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Book Review

Book review: Sawyer, Malcolm (2018): Can the Euro be Saved?, Cambridge, UK and Malden, MA, USA (138 pages, Polity Press, softcover, ISBN 978-1-509-51525-7)

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Book review

Sawyer, Malcolm (2018): *Can the Euro be Saved?*, Cambridge, UK and Malden, MA, USA (138 pages, Polity Press, softcover, ISBN 978-1-509-51525-7)

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This small book by Malcolm Sawyer is exceptional. It explains in a very clear manner what one can call the euro problem: why the project of the common euro currency was based on shaky foundations; the consequent weakness of the euro area economy; the changes in the framework of the eurozone and that of the European Union that would need to be implemented for the common currency to become a successful endeavour; and the reasons for which these changes are unlikely to ever occur. Several other books have been devoted to the euro problem, one of which was reviewed in the pages of this journal (Niechoj 2017), but Sawyer's book is particularly illuminating as it presents a well-theorized, yet easily understandable, argument.

Sawyer argues that the euro crises that started in 2010 were not caused by the sub-prime financial crisis and the ensuing worldwide recessions, but they 'served to bring to the fore the weakness of the construction of the euro area and its policy agenda' (Sawyer 2018: 46). He argues that the eurozone project was more a political than an economic project, as was explained to me before its inception by Raymond Barre, the former prime minister of France. As a result the convergence criteria for entry in the Eurozone had to be 'fudged' (ibid.: 11). Sawyer insists that the countries of a successful and sustainable currency union must have highly similar inflation rates, not at a point in time (at entry) but for a long period before and after the creation of the currency union – a super fixed exchange-rate regime – for otherwise it will be unsustainable. No mechanism was put in place to achieve such aligned inflation rates. Furthermore, not enough attention was paid to identify the exchange rate that would be appropriate for the irrevocable rate to be sustainable.

As is now well known, the central government was given no powers to provide stabilization transfer payments to the various member countries. The Maastricht Treaty restrained the possibility for these member countries to pursue counter-cyclical fiscal policies, and these restrictions were reasserted with the advent of the badly named Stability and Growth Pact. Sawyer adopts the vocabulary of the modern monetary theory (MMT) when he claims that the borrowing of eurozone governments 'is in effect in a foreign currency' (ibid.: 37), meaning that these countries cannot rely confidently on an intervention of the European Central Bank (ECB) if interest rates on their sovereign debt start to rise, since the ECB will only take in government securities that carry a high rating. And while the ECB is an 'independent' bank, refusing to be coerced by national governments, the non-elected ECB bureaucrats are often keen to advocate fiscal consolidation and structural reforms, that is, fiscal austerity and lower wages. I would add that the ECB clearly exceeded its mandate by putting the screws on the government and banking system of Greece during the Tsipras episode.

According to Sawyer, these rules and conventions about government deficits and central-bank interventions played a key role in creating the euro crisis and in generating a recession

and then stagnation in Europe. The ECB, stuck in its ordo-liberal history, acted too little and too late in 2010 and 2011, only coming to its senses with the arrival of Mario Draghi, while the European Commission just made things worse by assuming that the crisis had been caused by excessive government borrowing, by reinforcing the fiscal rules of the Maastricht Treaty, and by imposing further structural reforms in the hope that a more flexible labour market would miraculously create a greater demand for labour.

The second part of Sawyer's book is devoted to what needs to be changed to improve the eurozone set-up and generate prosperity, and why these changes may never happen. First, fiscal policy at the central and national levels should be based on attempts to regulate economic activity and not based on some version of 'sound' finance. Second, there needs to be a large EU budget, which can pursue general counter-cyclical fiscal policies and provide fiscal transfers to countries hit by a negative shock. This would be financed by a progressive tax system (in particular a federal corporate income tax, so as to reduce fiscal competition between members). Third, the independence of the ECB must be terminated. The ECB should 'act to support rather than undermine the fiscal policies of member countries' (ibid.: 80). In other words, beyond its role of the lender of last resort of banks, it should act without any afterthought as the buyer of last resort of government bonds, Sawyer even contending that 'it should stand ready to directly lend to national governments' (ibid.: 81). Sawyer endorses the creation of the European banking union and its possible extensions. On the price inflation front, since he is not convinced that central banks are that efficient at controlling inflation, and since near-equal inflation rates play such a key role in sustaining a currency union, Sawyer favours the creation of national agreements on incomes and prices, so as to coordinate developments in wages and prices. Sawyer also advocates an EU-wide social security system as well as an EU-wide unemployment insurance scheme.

Obviously the above proposals, mostly inspired by Keynesian or post-Keynesian economics, face several barriers. Sawyer maintains that the current agenda of the European Commission is based on doubtful assumptions: unhindered markets generate full employment and stability, financial markets cannot be wrong, and fiscal discipline is a compulsory requirement. German ordo-liberalism, instead of Keynesian policies, seems to be gaining ground among European decision-makers. Some of Sawyer's proposals would require important modifications to the existing treaties, while others would necessitate a more substantial political and fiscal union, which is likely to attract a strong political resistance. All in all, my reading of Sawyer's text is that he is rather pessimistic, as he concludes that 'the political forces which could shift economic policies in the directions suggested are weak or non-existent. ... Yet, unless profound reforms are made, the euro area, and more importantly the people of the European Union, face an uncomfortable future' (ibid.: 122).

Sawyer's book seemed so clear and convincing to me perhaps because I fully agree with his analysis! My only objection is when he writes that 'a balance-of-payments deficit in one country implies that the reserves of that country's central bank held at the ECB are falling' (ibid.: 65). In reality, such a deficit implies a fall in the TARGET2 balances of that country, but since (and this was perhaps the best feature of the eurozone set-up!) there is no limit as to how negative these TARGET2 balances can become, such a deficit is not a true financial constraint.

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