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Those Revolting Europeans

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The French are revolting. The Greeks, too. And it's about time.

Both countries held elections Sunday that were in effect referendums on the current European economic strategy, and in both countries voters turned two thumbs down. It's far from clear how soon the votes will lead to changes in actual policy, but time is clearly running out for the strategy of recovery through austerity — and that's a good thing.

Needless to say, that's not what you heard from the usual suspects in the run-up to the elections. It was actually kind of funny to see the apostles of orthodoxy trying to portray the cautious, mild-mannered François Hollande as a figure of menace. He is "rather dangerous," declared The Economist, which observed that he "genuinely believes in the need to create a fairer society." Quelle horreur!

What is true is that Mr. Hollande's victory means the end of "Merkozy," the Franco-German axis that has enforced the austerity regime of the past two years. This would be a "dangerous" development if that strategy were working, or even had a reasonable chance of working. But it isn't and doesn't; it's time to move on. Europe's voters, it turns out, are wiser than the Continent's best and brightest.

What's wrong with the prescription of spending cuts as the remedy for Europe's ills? One answer is that the confidence fairy doesn't exist — that is, claims that slashing government spending would somehow encourage consumers and businesses to spend more have been overwhelmingly refuted by the experience of the past two years. So spending cuts in a depressed economy just make the depression deeper.

Moreover, there seems to be little if any gain in return for the pain. Consider the case of Ireland, which has been a good soldier in this crisis, imposing ever-harsher austerity in an attempt to win back the favor of the bond markets. According to the prevailing orthodoxy, this should work. In fact, the will to believe is so strong that members of Europe's policy elite keep proclaiming that Irish austerity has indeed worked, that the Irish economy has begun to recover.

But it hasn't. And although you'd never know it from much of the press coverage, Irish borrowing costs remain much higher than those of Spain or Italy, let alone Germany. So what are the alternatives?

One answer — an answer that makes more sense than almost anyone in Europe is willing to admit — would be to break up the euro, Europe's common currency. Europe wouldn't be in this fix if Greece still had its drachma, Spain its peseta, Ireland its punt, and so on, because Greece and Spain would have what they now lack: a quick way to restore cost-competitiveness and boost exports, namely devaluation.

As a counterpoint to Ireland's sad story, consider the case of Iceland, which was ground zero for the financial crisis but was able to respond by devaluing its currency, the krona (and also had the courage to let its banks fail and default on their debts). Sure enough, Iceland is experiencing the recovery Ireland was supposed to have, but hasn't.

Yet breaking up the euro would be highly disruptive, and would also represent a huge defeat for the "European project," the long-run effort to promote peace and democracy through closer integration. Is there another way? Yes, there is — and the Germans have shown how that way can work. Unfortunately, they don't understand the lessons of their own experience.

Talk to German opinion leaders about the euro crisis, and they like to point out that their own economy was in the doldrums in the early years of the last decade but managed to recover. What they don't like to acknowledge is that this recovery was driven by the emergence of a huge German trade surplus vis-à-vis other European countries — in particular, vis-à-vis the nations now in crisis — which were booming, and experiencing above-normal inflation, thanks to low interest rates. Europe's crisis countries might be able to emulate Germany's success if they faced a comparably favorable environment — that is, if this time it was the rest of Europe, especially Germany, that was experiencing a bit of an inflationary boom.

So Germany's experience isn't, as the Germans imagine, an argument for unilateral austerity in Southern Europe; it's an argument for much more expansionary policies elsewhere, and in particular for the European Central Bank to drop its obsession with inflation and focus on growth.

The Germans, needless to say, don't like this conclusion, nor does the leadership of the central bank. They will cling to their fantasies of prosperity through pain, and will insist that continuing with their failed strategy is the only responsible thing to do. But it seems that they will no longer have unquestioning support from the Élysée Palace. And that, believe it or not, means that both the euro and the European project now have a better chance of surviving than they did a few days ago.