Europe's response to the global financial and economic crisis

To be a global player in the response to the crisis, Europe should advocate and work towards an inclusive partnership with all countries, not only the most powerful ones. It should ensure that the measures it puts in place seek to address the needs of all, particularly those most vulnerable to the effects of the crisis, both within Europe and in developing countries. These are the challenges of the new European Parliament and Commission whose mandate coincides with the period between now and 2015, the date for achieving the Millennium Development Goals.

Mirjam van Reisen
Europe External Policy Advisors (EEPA)
Simon Stocker, Louisa Vogiazides
Eurostep

Since the outset of the financial and economic crisis, the European Union has consistently presented itself as a key player in the global response to the crisis and in any reshaping of the global financial architecture. European leaders cite the EU's achievements of the past 50 years, and its commitment to social justice and solidarity to justify its leading position on the world stage. As Britain's Prime Minister Gordon Brown argued in the European Parliament on 24 March 2009, the EU is "uniquely placed" to take a lead in the effort to "build a truly global society sustainable for all, secure for all and fair to all". These words are echoed by other leaders, all of whom accept that the global financial crisis has social and human impacts in all parts of the world, not least in developing countries. Their responses, they say, will fully recognize the needs and realities of developing countries. What this means in practice is already being seen in the way that the EU and its Member State Governments are addressing the crisis and its impact. Despite the clear signs of the systemic failings of current approaches to promoting equitable and sustainable development, there is little sign so far of any commitment to seeking any real change.

Europe's position towards the global financial architecture

Europe's leaders readily recognize that there have been failures in the global financial system. It appears, however, that the measures they envisage to address these failures fall far short of a radical transformation of the system. While not all of the EU's leaders are part of the G-20, there is broad acceptance of the G-20's leadership in responding to the crisis. The measures adopted at the G-20 London Summit in April 2009 reflect the EU approach to addressing the economic crisis and reforming the global financial system in order to prevent future crises. These include the recommendation of USD 1.1 trillion in additional funds for the International Financial Institutions (IFIs), of which just a small proportion (USD 50 billion) was designated to "safeguard development in low-income countries." The USD 1.1 trillion comprises USD 750 billion to the IMF, USD 100 billion to the World Bank and USD 250 billion to shore up global trade. Europe's leaders, along with others in the G-20, agreed to inject some USD 5 trillion into their economies by the end of 2010 in order to boost their economies and safeguard employment.

The EU position certainly includes a commitment to strengthening financial supervision and regulation, with various levels of support going towards improved monitoring of credit rating agencies, the establishment of regulatory standards to end tax heavens and banking secrecy, the need for new accounting norms for placing bonuses under guardianship.

While some of these measures are welcome – as long as they are sufficiently comprehensive – they do not reflect a commitment to transforming the global financial architecture. On the contrary, they reflect a determination to maintain current structures and approaches intact, and restore stability through better management of current global economic and financial models. It is a response which seeks to ensure that control of any changes rests with the world's principal economic actors – which includes Europe. Since the G-20 membership is comprised of countries which have substantially gained from the current global system, there is little real incentive for fundamental transformation. And, since the global financial architecture has not only failed to tackle inequalities, but often increased them, there can be little confidence that maintaining the current model will bring the result that Gordon Brown and other European leaders claim.

A truly global and effective response to the crisis should not only involve the most powerful states and large emerging economies, but the global community as a whole, including all developing countries. As argued by the Commission of experts on reforms of the international monetary and financial system, chaired by the economist Joseph Stiglitz, "the welfare of developed and developing countries is mutually interdependent in an increasing integrated economy." Therefore, "without a truly inclusive response, recognizing the importance of all countries in the reform process, global economic stability cannot be restored, and economic growth, as well as poverty reduction worldwide will be threatened." [1]

1 The Commission of experts on reforms of the international monetary and financial system (2009). *Recommendations 19 March 2009*. Available from: <www.un.org/ga/president/63/letters/recommendationExperts200309.pdf>.

Europe's lack of willingness to effectively include developing countries in the global effort to address the crisis is reflected in its commitment to the G-20 process rather than to other international fora, notably the United Nations. In general, Europe's approach has been to confine the role of the UN to addressing the impact of the crisis on developing countries. For European governments the G-20 is the forum in which any changes to the global system will best reflect their interests. The UN Conference on the World and Economic Crisis and its Impact on Development was a conference that most of them did not want.

This preference can also be seen in the lack of any real commitment by European leaders to increase the representation of developing countries in the structures of the IFIs. Despite their agreement, in the framework of the G-20, to allocate USD 750 billion to the IMF to help countries affected by the crisis, this has not been accompanied by a strong commitment to transform the governance system of the IFIs and address their democratic deficit. The G-20 Communiqué called for the reform of the IFI "mandates, scope and governance to reflect changes in the world economy and the new challenges of globalization", adding that "emerging and developing economies, including the poorest, should have a greater voice and representation". Its members reiterated their commitment to implement the package of voice reforms agreed by the IMF board in April 2008, and agreed that "the heads and senior leadership" of the IFIs should be appointed through an "open, transparent, and merit-based selection process". This is however, far from a commitment to changing the institution towards stronger representation and involvement of developing countries in decision-making.

The majority of public comments and proposals for IMF governance reform are raised by governments from regions of the world that have little real representation. European leaders have been arguing in favour of the status quo. Belgian Finance Minister Didier Reynders told a Reuters interviewer that "for the moment the representation around the table is attractive. European countries are having to finance the Fund very strongly, so we have to take into account the size of each country's participation in the Fund." In other words the principle that voting rights should reflect financial contributions should be retained. Changes in governance should only reflect changes in global wealth – if the emerging economies contribute financially they can have a say. The poor will remain excluded.

The European position on IMF governance as well as the role of the UN clearly indicates a desire to maintain the architecture of the global financial system almost intact. Governments are certainly using the opportunity to implement changes that strengthen their own economies' respective positions in the financial system, such those regarding tax havens and banking secrecy, which at the same time allow them to avoid more comprehensive change.

Social impacts of the crisis in Europe

Since its creation in 1957, the European Economic Community (EEC) has brought greater prosperity and improved living conditions to the majority of its citizens. Founded with the integration of the economies of Member States as a central objective, it has progressively evolved into a common European market, involving free flow of goods, services and people.[2]

Parallel to the growth of the market economy, the EEC sought to decrease economic inequalities among regions through subsidies and other forms of aid, promoting social justice and solidarity. European countries generally share a common vision of how to improve the welfare of their citizens; this vision, which has come to be known as the 'European Social Model' implies the promotion of full employment, decent work, equality of opportunities, universal social protection and social inclusion.

In recent years, increasing financial deregulation and privatization has put the European Social Model under threat. In this new paradigm the welfare of citizens is increasingly provided by the market rather than the State, resulting in a progressive retreat of the state from several social and economic spheres. Although the market economy has successfully contributed to improved living conditions for the majority of European citizens, it has also brought problems. This is well illustrated by the deregulation and privatization of the pension systems. To address the increased strains in the public pension system, many European states resorted to privatization and liberalization. Citizens were encouraged to rely more on private pension funds, which, in turn, depend on the vicissitudes of the market. Before the crisis, pension funds were doing well, as the value of their assets steadily increased. Collectively pension funds have become substantial players in the equity market. However, the current economic and financial crisis has substantially reduced the value of many pension funds, jeopardizing the future pensions of many Europeans.

The economic recession resulting from the crisis further threatens Europe's approach to social welfare. The EU has forecast a 4% recession in 2009 in the Euro zone and estimates indicate that 8.5 million people in the EU will lose their jobs in 2009-10. This translates into an unemployment rate of 11.5% in 2010, its highest level since the Second World War. The crisis also has a significant impact on public budgets. Public deficits in the Euro zone are expected to reach 5.3% in 2009 and 6.5% in 2010.[3]

What is Europe's response? From the outset of the crisis the European Commission and its Member States have taken a variety of measures to counter the effects of the economic downturn, largely through recovery plans and rescue packages. The bulk of these have focused on the financial sector. In April 2009 the EU indicated that the cost of measures approved by the Commission to support financial institutions amounts to an estimated EUR 3 trillion. This figure encompasses the overall amount of guarantees (up to EUR 2,3 trillion), recapitalization schemes (EUR 300 billion) and rescue and restructuring support for individual banks and financial institutions (about EUR 400 billion).[4]

The logic of support to the financial sector is that state guarantees and recapitalizations will allow banks to make more loans available, thus stimulating an increase in investment, which is expected to create and maintain jobs. It is by no means clear, however, that devoting such large amounts of public resources to support the banking system will serve the needs of the majority of citizens. There are many reasons for scepticism. First, banks are being funded and supported by contributions from taxpayers, who are themselves less secure due to the economic downturn. Second, most of the measures seek to increase the availability of credit, through the provision of EUR 2,3 trillion of state guarantees. With the same objective, the European Central Bank has lowered its interest rate to a historically low level of less than 1%. Yet loose credit policy helped create the conditions for the financial breakdown in the first place. It is ironic that taxpayers, many of whom are suffering heavily from the crisis, are providing money to failing institutions, and to many of the senior managers within them, that contributed to the collapse of the system.

The growing unemployment crisis argues that more emphasis be given to addressing the social impacts of the crisis. Measures to integrate those who are excluded from the labour market, invest in social and health services and improve social protection systems are needed. Yet the scale of the state-funded stimulus packages and the substantially increased public budget deficits of European governments severely reduce the ability to fund social welfare schemes and investments in social services, not just in the short term but for the foreseeable future.

One casualty of the crisis was an extraordinary European Council Meeting on employment that would have involved labour ministers of all EU Member States, replaced by a meeting of the so-called "social troika" (Czech Republic, Sweden and Spain), the EC and social partners. This "downgrading" of the employment summit was not seen as a positive message to those losing their jobs as a direct consequence of the crisis. As John Monks, President of the European Trade Union Confederation, stated, the renunciation "gives the impression that European policy-makers are not sufficiently concerned about unemployment."[5]

The crisis has triggered unexpected reactions among European policy makers. Those who were promoting unfettered free market policies before the crisis are now actively seeking to secure State bailouts. Competition Commissioner Neelie Kroes, known as a fervent promoter of free market policies, said that "the past six months have shown that State aid control plays a key role in tackling the challenges of the economic crisis in a coordinated way across Europe (…). The responsibility now lies with the financial sector to clean up their balance sheets and restructure to ensure a viable future".[6] In this framework, state intervention is no longer considered an obstacle to development and economic growth. On the contrary, it is largely agreed that States have the responsibility to address the current recession through active intervention in the market. This paradigm shift suggests that when benefits and growth are secure, the State is encouraged to retreat, while in recessions, State intervention is encouraged as the necessary solution. In other words, profits remain private and losses are socialized. This is in clear contradiction to the principles of social justice and solidarity based on the idea that profits and losses should be shared equally.

At another level, the crisis may have triggered increased "Europeanism". An EC poll from mid-January to mid-February 2009 indicates that nearly two-thirds of the EU population believed that Europeans would be better protected if Member States adopted a coordinated approach, while only 39% believed that existing coordination was sufficient.[7] This suggests broad agreement that cooperation at EU level is necessary to tackle the financial crisis.

Recent electoral results in Iceland suggest that feelings of greater Europeanism are not limited to EU citizens. After the country was nearly bankrupted, Icelanders elected by a wide margin a president who favours joining the EU. Commission President Barroso argues that acting alone, countries like Ireland, Britain, France or Germany have much fewer instruments to cope with the crisis than if they act together:

2 The EEC was created in 1957 to bring about economic integration (including a single market) among Belgium, France, Germany, Italy, Luxembourg and the Netherlands. It was enlarged later to include six additional states and, from 1967, its institutions also governed the European Coal and Steel Community (ECSC) and European Atomic Energy Community (EAEC or Euratom) under the term European Communities. When the European Union (EU) was created in 1993, the EEC was transformed into the European Community, one of the EU's three pillars, with EEC institutions continuing as those of the EU.

3 European Commission. *Economic forecasts Spring 2009*. Available from: <ec.europa.eu/economy_finance/publications/publication15048_en.pdf>.

4 European Commission (2009). *State Aid Scoreboard – Spring 2009* update. Available from: <ec.europa.eu/competition/state_aid/studies_reports/2009_spring_en.pdf>.

5 Anon. "Exit le sommet sur l'emploi". *Le Soir.* 21-22 March 2009, p. 17.

6 European Commission. *State aid: latest Scoreboard reviews Member States' action to fight economic crisis. 2009.* Available from: <europa.eu/rapid/pressReleasesAction.do?reference=IP/09/554&format=HTML&aged=0&language=EN&guiLanguage=en>.

7 European Parliament. *European Parliament Eurobarometer hears calls for coordinated EU action in fight against financial crisis. 2009.* Available from: <www.europarl.europa.eu/news/expert/infopress_page/042-54004-110-04-17-907-20090420IPR54003-20-04-2009-2009-false/default_en.htm>.

"I think that if there is some impact of the crisis on the attitude towards the Lisbon Treaty it would probably be in favour of the Lisbon Treaty".[8]

Europe's role in promoting development

The EU is also claiming leadership in efforts to mitigate the social effects of the crisis in developing countries. As EC President Barroso argued, "Europe has taken the lead in ensuring that the G-20 lays foundations for a fair and sustainable recovery for all, including developing countries".[9] However there is an asymmetry between EC measures to address the effects of the crisis internally and those to help developing countries to do so, as shown by the funds injected into European economies compared to funds available to help developing countries. This asymmetry is also seen in its support to the IMF, which has imposed strong conditionalities on loans to poor countries, preventing them from implementing counter-cyclical economic policies to address the crisis.

As export revenues, foreign investment flows and remittances fall sharply, developing countries are hard hit by the global financial and economic crisis. The World Bank estimates that developing countries may face a financing gap of USD 270 to USD 700 billion and as many as 53 million people are likely to fall into poverty in 2009.[10] Bank president Robert Zoellick, speaking in London on the eve of the G-20 meeting, said that an estimated "200,000 to 400,000 babies will die this year because of the drop in growth".[11] The UN estimates that funding necessary to mitigate the effects of the crisis might be as much as USD 1 trillion. Yet many developing countries have limited fiscal space to react to the crisis, making external support critical.

Although Europe recognizes that developing countries will face a crippling financing gap, its commitments to official development assistance (ODA) remains insufficient. With almost EUR 50 billion disbursed in 2008, aid volumes are meagre compared to resources injected into European economies to safeguard banks and boost growth. In April 2009, EU governments had committed EUR 3 trillion to support financial institutions through guarantees or cash injections. If this level of finance can be made available so quickly to support financial institutions, it is difficult to understand why European governments are unable to increase their aid budgets.

In May 2009, EU Member States confirmed their intention to meet their collective promise to allocate 0.56% of EU GNP in 2010 and 0.70% of EU GNI in 2015 in ODA.[12] Yet Italy, Ireland, Latvia and Estonia have already slashed their aid budgets as an outcome of the crisis.

> "When we look at the welfare state and social protection systems the capacity of the EU Member States to address the rising demand for social security varies greatly. Thus in some cases we have increased social and unemployment benefits, extension of coverage for unemployment as well as social benefits, tax rebates or exemptions for specific groups including pensioners. On the other hand, other States are cutting back benefits. Hungary is reducing subsidies and private sector wages, as well as cancelling pension expenditure plans, and Finland is also expecting a reduction in social service spending. To offset the effect on the labor market, some countries also try to pursue active employment policies by maintaining workers through flex time, but despite these efforts the effects are still very drastic."
>
> Verena Winkler *(Eurostep, Belgium)*

At the same time the EC has proposed speeding up aid delivery by "frontloading" a significant portion of financial transfers to developing countries, amounting to EUR 4.3 billion in 2009. This includes EUR 3 billion delivered in the form of budget support, EUR 800 million for the food facility and EUR 500 million through an ad hoc FLEX mechanism designed to help the most vulnerable countries. However, this would not consist of new finance, suggesting that if agreed, there would be less funding available in future years. In addition, Member States who will have to provide the resources are already resisting.

Parallel to their aid commitments, European countries have contributed some USD 100 billion to the USD 1.1 trillion extra money for the IFIs. The USD 50 billion provided to safeguard development in low-income countries does not appear to be accompanied by any greater flexibility in fiscal and monetary policies to access IMF loans. Despite the recent "modernization" of IMF conditionality policies, the same old recipes of tight fiscal discipline and cuts in government spending seem to apply. In that context the ability to invest in the social sector remains low.[13] Once again there is a clear contradiction between the counter-cyclical policies applied within Europe and the fiscal constraint imposed on developing countries.[14] If Europeans think that expansionary financial and monetary policies are the way out of the crisis, why do they promote the exact opposite policies in poorer countries?

The crisis, a means to further Europe's interest?

Another impact of the crisis on Europe's relation with developing countries appears to be the acceleration of controversial measures such as budget support and the conclusion of Economic Partnership Agreements (EPAs).

Budget support

Recognizing that poorer economies are in urgent need of external finance as a result of the crisis, the EC 'frontloading' proposals envisage increased use of budget support, including some EUR 500 million from the 10th European Development Fund to support African, Caribbean and Pacific (ACP) countries hardest hit by the crisis. The EC also indicated it would review ongoing budget support operations in most vulnerable countries in order to assess possibilities for frontloading disbursements. The Commission's argument in favour of budget support is that it is a quick impact instrument allowing long-term predictable financing for government expenditure including in social sectors such as education and health.

However, budget support raises a number of concerns. First, internal capacity and opportunity to monitor budgets and resource allocation, which is critical for democratic accountability, is lacking in most countries. The use of international accountancy firms to monitor implementation increases the tendency for budget support to increase governments' accountability externally, undermining internal "ownership" and democratic accountability through national parliaments. Second, the EC has identified a number of conditions that should be met before budget support is considered, including democracy and respect for human rights. However, studies of a number of budget support agreements find little evidence of any comprehensive assessment being made of these conditions being in place.[15] Finally, the EC includes budget support in its calculations to meet a legal requirement established on the insistence of the European Parliament to use 20% of its aid for basic health and education, even though the OECD/DAC, which manages the classification system of development aid, considers that budget support should be classified separately from allocations to the health and education sectors.

8 Smyth, J. "Crisis likely to favour Lisbon Yes – Barroso". *The Irish Times*, 8 May 2009. Available from: <www.irishtimes.com/newspaper/world/2009/0508/1224246132086.html>.

9 European Commission. *Commission first to act on G-20 with strategy to support developing countries*. 2009. Available from: <europa.eu/rapid/pressReleasesAction.do?reference=IP/09/550&format=HTML>.

10 World Bank News, 12 February 2009.

11 Eurodad. *Not much on offer for poor countries to counter the crisis.* 2009. Available from: <www.eurodad.org/whatsnew/articles.aspx?id=3599&LangType=1036>.

12 Council of the European Union, 18-19 May 2009, Press release. Available from: <www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/gena/107921.pdf>

13 *Ibid.*

14 While transition countries such as Latvia and Romania are also obliged to seek IMF loans, they are in a better position to do so as the EC has raised a EUR 50 billion loan facility to help non-euro area European countries to cope with balance-of-payment facilities.

15 Alliance2015. "The EU's contribution to the Millennium Development Goals Poverty Eradication: From Rhetoric to Results?" Ed. EEPA, Brussels, September 2008.

EPAs

The establishment of Economic Partnership Agreements (EPAs), creating free trade regimes between the EU and ACP countries, is one of the major controversial elements of the Cotonou agreement. EPAs are intended to replace preferential trade agreements under the Lomé conventions which were held to be incompatible with WTO rules on barriers to trade. Originally EPAs were due to have been in place by the beginning of 2008, but in mid-2009 they remain a source of considerable contention.[16]

The EC has always portrayed EPAs as development agreements, a claim that their terms belie. First, they are likely to result in an important loss of custom tariffs for many ACP countries, for which the EU is often the main trade partner. Second, ACP countries often lack the infrastructure needed to compete in an open market economy. Aid for adjusting to EPAs or 'aid for trade' has been projected as an addition to the original financial envelope provided by the Commission, but analysis indicates that much of this will not be additional. Third, the inclusion of areas of trade on which there is no agreement, such as services and procurement, will open up areas of the economy of ACP countries to EU companies.

Despite these concerns, the EC argues that in the current crisis, EPAs will contribute to promoting economic growth and development in partner countries. João Aguiar Machado, one of the Commission's chief EPA negotiators, explains that the agreements would support development by creating a predictable trade environment which, in turn, would spur investment and create employment. In order to reassure distrusting ACP governments, Trade Commissioner Catherine Ashton recognized the need for greater flexibility in the negotiations and promised that the negotiation of full EPAs will reflect and respect the regional specificity of the parties to that agreement. However, in her speech to the Joint Parliamentary Assembly in Prague in April 2009, she expressed her wish that an agreement acceptable to all parties would be reached quickly and that all interim EPAs would be signed before the end of the current Commission in October 2009. With EPA negotiations having been deadlocked for so long, it seems that the urgency to address the effects of the financial and economic crisis is being used as an opportunity to accelerate the process and increase pressure on ACP governments to concede. ■

16 In June 2009, only the CARIFORUM countries (15 countries in the Caribbean) have signed a full EPA, and only Botswana, Cameroon, Ivory Cost, Lesotho and Swaziland have signed interim EPAs.

Panel on Indigenous Rights.

Peoples’ Voices on the Crisis*

On 20 June 2009, at the Church of the Holy Trinity in New York, the “Peoples’ Voices on the Crisis” initiative, brought together activists from over 30 civil society organizations, trade unions and grassroots groups on a local, national and international level to discuss the social and environmental consequences of the financial and economic crisis for working and unemployed women and men all over the world. At the event, advocates for social, economic, gender, labor and environmental rights offered testimonials on how the crisis is impacting local communities from Sudan to San Salvador to the South Bronx.

Miguel D´Escoto Brockmann at the Peoples’ Voices event.

This forum was also an opportunity for civil society leaders to share ideas and experiences on how to construct a global movement with local roots that can push for a new economic system based on human rights and environmental sustainability.

“Peoples’ Voices on the Crisis” was held in the context of the landmark UN Conference on the Financial and Economic Crisis and its Impacts on Development, which was the first truly multilateral forum to address the social impacts of the current financial meltdown. The keynote speaker of the “Peoples’ Voices” event was Father Miguel D’Escoto Brockmann, President of the 63rd Session of the UN General Assembly, who welcomed civil society’s support for the solutions to the crisis taking shape in the heart of the UN, and exhorted the participants to “inject a new spirit of responsibility and solidarity” with the people who are being disproportionately impacted by the crisis. The event concluded with a call by Social Watch Coordinator Roberto Bissio to advocate for reforms to the current global financial architecture that would help lift people out of poverty, instead of reinforcing current economic and social inequalities both within and across borders.

Disseminated throughout the Thematic Chapter of the Social Watch Report 2009 you have been reading key interventions from participants in this activity, together with some testimonials of the impact of the crisis in ordinary people the Social Watch network gathered in countries of the South. ■

* “Peoples’ Voices on the Crisis” endorsing organizations: Social Watch, Eurostep, LDC Watch, Institute for Policy Studies, Global Policy Forum, Center of Concern, ESCR-Net, Institute for Agriculture and Trade Policy, Global-Local Links Project, Jubilee USA Network, Jubilee South, GCAP Feminist Task Force, Alliance for Responsible Trade, Women’s Environment and Development Organization, International Council for Adult Education, UN Non-Governmental Liaison Service, Global Action on Aging, Latindadd, US Human Rights Network, CONGO Social Development Committee, Sub-Committee on the Eradication of Poverty, Hemispheric Social Alliance, Womens’ Working Group on Financing for Development, Medical Mission Sisters International, World Federation of United Nations Associations, International Youth and Student Movement for the United Nations, Enlazando Alternativas, Transnational Institute, Our World Is Not For Sale Network.
Video clips from “Peoples’ Voices on the Crisis” are available from the Social Watch YouTube channel: <www.youtube.com/SocWatch>.