De-financialisation for a socially responsible financial sector

Malcolm Sawyer

University of Leeds, UK and FESSUD

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Structure of presentation

- Financialisation: some remarks
- The economic impacts of financialisation
- Some modest proposals for re-structuring financial sector
- Can it be done?

Financialisation

- ‘financialization means the increasing role of financial motives, financial markets, financial actors and financial institutions in the operation of the domestic and international economies’ (Epstein, 2005).

Financialisation

- Financialisation in the Epstein sense has been long occurring. Verchelli, for example, identifies first era of financialisation (1860s to 1929) and a second era (since circa 1980).
- Also avoid discussion of how sharp a change financialisation since 1980 has been as compared with the 1950 to 1980 period.
- Focus on that period since 1980

Financialisation

- Financialisation has gone alongside globalisation, neo-liberalism, rising inequality – and avoid discussion over the relationship of financialisation with those changes.
- Financialisation (since 1980) as a world-wide phenomenon with variations between countries in terms of timing, speed and its nature.

Features of financialisation

- 'First, it refers to the large –scale expansion and proliferation of financial markets over the past thirty years. ..
- Second, the process has been closely interwoven with de-regulation of the financial system itself and the economy more generally….
- Third, financialisation, understood as both the expansion and the proliferation of financial instruments and services, has been associated with the birth of a whole range of financial institutions and markets, and corresponding acronyms, ….
- Fourth, at a systemic level, financialisation has been located in terms of the dominance of finance over industry. …

Features of financialisation

- Fifth, financialisation is strongly associated with market mechanisms, complemented or even reinforced by policies that have underpinned rising inequality of incomes and of inequality more generally….
- Sixth, though, consumption has often been sustained by the extension of credit, not least through the use of capital gains in housing as collateral….
- Seventh, it is not merely the expansion and proliferation of financial instruments and markets that are striking but also the penetration of such financing into a widening range of both economic and social reproduction – housing, pensions, health, and so on. …
- Finally, financialisation is associated with a particular culture which is to be interpreted broadly. ..

t have been the effects of financialisation?

- The term ‘financialisation’ is of relatively recent origins (perhaps early 1990s) but the growth and power of the financial system has long been analysed.
- In the mainstream often under headings such as financial development, financial liberalisation (and end of financial repression)

What have been the effects of financialisation?

- The financial development and liberalisation literature generally took a favourable view of the growth of the financial system:
- ‘Theory illuminates many of the channels through which the emergence of financial instruments, markets and institutions affect –and are affected by—economic development. A growing body of empirical analyses, including firm-level studies, industry-level studies, individual country-studies, time-series studies, panel-investigations, and broad cross-country comparisons, demonstrate a strong positive link between the functioning of the financial system and long-run economic growth.

What have been the effects of financialisation?

- While subject to ample qualifications and countervailing views noted throughout this article, the preponderance of evidence suggests that both financial intermediaries and markets matter for growth even when controlling for potential simultaneity bias. Furthermore, microeconomic-based evidence is consistent with the view that better developed financial systems ease external financing constraints facing firms, which illuminates one mechanism through which financial development influences economic growth. Theory and empirical evidence make it difficult to conclude that the financial system merely—and automatically—responds to economic activity, or that financial development is an inconsequential addendum to the process of economic growth.' (Levine, 2005, p. 921)

What have been the effects of financialisation?

- Students of financialisation have taken a much broader perspective on the effects of the growth of the financial sector (as indicated by the features listed above), and a less optimistic one.

- The financial development– economic growth nexus – has it changed?
- Bank of International Settlements studied ‘the complex real effects of financial development and come to two important conclusions. First, financial sector size has an inverted U-shaped effect on productivity growth. That is, there comes a point where further enlargement of the financial system can reduce real growth. Second, financial sector growth is found to be a drag on productivity growth.

Financial development

- Our interpretation is that because the financial sector competes with the rest of the economy for scarce resources, financial booms are not, in general, growth enhancing. This evidence, together with recent *experience* during the financial crisis, leads us to conclude that there is a pressing need to reassess the relationship of finance and real growth in modern economic systems. More finance is definitely not always better' (Cecchetti and Kharroubi, 2012, p.14).

Impacts of Financialisation

- There are many other areas where financialisation may have effects, generally adverse (recognizing the difficulties of separating out the impact of financialisation)
- Financialisation and inequality
- Financialisation, pursuit of ‘stakeholder value’ and investment and innovation

Financial liberalisation

- 'Whereas some have claimed that liberalisation of financial markets contributes to the efficiency with which these markets can transform saving into investment,…, others have pointed out that these liberalisations have contributed to various financial and economic crises in the past. … The evidence that emerges from these studies [of the relationship] remains inconclusive.' (Bumann, Hermes, and Lensink (2012), p.41)
- Based on meta-regression analysis 'our results indicate that, on average, there is a positive effect of financial liberalisation on growth, the significance of this effect is only weak. … Our analysis suggests that data from the 1970s generate more negative financial liberalisation coefficients'.

De-financialisation

- The essential argument here is that the growth of the financial sector has not brought any faster growth, it has been associated with rising inequality and with increased incidence of financial crisis.
- The key roles of the financial sector should be the provision of a payments system and the socially efficient allocation of funds. It is the growth of the financial sector away from these key roles which lie behind many financial crises.

Taxes

- The role of financial transactions taxes; financial activity taxes etc.
- The clear purpose of such taxes should be the reduction in the volume of transactions, and the release of resources which are engaged in those transactions.

Developing financial institutions

- Alternative models of banking – the benefits of diversity
- Mutual, regional organisations
- Micro-credit and micro-finance

- State development banks including ‘green’ investments

Guided lending

- Guided lending: setting targets for the direction of lending by banks cf. US Community Reinvestment Act

Is de-financialisation feasible?

- Financialisation includes the growing power of the financial sector – to argue for de-financialisation faces formidable political obstacles!

Is de-financialisation feasible?

- Is financialisation is the current stage of capitalism with its own momentum which cannot be reversed?