Europe in 2013: A Year of Decision

January 3, 2013 | 1000 GMT

Print

Text Size

Stratfor

By George Friedman
Founder and Chief Executive Officer

The end of the year always prompts questions about what the most important issue of the next year may be. It's a simplistic question, since every year sees many things happen and for each of us a different one might be important. But it is still worth considering what single issue could cause the world to change course. In my view, the most important place to watch in 2013 is Europe.

Taken as a single geographic entity, Europe has the largest economy in the world. Should it choose to do so, it could become a military rival to the United States. Europe is one of the pillars of the global system, and what happens to Europe is going to define how the world works. I would argue that in 2013 we will begin to get clarity on the future of Europe.

The question is whether the European Union will stabilize itself, stop its fragmentation and begin preparing for more integration and expansion. Alternatively, the tensions could intensify within the European Union, the institutions could further lose legitimacy and its component states could increase the pace with which they pursue their own policies, both domestic and foreign.

The Embattled European Project

It has been more than four years since the crisis of 2008 and about two years since the problems spawned by 2008 generated a sovereign debt crisis and a banking crisis in Europe. Since that time, the crisis has turned from a financial to an economic crisis, with Europe moving into recession and unemployment across the Continent rising above 10 percent. More important, it has been a period in which the decision-making apparatus created at the founding of the European Union has been unable to create policy solutions that were both widely acceptable and able to be implemented. EU countries have faced each other less as members of a single political entity than as individual nation-states pursuing their own national interests in what has become something of a zero-sum game, where the success of one has to come at the expense of another.

This can be seen in two ways. The first dimension has centered on which countries should bear the financial burden of stabilizing the eurozone. The financially healthier countries wanted the weaker countries to bear the burden through austerity. The weaker countries wanted the stronger countries to bear the burden through continued lending despite the rising risk that the loans will not be fully repaid. The result has been constant attempts to compromise that have never quite worked out. The second dimension has been class. Should the burden be borne by the middle and lower classes by reducing government expenditures that benefit them? Or by the elites through increased taxation and regulation?

When you speak with Europeans who support the idea that Europe is in the process of solving its problems, the question becomes: What problem are they solving? Is it the problem of the banks? The problem of unemployment? Or the problem of countries' inability to find common solutions? More to the point, European officials have been working on this problem for years now, and they are among the best and brightest in the world. Their inability to craft a solution is not rooted in a lack of good ideas or the need to think about the problem more. It is rooted in the fact that there is no political agreement on who will pay the price geographically and socially. The national tensions and the class tensions have prevented the crafting of a solution that can be both agreed upon and honored.

If the Europeans do not generate that sort of solution in 2013, it is time to seriously doubt whether a solution is possible and therefore to think about the future of Europe without the European Union or with a very weakened one. If, however, Europe does emerge with a plan that has general support and momentum behind it, then we might say that Europe is beginning to emerge from its crisis, and that, in turn, would be the single most important thing that happens in 2013.

At this point, a reasonable person will argue that I am ignoring the United States, which has different but equally significant economic problems and is also unable to generate consensus on how to solve them, as we have seen during the recent "fiscal cliff" affair, which will have many more iterations. But as valid as the comparison is on the financial level, it is not valid on the political level. The United States does not face the dissolution of the republic if it follows contradictory policies. The United States is more than two centuries old and has weathered far worse problems, including the Civil War and the Great Depression. The European Union is only about 20 years old in its current form, and this is its first significant crisis. The consequences of mismanaging the U.S. financial system are significant to say the least. But unlike Europe, the consequences are not an immediate existential threat.

The Other Costs of the Crisis

It is the political dimension that has become the most important, not the financial. It may well be that the European Union is in the process of dealing with its banking problems and might avoid other sovereign debt issues, but the price it has paid is both a recession and, much more serious, unemployment at a higher rate than in the United States overall, and enormously higher in some countries.

We can divide the European Union into three categories by measuring it against the U.S. unemployment rate, which stands at about 7.7 percent. There are five EU countries significantly below that rate (Austria, Luxembourg, Germany, Netherlands and Malta). There are seven countries with unemployment around the U.S. rate (Romania, Czech Republic, Belgium, Denmark, Finland, the United Kingdom and Sweden). The remaining 15 countries are above U.S. unemployment levels; 11 have unemployment rates between 10 and 17 percent, including France at 10.7 percent, Italy at 11.1 percent, Ireland at 14.7 percent and Portugal at 16.3 percent. Two others are staggeringly higher -- Greece at 25.4 percent and Spain at 26.2 percent. These levels are close to the unemployment rate in the United States at the height of the Great Depression.

For advanced industrialized countries -- some of the most powerful in Europe, for that matter -- these are stunning numbers. It is important to consider what these numbers mean socially. Bear in mind that the unemployment rate goes up for younger workers. In Italy, Portugal, Spain and Greece, more than a third of the workforce under 25 is reportedly unemployed. It will take a generation to bring the rate down to an acceptable level in Spain and Greece. Even for countries that remain at about 10 percent for an extended period of time, the length of time will be substantial, and Europe is still in a recession.

Consider someone unemployed in his 20s, perhaps with a university degree. The numbers mean that there is an excellent chance that he will never have the opportunity to pursue his chosen career and quite possibly will never get a job at the social level he anticipated. In Spain and Greece, the young -- and the old as well -- are facing personal catastrophe. In the others, the percentage facing personal catastrophe is lower, but still very real. Also remember that unemployment does not affect just one person. It affects the immediate family, parents and possibly other relatives. The effect is not only financial but also psychological. It creates a pall, a sense of failure and dread.

It also creates unrooted young people full of energy and anger. Unemployment is a root of anti-state movements on the left and the right. The extended and hopelessly unemployed have little to lose and think they have something to gain by destabilizing the state. It is hard to quantify what level of unemployment breeds that sort of unrest, but there is no doubt that Spain and Greece are in that zone and that others might be.

It is interesting that while Greece has already developed a radical right movement of some size, Spain's political system, while experiencing stress between the center and its autonomous regions, remains relatively stable. I would argue that that stability is based on a belief that there will be some solution to the unemployment situation. Its full enormity has not yet sunk in, nor the fact that this kind of unemployment problem is not fixed quickly. It is deeply structural. The U.S. unemployment rate during the Great Depression was mitigated to a limited degree by the New Deal but required the restructuring of World War II to really address.

This is why 2013 is a critical year for Europe. It has gone far to solve the banking crisis and put off a sovereign debt crisis. In order to do so, it has caused a serious weakening of the economy and created massive unemployment in some countries. The unequal distribution of the cost, both nationally and socially, is the threat facing the European Union. It isn't merely a question of nations pulling in different directions, but of political movements emerging, particularly from the most economically affected sectors of society, that will be both nationalist and distrustful of its own elites. What else can happen in those countries that are undergoing social catastrophes? Even if the disaster is mitigated to some degree by the shadow economy and emigration reducing unemployment, the numbers range from the painful to the miserable in 14 of Europe's economies.

Europe's Crossroads

The European Union has been so focused on the financial crisis that it is not clear to me that the unemployment reality has reached Europe's officials and bureaucrats, partly because of a growing split in the worldview of the European elites and those whose experience of Europe has turned bitter. Partly, it has been caused by the fact of geography. The countries with low unemployment tend to be in Northern Europe, which is the heart of the European Union, while those with catastrophically high unemployment are on the periphery. It is easy to ignore things far away.

But 2013 is the year in which the definition of the European problem must move beyond the financial crisis to the social consequences of that crisis. Progress, if not a solution, must become visible. It is difficult to see how continued stagnation and unemployment at these levels can last another year without starting to generate significant political opposition that will create governments, or force existing governments, to tear at the fabric of Europe.

That fabric is not old enough, worn enough or tough enough to face the challenges. People are not being asked to die on a battlefield for the European Union but to live lives of misery and disappointment. In many ways that is harder than being brave. And since the core promise of the European Union was prosperity, the failure to deliver that prosperity -- and the delivery of poverty instead, unevenly distributed -- is not sustainable. If Europe is in crisis, the world's largest economy is in crisis, political as well as financial. And that matters to the world perhaps more than anything else.

Send us your thoughts on this report.
