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## The Debtor State. Wolfgang Streeck, *Gekaufte Zeit: Die vertagte Krise des demokratischen Kapitalismus* (Berlin, Suhrkamp, 2013)

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TRYING TO CONVINCENCE people that we do not live in liberal democratic societies—that is, societies that have successfully reconciled free-market capitalism and democracy—resembles the challenge faced by the astronomers who first demonstrated that the earth rotated round the sun. First there are the taken-for-granted perceptions of everyday life: the sun rises and sets, so it must go round the earth; we have markets and we have elections, so we must have liberal democracy. Second, behind the everyday perceptions stand those who have powerful interests invested in perpetuation of the existing belief. Admittedly, the financial and other interests that benefit from the myth of liberal democracy do not threaten to torture and burn their critics, and allow them to occupy a small place in open debate; but otherwise the situations are similar.

The new view of the polity that is the contemporary social critic's equivalent to the heliocentric hypothesis is to see the modern state as being only partly responsible to its democracy and partly, through quite different channels, to global financial interests. The latter is not a partial aberration from a "normal" democratic situation, but a fundamental part of contemporary social reality. Further, in a kind of democratic theory equivalent to the law of entropy, the second aspect of states' responsibilities is growing at the expense of the former.

The task of providing the theoretical framework for this perspective has fallen to Wolfgang Streeck. In his latest book he argues that it is false to see contemporary governments as primarily responsible to the electorates that constitute democratic citizenship. Instead, they are responsible to two *Völker*, or sets of people: *Staatsvolk* (state people) and *Marktvolk* (market people). The former are nationally grounded, act as citizens with citizens' rights, are (periodically) voters, also express their concerns as public opinion, show loyalty and look to governments for some of the provisions of daily life. The latter are international, act as investors who make demands, operate (continuously) through auctions of public debt, also express their concerns through interest rate movements, show varying degrees of "confidence," and look to governments to

service debts owed to them. Streeck is here concentrating, not on the more familiar theme of the political power of corporate lobbies, but on the deeper transformation of state responsibilities produced by the rise of the debtor state; more specifically, by the transition from the taxation state (*Steuerstaat*) to the debtor state (*Schuldenstaat*). The taxation state has a primary relationship to its citizens, from whom it requires consent to levy taxation. (Indeed, this model predates democracy.) The debtor state, while maintaining this link, acquires a second one, which also serves, like taxation, as a major source of funds: the global financial markets from which it borrows money. As can readily be seen from the above list of their characteristics, the investors in the debtor state are more powerful than citizens: they are beyond reach of the state's control; they operate all the time and not just at elections; when they affect interest rates by their granting or withdrawal of confidence, they mobilize a far more potent expression of demands than the mechanisms available to citizens for expressing opinion.

One needs to raise one doubt at this point: what of states who do not have major debts? At present the lowest levels of public debt in the industrial world are found in several Central and Eastern European countries and in Scandinavia, with levels of less than 50 % of GDP, compared with over 80 % in France, Germany and the UK, and over 100 % in Greece, Italy and the USA. The importance of the debtor state within a polity should be proportionate to the size of public debt. If so, then the taxation or citizenship state should have retained most strength in the CEE countries and Scandinavia. That might be plausible for the latter, but is political citizenship really at its strongest in parts of Central and Eastern Europe, where the very lowest levels of debt are to be found? Governments in these countries are highly dependent on the favour of international capital holders, but in different ways: their dependence is primarily in terms of foreign investment. Where countries are attracting such investment on the basis of low costs (low wages, low social costs, low taxation), the autonomy of their governments can be at least as weak, and the pressure on them to follow a neoliberal path at least as strong, as when dependence takes the form of debt. Streeck's thesis therefore requires some extension to take account of this and perhaps other forms of dependence on global capital, with possibly varying implications for the relationship to citizenship.

Different again would be cases where countries do not attract much foreign capital, either to fund debt or low-value-added investment, but with what local capital they have find their place in low value-added

global markets. The downward pressures on workers' living standards and public social and material infrastructure are here at least as strong as in the other cases, but are exercised through mass product markets rather than through the more openly political demands of creditors and investors. Again, there is no fundamental criticism of Streeck's model here, just an indication of how it can be extended to construct a complete theory of the relationship between democratic and market constraints on states.

To construct the theory of the debtor state is probably enough for one book, as its historical development needs to be described. Streeck does this in an insightful and instructive way, which in itself lays bare important instabilities in modern capitalism. A capitalist economy has a permanent problem of reconciling different interests, in particular between those who work and those who invest. The economic system that emerged in the advanced economies after the Second World War, broadly if slightly inaccurately known as Keynesian, embodied certain compromises between these interests, focused on the welfare state and the pursuit of full employment. But for various reasons the relationship became unstable, particularly around distributional conflicts. To an important extent these were reconciled by the dramatic economic growth of the post-war years: if there is dispute over sharing the cake, make a bigger cake; then everyone gets more, whatever happens to respective shares. But what if, as occurred by the 1970s, the cake was ceasing to grow fast enough to contain distributional conflict? The first answer was to make false cake: to make the economy look bigger, even though it was not really so. This was the case of inflation.

But by the end of the 1970s inflation had become an unsatisfactory solution, partly because it eroded the value of investments. Regimes of tight money control were instituted. These had several negative implications for the post-war compromise of capitalist democracy, not least the end of governments' commitment to ensuring full employment. They did not resolve distributional conflicts, in particular, and wealthy interests were increasingly reluctant to pay enough in taxes to fund the demands made on public spending. The consequence was a large growth in public debt. In itself, state debt is not problematic, as it can be used as debt is used by businesses, to finance investments that will eventually be profitable and enable repayment of the debt itself. But this is not what was happening. State debt was being used to fund current spending programmes, with governments apparently giving up any prospect that they would be able to cover these by taxation. Public debt was performing the same

task that inflation had earlier done: providing false cake. In consequence governments now became dependent on the willingness of wealth holders to accept their debt, which raised the question of what needed to be done to win creditor “confidence.” In turn this led to the transfer of political power from citizens to creditors as in Streeck’s central thesis.

This was however not the end of the development of the means for reconciling distributional conflict. As states came under pressure to reduce their own debts, so new mechanisms became available to extend the debts of citizens themselves. Bankers in the deregulated global finance system found many ways of making large sums of money by taking on unsecured debts, in particular from people on medium and low incomes who stood little chance of paying their debts back, and trading these in the secondary markets that were developing extremely rapidly, spreading risk in a manner that seemed at the time to be self-stabilizing. As with state debt, household debt is not problematic in itself, provided it is used in ways that eventually generate earnings more than large enough to pay it back. But, again as with state debt, this is not what was happening. Particularly in the USA, families were remortgaging their homes or taking on large credit-card debt in order to fund current spending. It was, once again, the creation of false cake.

At each stage in this three-fold process, capitalism and the contemporary state were buying time—the “bought time” (*gekaufte Zeit*) of Streeck’s title—postponing the deepening gap that was emerging between the requirements of the owners of capital and those of the mass of citizens, the growing mutual incompatibility of capitalism and democracy. Streeck believes that the end of the line is now being reached, and that the compromise can no longer continue on its present terms. He argues, in effect—though these are not his own words—that for too long there have been attempts to fit democracy to the needs of capitalism, and that the opposite process now needs to be attempted, fitting capitalism to democracy. Streeck does not see much scope for optimism here, but there are straws in the wind that one could see as consistent with such a potential shift in direction. First, the OECD (2013)<sup>1</sup> and even the International Monetary Fund have started to express concern that the rise in inequality has begun to

<sup>1</sup> OECD, *Inequality and Poverty in the United States: Public Policies for Growth* (Paris, OECD, 2013).

threaten growth itself, especially in the USA. Second, advocates of the social investment welfare state (Hemerijck 2012<sup>2</sup>; Palier *et al.* 2012<sup>3</sup>) argue that a successful high-value-added capitalist economy depends on a strong social infrastructure.

But are global capitalist interests willing to accept such a reshaping of a social compromise? If we take, as does Streeck, the handling of the Eurocrisis as a major landmark, it is difficult to retain that potential optimism. Streeck presents the Eurocrisis as a major step in what we might see as the final de-democratizing shift from the taxation state to the debtor state. He describes how the participants in this process had a number of priorities: that the financial markets must be spared from sharing the burdens, which must be borne by states and their citizens; that indebted banks should not be nationalized, but helped by the state; that debtor states must not use bankruptcy to resolve their problems; and that if state debts were to be devalued, creditors must be largely protected from the consequences. He points to the difference between this approach to state debt crises and that towards corporate debt embodied in the widely praised US approach to bankruptcy laws, whereby deeply indebted firms are able to seek legal protection from their creditors, who eventually have to share in the losses. His arguments here are consistent with those of Massimo Amato and Luca Fantacci (2009, 2012)<sup>4</sup>, who contend that the modern system of capitalist finance (dating in their view at least back to the 18<sup>th</sup> century) has lost sight of the mutual relationship between creditor and debtor, in which both share responsibility for the fate of a loan. Reaching its apogee in the secondary and derivatives markets of today's deregulated system, the contemporary concept of this relationship has become one in which the creditor loses all direct responsibility for what happens to its loans, thereby ceasing to have any obligation to inform itself about the debtor's projects. In the case of firms that go bankrupt, creditors still stand to lose from this process. In the case of both loans to states and across-the-board crises of private finance, however, they seem now to have established the principle that they need to be protected from all but a minor share in the consequences. The importance of banks to the financial system is so great, they have successfully argued, that governments (and

<sup>2</sup> HEMERIJCK, A., *Changing Welfare States* (Oxford, Oxford University Press, 2012).

<sup>3</sup> MOREL N., B. PALIER and J. PALME, *Towards a Social Investment Welfare State?* (Bristol, Policy Press).

<sup>4</sup> AMATO M. and L. FANTACCI, *Fine della Finanza. Da dove viene la crisi e come si può pensare di uscirne* (Rome, Donzelli, 2009). AMATO M. and L. FANTACCI, *Come salvare il mercato dal capitalismo: Idee per un'altra finanza* (Rome, Donzelli, 2012).

therefore tax payers) have to indemnify them against their potential losses. The financial system has thus become a curious kind of collective good, where profits are privately appropriable but losses a public burden. Also, an alarming gap is opened in the market's own arrangements for monitoring debt and its use.

Streeck sees the European single currency and the institutions around it as the logical development of a European project that he sees as being primarily moulded on the free-market ideas of Friedrich Hayek, who already in 1939 had envisaged an international federation of states that would be based on free markets with minimal possibilities for democratic responsibility.<sup>5</sup> (Hayek was always more sceptical than many of his followers that democracy and capitalism were easy bed-fellows.) Streeck's approach to the European Union is therefore sharply critical. He sees the transfer of powers to it from nation states as part of the process of de-democratization, shifting competences from a democratically responsible level to one where the primary mandate is the creation of markets and the intensification of competition. Further, he advocates replacement of the single currency by a European "Bretton Woods," where separate currencies retain their ability to devalue within the constraints of an international agreement. The system would follow Keynes's original model of a special bank currency against which national currencies would be exchangeable, rather than the elevation of one national currency (the US dollar) as was the eventual Bretton Woods solution.

I have some doubts about this particular part of his argument, and think that Streeck may have exaggerated what could have been achieved by the Southern European countries if they had stayed out of the common currency and used devaluation as a means of managing their economic inadequacies. Their fundamental problem had been that, until the 1990s, large parts of their economies had depended on being the lowest-cost producers within the then Western EU, especially in light industries like clothing and textiles. When wages rose, as workers tried to lose their low-wage status, devaluation was used to keep overall costs and export prices low. To some extent this maintained workers' living standards, though only to the extent that they did not purchase imported products, or that domestic prices were not affected by international markets. Two developments during the 1990s threatened this pattern. First, the collapse of the Soviet bloc

<sup>5</sup> HAYEK F.A., (1939) "The Economic Conditions of Interstate Federalism", in *Economic Order* (Chicago, University of Chicago Press: 255-272).  
HAYEK, F.A. (1980) *Individualism and Eco-*

meant that the economies of Central and Eastern Europe entered the European economy, manufacturing goods in several sectors at lower cost than most southern European producers. Second, the Multifibre Agreement, which since 1974 had restricted imports of clothing and textiles from developing countries, protecting European and North American firms from very low-cost competition, was gradually phased out until it disappeared in 2004. There was no way that Southern European producers could have maintained their low-cost production path with occasional minor devaluations while their workers enjoyed improving or even just stable real incomes. These economies faced a serious challenge of up-grading their production so that they were not trapped in competition with very low-cost producers. The problem was widely perceived and understood by politicians, enterprises and unions at the time, and in some regions and industries of Italy and Spain action was taken, with some success. At the macro-level, elites saw entry into the European currency as a constraint that would force them out of the down-market, devaluation-dependent path, reinforcing incentives to up-grade their activities across the board and not just in a few industries. But in the event little was done to achieve this, at least in part because of the form taken by the governance of the single currency.

The criticism that should then be made of the European financial regime is not that it ruled out the devaluation path, but that it allowed governments to evade the constraints to which they had committed themselves. First, the rules of the single currency itself, based as Streeck argues on neoliberal principles, had regard to only a small number of monetary aggregates and did not monitor governments' general financial and fiscal behaviour. Second, banks, sovereign wealth funds and others in the deregulated global financial system, which had embarked on its irresponsible risk-sharing in secondary markets, were willing to lend money to these (and other) governments without regard to the growing size of their debts (just as they were doing with household debt). As a result, governments and firms lost their potential incentive to move up-market, and economies made inadequate adjustment to the changed competitive environment. When the financial system crashed, they were left highly exposed, not having modernized their economies and unable to pay their debts. Remaining outside the Eurozone would not therefore have helped these economies. However, the rest of Streeck's arguments remains valid: the design of the single currency was flawed and inadequate, because it was based on neoliberal principles; deregulated global finance did play



a major role in destabilizing these economies; and now the neoliberal conditions imposed on them as part of the European Central Bank “rescue” programme only make matters worse by doing the very opposite of enabling them to upgrade their infrastructure and productive capacity.

These reservations about the role of the single currency in Southern Europe’s crisis apart, Streeck has here provided an excellent and challenging account of the current state of relations between capitalism and democracy. My summary above does not do justice to its detail. For example, he provides an excellent critique of conservative arguments common during the inflationary crises of the 1970s, that society was threatening to become “ungovernable”; and, indeed, of critical theory’s equivalent contention that capitalism was threatened with a legitimation crisis (Habermas 1973).<sup>6</sup> Rather, he argues, working people were busily adapting themselves to the exigencies of the capitalist economy as, for example, many women joined the paid labour force. It was not the population that was defecting from the post-war compromise, but capitalist interests, that were becoming global, rejecting the Keynesian settlement, and increasingly making the political demands that now seem to be leading us from an uneasy balance between the taxation state and the debtor state to the latter alone. It was capital, not labour, that rejected the distribution of income produced by the post-war compromise. Streeck makes the telling point that if (as is often claimed) it was the unreasonable and unruly demands of the populace that lay behind the inflationary crises, the fiscal crises and the debt crises, how is it possible that the same period has seen a major rise in inequality, and massive transfers in the share of national wealth in most advanced countries from labour to capital?

Various normative and political conclusions can be drawn from Streeck’s account, as the above discussion has shown. But for academics the most immediate challenge is analytical: how do we describe the kind of political system towards which we are moving, if “liberal democracy” has become naïve and Panglossian? I have tried using “post-democracy” (Crouch 2004)<sup>7</sup>, but that is only negative. Streeck’s concept of a state whose democratic responsibilities to voters are required systematically to be shared with and often trumped by those to creditors takes us a major step forward.

COLIN CROUCH

<sup>6</sup> HABERMAS J., *Legitimationsprobleme im Spätkapitalismus* (Frankfurt/M: Suhrkamp, 1973).

<sup>7</sup> CROUCH C., *Post-Democracy* (Cambridge, Polity Press, 2004).