

Why the Green New Deal is a Response to the European Debt Crisis

By Gerhard Schick, financial policy spokesman of the Green Party in the German Bundestag

The global economic crisis has not been overcome; its character has merely changed. For us parliamentarians, its most tangible characteristic is the smoldering debt crisis in some Euro countries. Similar to the crisis in the banking sector, the European government debt crisis is typical of a large-scale financial crisis, the "Second Great Depression," and managing it has to be addressed in this context. If it were only an uncontrolled government debt accumulation in Europe, then it would now be appropriate to simply apply debt brakes to manage the public debt, and to work with stronger sanction options. But would this have prevented the problems in Ireland or Spain? No. The financial crises in Spain and Ireland have absolutely nothing to do with government irresponsibly incurring debt. The government debt only increased when the government had to react to the excessive indebtedness of the private households and banks that it had previously permitted.

The conservative reinterpretation of the debt crisis as a purely governmental debt crisis due to excessive government spending is politically smart but factually incorrect. Drastic austerity programs alone are therefore not very useful in overcoming the crisis. On the contrary, the current crisis policy aggravates the crisis in many areas.

Moreover, we should not forget that we have barely made any progress in coping with the crises of poverty and distribution, or in the crises involving the climate and resources. Climate change has largely disappeared from the headlines, and, in terms of concrete government action, the brakes are being applied to many climate policy questions. Research results, however, show to what extent climate change has advanced and what tipping points are imminent.¹ And, as in 2008, the connection with the strong increase in commodity prices becomes evident, as commodities increasingly become investment targets, with food and energy prices in strong correlation. The bottom billion has not gotten any farther today than it was three years ago, when we deliberately included this problem in the concept of the Green New Deal. It was, and, therefore, is correct to combine these three crises and to show the way out of them with an extensive package of measures, the Green New Deal.² With its three pillars:

- financial market regulation,
- ecological modernization of the economy, and
- new social balance,

the Green New Deal is still the right answer.

However, we must develop our concept further because the situation has changed and new knowledge is now available. It is actually the currently emerging slowdown in real GDP growth, which could soon lead to a recession, forcing us to take a position with regard to stimulus plans or the like. It is also important to place the current European crisis in the context of our response to the global economic crisis. It is my intention to contribute with this text in some way in regard to the financial market situation, the public debt, and the crisis of distribution by first analyzing the current situation in the financial markets, and, based on this, discussing proposals for the solution.

What exactly is going on currently on the financial markets?

The renewed turbulence in the financial markets contradicts all the lies in recent months that pretended that the financial crisis was over. It was actually the Federal Government, who wanted to convince people that it was only a crisis in Greece, Ireland and Portugal. In fact, we still have not overcome the global economic crisis that erupted in 2007. The crisis has simply changed its character. First, there was the bankruptcy of the real estate lenders in the USA; it was called the subprime crisis. Then, when the banks started to wobble, it was called the financial crisis. Later, some industrial companies got into difficulties, unemployment rose – and so it was an economic crisis. Now, governments are wobbling and there is talk about a debt crisis. It remains, in the end, however, one and the same global economic crisis. It is therefore useless to narrow the view on the question about public debt alone, and to focus on public expenditure as the major problem. We need a reorientation of economic and financial policy, not only in relation to public deficits. “Keeping this up” only drives us further into the crisis.

A correct analysis is important in this context. A physician can only prescribe the correct medication by chance if the diagnosis is incorrect. We should therefore discuss the causes of the crisis more in order to know what measures are in fact the right ones to take.

Every financial crisis is essentially a debt crisis: the debt-to-GDP ratio increases markedly and gets out of control. The debt can take on a different form in each financial crisis; in fact, it is quite typical that the debt takes on a new, unusual form, and is at first not perceived as debt at all. At first, it does not matter if the debt lies with banks, with private individuals, with companies, or with government authorities. It has to do with the overall debt-to-GDP ratio of a country or of the global economy.

Every loan, every promissory note in the possession of an individual is, however, at the same time an asset item: if a customer signs a savings bank certificate, it is part of his/her savings. The savings bank is, however, raising external capital; it is a debt for the savings bank. If a citizen buys a Federal Treasury bond at the Federal Debt Agency, this bond will become part of his assets. At the same time, the debt of the Federal Republic of Germany increases. Every debt crisis is therefore an assets crisis as well.³ The asset-to-GDP ratio is too big – it is also called a crisis of accumulation in the technical jargon. In some financial crises, the massive increase in asset prices is more at the forefront of public awareness, e.g., with the property bubbles in the US, Ireland and Spain, or Japan in the 90s (housing prices too high), or the dot com bubble (share prices

of the telecommunication companies too high). Since most of the house purchases in Ireland and Spain were in great part financed with loans, it would be just as correct to speak of debt crisis in each case. This is more a question of perception than a difference. As a rule, financial crises due to bursting asset price bubbles are especially profound and long-lasting. In the case of Japan, the burst housing and share price bubble of 1990 resulted in a so-called "lost decade." The economy and the investors have to this day never completely recovered from this bubble.

Historically, a credit boom has been the most reliable individual indicator of financial crises. This has been demonstrated by an economic history study of twelve industrialized countries from 1870 to 2008.⁴ Every time banks granted an above-average number of loans over an extended period of time, the probability of financial crises drastically increased. Debt brakes are therefore important to prevent financial crises – namely for the government, banks and private debt.

The following picture may be helpful in imagining the development of a financial crisis: if children keep piling up sand to form an increasingly higher mountain (accumulate assets), they collect sand from the area next to the base of the mountain (get loans) and keep shoveling it onto the mountain. Credit expansion and capital accumulation go hand in hand. At some point everything becomes unstable; the mountain starts sliding, and, to a certain extent, levels the differences between the mountain and the hole again. This is the financial crisis: share prices drop, assets are destroyed. But sliding to a new stability, which is no problem with a sand mountain, represents heavy disruptions in the economy, as we experienced in the fall of 2008. Here are a few figures:

- From 1980 to 2000, the debt-to-GDP ratio in the US rose from 170 to 270 percent, even 370 percent immediately before the outbreak of the financial crisis in 2007.⁵ It looks the same in other industrialized countries. In 2010, Japan reached an indebtedness of 456% of the yearly GDP, Portugal 366%, Belgium 356%, Spain 355%.⁶
- Only part of it is government debt. From 2007 to 2011, the government debt of the OECD countries has increased from 73.1% to 102.4% of the GDP.⁷ The debt level was already clearly too high before the outbreak of the crisis, and then it quickly increased again. This has a lot to do with the fact that the banks' debts were taken over by the governments and that the recession was counteracted with credit-financed stimulus plans. Private debt was thus turned into government debt. And, if no countermeasures are taken, the growth of government debt will continue in this manner. The Peterson Institute predicted a government debt of USD 50 trillion for the US in 2030.⁸
- In Germany, private debt increased from 17% in 1960 to 65% of the GDP in 2010.⁹ In the US, it is 117% of the annual GDP. In Ireland, it increased from 92% to 166% of the annual GDP from 2002 to 2007.¹⁰ The main reason was the loans taken out to finance properties, which have now strongly lost value after the property bubble burst – many private households are therefore heavily over-indebted.
- Many banks are heavily indebted because the return on the invested equity capital grows in this way (leverage effect). Banks thus contribute to an extremely debt-financed economy. This became evident in Ireland, for example: the ratio of the balance sheet total of

the Irish banks to the Irish GDP increased from an already high 360% in 2002 to above 800% in 2009.¹¹

An overall economic deleveraging is therefore necessary, that is, a correction to a sustainable debt-to-GDP ratio. This means a reduction of the total national debt-to-GDP ratio for governments. The debt must also be reduced in the case of private households, e.g., by way of personal insolvency, debt restructuring, or the sale of assets to cover the debt. For banks, this means deleveraging, a return to a sustainable ratio of equity capital to balance sheet total (leverage ratio). This process should preferably take place by selling asset shares, acquiring equity capital on the market, or retaining profits.

Debt, Assets and Distribution

Debt crises are also always assets crises, and the distribution issues should therefore always be looked at. To the extent in which debt and assets increase, the distribution will usually become concentrated in very few hands. This unequal distribution is increasingly destabilizing the financial markets because in this way the asset-to-debt ratio increases on the one hand, as does the GDP on the other hand. Because if debtors are so poor that they can no longer pay their debts, the debt instruments lose value, and the financial markets panic. This was clearly visible during the subprime crisis: the stagnating real income of a large part of the population and a poor "social policy" drove US citizens to over-indebtedness, and thus contributed to the financial crises. Before the most recent outbreak of the financial crisis, incomes in the USA were as unequally distributed as they had only ever been in 1929 before the Great Depression. A large part of the population actually experienced a welfare loss in spite of the economic growth. Since the people did not want to reduce their standard of living, they willingly accepted the path opened up by the policy of closing the constantly growing gap between income and consumption by an ever greater indebtedness. In contrast, the wealthy are unable to consume all their income, and an ever greater part of their income is in search of investment opportunities. In particular, the so-called high net worth individuals¹² and the funds they finance were invested in high-risk securities, which led to the subprime crisis.¹³ When the loans of the over-indebted house owners were no longer paid down and foreclosure sales increased, the subprime papers lost value. The banks that had invested in those securities got into difficulties.

Both phenomena fit together: The hyper-rich bought the debt securities with the mortgages of the impoverished American middle class behind them. If, for example, minimum wages had resulted in the fact that more of the revenue generated in companies had gone to the workers and less had gone to the hyper-rich, the workers would not have had to get into high debt in order to preserve their standard of living, and the hyper-rich would not have been able to buy so many debt securities. The financial bubble would have been smaller or would not have developed in this way.

The same applies to the regional imbalances between countries with current account surpluses (namely, capital export in order to invest the proceeds from exports somewhere abroad, Germany, for example) and current account deficits (namely, capital import in order to finance the too high consumption compared to production, Greece, for example). Germany's growing

capital assets and the growing debt of the countries in the periphery of the Euro zone as well as China's increasing investment volume and the growing debt of the US destabilized the global economy and thus contributed to the development of this financial crisis.¹⁴

An often-heard explanation of the present crisis is that the US Federal Reserve pumped too much money into the market, in particular after the attacks of September 11, 2001 and the burst of the dot com bubble. This is actually correct. I do not think, however, that this is the key reason. In phases of credit expansion as well as in phases of credit crunch the actual available credit and the capital market interest rate in a country do not depend only on the interest rate of the Central Bank. The convergence between supply and demand of capital in general is also absolutely crucial. And in this context, the commercial banks' loans play an important role on the one hand, and thus financial market regulation as well. Because it participates in the decision on how much or how little credit can be made available of a given amount of Central Bank money. In a global economy, on the other hand, it also depends on the impetus coming from abroad. In view of the appetite for capital in the US, the capital market interest rates should in fact have increased there long before 2008. But the large supply, especially from Asia, where a large amount of reserves in US securities were built up after the Asian crisis, has to be seen as a dominating influencing factor because interest rates have remained very low. It can actually be demonstrated that in the 2000s the long-term rates would have been much higher without the inflow of money from abroad.¹⁵

What is the way out of such a debt crisis?

How does one cope with a financial crisis? How can the too high debt-to-GDP ratio be reduced without triggering a new crisis? There are in fact only 4 ways:

1) Economic growth

If the real economy grows quicker than the increase in debt and assets, the ratio between the debt/assets, on the one hand, and the GDP on the other hand can be corrected. We Greens have also tried to somehow oppose the recession with the Green New Deal by means of "green recovery plans," and at the same time start an economic conversion program so that our economy becomes ecologically sustainable. This way is, however, only possible with limitations. Because there is the risk of being tempted to boost the additional growth by means of easy lending or additional government debt. The debt mountain will then grow quicker than the economy, and a new loan bubble will develop. Tackling the crisis will consequently stir up new crises. It is exactly this danger that is growing in the US. As long the growth is borne by a demand based on debt and not by an increasing demand in terms of real income gains, the problems will be exacerbated.

This has in part occurred in Germany. In 2009 and 2010, our country somewhat worked its way out of this crisis by means of high economic growth. The public debt has, however, grown quicker than the GDP. Nevertheless, the past short growth phase was more of a symptom of the crisis: because the German economy benefited from extremely low interest rates, which in particular were a consequence of the fact that Germany is seen as a safe haven and many

international investors wanted to invest money in Germany, even at extremely low interest rates. The recovery plans were also useful. In the last few years, the concentration of income and assets, however, kept increasing instead of decreasing. As much as some problems decreased because of the German economic growth, other problems have consequently been exacerbated. With regard to overcoming the financial crisis, we have therefore not gotten much further than we were in 2009.

2) Inflation and devaluation

Inflation devaluates debts and assets as far as they are valued in monetary units. If the money is worth less in relation to real goods (namely when prices rise = inflation), the debt-to-GDP ratio naturally drops. This is a very simple way out of the debt crises for most governments since it is at first almost imperceptible. But it has drawbacks. From a certain order of magnitude inflation often gets out of control and destroys the real economy. Nothing is gained then. And there is the risk of creating the basis for a new financial bubble through too permissive creation of cash. Besides, the distributive effects are often fatal: if the social benefits are not adjusted, the weakest in society will bear the heaviest adjustment burden. Finally, inflation is actually not very useful for the mainly short-term financed government debt. Because when the old bonds have to be paid back and new ones have to be issued instead, the higher inflation is again priced in by higher nominal rates in the conditions for the new bonds.

A special form of inflation is the devaluation of a currency in relation to other currencies. This is at first hardly noticed domestically. But import prices rise, which strengthen the domestic exports. And the debt and assets drop domestically relative to foreign countries. Iceland took this path, as did Great Britain. The value of the Icelandic crown in Euros was halved in 2007/2008. The British pound has been devalued by approx. 30% since the outbreak of the financial crisis. Thus all debts and assets held by foreigners in pounds dropped by 30%. If Great Britain had been in the Euro zone, it would then have probably been the first country requiring a bailout package. Because without this devaluation Great Britain would have required another form of debt cut. From a prospective point of view, Great Britain would have come under pressure on the financial markets similarly to Greece, Ireland or Portugal.

Devaluation is, however, a way that also entails dangers. Firstly, similarly to the First Great Depression, there is the danger of competitive devaluation: each country tries to solve its economic problems at the expense of the other countries. At that time, the consequence was an extensive collapse of international trade and of international financial relations, which only exacerbated the global economic crisis. Currently, this is most felt by Switzerland. It actually has no debt problem, but is afflicted by the devaluation of the other countries, namely: the revaluation of the Frank, and it is being presented with the invoice for this global financial crisis. In order to prevent such a competitive devaluation¹⁶, international monetary agreements, and over the long term, a stable global monetary system are very important.

Secondly, it makes a great difference if a country is predominantly indebted in national or foreign currency. Because the debts in foreign currency naturally increase with the devaluation.

The peculiarity of the European debt crisis is that this mechanism of devaluation or inflation is not available to the members of the monetary union.

3) Debt restructuring/ participation of creditors/ insolvencies

The participation of creditors in bank failures, and also in the case of Greece, has often been discussed in terms of justice. "Those responsible should also pay a little..." But there is also an economic reason for it. In order to reduce the debt/ assets-to-GDP ratio, the wealthy can be made to renounce a part of their assets/ debt securities – a debt cut. This is in the creditors' interest insofar as they can hope to be repaid at least part of the credits.

Debt cuts take place in over-indebted private households within the framework of personal insolvency; there are also insolvency proceedings available to companies. Orderly proceedings, however, do not exist for countries or large international banks. Nevertheless, there are many international examples of successful debt restructuring by countries and bank bailouts with the participation of creditors. This can occur in different ways: repayment waiver (haircut), reduced interest payments, term extension or conversion of debt securities into equity capital.¹⁷

A problem with this approach is that, unless a legal basis for the participation of creditors has previously been established which is subject to proceedings under the rule of law, confidence is lost when the investors realize that it is no longer possible to rely on property rights. Another problem is that debt restructuring may trigger uncontrolled waves of bankruptcies: if all players are heavily indebted, for many creditors a waiver of claims means that they themselves are heavily indebted. The result is a domino effect: there is one bankruptcy after another. In this way, the amount of the debt is reduced but these waves of bankruptcies also ruin sound companies or countries with an actually sustainable government debt. The real economy is damaged. And there is nothing to be gained with it because in fact it has to do with stabilizing the debt/ assets-to-GDP ratio. If the GDP recedes in the process (recession), this is counterproductive. Legal regulations are therefore necessary within which a participation of creditors is possible. Fallback systems are also required which intercept such waves of bankruptcies. Greece's debt restructuring must therefore necessarily be accompanied by a convincing European bank bailout mechanism.

I have therefore always argued for a merely partial and thus controlled participation of creditors - in bank failures, business bankruptcies, personal insolvencies, and in countries. This reduces the debt in a controlled manner at the expense of those who own the debt securities, and thus stabilizes the economy.

4) Redistribution

Since a high debt/ assets-to-GDP ratio is always a problem of distribution, redistribution is the key to the solution. As much as this also eliminates injustices, it has nothing to do with justice in regard to tackling the crisis. It is simply necessary to reduce the debt/ assets-to-GDP ratio. A tax on large assets with which debts will be paid back is therefore an important instrument to overcome the financial crisis.¹⁸ This applies in a similar way to other measures. If, by way of example, the wages in the US were raised at the expense of corporate profits, many an over-indebted

house-owner would be able to pay back their debts more easily, whereas assets would grow less strongly. The debt/ assets-to-GDP ratio would drop.

These measures, however, also have limitations. If too much is claimed too quickly, the asset prices collapse or companies incur losses, people become unemployed, and nothing would be gained. A stabilization of the economy by means of a distribution policy is, however, absolutely necessary if financial crises are to be prevented.

Every financial crisis lasts as long as a combination of these four methods returns the debt/ assets-to-GDP ratio to a sustainable relationship. If markets are left to themselves, there is the risk that this ratio is quickly corrected by a crash of the financial market and subsequent deflation, namely by a general reduction in price levels: the prices of shares and bonds would drop; property prices drop; more and more banks, private individuals, businesses and countries can no longer pay their debts. People reduce their consumption so that many actually sound businesses have to give up. The above-mentioned wave of bankruptcies. If the debt burden is to be reduced in a controlled manner, the four possibilities have to each be used very carefully. This takes time. Kenneth Rogoff and Carmen Reinhard thus predicted a long period of economic stagnation before the current debt crisis is overcome.¹⁹ Japan's example shows what can happen in the worst case.

Where do we stand today regarding the solution to the problem?

A solution to the debt crises has actually only made progress in some countries by means of devaluations as well as by the reduction in property prices. The latter has, however, driven many private individuals into over-indebtedness. The debt burden to GDP ratio has not yet reached a level that could be considered to be stable.

The banks' debt is still at very different levels. Billions of that debt was taken over by the governments (e.g. transferred to the bad banks).

A participation of creditors has only very rarely taken place. It can therefore be said that this debt still exists to a large extent. At the same time, the banks are still working with a very high amount of debt. Deutsche Bank, for example, is still financing more than 98% of its operations with external capital and less than 2% with own capital. This indicates a clear danger: if the central banks support the economy by means of low interest policies and the countries by means of recovery plans (which is correct), it may occur that part of the bubble diminishes in a controlled manner (e.g. the property prices in the US, Spain, Ireland, UK), but another bubble is developing at another point at the same time. It is therefore very important to associate the incentive with new regulations so that the additional liquidity is used to reduce the debt level and not to build up new assets financed by debts. This mistake was made when the dot com bubble burst. As right as it was that the US Central Bank counteracted with plenty of additional cash creation, it was wrong not to associate this with measures to control debt financing. The amount of debt therefore grew quicker than the economy between 2001 and 2006. Tackling the crisis nourished the next, still greater, crisis. Debt brakes are therefore extremely important, especially for banks.

The debt of private individuals who had invested in properties is still in part very high, e.g. in Ireland, Spain, Great Britain and in the US. An adequate form of insolvency does not exist in Ireland so that the individuals whose mortgage is higher than the actual value of their house cannot get rid of this debt. In this respect, the problem of the debt crisis has still not been solved.

The debt of the countries has grown massively during the crisis because the recovery plans and bank bailouts and decreased tax revenue inflated the deficits. The "indebtedness" of the central banks has grown strongly. The money supply and the central banks' balance sheets have been massively inflated.

What can be done?

Debt/ asset crises cannot be overcome quickly. It takes time. Time, however, only helps if it is used correctly. What is necessary is a mix of the already mentioned four methods:

1) Economic growth

The great danger currently is that a coordinated, synchronous government austerity policy stalls the economy. Heavy saving in Greece and Ireland can be handled by the European economy. If, however, Italy, Spain, France and Germany all apply the fiscal brake at the same time, it will become dangerous in terms of economic policy. Not all countries can generate export surpluses at the same time, nor can all players in an economy save at the same time.

The Green New Deal idea therefore remains correct: firstly, we must ensure that investments are made, and secondly that the investments are made in a sustainable, i.e. resource-saving and climate-friendly economy. Because otherwise the climate and resource crises would deepen. Our role as Greens must consist of ensuring that the crisis is used as a chance for the ecological transformation of the economy. The measures must, however, be financed such that they do not, in general, stand in the way of the debt ratio.

Growth impulses based on multi billions-financed debt to encourage private consumption can therefore no longer exist. But it is necessary to mobilize private and government capital for real investments. For this purpose, billions have to be redirected by properly setting out the regulatory and industrial impulses. Those who wish to be successful in reducing the government debt ratio need to get the private sector to make investments. Moreover, growth is only useful if it does not exacerbate the distribution imbalance. Statutory minimum wages, measures to strengthen the workers' side in the wage policy and a correction of the current tax policy are therefore very important.

2) Inflation

The European Central Bank has committed itself to a target of 2%. Some economists argue that the Euro zone would get out of the crisis more easily if this limit were set at 4%. A change in the inflation target is, however, not easy and entails the danger that the Central Bank loses credibility and is then unable to maintain the 4%. It is, however, important to realize that the danger of inflation is currently not nearly as high as feared by Germany. The monetary policy of the

European Central Bank is presently still expansive, even if, in my opinion, the tax increase some weeks ago was not going to be a very helpful signal that this cannot go on forever. This signal will probably have to be reviewed soon. But I consider that, apart from that, the policy of the Central Bank is essentially correct: it maintains the inflation target, but pumps sufficient liquidity into the markets.

3) Debt restructuring / deleveraging

The correct argument that uncontrolled bankruptcy can trigger detrimental domino effects has been the pretext in this crisis for virtually not allowing the participation of creditors at all. Therefore, Ireland was prohibited from involving the creditors in the bank bailout – a reason for the exploding Irish public debt and for resorting to the EFSF (European Financial Stability Facility) by Ireland. The German financial supervisory authority partially prohibited institutions to buy back their own low valued debt securities, although this would have been a market-friendly way of reducing the debt.

The banks were not systematically forced to retain their profits and thus strengthen their equity capital base. The big, dangerous mistake of the bank bailout under Steinbrück is just that: the existing possibilities of involving the creditors in the bailout, for example in subordinate debts, were not used. Strengthening the capital base of the institutions, namely deleveraging by selling part of the assets, raising new capital or retaining profits was not consistently enforced. Therefore, debts were not reduced but merely transferred to the taxpayers.

Has this changed under Schäuble, who has often mentioned the participation of creditors? No. With the planned 21%, the participation of creditors in Greece is far below what the market has already priced in. Some investors will still earn money because their securities quoted at 50% of the nominal value or less! In addition, the private creditors have long transferred their claims to the public sector.²⁰

In the meantime, German banks were only exposed with 20 billion Euros in Greece, while it still was 54 billion Euros in 2009. The contribution of private creditors will thus remain very limited.

The repurchase of government bonds at market prices can be an instrument in the solution to the debt crisis. In this way, the bond creditors participate in the burden of this crisis without an adverse impact on the market, and the debt of highly-indebted countries is reduced. As the Greek bonds are quoting with a reduction of up to 60%, a relevant contribution to overcoming the crisis can be accomplished. This should, however, not be carried out by the European Central Bank, but by the EFSF. Insofar as the depreciations are not absorbed by the banks, the banks should be recapitalized. The head of the IMF is right in demanding a massive recapitalization of the European banks. This should be enforced by the governments! If the banks do not receive the necessary money on the capital market, the European governments, have to carry out this recapitalization – the shares of the bank shareholders are diluted in this way. In order for the individual European governments to avoid being overwhelmed by the recapitalization of the banks, this should be done by a European bank bailout fund.²¹

Measures for a controlled reduction of the debt burden of the private households are also necessary. In this respect, I believe that it is correct to renegotiate mortgage debts in the US and to improve the possibility of private insolvency in Ireland. The measures of the Hungarian Government to reduce the debt burden of those indebted with loans in foreign currency are also heading in the right direction.

4) Redistribution

Redistribution has been the least used method. On the contrary, the concentration of assets has continued to grow in this crisis: the assets of the 11 million so-called high-net-worth individuals (HNWI) grew by 9.7% to 42.7 trillion dollars in 2010; they therefore now own more than before the outbreak of the crisis.²² Precisely the takeover of many bank debts by the governments has transferred the burden to the poorer segments of the population, which are frequently disproportionately affected by the cutback in the national budget, whereas the debts of the over-indebted private households are not taken over by the government. The reform programs in Greece, Portugal, Spain, Italy, Ireland, and also the debt ceiling in the US, intensify the problem of social inequality instead of reducing it. The improvements of the tax controls in Greece or the planned wealth tax in France are positive counter-examples. A wealth tax is also under discussion in Spain in the meantime. This will, however, not be enough to correct the undesirable development in the last few years. This also applies to Germany. Within the Green New Deal we therefore demand a new social balance which corrects the concentration of incomes and assets that has taken place in the last few years.²³ This also applies to other countries. The US needs tax increases for the super-rich; otherwise this crisis cannot be overcome. The rise of the Tea Party is even more dramatic. Their refusal of tax increases should finally be interpreted as a plan to drive the US still further into the crisis.

What does this mean in terms of the European debt crisis?

Similarly to the crisis in the banking sector, the European sovereign debt is a characteristic of the global economic crisis. We will therefore not solve the current problems in the Euro zone with drastic austerity measures and stricter penalties alone. As correct a debt brake is for Spain, it is not an answer to the causes of Spain's problems. The focus is set far too little on the stabilization of the financial market. Because weak banks are vectors of the crisis virus. They transfer the debt problems in one country to the whole monetary union because losses in the government debt business consume their own scarce capital and thus they themselves slip into over-indebtedness. If these debts have to be absorbed by their country of origin, its debt grows. The higher the banks' external financing is, the stronger is the effect. The interest of the society, therefore, is to put a brake on the banks' debt. The banks have opposite interests because their revenue grows with external capital financing while they transfer their own risks to the system.²⁴ We therefore need a binding debt brake for the banks, and not only in 2017. This would limit the systemic risk that is associated with the economically meaningful credit creation by the banks.

The same also applies to private households: property price bubbles which are not financed with loans are less dangerous because in case of a collapse of property prices, only the owners' own capital is reduced. If they have, however, assumed debts to finance the property, the owners may find themselves in the situation of no longer being able to service the debt. If this occurs with many debtors, the banks get into difficulties. The collapse of the property prices then causes a crisis in the banking sector. Lending limits and other debt brakes in private lending are therefore important. They limit the systemic risk that is associated with the economically meaningful credit financing of investments. They also have an anti-cyclic effect, and thus stabilize the economy in the course of economic activity.

In order that the additional liquidity of the central banks does not lead to the next bubble, problematic financial products have to be withdrawn from circulation. A regulation of exchange traded funds (ETFs) is necessary, to avoid a situation in which too much financial scrap can be hidden, and which played a central role in the most recent speculative case at UBS. The tax on financial transactions is necessary to dry up the very frequent computer trading which destabilizes the markets. Big banks must become smaller and be directly supervised by a European Banking Supervisory Agency.

The economic government of Europe is currently being discussed mainly within the context of controlling the national budgets. What is missing, however, is an approach regarding how the peripheral countries can make their economy competitive and how the current account imbalances, which led to the buildup of high assets in Germany and a high debt in the peripheral countries, can be prevented in the future. As a large ecological, social transformation program, the Green New Deal is an economic policy concept which we rightly formulated during the European election campaign 2009 for the whole of Europe. Precisely the conversion of energy use from oil imports to our own generation of energy in the area of renewable energies can be an important impetus for the southern countries of the Euro zone. Without sustainable, i.e. not purely financed on credit, economic growth, the countries affected by the crisis will never be able to put their public budgets in order. This structural change, however, requires time and real investments. It is of no use to evaluate every four weeks whether Greece will accomplish the turn or not. The country is in the process of reinventing itself. The first structural changes have been started. Such a process will realistically take five or more years until it comes to fruition. It was a tremendous mistake of the Federal Government in May 2010 to suggest that a short-term rescue package would solve the problems.

The coalition's tax policy has intensified the distribution imbalance. Additional plans, such as the abolition of the solidarity tax surcharge, would continue on this path. The Troika programs in the countries affected by the crisis likewise contribute to the exacerbation of the crisis. Because, true to the old economic political ideology which drove us into the crisis, the IMF, the European Central Bank and the EU Commission as well as the black-yellow Federal Republic and the conservative French Government still ignore the importance of a balanced distribution for economic stability.

A meaningful combination of the regulation of the financial markets, ecological modernization, and social balance will be important in overcoming the government debt crisis in Europe. This may presently not correspond to the public debate in Germany and not meet with acceptance by everyone. The situation is, however, so serious that we should fight for proper solutions, even if they are still unpopular at present.

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References

- 1 See for example, Edendorfer, Speech at the Federal Diet faction "Bündnis 90/ Die Grünen," (Alliance 90/The Green Party) retreat, September 2011.
- 2 Decision Green New Deal, Federal Delegate Conference, Erfurt, November 2008.
- 3 A good example is the combination of the debt clock and asset clock: <http://www.webdesign-plu-services.de/sozial-es/uhr.html>.
- 4 Schularick and Taylor: Credit Booms Gone Bust: Monetary Policy, Leverage Cycles and Financial Crises, 1870-2008.
- 5 Frankfurter Allgemeine Zeitung, 9/13/2011, page 29.
- 6 DB Research, 11/23/2010.
- 7 Ibid.
- 8 People having assets in excess of one million dollars.
- 9 Thomas Goda (2010): Global Wealth Concentration and the Subprime Crisis: A Quantitative Estimation of Causal Links.
- 10 I will not go into this issue any further within this paper.
- 11 Warnock und Warnock (2006): International Capital Flows and U.S. Interest Rates, NBER Working Paper 12560.
- 12 Some, like the Brazilian Minister of Finance, prefer the martial term "currency war" in order to show that there are massive conflicts of interest and that the countries are strongly acting against one another.
- 13 A special form of debt restructuring is being discussed under the keyword "financial repression." After the Second World War, when the US and Great Britain were heavily indebted, they forced their money lenders to lend them the money at convenient rates. This includes compulsory loans: People or funds having money are forced to lend this money under conditions at which they would not do so voluntarily. This is nothing more than if one borrows under market conditions and then enforces a waiver of interest, namely a form of debt restructuring.
- 14 Author's internal working paper on wealth tax.
- 15 Kenneth S. Rogoff / Carmen Reinhart (2010): This Time is Different: Eight Centuries of Financial Folly", Princeton University Press 2009.
- 16 An exception is the HRE shareholders who largely came out empty-handed and thus were involved in the bailout costs.
- 17 Reference to guest article Tagesspiegel.
- 18 Merrill Lynch Wealth Management and Caggemini, as cited in FAZ (Frankfurter Allgemeine Zeitung) on 06/24/2011.
- 19 Cem Özdemir und Gerhard Schick (2010): Counteracting the Crisis of Distribution – The Third Pillar of the Green New Deal.
- 20 The generation of systemic risks by a high bank debt can therefore be compared to causing climate changes by emitting power plants. The yield of the power plant increases, if there is no emission threshold, but this exacerbates the climate change.