

Why Europe Is Singing a Dirge Over Cyprus

By [Harold James](#)

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Europe can choose its own musical accompaniment to its latest crisis. In Berlin, American rapper 50 Cent's "All Things Fall Apart" has just had its premiere, so that soundtrack might be appropriate. Or the continent can reach back to Giuseppe Verdi, born 200 years ago, whose penultimate, and probably greatest, operatic achievement starts on the coast of Cyprus with a storm of fantastic violence and the opening words of its hero, Otello: "Esultate, rejoice! The war has been won; but Otello's achievement is later destroyed by his jealousy."

Today, Cyprus appears to have been rescued. But the rescue has fueled a growing rift that jeopardizes the future of European integration, partly owing to the way that the upheaval of the early 20th century — especially the Great Depression — has been re-enacted in the debates about the post-2008 financial meltdown and the subsequent euro crisis.

The interwar economic slump became intractable because it was also a crisis of social stability, democracy and the international political order. Widespread bankruptcy and unemployment increased social tension, ultimately making normal democratic politics

impossible. In Germany, the epicenter of democracy's collapse, radicals on both the right and the left raged against the postwar peace settlement and the Versailles Treaty.

In the last years of the increasingly unstable Weimar Republic, as democracy was fraying, German governments started to use their opponents' radicalism in an effort to extract security concessions from the Western powers. Domestic political pressure became a source of heightened international tension.

That is true in today's Europe as well. Democracy has become a central target of complaints by the European elite. Luxembourg's prime minister, Jean-Claude Juncker, a former chairman of the Euro group, has lamented that European leaders know what the right policies are but do not know how to be re-elected after implementing them. Similarly, after his recent crushing election defeat, Italian Prime Minister Mario Monti wistfully explained that Italy's voters were too impatient to bear reforms whose benefits would only become evident beyond the electoral cycle.

Events in Cyprus have exposed two other dimensions to the clashes over Europe's dual sovereign-debt and banking crisis. First, the discussion of a levy on bank deposits and whether small customers should be exempted put class conflict front and center. Second, the question of foreign, and especially Russian, depositors has turned the rescue of the Cypriot banking sector into an international relations problem.

The initial proposal to impose a one-time tax on accounts holding less than 100,000 euros (\$128,000) came not from the European Union or from Germany but from the Cypriot government, which must have known that it was likely to generate outrage. They also should have known that the Cypriot parliament would never vote for it. Perhaps the Cypriot government believed that mass protests, with placards denouncing the EU as a fig leaf for revived German domination of Europe, would strengthen its hand. After all, even moderate Cypriots were outraged by the bullying of their small island by Germany and by the EU.

The other side in the negotiations also played class politics. At one of the tensest moments, as Cyprus was seeking an alternative rescue package from Russia, the German Bundesbank announced the results of a new European Central Bank study indicating that average German wealth was lower than in the southern European states, largely because fewer Germans own their own houses. The message seemed clearly intended to influence the negotiations: Why should poorer Germans be expected to sacrifice to support Mediterranean millionaires?

In the aftermath of the financial crisis, income and wealth distribution have moved to the center of political debate. Even the Catholic Church seems to reflect the new mood. The election of Jorge Mario Bergoglio as Pope Francis is a clear reference to St. Francis of Assisi and the church's mission to stand up for the poor.

On the international relations front, after 2010, as deposits from Europe left Cypriot banks, deposits from Russian businesses and individuals increased, and Russia has many reasons to use money as a way of buying political control. Cyprus is a crucial staging post for U.S. security operations in the eastern Mediterranean, and the gas fields off the Cypriot coast might be developed as an energy source that would, at least after 2017, reduce European dependence on Russian supplies.

In an earlier phase of the crisis, Russia gave Cyprus a \$3 billion credit. But now, a new credit would serve only to make the burden of government debt unsustainable. A purchase of all or some of the problematic Cypriot banks is needed. In the aftermath of a crisis, that has been intensified by the rhetoric of class conflict, Russia might be able to extend its control more significantly and at a lower price.

Deepening social polarization, its use in financial negotiations and the intrusion of a new security element provide further evidence of what most economists and commentators on Europe have long argued: A monetary union is impossible to sustain in the absence of a political union. A state, especially in the modern form of the European welfare state, depends on effective mechanisms for arbitrating and resolving social disputes. These are mechanisms that the EU lacks, as the turmoil surrounding Cyprus has clearly shown.

As long as that remains true, European integration may be doomed by the time the music stops.

Harold James, professor of history and international affairs at Princeton University, is author of "Making the European Monetary Union." © Project Syndicate

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