintain Enron's rating almost to the resounding bitter end in 2001 of what also turned out to be one of the biggest stock market capitalizations in the U.S.? It is therefore the fiasco of these rating agencies was later to be the sources of the subprime crisis the perverse effects of which we are all still suffering today. However, these agencies – responsible for the second biggest crisis in world economic and financial history – have since this tragicomic episode paradoxically benefited from a rise in their power of influence since their rating of sovereign states are still religiously adhered to. If it is absolutely legitimate to be worried about the long-term consequences of public deficits, it would also be useful to wonder why any attention is still being paid to rating agencies. Initially created to play arbitrator – therefore to prove impartiality and neutrality – between the seller and the buyer of a security, these agencies have therefore failed miserably in serving the public, while appropriating considerable power over our standards of living.





## Neoliberalism and Alienation

The monetary system defined by Bretton Woods, relying on the value of key currencies to the green back and correlating that to gold, was abandoned in 1971-1972 by the U.S. which no longer had the means of defending this parity. It was ruled that currencies would be floated against one another, entirely subjected to the law of supply and demand, in other words, to market forces. A first gaping hole was thus opened, into which the then ardent supporters of the total freedom of financial flows were engulfed. The substantial increase in oil tariffs in 1973 further allowed petrodollars to be reinvested through financing which was launched in the invention of structured products allowing these funds to be channeled profitably toward western countries in full force. Very badly managed by central banks, the soaring oil prices infected the whole economy step by step which was suffering since the mid-1970s from unprecedented hyperinflation worldwide. Until President Carter asked Paul Volcker in 1979 to head up the Federal Reserve to engage in a historic and thankless fight against this hyperinflation. Certainly successful, but not without plunging the U.S. – and the world – economy into a recession in favor of interest rates having attained 20% in 1980! This hyperinflation and rising unemployment since the mid-1970s were a bargain for the monetarists – promoters and ultra-promoters of frenzied liberalism – whose leader and most iconic spokesperson was Milton Friedman.

This deadly combination of unemployment and hyperinflation was actually the ideal pretext for Friedman and his acolytes who squarely blamed lax monetary policy and fiscal and budgetary indiscipline at the time. According to them, the inflation was entirely due to the expansion of money supply by central banks. However, they considered that the supply of cash in circulation had produced another harmful effect, as harmful as hyperinflation. Friedman actually accused the creation of money for bloating the state and forcing, mechanically, the private sector to reduce its investments. As they start from the principle that too much state intervention kills private initiative, the monetarists therefore exerted considerable pressure to make governments drastically restrict their spending. The advent of Margaret Thatcher in Great Britain and Ronald Reagan in the U.S. further provided these supporters of “ultraliberalism” with the perfect opportunity to implement their theory,

which was gladly and diligently undertaken by the U.K. and U.S. governments. The advent of Margaret Thatcher in Great Britain and Ronald Reagan in the U.S. further provided these supporters of “ultraliberalism” with the perfect opportunity to implement their theory, which was gladly and diligently undertaken by the U.K. and U.S. governments. “Government is not the solution to our problem. Government IS the problem”, Ronald Reagan resolutely declared during his inauguration on January 20, 1981. From that period, economic conservatism and social regression were thus to reign supreme. How can we forget the devastating effect (on the U.S. economy) of the Reagan years, which embarked on a policy scrupulously used to reduce labor’s share in the national revenue (from 21.5% in 1980 to 12% in 2005), in order to increase that of the financial services’ (from 15% in 1980 to 22% in 2005)? The void left by the state was very naturally filled by hyperbolic expansion of the financial sector said to be efficient, even “perfect”. This finance was actually called on to provide all services to the economy with the result being the birth of financial markets! This finance was actually called on to provide all services to the economy with the result being the birth of financial markets! Of course, these already existed before the mid-1970s but only really caught on when a miraculous virtue discovered them, i.e. generating immense profit, therefore revenue and potentially jobs. The conditions linked to this growth and prosperity meant that the players had to assume a certain level of risk and the markets deregulated.

The all-knowingness/omniscience of the markets would optimally explore available resources. Markets would act like a justice of the peace who would restore order to business and household finances by imprinting all sectors of the economy with its benevolent efficiency. From that moment on, financial markets underwent a genuine transfiguration: they became “ideal” financial markets. The constant and democratized flow of information breathed efficiency into the markets in the sense where their prices reflected at any given moment the state of health of business, and therefore the economy. The admirers of the financial market were even persuade that its prices were the result of rational balance and that employment was in fact only a variable in the optimization of stock market valuations. It is from this period that the notion of the “disposable” worker or employee – which certainly goes back to the end of the 19<sup>th</sup> Century – was formally acknowledged, and publicly assumed by the leaders of this ideal market. And for good reason: any superfluous consideration and any kind of mind/spirit/soul searching should give way to markets which showed the price – and therefore the financial situation – of all the players. Everything had and must have a price, including man. As Eugène Fama said, born in 1939 and one of the founding fathers of this theory: “I take the market efficiency hypothesis to be the simple statement that security prices fully

reflect all available information”. “Simple” affirmation, accessible to all and easy to integrate, hence the appearance, among other things, of jobs where trading, selling and buying sufficed. This famous “efficiency” was not, however, quantifiable and was not either a verifiable fact through market research. All the same, this theory sparked general enthusiasm when it concluded that the benefits and risks involved would end up merged into one price for such asset at any given moment. What is the information available to investors and how is it reflected in the financial markets, are questions that Friedman, Fama and the others seem not to have dug up. Their postulate was too tempting after all: it implied that all economic agents behaved rationally and, particularly, it defined a universal standard – pricing – from which everything could be planned. It became possible to anticipate future fluctuations and the door opened to complex financial products which would be designed according to all possible and imaginable variations of pricing. But in particular (and this is what interests us from the point of view of the financial crisis which commenced in 2007), this model would identify and define all risks, even control them and curb them with instruments such as options. This all-powerful heady sentiment – according to which nothing very bad could happen and that, definitively, all risk-taking would be compensated – was global and was to prevail even with central bankers, the ultimate guardians of the temple... Nothing seemed likely to get in the way of infinite growth and uninterrupted appreciation of financial markets. Finally, the only risk was not daring to take risks!

In fact, let us remind ourselves of this period not so long gone where almost all the analysts, investors and traders fussed about “reducing risks to the global economy”, in defiance of Cassandras who showed mistrust and who recommended prudence *vis-à-vis* general market, financial and economic euphoria. This overwhelming majority claimed therefore that world imbalances were only the natural result of indulgent globalization. Only a minority – reduced to silence – fearing that the U.S., which was already experiencing difficulty in attracting sufficient capital to pay their deficits during this blessed period, found itself in an inextricable situation during this slowdown and perhaps might have been reduced to sell whole sectors of their economy to survive! The theorists of globalization debated to assess whether this widespread decline in macro-economic volatility was adequately reflected in stock markets. Actually, in a situation where the previous bubble of technological securities had been rapidly overcome, where the catastrophe of astronomical U.S. deficits predicted several times by the bad omens had never materialized and where ever increasing oil prices could not have interfered with the U.S. economy, the stock markets seemed still and always under-valued... What risk could there possibly be to borrow more to make capital more and more profitable? The use of leverage

was widespread, thus affecting the overall investment climate since the smallest investor was from now being financed in currencies at law interest rate (as the Japanese Yen or the Swiss Franc) to invest several times the amount borrowed in instruments with high returns. What is more natural than controlled volatility? Leaving cash sitting in an account meant at that time sacrilege: has financial history not been systematically written by and for winners?

The deregulation of our economies and money obviously comes directly from this assumption of the efficient market. No longer any need for regulation or safeguards if the market is efficient, therefore optimal. Useless to restrain an animal which is self-regulated by pricing, which eliminates the weakest – those who made bad decisions – and which makes the strongest win. Therefore, it is a genuine natural selection on which omniscient and infallible financial markets function. As self-regulation unfurls its beneficial effects on to the economy, the task of the state was therefore to be reduced to its simplest expression, as for example to try this and that to lower the “natural” level of unemployment. As such, the state was asked to withdraw its economic and financial regulatory authorities and only to punish the extreme cases. Therefore, it is Friedman and his consorts to whom we owe the succession of financial crises and earthquakes, since the 1987 stock market crash in 1987 to the 2007 subprime crisis by way of the Dot Com Tech Burst in 2000. Indeed it was impossible – even against nature – to have so-called regulations co-exist with efficient markets. In this best of worlds, embezzlement and fraud were impossible. Indeed, as the markets could not be efficient in the face of fraud, dishonest acts could no longer exist since the markets were precisely efficient. In this best of worlds, embezzlement and fraud were impossible. Indeed, as the markets could not be efficient in the face of fraud, dishonest acts could no longer exist since the markets were precisely efficient. This spurious circular argument was widespread among all the stakeholders, which is to say, among bankers and economists, of course, but also well entrenched with regulators and central bankers. The all-powerful president of the U.S. Federal Reserve for almost twenty years, Alan Greenspan thus declined to investigate presumed embezzlements regarding derivatives, or notorious abuses of mortgage loans on which colleagues or consumer defenders asked him to conduct. He sought refuge behind the dogma of efficient markets which could not, in all “logic”, tolerate suspicious behavior. U.S. justice itself is today exasperated with the attitude of financiers. “The perception is that no one takes white collar crime seriously” is one of the symptoms of this annoyance, declared U.S. federal judge Emmet Sullivan in the summer of 2012. Indeed, he deplored that senior banking executives on trial “come to trial, plead guilty and are sent home to watch their favorite programs”... He is not the only judge at this level to

make this bitter finding. We may remember another federal judge, Jed Rakoff, who in November 2011 had rejected a settlement of \$285 million reached between Citigroup – accused of selling its clients derivatives and “toxic” mortgages – and the U.S. regulator, the Securities and Exchange Commission (SEC). By demanding that a proper trial be held, Rakoff refused such a “deal” on the run and away from courtrooms. Is it not, however the SEC itself which made this decision, keen – it would seem – to protect the top U.S. bank? These secret agreements and other “guilty pleas” in high finance perhaps give the illusion that justice is served. They are only *carte blanche* granted to a world which remains persuaded that everything can be bought. Conviction which, of the rest, is not contradicted by justice.



## **The Respect of Uncertainty**

The fact remains that the economic recovery during the second half of the 1980s allowed monetarists and uber followers of liberalism to scream triumphantly of their theories by putting more pressure on the governments of the day, which let themselves very easily be convinced to free capital from the suffocating grip of the state. Friedman was quick to conclude that episodes of hyperinflation and high unemployment which prevailed in the 1970s were entirely to be blamed on the failure of state governance which therefore had to give way to markets. Only markets could, according to him, breathe stability into an economy which was affected by misplaced government decisions. Always avant-gardes, the U.S. and Great Britain championed financial deregulation and the retreat of state influence, supposed keys to a prosperity which it imposed everywhere. The zenith was reached under President Clinton, who even went on to declare in his 1995 State of the Union Address that “the era of big government is finished”! Since then, the all-powerful U.S. showed itself to be dominated by its financial markets. It goes without saying that the loss of state influence was accompanied by a necessary decrease in its spheres of activity, and therefore public budgets which had to be substantially revised downward. Such was the requirement of a finance sector which demanded sobriety and discipline from states while it feasted under the weight of mass profit generated with the hyperbolic expansion of “financial engineering”. The European Union caught up with this bandwagon since the beginning of the 1990s with the Maastricht Treaty, which dictated to its members to maintain their budgetary deficits under 3% of their DGP and their public debt below 60%. Similarly for the former Iron Curtain countries to which one was to teach the virtues of the new financial orthodoxy whose admitted objective was to establish a single neo-liberal model worldwide. To reign, globalization had to standardize everything in its path. The new priority was to implant liberally accessible markets everywhere, subject to state intervention severely restricted to the definition of their interest rates whose single objective was to control inflation. In fact, the role of the central banker would be summed as increasing rates if inflation exceeded the threshold of tolerance and vice versa. There is no mention of fighting unemployment, improving working conditions or eradicating poverty. On the contrary, this period was one of spectacular regression



of the social state from which the means of its solidarity were removed. It is true that its ultraliberal restructuring yielded revenue by way of privatizations.

It was impossible in such blur to control cross-border or cross-continental capital flow which no one wanted to harness or even assess. Liberalism had therefore enshrined globalization characterized by the free reign of financial markets – that is to say pricing – since everything was then given a value. Tsunamis of investments and liquidities thus flooded economies – even the most reclusive in the world – so much so that expansion, modernization and even the most basic needs of certain countries were assured by private capital, nothing altruistic since it was their profit in sight. It is globalization that China, Latin America – in short, those that are referred to by the generic name BRICS and which could include all emerging countries – owe the growth of their exports and their financial surpluses and reserves. Everywhere where globalization passed, nonetheless it required healthy public accounts, a condition sine qua non to its investment and its provision of funding, even if none of its experts wanted to explain why and in what it was economically required to maintain its public finances balanced at all times. Indeed it has been more than thirty-five years that states have been required to curb their public deficits for no other reason than the economists and experts recommend it, even if they cannot explain these requirements! Still, to abdicate the essential of their financial powers in favor of a sprawling and sophisticated corporation, our states, unfortunately, no longer have the same powers over the economy. Deregulation, globalization and financierization have not always so far – and despite five years of crisis – surrendered, knowing that the context can be found now weakened to breaking point by the absolutely huge imbalances between a small group of exporting countries and a massive group of importers-consumers-debtors... Globalization – created in the West – has therefore devoured its parents since it is practiced – and prospers – on the bed of massive deficits in the U.S. and Europe (except of course in Germany). This regression of the state characterized by abandoning the disenfranchised classes only made the inequalities wider. The tiny wealthy minority enriched itself more while exploiting the middle class along the way – those dependent on only their salary – and who suffered stagnation or a decrease in their real income. Therefore, what is the intangible economic law that dictates unequivocally that a state must spend less than 3% of its GDP and that its debts must always be under 60% of its GDP? This dogma of 3%, which now dictates European economic choices, is, however, only a fanciful invention of Guy Abeille, a French official in the Ministry of Budget. Which today recognizes that “3% (were) invented an hour one evening in June 1981, on a table corner, and not based on any economic theory”. For its inventor, this “round” figure also made

you think about the “Trinity”. In this same vein, the ESM (European Stability Mechanism) explicitly states that the states will have to be financed only by the financial markets and thus be exposed more to speculation and financial risks. This mechanism represents an extra gear to austerity with the consequence of relinquishing the democratic control of the European Parliament or national states. The unstated goal is to dismantle the welfare states and conduct internal devaluations which substitute usefully currency devaluations. Whereas, in reality, only economic activity, growth and salaries count, and it does not matter – not at all – that money comes from public funds or private investments.

The liquefaction of fall 2008 is therefore the poison gift of financial innovation. By making markets more liquid in favor of volumes increasingly more pharaonically traded, globalization led to financialization and securitization having attracted more and more institutions, businesses and the private sector which invested without relying on financial markets. As almost all these liquidities in circulation were invested and less and less money remained uninvested, markets become more volatile in favor of stakeholders who bought and sold very frequently. The so-called “real” economy – narrowly dependent on markets – was naturally affected – and infected – by their inherent stability through the driving belts of scholarships and bank loans. Even more serious for economic activity which was gradually considered as an “investment” exactly like another, which ended up upsetting traditional economic cycles. This radical shift in the economic paradigm generated by massive cash flows – ready to be invested but also all the more ready to be divested – was obviously transformed by the fall into disuse of whole sectors of the economy or investment was only profitable in the long-term (as the industrial sector) and the emergence of sectors of economic activity (finance and speculation) where the returns on investments were realized in the short-term. Under the complacent watch of central banks which, loyal to their adherence to monetarist theories, consecrated a reference instrument – interest rate – as the supreme regulator of the markets and the economy. In fact, deregulation had left them with only this leverage which they used, nonetheless, in all directions – and downward – with the one and only objective being to fight inflation, the sworn enemy of Friedman & Co. The manipulation of leveraging interest rates therefore conditioned investments directed to the real economy. In fact, deregulation had left them with only this leverage which they used, nonetheless, in all directions – and downward – with the one and only objective being to fight inflation, the sworn enemy of Friedman & Co. The manipulation of leveraging interest rates therefore conditioned investments directed to the real economy. Indeed, when interest rates were low, it was worth taking on some exposure to invest in the economy, but these funds were quickly extracted when compensation offered

by interest rates proved juicier. Certainly, we know since Keynes that the volume of investments in the economy is a function of the interest rate in effect. Central banks have played it nevertheless so – under the guise of fighting dynamically against inflation – that permanent instability reigned among the economic players. During the only decade from 2001 to 2010, the U.S. Federal Reserve thus reduced its rates from 6% in January 2001 to 1% in June 2003 to raise them to 5.25% in June 2006 and bring them down to absolutely zero since December 2008!

In acting in this way, central banks only gave investors reason a posteriori to favor a very short-term horizon. By raising or lowering their rates substantially in so little time and by displaying an extreme reactivity to any inflationary threat, they donned the clothes of speculators who were recognized in them. And have somehow endorsed their actions. How can businesses keep employees under such conditions marked by a volatility in the capital flows available to them when it is impossible to plan calmly in the medium- and long-term? It is therefore uncertainty which undermines the workplace and which makes it hesitant to do any large scale hiring because it cannot permanently rely on the capital available to it. That is why, if the theory of self-regulating markets is good for investors, it is, on the other hand, a curse for unstable economies and for employees who live on tender hooks in fear of losing their jobs at any given moment. Of the rest, if markets really had the ability to self-regulate, the effects could have only been beneficial to the real economy which would have been smoothed by markets always at their best. Unfortunately for financial markets – and particularly for our economies – uncertainty causes financial crisis. The slowdown of investments in favor of the economy and market volatility is effectively incompatible with a weak forecast of the future, such as defended by the monetarists.

In other words, this uncertainty which is impossible to control or quantify imposes on those whose job is to take risks surrounded by all precautions and all preventions so as to not be swallowed up in the whirlpool of inherent volatility comprising the full range of investments, from personal loans to derivatives. As it is obviously impossible to predict future crises, good governance likely to be dictated by the regulator must naturally tend toward transparency, exhaustive evaluation and strict monitoring of risk. However, how do you convince the supporters of the efficient market that risks are not always reflected in the price? And that operators only have access to fragmented and incomplete pieces of information on which they base their decision-making? And that external shocks regularly affect market price? In reality, only the advent of crises inflicts such lessons on investors and speculator while making a good number disappear in passing. That we did not listen to

Keynes – who more than half a century ago – indicated that “our knowledge of the future is fluctuating, vague and uncertain”! How do we defend the monetarist argument according to which it is easy to make “rational” predictions concerning changing markets when the scientists themselves would like to predict a volcanic eruption or an earthquake? Nassim Taleb does not tell us anything new with his judicious allegory of the black swan. Markets are not right, they are not transcendent and history tells us that it is littered with failures, losses, erratic movements, with all the side effects that we know about in our daily lives. How can theories about perfect and omniscient markets claim, as they do, to have a constructive impact on the economy if they exclude all reliable prediction? Keynes had had this famous saying: “there is no scientific basis on which to form any calculable probability whatever. We simply do not know”. It is his famous “we simply do not know”, a real call to be more modest than aficionados – to the admirers, should we say – of the divinity of “markets”.

Let us compare these sayings with the certainties of an economist like Burton Malkiel, born in 1932 and educated at Princeton and Harvard, who assures that “True value (of the markets) will win in the end” since the stock market is, always according to him, a “long run weighing mechanism”. Let us therefore be comforted since stock market valuations are expected to achieve a balance even allow our businesses to generate profits. And too bad if we have to experience strong turbulent periods: in any event it is what is implicitly admitted in this “long-term”, indicating the hollow existence of short-term ups and downs which would severely affect the real economy, which is asked to bear its troubles patiently until markets arrive at ultimate wisdom. Keynes was ironically saying that: “on the long run, we will be all dead”... Must we thus be resigned to support and suffer training and especially the collapse of these bubbles that generate crises, financial desolation and panic while waiting for some kind of messianic balance of markets? Since, according to economists like Malkiel, crashes would only be setbacks which gradually forge this final stage of balance. Except for these episodes, indeed regrettable but also necessary like childhood diseases such as measles or mumps, information available to agents – complete and correct – would allow them to make adequate decisions at any time for market harmony and the proper functioning of the economy. In doing so, these theorists of “rational decisions” characterizing the life of markets miss the fundamental psychological component which affects any investment process, such as trust and reliability that stakeholders consider when making their decisions. Trust being a highly volatile and unstable concept.



## **Economic Science or Economic Subjectivity?**

Investors have complete confidence in their decisions and in markets when the boom of real estate and stock assessments continues. Apprehension even from risk is clearly modified. Operators multiply actually speculative investments, even quite frankly dubious, since their level of optimism is pumped up and their suspicion anesthetized by euphoria. They even begin to buy securities and carry out all types of investments thanks to contracted borrowing which logically lead to an acceleration and intensification of the “boom”. It is the blessed era of profit for the entire chain of stakeholders. And with good reason, since the markets are only practically appreciating, knowing that any slide is considered a “correction” from which one should benefit by charging higher prices. However, the pinnacle is only attained when certain stakeholders buy conscientiously very risky assets – putrid – by focusing on the fact that the virtuous action of markets will assist in “normalizing” them, that is to say transforming them into so-called assets, while allowing them to cash in in the meantime a handsome added-value. In short, optimism and confidence reign supreme, so much so that investors, even the most reluctant and the least the least likely for losses, end up having their cake and eating it. Cash starts to flow freely, cash increases endogenously/internally since each purchased asset is resold with a profit: it is the characteristic of a bubble. This period is further marked by relatively low interest rates and by easy credit, fueling exactly all this reckless risk-taking. This almost uninterrupted soaring valuations and markets lead to a feeling of intoxicating wealth among the stakeholders since their portfolios and accounts reflect potentially very substantial profits. Hence there tolerance to increasingly heightened risk, itself comforted by an almost invulnerable feeling afforded by sham profits. Was it not Minsky who was the first to elaborate a theory according to which stable markets and economic and financial conditions would be the source itself of instability! Exactly as described, speculators and investors in the financial markets indeed take much more risks than the context in which their bets are made is calm. In other words, the collapse of the macroeconomic volatility encourages risk-taking, knowing that the fall will be harder! Excessive ambient widespread deregulation and laxity like

relaxation exert adverse effects in an environment where the protections and guardrails fall one after the other and while bubbles form and speculation grows. Hence Minsky's famous understandable conclusion that stability is itself generating instability. Even worse because more the numbing context of stability will have lasted longer and more violent the subsequent stall will be. Dilemma – or headache – for economic and financial leaders as for central banks because these repetitive sequences of “boom and bust”, ie bubbles and collapse of these bubbles, greatly affect the economic fundamentals. This is what Minsky called the smoothing action of the state which, through its budget deficits, is able to neutralize these upheavals by compensating for the interruption of private investment. This is actually a fundamental psychological component. Operators and stakeholders are pumped up by instilled confidence in favor of stable and flourishing conditions which, together with their lure for profit, always lead ultimately to a crisis situation and erratic volatility. Safety measures implemented yesterday and today in a nuclear station and having avoided until now a catastrophe are not absolute guarantees against an accident tomorrow... it must be acknowledged that a boom or a bubble is in reality a spiral which feeds itself: like a tornado sucking up everything in its way since comprised of loans taken out and granted with the single objective being speculation, a drastic increase in leveraging, inexistent risk management, a virtual increase in purchasing power and euphoric stock market appreciations for all stakeholders, including financial establishments which lend amounts intended to inflate the bubble further...

The interconnection between financial markets and the real economy has become such that economic activity, investment, growth, consumption and hiring improve and advance when optimism reigns in the stock markets. The dependence of the economy on finance makes it benefit from cash flow and constantly increasing profit margins when stock market valuations are on the upward trend. It is easy: this boom seems to start a new era which is, nevertheless, only a headlong rush, since the economy must be “financially fragile” to borrow from Minsky. However, a tiny pebble can – at a fateful moment – seize up the machine. Indeed, a wave of cash shortage appears due to a spontaneous freeze on credit or profits which become more complicated to rake in. Suddenly, investment is increasingly scarce, income falls, corporate profits are feeling the pinch, stock markets drop, and agents punctuating the whole food chain suddenly discover that their predictions were too optimistic... and therefore their positions were too high risk. As stock market valuations had been aligned with levels completely disconnected from the reality of economic data and the health of corporations, forecasts are reviewed downward and stock market adjustments begin to occur. Thus banks stop lending out of fear of default on payments at any time where

interest rates rise and an inverse spiral starts to feed itself with forced liquidation of their positions on behalf of those who speculated with credit. Thus, sales accelerate while under pressure from those who can no longer hold for having abused important leverage and markets collapse altogether under the weight of good securities which were themselves also “balanced” by those which now cannot be liquidated. The credit crush is thus implemented since banks no longer lend at all, not even to one another.

Financial crises and, even more serious, economic instability, are owed entirely to the Friedman school of thought, which concocted a theory on totally absurd assumptions. In view of regulatory agencies having done even less homework almost all the economists welcomed enthusiastically this theory of perfect markets. This notion of risk, presumably always quantifiable and therefore possible to identify, replaced the uncertainty cherished by Keynes. Suddenly, financial institutions could take more risks, with the approval of their regulatory authorities. Gradually, the system became so complex, financialization so sophisticate, banks so entangled, never ending sprawling institutions and regulators so overwhelmed by the events that it became completely impossible at the dawn of the 2000s to assess – even if only briefly – the overall risk incurred. In fact, certain financial products had reached such a degree of complexity (such as collateralized debt obligations or mortgage-backed securities, respectively insurance against default payments of a debtor or a real estate securitization) that it was outright impossible to deal with them – therefore to buy and sell them – on a regulated market. As the process consisting of attributing a price to them was incredibly opaque, these products were negotiated between a buyer and a seller at a mutually agreeable fixed price. This negotiation, called “over the counter”, benefited from a steep rise since its volume leapt from a total of \$157 billion in 2004 to half a trillion dollars in 2006 and 2007, according to the Securities Industry and Financial Markets Association! It goes without saying that the total lack of transparency was good news for banks which could freely multiply their profits thanks to dealing in OTC (over the counter) products and therefore outside regulatory control, even limiting, profit margins. So finance pushed logic so far from efficient and optimal markets that It even saw fit to do without it... Whatever the situation, the temptation was strong among bankers to concoct highly complex products – always more complex – with the single objective of avoiding all control from obsolete and benign authorities. A Financial Times article in September 2010 quoted a U.S. government authority who had disclosed that only two “over the counter” transactions had created the panic in the markets on a fateful day in 2008!



Acknowledging the shameful and inadmissible fact that the main regulatory agencies lacked the technical and intellectual ability to comprehend the inherent risks of the portfolios of the largest banks, the Bank for International Settlements suggested in 1998 that they delegate these responsibilities... to banks themselves, more capable, according to the BIS, of managing their own exposure! Banks were therefore authorized to evaluate and reevaluate independently their risks, which in other words meant leaving them to determine themselves their own capital quotas which must counterbalance these exposures. Unsurprisingly, they conducted logically an assessment a minimizing of their risks – what is more – by using very recent historical data with the objective of predicting future performance. How can we not be shocked by such a lack of lucidity – and honesty – from these banks which calculated their risk based on statistics often dating less than a year knowing that, furthermore, the last analyzed period was that of regular appreciation of the markets? No adverse or negative weighting was effectively introduced in their risk management since banks were not concerned with taking into consideration troubling episodes in the life of markets... This technique of evaluating banking risks was therefore based on the principle that the risk of default was confined at all times, that volatility would remain relatively low, that interest rates would be favorable... in short, that the term “crisis” had simply disappeared from the vocabulary. All was therefore for the best in the best of worlds for these financial establishments which delivered their very lucrative “business as usual” under the lax watch of the regulator. The temptation was therefore immense to step up the leveraging used and to commit to all types of loans in favor of all debtors in all sectors. After all, the models backed by general management identified the maximum risk incurred and, furthermore, the bonuses were there to encourage profits.

Economic science therefore required absolute surrender of prudence, weighting and decency – in short, morality – as the price for ensuring economic growth. The multiplication of productivity and growth and rise in purchasing power could not actually be deployed without a decline in traditional morality. The “Love one another” and the “no coercion in religion” have been abandoned in favor of the golden goose which is finance and to the cult of stock markets. Ancient religions were replaced by the efficiencies of the market whose dogma teaches that everything has a fair price. The invasion of this finance, which gradually came to occupy public and private spaces, turned us into zombies. Because we are only concerned, even obsessed, with arbitration – and the verdict – of the markets. Since financial innovation, derivatives and securitizations shot and killed prudential rules, by enshrining the advent and domination of securities. Ancestral morality effectively ceased to reign when risk disappeared. To commit a mortal sin once ran the risk of

rushing into hell. Today, all risk is likely to be controlled, “hedged”: mathematics taught us to manage risk which reduces the degree of simple technical consideration. By abolishing uncertainty, modern finance killed morality.



## **Keynesian Humility or Neoliberal Arrogance?**

The essence of the capitalist engine is uncertainty which translates into success for some, economic disappearance for others and more or less violent crises. It is therefore absolutely unthinkable to adhere to theories of perfect markets where information is efficient. The myth of self-regulation, which had once marginalized the state, was destroyed by the crisis which began in 2007 and has just been buried by European setbacks. Instability is the very heart of the world of finance: we suffer the brunt of it since 2007 and had been successively warned by Marx, Keynes and Minsky. Let us therefore return to reality and integrate uncertainty within our economic decision-making process and financial investment. Let us once again become modest and realistic and reduce our claims. Since the immense work and accomplishment of Keynes can be summed up in a single word – doubt –, as the monetarists and neoliberals are likened to their certainties which stick to them like glue. That it is healthy to have doubts! Doubt is the key underlying idea on which Keynes based all his theories. Doubt also leads to managing its risks or accepting measured losses, as it restrains the disproportionate bait of gain. The key doubt to all the most essential questions, and it is a survival instinct as a lesson in modesty, in both economic life and from the point of view of morality and intellectual honesty. Let us therefore learn again to respect and fear uncertainty which is an integral part of our daily lives. It is only having started arrogantly from his doubts that man multiplied acts with serious consequences.

Experts in economic science must therefore profoundly question their certainties again in light of today's collapse since they are woefully misguided. One thing is for certain: it is essential, in these almost unprecedented turbulent times to return simplicity to economics, since the resolution to the crisis lies in basic, even elementary, remedies. Just as, in the reverse, it is the sophistication of financial instruments and neo-conservative fallacious reasoning which deliberately made the situation worse. Macro-economic considerations (employment, income and production, the role of the state) must therefore take precedence over micro-economic data where actors are decked out with the "rational" qualifier and where the market is likely to calmly balance supply and

demand by using key straightforward mathematical models. During periods of financial and economic crises and in the face of such imbalances, microeconomics – which cannot stabilize activity – must cede to the forces of macroeconomics. What, of the rest, must even be admitted by a monetarist of the caliber of Friedrich Hayek (1899-1992) and Nobel Economics Laureate in 1974), who himself recognized in 1966 “the domination of macroeconomics and the temporary decline of microeconomics”. During periods of financial and economic crises and in the face of such imbalances, microeconomics – which cannot stabilize activity – must cede to the forces of macroeconomics. What, of the rest, must even be admitted by a monetarist of the caliber of Friedrich Hayek (1899-1992) and Nobel Economics Laureate in 1974), who himself recognized in 1966 “the domination of macroeconomics and the temporary decline of microeconomics”. Or by Friedman in person who, in a letter to Time Magazine in February 1966, resignedly asserted: “In one sense we are all Keynesians now; in another, nobody any longer is a Keynesian...”, meaning by that that, if Keynesian theories face a wall when they should integrate microeconomic factors, they are systematically called to the rescue in times of crisis. It is within this same optic that Friedman was to declare in 1997 about the Japanese crisis: “The Bank of Japan can buy government bonds on the open market, paying for them with either currency or deposits at the Bank of Japan, what economists call high-powered money. There is no limit to the extent to which the Bank of Japan can increase the money supply if it wishes to do so. Higher monetary growth will have the same effect as always. After a year or so, the economy will expand more rapidly; output will grow, and after another delay, inflation will increase moderately. A return to the conditions of the late 1980s would rejuvenate Japan and help shore up the rest of Asia”. Today, Friedman’s prescriptions for remedying Europe’s woes would be identical, if he were still alive... Still, Keynesian theories and their enthusiasts were sent to their laboratories in favor of the good times of the previous decades for not being able to integrate the dogma of the perfect market and for doubting the rationality of economic agents. In doing so, the “neo-cons” strived to make the state obsolete. However, salvation could only be assured today by the intervention of this same state. While it had been ironically asked not to inhibit self-correcting market forces, it is finally realized that only its action can rebalance the macroeconomic indices during recession.

Since it is macroeconomics which teaches us the fundamental operation of debt in rebooting economic activity. In other words, it is macroeconomics itself which shows that the effects of public spending, investment by the state and tax reductions are more dramatic episodes where consumption and producing are on the decline. It is also during times of crisis that the increase in public spending is the least harmful effect on

deficits. Despite virulent criticisms from orthodox economists who ridicule Keynesian principles while accusing them of favoring lax behaviors, even irresponsible, it is now evident that the solution to the crisis will be by intervention on the part of the state, a precondition to restoring investment. Keynesianism is not about spending, recklessness or some kind of encouragement of “grasshopper” behavior. In this regard, the neoclassical safeguards *vis-à-vis* the worsening of public deficits are outdated to totally silence the automatic – mechanical – reductions in these deficits upon the return of growth and confidence. Restoring healthy and robust growth must be the number one priority knowing that creditors themselves – who never required that austerity be implemented – are certainly aware that drastic reductions in public spending will notoriously diminish their chances of being repaid. How do you deny the proof that a nation’s wealth is the immediate result of what is produced by its citizens?

Moreover, contrary to microeconomic certainties and claims, the activity of the players in our economy are not guided by rationality or by a wise person and a generous quest for balance, but simply by intuition, instinct and greed, when it is not by a sense of panic... All this being said, confidence – which is very far from finding its source or its explanation in rationality – is naturally the cornerstone of this building: its presence allows for progress as well as growth, whereas its absence leaves the door open to all contractions. As they are the psychological and behavioral factors which condition particularly economic activity, only the soothing, regulating and stabilizing action of the state is likely to restore balance – and equity – during turbulent times. It is from this angle, less idyllic but oh so much more prosaic and realistic, that the economy and investment must be analyzed which, far from responding to noble aspirations, are the manifestations of our most intimate, yet sometimes most vile, instincts, appetites, anxieties and obsessions. Therefore, “Homo economicus” falls from its pedestal: it is its greediness and lack of scruples which are self-destructive. Debt itself is like a type of hot potato that everyone tries to pass around in a “game of musical chairs before the music stops” says Keynes. But, how do we explain the “irrational exuberance” of markets (the famous expression of Alan Greenspan, Chairman of the U.S. Federal Reserve from 1987 to 2006) or how do we understand, in contrast, stock market crashes? The return of the state will prevail when we admit that our control over the economy is at a minimum imperfect and limited by our own intellectual and mental abilities. Since, to borrow again from Keynes, economy “is one of these pretty, polite techniques which tries to deal with the present by abstracting from the fact that we know very little about the future”. Keynes, who never stopped reminding us that it was impossible to predict the future or even our future behavior, wished “economists could

manage to get themselves thought of as humble, competent people on a level with dentists”, adding “that would be splendid”...

Only typical Keynesian measures will save us now. Only government stimulus conducive to encouraging investment and job creation can actually save the economy, in the absence of private initiative and as part of an anemic demand. And only the determined action of central banks in the sense of compressing financing costs motivates companies to invest in the real economy, as long as the banking intermediation system plays its role. The objective is the famous “euthanasia of annuitants” that promotes the channeling of savings into investment and therefore into employment. As many emergency measures recommended even by the high priests of monetarism, Milton Friedman and Anna Schwarz. And even greedily applied in 2001 by the then President of the Federal Reserve, Alan Greenspan, and of course by his successor Ben Bernanke – yet a faithful follower of Friedman – from the intensification of the crisis in fall 2008. Taking advantage of its multiple quantitative rate cuts, did he not cause hatred and harsh criticism from the neo-liberals, who prefer clearly high unemployment to inflationary threats that challenge their wealth? The Republican candidate in the last U.S. presidential election, Mitt Romney, did not he hastened to demand the head of Bernanke? Besides, staying with the Republicans and with the right-wing people persuaded that tax cuts are a neo-conservative find... and who seem to ignore that it is Keynes who had first suggested reducing individual and corporate taxes as a way of boosting a faltering economy. While the great exponent of the Austrian School, Friedrich Hayek, was strictly against tax cuts so long as the state does not also reduce its lifestyle. Yet, is it not precisely the opposite course that was chosen by the most worthy descendant of the “neo-con” movement – that President George W. Bush – who, when he became president, adhered to tax cuts (especially for the more affluent), accompanied by an unprecedented surge in spending U.S. federal spending? Indeed, Keynes departed from the principle that large tax reductions should target the middle class, who would thus be encouraged to spend more, since it spends almost all its income, whereas the wealthy have a tendency to save. In the same vein, it is government that must take over when the private sector is no longer able to stimulate the economy. And why would it not be the “spender” of last resort in the exact same way as it is the lender of last resort? Indeed, aren’t the U.S. Democrats, like the U.S. Republicans, unanimous in demanding that the government cut its spending drastically in order to avoid falling off the fiscal cliff? Isn’t the very choice of this expression not likely to incur anxiety among a population – not necessarily aware of the technical debate – who is led to believe that the cataclysm is imminent? And that the only answer is sacrifice – more and more sacrifices – while the financial elite feasts and

the 1% become wealthier... The fact is that integrating the proposals discussed above – healthy state intervention against a backdrop of a devastated economy, maintaining low interest rates, tax cuts – are void and have no effect if the state decides to drastically reduce its lifestyle. Keynes taught us already: debts must be repaid only when the economy recovers. Otherwise: growth will be stifled in an environment where activity is very fragile. Tax increases, debt repayment and reduction in public spending can only be achieved without risk in a healthy economy. Knowing that, contrary to myth – or horror story – we the happy orthodox economists and “neo-cons” politicians, it is perfectly possible to arrive at a healthy economy despite, and in the presence of, a large public debt. Thus the true fiscal cliff would put into place today in the U.S. austerity measures comparable to the rigorously imposed dementia in Europe. It is not possible – or honest – to be guided in half measure by Keynes whose teachings are clearly cohesive.





## Financial Repression and Regulation

It has now been about five years that orthodoxy has been paralyzing all economic recovery and political correctness paralyzing the central banks. High unemployment – which will only worsen in 2013 in a country like France – changes nothing here. The obsession with deficits and anxiety about punitive markets unite the best of adversaries – the right and the left – in the same battle against the common enemy, though imaginary, namely inflation! Nothing should be done to stoke inflation, and everything must be sacrificed in terms of austerity. For it is said that we will one day be rewarded in return: in this life, or more likely in another life... A major nation – Japan – however just found the guts to break the touching consensus. In deciding to approach the problem from the right point while finally identifying its real priorities. It is indeed long before the Western world went dark, in 2007, that the dress rehearsal of our economic crisis wreaked havoc in this country. However late and timid were the reactions and actions of governments which followed since the implosion – in the early 1990s – of its real estate and stock markets. Constrained by the neo-liberal dogma that sees deficits equal to the Antichrist, the Japanese leaders systematically committed the childish mistake of reducing public spending before the current economic recovery was strong enough. To make room for a chronic deflationary regime to reign supreme in the late 1990s. A man – Shinzo Abe – who was just elected Prime Minister of that country by a sweeping majority nevertheless just decided to implement an “audacious monetary policy, a flexible fiscal policy and a strategy to encourage private investment”, in the words of his statement after his election victory. The sequence of this unconventional man’s arrival to power, as a radical change in approach to remedy this endemic evil, inflation, should not, however, leave anything to chance. Indeed, for the first time since 1980, this country is carrying clearing a trade deficit! If the Japanese fiscal deficit was actually tolerated by its citizens and its elite, just as was until now the anemia to its economic climate. If it did not matter after all that Japan’s public debt stood at 230% of its GDP (this figure being 110% in the U.S.), because 85% owned by nationals. The fact that Japan is no longer a creditor nation and that Japanese begin to owe money to foreign creditors has caused a national revival, intelligently operated by Mr. Abe, who has promised to transform the country’s

deficits into surpluses. To achieve this objective, the new Nippon government urgently needs the unwavering cooperation of its central bank – the Bank of Japan – which proved to be the least failed in its fight against deflation, as against the huge appreciation of its currency – Yen – having seen its value doubled since the early 1990s! These are the foundations of this new Japanese policy where “audacity” means weakening the Yen and inducing beneficial reflation into the economy through the lever of quantitative rate cuts, so deserved. Why preserve the independence of central bankers – personalities who occupy strategic positions of the first order without benefiting from the popular vote – if they refuse to make their ammunition available to economic growth, under the false pretext of the fight against inflation? As the monetary policy of a nation and the level of its national currency should serve business and employment, it is only natural that political leaders – elected officials – control them. Shinzo Abe’s platform consists precisely of intensive money creation which will also weaken the Yen, and at the same time allow the recovery of Japanese exports. Hence the stimulus program very recently enacted by Abe and which will reach the equivalent of 103 trillion yen (\$ 116 billion). An impressive amount that will inevitably produce positive results on the front of the fight against deflation, particularly in light of the bleak Japanese demographics. The Japanese example can inspire our European economic and monetary officials for the Japanese experience – the current one with Abe but also that of the “lost decades” – demonstrates the urgent need for determined and energetic measures to fight the recession.

Which already produce significant results, since the Yen began to depreciate greatly and optimism is gradually taking hold of the economy and investment in this country. Japan, widely studied and analyzed for its deflation and dramatic implosion of its speculative bubbles, will it one day ever be cited as an example for its about-face against orthodoxy? Accustomed to deflation, the – aging – Japanese population prefers by far saving to consumption. A very understandable attitude because it is actually better to refrain from buying today, if we know that the prices will be lower tomorrow or after tomorrow. As the Japanese economy has been stagnant for too long and Keynesian-like public spending virtually no longer has an effect on a jaded population, accustomed to an endemic recession, only a revolution in attitudes is likely to recover the activity of this country. In this regard, the most efficient way to induce such a psychological change is to reignite the appetite for consumption by adopting explicitly a target for inflation. The clear message sent by the new Japanese government and its central bank to their citizens is: “as your Yen is worth less tomorrow spend them today!” Posture for less heterodox, coupled with a completely new growth target fixed to the country’s stock market index. Indeed, the Japanese

Minister of Finance, Akira Amari, who said that his government would do everything possible so that the Nikkei reached 13,000 points by the end of the first quarter of 2013. This is the first time in world history that a government – responsible for the conduct of the affairs of the second or third largest economy in the world – clearly defines to its country’s stock markets a goal to be achieved! “Let the party begin”, is therefore the directive to the Nikkei required to take 17% more in six weeks. In reality, “the party continues”, since this index – which has already soared more than 30% since November 2012 – now finds itself at its September 2008 levels. Thus it has enriched domestic firms by about 38 trillion Yen in favor of the appreciation of their security, according to Mr. Amari’s calculations. The directives formulated by the Japanese Minister of Finance define therefore a general framework for increasing this index, with the knowledge that the operators, investors and speculators will only experience respite and “inner peace” when the 13,000 points will be met or exceeded. This, in order to unveil the new objective which will be defined therefore by the Japanese executive. Knowing that their investment stock – just like a car trip – always moves in the direction where we look... Still, will this chronicle of a spike announced by the Japanese stock market – which will further enrich and certainly the caste of traders and bankers – probably only do very little to benefit the vast majority of citizens of this country? To be useful, the nominal appreciation of the Nikkei – just as spectacular as it was, and it is! – combined with the devaluation of the Yen, should also result in an increase in the average Japanese income, and not only in a higher cost of living. In fact, Mr. Amari is not the first leader to designate the stock market with a goal to attain, since the President of the Federal Reserve Bank of Minneapolis, Narayana Kocherlakota, claimed in 2011 that the market capitalization would be “a central ingredient to economic recovery”.

The Japanese laboratory shows that it is therefore possible, under certain conditions, for a united regional group to take control of their destiny. To do this, a genuine financial repression must be put in place that can take many forms and paths. The objective is to smoothen the economic climate and healing, under duress, from the financial actors. In this context, it is vital to develop tools that will curb the appreciation of interest rates on the public debt, even that will cap them. In so doing, several avenues are possible which could be alternatively explored by government depending on the national context and the extent of the crisis. These very strict or more subtle measures will have the ultimate goal of containing certain capital funds within the national arena so that stakeholders benefit from the real economy or that they can be used by the state in the interest of collectivity. They are available in foreign exchange control and capital flow. Requiring higher reserve ratios from

financial institutions. Legally requiring banks to hold a certain portion of their reserves in Treasury bills of their home country or the regional organization to which they belong. Establishing a cap on the compensation of banking deposits and on the applicable taxes but also on fees collected on credit granted to economic actors. Offering preferential privileges and conditions to banks holding deposits with their central bank. Prohibiting or at the very least establishing a tightly controlled regulatory framework and taxing certain financial transactions. Taxing trading which would naturally lead investors to prefer tax exempt tools such as bonds, even those issued by certain corporations. The objective of these measures is to clearly channel funds which would have otherwise fled the country into maximizing the benefit to the real economy while facilitating the financing of public debt. This arsenal of financial suppression therefore leads to intense pressure applied on interest rates, which logically allows a reduction in public spending linked to the repayment of debt. Even better, since the energetic and intelligent implementation of this suppression may – with buy-in from the private sector and business which “would play the game” – bring about real interest rates which would become negative. That is to say that, in other words, these liquidities would have more interest in being invested in the economy that finding refuge in bank accounts, and this is precisely when interest rates would become negative that it is possible to repay its debts and economic growth benefits us all! That is why the state should finance ideally its budget by borrowing instead of taxing in the context of negative real interest rates. The efficiency of this financial suppression is even more assured when it offers the considerable advantage of being much more easily accepted and adopted than the increase in taxes or VAT. It is applied through leverage, like financial regulation, even inflation, otherwise less delicate and less direct than very unpopular (and often unfair) tax increase. Of the rest, increased regulation within the framework of this repression only responds to lax financial regulations, systematic during prosperous economic times. Since a so-called regulation must be evidently counter-cyclical, that is to say, that it must be shown to be stricter during the good times, whereas, the facts show, it is released under a stronger financial and banking system when the situation is more favorable. Indeed, it goes without saying that the first interest of finance is to manoeuvre within a minimal regulatory framework which stimulates and maximizes its profits. Still, this financial repression may (and should) be limited in time, a time necessary to proceed with liquidating (partially or wholly) the debt load. This financial repression is only repressive for a privileged minority, since it defines a new way of how a transfer of wealth and resources is carried out from the creditor and the investor towards the consumer and debtor.

Let us note that these “liquidations” are also likely to be conducted through a resurgence of inflationary pressures which suddenly reduce the debt load. Contrary to the biases of the majority of the economists, this phenomenon of deficit reduction as another form of financial repression which is inflation is beneficial provided that it is operated properly, knowing that there are only a few countries like Argentina or Zimbabwe which profited from it and, in these last two examples, have suffered. Thus it is Great Britain which benefited from liquidating its debts in phases for nearly half the period between 1945 and 1980 while the U.S. themselves could have offloaded part of their deficits thanks to negative interest rates for approximately twenty-five years during this same period. It is therefore possible to infer that each of these two countries could have reduced its deficits by 3 to 4% per year within this “liquidation” context permitted by financial repression knowing that the U.S. could have even reduced their debt at a significantly higher rate between 1945 and 1947, when they had negative rates of 9%! As for Australia, where the inflation rate was even higher, it would have been able to shave off deficits of 5% per year during this same period. As noted, the episodic use of this type of financial repression can reduce 30% of deficits if 3% is earned annually... There are therefore only developing or badly managed nations which experience a resurgence of inflationary pressures, and our central banks should have the wisdom to agree to let inflation run occasionally with the objective of relieving populations and deficits of all kinds since it can precisely slice quickly through all debt, both public and private. Our monetary and financial regulators could therefore do better by being more flexible and less stringent behind their ideological barriers by admitting that even remedies like inflation should be administered depending on the circumstances. From a practical point of view, it is enough that interest rates do not rise at the same rate as inflation. It is actually this delay – or this disconnection – between nominal interest rates (fixed by the central bank) and the inflation rate which sets off this gradual liquidation of debts in a quantity equivalent to the differential which is established annually between these two rates above. This financial repression must therefore be orchestrated with intelligence, even harmoniously, by the central banker, who must therefore work hand in hand with the executive branch of the country in question, and in the public interest. Cooperation even more precious than establishing these liquidations in favor of high inflation may only successfully implemented if the state has a more or less long term debt (five years) at fixed rates. Fixed rates which would avoid having to increase its repayments to adjust them when rates rise, inevitable during high inflation.



## **Inflation: Servicing Growth and Employment!**

The central banks of our Western countries can boast of a total victory over the front of the fight against inflation in the last thirty years. If they have indeed been successful in maintaining wages well below productivity, performance in the fight against recessions over the same period, however, leaves much to be desired. This lackluster report – the result of a consciously applied strategy – thus, resulted in a heavy trend of increasing unemployment in Western societies. Firmly rooted in attitudes, conditioning the actions and reactions of almost all employees, high and endemic unemployment has been insidiously implanted in our psyche as a new “normal”. For central banks whose ultimate goal is to control inflationary pressures, admittedly, full employment is certainly not a panacea! Indeed, a low unemployment rate often leads workers and employees to play the rule of supply and demand, i.e., to demand salary increases. Hence an acceleration in inflation. Central banks will not recognize it, but that is why they naturally tend to raise their interest rates when the economy improves: to keep unemployment at a level such that wages are always under control. Why? On the one hand to be able to display their success in their mission in terms of price stability. On the other hand to preserve capital and investors who, as we know, fear inflation. And not to harm corporate profits and thus to support the stock market... Let us be clear: this is in no way a plea for inflation. However, it would have been nice if the “track record” of our central bank contained slightly less success stories on the inflation front, and a little more marked in the fight against recession and unemployment. Since the interpretation in the “strict sense” of their mission by central banks has translated over the last thirty years into a very unfortunate consequence, i.e., the “wages” portion in the economy has steadily decreased. Not all is, however, lost, since the U.S. Federal Reserve unveiled at the end of 2012 an initiative refreshing on all fronts. For the very first time in its history, it announced the continuation of its quantitative tax cuts programs until the unemployment rate in the U.S. reaches 6.5%. Indeed, the 1978 Humphrey-Hawkins Act gave it two objectives: inflation and low unemployment. However, the Fed had never mentioned its concern about unemployment in its publications and statements until 2010. It had even pointedly ignored this priority since Paul Volcker until the first years of Bernanke as chair, including during the



long reign of the very controversial Alan Greenspan. In reality, the Fed like other central banks, relatively high unemployment was the key instrument allowing them to achieve their goal of controlling inflation. As it stands, the goal of the unemployment rate to 6.5% certainly does not seem ambitious enough. After all, the significant improvement in the labor market (and growth) contributes to narrowing the deficits “mechanically”. The resolution of the U.S. Federal Reserve will nonetheless constitute a revolution in attitudes, which we hope – however without any illusions – will be followed by the ECB... A profitable business must choose where to put its profits and cash. In this respect, when a business decides to invest, or otherwise conserve cash security, monetary policy of a central bank proves decisive. In fact, the problem is far from trivial. Indeed, without getting into espousing Apple’s stunning reserves – which amount to \$100 billion – and which makes some people say that this company is richer than the U.S. government! U.S. companies, to name a few, are sitting on a total cash of about 2,000 billion... The “uncertainty” factor is constantly cited by CEOs and their CFOs, who prefer to inflate their war chests or place them in in very low yield instruments, rather than commit to the future – by committing their funds. This uncertainty is nevertheless an integral part of any decision-making process and, in this regard, any self-respecting entrepreneur can handle this variable and adapt. For the entrepreneur, everything is actually uncertain: from technological evolution to consumer behavior, through tomorrow’s taxation... Corporate managers are obviously unable to predict the international environment or regulations in the years to come. This uncertainty is therefore a part of corporate daily life. Which did not prevent Google or Samsung, among others, from prospering. In fact, it is not so much this “uncertainty” factor which drives businesses to invest in low return investments and bet sparingly on the future, as it is the rate of inflation, or, at least, inflation expectations. Indeed, why would a treasurer be puzzled when he is sure that the inflation rate will not exceed 2% in the near future? The more this rate is low the more the company will actually be comfortable in this position to emphasize a very low profitability for its cash? These considerations relative to the absence of inflationary pressures go together, of course, with a pessimism – or skepticism – with respect to the prospects for growth. Strict common sense suggests indeed to refrain from any investment when the economy is sluggish or depressed, where nothing is lost in remaining liquid. In other words, it is only when prospects for growth re-emerge or there is a resurgence in inflation expectations should business be tempted to channel their cash into less secure horizons. Not until the consideration of uncertainty has disappeared from the radar. But the company may consolidate this change into asset allocation – in the direction of more aggressiveness – on a rational basis. This

“entrepreneurial” attitude thus will induce a virtuous circle because the investment itself will cause an increase in production and a revival of the inflationary trend. This is where the role of the central bank is instrumental, through its quantitative rate cuts program, i.e., its asset purchases in circulation, combined with a well-defined and tenable objective in terms of GDP. In the context of a depressed economy, only the central bank can indeed install this virtuous circle because its acquisitions and cash injections will lend credit to this growth target. Where growth prospects have improved, they, in turn, will have an optimal impact on its asset purchases. Moreover, the credibility of the central bank, as renewed confidence in future business conditions, can be further strengthened if the expansionist policy leads to a widening of the range of purchased assets by public institutions. To be reassured and heartened, businesses and consumers must be convinced that the central bank is in control, and just as energetic and determined. Indeed, it is only if the central bank orchestrates carefully this renewed optimism that confidence – which is a feeling and therefore volatile and emotional – is waiting for you. Only his unequivocal commitment to boost growth and restore jobs – even to tolerate a dose of inflation – will allow businesses to consider the future under more promising prospects. In the same vein, critics – often violent – against the U.S. Federal Reserve are unwelcome and exasperating. How indeed do you accuse this institution of contributing to the distortion of economic and financial conditions through its many programs to create money, as markets and the economy are themselves in such an upheaval? It is time to realize that our world today is nothing more than a cash trap since it has become next to impossible to reduce unemployment by reducing interest rates... which are already at zero. In such extreme circumstances, the duty of the Fed – as any other central bank – is to correct these distortions with a priority objective being restoring employment. Only its action in the sense of an increase in inflation expectations will contribute decisively to lower “real” interest rates when the nominal rate, itself, is at the bottom. The riskiest position – and certainly the least accountable and least befitting of a central bank – is to do nothing; the Fed (like the ECB in an ideal world) must engage in asset purchases to avoid liquefaction of its economy and curb unemployment. That’s why the only approach that motivates businesses to make their cash available to the real economy and for the benefit of future investment is in the hands of the central bank. Odysseus had asked to be tied to the mast of his ship to resist the song of the sirens. Today central banks find themselves in a similar situation. So much less poetic than the Odyssey, they are faced with a mission – inherently schizophrenic – which requires them to fight against inflationary pressures, while maintaining growth and economic fundamentals. How to honor a mandate to stabilize prices, which happens to be

fundamentally incompatible with the resumption of growth, reducing unemployment and redemption of government bonds and debt that nobody wants? Can central banks continue navigating this path, forcing them to adapt their monthly monetary and cash injections policy to changing economic and financial conditions, without risking the doom Ulysses faced with the sirens? For the first time in the history of central banks, the U.S. Federal Reserve has yet to cross the Rubicon committing to continue with its programs to create money (quantitative rate cuts) until the U.S. unemployment rate drops to 6.5%. This institution – under the leadership of Ben Bernanke – which certainly made us accustomed to his dynamism and pro-activity, yet is revolutionizing the profession of the central banker by correlating unequivocally printing money with the fight against unemployment. When, at the same time, the European Central Bank still displays on the main page of its website that its “primary mission is to maintain the purchasing power of the Euro, and thus price stability in the Euro Zone”. When it clings tenaciously to maintaining – on paper – the rate of inflation below 2%. While its moral obligation is to acquire Greek, Spanish and Portuguese Treasury bills to avoid a disaster in these countries and support the affected European populations. And while the very essence of this mission that it finds so hard to honor is inflationary. Very well aware of this fundamental incompatibility, the founding fathers of the ECB nevertheless focused all the vital energies of their institution on the quest (and maintenance) of the Holy Grail of stable prices. The German economist Otmar Issing, Member of the Board of the ECB, and its first President, the Dutch Wim Duisenburg, thus took the side of attaching their central bank to the mast of the sacred fight against inflation. At the expense of growth and jobs.

## **Regulation: Deconstruct and Stabilize**

Emerging and developing nations are very susceptible to shocks caused by the interrupted capital flow. In this regard, future jolts which will affect the European Union, strongly risk being the catalyst of a substantial upheaval on the front of capital movements across the globe. The only perspective – however quite benign and highly probable – of Greece exiting the EU would thus provoke a massive exodus of liquidities outside Greek banks toward Germany, while precipitating a worldwide stampede outside assets deemed “at risk”. If the economies of regional blocks are obviously subjected to multiple shocks, the responsibilities of inflow or outflow of capital are fundamental in reestablishing growth or in the advent of the recession. The Irish resurrection – following the liquidation of its banking system – is indeed beholden first and foremost to the strict control of foreign exchange, the rest of which was established with the consent of the IMF. As for emerging countries, their dependence on the inflows of capital well documented. Nations (like the U.S.) which regularly need short-term liquidity to financier their deficits are therefore threatened down to their vital powers in the event of capital flight, following a sharp reversal in their economic conditions or political pressures (we think, of course, of China and its massive Treasury bills holdings). That is why the best placed countries and regions of tomorrow which can amortize the inevitable shocks to come and, thus, benefit from a more stable growth will be those which will have implemented an arsenal of preventive measures regulating these flows while neutralizing certain speculation directly impacting these movements of capital. Capital flow transitioning globally and freely is actually very harmful for economies – mainly on developing ones – and must therefore be restrained to smooth out financial shocks.

Indeed, nothing replaces preemptive regulations which will reduce definitively erratic fluctuations on public accounts and which will protect upstream our economies. It is therefore the entire system which must be redesigned, or at the very least, reviewed through another prism, that of global imbalances and their collorary, namely a reform of the international monetary system whose objective would be to allocate capital more equitably. Under this optic, why would countries affected by a deficit in their balance of payments not levy a tax on the inflows of capital from nations with which they maintain a bilateral deficit? Under

this new interpretation, nations, benefiting from substantial surpluses in their current accounts, would thus actively participate in readjusting or compensating these imbalances. It is certainly clearly more complicated a priori to regulate capital flow than to influence trade surpluses and deficits. However, chasing massive deficits of the balance of payments between countries and regions would embrace the entire spectrum of imbalances which are the source of financial shocks and economic slowdowns. Nothing will be obviously accomplished without world cooperation and it is urgent to act. New economic and econometric research indicates that regulating capital would breathe a good dose of calm into markets. A recent study by the Bank of England – which cannot be accused of protectionism! – found a general increase in the financial and economic conditions if there was an international coordination of foreign exchange control. Finally, the IMF has data in sufficient quantities which attest that emerging nations which best resisted the crisis are also those which introduced before 2007 true regulation. It is therefore the political will to challenge the rules at the root of global investment and trade agreements which today are still lacking. Only a narrow and unequivocal coordination between industrialized nations, with integrated economies, and developing nations would regulate the two sides of capital so as to ensure stable growth. One of the fundamental lessons of this crisis is that the regulator may also be carried away by catastrophes. The mere mention of the Madoff name is in this regard sufficient to give him a lesson in modesty... As the error is human, regulation rarely succeeds in swimming against the current of established trends. As regulation further imposes common rules for the economy of the country, regional block or even the entire world, it is the entire system which has become weakened if the regulator errs.

Concerned with transparency, preoccupied with avoiding excessive risk taking and protecting investors, the regulator may, nevertheless, fail under the weight of too many complex laws. Such an example is the “Dodd-Frank” law, passed in 2010 in the U.S. whose objective – praised by all – was to prevent financial abusive behaviors and to allow authorities to seize – even dismantle – behemoth institutions, “too big to fail”. However, how do we act rapidly and optimally within a context where this legal text comprises 850 pages, i.e. more than twenty times more than the famous “Glass-Steagall” law adopted on the heels of 1929? The regulations alone (of the Dodd-Frank legislation) likely to include risky corporate transactions for bank capital – the famous “Volcker rules” – include 382 issues and 1,420 sub-issues! Certain explanations or clarifications of this law concerning technical points are also laid out in hundreds of pages. So that not even the regulator can claim to have read this law in its entirety... or understood it! Of the rest, only a third of the legislation is now in effect since, even by the own admission of Sheila

Blair, the former head of the FDIC (the U.S. regulator), this reform “se noie dans un océan de complexité”! Statistics published by a think tank, the “Sunlight Foundation” revealed an absurd number of consultation meetings about this reform between U.S. regulatory agencies and the largest financial institutions. Thus we are talking about 181 meetings organized over a two-year period with Goldman Sachs, 175 with JP Morgan Chase and 150 with Morgan Stanley, during which these banks tried by any means to influence and make the famous Dodd-Frank law more flexible with the obvious intention of gutting it its essential substance. Among some of the examples, Dodd-Frank is part of an increasingly more tortuous regulatory process whose key characteristic is however to create voids and blanks exploited by those who strive to violate these laws with impunity. Finally, did the U.S. Justice Department not abandon all legal proceedings against Goldman Sachs for the alleged subprime embezzlement in August 2012? Hasn’t the long investigation lasting four years on market manipulation of money charged to JP Morgan not been in legal limbo since the summer of 2012? Of the rest, this hypercomplexity is also disastrous for the economy itself, like this other example of a U.S. law passed in 2002 to fight against the “Enron” type of fraud, the Sarbanes-Oxley law. This led to an absurd result to discourage businesses strongly from raising funds on the stock market. With the initial objective of encouraging transparency, in reality this law accelerated the opacity of new companies that were no more than 12% in 2011 wishing to be publicly traded as opposed to 67% in 2002. The context, like financial products, is certainly more and more sophisticated. However, the regulator and the legislator should not fall into the trap of complexity which is precisely the trend of the world of finance. They should, on the contrary, fight with the assistance of simple and unequivocal regulations, with the singular priority being always the protection of their economic fabric. Since “more the state degrades, the more numerous are the laws”, said Tacite.

Concerned with transparency, preoccupied with avoiding excessive risk taking and protecting investors, the regulator may, nevertheless, fail under the weight of too many complex laws. Such an example is the “Dodd-Frank” law, passed in 2010 in the U.S. whose objective – praised by all – was to prevent financial abusive behaviors and to allow authorities to seize – even dismantle – behemoth institutions, “too big to fail”. However, how do we act rapidly and optimally when this legal text comprises 850 pages, i.e. more than twenty times more than the famous “Glass-Steagall” law adopted on the heels of 1929? The regulations alone (of the Dodd-Frank legislation) likely to include risky corporate transactions for bank capital – the famous “Volcker rules” – include 382 issues and 1420 sub-issues! Some explanations or clarifications of this law on technical points are also laid out in hundreds of pages. Even the

regulator claims that it has not read this law in its entirety... or understand it! Moreover, only a third of this legislation is now in effect since, as even admitted by Sheila Blair, former head of the FDIC (the U.S. regulator), this reform “is buried in an ocean of complexity”! Statistics published by a think tank, the “Sunlight Foundation” revealed an absurd number of consultation meetings about this reform between U.S. regulatory agencies and the largest financial establishments. Thus we are talking about 181 meetings organized over a two-year period with Goldman Sachs, 175 with JP Morgan Chase and 150 with Morgan Stanley, during which these banks tried by any means to influence and make the famous Dodd-Frank law more flexible with the obvious intention of gutting it of its essential substance. Among some of the examples, Dodd-Frank is part of an increasingly more tortuous regulatory process whose key characteristic is however to create voids and blanks exploited by those who strive to violate these laws with impunity. The context, like financial products, is certainly more and more sophisticated. However, the regulator and the legislator should not fall into the trap of complexity which is precisely the trend of the world of finance. They should, on the contrary, fight with the assistance of simple and unequivocal regulations, with the singular priority being always the protection of their economic fabric. Moreover, the scission of banking activities between commercial and retail establishments – whose deposits are covered by government guarantee – and the banks which deal with investments and speculation proves in this respect to be indispensable. The Volcker rules were indeed likely to remedy this, still less complex to interpret and apply a 298-page legal text! In comparison with the simplicity of the now defunct 1933 Glass-Steagall law, repealed in 1999, and which only had 37 pages... How does the legislator expect to make an unequivocal distinction between the banks which invest for their own account on the one hand and those which only carry out client instructions on the other hand? The effective line of demarcation between these two types of operations are a matter of interpretation and intention, with the knowledge that an establishment, or a trader, can quickly change – even cheat – by passing from one to the other according to its interest, even mood? Didn’t the Libor scandal actually reveal that the UBS traders in London were challenging one another over who could manipulate this rate the most? Therefore it is exclusively – almost mechanically – when Glass-Steagall was abolished that the volume of transactions exploded. These over-the-counter transactions, opaque and unregulated deals were only able to prosper when this law was repealed. As Glass-Steagall deprived investment banks from banking deposits – and therefore from financing at a cheap price –, its collateral effect was naturally to limit the increase of their puts, and therefore their risks. All the while increasing and diversifying the number of stakeholders in the

financial markets, thus becoming more liquid. While the repeal of the Glass-Steagall law would permit the rise in power of investment banks that were then able to develop a myriad of new financial instruments beyond the control of any regulatory agency. This separation between commercial banks and investment banks will thus allow the financial markets to become resilient, in the hope that the next conflagration will not be as dramatic as that of 2007-2008. While restraining considerably the power of banks which will by necessity have different objectives and priorities, even divergent. It is therefore vital today, in the interest of the real economy but also to save the financial sector from itself, to proceed without delay to limit the power of banks.





## **Redefining the State – A Lever of Public Health**

Keynes was one of the promoters of social democracy built on a fundamental pillar, full employment. It started of course from the principle that only capitalism guarantees individual liberties, private initiative and free enterprise. This does not prevent it from denouncing the faults of such a system promoting deregulation, itself generating intolerable anomalies in any civilized society. To this end, let us take its “General Theory” where it stated (in loose translation) that “the major faults of the economic society in which we live are not to provide full employment and consist of an arbitrary and unfair redistribution of wealth and income”. How to ensure that full employment and equity in the allocation of resources if it is not done through the active intervention of the state, and while it is important not to count on the charity of the private sector? That’s why the supporters of Keynesianism are also strengthening the powers and prerogatives of the state, whose only action is likely to smooth over the glaring inequalities, while imposing a protective regulation of public interest. It is not, however, going back to the teachings of Ricardo and Marx who argued that the capitalist system makes its profits by constantly maintaining a “reserve army of unemployed”. Their concept actually had a congenital defect wanting that this army of unemployed would disappear when the very notion of profits would be eradicated. Keynes, for his part, showed that long-term unemployment was caused, not by the pursuit of profit, but by variable and volatile private investment in uncertain times. As it is the fall in this private investment – or misused investment – which is the source of economic downturns and climbing unemployment, it is imperative to “socialize” this investment. To do this, businesses – as the government itself is an employer – must assure their employees’ purchasing power by allowing ongoing private investment, guaranteeing full employment. The essential prerequisite for the socialization of investment is a redistribution of income that would be the basis of full employment. In the Keynesian view, the public sector must therefore act in addition to the private sector, without ever trying to replace it. Today, seventy years later, equality and employment are still – and more than ever – the core concerns of our developed nations. Although the front line has moved significantly. Indeed, while the protagonists at the time of Keynes owned the means of production – i.e., the industries – and to a lesser

extent the pensioners. It is actually the power of finance – as a result of globalization – that crops individual freedoms while increasing imbalances and inequalities. This finance whose only priority is to maximize its profits instead of investing in the economy, its production tools and its jobs. This finance which uses all its resources to tear down barriers, decimate regulations and operate at levels to fight governments on equal terms. In this context, once again, only the action of the public authority is able to regulate, to smooth and fill gaps, so it is impossible to rely on the private sector, whose role is not to do thus. Keynes' fundamental contribution to democracy resides in this vision of the state as protector of the public good and as supreme regulator of private sector activity and market forces. To achieve these objectives, the state must therefore limit at the same time the power and profits of this finance.

Therefore, it's not because the state no longer has money or because the banks are empty that it can no longer do anything – it is neoliberal ideology that prevents money from being printed. It's not because the state no longer has money or because the banks are empty that it can no longer do anything – it is neoliberal ideology that prevents money from being printed. If nothing more can be done today, this powerlessness and this paralysis of state creates the neoliberal affairs that were not prevented from calling on them whenever the system was on the brink of imploding. Nowadays, it's more about saving capitalism than recognizing that it is impossible for it to reach full employment. Indeed, capitalism has no more of a philanthropic vocation than the financial markets have – which are the most visible and irritating product of it – and this is precisely why state intervention proves essential in calming down the economy, guaranteeing and protecting employment, and cracking down on abuse. If the state decided not to get involved in the money creation process, its sole source of financing would be in the issuance of bonds, knowing that the amounts borrowed within its national borders would be deducted from economic activity, rendering it lacking in money. Each Euro that the state lends to its nationals shall be one Euro less for investing and for business and consumer credit. Following the same reasoning, just as much employment is created thanks to government spending as is not created by the private sector. Indeed, state stimuli will allow new schools to be built, the road network to be improved and just as much work and expenditure that will clearly be made at the expense of industry and the services industry. Needless to say that good governance of public affairs leans towards sobriety and is clearly more advantageous – not only for public accounts but especially for developing initiatives and intelligence – with the private sector making the economy live on and prosper. It is due to all this that public deficits are rarely looked into by political authorities willingly or by choice, but rather out of a pressing need to compensate for the weak-

nesses of the public sector and what it lacks. It is therefore crucial to understand that public deficits are simply the consequence of the decline in aggregate demand and not their cause – deficits that will automatically be covered when the economy picks up. It is therefore crucial to understand that public deficits are simply the consequence of the decline in aggregate demand and not their cause – deficits that will automatically be covered when the economy picks up. By running into debt, by reducing taxes and by increasing spending, the state does nothing but fill gaps and holes left by the private sector. The economic cycle effectively works according to an interconnected diagram, in other words, a business area can only generate profit if another area spends or gets into debt at the same time.

In doing so, the state fulfills its public welfare obligations and puts people back to work by taking on, at least partially, the task of investing in the economy, temporarily put on hold by the private sector during the crisis. In this respect, tax reductions represent a leverage that admittedly matters, but which is also quite limited in effectiveness given the virtually zero impact on business profits and personal income. The same applies for maintaining low interest rates, which does not significantly favor lending to the real economy due to investors quickly resorting to more lucrative investments. With regards to money creation, if it is essential and if it undoubtedly occurs during a crisis period, it will not be able to continue on forever due to its implications on inflation and the bad practice that it instills in economic agents. These economic agents, in knowingly being able to rely on the generosity of the state, would be able to take part in more risky ventures. The state is therefore expected elsewhere, with its most effective and constructive action being on another level – that of the stabilization and regulation of private investment. It is by no means an issue of the government nationalizing companies, but rather of building partnerships with private sector operators so that its altruistic action serves as a regulator and conduit for private investment. Effectively limited to the areas of activity, the strength of companies and depending on the impact of a specific sector on the entire economy, this cooperation must lean towards achieving full employment, which could not be achieved without the stabilizing effect of the state. Contrary to what monetary theories would claim, the future is uncertain, the information available to us is incomplete and the markets are not perfect. This renders these partnerships and joint initiatives between public and private sectors imperative in achieving growth, buying power and employment. It is therefore essential to restore the state to its rightful place in the economic system, on condition that it can exercise its control rationally and without political calculations. Indeed, only the state can reduce uncertainty.

That is why capitalism must become the business of all, since it is – and it is not only a recent phenomenon – in the hands of a tiny minority who is in control and who jealously guard it. An imperceptible shift nevertheless took place since the beginning of the 1980s, as the power of money passed from the hands of the captains of industry to those in high finance. In doing so, this financial oligarchy has gradually extended its domination to end up by, toward the mid-2000s, reigning over the entire real economy to which it became totally addicted through leveraging financialization. This ultimate sophistication in finance (which led to the subprime crisis in 2007, which itself was the starting point of our actual crisis) has become essential to the economy by showering it with liquidities. In passing, this financialization granted credit to households to give them the illusion of making progress in their way of life. All businesses and economic actors therefore adopted the market as the supreme reference and welcomed regulations meant for them. Without realizing that this financialization reverted in fact to an accrued monopolization of powers. Powers which were imperceptibly passed from the captains of industry and business men (who had at least were familiar with their workers and their production) between the hands – and computers – of a tiny elite of financiers whose role was more or less to open the tap wide with liquidities. Entrepreneurial tradition had up until then really created an added value to our society. Technological revolutions left a profound mark on it in order to have formed the genuine driving forces for corporations to become prosperous and the individual to develop. Indeed, profit had only ever been an instrument for these true businesses, not the ultimate objective for finance, since it was constantly reinvested, indeed in the interest of these entrepreneurs, but also for the entire human chain participating in it.

## **Profit only for the Horizon and only for Ambition**

While profit is now the only horizon for finance and financialization which has contaminated everything in its path and which now only considers businesses as a lever for profit, a slot machine in the global casino which would buy and sell businesses, hire and lay off employees, according to the expected benefits. The dichotomy between industry and finance has in fact disappeared. Whereas it was still possible some twenty years ago to draw an unequivocal distinction between Renault and General Motors on the one hand and financial institutions like Société Générale or Goldman Sachs on the other hand. We are now witnesses to comical arrangements where a business like General Motors calls for help because its financial sector, the provider of credit, is in disarray. It is as if the production of vehicles was a side business, just good enough to justify and feed a financial sector which had proved far more lucrative than its traditional activities. Should we be surprised, in such a context, that Goldman Sachs rushes to buy up wheat stocks to leverage this other bubble? Mixing genres has therefore become global, completely in favor of finance and in defiance of any commercial interest and industrial strategy. It is the whole spectrum which is today contaminated by financialization: energy, real estate, foods. Even the functioning of the state and collectivities is also marked by the seal of this hyper financialization: whereas it was enough for them, in the very recent past, to issue bonds to finance their lifestyle, our leaders today are calling on banks to create scholarly arrangements for them based on “interest rate swaps”... Of the rest, nearly half of the derivatives in the world are interest rate swaps, coincidentally directly related to the Libor, whose scandal and manipulations were mentioned above... Would the next bubble to burst be these famous interest rate swaps? To which case our states and its taxpayers – i.e. us – would be the first to pay the price of this umpteenth speculative tribulation, potentially devastating for the world economy. Indeed, it has been estimated that the four largest U.S. financial institutions had on their books approximately \$170,000 billion in derivatives in favor of the economic actors of that country. Knowing that the international outstanding amount in derivatives represents twelve times the global GDP! All the facets of economic activity are thus entangled in a complex web woven by financialization. Of the rest, the sectors of activities do not matter at all in this financialization able to

prevail today in the machine tools sector (for example) to abandon it completely for investments in the agricultural sector, if it proves to be more profitable. The single only objective being to generate profits in cold cash: indeed, such is the ultimate expertise to the exclusion of all others. Hence for example Goldman Sachs which in 2012 invested \$10 million in the prisons of the State of New York, with the following perspectives: recover their money if recidivism drops by 10%, earn 2 more if this rate improves more, or lose 2.4 if the New York criminals do not change! Our societies have today attained such a degree of decadence that they have delegated such responsibilities to the financial sector, and their most elementary homework *vis-à-vis* citizens in need. The moral obligation of the collectivity is therefore vanishing in the face of “corporate bonds” – “social impact bonds” – issued by financial institutions which raise funds to generate profit while replacing the state. Organize the understaffed, to neglect working conditions, modernize reluctantly the tools of production, such have therefore become – amongst other things – the guidelines for managers of modern businesses, completely under the yoke of the financiers. How can we be surprised in such a context of the wave of suicides in a number of businesses confronted with the coldness of the juggernaut of money? These restraints imposed by the shareholders actually require the working ants to perform like world-class athletes. Without equivalent salaries, of course... Thus is the employee called upon to adapt instantly, even agree to lose his job, if such is the price to be paid for progress – or to maintain – profits? The ideals and energies of our politicians, financiers and even our intellectuals unanimously tend toward this singular objective of profit, elevated to the rank of pragmatic religion, which defined new codes which all of society must soak up and be inspired. That is why Anglo-Saxon countries and Germany are entirely focused on the gains of productivity as the single and only means to exit the crisis and reduce deficits. While categorically rejecting to pass through the exit door consisting of investing in business and training, understandably much more expensive for them. As the only improvements tolerated are those which affect productivity, all the criteria, optimization and research for solutions are scrutinized and shelled in terms of productivity. The only credo is therefore improvement in sacrosanct productivity – whose only priority is to find savings in both the production processes and salaries – whereas the gains in productivity which truly enrich a business over the long-term instead tend toward strategies for products sold, their range, their quality, and conquering new markets... so many determining factors obviously impacting on the success of any business and which can only succeed by adhesion and motivation of all of its employees. This supreme contempt for the value of work that we all accept in the interest of swollen speculative revenues – therefore on the

short-term – is it not the hallmark of decadence in our civilization? In fact, the life and management of businesses have been contaminated by the ills inherent in finance. With the assistance of always more sophisticated products, it raided both management and the working tool, considered therefore as a crude commodity negotiable upward or downward, depending on the needs and profit of the hour. Work has become a “commodity” – a crude raw material – deprived of any moral, and even, human regard. In fact, businesses which lay off are very often rewarded by the markets through an increase in their shares while, at the same time, those which hire run the risk of being judged with great caution by the armada of financial analysts comfortably seated in their armchair. Our financial system has thus forced our businesses to learn how to have only 100 employees do the work of 200 to maximize its profits. It is absolutely unlikely that no financial guru or an astute Wall Street observer” has ever, up to now, conducted the relation between this policy of the optimal spin of the employee and the very bad statistics of unemployment which defeat growth. When will the guardians of the temple finally understand that workers and employees contribute just as much as the shareholder to their wealth and winning “deals”? Let us acknowledge that it is clearly easier for a camel to pass through the eye of the needle that it is for the capitalism of today to be self-critical...

The iconic case in this regard is the British pharmaceutical giant GlaxoSmithKline, which all too recently pleaded guilty to federal crimes *vis-à-vis* the U.S. authorities by agreeing to pay fines in the amount of \$1 billion for circulating two medications not approved by the U.S. health regulatory authority (the FDA) and without having passed basic safety tests required by U.S. law for a third medication. GlaxoSmithKline was also forced to pay an additional \$2 billion to settle a class action lawsuit accusing it of having circumvented doctors to establish false certificates, all with the objective of accelerating the distribution of these relevant medications. According to the U.S. Department of Justice, the total amount of \$3 billion represents restitution for the biggest fraud in the entire pharmaceutical industry, bigger than the \$2 billion paid by Pfizer, the \$1.4 billion paid by Eli Lilly and the billion dollars by Johnson & Johnson. Of the rest, the fines paid in 2012 to U.S. regulatory authorities by financial and industrial actors achieved a record \$8 billion. It is, for example, the \$37 million paid by the military construction company ATK Launch Systems for having sold defective materials, or the 200 million paid by Oracle accused of having overbilled the U.S. government. From the intense pressure exerted on their employees (at all levels of the hierarchy) to achieve and exceed the objectives, to the permanent stress to which management is subjected as to the development in the stock price of the company that employs them. Returns on investments, figures related to their domestic and interna-



tional sales for their operating efficiencies. The violations of the law and the corruption now seem to be part of the rules of the game for businesses and the financial world, only concerned with producing good figures, exceeding the competition, conquering new markets and clients... until a few are mistakenly made to feel the “pinch”. Blithely trampled upon, ethics and morality are being eclipsed by promotions, bonuses and falsified accounts and reports. In this regard, Glaxo is only one more turn of events in a long path of corruption and scandals having affected (for a good fifteen years now) Worldcom, News Corp or Wal Mart... It is therefore the whole spectrum of the working world (and not only finance) which is infected by the conflict in interest, fraudulent accounting, false declarations and attacks on private life. Is modern capitalism therefore condemned to create monsters? Milton Friedman asserted that capitalism is freedom. Indeed, unless this freedom remains the preserve of a tiny minority who co-exist apart from and on top of an ocean of serfs.

The historically low level of interest in rates, against all odds, decisively inhibits any investment in the medium and long term by businesses. By trying to save the system through the lever of cash injections and quantitative rate cuts, central banks have actually contributed unwittingly to the swelling of a new speculative bubble. In fact, the really tiny interest rates, even negative, in some countries designed to encourage investment and boost economies have created a monster! While the stock market traditionally offered profitability and growth over the long term for investors, the bond market generated income. Quantitative rate cuts have indeed shaken this given because global liquidities have been therefore gradually clumped to international equity markets which had a big advantage in these times of depressed rates: dividends. As investors in search of profitability realized that the distribution of dividends on equity portfolios responded honorably to their search for yield. So they turned the stock market away from its original vocation of financing business into a machine to produce yield by proxy dividends. Unprecedented phenomenon for fifty years, the stock market has become an alternative bond market. This molting of global stock markets as a till for investors, fond of regular and substantial income, is clear evidence of consequences for the world of business, for workers, and of course for central banks as for politico-economic leaders. Whereas the primary purpose of the stock markets was to put the providers of capital in touch with businesses in need of their cash. Whereas investors are supposed to receive a share in the development of the business in return for the risk assumed by putting their capital at its disposal. The low interest rate environment sterilizes de facto the full range of investments. And the increased dependence of these businesses on the holders of cash – concerned about getting a return on the short term – redistributes thor-

oughly the resources. While forcing companies to change their strategy or the way they lead and manage their working tool. The same applies to central banks that find that their policy, often aggressive, of interest rate close to zero – far from forcing the hand of businesses to invest over the long term – leads them to opt instead for instruments favoring liquidity in the short or very short term. As the distribution of dividends or redemption of a portion of their own shares. Like Ford, which recently decided to double (from 5 to 10 cents) its dividend: this transaction will cost \$762.5 million but also authorized the soaring of its security by 35% in the last three months! As always, the world of money has found the solution to overcome – or circumvent – the pitfall of zero rates and cash injections by managing to find a new “cash cow”. Its greed has indeed inflated another bubble and, incidentally, distorted and perverted the whole economic theory that interest rates at such levels and dynamic money creation should logically benefit economic actors. Instead, the monetary transmission mechanisms were diverted to transform the capital markets into arm bandits systematically spitting out currency. In addition, the concept of risk management – designed to favor bond markets safer than the much more speculative stock markets – has faded. Conversely, the escalation of the risk premium – i.e., the compensation offered to the shareholder in exchange for the risk assumed – reached such levels that holders of cash (pension funds, big investors, sovereign wealth funds, etc.) do swear by the stock markets, with the considerable advantage of paying dividends, while the economy is somewhat depressed. The context of near absolute zero interest rates has only exacerbated this relentless quest for profits of global investment with, once again, disastrous consequences for the real economy. Entrepreneurs prefer to be able to devote their cash flow to pay dividends instead of investing in the medium and long-term in the interest of their company and its employees. Did central banks know that their hyper lax monetary policy would only exacerbate the war between labor and capital? In 2011, U.S. companies indeed spent \$650 billion in dividend payments and share repurchases compared to \$580 billion in investment and development. Given that the trend for 2012, the best year for stock markets in 10 years, should be even more damaging to jobs traditionally benefiting the tool of work. Worse yet, since the corporate bond issuance activity which planned to use these funds to invest in production facilities were heavily shunned in favor of those who had announced their intention from the start to recycle these sums into dividends and redemptions of their own title! The dominant influence of ownership on the strategies of companies listed on the stock exchange distorts therefore the business of the entrepreneur. To yield to temptation – sometimes warnings – holders who took their cash as hostage, the business manager and CFO have gradually become purveyors of regular income

at the expense of investment and of course employment. That political, economic and monetary officials finally deign to look closely at the stock theater and behind the scenes, if their concern is to restore economic growth and reduce unemployment. Because the big bosses of companies whose shares are listed have now completed their molt in central bankers, and play the game of financialization in the background. That is why it is no longer possible today to rely on them, or on their businesses, to boost our economies.

## **Enshrine and Reevaluate Work**

Competitiveness itself – repeatedly invoked – is it not a vague concept designating the ability of a country and its companies to confront competition? By focusing on competitiveness from the bottom – reality internal devaluation – which involves lowering the export prices simply by reducing the costs of production. Public discussion therefore focuses on labor costs while the cost of capital is never mentioned, whereas net income distributed today represents 10% of the added value of non-financial corporations. This historically record level since the Second World War, compared to 5.5% in 1999, concludes that the share for shareholders has increased to a considerable extent over the past twelve years. In other words, the complaints of employers who threaten to lower investments and research have no traction. In fact, they ignore the increasingly higher share that companies choose to distribute to owners of capital, regardless of the intensity of the economic and financial crisis. With a profound questioning of the ability of businesses to cope with all the rough edges of competitiveness due to these distributions. That is why the rights of employees undergo an unprecedented attack, which is why the costs should be compressed if the goal is to win market share in exports: these are clearly the requirements if the goal is always to remunerate more shareholders, capital and finally those who bet on the stock market... Logic however taken in inextricable contradictions, knowing that the Orwellian speech of industrialists and corporate bosses attain summits of implausibility and arrogance when they explain that the fight against job cuts is... to fight against the job! Understand once and for all that competitiveness is not necessarily synonymous with unemployment, with precariousness or with the explosion of inequalities, contrary to what markets and employers impose on employees and workers for over twenty years. Let's rebel therefore and reject with disgust the allegations of the President of the union bosses (MEDEF), Laurence Parisot, who said in 2005 in the Figaro: "Life is fragile, love is precarious, why should work be secure?" Indeed, such statements devote the defeat of the policy of which one of its tasks should be the determination of the rules of the economic game and the tutelage of neo-liberalism which is only a ploy aimed at putting Europe on the automatic pilot of a competition intended to resolve all issues. To replace the culture of the state with the obsession of sales

means to trample on the very essence of work, however, the source of all economic value.

This is why the only way to restart the economy is to give purchasing power to those who really spend in the real economy. Indeed, only the poor and middle classes are concerned and actually benefit from the economy. They alone are responsible for growth. The upper classes, for their part, hoard or invest in financial products. This is why it is imperative – even essential – to raise wages, including the minimum wage. Confiscation in good standing of the economic apparatus has been undertaken since the late 1970s by a tiny minority that has redistributed the product of the work of others largely in its favor. They are actually not so much our factories, industries and businesses that are not productive. This productivity was actually monopolized for the benefit of an elite who assisted, totally indifferent, to the widening of a gap between real wages and productivity. Germany itself, which stands as donor in the lesson of productivity was only able to benefit from growth above the European average due to constant sacrifices required of its population. The German export engine roars not only thanks to the productive power of its businesses. In reality, it is the so-called reforms to the “Hartz” businesses between 2003 and 2005 – which consisted of transferring resources and wealth of citizens to businesses and to the financial sector – that Germany must have boosted its exports. Actually, it is the wage cuts to, and drastic reforms of, its labor market that have improved significantly its productivity, compressing it at the extreme cost of labor. Reform claims initiated in August 16, 2002 where a group of experts led by the Director of Human Resources Volkswagen, Peter Hartz, presented to German Chancellor Gerhard Schröder, his proposals for the reform of the labor market. Ten years later, German society has become deeply transformed by these reforms. Indeed, an OECD study, published in late 2012, concluded that there had been a dramatic increase in income inequality in Germany, more than any other member of that organization. Having very finely maneuvered, the Hartz Commission was able to create a market of subsidiary – or parallel – work in its country dominated by low wages and not subject to social rights. In fact, these reforms deprive unemployed Germans of all their rights to unemployment benefits. They are therefore reduced to the status of social beggars! Thus, it is only after a year of unemployment that the worker is entitled to request a paltry monthly allowance of EUR347 per month, on condition that he has first exhausted his savings and on the express condition that his spouse is unable to support him. Why not also mention the obligation he has to accept any job, regardless of their qualifications and previous earnings. Hartz is therefore both a trap and the best way to poverty, how to arrive at a state of absolute insecurity, unthinkable and intolerable in a rich country like Germany. A study by the

German Equality Welfare Association actually reveals that three-quarters of those affected by these laws remain forever dependent on Hartz. Given that, moreover, the mere threat of falling into Hartz forces the unemployed to accept low-wage part-time jobs, devoid of security, pension rights and other benefits. The German dogma of the “low cost” worker was the result of these reforms... And, in fact, only 29 million Germans (of nearly 42 million workers) now have employment under the social security scheme while some 5.5 million of them work part-time, and more than 4 million earn less than EUR7 an hour! The German low-wage sector pulls by the bottom of all wages in the industrial sector by acting as a kind of infernal lever. The worker endures conditions similar to those still in force in the Third World and emerging countries.

It is therefore at the price of the sacrifice, hardship and sometimes humiliation of its employees that Germany owes its trade surpluses, not rational or qualitative productivity improvement. Would we in the rest of Europe – and even in Great Britain – accept such “Hartz” sinister and cynical measures, when the state becomes the Grand Inquisitor by requiring a list of accounts and jewelry from the employee so as to fix his unemployment compensation or benefits? Therefore it is at the expense of its employees, pushed ever more precariously, that businesses and major banks in this country owe their international success. It is therefore vital to raise Western wages today, not only to correct this outrageous inequality. But also to re-establish the traditional correlation between productivity, real wages and consumption. Therefore, it is inevitable to ask: the insistence – even the sheer determination – of neo-liberals to claim an improvement in the competitiveness of our businesses, is it motivated by a search for additional benefits for investors for this caste of shareholders or is it really intended for growth that would benefit all players in the economy, i.e., the consumer base? It is certainly legitimate to advance the productivity of each one... provided that its improvement translates into purchasing power for the ordinary citizen. Because growth will only be perpetuated by the transmission belt of increased income, which is why it is crucial to proceed first to the increase in the minimum wage. As, on the contrary, it is economically unjustified to leave so many resources in the hands of those who spend less or wrongly.

Let us for a few minutes consider the theory of the plot which, as it happens, would indicate to us that the financial world and business leaders are against full-time employment. The intervention of the state is however able to effectively address unemployment among our people. Through public investment, as in the construction or renovation of schools, hospitals or roads. Through social benefits, subsidies on staples,

even a reduction in direct taxation on certain fiscal households and SMBs. Through a reduction in VAT. So many measures which, combined according to an appropriate and targeted schedule and in rational doses are likely to result in a substantial reduction in unemployment. It goes without saying that this increase in the revenue of impoverished and average households would benefit first and foremost consumption, that is to say businesses and therefore, definitively, their general management as well as finance the provider of credit. They are, however, fiercely opposed to this type of economic recovery beholden to the state, as they vehemently fight against any increase in social benefits. Despite the positive impact on their own businesses and on the strong performance of the financial system. In reality, they are ideological reasons which feed the condemnation of big business and high finance against the growing role of the state in public life as well as in economic activity. It is of little importance that full-time employment can be reestablished by the intervention of the state, as they sweep a backhand that subsequent swelling of their own profits following this action by the state, if the price to be paid by them is losing control over the economy and government. That is why it is now high time to draw a final conclusion: the righteous and outraged attitude of finance and neo-liberals against public deficits is only a posture that gives them an excuse to dismantle social programs and reduce the size of government. As such, neo-liberalism actively seeks out confrontation by not having to constantly shake the specter of deficits, of which it doesn't give a damn! Knowing that its one and only objective is the very deepening of this crisis which will allow it to call for more shrinking of the government. Indeed, let us be under no illusion: the neo-liberals and high finance have an interest in fanning this psychosis of public deficits, whose increase in intensity will give them the perfect excuse to cut public spending and aid to needy citizens.

Finance – which today holds the keys to our prosperity – is indeed opposed to the use of public deficits to stabilize and reboot our economies, since it is aware that the return of the state would mean its death sentence. According to it, jobs would only be a variable of private investment in the economy: it improves in case of a recovery in confidence and must be reviewed without qualms downward depending on the decline in production and the decline in agreed upon funding with the economic actors. Full-time employment – or, at the very least, substantial improvement in unemployment is therefore not a priority for financiers who view it, on the contrary, as a danger of the proper running of their businesses. In the large financial and employer system, the employee and worker are actually pawns – or dead weight – to move forward and backward – even throw away – according to the profitability of the business and the investor strategy. When the value of work is

sacred, the employee becomes a “troublemaker going around in circles”... Moreover, it makes sense that employers are – at least intuitively – against full employment which would reverse the balance of power that would suddenly no longer be in their favor.

This confiscation of all power made our world slip *de facto* from state imperialism to financial imperialism, while profoundly changing our values along the way, since the benchmarks were all violated when dignity and respect were removed from the work ethos, yet holding our societies together. This financial imperialism has taken on another face and another character different from what dominated in the 20<sup>th</sup> Century since interest groups in certain former colonized countries or third world countries – since then given a promising new name “emerging” – are aligned and associated with the new elite of the former colonizing countries to exert their dominance over the mass of workers and employees throughout the world in favor of globalization, the ultimate creation of financialization. Only the state, even a union of states, is now even channeling this imperialism. The violence of today’s crisis, which seriously made high finance falter and which challenged its stranglehold, should stimulate a crystallization and encourage the emergence of a common front between corporate and political forces aiming to dethrone – or at least humanize – this oligarchy. It is of course out of the question to return to Marxism. But why not be inspired by Marx and his critical mind, not only to assassinate capitalism, but particularly to transform it, even bestowing ideological fundamentals on it, which would contribute to the material and moral enrichment of our societies? Even there, only the state – as the incarnation of the collectivity – can give this impulsion, even if it is also out of the question here to return to the classic notion of the state, since it is all the more imperative to rethink its role. It is indeed with great difficulty, at the price of sacrificing dozens of millions of human beings and at the risk of a new world war, that the communist dogma of the predominance of the state over the individual has given up the ghost. It has therefore been ruled out that the increased role of the state – which some call rightly *vows* – dons once again the robes of the former barbaric formulation where the state apparatus knew what was better for the citizens than they. Rethink the state and consider emphasizing its role in economic life should necessarily be bearing constantly in mind the sense of obligation of this same state *vis-à-vis* its citizens as well as its own limitations. If dismissing the financial oligarchy has been ruled out in order to replace it with a political autocracy, the present day crisis must nevertheless force an overhaul or a recalibration of the primary role of the state as protector and regulator. Keynes constantly told us that, far from accomplishing what the “individuals do already”, the state must start to do “things that it does



not yet do". Whatever it is, the state must "become part of the solution", to borrow the Reagan's phraseology, by pushing it further.

Is it not pathetic to note that the employer (mainly Anglo-Saxon, it is true) is clearly more concerned with engineering, financial arrangements, and other trading affecting his business that modernizing his production equipment and reducing unemployment? And for good reason: this financialization pushed to its present extremities transferred almost all wealth from the working world to the famous privileged "1%" who naturally found their account there. And who get richer and richer due to this financialization, without any consideration given to society as a whole. That is why the average person's income has not increased as much as work productivity. That is why we are constantly required to improve the productivity of our businesses. A marked improvement in their income revitalized the poor and middle classes, while having a relatively benign impact on corporate profits, of which the majority enjoyed result in total disconnection from the somber economic realities. The production and productivity abilities of our businesses must actually be improved. But they will not be sustainable or equitable unless the consumer buys goods and products and pays for services. Therefore if his income benefits from a substantial increase.

## We Need to Free Sisyphus

Milton Friedman published an article in the New York Times Magazine in September 1970 titled the Social Responsibility of Business is to Increase its Profits"! There he referred to his book "Capitalism and Freedom" where he assured that "there is one and only one social responsibility of business – to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game...". In fact, Friedman uses this analysis throughout to denigrate any hint of "corporate responsibility" where businesses should not stray. For him, an executive or a manager concerned about the social order does not act in the interests of his employers... Optimizing profits must thus be the only priority in the knowledge that whatever frees "social responsibility" must be restricted to the bare minimum required by law. According to Friedman, the position of a few CEOs who are concerned with moral and material comfort of their employees – in short, those who look to do more and better than required by law – equates for them admitting the predominance of "political mechanisms" over "market forces". How thus can we be surprised by the often irresponsible attitude of the business and financial world justified by the doctrine of a very influential Nobel Prize winner? Which doctrine espouses the merits of non-profit organizations, but imposes them as absolute dogma against which all other considerations and any value were to be eclipsed? Remember James Tobin, the Nobel Prize Laureate for Economics in 1981, who humorlessly declared: "Let's consider three propositions: Money is not important. Money counts. Only money is important". Friedman too often shifted from the second to the third"... This quest for profit – which became an absolute criteria – contributed to the fragmentation and compartmentalization of society where individuals had to – according to this logic – seek their fortune and safeguard their interests, far from all morality and at the risk of harming others. Since after all, and it is Friedman who asserts it in this article "society is a collection of individuals" whose only obligation is to seek out the best for themselves. For Friedman, individuals only have one obligation which is to ensure their prosperity and that of their employers.

Furthermore, and as if confirming what he said, the U.S. trading index, Standard & Poor's 500, recorded an increase of nearly 170% between August 1980 and August 1990 – i.e. in a space of ten years –

during which it soared by 340% more during the next ten years! How can we not be tempted by such a godsend which forced the hand and pocketbooks of the U.S. middle class into investing hope, savings, retirement funds and even their borrowing in market investments, including in the most speculative capitalizations? The rate of equity investments experienced an uninterrupted rise in U.S. households of whom 57% did speculative trading in 2001, compared with 39% in 1989. The following generation of investors was clearly less lucky than their parents, and for good reason... the S&P Index lost nearly 30% between August 2000 and August 2010. In reality, the losses were even more marked since with inflation at 25% during that period, the overall net losses of these investors amounted to more than 50% during the first decade of the 21<sup>st</sup> Century. However, this market nightmare which has been developing for about ten years now is further accentuated by a brief analysis of wages in the U.S. According to data from the U.S. Revenue Department (Internal Revenue Service), the average worker's wages increased by 140% between 1980 and 2000, moving from \$12,850 in 1980 to \$19,875 in 1990 and reaching \$30,650 in 2000. A figure of 140% from which inflation of 110% should be deducted, leaving a net improvement in the average wages in the U.S. by 30% in twenty years. A trend which is however also reversed – in any event which was largely challenged – at the dawn of this century since the increase in these wages, net of inflation, was no more than 3% over the following ten years. In reality, the Western citizen has been suffering from an insidious deflation in his income for more than ten years. At the same time, the gap widens irretrievably with the very wealthy, the famous “1%” who hold among themselves 42% of the national wealth! According to statistics established by the U.S. Federal Reserve Bank, these 1% would have increased their fortune by 2% between 2008 and 2011 while the middle class would have seen theirs melt by up to 39%!

Today, in a country like the U.S. the Gini coefficient – which is a measure of the degree of inequalities between the rich and poor in the same country – is comparable with the current coefficient in China! That China, which is building its economy and working on developing its social fabric, experiences massive imbalances between its classes is understandable. It is however disturbing to say the least that a nation such as the U.S. entertains – or indeed is content with – such inequalities between its own citizens. In 1970, the gross income of CEOs of large U.S. corporations was thirty times the average salary of a worker in the U.S. – this proportion being forty-five times for Great Britain. Today, these gaps in salaries have reached 260 and 80 times, respectively, for the U.S. and Great Britain! Since the end of the 1970s to this day, the income of the wealthiest 20% in these two countries has increased by approximately five times that of the poorest 20%. What does one make

of a boss who is 260 times better paid than the average worker? In a world where income is supposed to reflect the added value of the worker, is a CEO really worth, and does he really bring, 260 times more than the average employee, to his business or even society? Indeed, we are today living in a world where all the benchmarks and values (genuine values, not valuations) have been turned upside down. As such, nothing justifies such monumental gaps between the income of the top corporate leaders and their employees, as it is understandable that the average person may be offended by such an inequality, that I would not hesitate to call it “against nature”. In the same way that it is unacceptable that, in our Western nations with integrated and well developed economies, the income of the average person is entirely dependent on growth. His standard of living and his salary fall when economic activity slows down. It is therefore those with a ringside seat who pay the price of the recession, or indeed the idiocy – when it is not dishonesty – of others. Weighed up, would it not make sense, or indeed be natural, that improving the average worker’s income be a combination of the product of growth and better redistribution? Is not an equitable distribution of wealth and income within Western nations which claim to be civilized one of the fundamental keys of economic stability? Was Warren Buffet not surprised in his editorial of August 24, 2011 in the New York Times to learn that he paid 17% tax on his income (of \$40 million) when his employees paid about 36%?

Inequality is therefore, the same as greed and excessive deregulation, one of the fundamental reasons of economic and financial earthquakes that shook our Western countries these past years. In fact, and despite cosmetic measures or even by depth of our financial system, our economies will more or less for short periods be inevitably destabilized by more or less violent due simply to sudden differences in income. The damage caused by these flagrant inequalities to our economies is for the most part amplified by the totally inadequate responses by our political and economic leaders, who simply take note. Furthermore, the crisis, only worsened the situation of the middle class since the amount generously dumped into the system never benefited research or training, not even the modernization of our production equipment generating long-term jobs. Instead of putting our backs against the wall by the accumulation of these debts which will not resuscitate consumption, would our leaders not be better to tackle the sources of this endemic calamity, that is to say the flagrant inequality of income solidly anchored in our societies? Applying the same Pavlovian – or demagogic – balm will end up polarizing or fracturing a society more and more tempted by extremes. Education, and inequality in wages which is its counterpart, must be at the center of policies, with decisions hoping to offer our societies stable growth being the key to individual fulfillment. Social priorities must

finally be at the heart of any economic project. Because, as President Obama said substantively in his inaugural address on January 21, 2013, it is unthinkable that we make choices dictated by the markets and by neo-liberals who force us to sacrifice our citizens today on behalf hypothetical interests of future generations. Every citizen has a right to expect “security and dignity”.

Can democracy accommodate such flagrant injustices? Can the respect owed to each citizen – and to any legal immigrant in our country – be satisfied with a situation – pushed to the extreme since the middle of the 1980s – where the state gives up its supreme obligation of protecting and defending the interests of its people? Of its entire people, including – and particularly – the most needy? Nefarious laws passed in 1834 in England, such as the “New Poor Law”, which forced the poor to accept any job – even at a pittance – under the threat of being forcibly enrolled in humiliating “work houses”. As for the Personal Responsibility and Work Opportunity Act, passed in the U.S. at the end of the last century (1996) affecting the unemployed and the needy who were mainly women, Blacks and single parent families. All these beneficiaries of social assistance were deprived of vital aid from their government, under the scandalous pretext that they would thus be more motivated to find a job! This “charity” lavished on the unemployed – à la “assisted”, as it is fashionable to call it – by a society which continually lavishes him with contempt for being unemployed. Is it tolerable in a peaceful democracy? In a world enduring a severe crisis where the unemployment indices mechanically explode because of the private sector – and particularly – the financial sector – having staked everything, risked everything and monopolized everything for only its gain, can society continue to discredit and humiliate its citizens without jobs? And can it force them to accept any kind of work so as to stop showing them its solidarity? Is it in a peaceful society that we wish to live or in a fragmented world where the happy “insiders” would be constantly fighting the “outsiders” left on their own? Governments must make every effort to reintegrate our unemployed – through work or social activity – and stop blaming men and women who are victims of their situation. Get rid of this unhealthy fetish toward deficits and focus our energies instead on re-establishing full-time work, the only true framework that we can make for future generations.

Call on the great Keynes who warned us in his “General Theory” against the “society in which we live are its failure to provide for full employment”... Why, in this regard, not quantify and measure the degree of humiliation inflicted by our societies on its members? The moral abuse – and sometimes physical – inflicted on our fellow citizens who are less well-off, is it also not a net cost for our society, in the sense

where it undermines the effectiveness of labor and national harmony. Who today challenges that health coverage, public transit, national education and the other social benefits of the state contribute decisively to social peace and individual fulfillment? In reality, the ultimate question is: what price are we prepared to pay collectively to (try to) achieve a balanced and the most possibly just society? Since the period of relative economic stability and comfort for the middle class now well and truly over. Therefore, priorities need to be redefined, and in light of inevitable social upheavals, such as an ageing population, which will be one of the factors requiring the most social assistance. Demography galloping inequalities are therefore the two fundamental reasons which require the return of the state, since it is better to count on the government than on the private sector since it involves supporting the population. As the distinction – or so-called separation – between politics and the economy is only an urban legend maintained by the financial world to capture true power, it is incumbent upon the state to promote economic efficiency and competitiveness while actively supporting – even militantly – the most needy of its citizens To do this, a crucial equation to be resolved will be – to borrow from President Barack Obama during his inaugural speech on January 21, 2009 – not whether the “government is too big or too small but whether it works”, since the state must also learn to work efficiently to fulfill honorably its tasks. As the distinction – or so-called separation – between politics and the economy is only an urban legend maintained by the financial world to capture true power, it is incumbent upon the state to promote economic efficiency and competitiveness while actively supporting – even militantly – the most needy of its citizens To do this, a crucial equation to be resolved will be – to borrow from President Barack Obama during his inaugural speech on January 21, 2009 – not whether the “government is too big or too small but whether it works”, since the state must also learn to work efficiently to fulfill honorably its tasks.

It is therefore crucial to have a better understanding of the processes which led to the deterioration of our economic conditions which coincided with the shrinking of the state. The most shocking – and most revealing – manifestation of this withdrawal of public power was the long process of privatization affecting all sectors of Western economies for thirty years now. At first glance, it is easy to understand the motives of this genuine cult which seized all governments and which is to be found on the side of monetarism and neoliberalism. The private sector has thus intended to optimally manage whole sections of the economic activity through regulation instilled by markets considered “perfect”. Furthermore, the state offloaded a huge part of its tasks that it could no longer perform effectively due to lack of competent and competitive bureaucrats, unfortunately quite an acceptable argument since our

Western administrations “functioned” less and less properly, to borrow an expression from President Obama. In doing so, the transfer of its assets allowed the state to save, in line with the prescriptions of orthodox economists. In short, these large scale privatizations spread over three decades would benefit all: the state, which would have less responsibilities, and the private sector, which would earn more money by taking over from the government. In fact, the reality was unfortunately less rosy, in any case from the point of view of a population who therefore had to fight against a private sector only concerned with its profits. Companies expected to assure citizens of services until then provided by the state knowingly proceeded with a devaluation and depreciation of the services to optimize their profits. Obviously it is the average person who was aggrieved by this abdication of the state and large responsibilities in favor of the private sector.

An absolute leader in this regard, the Anglo-Saxon world pronounced with a light heart the end of the “era of big government”, the famous formula of President Clinton. It then became fashionable to lock the State in a type of chastity belt of which it would divest itself only to provide – reluctantly – the bare minimum. The consensus in this sense was of the rest the largest possible between the political, economic and financial elites: the company had to get rid of the state, its bureaucrats, its subsidies and its services... that it would no longer assure what was left. This regression by the state became even iconic of a West that showed its higher degree of civilization! The corollary is that society would henceforth be gradually divided into sections between those capable of taking flight with their own wings and the assisted of another age that had inexcusably missed the train of economic independence and globalization. Without wishing for it – but could it sill? –, the state became the promoter of a financial communization which sorted those who had adapted to this ultraliberalization and those who merely subjected to it. This genuine Darwinian selection extolled those who managed not to use public services and the others, considered as dead weight in society. This apartheid which was crushing and humiliating the less fortunate and the defenseless naturally rotted the social link by desecrating the state. In fact, by pleading with activism for the loss by the state of its essential power and prerogatives, our society had lost a fundamental landmark which had also served as cement through the centuries. The state for all had all but disappeared in favor of each man for his own. It is there that we all lost something vital: this solidarity which made us all look in the same direction and strive for objectives, not similar, but compatible. It is around the beginning of this era that Margaret Thatcher was to proclaim very significantly that “There’s no such thing as society... only individuals and families”!

What we have lost along the way? What still connects us? And what do we absolutely refuse? Must we be resigned to our present world marked by corporate and individual domination having taken collectivity hostage for their own interests? Has democracy become merely a vain word or will it save us? At a time when solidarity and fraternity – still only capable of saving the European structure – are sorely lacking among the political, economic and intellectual leaders of the EU, it is the people who must set the example and become the engine. This Europe – so taxed as a democratic deficit – must take its destiny in its own hands (popular) to reestablish general interest, prior to enthusiasm. Now that the elites let go – burdened by the fiasco of their neoliberal ideologies –, we must regain control over our destiny and restore the social link, far from any political calculation. However, it is those who are responsible for our destinies that must be the most ready and the first to react by favoring citizens and entrepreneurial energies to the detriment of financial markets, speculators and investors. But must we – and can we – wait for them when they are so obsessed with the fluctuations of these same markets which guide their actions and which dictate their law to them? How do we not be disconcerted in front of the declarations of Chancellor Merkel who, on a visit on June 27, 2012 with her French counterpart on the event of a crucial summit on the future of the Euro and Europe, cut through with a: “We need more Europe, we need a Europe which can function, markets are expecting this from us”? Therefore, must Europe react to the markets, unite more and become more inclusive? Should we as a corollary deduce that the European Union would have collapsed without pressure from the financial markets which gradually forced it to react? Should we compare our political leaders of today with Pavlov’s dogs, conditioned by the vagaries of market fluctuations that grip them?

Do we pause for a moment on this famous “golden rule” inscribed in the German, Spanish and Italian Constitutions (which will certainly be adopted soon by other countries), which requires that balanced budgets be engraved in the stone of what our democracies hold most precious, namely their Constitution? The golden rule which – incidentally – is an admission of scathing failure for a European central bank incapable of fulfilling its most basic obligation. Nonetheless, what religious dogma decrees that public accounts must always be balanced? Is this golden rule something other than the ultimate manifestation of the influence of financial markets on the political systems supposed to obey the majority of the popular vote, but which, in reality, comply with the requirements of a tiny minority of capitalists? Should we not instead inscribe in our Constitution the right to work, to shelter for all? Since it is only in such an assumption that we would really start to reduce – mechanically – our public deficits. Under the guise of this crisis, the Heads of State and the



European Governments have progressively changed them. As financial analysts, they anxiously scrutinize market vagaries and are suspended with respect to the verdicts by the rating agencies. In this regard, the will to implement this golden rule only proves that our political authorities have been transformed again into “traders”! Has this golden rule been adopted with the objective of calming markets, as it is clear that its ardent defenders are only anxious to caress the markets “up the right way”? Is the new mission of the Constitution of our democracy to become the peacemaker of the markets? And does this golden rule not come to the rescue of speculators justifying a posteriori their bets? In setting it out, our leaders are in fact sending them an unequivocal message which basically says: “You are right to bet against our sovereign debt. Therefore, we shall apply this golden rule and comply with your requirements. We are eager to prove to you the seriousness of our management”... Today it is indisputable that the financial markets impose their temper on our democracies.

So, have we arrived at the stage where the dream and enthusiasm for the European structure have been replaced with a financial system that meticulously sculpts, day in and day out, the Europe according to its standards? Is this a well-oiled European financial system of which we dream, or do our old democracies deserve nonetheless something better? Must we resolutely turn our backs on elite leaders who systematically misplace priorities? How do you explain to them that equality and justice, essential preconditions for the emergence of genuine democracy are also the keystones to making the world happy again?

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