Opinion&Analysis

QUOTE OF THE DAY

If you do not enter the tiger's cave, you will not catch its cub. – Japanese proverb

Euro zone crisis: What motivates Germany

STRUCTURAL REFORMS

Klaus Zimmermann

IN THE GLOBAL debate about the euro zone crisis, Germany has come in for a lot of criticism. The German position has been described as engaging in a "morality tale" (aimed at forcing other countries to pay back their debts).

Alternatively, it is regarded as a display of "nationalism" (by just pursuing narrow German interests) – if not as practising "hegemony" (by seeking to impose a German model on to the rest of Europe).

I am struck by how much these descriptions – juicy as they are in purely journalistic terms – miss what really drives the German government. To see what the real driving force is, just ask yourself this question: Why do Germans talk so much about the need for structural reforms in Europe?

German policymakers are painfully aware that, among the advanced economies, there is one major country where structural reforms – such a touchy matter in Europe – really are no political issue. That country is the US.

The US has the immeasurable advantage that embracing change on a continuing basis is simply built into its national DNA. Nobody there is asking for permission to engage in it. Change is simply happening all the time.

Much of the same is true in many of the dynamic emerging markets, especially in Asia. Like it or not, those are realities Europe has to contend with.

Unprepared

Next, ask yourself why Germany is so insistent on pursuing structural reforms in Europe. Because without them, Europe's mostly ageing societies are going to be woefully unprepared for the future. That would have a definite negative impact on Europe's growth in the future.

This explains why, from the German perspective, the current battle over Europe's economic future is not at all about Greece. Nor is it about the debt issue or "austerity". The underlying challenge is much larger than reform issues in one small country or implementing proper budgetary controls.

Rather, it is about how to make Europe's economies more flexible – via structural reforms. If the German government has a mission or a vision, then it is to do its part to ready Europe for the 21st century.

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A key ingredient is the need to reduce the public sector's share of national gross domestic product (GDP). That, too, is a task that is adopted in direct response to considering the US economic model and in view of the challenge from Asia.

Of course, none of these reforms can be formulated or applied in any cookie cutter fashion. Every country has its own peculiar mix of legacy issues to contend with (notably including Germany, which must continue on its own reform path).

Accordingly, contrary to an oft-heard argument in the international debate, very few decision makers in Germany actually think that other countries ought to apply "the German model". What is relevant about the German experience is the political dimension: If the continent's largest economy has accepted the need for reforms (and acted on it), then it is wise for all of its European partner nations to do the same. The good news is that many have done so.

Criticism

It is also appropriate for Germany to be clear about expressing the need for those nations who lag behind in the effort to do their homework – just as other nations point to Germany's weaknesses. Everybody needs constructive criticism and use it as motivation.

The alternative, putting one's head into the sand by sticking mindlessly to ways of managing an economy that are plainly out of whack, is a recipe for disaster.

Advocating for the need for change in Europe due to global realities is the very antithesis of nationalism. Doing so also has nothing to do with any hegemonic attitude on the part of Germany. If anything, it is leadership by example. And it certainly is no morality tale. It simply is the reality in which Europe has to operate – now that we have a truly global economy.

None of that means making short shrift of the balanced social model Europeans have come to appreciate. For example, Germany's approach to co-determination in industry – that is, involving the workforce in management decisions – has proven to be a pro-competitive force. Crucially, it has made German companies more nimble in reacting to global circumstances.

In conclusion, the German government's focus is neither on "Germanising" the rest of Europe nor is it on "Americanising" or, for that matter, "Asianising" it.

Given that rigid labour market structures mainly hurt the young generations, EU member governments have the clearest – and democratically legitimised – incentive imaginable to shape up. Breaking up those outdated structures is not done "for the Germans" – but first and foremost for these nations' own sake.

For that to happen, the key issue is to unravel the sweetheart deals among favoured groups in society (usually older, usually from the establishment) that are no longer affordable. Nations who fight necessary change do so at their own peril.

Succeeding in that battle is the best way to ensure that Europe has a common, prosperous future and is positioned to contribute its share to global growth in decades to come.

Klaus Zimmermann is the director of the Institut zur Zukunft der Arbeit, based in Bonn, Germany

Fragile Five currencies may soon be three

EMERGING MARKETS

Simon Kennedy

IN AUGUST 2013 as the US Federal Reserve considered when to slow its quantitative easing, Morgan Stanley identified the five major emerging markets with the most vulnerable currencies: Brazil, India, Indonesia, Turkey and South Africa.

Now, as Fed officials debate how soon to raise interest rates for the first time since 2006, India and Indonesia may have dodged the bullet. Morgan Stanley economists said they had enacted enough economic reforms to have passed "the point of inflection away from their old models of growth".

In India's case, inflation has halved since the end of 2013 and its current account deficit has shrunk. Investors have embraced Prime Minister Narendra Modi's pledge to cut red tape and he is also acting to reduce the budget shortfall. Governor Raghuram Rajan won a legal mandate for the Reserve Bank of India to target inflation. The rupee has even eked out a 1 percent gain versus the dollar this year.

Meanwhile, Indonesia has taken positive steps with President Joko Widodo's five-month administration scrapping fuel subsidies and aiming to cut the budget deficit to 1.9 percent of gross domestic product (GDP).

All told, the Morgan Stanley economists reckon India has completed 85 percent of the necessary adjustment and Indonesia 65 percent. The remaining Fragile Five have made much less progress. Morgan Stanley said Turkey had completed no more than 10 percent of recommended reforms, Brazil 15 percent and South Africa barely anything.

Current account shortfalls and inflation remain high in each and politics in the form of a widening corruption scandal at Petroleo Brasileiro, or Petrobras, in Brazil and lawmaker pressure on Turkey's central bank are worrying investors. Such an environment has reduced their ability to cut interest rates and Brazil and South Africa may even hike them this year.

More pain before any gain is the scenario Morgan Stanley economists see: Higher Fed rates and a rising dollar could help impose a "catharsis" and force them to act. – Bloomberg

Is Europe now showing signs of a continent overwhelmed?

the Globalist

GLOBAL ECONOMICS

Stephen Green

A GENERATION after the fall of the Berlin Wall, the reunified Federal Republic of Germany is becoming the reluctant leader of a new Europe. But it does so at a time when there is an existential question about the very identity and the whole future of Europe.

The question is one for all Europeans, but it must weigh most heavily on that inevitable and reluctant leader.

Europe is now in a long-term relative decline, both politically and economically. It is no longer the energetic, ambitious and aggressive continent it was when the Portuguese, the Spanish, the Dutch, the French and the British set out over the oceans to plunder, trade and colonise.

Europe also is no longer the continent whose technical brilliance the Chinese emperor Qianlong so notoriously spurned when Lord George Macartney sought to open commercial dealings with China in 1793. It is no longer the continent where an aggressive Germany sought to settle and Germanise vast tracts of Slav land to the east and unleashed a campaign of unbelievable brutality in pursuit of that goal. And it is no longer the front line of a Cold War between two superpowers with the capacity to destroy themselves and everyone else many times over.

Europe has retreated from being the self-defined centre of the world to being what it had been before the 15th century – a corner of the Eurasian land mass. It remains fertile, populous and wealthy, but it is profoundly uncertain about its identity and its future.

France and Britain – alone of all those former great powers – still lay claim to the ability to project military might over long distances, and they still preserve the legacy of their former global roles in the form of permanent seats with veto power in the Security Council of the UN. But neither any longer has the strength or the mass to sustain a significant military campaign alone.

Yet at no point in the decades after the war has Europe been able to develop any credible collective ability to project independent power. Looking forward, it is clear that it does not even want to do so.

Economic decline

Europe is also in relative decline as an economic force, not just as a locus of political power. Having led the world during the first industrial revolution of the 19th century, it then saw the centre of gravity shift away across the Atlantic at the beginning of the 20th century and especially after World War I. After the massive destruction of World War II, the US was firmly ensconced as the overwhelmingly dominant economic power.

At least this meant that (Western) Europe could position itself as part of a transatlantic relationship with shared interests, a common commitment to democracy and – up to a point – a common economic approach. As a result, Western Europe's economy grew rapidly for a while as it recovered from devastation, bringing the people of Europe a degree of widespread prosperity they had never known.

But this proved to be only an interlude. For since the epochal year of 1989, the rise of Asia has driven a new and historic shift of the centre of global economic gravity, this time to the east. The re-emergence of China as a great power, and the modernisation and urbanisation of so many countries in Asia – and increasingly in other continents which had in a previous era been dominated by imperial powers from Europe – have contrasted sharply with a sustained sluggishness in the old economies of Western Europe.

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Even if all had gone well for the Europeans, there would have been a decline in their share of the world's income. And they would have had to become used to dealing with new actors on the world stage.

But in fact the European performance has been weakened. This is partly due to the extreme stress within the euro zone, and partly to the global financial and economic crisis which was unleashed in 2008. So the crisis has, if anything, accelerated the historic shift towards the East. Europe is left struggling to find a secure foothold in a global marketplace that is becoming more interwoven – and where its ever-more sophisticated eastern competitors are conscious that their time has come.

China and the US may be wary of each other. However, both recognise that Europe is losing its historical significance. For Europe, loss of market share was of course inevitable. That has been the fate of all the early developers, including both the US and Japan.

It is the result of a historic reversion to the norm: Before the 19th century a country's share of global output was roughly in proportion to its share of world population. Then as now, China had the largest population in the world – and, as late as about 1820, China had the world's largest economy.

That changed with the onset of the industrial revolution. It enabled, for the first time in human history, some economies to produce consistently above subsistence level, thus creating a gap between the two ratios.

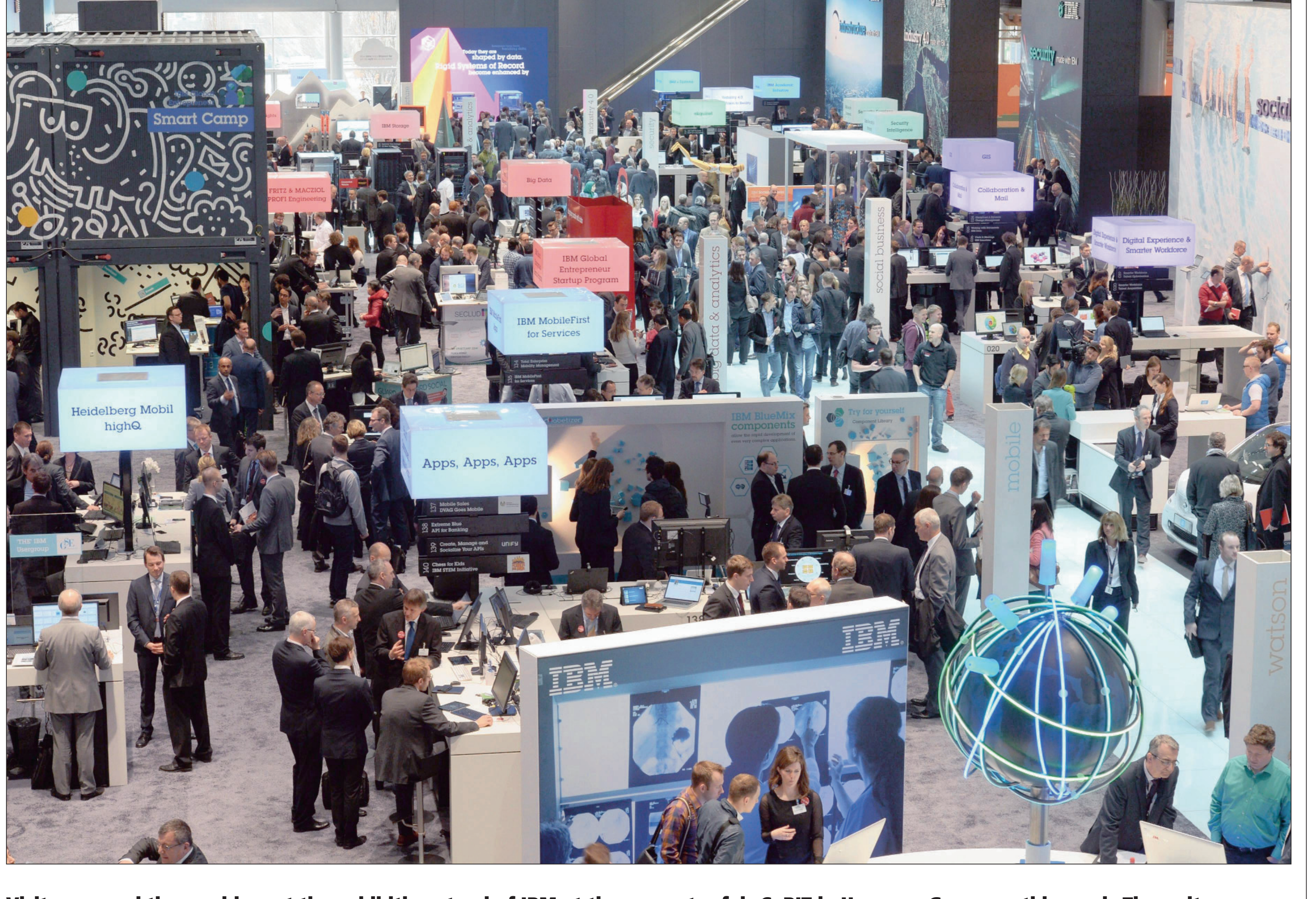
It was the Europeans first, then the Americans, and later the Japanese, who thus achieved enormous increases in world market share. At their peak, these developed countries represented less than a fifth of the world's population, but created around three quarters of world gross domestic product.

The gap is now closing again, as not only China but also country after country in Asia (and elsewhere in the emerging world) start to catch up with the standards of living that Europeans have come to take for granted. By 2020, on present trends, China may well be the world's largest economy again. This great convergence, with all that it implies, is the most important fact about the first half of the 21st century.

This is the great challenge to Europe. Its response to this new reality – to the new economic and cultural competition – has been underwhelming.

Editor's note: The above text is adapted from *Reluctant Meister: How Germany's Past is Shaping Its European Future* by Stephen Green, Haus Publishing (December 15, 2014)

This article initially appeared on The Globalist. Follow The Globalist on Twitter: @Globalist



Visitors crowd the corridors at the exhibition stand of IBM at the computer fair CeBIT in Hanover, Germany, this week. The writer says Europe's economic performance has been weakened partly due to the extreme stress within the euro zone, and partly to the global financial and economic crisis, which was unleashed in 2008. PHOTO: EPA

Agoa benefits outweigh any sector interests

RIGHT TO REPLY

AMBASSADOR Faizel Ismail's article "Agoa is of mutual benefit to SA and US" (17 March) is a crucial reading for readers who care about growth in Africa, South Africa and the future of US-Africa relations. The ambassador carefully explains the reasons behind the unfortunate hold-up in Agoa renewal talks.

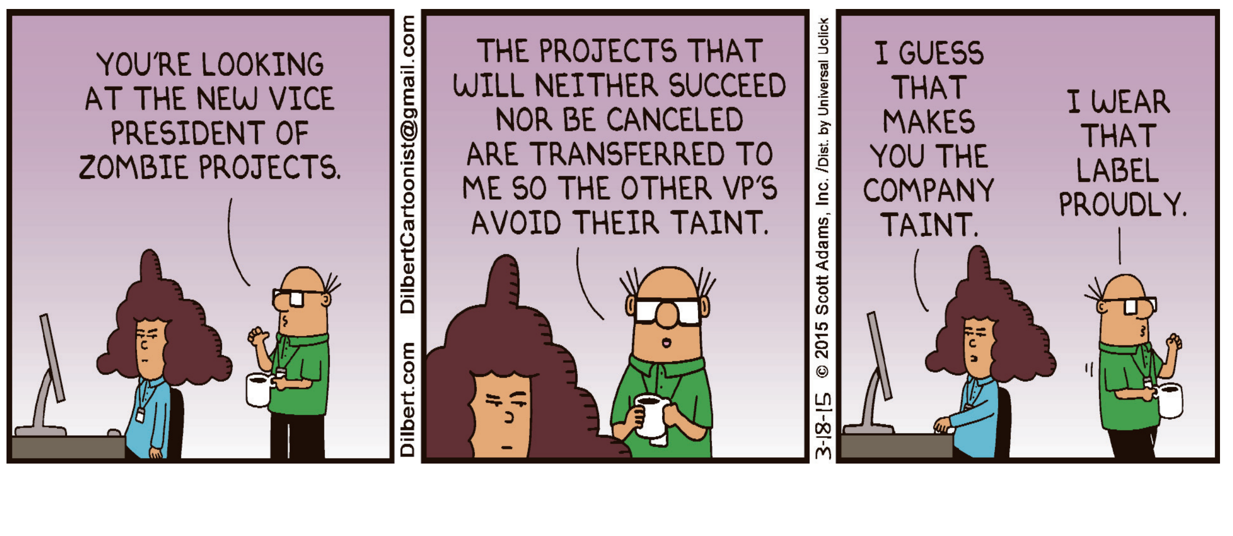
Ambassador Ismail, South Africa's special envoy on Agoa, makes a reasoned and responsible argument for Agoa's renewal. His article importantly notes that Agoa has played a tremendously positive role in job creation and economic growth in South Africa. More broadly, Africa has a vested interest in seeing South Africa's inclusion in the agreement renewed.

We should also remember that the World Trade Organisation has subsequently discredited the costing system that was used by the International Trade Administration Commission of South Africa (Itac) in the original anti-dumping investigation of US exports. Applying currently acceptable costing methods, it would be unlikely that any dumping by the US would have been found by Itac.

As the ambassador notes, we simply cannot allow the "narrow vested interests" of the South African Poultry Association (Sapa) to discontinue the essential economic benefits that Agoa brings to South Africa and the continent as a whole.

DAVID WOLPERT
CHIEF EXECUTIVE OF ASSOCIATION OF MEAT IMPORTERS AND EXPORTERS OF SA

DILBERT



DIARY

Study shows that money corrupts even the most honest

THEY say money can corrupt even the most honest of people. Now one social psychologist has revealed a series of experiments that shows this adage to be true.

Instead of transforming people into charitable benefactors, Professor Paul Piff believes money causes people to break the rules at the expense of others.

"It makes you more attuned to your own interests, your own desires, your own welfare," the University of California researcher told Lucy Hooker at the BBC.

"It isolates you in certain ways from other people psychologically and materially. You prioritise your own needs and your own goals and become less attuned to those around you. In one experiment, Piff spent an afternoon going back and forth over a pedestrian crossing in Los Angeles.

He found that none of the least expensive cars broke the law, while almost 50 percent of the most expensive car drivers sped across the pedestrian crossing.

In another study, Piff brought in more than 100 pairs of strangers into the lab, and flipped a coin to assign one of them to be a rich player in a rigged Monopoly game. The rich players collected twice the salary when they passed Go, and were able to roll both dice instead of one, so they got to move around the board more.

Hidden cameras revealed that rich players became ruder toward the other person, less sensitive to the plight of the poor players, and more demonstrative of their material success. – Daily Mail