**Comparing the Eurozone and the Latin American Crisis Adjustments: Macroeconomic Unbalances, Intellectual Consensus and Social Fragmentation**

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**ABSTRACT.**

Many scholars have looked for similarities between the crisis in the Eurozone and those registered in the past in developing countries and particularly in Latin America. Problems of balance of payments, public debt, overvaluation of the exchange rate and unregulated capital inflows are frequently mentioned to compare common features of different crisis events. Also, processes of welfare state retrenchment and labour market segmentation are compared. The paper aims to discuss common features of the Latin American past crisis and current crisis in the Eurozone in order to learn how a faulty institutional design and policies can arise from a defective understanding of how financial capitalism works. This analysis aims to place in the political economy perspective of regulation theory two common features of those crises: the construction of the intellectual consensus leading to ignore some of the most important causes of the crisis (like the currency board in Argentina and the comparable overvaluation of the euro for peripheral economies of the zone) and the insufficient effects of demand policy to foster the return to sustainable growth in correlation to the limits of investment expansion

**Keywords:** Latin America, Eurozone, financial crisis, macroeconomic adjustment, social and labour policies, intellectual consensus.

1. **LATIN AMERICAN AND EUROZONE CRISIS IN COMPARATIVE PERSPECTIVE[[2]](#footnote-2)**

Many scholars have looked for similarities between the crisis in the Eurozone and past crises in Latin America. The use of the term “periphery” for some of the less developed Eurozone countries signals the presence of some comparable features between the Eurozone and Latin America. It is worth recalling that Latin American structuralism school has analysed the dichotomy between core and peripheral countries in order to stress the heterogeneity and dependence relations of capitalist international development (Prebisch, 1981). Currently, this distinction is been used systematically in the official rhetoric of the Eurozone in order to blame some less-developed countries for their monetary and financial dependency on the most developed Eurozone partners (Légé and Marques Pereira, 2013).

The comparison is also stimulated by the fact that, after many crises experienced over three decades, from 2002 onwards there has been no financial crises in Latin American economies despite the strong negative shocks caused by the United States sub-prime crisis in 2008-09. Meanwhile, the Eurozone still remains in the middle of a profound crisis.

Looking at the Latin American trajectories in the first decade of this century, some authors suggest that countries in the region have “learned” from their past experience, making significant changes in their macroeconomic policies during the 2000s with respect to previous years (Frenkel, 2012; Ocampo, 2010). For instance, the absence of a lender of last resort in international currency has been one of the main problems during past crises. To compensate this absence and in a favourable international context of high commodity prices, in the last years many Latin American economies have built up balance of payments surpluses through export growth in order to accumulate large volumes of foreign exchange reserves. Also, some countries in the region learned from the failure of past pro-cyclical policies taken to overcome depressive tendencies during crisis; at most, the lesson is that intervals of recovery following these policies have been no more than short-lived episodes.

Of course, there are many differences between the Eurozone and Latin America. For instance, in past Latin American crises the absence of a lender of last resort in international currency raised the exchange rate risk as well as the risk of default on debts in international currency (both private and public). In contrast, in the Eurozone there is no exchange rate risk for its members (at least until a country member decides to quit the zone). Also, the risk of default of public debts is due mainly to the reluctance or inability of the European Central Bank (ECB) to play a credible role of lender of last resort for member countries.

Still, it is possible to find common elements. One of them is the incorporation into the “Troika” of the International Monetary Fund (IMF), which was a key player in Latin American past crises (Fritz, Dullien et al., 2014). In the case of the Eurozone the IMF has been called in the Troika mainly to support the “rescue” policy packages while in Latin America also played the role of lender. Its inclusion in the bail‐out packages in Greece, Portugal and Ireland was not the need for funds, but rather the idea that there is need to seduce financial markets and to draw upon the IMF’s wide experience in designing and implementing adjustment programmes in times of crisis. Most of this experience was in Latin America.

The comparative analysis of different crisis events in financially depended peripheral countries could help to learn how to manage (and avoid) crises in an integrated financial world. Instead of looking at internal problems of different countries, comparing crisis scenarios and policies applied in different regions could help to learn in what way a faulty institutional design can arise from a defective understanding of how financial capitalism works in a complex internationally integrated economic system. Also the comparison can help to understand how crisis and austerity policies press for labour and social division, eroding the very bases of modern welfare state institutions.

**B. CRISES IN PERIFERAL LATIN AMERICAN ECONOMIES**

Since the beginning of the financial globalization, and until the first two years of the 2000s, Latin American countries experienced two big waves of crises (Frenkel, 2013). The first one was in the early 1980s, when deep financial (and currency) crises were experienced by Argentina, Chile, Uruguay and Mexico, while Brazil confronted a public foreign debt crisis without a domestic financial crisis. The second wave began in 1995 with the Mexican and Argentine crises, followed by the Brazilian currency crisis in 1998; Argentina and Uruguay suffered financial and currency crises in 2001-2002 which constitute so far the last financial crises in peripheral Latin American economies.

With the exception of Argentina in 1995 (under the currency board exchange regime), all these crises ended up in devaluations and some type of bail out and restructuring of the domestic financial systems was also applied (including the refinancing of private debts supporting significant fiscal costs). Debt management is crucial to understand post-crisis developments. For instance, since none of the Latin American debt restructurings processes in the 1980s included substantial alleviation of the debt burdens, most countries experienced many years of stagnation and high inflation. Meanwhile, more successful results are found in the case of Argentina’s debt default at the end of 2001, which is the major explanation of fast recovery after the deep recession of 1998-2002 (Lo Vuolo, 2007).

Each wave of these crises was preceded by booms of capital inflows expanding liquidity and credit and feeding bubbles in financial and real assets (Frenkel and Rapetti 2010). The resulting expansion of aggregate demand led to output and employment growth, along with non-tradable price increases. In general, these price increases provoked an appreciation of the real exchange rate which reinforced capital inflows seeking to obtain quick rent given the financial arbitrage between domestic and foreign assets. This in turn accelerated the expansion of credit and output growth.

International organizations played a key role during the boom phases preceding the crises imposing macroeconomic and public policies thanks to the need to obtain their support in financial markets. These policies typically included the liberalization of the capital account of the balance of payments, the liberalization of the local financial market, some sort of exchange rate fixation (pegs or active crawling-pegs), re-regulation of labour markets and privatization of most public services.

In short, the region experienced the main features of a financial-led growth regime, setting high profitability thresholds for investment and exerting intense pressure on labour delinking productivity and wage increases (Aglietta, 2012; Boyer, 2000). With growing inequalities in wealth and incomes, the dynamic demand is provided by the expansion of credit, supported by low interest-rate policies (and overvalued exchange rates in many Latin American countries).

In Latin America the combined effect of the real exchange rate appreciation and financial-led growth weakened exports and stimulated imports. The worsening of the trade balance together with the increase in debt payments turned the current account into deficit. At the beginning of the cycle, capital inflows were higher than the current account deficits (and foreign exchange reserves accumulated). However, at some point current account deficit became larger than capital inflows and the balance of payments result turned negative. These contracted liquidity and credit, asset prices bubbles gradually deflated, and illiquidity and insolvency emerged.

The contracting phase usually began by a stop of capital flows combined with the persistent increase in the current account deficit and the narrowing trend in international reserves. These processes threatened the exchange rate management and increased the probability of default of the foreign debt issued in international currency. This is because the sustainability of that type of debt has a specific default risk associated to the potential lack of liquidity in foreign currency. This shortage can force debt default even when the government has resources in domestic currency, due to the lack of a lender of last resort in foreign currency.

The contracting phase reinforces itself because higher risk premiums and higher interest rates are needed to attract foreign capital. Thus, the economic activity shrinks even more, further illiquidity and insolvency reduces the credibility of the exchange rate policy and increases the default risk. In this way, the crisis emerged as the culmination of the same processes that caused the boom phase and encouraged greater risk-taking.

In Latin American countries the contracting phase ends in a financial and exchange rate crisis because the fall of foreign currency reserves in the Central Bank leads to changes in the exchange rate regime and commonly a bail out or some type of debt restructuring. The common feature during crisis time is that, even after adjustments have been made in the external sector, a large proportion of the financing needs must be covered from capital markets.

This scenario reinforces the power of financial organizations because the State has to rescue all economic agents, including banks in the first place. The IMF, the World Bank and other international institutions lend some money but mainly play the role of guarantors that countries will apply the “healthy” policies needed to gain the financial market confidence. International organizations guarantee the immunisation of policy adjustment against pressures from below.

**C. CRISES IN PERIPHERAL EUROZONE ECONOMIES**

The changing rhetoric of the ECB and other European authorities with regards to the Eurozone crisis resembles the Latin American past experience. After denying at the beginning the very existence of the crisis in the Eurozone and then arguing that it could be solved easily since there were no risk of contagion from countries in trouble to the rest, country governments and European authorities (including the ECB) moved to the centre-periphery explanation for the crisis (Légé and Marques Pereira, 2013). Nowadays, the official rhetoric preaches that it is a problem of Eurozone peripheral countries which depend on financial assistance from the centre. The solution is to apply healthy fiscal adjustment and austerity measures in order to convince financial markets that peripheral Eurozone countries have the power to pay their debts.

This vision has many flaws. As in Latin America, crises in Eurozone countries were also preceded by capital inflows. Similar to the years preceding crises in Latin America, and in contrast to the US[[3]](#footnote-3), in the Eurozone these capital inflows resulted from changes “outside” the national macroeconomic policy: the creation of the Monetary Union. The common currency operated as a strong incentive for arbitraging between core and peripheral Eurozone countries’ assets since it promoted a sort of risk convergence[[4]](#footnote-4). However, since the Euro did not result in an inflation convergence within the Eurozone, in practice countries showed different interest rates and exchange rates in real terms. As a result, in the Eurozone peripheral countries the lower real interest rates and the more appreciated real exchange rates stimulated capital inflows, growth, external deficit and external debt. These capital inflows accelerated because risk convergence took place when global credits have expanded all over the world.

Other similarity between Latin American economies and countries in the Eurozone is the following: all of them issue debt nominated in a currency they do not emit. The Euro works as a foreign currency for every Eurozone country. As a result, financial markets doubt (and speculate) about the capability of some European countries to pay their debts in Euros, as in the past they doubted (and speculated) about the capability of Latin American economies to pay their debt in foreign currencies.

This situation resembles the experience of Argentina between 1991 and 2001, when a dual monetary system was implemented and the exchange rate was fixed by the law at one peso to the dollar (Lo Vuolo, 2003; Cibils and Lo Vuolo, 2007). However, apart from the different level of development, two important differences between Argentina under the Convertibility plan and the Eurozone countries can be identified.

One difference is the degree of financial integration in Europe and the other is the ECB. The Argentine banking system during the Convertibility rule was relatively insulated from the international financial system, but highly dollarized and constrained by the currency peg. In contrast, the creation of the Eurozone fostered cross-border mergers and acquisitions that have effectively integrated the balance sheets of the respective national banking systems (Toporowski, 2013). Accordingly, banks in all countries of the Eurozone are exposed to risks in other countries since they have assets or subsidiaries in other countries or they have liabilities to the ECB. In fact, the large European banks played an active part in the expansion of debt and toxic assets not only in the Eurozone but also in the US. Indeed, when the crisis broke out in 2007 in the US, these European banks found themselves in a position comparable to that of the American banks (Servén and Nguyen, 2010).

This is not the only difference between the Eurozone crisis and past crises in Latin American countries. In the Eurozone –in principle- the exchange rate risk plays no role in the portfolio decisions leading to capital outflows neither have capital flows been directly influenced by the evolution of external accounts (Eurozone countries do not carry stocks of international reserves and do not have risks of devaluation). But, on the other hand, public debts in the Eurozone do have a specific liquidity risk of default similar to that of public debts issued in foreign currency in Latin America. Not surprisingly, during crises private debts were taken by the State, directly as in Latin America, or indirectly by supporting banks in the Eurozone.

Even when the Eurozone shows many institutional and economic differences with Latin American countries, still a large proportion of the financing needs of the debtor Eurozone countries must be covered with funds from the financial markets. For many reasons, the ECB has not eradicated the possibility of default on public debts (at least for the financial operators).

This fact helps to explain why the IMF was included in the so-called Troika. The European Commission and the ECB ask the IMF for advises on how to apply debt restructuring, under which conditions to provide liquidity and what kind of austerity policies are needed to put indebted countries back to the “normal” financial order (Fritz, Dullien et al., 2014). As in Latin America, country governments and European institutions call the IMF to play the role of a respectful institution which past experience guarantees efficiency on implementing, monitoring and enforcing conditionality of rescue packages.

As a result, fiscal austerity is the main objective of the policy orientation of the “Troika” and the justification is the need to seduce financial markets. For the IMF and its partners, all crises look similar since all indebted countries need a loan, and all need to make big changes in order to pay the debt and live within their means after a period of excess expenditure.

**D. AUSTERITY PRO-CYCLICAL POLICIES**

As the Washington Consensus in past Latin American crises, the rhetoric of the Troika spreads the idea that austerity measures will have a net expansionary effect on output due to the positive effects on private expenditures. Those policies are well-known in Latin America: the institutionalization of rules for fiscal policy which restricts the room for counter-cyclical macroeconomic policy manoeuvre, the adoption of structural reforms such as privatization of public enterprises, de-regulation of the labour market, retrenchment of social policies, etc.

Austerity policies seek to force what is called an “internal devaluation” of domestic prices (labour costs in the first place). In such a view, wage flexibility is a substitute for the impossible exchange rate flexibility in the Eurozone; the rhetoric preaches that competitiveness should be obtained by low wages and low wages will increase competitiveness, future to growth and more employment (Toporowski, 2013). In this way, governments choose to confront domestic social and political conflicts arising from austerity policies, worsening the economic performance, in order to send conventional “positive” signals to financial markets.

Latin America experience on this policy packages show many logical flaws in this argument. Among others, lower wages reduce domestic demand, which is very difficult to replace by foreign demand. Moreover, with a regime of low inflation, which can turn into deflation, and without the possibility of expanding public expenses, the system has few mechanisms for eliminating the debt burden. Fiscal austerity causes reductions in GDP, unless offset by trade surpluses or private sector investment. Attempts to reduce government debt when the economy is in recession cannot succeed because GDP will start to fall well before governments cease deflating their economies. In the case of the Eurozone, financial uncertainty and recession as a corrosive impact on global growth, too.

In Latin American countries, the alleged expansionary effects of low wages and austerity measures have been no more than short-lived episodes. The austerity policies taken have proved powerless to overcome the strong depressive tendencies at work. Following these policies the crisis became systemic, affecting every part of the economy: banks, firms, households, states.

Again, Argentina is a good example that time matters because, under the Washington Consensus tutelage, the country went from one austerity plan to another: recession began in mid-1998, default of the debt and devaluation took place at the end of 2001. While the country stagnated and unemployment increased to high levels, the spread on public debt relative to the American interest rate reached 2,500 basis points[[5]](#footnote-5). Given the liquidity shortage several parallel currencies appeared in the provinces (Théret and Zanabria, 2007). On December 2001, the government ordered the freezing of bank deposits and put in place drastic foreign-exchange controls. Soon after, the new provisional government declared the default of public debt, the dollar peg was eliminated at the beginning of January 2002 and de-dollarization of the economy was forced.

After all these drastic measures, the Argentine economy started to grow in the second semester of 2002 and sustained a very high rate of growth in the following years. In 2005, the country restructured most of the debt with an important haircut in comparative historical record (Damill, Frenkel et al., 2010; Cibils and Lo Vuolo, 2007).

Greece since late 2009 resembles the Argentina period between 1998 and 2001. Both the Greek government and the Troika denied the possibility of a Greek default while devaluation was impossible as a member of the Eurozone. They imposed policies of sharp reduction of wages, public spending cuts, regressive tax rises and pressures for large-scale privatizations. The result has been a huge drop in GDP. Instead of halting the steady growth in public debt, austerity measures sent it up. Meanwhile, the cumulative recession reduced the current account deficit but not as the Troika projected.

The official rhetoric blames national policies of “peripheral” countries for these results. However, for financial operators national policies are not the only element taken into account to assess the country’s risk and to seduce capital inflows. The main problem for the Eurozone is that the Euro is incomplete as a currency, for its sovereign guarantor has not been realized. Briefly, “the Eurozone has a central bank without a government, governments without central banks and banks without an effective lender of last of resort” (Toporowski, 2013).

Instead of adjusting this faulty institutional design, political authorities insist to push those austerity measures and fiscal adjustments that did not work in past Latin American crises. In contrast to the doubts about the effect of austerity policies to seduce financial markets, these types of policy responses to the crisis foster a dangerous social political climate of winners and losers and many distributional conflicts emerge. In these aspects, the Latin America experience can also teach some lessons to Europe.

**E. LABOUR MARKETS AND SOCIAL POLICIES**

E1. LATIN AMERICAN EXPERIENCE: INSECURITY WITH MORE CONDITIONAL FOCALIZED PROGRAMS

Processes of socio-economic and institutional change during crises cause large problems for modern welfare states. Latin American experiences teach that austerity measures directly affect the central supporting pillars of the welfare capitalist system, meaning employment and fiscal expansion. During crises, labour markets and social policies are confronted with critics tending to undermine their legitimacy. In a time of severe economic hardship, “insiders” protected under welfare state policies feel that their living standards are declining while the number of “outsider” rises, and their lives depend more than ever on sometimes discretional social transfers.

During the 1980s and 1990s deregulation of labour relations was prescribed in Latin America, even when informality accounts for a great part of employment. More insecure labour relations and a closer connection between contributions and benefits in social security (including privatization) were some of the recipes to boost financial markets, growth, workers’ effort and employment.

As a result, increasing number of people started to fall out of protected work patterns, while wages and labour costs decreased sharply. Subcontracting, part-time work or jobs without contract, reduction of public employment, the expansion of jobs in microenterprises, domestic service and self-employment, excessive working hours for some groups, were all part of the reconfiguration of labour markets. None of the preached were reached: More people fell out of “normal” work patterns and we see no decline in the size of the informal economy across the region (Lo Vuolo, 2009a).

At the same time, the universalistic aim of social policies was confronted with the argument that it did not serve in the best interest of the poorest groups. Thus, social policymakers were advised to set aside such universalistic aims and boost private social insurance. The alleged “over-protection” that certain categories of workers enjoyed within the social security system helped legitimize policies to reduce benefits and foster selectivity, despite the social insurance legacy. The poorest groups would receive residual subsidies by means of social assistance programmes when they prove need trough a means test.

As a result, the distribution of income worsened all over the region (Cepal, 2010). During the 1990s the Gini index increased in almost every Latin American country (except for Colombia and Uruguay). At the beginning of 2000s open unemployment averaged 9 per cent, showing a marked growing tendency, with peaks of 20 per cent in Argentina and 16 per cent in Uruguay, Colombia and Venezuela. Public employment dropped and employment in low productivity services increased. Far from the sustainable growth promises, the economic and social situation worsened and the second wave of crises affected many countries first around 1995-1997 and then in 2001-2002.

While insecurity in labour markets, lack of social security coverage and regressive income distribution become a generalized feature, the demands for compensation systems have grown. As a result, since the 1990s the region witnessed a general tendency to set up focalized poverty alleviation schemes with separate administration and mainly related to some test of poverty. More recently, a new wave of targeted assistance programs known as Conditional Cash Transfer programs has swept over Latin America (Cechini and Madariaga, 2011)[[6]](#footnote-6).

Past and recent experience of the region shows that the potential to achieve universal inclusion through separate, targeted and contribution-based schemes is inherently limited. Latin America shows that the more insecure labour economies are, the more stable and well-funded income maintenance and public service systems must be in order to integrate and make economically efficient heterogeneous societies. Europe is not taking into account these evidences.

In this way, the Eurozone experience is showing that contemporary political and economic system must legitimize itself not only among the population but mainly among the profit-dependent owners and managers of capital. Only is the latter expectations are satisfied can the former too been satisfied (Streeck, 2014, 21).

 E2. THE EUROZONE ADJUSTMENT: THE LATINOAMERICANIZATION OF LABOUR MARKETS AND SOCIAL POLICIES?

Continental European countries are in the onset of similar processes than Latin America in the past, but under different institutional and economic development. Since the early 2000s, a wave of social policy reforms has been developing showing new trends in social protection:

*“Activation of the unemployed, the limitation of early exit, measures for increasing the participation of women, older workers and unskilled workers are amongst the biggest innovations. Important pension reforms have also been adopted, aimed at further reducing the cost of public pensions and at favouring the development of private fully funded complements. In health care, in the countries with a health insurance system, more regulatory power has been given to the state, and more competition between health insurances is being introduced. Minimum income protection has also been generalized, to protect the weakest from the further retreat of social insurance that has happened through the structural transformation of traditional social insurances*” (Palier, 2010, 356).

The crisis in the Eurozone is accentuating these processes and widening differences in earnings between low and high skilled workers. Resembling past scenarios in Latin America, the crisis in Europe raises the debate about the responsibility of labour regulations in the economic crisis and the inequality impact of labour policies themselves. For instance, minimum wages are said to be particularly harmful to the employment chances and hence (relative) living standards of less-skilled workers. Even when labour markets have not been deregulated wholesale in Europe, the number of “atypical” or “nonstandard” employment relationships has risen sharply, as has the number of working poor.

Unemployment risk and gender inequality is an additional dividing line in the insider-outsider conflict in the labour market emerging from austerity policies. In many parts of Europe, women unemployment risk is considerably higher than that of men and this divide is exacerbated by the cutbacks in public sector jobs, where women make up the majority of the workforce. Meanwhile, in the private sector, where women tend to have reduced paid opportunities across the board, low-wage jobs are growing. Overall, these processes have reinforced the distinction between workers who are still linked to the core labour market (even if temporarily unemployed) and those who are moving away from it.

These processes not only generate pressures for the development of a secondary labour market but also for a secondary type of welfare protection. Welfare institutions and programs are being modified in order to pave the way for a trend that make them very distant from those that prevailed in the past (Palier and Thelen, 2010).

As was the case in Latin America (Lo Vuolo, 2002), pensions are in the centre of the welfare state retrenchment in Europe. The crisis reinforced cost-containment reforms tightening eligibility conditions, strengthening the link between contributions and benefits, increasing retirement ages, changing indexation rules from wages to prices, etc. (Kohli and Arza, 2010). Recent reforms have strengthened the link between the amount of contribution and the volume of the benefits (through a change in the calculation formula and/or stricter entitlement rules) and usually meant a shift away from redistributive (horizontal and vertical) toward actuarial principles and a potential reduction in the coverage of social insurance.

While unemployment insurance benefits are generally limited in time, unemployment in Europe is becoming to a large extent structural in nature. Many of the structurally unemployed are not even entitled to unemployment insurance benefits, since they have earned no or insufficient social entitlements. As a result, most European countries have either created or expanded and generalized minimum income guarantees and social assistance schemes that in the past were implemented as a residual and temporary social safety net for very small population groups in Europe have now become a quasi-permanent source of income to large sections of the population.

In his way, in Europe many of social and labour policy changes are been framed as part of a distinction between what type of social benefits and who should remain in the world of occupational social protection (and be financed through contributions) and what type of social benefits and who should be transferred to the world of social assistance, aimed at those with atypical employment situations (and financed through taxation). As in Latin America, retrenchment in social insurance programs thus reinforces dualism and fragmentation in social benefits to the extent that it is accompanied by a clarification of responsibility, and a shift in funding as the welfare system has come to rely more heavily on taxation to support the (non-contributing) working poor.

The expansion of assistance focalized programs show preferences for a meritocracy that allegedly expresses itself in terms of success in a more heterogeneous labour market, in the punitive conditions that the counterparts demand beneficiaries to comply with, and through the institutional separation between contributive and non-contributive policies are some strong elements among them. These preferences vary between countries, as do institutional configurations of their welfare regimes, but generally they are present in most cases.

It could be argued that these changes are marginal. However:;

“*Institutional change often, probably mostly, takes place as a gradual change, chich may for a long time be dismissed as marginal, even after the marginal has become the core and the principal force shaping the dynamic of development”* (Streeck, 2014, xiii)

The assistance cash transfer programs is the easiest and cheapest way to preserve traditional conceptions of meritocratic social protection system adding the perception that the outsiders are “being attended”. This scenario increases the dilemma of horizontal solidarity in countries where labor ethics have always been the prevailing value, which share the social insurance ethos.

However, the Latin America experience shows that cutbacks to the state services are never sufficient because at the same time economic recession means fewer taxes. This creates a destructive environment of winners and losers. In this scenario, the challenge is not only to find a new optimum in response to changed economic conditions but also to avoid an increasing social divide.

**F. CAN THE EUROZONE LEARN FROM THE LATIN AMERICAN EXPERIENCE?**

Latin America experience can give some elements to analyse the crisis in the Eurozone and its potential impacts in the economy and the society. The first lesson relates to the relevance of financial capitalism to explain the boom phases preceding the crisis and the importance of “non-national” elements to explain the boom. International organizations in the case of Latin America and the institutional organization of the Eurozone are relevant to explain the economic cycles and public policies.

The second lessons refer to the key role of the exchange rate and debt accumulation in the economic cycle. In current financial capitalism, the common feature during crisis time is that a large proportion of the financing needs must be covered from capital markets, reinforcing the power of financial organizations over the State which has to rescue all economic agents, including banks (in the first place).

The third lesson refers to the importance of the official rhetoric in order to understand how crisis adjustment will evolve. Blaming countries showing debt stress as “peripheral economies”, the official rhetoric looks to convince that problems should be solved within national boundaries. International organizations are the solution since they are supposed to know how to applied healthy fiscal adjustment and austerity measures taking distance of national pressures. In this way, the priorities seem to be debt payments and the rescue of financial institutions.

The fourth lesson is that debt management is crucial to understand post-crisis developments. Past crisis experiences in Latin American countries teach that some type of bail out and restructuring of the debt should be applied in order to reach substantial alleviation of the debt burdens over fiscal accounts. It is not possible to reduce debt burden through the alleged expansionary effects of low wages and austerity measures. The longest you apply austerity policies, the crisis risks to became systemic, affecting every part of the economy: banks, firms, households, states.

The fifth lesson regards the impacts of austerity policies on social division. When country governments chose to face domestic social and political conflicts in order to gain financial markets confidence about debt payments they provoke structural changes in society that will be difficult to reverse. Structural adjustment policies are the practical form to impose insecurity in labour markets, to cut social security coverage benefits and to advance more regressive income distribution. These are not “transitory costs”, but a huge change in the structure of the whole society. Along with the preservation of the financial system, the priority seems to be the preservation of the meritocratic structures of social security regimes. Conditional focalized programs could be expected to spread in the Eurozone looking for political control of losers (Lo Vuolo, 2014b).

However, alternative decisions to adjustment policies are not easy, mainly if we consider the heterogeneity among the Eurozone countries. Some critics of adjustment policies propose to indebted governments to default on their debts and exit from the monetary union, to allow a new currency to be depreciated in order to recover competitiveness. The experience of the Argentine recovery after the last financial crisis of 2001-02 is frequently cited in order to support this alternative.

This experience is not always well understood. The measures taken at that time have many economic and social costs and the recovery is explained for many external and short-lived factors (Lo Vuolo, 2007, Lo Vuolo, 2009b). Thus the sixth lesson is that the Argentine option has many risks. Mainly, the collapse of the banking system because banks holding government securities would become insolvent due to the reduction in the value of their assets and the increase, with the devaluation of the new currency, in the value of any euro liabilities that they may retain. Those banks would probably be subject to mass withdrawals of deposits as citizens in the countries exiting from the monetary union try to obtain cash in order to keep their savings in appreciating Euros.

The seventh lesson is that, even when Eurozone economies do not have exchange risk, they do have a specific liquidity risk of default similar to that of public debts issued in foreign currency in Latin America. The operation of the ECB as a credible lender of last resort for governments could alleviate this problem. But in order to play the role of other central banks, the ECB must necessarily make political decisions about which market or financial actor to support. In this option there will be winners and losers, too.

The eighth lesson is that politics and institutions are the key for the solutions. In the case of the Eurozone, the legitimacy of the ECB is not grounded in any political sovereignty and it is not even required to interact with country governments. Moreover, the Eurozone do not have any other mechanisms for region-wide macroeconomic regulation (beyond an arbitrary and uniform limit imposed on the public deficits). Meanwhile, austerity policies can erode the legitimacy of country governments. In this scenario, social institutions appear as inherently contradictory, unstable and involving no more than temporary compromises.

The ninth lesson is that a growing divide between winners and losers can be expected in the Eurozone as a result of austerity policies. Eurozone countries are facing more structural labour market exclusion, more low-paid employment, high levels of involuntary unemployment, and benefit dependency among those of working age. These are not transitory features of or a transitional economy but are becoming permanent elements of Eurozone countries. In short, financial and fiscal crisis of contemporary capitalism in different regions of the world can be viewed as part of the developmental continuum of society as a whole.

The tenth lesson is that even growth, if possible, would not be capable of solving these distributive conflicts. Recent events in Latin America are a good example of this. Even after years of growth after the crisis, structural economic and social problems are still there and countries that were considered as “emergent economies” are again facing serious economic problems that threaten their recent distributive gains recession (Lo Vuolo, 2015).

The development of assistance schemes shows that instead of a temporary cyclical change on the labour market, the increasing number of atypical workers, the development of long-term unemployment and the growing numbers of outsiders is a durable phenomenon that necessitates a permanent answer. In this way, the Eurozone seems to be institutionalizing a new type of highly fragmented labour market and social protection system, resembling what has been the case for a long time in Latin America.

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2. This paper is based on Lo Vuolo, 2014a. [↑](#footnote-ref-2)
3. In the US, the real state bubble that started with the securitization of mortgages (and other debts) and financial derivatives feed endogenously the booming phase, all processes well described in the work by Hyman Minsky (Minsky, 1977).The entry of China into the world market amplified this trend reversing the historic direction of capital flows that previously flew from the West to the emerging economies and then from China and other exporting countries to the US. These flows fuelled the expansion of credit that was further multiplied by the growth of securitization and derivatives trading, centred on the big banks. [↑](#footnote-ref-3)
4. Interestingly, after the European Council ratified the list of countries eligible for admission (May 1998) in few months the spread between the 10-year interest rate on public debt in Spain and the German rate fell from 5 per cent to zero (Aglietta, 2012). [↑](#footnote-ref-4)
5. More or less the same level of Greek spreads relative to German Bunds in autumn 2011. [↑](#footnote-ref-5)
6. Critical evaluations of the targeted and conditional income transfer programs themselves point to numerous problems, such as arbitrary selection of beneficiaries, interference into people's lives, political clientelism, stigmatization of recipients, incapability of achieving universal coverage and of acting preventively with regards to income poverty, fomentation of poverty traps and of informality, etc. (Lo Vuolo, 2012). [↑](#footnote-ref-6)