Submission to the European Parliament Economic and Monetary Committee

On austerity and the Troika's engagement with the euro area programme countries

Introduction

Social Justice Ireland is an independent think-tank which advances the lives of people and communities through providing independent social analysis and effective policy development to create a sustainable future for every member of society and for societies as a whole. We work to build a just society through developing and delivering credible analysis and policy to improve society and the lives of people. We identify sustainable options for the future and provide viable pathways forward. In all of this we focus on human rights and the common good.

We welcome this opportunity to present our views on austerity and the Troika's engagement with the euro area programme countries. We welcome it especially for three reasons:

- We met with the Troika on twelve occasions during Ireland's three-year Bailout programme. For each of these meetings we prepared detailed briefing material focused on analysing the approach the Troika took, identifying its various impacts, particularly on people who are poor and/or vulnerable, and identifying pathways forward that would reverse the hugely negative impacts that were emerging.
- In 2012 we conducted the first ever study of the impact of the policies being followed by the Troika in the five EU countries most at risk (Greece, Portugal, Ireland, Spain and Italy). This study was published by Caritas Europa, who had commissioned it, on February 14, 2013.
- In 2014 our second study of these five countries together with Cyprus and Romania will be published by Caritas Europa.

In this submission and presentation to the European Parliament Economic and Monetary Committee we:

1. Argue that The Troika approach in programme countries was NOT based on evidence.
2. Suggest that a response based on evidence would have primarily focused on eliminating the problems that had arisen in the irresponsible financial sector.
3. Critique the austerity pathway followed by the Troika (arguing that it has an unsound academic basis; has been a failure in practice; and is morally unethical).
4. Show how selective use of data by the Troika led to inaccurate analysis which, in turn, led to inappropriate policy proposals being made. We provide five examples of this process from among those we presented to the Troika during our meetings in recent years.
5. Highlight issues that arise for the European Union on the social dimension of policy and on governance. These flow from the experience of programme countries in recent years.
6. Look to the future. Under this heading we provide elements of a guiding vision for the future and we outline five pillars of policy that should be included in all country programmes and should be monitored in their implementation throughout the programme's timeframe. We also suggest some recommendations we believe should be included in the Committee's final report.

1. Troika approach was NOT based on evidence

1.1. *Evidence versus assertion*

In an interview given to six major newspapers in six different countries[1] and published on 26th January, 2012 the German Chancellor Angela Merkel argued that austerity was necessary because of the budgetary negligence of countries over many years. She emphasised the "extreme debt of certain countries, accumulated over many years".

This is an example of a selective use of data that led to an inaccurate analysis which in turn has led to an inappropriate policy response. What is demonstrably false has been accepted as self-evident; this is a dramatic illustration of the failure of politicians, public officials, academics and commentators who have constantly supported this position.

Inaccurate analysis is not confined to Angela Merkel. On 21st October 2012 *Social Justice Ireland* published a briefing[2] it had presented to the Troika (European Commission, European Central Bank and the International Monetary Fund) during their quarterly monitoring visit to Ireland. The key issue addressed in that briefing was what *Social Justice Ireland* described as "the selective use of data by Troika organisations which is leading to inaccurate analysis which in turn is producing inappropriate policy recommendations for Ireland". Some aspects of this briefing are addressed in section 4 of this submission.

The briefing we made to the Troika at the time highlighted the selective use of data by Troika members in the analysis and documentation they had produced during the previous year. This was leading to inaccurate analysis which in turn was leading to inappropriate policy proposals being made.

Five examples of this selective use of data were identified in the briefing. These concerned (i) the poverty rate, (ii) reducing unemployment payments over time, (iii) increases in welfare rates in the previous decade, (iv) replacement ratios and (v) the distribution of the 'hits' during the recession. In each of these cases the *Social Justice Ireland* briefing identified the selective use of data in Troika publications, showed how this led to inaccurate analysis and this, in turn, led to inappropriate policy proposals.

1.2. Was there 'budgetary negligence and extreme debt accumulated over many years'?

Let's look at the evidence for Angela Merkel's claim. The public finances of member states in the EU before 2008 were keeping to the convergence criteria of the Stability and Growth Pact (de Grauwe 2011). In 2007 the average budget deficit of the 27 member states of the EU was 0.9 per cent of GDP. This is a long way below the 3 per cent threshold.

Public debts show a similar pattern. From 1999 to 2007 the average public debt of the EU member states went from 65.7 per cent of GDP to 59 per cent. This is below the 60 per cent threshold that applies to this issue. In the following three years this average rose to 80.1 per cent and has continued growing since.

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[1] The interview was published by El Pais (Spain), the Guardian (Britain), La Stampa (Italy), Le Monde (France), Gazeta (Poland) and Süddeutsche Zeitung (Germany).

[2] Available at www.socialjustice.ie

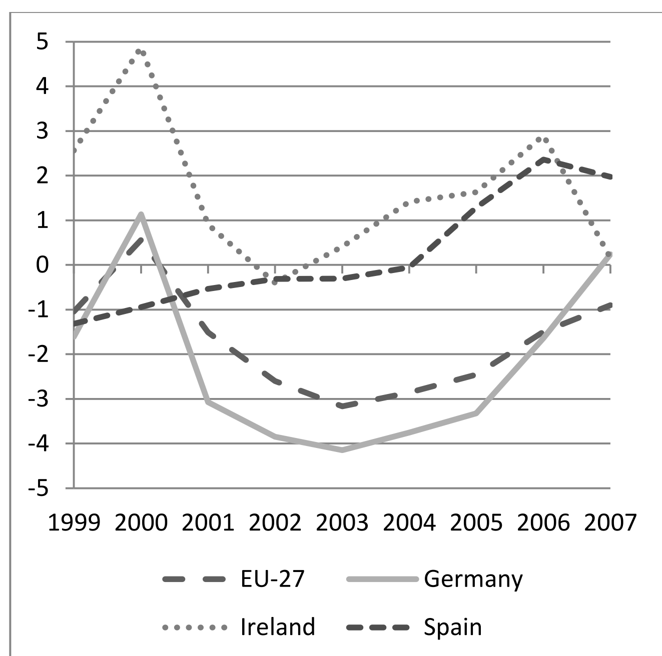
In the period 2000 to 2007 the only Budget deficit in Ireland was in 2002; even then it was minus 0.4 per cent of GDP which is very low. In all other years during that period it was in significant surplus. By 2010 it had reached minus 32.4 per cent of GDP because of the bailout of the financial sector. In another country currently at risk, Spain, in the period 2005-2007 there were budget surpluses (see Table 1 and Table 2).

The fiscal position of Spain and Ireland sharply reversed in 2008 due to the bursting of credit fuelled asset price bubbles, which had been inflated by poor regulation of both the banking sector and commercial and residential construction sectors.

This situation is summarised well by Christohe Degryse: "With the exception of Greece – which is a special case – there has been no general drift that might have justified the constriction of budgetary rules and the imposition of forced austerity. The great upheaval has resulted from the bailout of the banking and financial industry and support for the real economy to avoid a great depression" (Degryse 2012).

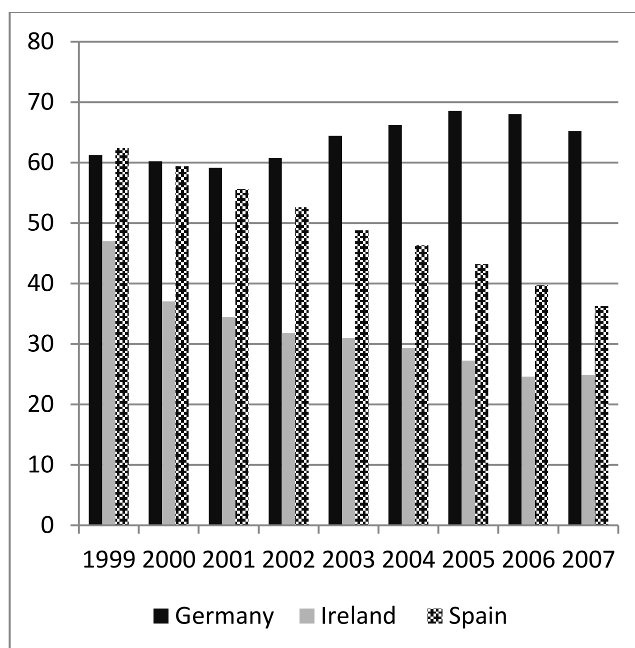
He goes on to cite Martin Wolf in support of this position: "it is not budgetary indiscipline that was at the origin of this crisis. The indiscipline of the financial sector and, generally speaking, of the private sector, including lenders in the countries at the heart of the zone, played a much more important role" (Wolf 2011).

Table 1 – General Government Net Lending (+) or Net Borrowing (-) for selected countries, 1999-2007



Source: AMECO database (2013).

Table 2 - General Government Gross Consolidated Debt as a % of GDP in selected countries, 1999-2007



Source: AMECO database (2013).

2. What would a response based on evidence have looked like?

2.1. How not to respond to an irresponsible financial sector

An accurate analysis would identify that the crisis of 2008 was caused by the financial industry, how it was framed and regulated and how it operated in the real economy. Such an analysis should have led on to the development and implementation of measures at an EU level to regulate financial institutions and to secure good governance in this area.

Such initiatives could have included rigorous regulation of the sector, the introduction of a financial transaction tax, the elimination of tax havens, the tackling of financial fraud and tax evasion, the separation of commercial and investment banking, and so on. Little if anything effective was done in these areas. Instead what we did get - especially from 2010 onwards - has been a very strong focus on the false claim that the crisis was caused by a catastrophic profligate drift in public finances.

The capacity and success of the financial sector to delay introduction of the necessary changes has been in inverse proportion to the social resistance to austerity. The financial sector has got most, if not all of its money back, bank debt has been transferred to the sovereign and the bills are, for the most part, being paid by ordinary citizens who had no hand, act or part in causing the crisis.

Since 2009 *Social Justice Ireland* has consistently pointed out that this was the likely outcome of the policies put in place to address the 2008 crisis. The analysis was not accurate so the policy pathway has been inappropriate. In 2010 Paul Krugman, Nobel Prize winner in economics, pointed out that erroneous diagnosis by Europe's leaders was producing bad remedies (Krugman 2010).

The EU has focused principally on increasing supervision of public finances and introducing draconian sanction mechanisms in cases where thresholds are crossed or targets are missed. The Fiscal Compact which has become part of the European Treaty has imposed extraordinary limitations on any country trying to work its way back to fiscal solvency and to produce high levels of employment for its labour force.

The justification for this approach is that it 'reassures the markets' so that they continue to provide finance to governments at low interest rates (while making it exceedingly difficult for groups such as small and medium enterprises to borrow at any interest rate). The former president of the European Central Bank, Jean-Claude Trichet argued that this approach was necessary to satisfy the financial markets. The ECB, the European Council and the Ecofin Council also argued that the first priority was to re-establish the confidence of these markets.

A series of initiatives were to be prioritised. In practice this meant the 'social' component of government policy in practice became the main adjustment variable in the management of the debt crisis. Social services and the social infrastructure that supports the delivery of such services were reduced dramatically and the savings used to support the on-going dominance of a financial sector that had gambled recklessly, acted illegally in some cases and succeeded in having much of their gambling losses repaid, in many cases repaid in full.

To this end austerity was imposed.

3. Critique of the Austerity pathway followed by the Troika - a road to nowhere

Austerity has been exposed as:

- Having an unsound academic basis,
- Being a failure in practice, and
- Morally unethical because poor and middle-income people have borne an unfair share of its consequences.

Let us look at these three issues.

3.1. Austerity has an unsound academic basis

This is an extraordinary story. The key academic study used to justify austerity in recent years in countries such as Ireland was been exposed as profoundly flawed.

The authors of the study made mistakes by omitting several countries that should have been included, by using a wrong mathematical formula in its spread-sheet and by providing unusual weights to various countries. The end result is that when corrected the data shows the opposite of what was originally claimed.

This is more than a trifle ironic as this flawed study was cited to support their case for austerity by policy makers ranging from European Commission Vice President Olli Rehn to President Obama's Treasury Secretary during his first term in office Timothy Geithner, from George Osborne, the UK chancellor to Paul Ryan, the US congressman who was the Republican Party's candidate for Vice President in the November 2012 election.

Here's the whole story. In January, 2010, two Harvard economists published an academic paper that addressed the biggest policy question the world was facing i.e. should public spending be reduced to stop the rise in a nation's borrowing or should the state invest resources to generate economic growth as the pathway out of recession? The paper was titled "Growth in a Time of Debt" and was written by Carmen Reinhart and Kenneth Rogoff. The main conclusion from Reinhart-Rogoff was that countries with a debt-to-GDP ratio above 90% have had a negative growth rate (i.e. they declined), on average, since 1946.

Having studied a sample of 20 advanced economies over the post-war period Reinhart-Rogoff claimed that average annual GDP growth ranged between about 3% and 4% when the ratio of public debt to GDP was below 90%. But average growth collapsed to -0.1% when the ratio rose above a 90 per cent threshold.

This notion had and continues to have huge implications for Europe, where debt-to-GDP ratios are near the theoretical danger zone. It was especially important for countries such as Ireland whose debt/GDP ratio was heading towards 100%+ at that time.

On April 16, 2013 a new study was published which shows that Reinhart-Rogoff made a series of mistakes that have profound implications for policy on austerity. This paper, written by three economists at the University of Massachusetts, (Thomas Herndon, Michael Ash and Robert Pollin) tried to replicate Reinhart-Rogoff's 2010 results and found them guilty of excluding data, spreadsheet errors and unorthodox weighting of certain countries.

The new study finds that Reinhart-Rogoff omitted crucial data from Australia, Canada and, particularly, New Zealand, which changed the entire conclusion of their paper. When this and other mistakes are corrected the average growth rate for countries with debt-to-GDP ratios above 90% was +2.2%, not -0.1% as Reinhart-Rogoff claimed. The academic basis that has been used to justify the on-going insistence on austerity has now been shown to be false.

There is an additional problem with the Reinhart-Rogoff thesis. It may well have got the direction of the causation backwards i.e. it may well be that low economic growth leads to high levels of government debt, not the other way around. That is material for another day. The key issue is that one of the main pillars of the academic justification for austerity has been discredited.

Writing in the *Financial Times on April 19, 2013* Ash and Pollin state:

> "Of course, one could say that these were special circumstances due to the 2007-9 financial collapse and Great Recession. Yet that is exactly the point. When the US and Europe were hit by the financial crisis and subsequent collapse of private wealth and spending, deficit-financed government spending was the most effective tool for injecting demand back into the economy. The increases in government deficits and debt were indeed historically large in these years. But this was a consequence of the crisis and a policy tool for moving economies out of the deep recession. The high levels of public debt were certainly not the cause of the growth collapse.
>
> The case for austerity has never relied entirely on Prof Reinhart and Prof Rogoff. But the other major claims made recently by austerity hawks have also not held up well. Focusing on the US case, austerity supporters circa 2009-10 consistently argued (frequently in this newspaper) that the large US deficits would lead to dangerously high inflation and interest rates. Neither of these predictions came true. In fact, both inflation and the interest rates on US Treasuries were at historic lows in the four years, 2009-12, during which government deficits were at their peak.
>
> It is also not true that the large deficits have created an unsustainable burden on US government finances. In fact, since 2009, the US government's interest payments on debt have been at historically low levels, not historic highs, despite the government's rising level of indebtedness. This is precisely because the US Treasury has been able to borrow at low rates throughout these high deficit years.
>
> **We are not suggesting that governments should be free to borrow and spend profligately. But government deficit spending, pursued judiciously, remains the single most effective tool we have to fight against mass unemployment caused by severe recessions.** Recent research by Prof Reinhart and Prof Rogoff, along with all related arguments by austerity proponents, does nothing to contradict this fundamental point." (emphasis added)

Throughout the years of the Troika engagement with Ireland, *Social Justice Ireland* constantly called on Government to increase its investment programme substantially and called on the Troika to enable such investment to be prioritised. We did this because of our conviction that without investment there won't be jobs; without jobs there won't be prosperity; without prosperity we'll be stuck in austerity. This has been our publically stated and often-repeated position since 2009.

3.2. Austerity has been a failure in practice

What austerity has produced in practice in Ireland is structural unemployment, rising poverty levels, a sustained child poverty problem, on-going adult literacy challenges, high emigration, lengthening social housing waiting lists and declining physical and social infrastructure.

The Irish Government's austerity approach has, however, protected the rich at the expense of the rest of us. In practice it has produced the single biggest transfer of resources from low and middle income people to the rich and powerful in Ireland's history. The main beneficiaries of this transfer have been parts of the corporate sector (mostly multinationals) and wealthy individuals.

This situation has been mirrored in other vulnerable countries. In the period 2010-2012 substantially more than €700 billion in public spending cuts were decided on in fifteen EU countries[3] (Degryse 2012). These cuts, for the most part, were made in the areas of social protection, public employment and public investment. In most cases the budget cuts were accompanied by tax rises particularly VAT (which disproportionately impacts low-income people) and wage freezes.

This is a road to nowhere. The austerity approach has been challenged by a wide range of people and institutions. While all agree that it is crucial that countries manage their finances in a responsible manner and pay their way over time it is clear that the 'austerity' approach is based on a deeply flawed analysis and that a change of direction is needed if we are not to "cause the economic suicide of the entire continent" (Krugman 2012).

3.3. Austerity has been morally unethical

We have seen that the austerity approach adopted by the EU and promoted by the Troika was not based on an accurate analysis of causes, on a credible economic theory or on sound research. The moral basis for this approach has also been unethical. The bond-holders and gambling bankers who caused much of the crisis have been repaid in full and have made no contribution to rescuing society from the mess they created.

In practice it was those on low and middle incomes who have borne the brunt of the adjustment rather than the rich and powerful. This has been dramatically illustrated in Ireland's case.

In his contribution to *Social Justice Ireland*'s conference '*A Future Worth Living For*' (19th November 2013) Dr István Székely of the European Commission noted that the cumulative consolidation efforts of the 2009-2013 period were progressive. He stated that the Budgets of that period took more as a percentage of total ***income*** from those higher on the income distribution scale than those lower down the income distribution scale. He cited research by the Economic and Social Research Institute (ESRI) to support his claim. While this statement is, strictly speaking, correct it is only ***a part of the truth***.

It is important to realise that a single piece of data, while accurate in itself, can often lead to a false interpretation of the overall reality. It is essential that all the relevant data be made available so as to ensure that the analysis is accurate. Otherwise a selective use of data can produce an inaccurate

[3] Austria, Belgium, Cyprus, Czech Republic France, Germany, Greece, Hungary, Ireland, Italy, the Netherlands, Portugal, Romania, Spain, United Kingdom.

analysis which in turn can lead to inappropriate policy recommendations being made and implemented.

For example, the data cited by Dr Székely, as he clearly pointed out in his paper, referred to the impact of **Government Budgets** on people's income.

However, many other things were impacting on people during these years. For example, many people lost their jobs or saw their home go into negative equity. Government Budgets cut many services while increasing the charges for others – which had a disproportionately negative impact on those with low to middle incomes who are more likely to depend on such services.

So who did bear the brunt of the huge retrenchment Ireland has experienced in the period 2008-2013? *Social Justice Ireland* has published a detailed analysis of the data currently available. It may be accessed on our website www.socialjustice.ie.

It shows clearly that:

- The poorest 10% of the population lost 18.4% of real disposable income compared to 11.4% loss among the richest 10% since the crash of 2008.
- The situation is worse if cuts in services and increased charges are included in the calculations.
- The gap between low and middle-income Ireland on the one hand and the rich on the other hand has widened dramatically.
- Budgets introduced *under the tutelage of the Troika* were regressive, taking more as a percentage of income from those who have least.
- The real impact of these budgets was even more regressive because this calculation does not include the impacts of reductions in services and increased charges introduced in these years, which impact disproportionately on the most vulnerable.

Table 3 is taken from that analysis. It shows the change in average real incomes by decile of disposable income per adult equivalent between 2008 and 2011, as calculated by the ESRI. (This means that the disposable income has been adjusted to take account of the Consumer Price Index.)

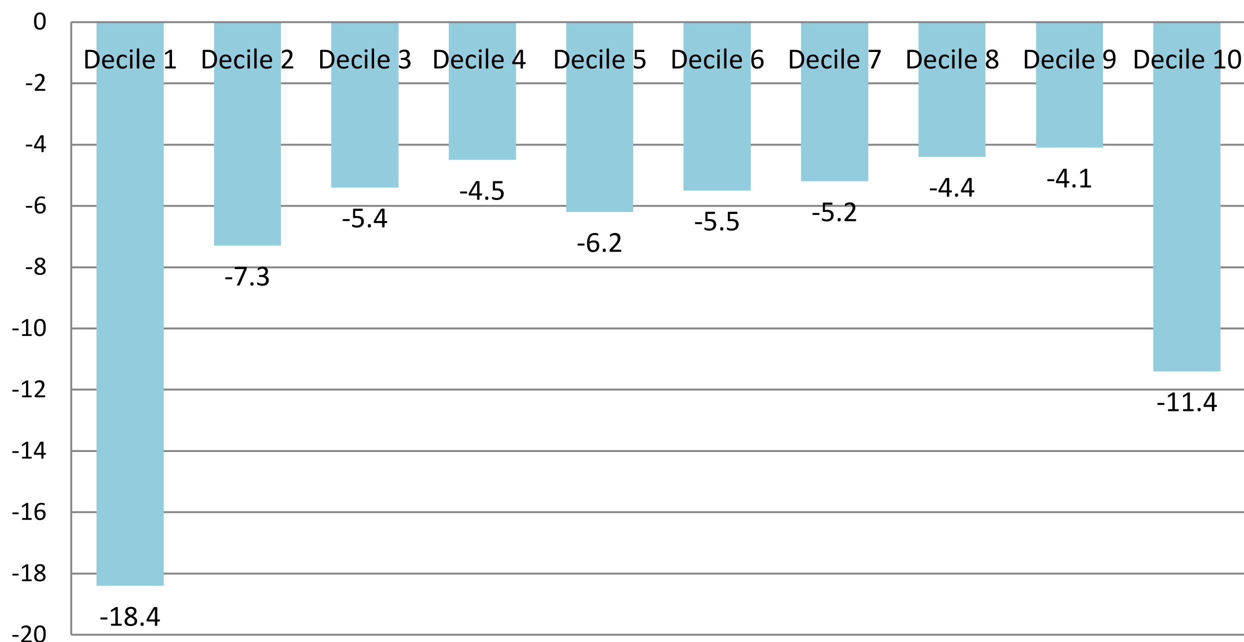
This table shows that the poorest ten per cent of the population saw their real disposable income fall by 18.4 per cent in the period 2008-2011 while the richest ten per cent of the population experienced a fall of 11.4 per cent. (Note: disposable income means all income one has after taxes have been paid and social welfare payments received i.e. the money people have in their pockets *before* they start to pay their bills.)

It should be noted that an examination of this change comparing 2009 and 2011 – a comparable period to that examined by the ESRI in their analysis of budgetary changes – would be likely to reveal larger decreases in real incomes for those in the lower income deciles given the increases in social welfare rates introduced in 2009, and the later reductions in social welfare payments introduced in 2010 and 2011.

Moreover, changes in Ireland's labour market from 2011 on, particularly those surrounding the striking down and changes to Employment Regulation Orders or Registered Employment Agreements, and the system of Joint Labour Committees, may also have had adverse effects on

income inequality, reducing income for the low-paid, which is likely to be seen when SILC data from 2012 and 2013 become available.

Table 3 – Percentage change in average real incomes by decile of disposable income per adult equivalent, 2008 and 2011



Source: Callan et. al (2013: 9)

Data are not available to update these numbers. However they are likely to show an even more regressive situation as the budgets introduced by the Irish Government under the tutelage of the Troika in the years 2012-14 were regressive, taking more as a percentage of income from those who have least.

As noted already, the overall BUDGET impact since 2008 is not as regressive as this table shows. That is because this table includes ALL the impacts on people's income over this period. The Budget impacts are not the whole story. It is also important to recall that the Budgets introduced by the Irish Government prior to the Troika's engagement with Ireland were much more progressive than those introduced under the Troika's guidance.

The real impact is even more regressive because, as noted above, this calculation does not include the impacts of reductions in services introduced in these years, which impact disproportionately on the most vulnerable. In recognising this reality it is important to place it in the wider context of what the Troika has since discovered about the effects of their approach to recovery not just in Ireland but across a wide range of other countries in the 'developed' world that experienced difficulties in recent decades.

International Monetary Fund (IMF) researchers have examined a sample of 17 OECD countries who implemented fiscal consolidation between 1978 and 2009 and concluded that fiscal consolidation 'typically led to a significant and persistent increase in inequality, declines in wage income and in the wage share of income, and increases in long-term unemployment' and noted that governments 'may have the flexibility to design the fiscal adjustment in a way that lessens the distributional impact or they may be able to offset some of the distributional impact through other measures' (Ball et. al., 2013: 11). The IMF Managing Director, Christine Lagarde, (2012) has

argued for "fiscal policy that focuses not only on efficiency, but also on equity, particularly on fairness in sharing the burden of adjustment and on protecting the weak and vulnerable". As successive regressive budgets were implemented it became clear that the overall progressivity of adjustment was being reduced.

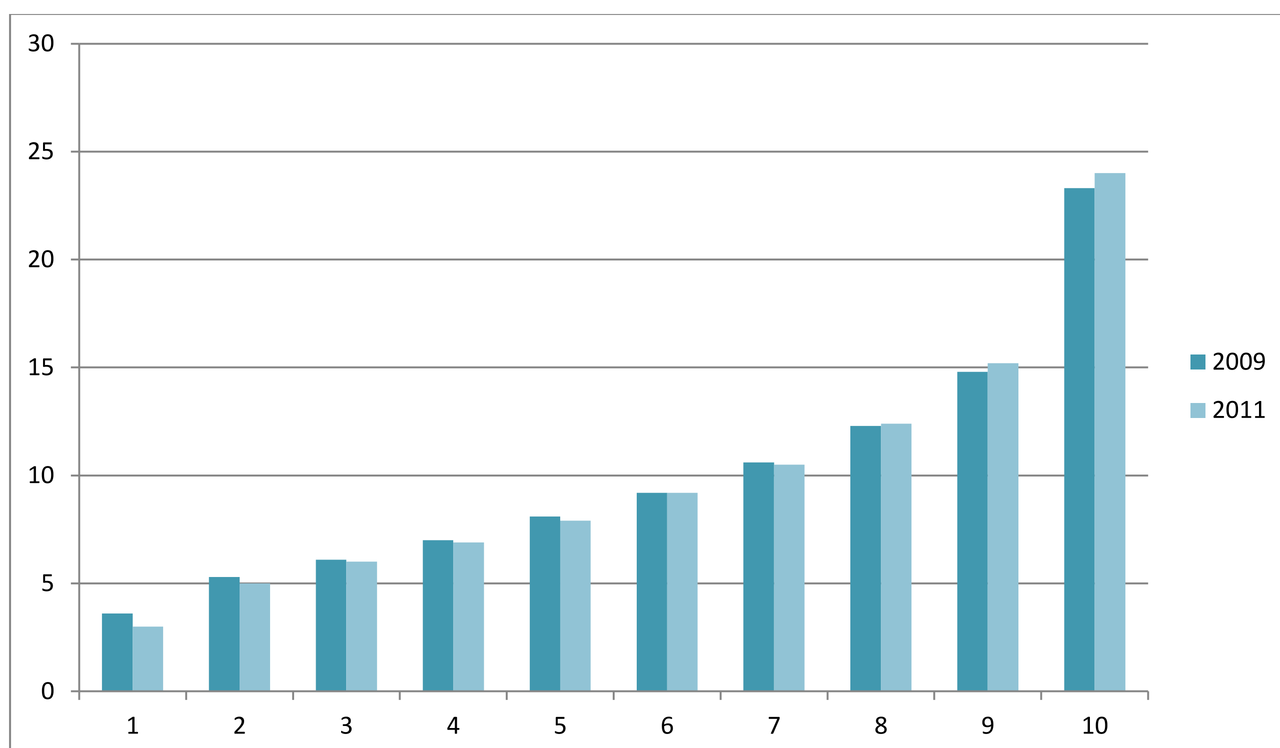
Growing inequality

Data from the EU-SILC study conducted by the Central Statistics office (CSO) indicate that income inequality has increased between 2008 and 2011 with the Gini coefficient, a common measure of inequality, rising from 29.3 in 2009 to 31.3 in 2011. (Data are not yet available for 2012 and 2013. However, as the budget in each of those years was regressive inequality is likely to have worsened.)

This increase has occurred despite the progressive budgetary stance in 2009. Given the regressive or neutral nature of government budgets since 2010 and the persistence of unemployment, it is likely that inequality has continued to increase, possibly at a higher rate. Moreover, the longer-term effects of public expenditure cutbacks in areas such as education, health and other services only become visible after some time, and there may be deep and long-lasting effects on the life chances of many vulnerable young people.

Table 4 shows the income distribution in Ireland in the years 2009 and 2011 (but does not include the income falls identified in Table 2 above). This confirms the widening gap between low and middle-income Ireland on the one hand and the richest 20 per cent of the population on the other hand. Only the top two deciles have seen their share of disposable income grow significantly in this period. As stated already when data become available for 2012 and 2013 this situation is likely to have worsened partly due to the regressive nature of Budgets 2012 and 2013.

Table 4 - Decile shares of equivalised disposable income among persons, 2009-2011



Source: Callan et. al (2013: 8).

4. The Troika – How selective use of data led to inaccurate analysis which, in turn, led to inappropriate policy proposals being made

Selective use of data by Troika members in the analysis and documentation they produced during the years of Ireland's bailout led to inaccurate analysis which in turn led to inappropriate policy proposals being made. This is totally unacceptable.

The Troika's analysis set most of the parameters for the Irish Government's decisions on the Budget and other key areas of policy. Consequently, it was crucially important that the Troika's analysis be as accurate as possible.

Social Justice Ireland provided the Troika with a detailed analysis of a wide range of examples of selective use of data in Troika publications which led to inaccurate analysis and inappropriate policy proposals. We present a few examples here.

4.1. On the poverty rate

An example of this unacceptable process in practice can be seen in the analysis provided on poverty. This analysis stated that poverty was reduced between 2006 and 2010. What this statement hid was the fact that poverty had fallen dramatically in the period 2006-2008 but had risen dramatically from that point onwards.

Based on this selective use of data one could conclude that no damage was being caused to Ireland's poorest when, in fact, an analysis of the full data shows that their situation had been deteriorating significantly from 2009 onwards.

4.2. On reducing unemployment payments over time

Another example of this unacceptable process in practice can be seen in much of the discussion concerning the rates of social welfare payments made to people who are unemployed. The argument made in Troika publications was that Ireland's job-seekers allowance did not fall over time. This contrasts with the situation in many other EU countries.

This analysis however is a selective use of data as it fails to inform the reader that in many other EU countries people receive a high level of social welfare payment when they first become unemployed – often a high percentage of their salary prior to becoming unemployed. Over a period of time the level of this payment is reduced.

By contrast in Ireland there is no such tiered system. The very first payment made to a person who becomes unemployed in Ireland is below the poverty line and remains that way for the duration of their unemployment. Once this fact is revealed recommendations urging its reduction so as to be in line with other EU countries are exposed as being inappropriate.

4.3. On increases in welfare rates in the last decade

A further example linked to the two items already highlighted relates to the claim that welfare rates have been raised far faster than pay or inflation rose in the period since 2004. This again is a selective use of data. It ignores the fact that welfare rates had fallen far behind all other groups in society in the period prior to 2004. The increases in welfare payments in the period 2005-2007 only went part of the way towards re-balancing this situation.

In the 25-year period between 1986 and 2011 Government ministers had seen their after-tax income rise by more than €1,500 a week and TDs had seen their after-tax income rise by more than €840 a week. Clerical officers' after-tax incomes rose by more than €390 a week in the same period. Those on the average industrial wage had seen their incomes rise by more than €340 a week. By contrast the income of an unemployed person rose by less than €144 a week – and €51 of that was attributable to welfare increases in the three years from 2005 to 2007.

By ignoring the broader data the Troika could justify recommending reductions in social welfare rates that still remained below the poverty line.

Any fair and objective analysis would acknowledge that the increases in social welfare rates in the last decade went only part of the way to bridging the gap that had been allowed to develop between the poorest and the rest of society in the preceding two decades.

4.4. On Replacement Ratios

Closely linked to this was the claim that replacement ratios were high in Ireland and consequently welfare rates for job seekers should be reduced. Again, while there are examples of problematic replacement ratios the typical situation is the opposite of that presented in the analysis provided by the Troika. This in turn led to inappropriate policy proposals in this area. The National and Economic Social Council (NESC) addressed the issue of replacement rates in their publication '*Promoting Economic Recovery and Employment in Ireland*'. The NESC research showed that only 5 per cent of people on the Live Register receive both rent supplement and an increase for qualified adults and for qualified children.

NESC noted that the degree of attention paid to this 'perfect storm' which is regularly used to present replacement rates in Ireland as high and interpreted as evidence of a disincentive to work is not related to labour supply concerns. The NESC study showed that Ireland's replacement ratios are very positive in terms of encouraging people to take up employment.

4.5. On distribution of the 'hits' during the recession

A further example of this selective use of data, linked to some of the examples already provided, was the claim that the 'hits' had been distributed fairly in Government budgets during the programme.

This conclusion ignored a study by the European Commission that showed Ireland was one of only two EU countries where the upper quartile of households had **not** taken the greatest impact of the rise in financial distress.

This European Commission study (published September 2012) showed that over the previous year Italy recorded a particularly sharp rise in financial distress followed by Greece, Ireland, Cyprus, Portugal and Spain, with the upper quartile seeing the greatest impact of the rise in all countries except Cyprus and Ireland where the lower quartiles bore the brunt.

In our Briefing supplied to the Troika in October 2012 we provided full details on these and related issues. We provided many examples of where data had been selectively chosen, where this selectivity had led to inaccurate analysis which in turn had led to inappropriate policy proposals being made. Copies of this material are available if the Committee wishes to analyse them.

5. The EU – Other issues that arise from the experience of programme countries

In moving beyond the flawed analysis and inappropriate policy responses that have characterised the response to the 2008 crisis in the EU there are two issues that need to be included in the discussion which have been more or less omitted from the wider discussion in the EU to date. These are

- The social dimension and
- The issue of governance.

Social Justice Ireland has dealt with these issues extensively elsewhere (Healy et al 2013; Reynolds and Healy 2012, 2011). We wish simply to make a few comments on these issues here.

5.1. The Social Dimension

On the social front the political leadership of the EU has failed to provide the necessary support for countries in difficult situations. These have been forced into a situation of 'internal devaluation' in which the financial sector has been protected but services such as healthcare and pensions have been cut back, unemployment has been allowed to rise dramatically and emigration of people of working age has in practice been encouraged even though every government denies that this is the case. Their deeds, or lack of same, give the lie to their words where these issues are concerned. The social dimension has been the adjustment variable for managing the crisis. The claim by the president of the European Central Bank Maria Draghi that the European social model is dead simply serves to highlight how 'taken for granted' this position has been among the EU's unelected elite.

This situation is going to be exacerbated even further by the structural reforms that have been put in place. These are focused on reducing each Government's borrowing and debt while ensuring they cannot increase their expenditure at more than a very low rate even though such expenditure in many cases is the only hope these governments have of getting out of the crisis. It should be noted that without investment there won't be jobs on the scale required. Without these jobs there won't be recovery. Without recovery then austerity will continue. But the rules of institutions such as the ECB and the European Commission put very inappropriate barriers in place to block such necessary investment even when its repayment is ensured. In such a situation one must question the motivation of those putting these rules in place.

Respect for human dignity is a founding principle of the European Union, whose aims include promoting full employment and social progress, combating social exclusion and discrimination and promoting social justice and social protection (European Commission, 2008). The Treaty

provides that the EU should support the activities of member states in integrating people excluded from the labour market (Article 137(1) (h)). The right to social and housing assistance so as to ensure a decent existence for those who do not have sufficient resources is enshrined in the Charter of Fundamental Rights of the European Union.

The Europe 2020 Strategy, adopted by the Council in 2010, aims to turn the EU into a 'smart, sustainable and inclusive economy delivering high levels of employment, productivity and social cohesion' (European Commission, 2010). Its setting of targets to increase levels of employment and education, reduce poverty and social exclusion and improve environmental sustainability are significant, because they highlight the importance of social policy goals to a vision for Europe's future well-being. They also point to the possibility of a more integrated and coordinated approach to economic, social, employment and environmental governance.

What is missing from most European documents is any real commitment to redistribution, fair taxation, solidarity or the elimination of poverty; there is a distinct lack of focus on outcomes. There are weak commitments on a few relevant issues in the EU2020 Strategy but there has been a total lack of support on the scale needed for the initiatives required to achieve even these modest targets. Many countries are further away from these targets today than they were when they were introduced in 2010. Other countries ignore the targets in practice and there is little or no effort to insist that even these limited targets might be achieved.

In its 2013 Social Investment Package, the European Commission recognised that welfare systems fulfill three functions – social investment, social protection and stabilization of the economy and that member states that take a social investment approach in their social policies have more inclusive growth than others (European Commission, 2013). A social investment approach involves putting greater focus on policies such as childcare, education, training, active labour market policies, housing support, rehabilitation and health services that have both immediate effects and returns over time – strengthening current and future capacities and preparing people to face life's risks rather than just repairing the damage.

More integration of social policies has recently been underlined again by the Commission in its Communication on strengthening the social dimension of the EMU (2013). This Communication discusses the possibility of an insurance system to pool the risks of economic shocks across member states thereby reducing fluctuations in national incomes.

In 2008, the European Commission adopted a Recommendation on the active inclusion of people excluded from the labour market (subsequently endorsed by the Council and the Parliament). The Recommendation commits to a balanced approach to active inclusion involving three equally important pillars:

1. inclusive labour markets – ensure 'effective help to enter or renter and stay in employment',
2. adequate income support – 'recognise…[the] basic right to resources and social assistance sufficient to lead a life that is compatible with human dignity as part of a comprehensive, consistent drive to combat social exclusion,'
3. access to high-quality services – 'appropriate social support through access to quality services… including….services…essential to supporting active social and economic inclusion policies' (European Commission, 2008).

The Resolution recommends a 'comprehensive policy design defining the right mix of the three strands….taking account of their joint impact on the social and economic integration of

disadvantaged people and their possible interrelationships, including synergies and tradeoffs' (European Commission, 2008).

In this context it is also important to realise that, despite all of these commitments and claims that the social dimension is crucial for the EU's future, inequalities have been growing during this period. An OECD report (2011) shows that even traditionally 'egalitarian' societies such as Germany, Sweden and Finland, have seen inequality grow during the decades leading up to 2008. This, however, has not received the attention it should have even though again the research shows clearly that there will be no permanent exit from this crisis without a reduction in inequalities (Wilkinson and Pickett 2010; Reich 2013).

What is also notable at EU level is that, more and more, social policy is being transformed into a tool with the single purpose of making enterprises and the economy more productive. So it is not surprising to see the Directorate responsible for economic and financial affairs in the EU increasingly being the one that is responsible for social policy. Rather than protecting the vulnerable such an approach undermines the protections that exist. This is a myopic approach that sees everything as being at the service of the market economy. Side by side with these developments there has been a down-playing of social dialogue. On this, as on so much else, the research is ignored. Recent studies have shown that where there have been effective institutions of social dialogue they have helped to reduce the impact of the crisis (Laulom et al. 2012).

Grahl and Teague (2013) have warned that without a 'social union' to complement the monetary union the Eurozone and European Union will increasingly lose legitimacy. They have recommended a range of social policy co-ordinations and adjustments to current European policies. For example, they note that if programme countries are to continue with internal devaluation, such a development should be pursued by reducing high income and wage inequality rather than reducing the wages of the low-paid. Conversely, those countries with current account surpluses should boost income to the low-paid and reform of their welfare states, thus raising Eurozone demand and reducing inequality within the surplus countries. The current European assessments of employment policy - the Lisbon assessments and the Europe 2020 targets – would thus take on a very different character.

5.2. Governance

Many questions are being raised about democracy in the context of what has been happening in the EU since 2008 (de Witte 2011). The crisis of the financial industry exposed a major democratic deficit when the EU came to develop its response. Huge effort and major resources were put into saving the euro but with little or no public discussion or real democratic scrutiny. Parliamentary discussions, where they did take place, were often guillotined and little notice was taken of any critique provided. It's important to remind ourselves of the range of developments in recent years: the European Stability Mechanism was established; the 'golden rule' was inserted into national constitutions; the procedure for adopting national budgets was Europeanised and the powers of national parliaments were limited on these issues; so-called 'reform' programmes were imposed on countries. All of this was done with very little democratic scrutiny.

There are further challenges on the governance front. There is a risk that a two-speed Europe may emerge where some countries will be excluded from the core decision-making processes. There is also a danger that some countries will be allowed to run their own budgetary and fiscal affairs while others will be dictated to by European institutions. The new development which sees countries sending their budgets to Brussels for scrutiny before they are scrutinised by their own

parliaments raises questions concerning democratic accountability. The European Commission may now seek revisions or take an even more active role on budgetary matters where some countries are concerned. How does such a development sit with democratic legitimacy (de Grauwe 2012)? The Commission does not bear the political cost of its decisions. This is leading some people to move towards a position where they see their own national government as the agent of other states or of organisations such as the IMF, the ECB and/or the European Commission – all bodies without democratic accountability (Streek 2011).

What concerns *Social Justice Ireland* most in this area is that the measures being adopted were designed to meet an emergency situation. However they are becoming permanent as they wend their way into the EU treaties, national legislation and other processes. We believe that many of these measures were developed on the basis of a false analysis as we have pointed out already and consequently are inappropriate responses to the real situation. So we are turning policy decisions based on inaccurate analysis into permanent treaty-based actions that must be followed. The folly of this situation is likely to be exposed in the years immediately ahead as countries such as Ireland are barred from making well-founded, evidence-based decisions which will mean that Irish society may suffer a great deal unnecessarily. The neo-liberal approach to development may well have succeeded in embedding its inappropriate policy approaches so deeply in the EU structures and processes that EU governments will not be in a position to respond appropriately to major economic, social or political developments. This democratic deficit is a very worrying development.

All of this suggests that there are major challenges ahead. There is an urgent need to:

- Put processes in place to ensure that debt created by the financial sector does not become sovereign debt.
- Ensure macro-economic stability.
- Reverse the growing inequalities across society; this involves reversing the hyper-concentration of wealth and of economic and social disintegration.
- Move towards just taxation.
- Put sustainability (economic, social and environmental) at the core of all policy decision-making.
- Reform governance.

6. The Future

6.1. *The need for a new guiding vision*

The economic crisis in Ireland and in the other programme countries is partly the result of the failure of an economic and social philosophy that elevated private greed over the public good, one that created a false 'national pride' which measured the country's success by the accumulation of individual wealth. This myopic philosophy was sustained over a decade of credit-driven financial speculation.

During these 'boom' years, fragments of the desire for a more equal Ireland remained, but this vision was too vague and imperfectly formed to be truly effective. With the onset of the crisis,

successive governments turned to the outworn neo-liberal dogmas of the 'boom' years, and critics were simply informed that 'there is no alternative'.

There are many policy areas outside individual nation's control at the present time. Yet, even within the macroeconomic restrictions contained in the Fiscal Compact, there are real choices to be made about the appropriate distribution of wealth, power and income in our society, the amount of resources our welfare state and health service receive, and the level of taxation required to furnish the resources necessary for a compassionate and civilised society.

Ireland, the other programme countries and the EU generally need a combination of vision and pragmatic policies that can truly move the countries and the Union towards a desirable and sustainable future.

Social Justice Ireland believes *both* Ireland and the wider EU should be guided by a vision of becoming a just society that respects human rights, protects human dignity, facilitates human development, and preserves the environment. The core values of such a society would be the inviolability of human dignity, equality, human rights, solidarity, sustainability and pursuit of the common good. All those living in programme countries or the EU as a whole should have what they require to live life with dignity and to fulfil their full potential, including sufficient income, access to services they need and active inclusive in a genuinely participatory and democratic society.

6.2. A Policy Framework for a Fairer Future – and proposals for the Committee's recommendations

To achieve this vision we propose a policy framework, applicable to all programme countries, that identifies five key policy areas for reform.[4] The Committee's recommendations should address each of these issues.

1) The first is macroeconomic stability, which, in Ireland's case, requires a stabilisation of Ireland's debt levels, fiscal stability and economic growth, and an immediate boost to investment, which has collapsed during the crisis.
    - The Committee's recommendations should propose
        - A substantial reduction in Ireland's bank-related debt. 30 per cent of Ireland's existing debt to GDP ratio relates to the bailout by the Irish government of banks and bondholders who gambled recklessly in Irish banks.
        - Much stronger control of the financial sector than is currently being proposed by the European Commission.
2) The second is the need for a just taxation system, which, in Ireland's case, would require an increase in the overall tax-take to the European average; such an increase must be implemented equitably and in a way that reduces income inequality.
    - The Committee's recommendations should propose

[4] An earlier version of this framework can be found in Healy et al. (2013).

- That Troika programmes not focus primarily on cutting expenditure over increasing taxation. Such an approach has consistently led to those who are vulnerable and on low incomes taking proportionately larger shares of the 'hits' associated with these programme processes.

- That all sectors (including business) contribute to the recovery process through increasing their contribution to the state's taxes.

3) The third area is social protection which requires investment in the social infrastructure, the prioritisation of employment and a commitment to quantitative targets to reduce poverty.

    - The Committee's recommendations should propose

        - That programme countries must be subject to the requirements of meeting their country targets within the EU2020 Strategy. Currently, programme countries are not required to do so. Having this requirement in place would ensure that Government decisions were moving in a fair and socially inclusive direction.

        - That all adjustment programmes should have a requirement to protect those who are poor and/or vulnerable and that implementation of this requirement be independently monitored on a quarterly basis as all other aspects of the programme are monitored.

4) The fourth area is that of the governance, which, in Ireland's case, requires new criteria in policy evaluation, the development of a rights-based approach, and the promotion of deliberative democracy.

    - The Committee's recommendations should propose

        - That all programmes be bound by the Charter of Fundamental Rights of the European Union and the Treaties.

        - That social partners (including, in Ireland, the Community & Voluntary Pillar, the Environmental Pillar and the Farming Pillar as well as the Employers Pillar and the Trade Unions) should be involved in the design, implementation and monitoring of adjustment programmes, current and future.

        - That European guidelines be established to ensure appropriate democratic control of the implementation of measures at national level.

5) Fifth, policies must be adopted that create a sustainable future, through the introduction of measures to slow down climate change and protect the environment, the promotion of balanced regional development, and promotion of new economic and social indicators to measure performance alongside traditional national accounting measures such as GNP, GDP and GNI.

    - The Committee's recommendations should propose

        - That the EU's development generally be based on policies that promote sustainability and, thus, reduce the likelihood of similar problems emerging in the future.

- That all countries in the EU be required to develop a range of new economic, social and environmental indicators to measure real performance alongside traditional national accounting measures such as GNP, GDP and GNI.

7. Conclusion

It is long past time to reflect on what type of economic and social vision the EU and the programme countries wish to pursue in the future. Citizens have been deeply disorientated and demoralised in programme countries by the years of austerity. A progressive future often seems out of reach. The old model, built on unsustainable credit-driven finance, has failed. Given this, it is vitally important that we advocate a new framework for the future and re-emphasise the goal of creating a social Europe.

The years ahead will still be extremely difficult, but it is possible to confront the challenges that we have identified and build a better future, one that is desirable, viable and sustainable. This will require the recognition and vindication of social, economic and cultural rights, and a real debate about the future level of taxation and distribution of resources in society. This should be carried out in the spirit of deliberative democracy, ensuring that all are able to contribute to a national debate. Government must play its part by ensuring that it pursues evidence-based policies, and that policy-making is transparent and that it is accountable to the public for its actions and analyses.

Above all, we should remember the words of the philosopher Raymond Williams, who wrote, ‘to be truly radical is to make hope possible, rather than despair convincing’.

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