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Europe's Future - The Relevance of Keynes's Economic Consequences of the Peace

Summary: The purpose of this paper is to use the analysis and recommendations of *The Economic Consequences of the Peace* in order to illustrate how Keynes's approach could be used for an inquiry into the nature of the current euro crisis. The euro crisis should not be separated from the crisis of the European Union itself, since it is almost impossible to assume that the effects of the demise of the euro area would not be a direct cause of the unraveling of the European Union, the most vast, complex, and tenacious effort of economic and political integration in modern history. Certainly, the conclusions and remedies proposed by Keynes should not be overlooked and it is possible to draw some broad conclusions on how his approach would affect the considerations regarding possible remedies for the current crisis.

Key words: Keynes, European Union, Eurozone crisis, Government debt.

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The shock of World War I, the downfall of the *belle époque*, the length of the war, the unforeseen immensity of human suffering, and the number of casualties made it obvious, at the very least to a part of the political and intellectual elite, that a whole world had come to an abrupt and tragic end. Indeed, what perhaps was even more astounding was that no one had predicted it. This destruction of a world that had been perceived as moving rapidly to a prosperity and technological advance never seen before in human history seems to be a good starting point for a discussion on *The Economic Consequences of the Peace*. In fact, this is the starting point of the book itself and deserves to be quoted in full:

“The power to become habituated to his surroundings is a marked characteristic of mankind. Very few of us realise with conviction the intensely unusual, unstable, complicated, unreliable, temporary nature of the organisation by which Western Europe has lived for the last half century. We assume some of the most peculiar and temporary of our late advantages as natural, permanent, and to be depended on, and we lay our plans accordingly. On this sandy and false foundation we scheme for social improvement and dress our political platforms, pursue our animosities and particular ambitions, and feel ourselves with enough margin in hand to foster, not assuage, civil conflict in the European family” (John Maynard Keynes 1920, p. 1).

Against the background of the current crisis that is shaking the foundations of the European Union this remarkable opening passage seems strikingly familiar. In-

deed, it could be quoted verbatim today, with hardly anybody guessing its author or the year when it was written.

In its time, it seems to have been written not only to underline the need for a deeper understanding of the economic, social, and political forces that shape the world, but also to accentuate the lack of understanding of fundamental changes that had already occurred, but remained invisible to the elite immersed in its daily *modus operandi*. The most disturbing aspect of the settling of European affairs at the Versailles Conference, which led Keynes to resign his membership in the British delegation, was this lack of understanding of fundamental changes in the economy of Western Europe on the part of the Allies' leaders, and their inability to rise above their short-sighted political agendas. The eloquent passage describing the inability of the Western leaders to deal with the crux of the problem facing Europe deserves to be quoted:

“The proceedings of Paris had all the air of extraordinary importance and unimportance at the same time. The decisions seemed charged with the consequences to the future of human society; yet the air whispered that the word was not flesh, that it was futile, insignificant, of no effect, dissociated from events; and one felt most strongly the impression, described by Tolstoy in *War and Peace* or by Hardy in *The Dynasts*, of events marching on to their fated conclusion uninfluenced and unaffected by the cerebrations of Statesmen in Council” (Keynes 1920, p. 4).

The grand settlement of the affairs of a new European order, after the greatest destruction in its modern history was, therefore, according to Keynes, being conceived with a lack of understanding of the fundamental interdependence of the European and world economies, accompanied by the Western leaders' lack of political will to address these issues on a basis that would transcend their immediate political agenda, internal political constraints, and vanity manifesting itself in self-aggrandizement.

“The future life of Europe was not their concern: the means of livelihood was not their anxiety. Their preoccupations, good and bad alike, related to frontiers and nationalities, to the balance of power, to imperial aggrandisements, to the future enfeeblement of a strong and dangerous enemy, to revenge, and to the shifting by the victors of their unbearable financial burdens on to the shoulders of the defeated” (Keynes 1920, p. 51).

1. Europe - An International Political Economy Approach

Keynes's description of the development of Europe from 1870 to 1914 is a remarkable broad illustration of what today we call globalisation. He depicts the vast difference between a “self-subsistent” Europe before 1870 and the Europe at the outbreak of World War I. The underlying causes were, according to him, a rise in agricultural production, a rise in industrial production, the economies of scale, and a growing population. This enabled large immigration overseas, where the need for railroads, ships, infrastructure, and construction provided the demand for European industrial and capital goods. This led to prosperity on an unprecedented historical scale, offering the middle and upper classes “at a low cost and with the least trouble, conveniences, comforts, and amenities beyond the compass of the richest and most powerful monarchs of other ages” (Keynes 1920, p. 9).

Thus, the first modern globalisation transformed the world beyond imagination in less than half a century. The following passage from *The Economic Consequences of the Peace* espouses and elaborates on some of the main improvements resulting from this wave of globalisation:

“The inhabitant of London could order by telephone, sipping his morning tea in bed, the various products of the whole earth, in such quantity as he might see fit, and reasonably expect their early delivery upon his doorstep; he could at the same moment and by the same means adventure his wealth in the natural resources and new enterprises of any quarter of the world, and share, without exertion or even trouble, in their prospective fruits and advantages; or he could decide to couple the security of his fortunes with the good faith of the townspeople of any substantial municipality in any continent that fancy or information might recommend. He could secure forthwith, if he wished it, cheap and comfortable means of transit to any country or climate without passport or other formality, could despatch his servant to the neighbouring office of a bank for such supply of the precious metals as might seem convenient and could then proceed abroad to foreign quarters without knowledge of their religion, language or customs, bearing coined wealth upon his person and would consider himself greatly aggrieved and much surprised at the least interference” (Keynes 1920, pp. 9-10).

Keynes then goes on to point to the rising populations of the German, Austro-Hungarian, and Russian Empires as an underlying source of change in the social and economic spheres of society at large. This large increase in population, accompanied by a sharp reduction in tariffs, was creating a vast market of close to 300 million people. Furthermore, the gold standard facilitated a rise in capital flows and foreign investment. Industrialization, transportation, and urbanization were transforming the Continent.

The rise of Germany as the foremost industrial power in Europe was making it the largest or second-largest trading partner of most other countries, with a large role as a foreign investor in Russia, Austria-Hungary, Romania, Bulgaria, and Turkey. By a system of “peaceful penetration she (Germany) gave these countries not only capital, but what they needed hardly less, organisation. The whole of Europe east of the Rhine thus fell into the German industrial orbit and its economic life was adjusted according” (Keynes 1920, p. 15). Germany had a complex industrial machine, “dependent for its working on the equipoise of many factors outside Germany, as well as within” (Keynes 1920, p. 11). Above all, it had become the central economy of Europe. “Round Germany as a central support the rest of the European economic system grouped itself, and on the enterprise of Germany the prosperity of the rest of the Continent mainly depended” (Keynes 1920, p. 14).

This, then, is the international political economy approach to the explanation of the rise of globalisation in the pre-World War I period. It is possible to actually see the virtuous circle at work in this analysis. Greater productivity leads to larger populations, larger markets, more immigration - in short to a rise in demand for industrial and capital goods. This leads to further industrialization, which, accompanied by a gold standard, leads to a rise in foreign trade and foreign investment, and so to further industrialization and urbanization. The combined effect is higher interde-

pendence and further stimulus to growth fuelled by the further expansion of industrialization and rises in productivity. In this world all is fine and well, provided that these processes continue on and on, never coming to an abrupt stop. In this regard, when describing this aspect of the German economy, Keynes is really depicting the economic dynamics of the Continent: “Only by operating this machine, continuously and at full blast, could she (Germany) find occupation at home for her increasing population and the means of purchasing their subsistence from abroad. The German machine was like a top which to maintain its equilibrium must progress ever faster and faster” (Keynes 1920, p. 11).

Yet Keynes really sees the precondition for Europe’s economic rise in internal factors of social and economic organization. This type of analysis falls into the category of political economy *par excellence*. In his own words, “Europe was so organised socially and economically as to secure the maximum accumulation of capital” (Keynes 1920, p. 16). What this actually means was that high income-inequality, with the upper classes’ higher propensity to save, made possible the rise of fixed capital which created the foundation for growth. This would never have occurred in a social setting with a more equitable distribution of income. This type of reasoning was compatible with that of the mainstream economists of the time, those that later Keynes would call the “Classics”. It is also identical to Marx’s analysis of the rise of capitalism.

It is somewhat ironic that Keynes himself would later stress the discrepancy between saving and investment as the major cause of stagnation and underemployment. In other words, savings in his system became a function of higher income propelled by investment, as opposed to investment being a function of higher savings. In other words, the system of highly unequal income distribution may have not been theoretically necessary for high growth.

Still there is no doubt that Keynes firmly held the mainstream view and the following passage, which I quote here at length, could not be more explicit proof:

“Thus this remarkable system depended for its growth on a double bluff or deception. On the one hand the labouring classes accepted from ignorance or powerlessness, or were compelled, persuaded, or cajoled by custom, convention, authority and the well-established order of Society into accepting a situation in which they could call their own very little of the cake, that they and Nature and the capitalists were co-operating to produce. And on the other hand the capitalist classes were allowed to call the best part of the cake theirs and were theoretically free to consume it, on the tacit underlying condition that they consumed very little of it in practice. The duty of ‘saving’ became nine-tenths of virtue and the growth of the cake the object of true religion” (Keynes 1920, p. 17).

This worked well, in the sense of promoting growth and a general rise in gross domestic product to the level at which it could sustain Europe’s growing population. In short, society as Keynes puts it was working for “progress”. The question of the sustainability of this type of socio-economic equilibrium had not, it seems, been raised in any disturbing manner before the destruction of what was later called the Great War.

Keynes found another element of the pre-WWI international system to be of outstanding importance for the preservation of the growth model just described. This

was the reliance on the import of cheap foodstuffs from overseas, primarily from the United States. The import of foodstuffs on favourable terms enabled Europe not only to sustain a growing population, but also, since foodstuffs are an important element of the wage bill, to maintain the stability of its social arrangements. Cheap foodstuffs made European exports competitive. Furthermore, income from foreign investment was largely reinvested and accumulated, thus creating a sense of security concerning possible downturns in the future. Many must have hoped and thought that this would last forever.

There are two possible ways in which this type of growth and accumulated wealth could end, wrote Keynes: "lest, population still outstripping accumulation, our self-denials promote not happiness but numbers; and lest the cake be after all consumed, prematurely, in war, the consumer of all such hopes" (Keynes 1920, pp. 17-18).

In fact, according to Keynes, the cheap foodstuff imports were already coming to an end due to rising demand in the United States. Western Europe was turning to Russia and Romania for exportable surpluses. Nevertheless, had it not been for the war, who can really tell how long this balance of factors that was fostering growth in Europe would have continued? What, then, caused the world to go down in flames, destruction, and human suffering, on a scale not seen before the outbreak of the war?

2. Europe before the War - The Primacy of Politics

This leads us to what seems to be an implicit view of the primacy of politics. How else can one explain the destruction of an epoch in which unprecedented economic and technological progress was unfolding? According to Keynes, the public seemed unaware or considered unimportant the rumblings that surfaced in the press:

"The projects and politics of militarism and imperialism, of racial and cultural rivalries, of monopolies, restrictions and exclusion, which were to play the serpent to this paradise, were little more than the amusements of his daily newspaper, and appeared to exercise almost no influence at all on the ordinary course of social and economic life, the internationalisation of which was nearly complete in practice" (Keynes 1920, p. 10).

There is a trace of an implicit theory of why the war broke out in *The Economic Consequences of the Peace*. It is not elaborated, nor particularly underlined, but rather put into the broader context of the sustainability of the living standards achieved in Europe in general and Germany in particular, given population growth and the coming to an end of cheap cereals from North America and Russia due to their own rise in population. This could imply that Germany which had the largest population growth in Europe went to war because of concerns over obtaining foodstuffs¹.

However, since there is no deeper explicit analysis of why the war broke out, it is difficult to assume that at the moment of writing *The Economic Consequences of the Peace*, Keynes saw anything but the politics of folly as the main reason for the outbreak of the war. For there is no analysis of the politics of imperialism, the naval

¹ I thank Victoria Chick for pointing this out to me.

race between Britain and Germany, the colonial aspirations of Germany, or other “rivalries”. Rather, “moved by insane delusion and reckless self-regard, the German people overturned the foundations on which we lived and built”, writes Keynes in the opening paragraph (Keynes 1920, p. 1). Thereafter, his major concern is the politics of the Peace Conference, which will complete the devastation of the war if the Peace Treaty arrived at through petty politicking, is implemented:

“But the spokesmen of the French and British peoples have run the risk of completing the ruin, which Germany began, by a Peace which, if it is carried into effect, must impair yet further, when it might have restored, the delicate, complicated organisation, already shaken and broken by war, through which alone the European peoples can employ themselves and live” (Keynes 1920, pp. 1-2).

Certainly, Keynes being a participant made him an outstanding witness to the political tactics of the Peace Conference. His account would have been merely interesting were it not for his magnificent intellect, which makes his analysis of the goals, tactics, and personalities of the major players indispensable to anyone interested in the unfolding of the Peace Conference. Keynes was not only the first to offer his account, but managed, I believe, to define the prism through which the Peace Conference has been viewed since. This does not mean that some of his analysis and conclusions in this regard did not come under criticism almost immediately (Clive Day 1920). The most original came from Veblen (Thorstein Veblen 1920) who criticized *The Economic Consequences of the Peace* for missing the hidden essence of the Conference which in his view was the tacit formation of an alliance against Bolshevism. In fact, Veblen was also in disagreement with Keynes on the treatment of Germany as he had written a book (Veblen 1917) on the possibilities of an enduring peace before the United States entered the war, in which he argued not only for harsh terms for Germany but also for a thorough reform of its political system in order to ensure the dismantling of what he called “the dynastic state” as a necessary prerequisite for the avoidance of a future war.

It is beyond the scope of this paper to go into details concerning the recollection of the Conference itself. Suffice it to say that through his description, subjective as it must be by definition, Keynes points to two major characteristics of the leaders of the Allies: a) an obsession with their own national interests (Clemenceau), personal agendas (Wilson), and internal political constraints (George), and b) the lack of both will and understanding of the detrimental consequences of the Treaty, in its final version. Keynes seems to attribute the resultant dire outcome of the Conference to the personal traits of the leaders of the three major Allies, rather than the deeper causes that may have determined their attitudes.

This is consistent with his treatment of politics as an independent variable when briefly discussing the origins of the war. Although in the historical interpretation of social sciences the “free will” of the major political actors is often seen as limited due to various historical, circumstantial, or ideological constraints, one should keep an open mind in this regard concerning the Peace Conference. After all, Keynes himself underlined some of the major constraints mentioned above, yet remained adamant that the personalities of the three major victorious powers were to blame. In fact, it is difficult to imagine a situation less constrained by various other

factors than a peace conference such as the one at Versailles, where the leaders of the victors could exercise the freedom to abolish empires, legitimize new states and borders within Europe and create new states in the Middle East, while imposing a harsh peace on the defeated. If ever the leaders of nations can act according to their free will, there is no better opportunity than at peace conferences after cataclysmic wars. In such a case personal characteristics such as prejudice, vanity, obsession, ignorance, callousness, self-righteousness and the like may not only colour, but can dominate the decision-making process.

Methodologically, this, however, elevates politics to a level where political leaders seem to have freedom of action far beyond the ordinary. Nevertheless, in this particular case Keynes sees the Conference as an opportunity for making an effort at restoring Europe to what it once was. He sees the flaws of the leaders in their failure to rise to the occasion and assume the responsibility for perhaps politically unpopular measures that would enable the peoples of Europe to rebuild and avoid the threat of extremism.

Here, though, there is a certain contradiction. Although the task of the Conference was to try to restore what had been destroyed, Keynes himself had defined the period before the war as hinging on a precarious multi-equilibrium of economically sustainable populations, a web of international interdependence, and a lack of class conflict maintained through a system of accepted norms. Keynes himself was uncertain whether or not such a pacified class conflict could be restored:

“I seek only to point out that the principle of accumulation based on inequality was a vital part of the pre-war order of Society and of progress as we then understood it and to emphasize that this principle depended on unstable psychological conditions which may be impossible to re-create. It was not natural for a population, of whom so few enjoyed the comforts of life, to accumulate so hugely. The war has disclosed the possibility of consumption to all and the vanity of subsistence to many. Thus the bluff is discovered: the labouring classes may be no longer willing to forgo so largely, and the capitalist classes, no longer confident of the future, may seek to enjoy more fully their liberties of consumption so long as they last and thus precipitate the hour of their confiscation” (Keynes 1920, p. 19).

This then, brings us back to political economy and income distribution as the centrepiece of the analysis of the rise in growth.

In Keynes's analysis there are different levels of determining factors that contribute to the rise of globalisation in the 1870-1914 period, which need to be connected in such a manner as to provide a coherent causality and interpretation of the whole (or Europe, in this case). It seems to me that one, albeit not the only explanation might run in the following direction. The cheap foodstuffs from overseas enabled a growing population, which with technological progress brought about ever-rising accumulation of fixed capital due to high profits and a radically unequal distribution of income, the latter made possible by the pacification of class conflict. This growth, assisted by the gold standard, led to a rise in foreign trade and foreign investment on an unprecedented scale, leading to overseas development that encouraged immigration. This process then continued, although some strain was felt (the coming of the end of cheap foodstuffs), until political extremism brought about its demise.

This reconstruction of Keynes's theoretical explanation for the rise of Europe in the described period is illustrative and I do not consider it to be the only possible or "true" interpretation. However, I think is worth insisting on the method of political economy and international political economy that I find provides the foundation for his analysis and recommendations in *The Economic Consequences of the Peace*. Having said this, it is time to turn to a very brief analysis of the Treaty and Keynes's recommendations, and the ethical dimension of his approach.

3. The Treaty and Recommendations

The very first paragraph of the chapter on the Treaty explains how the analysis of the delicate web of interdependence of the social and economic structure that made up Europe before the war, which would be the basis of an effort at the reconstruction of a European edifice akin to the one that existed before the outbreak of the war, was the last thing that informed the minds of the major statesmen under whose eldership the Treaty was drafted and signed:

"The future life of Europe was not their concern: the means of livelihood was not their anxiety. Their preoccupations, good and bad alike, related to frontiers and nationalities, to the balance of power, to imperial aggrandisements, to the future enfeeblement of a strong and dangerous enemy, to revenge, and to the shifting by the victors of their unbearable financial burdens on to the shoulders of the defeated" (Keynes 1920, p. 51).

At the very outset, notes Keynes, there was insincerity on the part of the Allies, as they had agreed to Woodrow Wilson's Fourteen Points. The German government rightly thought that this platform would be the starting point for a just settlement, in spite of reparations and the return of Alsace-Lorraine - lost to Prussia in the war of 1871 - to France. Instead, a "Carthaginian Peace" was imposed. This Keynes attributed to Clemenceau, who manipulated Wilson and marginalized Lloyd George.

The analysis of the Treaty is detailed, but the goals of the Treaty regarding Germany along with the description of its economy were succinctly put:

"The German economic system as it existed before the war depended on three main factors: I. Overseas commerce as represented by her mercantile marine, her colonies, her foreign investments, her exports and the overseas connections of her merchants; II. The exploitation of her coal and iron and the industries built upon them; III. Her transport and tariff system. Of these the first, while not the least important, was certainly the most vulnerable. The Treaty aims at the systematic destruction of all three, but principally of the first two" (Keynes 1920, p. 61).

These then are the goals: the rest is merely execution, which *The Economic Consequences of the Peace* elaborates on at length. Here Keynes brings out the hard empirical evidence and estimates the value of certain punitive measures to the German economy. Even harsher were the terms that set reparations at an impossible level by making Germany "liable for the total cost of the war". This politically charged phrase, used by Lloyd George in the British election campaign of 1918 after the Armistice, led to the interpretation that added all kinds of burdens, including pensions for disabled allied soldiers and for the families of those killed in action. Thus repara-

tions were, according to Keynes, set at a level that Germany could not repay, and according to his estimates had to be scaled down to a quarter of the sum. It is extremely difficult to judge such estimates. Certainly, other economists such as Clive Day and Allyn Young, who were also present at the Conference in an official capacity, had their own views on the Conference, the estimate of the reparations, and on Keynes's book (Day 1920; Allyn Young 1924). The details of the approximation of the reparation figures are beyond the scope of this paper, although Keynes goes to great lengths to provide estimates based on figures from the pre-war German economy.

The most damning condemnation of the Conference comes not from the figures that were reached, but rather from the disinterest shown in a serious assessment of the reparation figures which, according to Keynes, was evident in the deliberations of the Allies' leaders. In Keynes's own words:

"Thus a scientific consideration of Germany's capacity to pay was from the outset out of court. The expectations which the exigencies of politics had made it necessary to raise were so very remote from the truth that a slight distortion of figures was no use, and it was necessary to ignore the facts entirely. The resulting unveracity was fundamental. On a basis of so much falsehood it became impossible to erect any constructive financial policy which was workable" (Keynes 1920, p. 137).

Keynes then gives a gloomy judgment on the results of the Conference:

"The treaty includes no provisions for the economic rehabilitation of Europe - nothing to make the defeated Central Empires into good neighbours, nothing to stabilise the new States of Europe, nothing to reclaim Russia; nor does it promise in any way a compact of economic solidarity amongst the Allies themselves; no arrangement was reached at Paris for restoring the disordered finances of France and Italy, or to adjust the systems of the Old World and the New" (Keynes 1920, p. 211).

In other words, not only were there no substantial results, but the leaders ignored the most fundamental issue: "It is an extraordinary fact that the fundamental economic problem of a Europe starving and disintegrating before their eyes, was the one question in which it was impossible to arouse the interest of the Four" (Keynes 1920, p. 211).

Seeing the repair of the economic interdependence of Europe and the most urgent need, Keynes set out to suggest what he considered to be the necessary remedies. These included: (a) a revision of the Treaty, (b) the settlement of inter-Ally indebtedness, (c) an international loan, and (d) reform of the currency. His other major concern was the need to repair relations between Central Europe and Russia.

However, today we would probably see his most relevant proposal as that to create a Free Trade Union in Europe. Furthermore, his proposal to revise the Treaty by appending the Coal Commission to the League of Nations (its membership broadened to include Germany and other European states) in order to ensure the distribution of German coal supplies is striking. What is more, it is complemented by his other proposed Treaty revision, which was aimed at ensuring a supply of iron to Germany from Lorraine.

The aim of the Coal Commission proposal was to allow Germany to continue its industrial production and strength. The Free Trade Union, to which Germany, Poland, and the new states created after the fall of the Austro-Hungarian Empire

were to belong, was to provide an environment that would both enhance and keep in check potential rivalries and conflicts, thus preventing the disruption of the economic space that had been unified under the old Empires. Responding to potential criticism that this would give Germany the chance to dominate *Mittel-Europa*, Keynes's hope was that other states, including the Great Powers (France and Britain), might join at a later date and benefit from its non-discriminatory tariffs. In the first instance this would help Germany recover and include it in a web of relationships that would allow for both its potential prosperity and the pacification of its imperialistic tendencies.

The proposal on finance was twofold. The first task consisted of annulling the inter-Ally debt through Britain writing off all the debt owned by the other European Allies - France, Italy, Belgium, Serbia, etc. In fact, Britain should take the high ground and forgo its claims on German war reparations by transferring it to its other European Allies. For its part, Britain should appeal to the United States to write off British debt (the bulk of United States loans having gone to Britain) as well as the debt of other Allies. This, according to Keynes, would simplify the situation and provide the prerequisites for a favourable economic climate. It would also erase the possibility of a potentially absurd outcome:

"Failing such a settlement as is now proposed, the war will have ended with a network of heavy tribute payable from one Ally to another. The total amount of this tribute is even likely to exceed the amount obtainable from the enemy; and the war will have ended with the intolerable result of the Allies paying indemnities to one another instead of receiving them from the enemy" (Keynes 1920, p. 259).

Finally, Keynes advocates an international loan by the United States in order to fire up the European economy. This debt would be repayable and guaranteed. It would provide Europe, Allies and former enemies alike, with liquidity to put the devastated economies into motion, providing necessary foreign exchange and stabilizing currencies.

Lacking all of these or similar measures presents a danger to the survival of the fabric of society itself. The already visible inflation in Europe could be, according to Keynes, just a prelude of things to come. The debauchery of a currency is the road to the destruction of both states and societies. Finally, impossible demands cannot be met, so Keynes predicts that in real terms the reparation demands will never be met. The reconstruction of Europe should be built on the basis of a just and equitable peace that allows Germany to remain an industrial powerhouse. The alternative is Bolshevism or populist movements that could empower the reactionary forces that had brought Europe to ruin to begin with.

The key, therefore, is sound economic analysis in order to both recognize the nature of the problems faced and to provide adequate proposals for the reconstruction of Europe as a unified economic space. Methodologically, this then puts economics at the highest level of cognition in relation to social and economic problems and their remedies through public policy. Indeed, Keynes as a public intellectual, a status he earned through the publication of *The Economic Consequences of the Peace*, did more than any other economist to affirm the economist's role in contributing to social, economic, and political solutions through public policy.

Keynes was judging the results of the Conference on the basis of *consequences*, the crucial word in his title. He is very explicit about this: "I am mainly concerned in what follows, not with the justice of the Treaty - neither with the demand for penal justice against the enemy, nor with the obligation of contractual justice on the victor - but with its wisdom and its consequences" (Keynes 1920, pp. 59-60).

In his sequel to *The Economic Consequences of the Peace*, published in 1922 under the title *A Revision of the Treaty*, in which he claims to add nothing new, Keynes describes the role of the intellectual in forming public opinion. According to Keynes, politicians by the very nature of politics are often put in a position where they do not dare to contradict the opinion of the masses. The private individual by contrast is under no obligation to "sacrifice veracity to the public weal" (Keynes 1922, p. 3) and can by voicing well-informed enlightened "inside" (unspoken) opinion contribute to the return to rational policy by affecting the "outside" mass opinion. Thus, Keynes saw his role as twofold. On the one hand he was impacting on public opinion to muster support for a revision of the Treaty, while on the other he was appealing to policy makers to keep long-term self-interest in mind so that they could revise the Treaty once the emotionally charged policies towards Germany blew over.

Nevertheless, when reading *The Economic Consequences of the Peace*, one feels a deep humanistic compassion for the sufferings of human beings throughout devastated Europe and a fear of the destruction of European civilization in which Keynes felt deeply rooted. "It was the task of the Peace Conference to honour engagements and to satisfy justice: but not less to re-establish life and to heal wounds" he writes, and adds in the next sentence: "These tasks were dictated as much by prudence as by magnanimity with the wisdom of antiquity approved in victors" (Keynes 1920, p. 23).

In a recent paper, Anna M. Carabelli and Mario A. Cedrini (2014, p. 110) point out that in this context magnanimity is related to debt forgiveness as a gift that would trigger shared responsibility for the reconstruction of Europe, and that such a gift could be seen as a possible precondition for building trust for cooperative behaviour, overcoming ingrained antagonisms between the actors. In another recent paper, Maria Cristina Marcuzzo (2011) distinguishes between "reason" and "reasonableness" in Keynes's approach when writing *The Economic Consequences of the Peace*. She finds (drawing on Habermas and Rawls) that "reasonableness" in this context includes the principle of fairness and cooperation. This means that *reasonableness* includes judgment contingent on context and knowledge. Reason, on the other hand, simply means utilitarian rationality.

All these points should be well taken. However, it does not do full justice to Keynes's role as a public intellectual. What is lacking in this explanation is the inner ethical need for or feeling of the duty to speak unpopular truths that one feels guided Keynes to write *The Economic Consequences of the Peace*. Recently, Sherry D. Kasper (2010) has eloquently elaborated Keynes's legacy as a public intellectual, motivated throughout his lifetime by an inner moral need to voice the truth in times of social crisis. Indeed, his anguish, his condemnation of injustice, and his passionate higher moral purpose in an effort to prevent a policy that would lead to populism and

barbarism resonate on almost every page of *The Economic Consequences of the Peace*. Keynes does not shirk from making his value judgment obvious to the reader. It is the survival of Europe as a civilization based on a more-or-less market economy with individualism at its centre and with class conflict pacified through a kind of social compact that he wishes to bring back to life after the devastation of the war.

The Economic Consequences of the Peace was an influential book. There are those who think that it was empirically unfounded, but that it achieved its purpose of relaxing the reparation claims (Etienne Mantoux 1946). The mainstream opinion is that its advice went unheeded, but that it was prophetic. Ending this section, the obvious question is does it have any relevance to the crisis of the European Union that we are witnessing today?

4. Europe's Golden Growth

So much has been written on the current crisis of the Eurozone and the European Union that I will focus on a few broad aspects that I find to be relevant to the discussion of a period almost a century ago.

The first modern globalisation, described in *The Economic Consequences of the Peace*, ended with the outbreak of war. A new wave of globalisation, which the vast majority was unaware of, began after World War II and commenced with a reconstruction of Europe much in line with the remedies suggested by Keynes in *The Economic Consequences of the Peace*. The European Coal and Steel Community seems to have much in common with the role of the Coal Commission that Keynes proposed in 1919. Parallels can be drawn between Keynes's proposal for a United States liquidity loan in order to stabilize currencies and promote production and trade, and the Marshall Plan thirty years later. Most importantly, the conditionality of the Marshall Plan in terms of backing the building of a market economy, free trade, and cooperation on a European level was exactly what, according to Keynes, was missing from the Versailles Treaty, which he criticized so passionately.

Ironically, all of these institutional arrangements were only created after much strife and negotiation. In other words, in spite of *The Economic Consequences of the Peace* and the fact that Keynes's reputation was at its peak at the end of World War II, his earlier recommendations for the rebuilding of Europe were ignored.

Keynes, however, did make a personal contribution to this new wave of globalisation through his work on the creation of the Bretton Woods system, which successfully speeded up the process of globalisation for the next quarter century. It is true that his original proposal on a "clearing union" and a world currency "bancor" were not accepted. Rather, the American "White Plan" became the basis of the new international monetary system. Still Keynes's firm belief that full employment policies required domestic control over interest rates and that capital controls were necessary to ensure this, along with relatively fixed exchange rates to prevent speculation, was embodied in the very foundation of the new system.

The underlying international political economy factors at the outset of the "new beginning" of a European union (at the time of Western European countries) were not very conducive to a return to prosperity. The European Union was forged against a background of rivalry between socio-economic systems, potential military

conflict (dubbed the “Cold War”), and a general fear of a return of the Great Depression of the 1930s.

Today, it is easy to take a mellower look at the past. The truth is that Western Europe faced many seemingly unsurpassable obstacles. First, there were the political obstacles to reintegrating Germany into Western Europe. Then there was the problem of current account deficits and lack of real convertibility leading to what was called a dollar shortage. The dismantling of price controls and rationing was not an easy process, since it was accompanied by inflationary pressures and devaluations. All of these had to be overcome politically and by economic policies, the Marshall Plan being a crucial supporting factor.

Another aspect of post WWII reconstruction was the bankruptcy of the pre-war political and social systems. While the defeat of Fascism and Nazism was obvious, the ruling elites of some of the other countries had to acknowledge that class conflict and harsh ideological struggles had to a large extent radicalized politics and delegitimized the political order of these societies. This was especially true of and most visible in France during the late 1930s. What this meant was that the new political elites sought to derive their legitimacy from diffusing class conflict through co-operation and coordination between employers and workers, provided through the intermediary and sometimes dominant position of the state. Thus, negotiations with trade unions on profits and wages, and the encouragement of various forms of worker participation in decision-making were institutionally established in most Western European countries. This then, was the internal political economy through which the social question was dealt with, on the one hand making room for stable profits and on the other creating a social welfare state and decreasing income inequality.

Another aspect of the post-WWII Western European economy was the fact that the reconstruction of Europe became a perfect stage for the adoption of new technologies. The technological management and organizational advances and achievements of modern industry in the United States in the 1930s had not been widely transferred to Europe in the period preceding WWII. This meant that, given the general educational level and skills of the workforce, the time for applying these various innovations through extensive industrialization and growth was ripe and would lead to a certain catching-up with the United States, i.e., to “convergence”. Thus, coordinating mechanisms for the activation of widespread and interrelated industries seemed to be the obvious solution and they included government agencies, planning, and nationalized industries. Along with the described effort of achieving cooperation between employers and the unions, these elements constituted the foundations of what Barry Eichengreen (2008) has described as “coordinated capitalism”.

With the economic take-off into the “golden age” of economic growth the integration of Europe had begun, and it continued and deepened. The virtuous circle of growth, higher standards of living, and higher demand and consumption leading to higher investment and growth was working at its best. An ever-widening market became broader and deeper through ever-increasing integration. This was the Keynesian dream come true. The basis of it was the described social compact between employers and the work force mediated by governments, and the reliance on the welfare state that made the countries of Europe distinct. What is even more important is that this remains the defining element of European Union countries to this day.

During the period after the demise of the Bretton Woods system, various problems arose. I will not dwell on them here, pointing out that the European Union not only muddled through but expanded, its integration deepening. With the fall of communism it acquired a new dimension and purpose. It had the historical task of expanding and integrating new members, finally overcoming the historical division of Europe. The accession of ten new members in 2004, two more in 2007, and one in 2013, bringing the membership of the European Union to 28, along with the promise to keep the door open for others (foremost the Western Balkans), has so far been the historic heroic peak of the European Union.

The sixty years (since World War II) of growth, stability, and integration in European history relied on a pacification of European rivalries, the shifting of the burden of defence expenditure onto the United States during the “Cold War”, the social welfare state based on a social compact between employers and workers, technological catch-up, and extensive growth and industrialization. It was also based on ever broader and deeper integration, growing foreign trade, and a large role for government in economic affairs. In fact, in terms of trade and foreign direct investment within its European Union borders, Europe has become more integrated than ever before.

As Section 4 draws to an end, I would like to summarily point out what I view as important similarities between the problems perceived and the level of analysis, versus recommendations found in *The Economic Consequences of the Peace (ECP)*. Then I would like to introduce some of the solutions applied during the reconstruction Europe after the Second World War (as already discussed in this section as well as Section 3).

I find similarities between Keynes's recommendations concerning the Free Trade Union and the Coal Commission appended to the League of Nations and what emerged after World War Two, first as the European Coal and Steel Community, and then as the European Economic Community. Then there is Keynes's recommendation for liquidity taking the form of a loan from the United States similar to the Marshall Plan. I would also like to mention the historical institutionalization underlying Europe's Economic Community, which over the decades evolved into the European Union as we know it today. I find these points striking and present them in schematic form below (see Table 1).

5. The European Union - Globalisation and Crisis

Despite periods of difficulty and muddling through, up to the financial crisis of 2008 the European Union was considered a major and unique success. It deserves to be seen that way still. However, at the moment it is facing more than an economic recession and more than a common currency crisis. It has a deeper identity problem that is related to a changing globalized world. Basically, the very foundations of the European Union have been seriously shaken and there is a need to rethink its pillars and identity.

In short, since the scope of this paper does not allow a detailed account, let me just remind that through most of its history European integration was forged and advanced under very different circumstances. Firstly, the Cold War, the threat of com-

Table1 Keynes's Recommendations for European Reconstruction in the ECP and the Evolution of the EU after WWII

Analysis level and recommendations	Keynes – ECP	Europe - 1946-2008
International political economy	Europe - complexly integrated and interdependent Formation of Free Trade Union	Europe - complexly integrated and interdependent Formation of European Economic Community and evolution into European Union
International political economy	Central role of Germany, east of the Rhine in FDI and trade	Central role of Germany, largest European economy and largest investor in Eastern Europe
Political economy	Pacification of Class Conflict - through balance of self-restraint of classes (low wages for labour-high savings of capitalists)	Pacification of Class Conflict - through social compact between classes and state mediation
Cooperation in the use of key resources	Coal Commission appended to League of Nations	European Coal and Steel Community, Euratom
Starting up the economy, trade, and dealing with currency crisis	Appeal for liquidity loan from the United States	Marshall Plan - dealing with dollar shortage and providing liquidity

Source: Author's analysis - summary table.

munism, and NATO membership contributed to the formation of a perception of common purpose and destiny. Secondly, the division of Europe into Western and Eastern Europe and the ideological and potential military conflicts with the communist bloc hastened the reintegration of West Germany with the rest of Western Europe and led to the permanent pacification of traditional rivalries between states in this part of the continent. In turn, this fostered the need for closer cooperation and deeper economic integration. As already described, there was a need in the major Western European states to achieve legitimacy through the pacification of class conflict by including unions, broadening worker rights, and expanding the welfare state. Finally, the process of deeper and wider integration was accompanied by a process of "convergence" between the older and wealthier states and newcomers. This last aspect provided a strong motivation for radical reforms undertaken by Central and Eastern European countries in order to achieve membership in the European Union during the last huge wave of expansion. All of these phenomena, needless to say, contributed to the legitimacy and attraction of the European Union.

Today things look very different. The Cold War ended a long time ago. The current crisis in the Ukraine will not rekindle it: at most it will bring on a Cold Peace. The traditional rivalries in Europe have also been pacified for a very long time. There has not been anything that could even come close to the danger of a military conflict between members of the European Union, nor are any in sight. In other words, in spite of the Ukraine crisis and rhetoric from the media, a war with the Russian Federation seems inconceivable: as is conflict between members of the European Union. The general perception is that lasting pacification of potential conflict among member states has been achieved. The unions have less leverage than before, while labour market reform has curtailed workers' rights.

Volumes have been written on how globalisation is affecting the European model of the welfare state. Globalisation has created extra demands on the welfare state and the question arises as to how much further this process can go. In the European context we should also be aware of the long-run pressures. There is no clear-cut answer as to whether or not globalisation impedes the welfare state or whether the welfare state impedes globalisation. Given the costs of globalisation, the scope of the welfare state may actually be enlarged. The major issue is really whether or not the cost of the welfare state is sustainable under globalisation. In other words, the loss of manufacturing and agricultural employment and an ageing population will contribute to the rising cost of the welfare state.

Finally, instead of convergence we have a deepening divide between the “North” and the “South” throughout the European Union. This divide has acquired a particularly dangerous form within the Eurozone as a divide between “creditors” and “debtors” that puts a strain on the future of the euro as the common currency.

The described changes regarding the very pillars of European integration and identity have made the European Union less attractive and less legitimate in the eyes of voters, especially among younger generations that have no memory of the hard struggles of the consequences of war and the difficulties of reconstruction, nor of the potential military conflict between the superpowers that could have embroiled Europe. Instead, the new generations feel the brunt of unprecedented unemployment rates, stagnation, and lack of hope. This estrangement from the European Union and its institutions during the crisis have led to a deficit of legitimacy and to the institutions of the European Union being perceived as distant, alienated, and lacking democratic control.

All of this has come to the forefront with the crisis of the Eurozone and its handling by the member governments. Even before the crisis, after the Greek admission of a huge budget deficit in 2010, there was reason to be concerned about the way the Eurozone was set up and the enforcement of its rules. These were the famous Maastricht criteria concerning budget deficits, government debt, inflation, and long-term interest rates. These criteria were designed to foster the creation of the Eurozone. They were also designed with the hope that they would enable convergence of economic policies. They were, however, formed under the implicit assumption that the world economies had entered a phase of low volatility and that what mainstream economists had called the “Great Moderation” would last forever. The Washington Consensus and the Great Moderation were to be the macroeconomic version of the “end of history”.

In retrospect, the decision to include countries of low competitiveness (Greece) and sluggish growth (Italy, Portugal) in the Eurozone may seem to have been a mistake. The common currency does not allow them to adjust except through “internal devaluation” i.e., a nominal cut in wages, pensions, and social benefits. This creates the extra strain of a political divide within countries as well as between the members of the Eurozone, in the midst of the heaviest crisis in European history since World War II. What compounds the problem is that two of these economies are very large (Italy, Spain) on a worldwide, let alone a European scale. Let me point out in passing that the fates of the Eurozone and the European Union are unambiguously

linked and it is difficult to imagine the downfall of the one without the unravelling of the other.

Finally, it seems that one more aspect of globalisation needs to be mentioned. This is the ever-increasing role of financial markets in European financing. In the post-World War II period the European corporations depended heavily on close relationships with banks for finance. This led, so it is believed, to more long-term profit maximization, as opposed to the short-term quarterly goals of corporate executives in the United States' model of reliance on financial markets. Over the last two decades European finance has undergone a profound change, with overall bank financing dropping from over 70% to less than 50% in the three largest Eurozone economies, Germany, France, and Italy (Eichengreen 2008, pp. 419-420). This shifts the corporate governance model towards a convergence with the United States model, thus undermining one of the pillars of the social compact between employers and workers. The long-term view of profits stemming from close relationships between banks and corporations that provided an environment of stable relationships between capital and labour could be undergoing fundamental change. The erosion of these characteristics of Europe's organizational structures and institutional relations renders this system increasingly fragile and potentially unstable.

The major issue is internal adaption to changes in the world economy in the long run. According to Frieden (2009), the major difference between the globalisation of the period before World War I and the current wave of globalisation is that in the former global setting political elites were positively inclined to the ever-growing integration of the world economy and were not constrained by internal politics. This meant that adaption to changes in the previous globalisation were often painful, in terms of not-insignificant drops in both prices and wages. Clearly, this type of adaptation is impossible in Europe today. It has become common to plead for a reform of this social model and for labour market legislation, with the aim of giving it more flexibility and thus enhancing competitiveness (André Sapir 2006; Jean Pisani-Ferry 2008). Another impediment to competitiveness that corporations and businesses would like to see streamlined is extensive government regulation. These are not small tasks and cannot be easily achieved in democratic societies.

All of these deeper causes are linked to a major shift in manufacturing and trade that stems from the rise of emerging markets and relies on the ever-increasing and for a long time self-reinforcing integration of the world economy. Without adaptation, the survival of the European model, the European Union as a single market, and the Europe Monetary Union are all in question. Long-term reform is needed to enable the European Union as a whole to benefit from globalisation. These deeper processes correspond to the deeper factors that determine economic and social reality, which are analogous to the processes that Keynes found important when analysing the previous globalisation.

6. The Eurozone Debt Crisis

The world financial crisis of 2008 triggered a new expansion of government debt in the European Union and the Eurozone. The financial markets had assumed that the government bonds of the Eurozone countries held similar low risk, thus almost equa-

lizing the yields on these bonds throughout the Eurozone. When Greece admitted that it had underreported its level of government debt, the financial markets woke up to the idea that a Eurozone country could actually default on its debt. This immediately led to a differentiation of bond yields for countries identified as higher risk, thus making the refinancing of their debt extremely expensive compared to that of German bunds (the country with the lowest risk).

All of a sudden the deficiencies of the Eurozone became visible. What was obviously lacking was what every monetary union should have: (i) a central bank in the full meaning of the word, that is, a lender of last resort; (ii) a mechanism to mutually provide guarantees (at least in part) for sovereign debts of the member states; and (iii) a system of fiscal transfers. Not only did the Eurozone not possess all of these instruments, it did not possess a single one of them. In other words the common currency had no real central bank, no banking supervisor, and no fiscal backing of any sort.

These were then the major issues that needed to be addressed. Instead, what the world saw was a slow and inadequate response to the issue of government debt, with procrastination and brinkmanship on almost all issues.

What is striking about the crisis of the Eurozone is the long drawn-out negotiation on the remedies and solutions, which has cast a shadow on the ability of the Eurozone countries to save the European Monetary Union. Of course, these negotiations are far more complicated than, say, the ones conducted by the Four, as described in *The Economic Consequences of the Peace*, due to the very existence in the European Union of 28 members and all its institutions, as well as the Eurozone with its 19 members and its major institution, the European Central Bank (ECB). In fact, the whole European project can be described as a never-ending negotiation and consensus-building process.

Once again the negotiations dealing with the crisis, displayed the overwhelming dominance of national interest and internal political constraints. The primacy of everyday politics was reasserted in spite of the costs or the gravity of the situation. There was barely an attempt to approach the problem from the standpoint of the Eurozone or the European Union as a whole, other than to adopt last minute stopgap measures. One cannot but recall Keynes's description of the Conference in Versailles: "A sense of impending catastrophe overhung the frivolous scene; the futility and smallness of man before the great events confronting him..." (Keynes 1920, pp. 3-4).

The handling of the crisis has been inadequate from the very beginning and the future of the common currency remains unresolved. A series of fundamentally mistaken decisions can be identified in the way the crisis was approached. Firstly, the backing of all banks, stemming both from the fear that a Lehman-style default would trigger a major financial crisis and from lobbying by the banks, led to complete government backing of the banking sector. This directly led to a rapid increase in government debt, and to a vicious circle of bank and government debt. This model was established by the Irish government with its promise (in order to calm the panic after the crisis broke out in 2008) of a government guarantee of all bank debt, thus shifting the burden onto the taxpayers. When the Irish government sought to backtrack on

this decision in 2010 when seeking a loan from the European Union and the IMF, it was pressured by the ECB to back down and stand by its earlier promise.

Secondly, the handling of the Greek debt showed that muddling through for domestic political reasons lead to too-little-too-late policies that actually amplified the problem. When the magnitude of the government debt was revealed in 2010 it was obvious that Greece was insolvent. The logical remedy would have been a major debt write-off. Instead, the servicing of the debt was treated as a liquidity problem. This, in turn, through tactics created to avoid handing the problem solely to the IMF as well as to satisfy the no-bailout rules of the Eurozone, created the Troika (IMF, ECB, EC) and turned the issue of Greek debt into a full-blown Eurozone crisis. In other words, not dealing with the issue by pretending that it was not a problem of insolvency did not prevent the financial markets from forming a realistic opinion and identifying possible risk in other countries of the Eurozone "periphery", thus pushing up interest rates. The main beneficiaries of the Greek bailout were foreign banks, mainly French and German. The banks were able to sell Greek bonds at a higher price, were paid in full on the ones due, and received interest on the ones remaining.

In order to avoid future Greek-style bailouts, the German chancellor Angela Merkel got French president Nicolas Sarkozy to agree (October 2010) that in future private bondholders would have to bear the consequences if banks ran into problems. This only added fuel to the fire, since the financial markets calculated that some of the other economies in the Eurozone might also become insolvent. The fact is that all the actions taken during the two-year period that included the first Greek bailout of 110 billion euro (May 2010), the Irish bailout of 85 billion euro (November 2010), and the 78 billion euro bailout of Portugal (May 2011), just managed to make a temporary dent in the expectations of the financial markets. It looked like things were spinning out of control, and worse was to come.

The question is why did the leaders of Europe allow such unrealistic goals to be set? From the outset it must have been clear that there was no way in which it would be possible for a government that had such a large deficit (15.5% of GDP) and a debt then estimated at 130% of GDP to service a three-year bailout loan of 110 billion euro at 5.5% while at the same time running a current account deficit (Philippe Legrain 2014, loc. 1244 of 7949). The austerity measures naturally put the Greek economy into recession and on a downward spiral of falling GDP, falling employment, falling fiscal revenue, and a higher government debt ratio. Under these circumstances, with difficult measures being passed, the need for a second bailout became obvious. Another bailout package was proposed, along with the largest private debt reduction and restructuring in history, through a deal with the private creditors. Throughout this period the Greek economy was sinking, with a yearly drop in GDP of 7% in 2011 alone, and will cumulatively be around 25% from the beginning of the crisis by the end of 2014, with a similar or higher unemployment rate.

What made things worse was the open discussion of the possible exit of Greece from the Eurozone, dubbed the "Grexit" in 2012, making the financial markets react once again. Launching this as a real possibility, at a time when what would actually be undertaken was still unclear, was a serious political mistake with potentially dire economic consequences. In the end it was taken off the agenda. Under certain circumstances it might become an option again.

Is it really surprising that such harsh austerity measures, along with an overbearing foreign presence and *diktat*, should inspire populist movements on both the left and right of the political spectrum? Only through an electoral law that allocates 50 bonus seats in the Greek parliament to the party that gets the most votes (hardly a device compatible with representative democracy) were the major traditional parties, backed by a left-leaning partner, able to form a coalition that pledged to keep Greece in the Eurozone, thus acquiescing to the hard austerity measures of the second European bailout package.

While the contents of this paper were being finalized, political turmoil became especially evident with the electoral triumph of Syriza, a radical left-wing coalition that was widely supported and propelled into power by widespread anti-austerity sentiment. The coalition had pledged to renegotiate the terms of the austerity program with the countries and institutions holding Greece's external debts. The dynamics of the political drama that once again included the possibility of "Grexit" are beyond the scope of this paper. However, it is important to stress that the leadership of Syriza shifted to a complete reversal of its original opposition against policies of austerity; through negotiating a new 86 billion euro bailout.

It is not my purpose here to go into detail concerning the conditions of the previous bailout package for Greece. The many items include a radical restructuring of government at both national and local levels, a restructuring of the national health service, a decrease in public sector salaries and pensions, higher VAT, caps on pensions and public salaries, 15 billion euro of privatization revenue in a few years and 50 billion euro over the medium term, etc. This type of speedy privatization under public pressure could result in fire-sale prices and low revenues. In fact, such prices would come close to downright expropriation.

The more recent bailout package basically amounts to a continuation of austerity policies. Revenues derived from the privatization of public assets remain targeted at 50 billion euro; however, the deadline for these revenues has been extended to 30 years and will essentially be managed by the member organizations forming the Troika. The further reform of the pension system and labour market, along with the goal of achieving a 3.5% primary budget surplus by 2018, are essential elements of the program that also includes automatic cuts in public spending if fiscal targets are not met. In short, the more current policies are a continuation of the past policies. The only difference that can be noted at this point is that the IMF has come to the conclusion that the debt is unsustainable and that a write-off is necessary (International Monetary Fund 2015). I am willing to predict there will be a further drop in the Greece's GDP within the next couple of years, and that at some point these sizeable external debts will be written off.

At this point, it would be, it seems, instructive to make an attempt to compare Keynes's analysis and policy prescriptions in regards to the Versailles Treaty's treatment of Germany and the measures being forced on Greece today. Both countries were seen as culprits and had been portrayed in the media at large as deserving punishment. Both have had harsh measures and conditions imposed upon them that were impossible to meet. Furthermore, both countries have been dealt with politically on the basis of an internationally backed ultimatum. In both countries there occurred

deep social consequences that bred a politics of resentment. The analogies between Keynes's analysis and predictions concerning the consequences for Germany of the policies of the victors at Versailles and the Versailles Treaty and the treatment of Greece in the current crisis by the Eurozone countries are depicted in the following table (see Table 2).

Table 2 A Comparison of Keynes's Recommendations, Analysis and Predictions Concerning the Consequences for Germany and an Analogy with the Current Greek Debt Crisis

Keynes's analysis and predictions ECP	The policy of the victors at Versailles	Germany - results of the Treaty	Greece - results of the bailout package
Primacy of politics	Primacy of politics	Primacy of politics	Primacy of politics
Need for equitable post-conflict solutions	Germany seen as major culprit Method – ultimatum	Punishment - no voice	Greece seen as major culprit Basically - ultimatum
European perspective	National perspectives, goals and constraints	Expropriation of resources and extreme reparations	Quick privatization and harsh austerity measures
Prediction - loss of confidence of society in itself and future	No concern for internal political outcomes	Loss of confidence of society in itself and its future	Loss of confidence of society in itself and its future
Prediction - dire economic conditions breed extreme political movements	No concern for internal political outcomes	Politics of resentment and extreme political movements - Nazism	Politics of resentment and extreme political movements - Golden Dawn

Source: Author's analysis - summary table.

True, the analogies break down when it comes to certain historical and economic features. Greece has not been blamed for starting a major world war, as was the case with Germany. More importantly, Greece's economy is small, comparatively speaking - which makes the treatment of Greece even more incomprehensible.

Another interesting parallel is the way German reparations were dealt with and the way the issue of Greek debt is being handled in terms of ability-to-pay criteria, which Keynes considered should be lenient enough to enable recovery, i.e., growth. Looking back at the post-Versailles period, it becomes obvious that the unrealistic demands on Germany led to its inability to make coal deliveries, which prompted the occupation of the Ruhr. The outrage that followed further sowed the seeds of resentment and passive resistance and set the stage for the hyperinflation that was to come. This had to be dealt with through modification of the debt, accompanied by easing of the repayment schedules. The Dawes plan (1924) eased the repayment schedule and provided US loans to Germany so that it could pay the reparations. It also provided for the end of the occupation of the Ruhr. However, the Reich bank remained under Allied supervision. Although this stabilized the German economy for a while, it soon became obvious that in spite of growth and the stabilization of the currency, the burden of the debt was so crushing that the payments could not be met. The Young plan that was introduced in 1929 reduced the debt to less than half the original sum and eased annual repayment. Again the reparations were financed through credit provided by American banks. The Wall Street Crash of 1929 dried up American credit and president Hoover proposed a moratorium. After the banking crisis in Germany,

the Great Depression made it impossible to expect payments. Another conference was held in Lausanne in 1932. There was a consensus to reduce the remainder of the debt by 90%, but this was conditional on the United States writing off Allied debt, which the US Congress refused to do. The Nazi regime repudiated the debt. All in all, Germany repaid around 12% of the debt (Sally Marks 1978, p. 233).

It is interesting to note that after World War II the remainder of the debt was taken up at the London Debt Conference in 1952. According to this settlement, all of German debt from 1919-1945 was accounted for. Half of the debt was written off on the spot. The other half was subsumed in the repayment of a portion of the Marshall Plan, which was given priority. The rest of the debt was to be paid after the reunification of Germany. According to Helge Berger and Albrecht Ritschl (1995) the United States pushed this on the other parties involved to give Germany foreign debt relief on a large scale. It should also be remembered that Germany had an enormous write-off in terms of internal debt, in which the creditors were basically wiped out. This was done through a simple currency reform under the auspices of the United States Army in 1948. Needless to say, the effect of these measures was the removal of a debt trap that would have had disastrous consequences for the West German economy, the very type of debt trap that Greece is now being thrown into.

A comparison of Keynes's predictions, the results of the Treaty, the consequences for Germany and the possible outcomes of the current Greek debt crisis are given in the following table (see Table 3).

Table 3 Keynes's Analysis and Predictions, the Results of the Treaty for Germany and the Probable Results of the Current Austerity Programme for Greece

Keynes's analysis and predictions ECP	The policy of the victors at Versailles	Germany - results of the Treaty	Greece - results of the bailout package
Criteria - ability-to-pay - impossible conditions bound to fail	Will set exact amount of reparations later - but will be high as a matter of principle (226 billion Marks)	Failure to provide coal under Treaty, occupation of Ruhr, resentment and hyperinflation (1923) Dawes plan (1924) Young plan (1929) Lausanne (1932) Nazis repudiate debt Reparations paid: 12% of total	25% drop in GDP, high unemployment (>25%) First bailout (2010) Second bailout (2011) Private Sector Initiative (PSI) - 53% write-off and restructuring Grexit - discussed and abandoned New Grexit discussed (2015) Third bailout (2015) Possible new write off?
Possible outcome - unstable and disorganized Europe	No concern for outcome in terms of Europe	Nazi regime - World War II	Lost decade - further drop in GDP Radical politics??

Source: Author's analysis - summary table.

7. Europe's Future

Finally, there was action. In August 2012, as rising risk premiums on Spanish and Italian sovereign bonds were threatening the very survival of the Eurozone, the European Central Bank (ECB) President Mario Draghi announced that the ECB would "do whatever it takes" to preserve the Eurozone. This meant using "outright monetary transactions", i.e., the unlimited purchase of government bonds, provided governments subscribe to the rules of the newly established European Stability Mechanism. In other words, the ECB did become a potential lender of last resort. Furthermore, there has been agreement on the creation of a banking union, with the ECB acting as supervisor. In 2014 the ECB began supervising around 130 banks with 80% of Eurozone assets. Also, it was agreed that a Single Resolution Mechanism (SRM) worth 55 billion euros would be established over a period of ten years. All of these were no doubt steps in the right direction, but have still not put an end to the Eurozone crisis.

Certainly, the decision by the ECB to step in with "outright monetary transactions" and the very announcement of that policy helped to reduce the financial markets' pressure on borrowing by Spain and Italy. However, the German Constitutional Court had ruled against this ECB pledge to buy unlimited government bonds of distressed countries and had called on the European Court of Justice (ECJ) to confirm its decision. This was a step backwards and could have made the ECB less effective in dealing with sovereign risks. In other words, it jeopardized the ECB's ability to be a lender of last resort. In June of 2015, the ECJ ruled in favour of the ECB commitment and informed the German Constitutional Court that will make its own decision affecting Germany's role in this on-going process. This makes the establishment of a banking union, a complicated task, even more urgent. What is lacking is Eurozone deposit insurance, analogous to deposit insurance in the United States. This would eliminate the risk of a potential run on the banks in a peripheral Eurozone country and thus stabilize the banking sector at the Eurozone level. Such an institution would both be funded by the banks and would need some kind of fiscal backup to succeed. At the moment there is no political will to set up such a mechanism.

This brings us to the issue of fiscal federalism which is needed to some extent to back up both the ECB's role as bank supervisor and lender of last resort and, above all, to relieve the pressure of the financial markets on the heavily indebted governments. This would mean some mutualisation of debt through Eurobonds that would be backed by all members of the Eurozone. Here there are several options, of which the one introducing redemption bonds proposed by the German Council of Economic Experts is probably the most politically viable (Hasan Doluca et al. 2012). The basic idea is to have a mutual guarantee of bonds above the government debt of 60% set by the Maastricht Treaty. These would then be slowly phased out through the slow adjustment of debt (25 years) that governments had agreed to in the fiscal compact to bringing down debt to the level set under Maastricht.

In this context it is worth mentioning that, given the current numbers, if the Eurozone was federalized like the United States it would have a similar debt and a smaller current budget deficit as a percentage of GDP, and would probably be able to borrow more cheaply or at the same rate as the United States is currently doing. This

would not necessarily imply bailouts for individual states: in the United States there is no such bailout policy for individual states, most of them being subject to self-imposed balanced-budget laws.

This is unlikely, as European leaders have only acted, under extreme pressure, to prevent the unravelling of the Eurozone and not to fundamentally fix it. As at the time when Keynes wrote *The Economic Consequences of the Peace*, the primacy of politics has been evident. This is natural up to a point. What seems to be somewhat disconcerting is the overwhelming primacy of national politics and internal political constraints that are endangering the survival of the European Union, a project and work in progress that had proved to be the most successful peaceful political and economic integration in world history. The European Union was for so long a positive-sum game and can continue to be so in the future. In fact it was considered as such precisely for the reason that it affirmed the national interests of its members. I feel that having looked at the problems of Europe from a European and not a national (and certainly not a nationalist) perspective, Keynes would have agreed to a more federalized Europe as a response to the current crisis. Of course, this does not mean that he would have necessarily agreed with all of the proposed solutions or with any one in particular.

So far, the European Union has responded to challenges by ever-deeper integration. It seems to be such an obvious solution, yet one should remember that it was brinkmanship, an inadequate and late response, a failure to grasp the gravity of the situation, and an underestimation of consequences that led to the end of globalisation in 1914. This time, once again, events may overtake the actors and bring down the European Union as we now know it. Surely, just as at the time when *The Economic Consequences of the Peace* was written, quick, broad, and magnanimous measures are needed to restore and advance the vision of the European Union as a model of a democratic, prosperous, socially equitable, knowledge-based, innovative society, firmly linked through a federation of nations that share common values. In his appeal for American aid Keynes pointed to a “Europe, the mother of art and knowledge, in spite of everything” (Keynes 1920, p. 268).

In 1919 Keynes wrote: “Europe is solid with itself. France, Germany, Italy, together, and Austria and Holland, Russia and Romania and Poland, throb together, and their civilisations are essentially one. They flourished together ... and they may fall together” (Keynes 1920, p. 3).

At the time he also noted that he could not “disinterest himself from the great unfolding of the great historic drama of these days which will destroy great institutions, but may also create a new world” (Keynes 1920, p. 6). One wishes that the European leaders would heed his words.

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