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Europe Suffers A Failure On The Part Of Its Leaders To Lead

By Alberto Mingardi

European leaders have been meeting regularly to resolve the European crisis since its eruption. After every one of these "summits" they manufactured new institutional devices, hoping to calm markets down. As the tempest continues to rage, a perception is emerging that the old continent has taken on "austerity" measures to the point of endangering its own growth prospects.

By committing to fiscal discipline, are member States making the current recession even worse, dragging Europe into a spiral of poverty and despair? No. The problem is not fiscal consolidation per se—but in the means chosen to pursue fiscal consolidation: higher taxes rather than cutting spending.

According to the European Commission, member states must strive to produce primary surpluses worth on average 0.9% of GDP (Germany), 4.3% of GDP (France), 4.7% of GDP (Italy), 6.9% of GDP (Greece), and 8.1% of GDP (Spain) over the next three years to meet the budgetary consolidation requirements. These figures are unattainable in the context of a severe recession. Primary surpluses of this kind cannot materialize without robust economic growth.

Austerity, in the shape being pursued nowadays in Europe, relies basically on heavier taxation—and not on robust spending cuts– which pushes fiscal balance further out of reach.

European governments are large and intrusive. Neither Italy, France nor Spain, let alone Greece, has ever known the kind of privatization cure Margaret Thatcher administered to Britain, though it should be said that Italy privatized rather extensively, in the 1990s. Despite that, the state owns insurance companies, stakes in major energy companies, the postal service, the train service, local transportation, a cornucopia of local "public services" not particularly renowned for their efficiency in delivering—but obviously dear to the political class, as a means to keep their grip on the Italian economy. The same can be said for other Mediterranean countries.

What is indeed astonishing is that, in this context, nobody seems to be ready to try the straightforward device to trim the public debt by virtue of selling the huge Italian state holdings or severely cutting public spending. Instead, the political class seeks to squeeze its already highly taxed citizens like lemons.

"Privatization", on the other hand, remains an almost unspeakable word. Governments claim to fear selling "below the right price"—a strange characterization of assets that are not on the market, and whose value is thus unknown. Actually, they simply want to have their cake and eat it too: they dream of a way out of a crisis generated by an excess of public debt that does not entail a retrenchment of government activities.

Italy's public spending is worth half of the national income and, net of pensions public employment makes up the lion's share. A country of 58 million, Italy employs over 3 million in its public service. The Monti government announced spending cuts recently, but retreated rather quickly. "Provinces," a middle-ground government level between regions and municipalities, will not be eliminated. Smaller public hospitals will

not be closed down. Public employment will not be cut substantially—as trade union leaders have already announced a general strike in retaliation, if ever the unthinkable were to happen.

A government report estimates € 295 billion of a total of € 728 billion of the public spending that can be tackled. The most likely outcome of the government "cuts" will be paltry savings of € 4.2 billion s in2012, followed by €10.5 billion in 2013. This is hypocrisy—an ostensible tribute paid to the virtue of constraining government. The French are not even trying to be hypocritical, as Mr. Hollande seems to believe that soaking the rich will be enough to spare his country from tragedy.

The timidity of national governments is now the real threat to the survival of the European Union. Italy's public debt, at about €2,000 billion is over 120% of its GDP. Recognizing this to be an exceptional problem should bring the Italian government to take new, bolder courses of action – but it has not.

The problem is political, and won't be necessarily solved by another European governance arrangement. On the one hand, as the "senior partner" of the EU, Germany is calling its fellow member states to adopt a degree of fiscal responsibility, but it cannot dictate what mixture of higher taxes and lower spending any of them shall pursue. On the other hand, consensus is trumping reality: national governments estimate the political cost of cutting public employment to be too high, particularly in a recession and fear the possible social unrest this would likely cause. Blaming financial markets, Mrs. Merkel, or the euro for their current predicament is much cheaper.

The sad truth is that the problem in Europe today is not too little public spending; instead, it is missing strong leadership. In "The Iron Lady" movie, Meryl Streep as Margaret Thatcher refuses to renounce her plans to cut spending as recommended by her cabinet colleagues fearing electoral losses. Mrs. Thatcher had a vision, the vision of a lighter government to unleash Britain's energies, and a remarkable taste for saying "no." Europe's current leaders have neither.

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