

# The Australian

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## Angry IPODs have reason to revolt

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**HOWEVER misguided their slogans and questionable their tactics, it is difficult not to sympathise with the young protesters in London, Paris and Madrid whose street marches marked 2010.**

After all, their elders have left them a legacy of public debt that can only translate into future tax increases and spending cuts.

Pressures for fiscal retrenchment will doubtless be even stronger next year. Interest rates on government bonds are about 12 per cent in Greece, 8.6 per cent in Ireland and 6.4 per cent in Portugal, compared to a mere 2.6 per cent in Germany: clearly, markets have not found the European Financial Stability Facility as reassuring as all that.

And with the US and the European countries poised to borrow a historically high \$3.5 trillion to fund fiscal deficits, interest rates are likely to rise, so that debt servicing will weigh even more heavily on public budgets. This will force greater tax increases and reductions in outlays if fiscal targets are to be achieved.

Whether those targets will indeed be met remains to be seen. With 21 per cent of the labour force out of work in Spain, 15 per cent in Greece and 13 per cent in Ireland, securing real improvements in budget deficits will test political systems that have long found fiscal discipline a struggle.

But the problems go far beyond the most egregious basket cases. And whatever the role of the euro, their origins predate the move to a common currency.

Rather, an important factor is that Europe's overall productivity performance has been poor for some time.

From 1973 to the early 1990s, European productivity increased to levels close to or even exceeding those in the US. After that, however, productivity growth in the European Union halved, just as US productivity levels surged. By 2007, gross domestic product per hour worked in the EU was about 12 percentage points below the US level. And partly as a result of high tax rates, Europeans now work 20 per cent fewer hours per head than Americans, so the gap in output per hour leads to an even greater gap in total output.

Slowing productivity growth constrained the tax base that could be used to fund public expenditure. But instead of cutting back on powerful constituencies, many European governments accumulated debt, shifting tax burdens to future generations.

Those burdens will prove all the more painful as, rather than leave assets that could help pay off debt, much of the public spending has gone to fund consumption or on white elephants.

And the pain is increased further by the widespread protection of labour market insiders through stringent unfair dismissal regulations. These have imposed high costs on Europe's young, who have struggled to gain secure jobs. The result has been a marked rise in income inequality between cohorts of working age.

The French case is symptomatic. In 1977, the earnings gap between 30 to 35-year-olds and 50 to 55-year-olds was 15 per cent; now, it is 40 per cent.

Moreover, while earnings continue to rise for the baby-boomer cohorts, cohorts born since the mid-60s have experienced stagnant incomes, a far greater risk of unemployment and slow rates of job advancement.

This is all the more striking as periods of rapid technological change typically increase the relative income of younger cohorts, who have more up-to-date skills. In other words, the between-cohort income spread usually narrows, even if the within-cohort spread rises, as has occurred in the US.

Overall, young Europeans face a double whammy: they will have to make good years of wasteful spending and do so out of incomes lower and more uncertain than those of older generations. Little wonder they are referred to as the iPod generation: Insecure, Pressured, Over-taxed and Debt-ridden.

The politics this gives rise to are made poisonous by the widespread loss of credibility of European political elites.

In many countries, those elites are increasingly a gerontocracy: in 1981, for example, the typical French parliamentarian was 40; today, he or she is 60. And that the elites are embroiled in scandals further undermines their legitimacy.

So does the fact the elites have no credible answers to European society's challenges, most obviously immigration. Here too, protecting labour market insiders has imposed high costs, compounding the many other problems of integration.

A recent French government report finds that adjusting for factors such as age and education, the unemployment rate for migrants is 1.5 to 2 percentage points greater than for the native born, with an even greater gap for migrants from Africa. While that may be unsurprising, the study also finds that second generation migrants are even more disadvantaged than their parents were.

It concludes that despite substantial public spending, the social problems of areas with a high proportion of migrants are worsening, including in terms of violent crime. And the evidence it surveys suggests the French situation, while hardly satisfactory, is no worse than that in The Netherlands and Sweden.

To all this, neither the social democrats nor the traditional conservative parties have any sensible response. And neither is capable of channelling popular discontent. As a result, Europe's Tea Party movement has taken forms far more virulent than its US counterpart, including xenophobic, at times overtly racist, organisations such as the Swiss Union of the Democratic Centre, the New Flemish Alliance in Belgium and Geert Wilders's Party For Freedom in The Netherlands.

This is not to say nothing good has come from the current crisis. Some madcap projects, such as Greece's national broadband network, have been shelved. And fiscal accountability has been enhanced, including by strengthening independent review of budget proposals. Australia could learn from these efforts.

And with so much wasteful spending of our own, we could also learn from the high costs the fiscal reckoning will impose on Europe's young. Trashing shops is no way to solve the problems, but they are right to be angry. Up to us to see if we can do better.

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