Closing Comments by James K. Galbraith at a Symposium of the Global Progressive Forum, Res Publica and the Parliamentary European Socialists, Lisbon, July 10, 2010, in the presence of Prime Minister José Socrates.

Thank you very much, indeed. Prime Minister, organizers of this conference, thank you, especially, for the opportunity to make brief closing remarks.

As I said yesterday, the conduct of the socialist governments – especially in southern Europe and the conduct of this government in particular -- in the face of the crisis has been disciplined, effective, and realistic, under very difficult circumstances and extreme external pressures. Realism is a virtue in and of itself. It is a virtue in setting, articulating, and carrying forth economic policy. And I have to believe that it must also be a political virtue, for it is easier for people to face and accept difficult choices when these are presented without illusions, and when they can see for themselves that the public sector and the Government is working in their interests.

I think a conclusion that one can fairly draw from the discussion in the last two days and especially this morning, is that it is clear that the Social-Democratic movement, the Socialist Movement, has a vision of how to come out of this crisis. It is a vision rooted in the values of greater human equality and the values of effective human development. It is a vision of a credible and functioning social welfare state, as part of an ongoing project of economic construction and environmental sustainability.

And these are very important points to make, because they have to be sustained in international debate under very difficult and trying conditions. The treaty obligations and the budget standards to which you are being held are not realistic in the same sense. They lack economic justification. They exist for ideological, political, and historical reasons only.

More important, the cuts – the very difficult, in many ways savage cuts that you are being asked to implement will not achieve the budget goals that are demanded. For a very straightforward reason: economies will contract and tax revenues will fall. A study conducted by the top staff of the International Monetary Fund shows that, since the onset of the crisis, fully half of the increase in budget deficits is the simple result of the collapse of tax revenues as a result of falling economic activity. And a further large share is due to the relationship between lower economic growth and previously existing interest payments on national debts. Less than 10% is due to increased public spending in response to the crisis -- less than 10%. Since market participants know this, budget programs based on the treaty standards are inherently not credible.

It is therefore not realistic to expect that credit markets will reopen as they were before. So, as Keynes wrote in 1920 of another unrealistic treaty, that of Versailles, what is required ultimately will be a revision of the treaty.

What has happened in the credit markets is very likely irreversible; a Rubicon has been crossed. Financial weapons of mass destruction, like the other kind, cannot be un-invented. I'm referring here to the mechanism of credit default swaps, which make the government bond markets extremely speculative. The vulnerability of the bonds of small European countries, to a flight to safety and to speculative attack, is now a feature of the scene. It’s a rock in the channel. And if the channel cannot be navigated then a new one must be dug.

The European Central Bank has recognized this reality; grudgingly, but still -- and should be encouraged in having done so. Trapped in a cult of infallibility, central bankers often have a great deal of difficulty recognizing changes in their circumstances and accepting the need to change their policies, but when they do that we should encourage them. A new institution -- a European debt management agency such as recommended yesterday by Poul Rasmussen -- would be very helpful. But meanwhile, the purchase of government bonds, the stopgap of bond purchases by the European central bank, is better than nothing.

One further point in the cause of realism in facing this crisis. It would be very useful if economic policy discussions, in Europe and elsewhere, were conducted with a basic respect for national income accounting rules, and for the ordinary laws of double-entry bookkeeping. In particular, in a Europe which has balanced trade, it is arithmetically not possible for one country to run a surplus unless others run deficits of exactly equal amounts. Suffusing these words with moral overtones is not helpful. The surplus is not a sign of virtue and the deficit is not a sign of vice. They are merely opposite sides of an accounting relationship which is, by definition, exactly equal on both sides.

There is no virtue in seeking balance. There is no necessity that every country run a balanced current account, and certainly not within an integrated entity like Europe. Zero is not the middle number. What is necessary is that the surplus countries be satisfied to hold the bonds of the deficit countries, and to do so at reasonable interest rates permitting them to go about their business financing economic development and pursuing their goals in a reasonable way. Once that necessity is recognized, a large part of the crisis will simply go away. I should point out that there is no crisis in the relationship between the United States and China. China runs a surplus, but holds our debt and doesn't try to tell us what to do; and one could only hope that inside Europe there could be an equally harmonious and reasonable relationship between sovereign nations.

I spoke yesterday about the large Constitutional issues facing Europe, and I won't repeat that now, but I will close by raising one final issue: The question of what the final objectives of economic policy should be. This is something that needs to be discussed. Budget deficits and debt levels, specified to arbitrary and capricious targets; these are not final objectives of economic policy. They are at best means to some larger goal. The same is true of interest rates or other instruments of monetary policy.

This is a question that we faced in the United States, in the Congress of the United States, in the 1970s. And there at that time, as a very young member of the professional staff of the Banking Committee at the House of Representatives, I was on a team that drafted what became the Full Employment and Balanced Growth Act of 1978; the Humphrey-Hawkins Law. The law did a number of useful things, including establishing the primacy of the Congress of the United States over our central bank, establishing who worked for whom and to what goals. But its larger symbolic statement, was to declare what the broader economic objectives of policy for the government of the United States actually were, and the phrasing here was important.

We chose to write into law, that the goals for economic policy for the United States were full employment, balanced growth, and reasonable price stability. Full employment, balanced growth, and reasonable price stability. Economists scoffed. But the standard has held up over, now, more than 30 years. And it is a respected standard by the relevant agencies of the United States, including by the central bank. So, while I'm not one -- I'm not the kind of American who says you should do as we do – I'll just close by suggesting that this is a good example. It is something worth remembering; something worth thinking about. And I commend it to you as an example of international good practice in economic policy. Thank you very much, indeed.

(Transcript by Amy Masarwe.)