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Higher wages can save the eurozone

Higher wages for German workers increase domestic demand – and prevent other eurozone countries' indebtedness

Read this article in German.

Nationalism is regaining momentum in Germany. Everywhere left-wing intellectuals emphasise that the nation, as an entity, takes on particular importance as a benchmark for solidarity. When liberal elites don't know what to do next, they become patriotic. But what if they were to tackle the economic grievances underlying the fear of immigration?

Instead, they purport to know that eliminating precariousness in the labour markets is impossible. They dismiss full employment policy through wage increases as populist. And for them, Keynesianism only features as an increase in government spending, which leads to debt and a burden on future generations.

A Keynesian policy, however, does not consist only in creating debt. Debt-financed government spending is on the agenda only when neoliberal economic policies have stifled growth through austerity and a consumption crisis that must be dealt with.

If Social Democrats want to improve their image, they need to present a concept beyond surely laudable socio-political demands: something to help steer the economy in the interest of the workforce or those forced into precarity. The current neoliberal strategy for optimising the economy, mixed with a bit of salvation army activity to secure the loyalty of its supporters, isn't a convincing one.

Taking down neoliberalism

Two neoliberal arguments usually serve as a dismissal of another economic policy. First, profits are needed to finance investment, otherwise jobs will be lost. Second, low wages improve international competitiveness and, in doing so, create jobs.

But this can be countered by some very simple economic insights: in every economic crisis, there's high unused capacity and, thus, the opportunity to produce surpluses that could be invested. At the same time, in all crises, employment and investment both fall. During economic upturn however, investment, profits and employment increase — until full employment is achieved. Therefore, empirically there's nothing to suggest that investment depends on a decline in consumption.

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For 70 years, Keynesian economists have been persuasively arguing that in order for companies to make a profit in the consumer goods sector and sell their products at higher prices than their costs, there must be enough income from labour. Wages generate additional demand and allow profit creation.

If higher government debt and continuous export surpluses are to be avoided, then wages in Germany would need to rise sharply, as the demand generated by these higher wages would drive growth. The production of new capital goods is particularly crucial here. However, no one buys an additional machine if the demand for the consumer goods it produces does not increase. If wages do not increase sufficiently, there's only one way out: the additional goods must be exported abroad. So the export surpluses arise automatically when domestic consumption is too low.

Currency revaluation

The neoclassical mainstream believes that capitalism is a zero-sum game in which one can only invest what one saves and therefore has not already consumed. That's why it simply rejects the concept of rising wages. But if investment is generated by rising demand, following these neoliberal prescriptions means economic stagnation.

It gets even worse: added to their general rejection of wage increases, these misguided economists argue that such increases lead to a deterioration in competitiveness at the global level. On the contrary, competitiveness is determined by the exchange rate, because at the international level labour costs are only important when seen in relation to exchange rates. During the period of national currencies in the euro zone, the Deutsche Mark was continually revalued upward because Germany's exports were so high. The assets of the Republic's affluent class increased due to its exports.

If social democracy cannot ensure that rising wages create an adequate level of demand in Germany, that demand must be created elsewhere, for example through borrowing in the EU's south, as before the euro crisis.

However, this did not improve the competitive position of the German economy. On the contrary, the appreciation jeopardised German's competitiveness. The employment miracle at the beginning of the Red-Green Coalition (1998-2005) was a result of the speculation of international capital against the euro, which was considered vulnerable to crisis. The low euro exchange rate reduced the prices of German exports on the world market.

However, calls for a return to national monetary policy are illusory: even in the time of free and regulated exchange rates after the collapse of the Bretton Woods system, the German government has limited revaluations, so that Germany's economic partners have remained below their potential or stagnated.

Helping German workers is helping the EU

Within the euro zone the situation is quite different because having no exchange rate can have a balancing effect. Here, German wage policy has led to permanent export surpluses. However, slightly higher wages as well as higher investment (and consequently less German competitiveness) would benefit the partners and would not hurt Germany, provided that domestic demand in Germany increases sufficiently.

The working class has regularly supported this export surplus policy with wage restraint because it believed that this would protect its own jobs. However, this resulted, due to the lower propensity to buy on the part of the workforce with lower wages, in a decline in employment in domestic-oriented industries. Nevertheless, some of the 'new nationalists' praise this as demonstrating the superiority of a German wage bargaining process that is based on the motto, 'Saving is a national achievement.' According to their understanding, German workers are simply more reasonable than the those of the southern countries of the EU.

If social democracy cannot ensure that rising wages create an adequate level of demand in Germany, that demand must be created elsewhere, for example through borrowing in the EU's south, as before the euro crisis. However, the crisis has shown that this indebtedness of the other euro countries is not sustainable in the long term. Therefore, in that case the only remaining option is helping the other EU partners economically to generate sufficient demand there.

At European level, the Social Democrats can work towards small price corrections, such as greater investment and an unemployment insurance. But this policy is only partly effective because of the limited volume of such programs. The Social Democrats can achieve much more on a national scale by abandoning their neoliberal illusions. Strengthening the EU and expanding demand in Germany will then be just two sides of the same coin.



Hartmut Elsenhans
Leipzig

Hartmut Elsenhans is a German political scientist. He is considered one of the leading theorists of global Keynesianism. Most recently, he taught and conducted research as a professor of international relations at the University of Leipzig. His research interests include the political economy of the international system and development strategies and social movements in the Third World.



Hannes Warnecke-Berger
Kassel

Dr Hannes Warnecke-Berger is a research associate at the Department of International and Inter-Community Relations of the University of Kassel. He researches global political economy, development theory, violence and migration.