Has the Economic Crisis Reached its Peak?

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In July-September 2011 the stock markets were again shaken at international level. The crisis has become deeper in the EU, particularly with respect to debts. The CADTM interviewed Eric Toussaint about various facets of this new stage in the crisis.

CADTM: Has the crisis peaked yet?

Eric Toussaint: The crisis is far from over. Even if we only consider the financial aspects, we must be aware that private banks have continued to play an extremely dangerous game which profits them as long as nothing goes wrong, but which is prejudicial to the majority of the population. The amount of bad assets on their balance-sheets is enormous. If we look at only the top 90 European banks, the fact is that over the coming two years, they will have to refinance debts to the tune of an astronomical EUR 5,400 billion. That represents 45% of the wealth produced annually in the EU. The risks are colossal and the policies adopted by the ECB, the EC and the member States of the EU will not solve anything – indeed quite the contrary.

A central aspect of the risks taken by the European banks needs to be emphasized. They finance a significant part of their operations by making short-term loans in dollars from the North-American lenders known as "US money market funds" at a lower rate than the ECB's. Furthermore, to return to the case of Greece, how could the European banks possibly settle for 0.35% over 3 months if they had to borrow from the ECB at 1%? They have always financed their loans to European States and companies using loans they themselves took out from the US money market funds – and they continue to do so. Now those money market funds were scared by what was happening in Europe and also by the dispute over the US public debt between Republicans and Democrats. So by June 2011, that source of low-interest finance had just about dried up, which has hurt major French banks most. This was what precipitated the tumble they took on the Stock Exchange and led to the increase of pressure on the ECB to buy back their bonds and thus provide them with new money. In short, this demonstrates the extent of the knock-on effect between the economies of the USA and the EU. It further explains the continual contact between Barack Obama, Angela Merkel, Nicolas Sarkozy, the ECB, the IMF … and the major banks from Goldman Sachs to BNP Paribas and the Deutsche Bank. A breakdown in the flow of dollar-loans to European banks could cause a very serious crisis in the Old World, just as difficulties encountered by European banks in repaying their US lenders could trigger off a new crisis on Wall Street.

Since 2007-2008, banks and other institutional investors have displaced their speculation activities from the property market (where they had created a bubble which burst in nearly a dozen countries,including the USA) to the public debt market, the currency market (where the equivalent of USD 4,000 billion changes hands every day, 99% purely for speculative purposes) and the primary resources market (petroleum, gas, minerals, food commodities). These new bubbles can burst at any moment. A possible trigger could be if the US Federal Reserve decided to raise interest rates (followed by the ECB, the Bank of England, etc.). In this respect, in August 2011 the Fed announced its intention to maintain its base rate near zero until 2013. However other events could trigger off a new bank crisis or a crash on the Stock Exchange. The events of July-August 2011 show us it is time to muster our energy in order to prevent the private financial institutions from doing any further damage.

The extent of the crisis is also determined by the volume of the US public debt and the way it is financed in Europe. European bankers hold more than 80% of the total debt of an array of European Union countries in difficulty such as Greece, Ireland, Portugal, the Eastern European countries, Spain and Italy. In volume, Italian public debt paper amounts to EUR 1,500 billion, more than twice the combined public debt of Greece, Ireland and Portugal. Spain's public debt comes up to EUR 700 billion, i.e. about half of Italy's. The arithmetic is simple: the public debts of Spain and Italy added together represent three times the sum of those of Greece, Ireland and Portugal. As we saw in July-August 2011, while each country continued to pay off its debts, several banks almost collapsed. The ECB had to intervene to save the day. The financial scaffolding of the European banks is so fragile that an attack through the Stock Exchange is enough to bring them down… Not to mention what would happen if the Stock Exchange crashed, which cannot be ruled out.

So far, with the exception of Greece, Ireland and Portugal, the States have managed to refinance their debts by taking out new loans as and when the borrowed capital fell due. The situation has worsened significantly over the last few months. By July/early August 2011, the interest rates demanded by the institutional investors to enable Italy and Spain to refinance their public debt as it fell due with 10-year loans had literally exploded to reach 6%. Once again, the ECB had to intervene, buying up massive amounts of Spanish and Italian debt paper to satisfy the bankers and other institutional investors and bring down interest rates. For how long, though? Italy will have to borrow about EUR 300 billion in August 2011 and July 2012 as that is how much they will require to honour bonds that fall due over that short period. Spain's needs will be considerably lower, at about EUR 80 billion, but that is still a hefty sum. How will the institutional investors behave over the coming twelve months and what will happen if their borrowing conditions on the North-American money market funds become stiffer? Many other events could aggravate the international crisis. One thing is certain: the present policies of the EC, the ECB and the IMF cannot result in a favourable outcome.

CADTM: On several occasions you have written that the private debt was far greater than the public debt. So far you've been talking about public debt.

Eric Toussaint: There is not a shadow of a doubt that the private debts are much higher than the public debts. According to the last report by the McKinsey Global Institute, the sum total of private debt worldwide comes to USD 17,000 billion, i.e. about three times the sum of all public debts, which is USD 41,000 billion. There is a great risk that private companies, including banks along with the other institutional investors, will not be able to repay their debts.

Bankers, chief executives of other companies, the traditional media and governments only discuss public debt and use its increase as a pretext to justify new attacks on the social and economic rights of the majority of the population. Austerity and the reduction of public deficits by axing social budgets and civil service jobs have become the only way of raising funds, along with privatizations and more consumer taxes. For appearances' sake in Europe, some governments have added a tiny tax for the rich and talk of taxing financial transactions.

Obviously the increase of public debt is the direct result of 30 years of neoliberal policies. They have used loans to finance fiscal reforms in favour of the wealthy and of large private companies. They have rescued banks and large companies by getting the State budget to take on part of their debt or other losses. Due to the recession, there have been new falls in tax revenues and an increase in some public spending to help victims of the crisis. The combined effect of these different factors has been to increase the public debt. It all comes down to deliberately unjust social policies which aim systematically to favour one social class only. A few crumbs are tossed to the middle classes to keep them quiet. On the other hand, the great majority of the population have been hit by these policies and seen their rights trampled underfoot. That is why the public debt has to be seen as globally illegitimate. And that is why I have been focusing on the public debt in this interview, because we absolutely must find a positive solution to this problem.

Translated by Christine Pagnoulle and Vicki Briault in collaboration with Judith Harris

See the first part "Greece" http://www.cadtm.org/Greece , the second part "The great Greek bond bazaar" http://www.cadtm.org/The-great-Greek-bond-bazaar, the third part "The ECB, ever loyal to private interests" http://www.cadtm.org/The-ECB-ever-loyal-to-private, the fourth part "A European Brady deal: austerity for life" http://www.cadtm.org/A-European-Brady-deal-austerity , and the fifth part " CDS and rating agencies: factor(ie)s of risk and destabilization" http://www.cadtm.org/CDS-and-rating-agencies-factor-ie

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