The Rotten Heart of Europe

A technical note on EMU and the rise of world-wide narco-capitalism

by Arno Tausch

e-book # 44

Foreword to the reprint of a book chapter from the work: Globalization and European Integration.

There were many critics of European Monetary Union in the 1990s. The quantitative world systems scholar Arno Tausch, from Innsbruck University, in an electronic book, published in 1998 by the World Systems Archive of the University of California, Riverside predicted with many others that the Euro-zone will disintegrate. As the analyst Christopher M. Quigley recently reminded his audience (http://www.marketoracle.co.uk/Article19081.html) recent and unfolding events in Greece were foretold by the former European Union economist Bernard Connolly in his classic book “The Rotten Heart of Europe.”


Let us quote just two passages from the Connolly book:

“As we shall see, in France the long arm of the authoritarian state has pressurized dissident economists and bankers, deployed financial information programmes on international TV channels, threatened securities houses with loss of business if they questioned the official economic line, and shamelessly used state-owned and even private-sector banks, in complete contradiction with their shareholder’s interests and Community law, to support official policy. ………. The economic profession in Europe organized literally hundreds of conferences, seminars and colloquia to which only conformist speakers were invited; and the Commission’s “research” programmes financed large numbers of economic studies to provide the right results from known believers.”

Connolly also said at the time:

“My central thesis is that the ERM and the EMU (European Monetary Union, the mechanism with ultimately brought the Euro into technical existence) are not only inefficient but also undemocratic: a danger not only to our wealth but to our freedom and ultimately, our peace.”
Christopher M. Quigley is right in insisting that under the current Euro regime we have stable exchange rates between the Euro countries but there is no harmony between the disparate economies that make up Euroland. The Euro is not a “currency” as such but in actual fact is an exchange rate mechanism only. The Euro is allowing cheap German goods flood Europe and explains why it has 200-300 billion Euros of trade surpluses with its economic partners.

“In a survey last week over 80% of Greeks said they wanted to exit the Euro but this voice is not being reported in much the same fashion that Connolly’s concerns were silenced by elite bankers and politicos. However, in 1995 when the Euro mechanism was being set up the world was less connected. Today we have international hedge funds connected through Cray computers ready to “play” the markets. As soon as traders realize the Euro is a one way bet they will opt to profitably destroy the exchange mechanism because of its exposed failings. The Emperor has been seen to have no cloths. As sure as night follows day they are going to reap their reward. They will seek to emulate George Soros when he reaped his one billion sterling paycheck on the 16th. September 1992 (“Black Friday”). It was that day the bank of England lost 3.4 billion sterling in one single 24 hour period, defending a flawed exchange link to Euroland. It is my suspicion that Germany sees this as a very real scenario and does not desire to waste its hard won foreign reserves on a “Norman Lamont” (The “Black Friday” chancellor of the British exchequer) type endgame.” [Christopher M. Quigley, http://www.marketoracle.co.uk/Article19081.html]

Quigley proposes that the “PIIGS”: Portugal, Italy, Ireland, Greece and Spain, should form a league for the purpose of national economic restructure. This league should negotiate an exit from the Euro and allowing their currencies to “float” once more. This will immediately allow their economies to become competitive again without widespread deflation. Most importantly all Euro loans must be devalued based on a new negotiated exchange conversion, as per the Argentinean model.

Bernard Connolly lost his job at the Commission; the European Court of Justice states in his final judgement (JUDGMENT OF THE COURT, 6 March 2001):

4 By letter of 18 August 1995, Mr Connolly applied to be reinstated in the Commission service at the end of his leave on personal grounds. The Commission, by decision of 27 September 1995, granted that request and reinstated him in his post with effect from 4 October 1995.

5 Whilst on leave on personal grounds, Mr Connolly published a book entitled The Rotten Heart of Europe - The Dirty War for Europe's Money without requesting prior permission under the second paragraph of Article 17 of the Staff Regulations.
6 Early in September, and more specifically between 4 and 10 September 1995, a series of articles concerning the book was published in the European and, in particular, the British press.

7 By letter of 6 September 1995, the Director-General for Personnel and Administration, in his capacity as appointing authority … informed the applicant of his decision to initiate disciplinary proceedings against him for infringement of Articles 11, 12 and 17 of the Staff Regulations and, in accordance with Article 87 of those regulations, invited him to a preliminary hearing.

8 The first hearing was held on 12 September 1995. The applicant then submitted a written statement indicating that he would not answer any questions unless he was informed in advance of the specific breaches he was alleged to have committed.

9 By letter of 13 September, the appointing authority again invited the applicant to attend a hearing, in accordance with Article 87 of the Staff Regulations, and informed him that the allegations of misconduct followed publication of his book, serialisation of extracts from it in The Times newspaper, as well as the statements he made in an interview published by that newspaper, without having obtained prior permission.

Leaving the question of intellectual freedom aside, Tausch shows in his e-book, 1998 by quantitative means that the dire predictions voiced by Connolly, Freedman, Rothschild and so many others are true. He states sarcastically:

“The above mentioned positive redistribution effect on a European scale between the North and the South (and later on, between the West and the East) could be endangered by the long-term effects of EMU. The proponents of EMU maintained all along, that it will be engine of political and economic unification on the continent. We fear that the long-term effect of the project will be an increasing nationalism and a cultural conflict along the old cultural frontier, the Limes, between the Latin and the Germanic Europe, between the wine and the beer culture, between the olive oil consumers and the sausage eaters. An increasing number of scholars propose an alternative course of action that stresses the political and social cohesion in Europe as the main pillars of a true European Monetary Union (Rothschild, 1997). There is the danger, that Euro-monetarism will accelerate the tendency of the world system on its path towards financial speculation, narco-capitalism, and the shifting of resources away from the Atlantic region towards the Pacific. On the other hand, it is evident that Europe’s long-term ascent from the Long 16th Century onwards from the state of a former periphery of the world system to a center (Arrighi, 1995; Amin,
1975), which was based on agrarian reform and mass demand, is now threatening to be reversed by the application of monetary orthodoxy.”

Only at very small and at very high levels of already existing unemployment, a ‘shock therapy’ might work to flatten out budget deficits. But else, there is an across the board negative correlation between unemployment and budget surplus, i.e. increasing unemployment still increases deficits. Saving has limits. Trying to lock countries like France and Germany together via their currencies does not forge one nation; instead it turns domestic monetary questions into international political conflicts’ (Connolly, 1995: 1995). Europe does not form an integrated economic region with truly European transnational corporations; Europe forms only a preferential market (Amin, 1997). Europe does not have a continental societal project, that would integrate such areas as research and development, public markets, and would have a joint commercial and corporate law, and as yet does not integrate the vital sectors of film and TV production. Trade union and other social law would have to be integrated, and Europe does not have as yet a joint project of external relations with the other regions of the world economy (Amin, 1997; Friedman, 1997). The EMU project should facilitate a truly common market. As the critics of the project have shown all along, the project could only function if there is a parallel economic and social policy in the member states of EMU; that means harmonization of tax and expenditure systems, the integration at the level of corporate policy, and the harmonization of trade union policy at the European level. There would have to be a coordinated European policy not only of the internal, but also of the external opening of markets - especially regarding foreign investment and capital inflows from third countries (Amin, 1997).

Economists from all around the world preached that external changes and shocks will not be answered anymore by changes in the external exchange rate. Since the exchange rate is not anymore a factor of economic policy regulation, either migration, wage flexibility, fiscal policy or economic transfers from other countries will become the main regulatory mechanisms in the new, monetarily united Union (Friedman, 1997; see also Klaus, 1997; Beirat 1996; Stephen Roach from Morgan Stanley Dean Witter, Neue Zuercher Zeitung, Monday, 16th of June, 1997: 16). Labor is not that flexible; so the result will be - in all probability - economic transfers within the EMU countries. Economic transfers are the inevitable result of monetary union (a contradiction, perhaps spelt out most clearly by the neo-liberal former acting Czech President and neo-liberal economist Vaclav Klaus, 1997). This scenario will lead to the inevitable result of a loss of autonomy of national fiscal policies (Klaus, 1997). Such a scenario is all the more likely since there is no convergence in the productivity of labor in the EMU countries themselves. Without a financial transfer system from the rich to the poor regions, the EMU will prove to be not operational, anywhere up to $bn 1000 DM will have to be transferred (Borchert, Sueddeutsche Zeitung, 1st
March, 1997: 25; Watzal, 1997), thus repeating the experience of the integration of the New Laender into the Federal Republic.

The problems of the classic ‘euro-monetarist’ Maastricht package are compounded by the fact that not governments, but parliaments decide on fiscal policy in European democracies - thus making the signatures of heads of governments or foreign ministers under treaties of stability liable to parliamentary control - or worse - Maastricht will lead to the gradual erosion of the role of the national parliaments in favor of the executive branch.

In his empirical analysis, Tausch shows that the obsession with inflation should give way to an obsession with economic growth. The ups and downs of the exchange rate are determined primarily by economic growth (‘the basics’), and not by monetary aggregates. Tausch also shows the contradictions arising from overlooking the effects of illegal money on Europe. A hard EURO would attract an enormous amount of illegal Eastern capital to Western Europe. Market imperfections and the peripheral position of Eastern Europe in the world economy cause a tendency towards a secular current account balance deficit in most of the new democracies (at least those with historical records of big landholding and a weak national state) that can practically only be closed by the shadow economy, including illegal migration and money laundering. Current account balances determine only to a certain extent international reserves, and indeed, excess reserves are a good signal for money-laundering processes taking place in the economy, but such excess reserves dampen inflation. The transformation economy, successor to peripheral socialism 1945 - 1989, Nazi occupation 1938/39 - 1945 and peripheral capitalism 1450 - 1939, is characterized, as Amin teaches us, by a secular current account balance deficit, that has to be closed by almost any means - including imports of ‘illegal savings’. Like all wealth-owning capitalist classes, the shadow economies of Eastern Europe become very interested in financial stability and the canon of ‘property rights’, once their illegal money is parked. The stability of the East European exchange rates depends on these very same huge semi-legal and illegal reserves that were accumulated by the opening of the twin Pandora’s boxes of open borders and liberalized world financial markets.

But dependency becomes decisive, when long-term growth perspectives of East and Central European economies are being determined. There are indeed ‘the balance of payments constraints’ on economic growth: not only the stability of the Eastern currency, but also short-term Eastern economic growth becomes largely dependent on the import of ‘narco’ and other laundered money, that neatly shows up in the international reserves statistics.

The stability of the capitalist system needs labor as an organized, countervailing power, that the very EURO process, as it is now underway, is about to put into
question. At least a medium-level unionization rate and earnings growth rate will be necessary to stabilize capitalism.

Arno Tausch (1998)

The Rotten Heart of Europe? A technical note on EMU and the rise of world-wide narco capitalism

Reprint of a book chapter from the work: Globalization and European Integration

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http://wsarch.ucr.edu/archive/books/tausch/spartoc.htm
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The above mentioned positive redistribution effect on a European scale between the North and the South (and later on, between the West and the East) could be endangered by the long-term effects of EMU. The proponents of EMU maintained all along, that it will be engine of political and economic unification on the continent. We fear, that the long-term effect of the project will be an increasing nationalism and a cultural conflict along the old cultural frontier, the *Limes*, between the Latin and the Germanic Europe, between the wine and the beer culture, between the olive oil consumers and the sausage eaters. This is the main hypothesis of the following Chapter. And this is not a Chapter against the EMU, it is a Chapter against Euro-monetarism. An increasing number of scholars propose an alternative course of action, that stresses the political and social cohesion in Europe as the main pillars of a true European Monetary Union (Rothschild, 1997). There is the danger, that Euro-monetarism will accelerate the tendency of the world system on its path towards financial speculation, narco-capitalism, and the shifting of resources away from the Atlantic region towards the Pacific. On the other hand, it is evident that Europe’s long-term ascent from the Long 16th Century onwards from the state of a former periphery of the world system to a center (Arrighi, 1995; Amin, 1975), which was based on agrarian reform and mass demand, is now threatening to be reversed by the application of monetary orthodoxy. The Maastricht debate is characterized by the following basic fallacies: **Fallacy number one: by high unemployment you can control inflation.** At the outset of this technical appendix, we would thus like to state that unemployment, first of all, is an enormous waste of economic resources. For 18 western democracies with complete UNDP (or Federal Ministry of Labor of the Republic of Austria) data for 1995, we have:

Graph 9.13: Unemployment is a waste of resources

![Graph showing the relationship between unemployment and budget surplus/deficit](image-url)
Legend: unemployment rates (x-axis) and budget balances (y-axis, per GDP) in OECD countries. Compiled from data series, published in the international press, 1998

Thus, only at very small and at very high levels of already existing unemployment, a ‘shock therapy’ might work to flatten out budget deficits. But else, there is an across the board negative correlation between unemployment and budget surplus, i.e. increasing unemployment still increases deficits. Saving has limits. And here, the sad story of Euro-‘monetarism’ begins (the hyphens are to indicate, that the relationship between real monetarist theory of the Milton Friedman type to contemporary European applications is far from certain; see also Friedman’s excellent essay on the EURO, 1997:

‘Jacques Rueff, fierce 1950s critic of American monetary hegemony, once said: ‘Europe will be built through a currency or it will not be built at all’. What the ERM story shows is quite the opposite: trying to lock countries like France and Germany together via their currencies does not forge one nation; instead it turns domestic monetary questions into international political conflicts’ (Connolly, 1995: 1995)

It is time to stress the fundamental weaknesses of the EMU project from the viewpoint of world system theory. Up to now, Europe does not form an integrated economic region with truly European transnational corporations; Europe forms only a preferential market (Amin, 1997). Secondly, Europe does not have a continental societal project, that would integrate such areas as research and development, public markets, and would have a joint commercial and corporate law, and as yet does not integrate the vital sectors of film and TV production. Trade union and other social law would have to be integrated, and Europe does not have as yet a joint project of external relations with the other regions of the world economy (Amin, 1997; Friedman, 1997). The EMU project should facilitate a truly common market, the free movement of capital and stable external exchange rates. As the critics of the project have shown all along, the project could only function if there is a parallel economic and social policy in the member states of EMU; that means harmonization of tax and expenditure systems, the integration at the level of corporate policy, and the harmonization of trade union policy at the European level. There would have to be a coordinated European policy not only of the internal, but also of the external opening of markets - especially regarding foreign investment and capital inflows from third countries (Amin, 1997). The ongoing negotiations on the Mutual Agreement on Investment (MAI) run counter to the very spirit of a European social area; as Jadwiga Staniszkis, as a lone preacher in the desert, has repeated here in Poland. We all know by today the Maastricht criteria (Rothschild, 1997) and the ‘shopping list’ of anti-EMU arguments:

a. in the examination year an inflation rate no more than 1.5 percent above the average of the three EU states with the lowest price rises
b. a long-term rate of interest within two percentage points of the average of the three ‘best’ countries
c. a national budget deficit (covering national, federal and local governments) less than 3 percent of GDP
d. a public debt ratio which does not exceed 60 percent of GDP
e. a currency for two years within the normal band of EMS

Fallacy number two now arises: that economic theory supports the EURO. Academic economists found 24 main arguments against the EURO:
i. external changes and shocks will not be answered anymore by changes in the external exchange rate. Since the exchange rate is not anymore a factor of economic policy regulation, either migration, wage flexibility, fiscal policy or economic transfers from other countries will become the main regulatory mechanisms in the new, monetarily united Union (Friedman, 1997; see also Klaus, 1997; Beirat 1996; Stephen Roach from Morgan Stanley Dean Witter, Neue Zuercher Zeitung, Monday, 16th of June, 1997: 16)

ii. but labor is not that flexible; so the result will be - in all probability - economic transfers within the EMU countries. Economic transfers are the inevitable result of monetary union (a contradiction, perhaps spelt out most clearly by the neo-liberal former acting Czech Premier and neo-liberal economist Vaclav Klaus, 1997). This scenario will lead to the inevitable result of a loss of autonomy of national fiscal policies (Klaus, 1997). Such a scenario is all the more likely since there is no convergence in the productivity of labor in the EMU countries themselves. Without a financial transfer system from the rich to the poor regions, EMU will prove to be not operational, anywhere up to $bn 1000 DM will have to be transferred (Borchert, Sueddeutsche Zeitung, 1st March, 1997: 25; Watzal, 1997), thus repeating the experience of the integration of the New Laender into the Federal Republic

iii. the problems of the classic ‘euro-monetarist’ Maastricht package are compounded by the fact that not governments, but parliaments decide on fiscal policy in European democracies - thus making the signatures of heads of governments or foreign ministers under treaties of stability liable to parliamentary control - or worse - Maastricht would have led to the gradual erosion of the role of the national parliaments in favor of the executive branch

iv. according to the textbooks, the function of financial markets is the transfer of savings into the financing of real economic investments (Beirat, 1996). On a global scale, European and Atlantic region savings in general will be transferred to real economic investments in East Asia, formerly the most dynamic region of the capitalist world economy (Arrighi, 1995), to be succeeded today possibly by China, and India. Gross domestic savings in the European Union are only 20%, and gross domestic investment only 19% of GDP. In the US, savings (15%) and investments (16%) are even lower. Before Fall 1997, the international system seems to work in a very simple way:

international debts financed the Asian/US economic compound. On a global scale, East Asia achieved an investment boom (37% investments per GDP), followed by South-East Asia and the Pacific region (33%), while Eastern Europe and the CIS stood at 22% savings and investments each (UNDP, 1996). Only Sub-Saharan Africa has a lower savings and investments rate than the EU and the USA. At the heart of the ‘euro-monetarist’ Maastricht prescriptions against the European ills now lies the assumption, that monetary policy will influence only prices, but not output and employment. The EMU-optimists hope that the single currency will be an ideal instrument for Europe to sustain in international economic competition. But a ‘hard’ EURO will be of a negative influence on trade-, and hence, on European current account balances with the rest of the world, since European exports will become more expensive and European imports will become cheaper internationally. Until now, devaluations were a proper economic policy instrument of the weaker European economies to balance their negative current accounts, as the example of Spain and Italy over the last years amply demonstrates. This instrument would now be absent; only migration, the wage rate, transfers and or unemployment would be the only options left for the European mezzogiorno under EMU (see above, and Boyer, 1996, Friedman, 1997). A sinister argument could even be, that the motives for the EMU project could be rather inner-European competition. A ‘hard’ EURO comprising the
European mezzogiorno, would ruin exporters in the South (that made important headway against the dominance of the German work bench in Europe over recent years) while cementing the position of German and a few other multinationals - banks and companies - on an increasingly protected European home market. Then, indeed, the European Union would become what Samir Amin has contemptuously called (although we do not agree with him here) - the democratic ‘Fourth Reich’ (Amin, 1997). Germany, far away from being Europe’s ‘growth locomotive’, is on its ‘best’ way to become an economy, typically characterized by double deficits: total debts of the public sector exploding since the 1970s (reaching DEMbn 2133.3); subventions standing at DEMbn 116.2; unemployment, for years cosmetically ‘polished up’ by excluding the German East from the country’s international statistics, now at 10.9% and reaching the highest levels since the end of the Weimar Republic.

on the other hand, the ‘euro-monetarist’ package against future inflation under EMU, that solely relies on 5 monetary criteria, overlooks the very plausible role of encompassing trade unions in combating inflation - an argument, originally also conceded by neo-liberal economic theory. Furthermore, the ‘euro-monetarist’ Maastricht strategy, as envisaged by around 1995-1997, would have brought about a monetary union between precisely those EU countries that already are in the upper ¼ or 1/3 of stability on the European continent - with uncertain implications for the unfortunate rest (Beirat, 1996). The election victory of the French left on June 1st 1997 is inseparable from the strains that the original ‘euro-monetarist’ interpretation of the Maastricht project brought about. The annual rate of inflation in EU-Europe is the minor problem: the real problem is massive European unemployment and the massive social disintegration of the European cities.

you cannot exclude an entire region from the project of European Monetary Union. The Kohl/Waigel strategy would have relied on the European North, and not on the South. The political backlash against Euro-monetarism, Frankfurt (Franfort?)-style, is only too well understandable, considering the high social costs that French society in particular would have had to bear. Dramatic words are being used by European politicians nowadays: the EURO should guarantee peace on the European continent et cetera. But: it creates the very conflicts between a ‘hard’ and a ‘soft’ European economic zone. But a ‘weak’ Euro’ would, most probably, also be no alternative: restructuring of ailing European enterprises will be postponed; with capital markets most probably reacting by pushing up interest rates (Neue Zuercher Zeitung, 16th of June, 1997: 9), thus prolonging the vicious downward cycle of the European political economy. The only real alternative would be to follow a socio-liberal flexible growth path.

currency speculations against the Italian Lira as the weakest part in the European currency chain are very likely in 1998 (Beirat, 1996). Why was Italy taken on board? The performance of austerity of the Italian economy over the last years was remarkable in capitalist terms, and unemployment has declined from the 1996/97 record of 12.1% to 11.9% (IFRI, 1998). But the arithmetic of the EU Council provides the real answer: the 10 countries which fulfilled two, three or four Maastricht criteria by 1996 (Belgium, Germany, Finland, Netherlands, France, Austria, Luxembourg, Denmark, Ireland, United Kingdom) would have had 55 votes on the EU council, while the ‘outs’ (Sweden and the European ‘mezzogiorno’) would have had enough votes (32) to block voting in the Council, so it was decided to take on board the ‘weaklings’ except Greece (Beirat, 1996; our own calculations from Weixner and Wimmer, 1997). This perspective could have also blocked the project of extending Europe eastward; but the price will now be a more vulnerable Euro. The calculation for the speculators is simple: take sufficient Lira credits in spring 1998, change them
into $ or Pounds, spread the rumors, that the Lira will be devaluated, and pay back calmly your credits with enormous profits, while the Lira goes down the river Tiber. Another plausibility, though, could be continued massive inflows of capital, including laundered one, into Europe during the first years of the EURO, to be followed by a crisis of the US $ in 1999/2000. The harshest times of the EURO would then come by around 2004 or 2005.

viii. All this will lead to a ‘deficit’ of democracy in the Union; in accordance with the liberal doctrine that the weakening of democracy is - inter alia - the result of the geographical distance between the locality, where decisions are taken, and the citizens, who are the subject of these decisions (Klaus, 1997)

ix. 1996, Portugal, Spain, Italy and Greece did not meet any of the first four criteria; Sweden missed three criteria; Germany and Austria two; and the rest of the Union at least one of the criteria (Weixner and Wimmer, 1997). Only Luxembourg met all the five Maastricht criteria (Weixner and Wimmer, 1997; Rothschild, 1997)

x. international financial speculation will prove to be a formidable factor in the line-up for the realization of the whole project. On ‘Black Friday’, July 30th 1993, the Bundesbank had to buy foreign currencies to the tune of $bn 30 DM under the old EMS (Weixner and Wimmer, 1997). Now, the political conflict lines in Europe would suggest: either a ‘weaker’ EURO against the Dollar and the Yen, which is good for the European export industries and the European South on the world markets; an option, probably supported by the new left wing governments around Europe; with the inevitable flight into real estate and the Dollar by the accumulated wealth in Germany (and, to a minor extent in the other countries) to the tune of over DMbn 4000 to DMbn 5000 as the immediate consequence; or Maastricht is realized at the cost of transforming the European East and South into a mirror-picture of the process of the integration of the New Laender into Germany after 1989. The vast size of accumulated savings in Germany, together with the savings of the European shadow economy, are an immense pool of potential speculative money, should the EURO project get into real trouble. Anything can happen: transfers into US $, real estate, Yen, Swiss Francs, Swedish Crones. Remember in this context, that - compared to these huge amounts of accumulated legal and illegal wealth - the German currency reserves are ‘only’ $bn 80.2: a sustained speculation against the Deutschmark on the international financial markets could trigger-off a panic reaction on the part of German wealth-holders, which could mean the end of the EMU project. Hardly observed is the fact, that German currency reserves amounted $bn 85.3 in 1996 and melted down to 80.2 in March 1997. Seen in such a way, parts of the political class that rules Germany knew well enough, why it insisted all along on a ‘hard EURO’ - to the detriment of European export industries. But you cannot expect banking capital to rule against banking capital. In a real battle over international finances, the European strategic currency reserves are small compared to the Asian reserves, brought about by the enormous accumulated current account balances over the years - even after the crash in 1997. In 1997, shortly before the crash, Taiwan alone had currency reserves to the tune of $bn 88.0; Japan 218.2; China 114.0; Hong Kong 69.6, Singapore 77.3; while Switzerland had 35.3; and the USA only 56.2, with the big European economies like France, Spain, the Netherlands and Italy holding reserves to the tune of around 25 to 60 billion $ each. Well-established German financial institutes already more and more propagate Dollar savings accounts - a clear sign how real the re-transfer of German savings into US $ already has become, only temporarily halted by the currency crisis in Asia. It is significant, that the European mezzogiorno states Spain (60.6) and Italy (45.4) have increased their foreign currency reserves by about $bn 30 last year, and together already have larger reserves than the Federal Republic of Germany
xi. Public opinion in the richer countries of the Union is mostly against the whole project, with rejection rates in 1996 already ranging from 46% in Austria to 64% in Denmark (Weixner and Wimmer, 1997)

xii. The erosion of the EMU-project finds its counterpart in the erosion of the state of public finances in the Federal Republic of Germany. The economic consequences of Mr. Theo Waigel are very clear to judge: he presided over the doubling of Germany’s public sector debt to $bn 1259 during his record tenure as Germany’s longest-serving finance minister. His ‘defiant alchemy’ in his bitter dispute with the Bundesbank over German gold reserves is but the last straw in a long chain of events (Financial Times, Weekend, May 31st, June 1st, 1997)

xiii. The shadow economy will partially have to come out from the darkness, most probably increasing the already existing capital flight into the Dollar, the Yen, the Stock Exchange, and into real estate. Indeed, considering the volatile character of international finances, a real avalanche could ensue, making the EMU-project impossible in the long run after a calm start

xiv. The Maastricht criteria will prove to be an instrument of anti-Keynesian global governance (Raffer, 1997). But the reception of neo-liberal economics by the EU-Commission and the Maastricht heads of governments was highly selective: while they seem to imply the importance of 5 monetary criteria, the Union overlooks day by day other neo-liberal prescriptions in important policy areas - from human capital policy over trade policy to agriculture

xv. If General Motors, AT & T, and individual households had been required to balance their budgets in the manner applied to the Federal Government (which in the US is under similar pressures as the governments in Europe), there would be no corporate bonds, no bank loans, and many fewer automobiles, telephones and houses (Vickrey, 1996). The Maastricht criteria are part and parcel of the 15 fatal fallacies of financial fundamentalism

xvi. A more useful arrangement than Maastricht would have been to achieve first a certain degree of European political cohesion in order to arrive at a more consensual democratic and better enforceable economic framework (Rothschild, 1997; Amin, 1997)

xvii. There are fundamental differences between the ‘freedoms’ for capital and labor - the first can be moved without having to learn a language and without leaving behind friends and a familiar environment - labor even when organized in a union cannot threaten to transfer as to another firm or country. The freedom of labor does not present a countervailing power to the bargaining power obtained by business through the complete liberalization of capital movements; on the contrary; that bargaining power is strengthened by the uninhibited possibility of attracting workers from low-wage EU countries (Rothschild, 1997). The basic policy approach of Maastricht and the Commission overlooks this important fact

xviii. Real outcomes in economic life, such as growth, employment, productivity, development, income distribution, do not figure at all in the so-called convergence criteria (Rothschild, 1997)

xix. Full employment is a good precondition against inflation

xx. The harmonization of social conditions in the Union by the Social Charta remains one of the most important tasks for an effective, real monetary union, because this would lay down the conditions for a convergence in the real welfare conditions of the countries concerned (Rothschild, 1997)

xxi. with the Maastricht criteria, Kalecki’s prediction, dated 1943, about a political business cycle with the entrepreneurs losing any real interest in full employment would come true (Rothschild, 1997; Raffer, 1997)
the institutionalized acceptance of neo-classical economics, inherent in the Maastricht criteria, is only one-sided. The Free Market optimism which had been developed on the assumptions of atomistic competition between powerless firms is transferred to a world of oligopolies and mammoth corporations (Rothschild, 1997).

The negative attitude to special protective treatment for the poorer regions and their development is the more astonishing in view of the fact that the Union is not opening its own economic frontiers world-wide (Rothschild, 1997).

The conflict between the ‘ins’ and the ‘outs’ would increase instead of decrease under a scenario of a strict implementation of the Maastricht criteria. Eastward extension of the Union would be more important than monetary union (Amin, 1997). Maastricht-style monetary union would, especially for the new members of the Union in the East, mean a two-class type of European integration.

Fallacy number three now consists in the assumption, that you can exclude the shadow economy and its accumulated savings from the EURO debate. A new currency will mean for the gangsters: open the money suitcases and try to exchange or place any bill that is not yet placed. But for many members of the huge and growing criminal underworld (there were 87 prisoners per 100000 population in the EU alone in 1993; i.e. a rise against the 77 per 100000 in 1987) the question of EMU is also a fundamental one: emerge with the cash? Place it somewhere? Exchange it for $ bills? To give an impression of the size of the criminal underworld, it might suffice here to state that in EU countries alone, there is a prison population of about 320000 people. Extending the Union eastwards and including the Czech Republic, the Slovak Republic, Hungary, Romania, Bulgaria and Poland, would mean adding to it another 153000 people to this entire army. Just to give an imagination about the size of the problem, it might suffice here to state that by comparison, the entire armed forces of the European Union are only 2068000 people (all data calculated from UNDP, 1997). The battle over the EMU-project now unfolds on the international financial markets. On paper, the USA face the same current account balance trends as Germany faced them - to be weighted at any rate by the role of the $ in international transactions. Until recently, ‘their’ American-Asian-Pacific economic space attracted - mainly via the Japanese bank - a large percentage of the surplus capital of the world, partly also, because both legal and illegal funds, in anticipation of the EURO, flowed to that region. Japan’s high official current account balance also pointed in a downward direction, but currency reserves go up - a clear indicator for the hypothesis, that both legal and illegal world surplus capital flows into Japan. Only experience will be able to tell us, how the recent currency crisis in East Asia is connected to major possible ‘tectonical shifts’ in international crime, international finance and surplus flows. It is entirely possible that a briefer strength period of the European currencies in the run-up to the EURO, will be followed months or years later, by a renewed Asian-oriented flow. Let us not underestimate especially the economic power of the Japanese Yakuza, the richest criminal organization in the world. The profit opportunities for the international speculators are enormous - 1997: rock the boat in Asia, jump in profits number one. Method: lending of local overvalued currencies, selling it into $ or European currencies. Pay back calmly your credits in local currencies, which are severely down. Now, 1998: perhaps rock the boat in Europe. Method: lending of Lira, selling it into $ or Asian currencies. Pay back calmly your Lira credits, which are worth nothing anymore. Now, 1999: rock the boat in America: Method: lending of $, selling it into Asian currencies. Pay back calmly your $ credits, which are worth nothing anymore as Asia recovers and the Arrighi cycle of financial transfers from the Atlantic to the Pacific nears its finish; America then stumbles, because of its current account.

On a world level, it is also absolutely unrealistic to overlook the power of international drug cartels and other criminal groups. 20 ‘narco states’ (soft on drugs, according to the US State
Department terminology, US State Department, 1996) had a considerable power over international reserves. The leading ‘drug countries’ with comparable data (see list at the end of the graph) control already $bn 324.137 currency reserves, while the 10 leading western industrial democracies and financial places (Japan, USA, Germany, France, United Kingdom, Italy, Spain, Austria, Switzerland, Sweden) still control $bn 739.707. After the three-fold rock the boat strategy around the globe is finished, the gangsters and speculators will have been able to shift then this relationship decisively, to perhaps $bn 500 to 500 or even worse. Already today, an alarming proportion of OECD country currency reserves at any rate also stem from the proceeds of money laundering, as the comparison between current account balances and international reserves suggests:

Graph 9.14: International reserves of 20 narco states and 10 leading western democracies

Legend: international reserves - bars, left-hand scale; current accounts - dotted line, right-hand scale in 1000 $. The currency reserves of the narco states are the following:

<table>
<thead>
<tr>
<th>Country</th>
<th>Reserves</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bolivia</td>
<td>793</td>
</tr>
<tr>
<td>Brazil</td>
<td>38492</td>
</tr>
<tr>
<td>Taiwan</td>
<td>97653</td>
</tr>
<tr>
<td>China</td>
<td>57781</td>
</tr>
<tr>
<td>Dom R</td>
<td>259</td>
</tr>
<tr>
<td>Ecuador</td>
<td>2003</td>
</tr>
<tr>
<td>Guatemala</td>
<td>943</td>
</tr>
<tr>
<td>India</td>
<td>24221</td>
</tr>
<tr>
<td>Colombia</td>
<td>7862</td>
</tr>
<tr>
<td>Lao PDR</td>
<td>68</td>
</tr>
<tr>
<td>Lebanon</td>
<td>4210</td>
</tr>
<tr>
<td>Country</td>
<td>Value</td>
</tr>
<tr>
<td>--------------</td>
<td>--------</td>
</tr>
<tr>
<td>Malaysia</td>
<td>26339</td>
</tr>
<tr>
<td>Mexico</td>
<td>6441</td>
</tr>
<tr>
<td>Myanmar</td>
<td>518</td>
</tr>
<tr>
<td>Nigeria</td>
<td>1649</td>
</tr>
<tr>
<td>Pakistan</td>
<td>3716</td>
</tr>
<tr>
<td>Paraguay</td>
<td>1030</td>
</tr>
<tr>
<td>Peru</td>
<td>7420</td>
</tr>
<tr>
<td>Thailand</td>
<td>30280</td>
</tr>
<tr>
<td>Venezuela</td>
<td>12459</td>
</tr>
<tr>
<td>20 narco states</td>
<td>324137</td>
</tr>
</tbody>
</table>

Definition: A narco state is understood here as a country, figuring on the list of statements of explanation by the US Department of State International Narcotics Control Strategy Report, 1996

Even the most powerful capitalist nations are - due to the mechanisms of international financial markets, practically at the mercy of the currency reserves accumulated in the 20 leading narco states of the South (international reserves):

Graph 9.15: The share of narco states in international reserves of the main world financial centers
Legend: the share of different groupings in world-wide currency reserve holdings, end-1997. Our own calculations from Fischer Weltalmanach and the international press.

In the direct comparison between Japan, the US and Germany, we also see the basic weakness of the *Deutschmark* against the main contenders:

Graph 9.16: currency reserves and current account balances since 1990 in the world system - Germany, Japan and the USA compared

Legend: current account balances: columns (right-hand scale); currency reserves: lines (left-hand scale)

Legend: data and projections on the current account balances of Germany, Japan, and the United States of America from 1990 onwards
Legend: currency reserves in the major capitalist centers from 1990 onwards

Legend: current account balances per GNP; and projections about their future development.
Sources: Data for the last Graph are IFRI (1998), the other data were from Fischer Weltalmanach and Economist:
Asia’s hour will still come, while Maastricht tries to achieve a stability that it can never achieve. One of the real reasons of financial instability on a global scale is to be found in the ever-larger share of drug money in international reserves and savings. $85 billion in drug profits are laundered through the financial markets each year, with an upward tendency. With total world savings at 22% of world GNP (25385 US$ billions), these profits are 1.5% of world savings. The volume of the drugs trade - at least $bn 500 - is 9% of world savings and approximately double the size of the largest single currency holdings of any country in the world system, Japan. The drug lords could ruin the international financial system.

Maastricht walks another path - that of financial austerity, to bring about financial stability. The present ‘working poverty’ US boom, on the other hand, will definitely come to a halt. World system theory argues here, that hegemonic capital leaves the hegemonic centers during eras of the de-legitimatization of the world system, after the period of world hegemony, lasting one Kondratieff cycle, came to an end (Chase-Dunn and Hall, 1997).

Another fallacy, fallacy four, of the Maastricht process is that it excludes the option of full employment. UNDP-data 1996 show that labor force participation rates and inflation rates in the highly developed countries had quite a negative correlation with each other which flattens off only at very high levels of employment, thus indicating certain limits of the ‘NAIRU’ debate (‘non-accelerating inflation rate of unemployment’) (Beirat, 1996). Maastricht policy brings about not only short-term, but also middle range and long-term unemployment; which - in the long run - is a very costly strategy, even increasing the very inflation process.

<table>
<thead>
<tr>
<th>Year</th>
<th>CR GER</th>
<th>CR USA</th>
<th>CR JAP</th>
<th>CUR AC GER</th>
<th>CUR AC USA</th>
<th>CUR AC JAP</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td>104547</td>
<td>173094</td>
<td>87828</td>
<td>46800</td>
<td>-92160</td>
<td>35870</td>
</tr>
<tr>
<td>1991</td>
<td>96657</td>
<td>159273</td>
<td>80626</td>
<td>-19497</td>
<td>-3690</td>
<td>72905</td>
</tr>
<tr>
<td>1992</td>
<td>122686</td>
<td>147526</td>
<td>79697</td>
<td>-25563</td>
<td>-66380</td>
<td>117640</td>
</tr>
<tr>
<td>1993</td>
<td>114822</td>
<td>164620</td>
<td>107989</td>
<td>-25563</td>
<td>-103925</td>
<td>131510</td>
</tr>
<tr>
<td>1994</td>
<td>113841</td>
<td>163591</td>
<td>135145</td>
<td>2327</td>
<td>-136484</td>
<td>133900</td>
</tr>
<tr>
<td>1995</td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>1996</td>
<td>85360</td>
<td>71200</td>
<td>202700</td>
<td>-18500</td>
<td>-165100</td>
<td>63400</td>
</tr>
<tr>
<td>1997</td>
<td>80200</td>
<td>56200</td>
<td>218200</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Graph 9.17: unemployment, labor force participation rate and inflation in developed capitalism

Since official unemployment statistics tell us only half the story about unemployment, the negative influence of labor force participation rates on inflation are telling indeed:

9.17 (continued)
<table>
<thead>
<tr>
<th></th>
<th>LFPR</th>
<th>inflation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Canada</td>
<td>53</td>
<td>1,4</td>
</tr>
<tr>
<td>USA</td>
<td>50</td>
<td>1,7</td>
</tr>
<tr>
<td>Japan</td>
<td>52</td>
<td>3,4</td>
</tr>
<tr>
<td>NL</td>
<td>46</td>
<td>1,7</td>
</tr>
<tr>
<td>NOR</td>
<td>50</td>
<td>2,2</td>
</tr>
<tr>
<td>SF</td>
<td>52</td>
<td>1,5</td>
</tr>
<tr>
<td>France</td>
<td>44</td>
<td>1,6</td>
</tr>
<tr>
<td>Iceland</td>
<td>56</td>
<td>1,2</td>
</tr>
<tr>
<td>Swed</td>
<td>54</td>
<td>1,3</td>
</tr>
<tr>
<td>Spain</td>
<td>41</td>
<td>2,7</td>
</tr>
<tr>
<td>Australia</td>
<td>50</td>
<td>1,6</td>
</tr>
<tr>
<td>Belgium</td>
<td>41</td>
<td>1,9</td>
</tr>
<tr>
<td>Austria</td>
<td>46</td>
<td>2</td>
</tr>
<tr>
<td>NZ</td>
<td>48</td>
<td>0,7</td>
</tr>
<tr>
<td>CH</td>
<td>53</td>
<td>1,1</td>
</tr>
<tr>
<td>UK</td>
<td>50</td>
<td>2,3</td>
</tr>
<tr>
<td>DK</td>
<td>57</td>
<td>2</td>
</tr>
<tr>
<td>GER</td>
<td>50</td>
<td>2,1</td>
</tr>
<tr>
<td>IRE</td>
<td>37</td>
<td>3,6</td>
</tr>
<tr>
<td>ITA</td>
<td>43</td>
<td>2,1</td>
</tr>
<tr>
<td>GRE</td>
<td>42</td>
<td>0,9</td>
</tr>
<tr>
<td>ISR</td>
<td>39</td>
<td>2</td>
</tr>
<tr>
<td>LUX</td>
<td>43</td>
<td>2,8</td>
</tr>
<tr>
<td>MAL</td>
<td>37</td>
<td>3,2</td>
</tr>
<tr>
<td>POR</td>
<td>49</td>
<td>3,3</td>
</tr>
</tbody>
</table>

**Fallacy five consists in overlooking what a ‘hard’ EURO will mean for the European exporter.** Like in the former GDR, it will mean an enormous upward push in the price of export goods on world markets. This analysis maintains all along, that factors, like the position in the world economy, are far more important variables than mere monetary aggregates. So why should Germany push so hard for a ‘hard EURO’? The hypothesis, that German corporations and banks, by a policy of a hard EURO, rather tend towards eliminating present and future unwelcome competitors from the closed European home market, instead of providing the European backbone in the trilateral competition between Asia, America, and Europe, finds further support by a look at the current account balances of the world’s leading industrial nations, in comparison with the EU, by around end 1996:
Legend: current account balances in OECD democracies. Sources: for this and the following graphs, we used *Fischer Weltalmanach* and *Economist* data

When proponents of the EURO in Germany (and Austria) maintained that it will mean a welcome future exclusion of competitive de-valuations, this argument overlooks the fact, that hundreds of countries can still competitively de-value, while the less than a dozen member countries of EMU cannot. Faced with an ever stiffer competitive pressure from the world markets, Germany and her northern European partners indeed seem to be inclined to a policy of monetarily regulating, if not dominating, the chances for export of the European continent. **Only a ‘hard’ EURO would prevent profoundly enough the unwelcome low-value-currency-driven competition from the European mezzogiorno countries, a competition, which is, *nota bene*, partly the result of the run-away of the very German (and other Northern European) productive capital abroad under present-day social and policy regulations.** A closer look at the trade-weighted exchange rates of major European and world currencies also shows to us that an upward pressure on the Deutschmark, should the EMU project fail, would not be maintainable in the long-run, a short and desperate attempt to create a mini-EMU after a possible failure of the large EMU project notwithstanding. A third path would be to ‘recycle’ German and other northern European savings into real transfers towards the Mediterranean EU countries, and later, the East. But it would be politically unthinkable in the long run and would create enormous pressures on the labor markets and for export industries. The story of exchange rates over 1996/97 is quite different from what politicians sometimes pretend. The strength of the Deutschmark is a myth:
Legend: trade-weighted exchange rates of major OECD currencies since 1990 (=100). Our own compilations from the Dialog-archive (http://www.dialogselect.com)

**Fallacy six consists in overlooking the real weakness of the D-Mark over recent months, and it also consists in overlooking that this trend will continue.** Short of direct speculation, the following swings could be tentatively interpreted, without maintaining any rigor from that first inspection of the empirical data:
Already, in more analytical terms, the following cross-national analyses from the ups and downs of the exchange rates are possible, using the data base of the ‘Economist’ newsmagazine (Economic Indicators, comprising GDP growth, unemployment, inflation, current account balance per GDP, growth rate of broad money supply (M2), interest rates (banks prime rate), foreign reserves) for 12 leading economies in the world over 1996/97. Available data series also show, that the obsession with inflation should give way to an obsession with economic growth. **The ups and downs of the exchange rate are determined primarily by economic growth (‘the basics’), and not by monetary aggregates.** Since I am not a monetary economist, such a heterodoxy does not bother me at all. Thus, we expect an underlying, basic strength of the US $ for 1997 and 1998, since America will have a stronger growth than Europe:
Table 9.12: The determinants of the 1996/97 exchange rate rise or fall

<table>
<thead>
<tr>
<th></th>
<th>dyn gdp</th>
<th>inflation</th>
<th>current acc</th>
<th>constant</th>
</tr>
</thead>
<tbody>
<tr>
<td>interest r</td>
<td>-0.194708194</td>
<td>0.198525086</td>
<td>0.651907557</td>
<td>-11.13735669</td>
</tr>
<tr>
<td>dyn m2</td>
<td>3.0906341351</td>
<td>1.853312658</td>
<td>1.037982666</td>
<td>0.555292814</td>
</tr>
<tr>
<td>inflation</td>
<td>0.571997567</td>
<td>3.32883147</td>
<td>10</td>
<td></td>
</tr>
<tr>
<td>dyn m2</td>
<td>-0.395138614</td>
<td>2.107761653</td>
<td>0.173988824</td>
<td>t-Test</td>
</tr>
<tr>
<td>dyn gdp</td>
<td>0.191259286</td>
<td>1.173988824</td>
<td>0.348103742</td>
<td>3.066290195</td>
</tr>
<tr>
<td>constant</td>
<td>-0.581775269</td>
<td>-0.436197965</td>
<td>0.43290356</td>
<td>-7.73318113</td>
</tr>
<tr>
<td>inflation</td>
<td>0.57734929</td>
<td>0.95437895</td>
<td>0.348103742</td>
<td>3.066290195</td>
</tr>
<tr>
<td>dyn m2</td>
<td>3.415049808</td>
<td>10</td>
<td></td>
<td></td>
</tr>
<tr>
<td>inflation</td>
<td>-1.397499812</td>
<td>2.075493246</td>
<td>0.457049021</td>
<td>t-Test</td>
</tr>
<tr>
<td>dyn gdp</td>
<td>0.457049021</td>
<td>1.243605017</td>
<td>1.243605017</td>
<td>t-Test</td>
</tr>
</tbody>
</table>

Legend: as in all EXCEL 5.0 outprints in this work, first row: unstandardized regression coefficients, second row: standard errors, last row: t-Test. The values immediately below the standard errors are $R^2$ (third row, left side entry), $F$, and degrees of freedom (fourth row).

The case for reflating Europe’s economies can even be stated in a provocative fashion:
Graph 9.21: growth, consumer price rises (1997 in %) and changes in the trade-weighted exchange rate, 1996/97

Legend: economic growth (x-axis) and growth of the value of the exchange rate (y-axis) in major OECD democracies. Our own compilations from *Economist* and Dialog archive.

Legend: inflation (x-axis) and exchange rate dynamism (y-axis); see above
Post-hoc predictions from an **anti-shock-strategy model** for the real observable data 1996-97 show, that the Graph above strikingly corresponds to realities:

<table>
<thead>
<tr>
<th>dyn exchange rate</th>
<th>trend dyn exchange rate 1997</th>
</tr>
</thead>
<tbody>
<tr>
<td>-0,5</td>
<td>-3,995184827 Australia</td>
</tr>
<tr>
<td>-2</td>
<td>-2,703252268 Austria</td>
</tr>
<tr>
<td>-3,8</td>
<td>-1,949520884 Belgium</td>
</tr>
<tr>
<td>13,2</td>
<td>6,666692706 Britain</td>
</tr>
<tr>
<td>0,5</td>
<td>-1,123946096 CND</td>
</tr>
<tr>
<td>-1,8</td>
<td>-1,123946096 DK</td>
</tr>
<tr>
<td>-3,5</td>
<td>-5,716929108 France</td>
</tr>
<tr>
<td>-4,4</td>
<td>-3,385140249 Germany</td>
</tr>
<tr>
<td>-0,2</td>
<td>-1,949520884 Italy</td>
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<td>-3,5</td>
<td>0,742733688 Japan</td>
</tr>
<tr>
<td>-4,5</td>
<td>-0,226527905 NL</td>
</tr>
<tr>
<td>-2,6</td>
<td>-1,123946096 Spain</td>
</tr>
<tr>
<td>-5,7</td>
<td>-4,524645115 Sweden</td>
</tr>
<tr>
<td>-5,6</td>
<td>-6,253881584 CH</td>
</tr>
<tr>
<td>5,8</td>
<td>8,067014719 USA</td>
</tr>
</tbody>
</table>

One consequence of this **empirical relationship between inflation and upward movements in the trade-weighted exchange rates** is a prediction of the behavior of the major currencies on the world markets in 1998. The prediction is based on the *Economist’s* prediction of inflation in Europe and in the major other economies of the world in 1998.

*Economist* predictions of inflation for 1998

<table>
<thead>
<tr>
<th>predicted inflation 98</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>2,9</td>
<td>Australia</td>
</tr>
<tr>
<td>2,3</td>
<td>Austria</td>
</tr>
<tr>
<td>2,1</td>
<td>Belgium</td>
</tr>
<tr>
<td>3,2</td>
<td>Britain</td>
</tr>
<tr>
<td>2,1</td>
<td>CND</td>
</tr>
<tr>
<td>2,7</td>
<td>DK</td>
</tr>
<tr>
<td>1,9</td>
<td>France</td>
</tr>
<tr>
<td>2,1</td>
<td>Germany</td>
</tr>
<tr>
<td>2,6</td>
<td>Italy</td>
</tr>
<tr>
<td>1,2</td>
<td>Japan</td>
</tr>
</tbody>
</table>
The consequence of this assumption then would be the prediction of the exchange rate dynamics for 1998:

<table>
<thead>
<tr>
<th>Country</th>
<th>Trend Dynamics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Australia</td>
<td>-3.896702</td>
</tr>
<tr>
<td>Austria</td>
<td>-2.60315</td>
</tr>
<tr>
<td>Belgium</td>
<td>-1.848608</td>
</tr>
<tr>
<td>Britain</td>
<td>6.774112</td>
</tr>
<tr>
<td>CND</td>
<td>-1.022222</td>
</tr>
<tr>
<td>DK</td>
<td>-1.022222</td>
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<tr>
<td>France</td>
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<tr>
<td>Germany</td>
<td>-3.285848</td>
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<tr>
<td>Italy</td>
<td>-1.848608</td>
</tr>
<tr>
<td>Japan</td>
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<td>Sweden</td>
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</tr>
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<td>CH</td>
<td>-6.161048</td>
</tr>
<tr>
<td>USA</td>
<td>8.17525</td>
</tr>
</tbody>
</table>

If you want to invest your money in Sterling or US $, do it. Do not go in for Swiss Franks, Deutschmark, Swedish crowns, or French Francs, or Lira:
Fallacy seven is equally important as the six previous ones. It consists in overlooking the effects of illegal money on Europe’s poorer East. A hard EURO would attract an enormous amount of illegal Eastern capital to Western Europe, while the crooks will not hesitate to change their partially existing D-Mark wealth into $ or other non-EURO currencies, should the need arise. Market imperfections and the peripheral position of Eastern Europe in the world economy cause a tendency towards a secular current account balance deficit in most of the new democracies (at least those with historical records of big landholding and a weak national state), that can practically only be closed by the shadow economy, including illegal migration and money laundering:
<table>
<thead>
<tr>
<th>Country</th>
<th>GDP</th>
<th>budget</th>
<th>unemployment</th>
<th>inflation</th>
<th>current acc</th>
<th>reserves</th>
<th>debt</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bulgaria</td>
<td>11.6</td>
<td>-1.2</td>
<td>16.3</td>
<td>1.9725</td>
<td>0</td>
<td>0.5</td>
<td>10.3</td>
</tr>
<tr>
<td>Croatia</td>
<td>18.8</td>
<td>-0.9</td>
<td>16.7</td>
<td>4.4</td>
<td>1.5</td>
<td>2.2</td>
<td>4.1</td>
</tr>
<tr>
<td>Czech R</td>
<td>52.7</td>
<td>0.5</td>
<td>3.9</td>
<td>6.7</td>
<td>4.5</td>
<td>12</td>
<td>18.1</td>
</tr>
<tr>
<td>Estonia</td>
<td>4.2</td>
<td>0.2</td>
<td>4.5</td>
<td>9.2</td>
<td>0.4</td>
<td>0.6</td>
<td>0.4</td>
</tr>
<tr>
<td>Hungary</td>
<td>44.4</td>
<td>-1.4</td>
<td>11</td>
<td>18.8</td>
<td>0.5</td>
<td>9.7</td>
<td>27.6</td>
</tr>
<tr>
<td>Latvia</td>
<td>5.4</td>
<td>0</td>
<td>7.5</td>
<td>6.8</td>
<td>0.3</td>
<td>0.7</td>
<td>0.4</td>
</tr>
<tr>
<td>Lithuania</td>
<td>7.7</td>
<td>-2.3</td>
<td>6.2</td>
<td>7.3</td>
<td>0.4</td>
<td>0.7</td>
<td>1.2</td>
</tr>
<tr>
<td>Poland</td>
<td>115.7</td>
<td>-0.9</td>
<td>13</td>
<td>15.3</td>
<td>1.1</td>
<td>21.1</td>
<td>40.7</td>
</tr>
<tr>
<td>Romania</td>
<td>35.5</td>
<td>0.1</td>
<td>7.2</td>
<td>176.8</td>
<td>0.2</td>
<td>1</td>
<td>6.9</td>
</tr>
<tr>
<td>Russia</td>
<td>450.7</td>
<td>-6.8</td>
<td>9.7</td>
<td>15.1</td>
<td>1.6</td>
<td>11.3</td>
<td>122.8</td>
</tr>
<tr>
<td>Slovakia</td>
<td>18.8</td>
<td>-0.5</td>
<td>13.4</td>
<td>6.5</td>
<td>0.2</td>
<td>1.5</td>
<td>7.8</td>
</tr>
<tr>
<td>Slovenia</td>
<td>18.4</td>
<td>0.4</td>
<td>14.5</td>
<td>8.2</td>
<td>0</td>
<td>2.4</td>
<td>4</td>
</tr>
</tbody>
</table>
GDP, current account, reserves and debt are given in $bn, budget is given as percent of GDP, unemployment and inflation are the usual percent rates. Our own compilations from *Economist, 1998, current issues*

Strict financial discipline indeed brings about less unemployment and not more, by international cross-national comparison. But rising unemployment pushes inflation up, and not down.

Graph 9.23: stability criteria and economic performance in the transformation countries

Legend: government budget balance (x-axis) and unemployment (y-axis). Data: *Economist, 1998*
Graph 9.24: unemployment and inflation - the evidence from Eastern Europe and the former USSR

Legend: unemployment (x-axis) and inflation (y-axis). Data: Business Central Europe, current issues

Thirdly, current account balances determine only to a certain extent international reserves, and indeed, excess reserves are a good signal for money-laundering processes taking place in the economy, but such excess reserves dampen inflation. The transformation economy, successor to peripheral socialism 1945 - 1989, Nazi occupation 1938/39 - 1945 and peripheral capitalism 1450 - 1939, is characterized, as Amin teaches us, by a secular current account balance deficit, that has to be closed by almost any means - including imports of ‘illegal savings’. Like all wealth-owning capitalist classes, the crooks of Eastern Europe become very interested in financial stability and the canon of ‘property rights’, once their illegal money is parked. The right-hand upper outlayers in our following graph - the Czech Republic, Hungary, Poland, Slovakia, all have nowadays a much higher proportion of foreign currency reserves to their GDP as one might expect from the current account balance. Only the first, rising parts of our curves - or the straight fitting line - correspond to economic wisdom, while much of the rest is due to the global casino of money laundering and capital flight:
Graph 9.25: reserves and current account balances in the world system

1) Eastern Europe

Legend: current account balance (in $ bn) (x-axis) and currency reserves (in $ bn) (y-axis).

Data: *Business Central Europe*, current issues

2) developed western democracies
Legend: see above; source: Fischer Weltalmanach and UNDP

3) developing countries
Eastern European inflation, to a great part, is also linked to the problem of illegal capital inflows that boost reserves in excess of the available current account balances, contributing to a dampening of the inflation process in the semi-periphery:

Graph 9.26: ‘excess reserves’ (money-laundering) and inflation

Legend: regression residuals from Graph 9.25 1), above (x-axis) and the inflation rate (y-axis). As to the data sources, see 9.25; plus EXCEL non-linear trend-line projections and residual value calculations. Put in simple terms: the more ‘unaccounted’ and ‘strange’ reserve currency inflows, the lower is the inflation rate.

Thus, one might say, that the stability of the East European exchange rates depends on these very same huge semi-legal and illegal reserves, that were accumulated by the opening of the twin Pandora’s boxes of open borders and liberalized world financial markets:

Table 9.14: stability conditions of Eastern currencies

<table>
<thead>
<tr>
<th>inflation</th>
<th>current acc</th>
<th>reserves</th>
<th>debt</th>
<th>growth</th>
<th>constant</th>
</tr>
</thead>
<tbody>
<tr>
<td>-177,34449</td>
<td>-36,68374</td>
<td>204,515725</td>
<td>15,3515777</td>
<td>0,35514332</td>
<td>-1558,1171</td>
</tr>
<tr>
<td>117,86279</td>
<td>41,2055865</td>
<td>104,321881</td>
<td>129,842067</td>
<td>1,40047248</td>
<td>850,153922</td>
</tr>
<tr>
<td>0,60849828</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Legend: as in all EXCEL 5.0 outprints in this work, first row: unstandardized regression coefficients, second row: standard errors, last row: t-Test. The values immediately below the standard errors are $R^2$ (third row, left side entry), $F$, and degrees of freedom (fourth row).

But dependency becomes decisive, when long-term growth perspectives of East and Central European economies are being determined. There are indeed ‘the balance of payments constraints’ on economic growth: **not only the stability of the Eastern currency, but also short-term Eastern economic growth becomes largely dependent on the import of ‘narco’ and other laundered money, that neatly shows up in the international reserves statistics** (see also Chapter 8 for the contradicting results on a more long-term basis at the level of the world system).

Table 9.15: the balance of payments constraint on economic growth in the transformation states

<table>
<thead>
<tr>
<th>budget</th>
<th>unemployment</th>
<th>inflation</th>
<th>current acc</th>
<th>reserves</th>
<th>constant</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.04146493</td>
<td>0.04189921</td>
<td>0.00122375</td>
<td>0.15937235</td>
<td>1.42604392</td>
<td>2.90491826</td>
</tr>
<tr>
<td>0.13145571</td>
<td>0.24323974</td>
<td>0.00246502</td>
<td>0.19867407</td>
<td>0.43335864</td>
<td>2.98086477</td>
</tr>
<tr>
<td><strong>0.86923249</strong></td>
<td><strong>2.40001513</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>7.97659149</td>
<td>6</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>229,728731</td>
<td>34,5604357</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>0.31542889</td>
<td>0.49644786</td>
<td>0.80217993</td>
<td><strong>3.29067843</strong></td>
<td>0.97452199</td>
<td></td>
</tr>
</tbody>
</table>

Legend: as in all EXCEL 5.0 outprints in this work, first row: unstandardized regression coefficients, second row: standard errors, last row: t-Test. The values immediately below
the standard errors are $R^2$ (third row, left side entry), $F$, and degrees of freedom (fourth row).

One plausibility is, of course, that the Central and East European economies, sandwiched by the process of negative current account balances and the march of the shadow-economy, will return to a process of arms manufacturing and arms exporting, which was one of the backbones of their economies in the 1980s and before. A time-series analysis of US ACDA data shows this hypothesis to be not without foundations:

Graph 9.27: towards a resumption of the arms exporting mechanisms in Eastern Europe? - The Polish case re-considered

Legend: total arms exports (in constant US $, 1987) and the share of arms exports per total exports (right-hand scale), as well as the polynomial function fitted by the EXCEL program to the data series (trend-line). The function leaves less than 2% of arms exports unaccounted for. Our own compilations from the US ACDA web-site.

**Fallacy eight is to overlook that in the long run, the stability of the capitalist system needs labor as an organized, countervailing power, that the very EURO process, as it is now underway, is about to put into question.** In the developed capitalist countries, the empirical relationships suggest a new, labor-oriented approach to stabilization policy. Our Aristotelean message of a middle course is: at least a medium-level unionization rate and earnings growth rate will be necessary to stabilize capitalism, while at the same time the empirical support for a shortening of the weekly working hours as a way out of the crisis is rather weak.
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