Lecture: Heiner Flassbeck

How to rescue our sinking economies

Luxembourg, Maison de l'Europe

27 June 2013

On the 27 June 2013, the Luxembourg Institute for European and International Studies (LIEIS), in association with the Representation of the European Commission in Luxembourg, organized a lecture by Prof. Heiner Flassbeck: "*How to rescue our sinking economies*". In his presentation the former Director of the United Nations Conference on Trade and Development's (UNCTAD) Division on Globalization and Development Strategies addressed the roots of the global economic problems and criticised the prevailing neoliberal approach to resolve them.

In his introductory remarks, Armand Clesse, Director of the LIEIS, referred to the double meaning of the lecture's title: he emphasized the pessimistic connotation expressed by the word "sinking" and the hope for change implied by the word "rescue". Dr. Clesse pointed out that Professor Flassbeck has combined action and reflection in his career for many years as he has not only worked as a political advisor, but also as a professor and author.

After having expressed cautious optimism for a potential shift towards an alternative way out of the crisis, Professor Flassbeck explained that he would speak about the global economic problems and then proceed to the situation in Europe.

Initially, Professor Flassbeck addressed the ratio between income and unemployment, which has been challenging the neoclassical paradigm since 2008. He explained that the basic assumption of neoliberal economic thought from the 1970s to the late 1980s has been that high employee compensation correlates with high unemployment. However, the current rise in unemployment, which is at the highest level since World War II, goes hand in hand with a decrease of the wages, contradicting this rationale. Given this flaw in the neoliberal paradigm, Flassbeck called for a new logic to finding a solution for the global economic crisis. In this vein Professor Flassbeck stressed the crucial role of the labour market. He highlighted that the shift of power to the employers, and the related wage decline that has been taking place since 2008, should be seen as a major obstacle to economic recovery. Professor Flassbeck stressed that the neoliberal confidence in cutting hours and wages to help the economy recover should be rejected. He explained that the labour market does not follow microeconomic rules and that, on the contrary, it is part of the global economy. When it comes to solving the global economic crisis, Flassbeck said, the reliance on monetary and fiscal policy to give an economic boost will be inefficient, as long as wages remain low. In fact, positive income expectations should be created in order to stimulate consumption and thus economic growth. 80% of a country's GDP is generated by domestic demand, while export-shares only account for 6-7%, making the consumption rate the key to recovery. Focusing on export, which is what has been done up until now, will not help resolve the current economic problems.

By advocating a general increase in the level of income, the German economist clearly rejected the austerity policy promoted by the European Union and the International Monetary Fund (IMF). Flassbeck referred to the example of crisis countries like Portugal or Greece, where the adjustment of the labour costs did not result in an economic improvement. On the contrary, despite a wage cut of 24% the Greek GDP continues to decline, which he considers evidence that salary decreases affect national demand, as well as economic growth, in a negative way. He added that decreasing wages will not help the weakened economies of Southern Europe become more competitive as Germany holds an unassailable advantage in terms of labour costs.

This led to the final point of Heiner Flassbeck's analysis, namely the role that low German nominal wages play in the current economic crisis. When comparing the economies of France and Germany from 1999 on, it is clear that both countries experienced the same increase in productivity. However, the fact that the nominal wages are much lower in Germany provides it with a competitive advantage. According to Flassbeck this is the main reason for the rising trade imbalance in the Eurozone and has acted as a catalyst for the European Union's economic problems. In this context, Prof. Flassbeck criticised what he called "the perverted German economy", which is characterized by a focus on savings and a prohibition of private, and respectively public debt. In fact, he stated that the on-going universalization of this "debt phobia" has deleterious effects on the global economy, because if the number of savers exceeds that of the debtors the demand will fall apart.

To give an example, he showed that if the government and the companies spent 100 Million euro on wages each year, and the private households maintained a savings ratio of 10%, neither the government nor the companies would recuperate the full amount of money they had spent. Given the fact that the savings of these private households go hand in hand with a decrease in consumption, a company's capital for investments would decline over the years. He suggested that in Germany, where the savings ratio is one of the highest, monetary reserves will soon be depleted, due to the fact that these savings are invested in foreign countries and thus consumed abroad. As a consequence, there will not be any reserves for social needs in Germany in twenty years, which is why he argued that savings should always be kept in the countries of origin.

During the question period Professor Flassbeck was asked if China exercises the similar negative influence on the global economy that Germany does to the Eurozone. He responded that on the contrary, the Chinese have increased wages about 20% each year and stimulated domestic demand this way. Another observer objected that higher wages in addition to the required social security would harm the companies' competitiveness. Professor Flassbeck answered that companies save too much of their money, and that they should invest it instead.

In conclusion, Heiner Flassbeck pleaded for an increase of the nominal wages in Germany in order to stimulate the national demand and to achieve a harmonization of the labour costs among the EU member states.

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