THE EURO-ZONE CRISIS—WORSE THAN IT APPEARS? OR SO WE'RE BEING TOLD

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When President Obama dispatched Treasury Secretary Geithner to Wroclaw, Poland last month to sit in at the meeting of the 17-nation Eurozone finance ministers, it was because, as he put it later, the way the Europeans were handling the continent's debt crisis is "scaring the world." Geithner dutifully told the ministers; the message and the President's later comment were not well received.

"Obama's lecture on the Euro crisis . is overbearing, arrogant and absurd," editorialized the German newspaper Bild. "In a nutshell, he is claiming that Europe is to blame for the current financial crisis, which is `scaring the world.' Excuse me?"

"The American president seems to have forgotten a few details," the paper said.

"The most important trigger of the financial and economic crisis was U.S. banks and their insane real- estate dealings, The U.S. is still piling up debt. . The American Congress is crippled by a battle between the right and the left. The banks are gambling just as recklessly as they did before the crisis.

"The president's scolding is a pathetic attempt to distract attention from his own failures. How embarrassing."

"I found it peculiar that, even though the Americans have significantly worse fundamental data than the euro zone, that they tell us what we should do," said Austrian Foreign Minister Maria Fekter. "I had expected that, when he tells us how he sees the world, that he would listen to what we have to say."

Was Geithner overbearing in his admonition to the Europeans? Perhaps. He is said to be that way sometimes. Was President Obama undiplomatic in publicly rebuking the Atlantic allies for moving to slow to confront the crisis? Could be. He has become a lot more outspoken recently.

"In normal circumstances comity would require deference by others to European authorities on the resolution of European problem," Harvard University economist Lawrence Summers wrote recently. "Now when these problems have the potential to disrupt growth around the world all nations have an obligation to insist that Europe find a viable way forward."

The tone of the Obama Administration's remarks on the European economic crisis reflects what Financial Times Martin Wolf recently referred to as "the panic."

"This is code red," New York Times columnist Thomas Friedman wrote September 25. "We are facing a possible global financial contagion triggered by European banks choking with sovereign debt spreading their woes to an already weakened U.S. financial system."

"I have never see Europe's policymakers as scared as I saw them in Washington last week," wrote Financial Times associate editor and European economic columnist Wolfgang Munchau the following day. The combination of the continent's credit crunch and the general world economic slowdown, he wrote, "are about to throw the Eurozone back into recession."

Then in a September 29 article titled, "How to stop a second Great Depression," financier George Soros wrote, "Financial markets are driving the world towards another Great Depression with incalculable political consequences. The authorities, particularly in Europe, have lost control of the situation. They need to regain control and they need to do so now."

Albeit slowly and miserly, the Europeans appeared to be moving last week to come to grips with the crisis. The consensus amongst knowledgeable observers appears to be that a default on its debt is inevitable and we can expect action to try to prevent "contagion" - that is similar collapses in Spain, Portugal, Ireland and Italy.

Most of the current prognosis as dire, but there are those who think it is not dire enough, that what the chief economist for the International Monetary Fund called "dangerous new phase" in the world economy is more perilous than is being publicly admitted.

Prominent British economist Will Hutton, writing in the Observer September 17, suggests that the situation is even worse than, Geithner, Summers, and Obama describe - or are prepared to admit. The ailing euro is part of a wider crisis he wrote, "Our capitalist system is near meltdown."

"A 1930s-style crash threatens us and our financial partners. Collective action is the only solution," wrote Hutton, a governor of the London School of Economics and visiting professor at Bristol University.

"Eighty years ago, faced with today's economic events, nobody would have been in any doubt: we would obviously be living through a crisis in capitalism, wrote Hutton. "Instead, there is a collective unwillingness to call a spade a spade. This is variously a crisis of the European Union, a crisis of the euro, a debt crisis or a crisis of political will. It is all those things, but they are subplots of a much bigger story: the way capitalism has been conceived and practiced for the last 30 years has hit the buffers. Unless and until that is recognized, western economies will be locked in stagnation which could even transmute into a major economic disaster."

Hutton went on:

"Simply put, the world has trillions upon trillions of excessive private debt financed by too many different currencies whose risk is allegedly mitigated by even more trillions of financial bets which in aggregate do not minimize the systemic risk one iota. This entire financial edifice, underwritten by tiny amounts of capital, has been created over three decades backed by the theory that markets do not make mistakes. Capitalism is best conceived and practiced, runs the theory, by hunter-gatherer bankers and entrepreneurs owing no allegiance to the state or society."

"This is nonsense. Business and the state co-generate wealth in a system of complex mutual dependence. Markets are beset by mood swings and uncertainty which, if not offset by government action, lead to violent oscillations. Capitalism without responsibility or proportionality degrades into racketeering and exploitation. The prospect of limitless pay is an open invitation to bad, or even criminal, behavior. Good capitalism cannot happen without referees to blow the whistle or robust frameworks in which markets can function; neither is reliably created by capitalism itself, hence the role of democratic government. Yet the world is trying to solve the legacy of the last 30 years as if none of this were true and, instead, that the practice and theories that created the mess are still valid."

"US treasury secretary Tim Geithner, joining EU finance ministers in Poland as again they pondered how best to end the ongoing euro crisis, was at least recognizing today's interdependencies between countries when he urged his fellow ministers to stop bickering because the markets were terrified by the threat of a catastrophic event - with all the risk that posed the US."

Hutton went on to say that British Finance Minister George Osborne "was also right to declare that a strong euro was in Britain's interests."

"But worrying about how a failed euro might impact on yourself is old speak," he continued. "What the markets need to hear is that western politicians - whether in the eurozone or not - see the euro as part of the potential solution to capitalism's current crisis, not its cause, and that they are prepared to do all in their power to support the reforms necessary to make the euro survive and take other measures vital to make the world financial system functional again. Geithner and Osborne must put some money where their mouths are."

"If the euro breaks up, the cascade of subsequent bank failures and debt write-downs will be no less threatening and Britain will be pulled into the vortex," wrote Hutton. Noting that the EU has created a financial stabilization facility "to try to hold the line," Hutton wrote, "But there is no urgency in launching it; it is still not a proper fund but, rather, a stop-gap provider of borrowing facilities and it is too small. As bad, the German and French governments are wedded to collective European austerity; they want to impose long-term balanced budgets not only on themselves but chilling austerity on the unfortunate states which have to borrow to support their banks and bond markets."

"An entire continent is to be blighted by lack of demand in the midst of a capitalist crisis, compounded by Britain's scorched earth, deficit-reduction plans," wrote Hutton. "Already, many European banks are technically insolvent, recognized by Christine Lagarde, the IMF's new managing director, if not by the banks themselves."

Noting the promises by major national banks in other capitalist powers to lend money is "easing the crisis for a while" he suggests "the outside world needs to go much further." "Europe's stabilization facility must become a fund with a capacity to lend and intervene to see off speculators: Britain, the US, Switzerland and Japan, along with China and oil-rich Arab states, need to contribute alongside Germany."

"We are living through the most dangerous confluence of economic circumstances in modern times," wrote Hutton. "Trying to pretend the interdependencies do not exist or that the collapse of the euro is the answer can only make matters worse. It is a straight choice: we do all we can to help each other or risk going down in what could be the worst economic contraction for a century."

Economist Paul Krugman wrote in the New York Times September 26 that he sees "no sign at all that European policy elites are ready to rethink their hard-money- and-austerity dogma." The same could be seen here at home. "Mr. Geithner asked for a more financially powerful bailout fund along with short- term stimulus from Europe's wealthier economies," the Times said editorially last week. "But his ability to persuade has been undercut by House Republicans who insist on imposing untimely austerity on the United States."

But don't just think of Democrats versus Republicans .There is an unpartisan U.S. policy elite and it is wedded to the same dogma. Its members are lined up against any proposal to stimulate the economy to increase employment while pushing a series of austere measures, including sharp cutbacks in social programs such as Social Security, Medicare and Medicaid. While such a prospect appears to have receded a bit recently they have not given up by any means.

"One of the main problems today is too much debt in the global financial system - among sovereigns, banks, and households, and especially among the advanced economies," says IMF chief Lagarde, "This is denting confidence and holding back spending, investment, and job creation. These countries face a weak and bumpy recovery, with unacceptably high unemployment. The eurozone debt crisis has worsened, and financial strains are rising. Political indecision in some quarters is making matters worse. Social tensions bubbling beneath the surface could well add fuel to the crisis of confidence."

Lagarde said recently that "Everyone - including markets - realize that commitments to cut spending cannot survive a lengthy stagnation with prolonged high unemployment and social dissatisfaction."

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