The G20 debacle in Mexico

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When the Group of 20 became the world's leading economic forum in the wake of the collapse of Lehman Brothers in September 2008, there were hopes it would provide the mechanism for a solution to the financial crisis and a "rebalancing" of the world economy.

After all, it was claimed, the new body contained all the old powers as well as rising ones such as China, India and Brazil. At the G20 meeting in London in April 2009 there was broad agreement on the necessity for "stimulus" measures, largely in the form of low interest rate policies and bailouts for the major banks. But by the end of the year, concerns were raised over the Greek debt and within months the crisis of the euro zone was rapidly taking shape.

By June 2010, sharp differences had started to emerge among the major powers. While these were couched in terms of "austerity" versus "stimulus," they centered on the role of governments and central banks in propping up financial institutions.

The US, concerned about the impact of a collapse of the euro zone on its banks and finance houses, has been urging Germany and other major European powers to do more to boost the European financial system and end the sovereign debt and banking crisis. Germany, on the other hand, fearful that its banks will be sucked into the vortex, has so far resisted.

Meanwhile, the tensions continue to deepen. While every effort is made to keep them out of public view, they erupted to the surface on the eve of the two-day G20 summit held Monday and Tuesday in Los Cabos, Mexico.

Arriving for the talks, European Commission President Jose Manuel Barroso was asked by a Canadian reporter why North Americans should help pay for Europe's crisis. "We are not coming here to receive lessons in democracy or in terms of how to manage our economy," he shot back. "This crisis was not originated in Europe. This crisis was originated in North America. Many in our financial sector were contaminated by unorthodox practices by some sectors of the financial market."

While insisting that US financial practices could not be held responsible for the European crisis—in spite of all the evidence to the contrary—the *Wall Street Journal* did note that "Barroso's language, briefly tinged with anger, showed how tensions are boiling over as the crisis moves into a more dangerous phase."

Signs of that "more dangerous phase" have been clearly visible in recent days. The interest rate on short-term Spanish debt jumped to 5 percent on Tuesday compared to just under 3 percent last month. And the rate on 10-year Spanish bonds has climbed to more than 7 percent as international investors withdraw their cash.

The flight of capital out of Spain means that official government funding will be needed to plug the gap, fueling fears that the recent provision of €100 billion to Spain by euro zone governments will prove far too small and that a sum more like €500 billion will be needed.

Another sign of the deepening crisis is the fact that boosts to the financial markets are proving to be ever-more short lived. The bounce in the markets provided by the provision of funds to Spain earlier this month lasted about half a day, before Spanish and Italian interest rates started rising again, while the rise sparked by the results of the Greek election was even shorter.

The Institute for International Finance, a group comprising some of the world's biggest banks, called on the G20 to take urgent action in the face of "very real" risks of a global recession. "There are worrying signs of fragmentation, including retrenchment in international banking, reductions in cross-border lending and in finding markets," a letter from the IIF declared. Decisions by investors to "scale back" were creating "additional market tensions."

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According to leaked drafts of the communiqué, obtained before discussions had concluded, the euro zone members of the G20 have pledged to “take all necessary policy measures” to safeguard the single currency, while the G20 as a whole is committed to action to generate growth and restore confidence.

But such phrases are virtually meaningless, having been issued on numerous occasions in the past three years and always accompanied by the rider that action has to be “based on country-specific circumstances.” In other words, national governments can do as they like and there is no globally coordinated economic policy, nor any agreement on what it might be.

The communiqué was also reported to have included a stipulation that, as well as taking measures to ensure stability, the euro zone members of the G20 would also “break the feedback loop between sovereigns and banks.”

This refers to the situation where the money that is provided to countries with the biggest sovereign debt problems goes to that country’s banks, which in turn invest these funds in the bonds of their own government. In other words, the most indebted countries and the weakest banks have become increasingly dependent on each other—a situation that has been likened to two drunks leaning against each other to prevent both from collapsing.

As with its other proposals, the G20 did not spell out how it intended to break this “negative feedback loop.”

The absence of concrete measures is an expression of the fundamental factors underlying of the crisis of the euro zone and the world financial system more broadly.

The complex interconnections of the global financial system are one very graphic expression of the processes of globalization that have developed over the past three decades, heightening to an explosive point the contradiction between world economy and the system of rival nation-states and great powers in which the capitalist system remains rooted.

This contradiction led to the breakdown of the capitalist system in 1914 and the eruption of war. But all that followed 1914—world war, depression, fascism and mass unemployment—will develop again unless the crisis is resolved through the intervention of the international working class to overthrow the bankrupt capitalist order and establish the basis for a global socialist economy.

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