STUDIEN

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INEQUALITY AND FINANCIALISATION: THE CASE OF THE EU

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INTRODUCTION

After the collapse of the Bretton Woods system and the elimination of the system of fixed exchange rates, global finance made new inroads into the world economy, while the deregulation of financial services marked the beginning of the era of financialisation. Inequality in the distribution of income and wealth feeds the process of financialisation and is fed by it. It is a two-way relationship, which has favoured the meteoric rise of the economic, social, and political power of finance in the past thirty years. This rise has been marked by financial crises of varying intensity in different localities. The financial crisis which erupted in late 2007, however, has been both deeper and more widespread across the developed financial systems of the world than in the past, aggravating the distributional inequalities that are inherent in the process of financialisation.

In the EU, the era of financialisation is associated with the introduction of the Single Market in the mid-1980s and of the single currency in the 1990s, as well as the pursuit of financial integration from the late 1990s onwards at the expense of financial stability and consumer protection. As in other parts of the advanced capitalist world, the 2007/2008 financial crisis was succeeded by an economic crisis in the EU as well. Five years later, it is still unfolding. Certain areas are converging towards low growth, while others are deep in recession. The distributional implications of these trends are especially important. In this paper, we shall discuss the connections between inequality and financialisation in the EU. In this respect, the following areas of enquiry are pertinent:

- Re-visiting distribution and tracing the theoretical approaches and debates that have marked this area of economic thought from the classics to the present;
- Exploring the theoretical, as well as institutional/historical roots of finance and finance–led capitalism;
- Examining the articulation between finance and distribution

The above questions will be discussed in the context of the EU, as a special area of interest in view of its historical trajectory, its size, and presence in the global system, as well as of the developments currently taking place. The study is divided into three parts, as follows:

- Part I deals with the theoretical aspects of income distribution and of money and finance.
  - Section 1 is taken up by a discussion of the theoretical considerations of the distribution of income;
  - Section 2 looks into the notion and development of financialisation and its connection to distribution.
- Part II looks into the case of the EU financial services sector and the way this is tied to economic and social developments.
  - Section 3 discusses EU financial policy and structures;
  - Section 4 examines in some detail the EU response to the financial crisis and financial policy reform.
- Part III discusses the pattern and extent of inequality in the EU in relation to finance.
  - Section 5 reviews trends in the functional distribution of income in the EU;
  - Section 6 looks into the personal distribution of income and wealth, taking into account the implications of the crisis and of austerity.

The last section of the study draws together the strands of our analysis, summarises, and concludes.

PART I – THEORETICAL CONSIDERATIONS

1 THE DISTRIBUTION OF INCOME FROM CLASSICAL ECONOMICS TO THE CONTEMPORARY MAINSTREAM

1.1 From classical to neoclassical economics

The notion of labour as the essence of value was present in the classics. For example, Adam Smith, in his *Wealth of Nations,* notes that 'In that early and rude state of society which precedes both the accumulation of stock and the appropriation of land, the proportion between the quantities of labour necessary for acquiring different objects, seems to be the only circumstance which can afford any rule for exchanging them for one another. … In this state of things, the whole produce of labour belongs to the labourer; and the quantity of labour commonly employed in acquiring or producing any commodity, is the only circumstance which can regulate the quantity of labour which it ought commonly to purchase, command or exchange for'.[1]

David Ricardo was even more explicit, directly linking the question of value to the distribution of income and thereby defining economics as a field of enquiry: 'The produce of the earth – all that is derived from its surface by the united application of labour, machinery, and capital – is divided among three classes of the community; namely, the proprietor of the land, the owner of the stock or capital necessary for its cultivation and the labourers by whose industry it is cultivated. But in different stages of society, the proportions of the whole produce of the earth which will be allotted to each of these classes, under the names of rent, profit and wages, will be essentially different; depending mainly on the actual fertility of the soil, on the accumulation of capital and population, and on the skill, ingenuity and instruments employed in agriculture. To determine the laws which regulate this distribution, is the principal problem in Political Economy'.[2]

The notion that value is a relationship between people was further taken up by Karl Marx who stipulated that common to all things is the 'human labour power expended in their production (and) embodied in them … When looked at as crystals of this social substance, common to them all, they [these things] are Values'.[3] Accepting that all things exchange at prices proportional to their values, Marx applied it to labour power, which is essential to understanding capitalist accumulation. In other words, the worker receives his value, his cost in terms of labour-time, and the employer makes use of him to produce more value than the worker costs, which the employer appropriates. Thus, Marx, a student of Ricardo, provided a fundamental answer to the question posed by the latter.

Considering the labour-unit as a measure of value posed the moral question as to the role of capital. Was labour alone to have the credit for creating value? Does this imply that profits are an imposition on the workers? As Joan Robinson has succinctly pointed out, 'from the orthodox camp the labour theory, with its disagreeable smell, was swept out and utility came in', whereby 'utility is a metaphysical concept of impregnable circularity; utility is the quality in commodities that makes individuals want to buy them and the fact that individuals want to buy commodities shows that they have utility'.[4]

Under conditions of laissez-faire, or perfect competition, consumers are thus guided in their decisions by the marginal utility offered by consuming one more unit of a good, while producers are guided in theirs by the marginal cost of producing an extra unit of production.[5] The utility of goods consumed by workers is no different from any other, while what matters is the freedom of choice, according to the neoclassical school.

With utility came mathematics and elegant diagrams, while static equilibrium afforded a stable basis for economic analysis and peace of mind to the neoclassics, even though the assumptions on which such a model rests are completely unrelated to the real world.

Connected to this conception is the justification of inequality on the grounds that only the rich save, so that inequality is necessary for capital accumulation. In other words, the total to be shared is increased through inequality to such an appreciable extent that even the smallest share becomes larger than it otherwise could have become. Therefore, the redistribution of income is not expected to raise anyone's income in any considerable way. In Joan Robinson's words, 'This is an ideology to end ideologies, for it has abolished the moral problem. It is only necessary for each individual to act egoistically for the good of all to be attained.'[6] In fact, this was the political platform of the neoclassics and of laissez-faire.

1.2 Keynes and Kalecki

The orthodoxy of side-stepping the distributional aspects of the socio-economic system was challenged by the crash of 1929. John Kenneth Galbraith, in his classic study, *The Great Crash 1929,* considers income distribution as one of the five 'weaknesses' leading up to the disaster: 'In 1929 the rich were indubitably rich … five per cent of the population with the highest incomes received approximately one-third of all personal income. The proportion of income received in the form of interest, dividends and rent … was about twice as great as in the years following World War II. This highly unequal income distribution meant that the economy was dependent on a high level of investment

1 Adam Smith, *Wealth of Nations* (Everyman's Library edition) Vol. I, pp. 41–42. **2** *Works of David Ricardo,* ed. P. Sraffa, Vol. I, 'Preface to the Principles', The Online Library of Liberty, p. 55. **3** Karl Marx, *Capital,* Vol. I, pp. 3–5. **4** Joan Robinson, 1974, *Economic Philosophy* (first published in 1962), Penguin Books, England, p. 48. **5** The concept of utility is associated with the work of Jevons, Walras, Wicksell, Pigou and Marshall, amongst others. **6** Ibid, p. 53.

or a high level of luxury consumer spending or both … Both investment and luxury spending are subject inevitably to more erratic influences and to wider fluctuations than the bread and rent outlays of the $ 25/week workman' (Galbraith, 1992: 194–195).[7]

As the Great Depression of the 1930s followed the Great Crash, orthodoxy was successfully challenged by John Maynard Keynes, whose strategy was to demonstrate that orthodox theory was merely a 'special' case of a more general theory. Keynes' concern was with the high unemployment and economic stagnation of the time. In attempting to explain it and to propose policies to overcome it, he broadened his outlook to include many areas neglected by mainstream economics until that time. Distribution was one of these areas.

Keynes was not against moderate income differentials. However, he believed that great income differentials were undesirable and harmful. In Keynes' own words, 'The outstanding faults of the economic society in which we live are its failure to provide for full employment and its arbitrary and inequitable distribution of wealth and incomes. The bearing of the foregoing theory on the first of these is obvious. But there are also two important respects in which it is relevant to the second' (Keynes, 1936: 372).[8] More specifically, as Hyman Minsky has pointed out, the *General Theory*'s relevance to questions of income distribution is due to its 'refutation of the argument that income inequality is necessary to promote savings and to its pointing toward a regime in which, as a result of an epoch of full employment accumulation, the scarcity of capital would be much reduced' (Minsky, 2008: 148).[9]

Keynes himself was optimistic that in a regime of continuous full employment, investment would lead to 'the euthanasia of the rentier and, consequently, the euthanasia of the cumulative oppressive power of the capitalist to exploit the scarcity value of capital' (Keynes, 1936: 376). One of his contemporaries, the Polish economist Michal Kalecki, disagreed.

During the period that Keynes was working out his ideas, Kalecki independently arrived at similar conclusions, albeit through a different route. Given his Marxian background, Kalecki's writings emphasise the class distinction between workers and capitalists and the accommodating role that workers play. Thus, his theory of the determination of national income is based on the distribution of income and the spending propensities of capitalists vis-à-vis workers in a world where firms have some degree of monopoly power.

While Kalecki thought that demand expansion is not only a necessary condition for growth, but also a sufficient condition, he remained pessimistic as to its attainment. The reason for his pessimism was what he called the 'political business cycle', which links economic developments to the condition of political forces. More specifically, he foresaw that a state of permanently high employment would alter the power equilibrium within society and improve the bargaining power of workers. 'In this situation a powerful block is likely to be formed between big business and rentier interests and they would probably find more than one economist to declare that the situation was manifestly unsound. The pressure of all these forces and in particular of big business – as a rule influential in Government departments – would most probably induce the Government to return to the orthodox policy of cutting down the budget deficit" (Kalecki, 1943: 330).[10]

Keynes reshaped the prevalent economic thought of his day so much so that a 'Keynesian revolution' was believed to have taken place.[11] However, more than 75 years after the publication of the *General Theory,* it is Kalecki who seems to have been vindicated by events on the economic, social, and political level.

1.3 Present-day mainstream economics

As economic policy moved away from the goal of full employment since the 1970s, the old neoclassical orthodoxy re-emerged in economic theory and policy formulation. This is what we may call the 'present-day mainstream view', i. e., the view that prevails in economics as a field of enquiry and which is taught in most universities around the world. This view is influential in terms of policy, and it is in turn influenced by the outlook of policy makers.

According to the current mainstream view, distribution is locked out of the 'positivist-scientific' body of economic knowledge, that is, it is not taken into account in trying to understand 'what is, was or will be', so as to offer 'interpretations [of] any disagreements [which] are appropriately settled by an appeal to the facts' (Lipsey, 1970: 4).[12] By contrast, distribution is seen to belong to the sphere of 'normative' economics, whereby 'different individuals have different ideas of what is good or bad and thus of what constitutes the good life. It follows that disagreements over distribution cannot be settled merely by an appeal to the facts' (ibid: 5). The secondary status of distribution as a 'soft' area of academic enquiry in an otherwise 'hard' science is thus well established.

On the other hand, in view of the multi-faceted character of distribution, different aspects of it are to be found in different parts of mainstream economics. In particular, the functional distribution of income between capital and labour is discussed in relation to factor pricing, while consumption is discussed in relation to consumer choice. In these micro level discussions, the economic implications of the distribution of income and wealth per se for the workings of the economy as a whole are carefully avoided.

More specifically, factor pricing is explained in terms of the marginal productivity of a factor of production

7 J. K. Galbraith, 1992, *The Great Crash 1929,* Penguin Books, England. **8** John Maynard Keynes, 1936, *The General Theory of Employment, Interest and Money,* reprinted as Vol. 7 of The Collected Writigs of J. M. Keynes, N. Y. Harcourt. **9** Hyman P. Minsky, 2008, *John Maynard Keynes,* McGraw Hill, USA (first edition published in 1975). **10** Michal Kalecki, 1943, 'Political Aspects of Full Employment', *The Political Quarterly,* Vol. 14, Issue 4, pp. 322–331. **11** See for example Chapter 4 in Joan Robinson's treatise on *Economic Philosophy*. **12** R. G. Lipsey., 1970, *An Introduction to Positive Economics,* 2nd Edition, Weidenfeld and Nicolson, London.

and of the demand conditions for the commodity to be produced (derived demand), on the demand side. On the supply side, it is asserted that factors will move between occupations in search of the highest rewards. The combination of the demand and supply of factors of production constitute the so-called 'traditional theory of distribution' (ibid: 483).

The distributional aspects of production and consumption are further implicitly referred to in the discussion of consumer choice, which is linked to the income and price elasticity of demand, but not to the distribution of income and thus of consumption per se.

Distribution in its own right comes into mainstream economics under 'welfare economics', as one part of the dilemma or trade-off between equity and efficiency. The very juxtaposition of the two concepts is indicative of the treatment of distribution, whereby

'… we can transport money from rich to poor only in a leaky bucket … Given (i) a social preference for equality (or at least for more equality than market-determined incomes provide), and (ii) a cost of altering the market-determined distribution, society faces a trade-off between equality and efficiency. The resulting optimum will normally be a compromise' (Okun, 1983: ?).[13] In fact, Okun's 'leaky bucket' is characteristic of a discussion that compares equality with the abstract notion of Pareto efficiency, whereby 'An allocation is Pareto-efficient for a given set of consumer tastes, resources and technology, if it is impossible to move to another allocation which would make some people better off and nobody worse off' (Begg et al, 1991: 259).[14]

This view of efficiency is based on the notion or belief, if not faith, that the market mechanism is the best arbiter of the allocation of resources. Anything that intervenes in the workings of the market is a distortion. Hence, statements such as the following are quite common: 'Redistribution of income is costly. In order to redistribute income, taxes must be levied to take resources from some people so that they can be given to others' (Fischer et al., 1988: 397).[15]

Overall, mainstream economics has marginalised the issue of distribution and its significance for the economy by way of fragmenting and compartmentalising its discussion across different areas of the field. Thus, the distribution of income between capital and labour is linked to marginal productivity and to relative prices, while the role of labour institutions is discussed separately. Similarly, the distribution of consumption is buried away in the theory of consumer choice, while the distribution of income and wealth is put into relationship with an abstract notion of efficiency and found wanting! The practical effect of the mainstream treatment of distribution is that this lags seriously behind other areas of theoretical and empirical enquiry in economics as a discipline. As a result, several generations of economists are not conversant with the economics and politics of distribution. This hinders their ability to grasp the implications of rising inequality, as has become clear through the newly found interest in the underlying causes of the current financial and economic crisis.

2 INEQUALITY AND FINANCIALISATION – CONCEPTS AND LINKAGES

2.1 Money and Finance

Defining money proved as difficult for the classics as defining a measure of value. Ricardo's pondering over this matter is characteristic: 'The only qualities necessary to make a measure of value a perfect one are, that it should itself have value, and that that value should itself be invariable, in the same manner as in a perfect measure of length the measure should have length and that length should be neither liable to be increased nor diminished: or in a measure of weight that it should have weight and that such weight should be constant. Although it is thus easy to say what a perfect measure of value should be, it is not equally easy to find any one commodity that has the qualities required' (Ricardo, p. 55).

Marx solved the riddle by pointing out that money is a social convention and that labour is the ultimate measure of value. Marx also noted the multiple uses of money and in particular the fact that it is a store of value as well as a means of payment. The neoclassics understood money as a 'veil', neatly separating the economy into a monetary and a real sector. It was Knut Wicksell who challenged the 'helicopter drop of cash' implicit in the Quantity Theory of Money, arguing that the original increase in the supply of money is endogenous, created by the relative conditions of the financial and the productive sectors. In particular, banks provide credit by creating deposits upon which borrowers can draw. Since deposits constitute part of real money balances, banks 'create' money. Insofar as money thus created leads to an increase in aggregate demand, it is not a 'veil' – agents do react to it and this is not due to some irrational 'money illusion'.[16]

The tendency for financial capital to dominate industrial capital was further elaborated by Rudolf Hilferding, who discussed the notion of 'finance capital' in his 1910 publication of the same name.[17] This was seen as a certain form of capitalist organisation, in which banks are the central organising mode of industrial production, which is subject to ever increasing cartelisation. In particular, 'the dependence of industry on the banks is a consequence of property relationships. An ever-increasing part of the capital of industry does not belong to the industrialists who use it. They are able to dispose over capital only through the banks, which represent the owners. On the other side, the banks have to invest

13 Arthur M. Okun, 1983, *'Further Thoughts on Equality and Efficiency'* in Joseph A. Pechman (ed), *Economics for Policy Making, Selected Essays of Arthur M. Okun,* MIT Press, Cambridge. **14** David Begg, Stanley Fischer, and Rudiger Dornbusch, 1991, *Economics,* 3rd Edition, McGraw-Hill Book Co., England. **15** Stanley Fischer, Rudiger Dornbusch, and Richard Schmalensee, 1988, *Economics,* 2nd Edition, McGraw-Hill International Editions, Economics Series, Singapore. **16** Knut Wicksell, 1962, *Interest and Prices,* Library of Congress (originally published 1898).

an ever-increasing part of their capital in industry and in this way they become to a greater and greater extent industrial capitalists. I call bank capital, that is, capital in money form which is actually transformed in this way into industrial capital, "finance capital"' (Hilferding, 1981: chapter 14). Hilferding's notion of the links between finance and industry underpins the implications of the power relations between different factions of capital. Wicksell's argument, on the other hand, points to the dominant role of banks in creating money over and above the needs of industry, a point of special interest in relation to distribution, as well as financialisation.

The endogeneity of money was also accepted by Keynes, who emphasised the multiple uses of money in relation to 'liquidity preference' – i. e., the precautionary and speculative motives for demanding liquidity. By viewing (liquid) financial markets as an explicit part of the economic system and the role of money (as a store of value) in the workings of the economy, Keynes linked employment and distribution to finance, a connection which was ignored even at the height of the Keynesian epoch.[18]

Keynes' notion that money is connected with financing through time formed the basis for Hyman Minsky's 'Financial Instability Hypothesis', which describes a 'capitalist economy which does not rely upon exogenous shocks to generate business cycles of varying severity. The hypothesis holds that business cycles of history are compounded out of (i) the internal dynamics of capitalist economies, and (ii) the system of interventions and regulations that are designed to keep the economy operating within reasonable bounds' (Minsky, 1992: 9).[19]

In contrast to the above-cited views, which span the better part of a century of economics, the present-day mainstream view continues to regard money as an exogenous variable. Furthermore, the role of the financial sector in the economy is seen separately from the dynamics of the prevailing accumulation regime. The fact that financial markets are assumed to be 'efficient' makes the mainstream view even more detached from reality and therefore dangerous, the Efficient Market Hypothesis being the antipode of the Financial Instability Hypothesis.

More specifically, according to the Efficient Market Hypothesis, the (fictional) representative agent's risk attitude is not affected by boom and bust, his expectations are exogenous and homogeneous while the market is characterised by both perfect information and liquidity, and, of course, there is no connection between the financial sector and the rest of the economy. Clearly, this is an idealised world, based on elegant but unrealistic concepts and models, as was amply demonstrated by the 2007/2008 financial crisis.

2.2 Neoliberalism and financialisation

Outrageous as the assumptions of the present-day mainstream view are – based mostly on neoclassical foundations – they have served neoliberalism well, i. e., the accumulation regime which appeared in the late 1970s and has since become the dominant economic, social, and political paradigm. Following the collapse of the Bretton Woods system of fixed exchange rates and the two oil crises of the 1970s, there has indeed been a paradigm shift from an interventionist Keynesian-type policy regime to a pro-capital, liberal one, in which the goal of full employment was abandoned, tax rates for the wealthy were reduced, the social provisioning role of the state was shrunken, the financial system was deregulated, and capital was freed from national control. This was a political, as much as an economic, shift in the relations between capital and labour. Wages stagnated in relation to productivity, while the power of trade unions was eroded. Income distribution worsened, as the pay of the new 'superstars', the CEOs, sky-rocketed.[20]

Over time, the new paradigm produced two trends: (a) the accumulation of assets by a small number of individuals, mainly in the Western countries, which pushed them into taking increasingly riskier positions in the financial sphere, in their search for consistently high yields, and (b) the accumulation of debt by households trying to make up for the loss in their income and for the curtailment of public services. These tendencies were further reinforced by the low-interest-rate policies of the major central banks (especially the ECB and the Federal Reserve), aimed at sustaining demand.

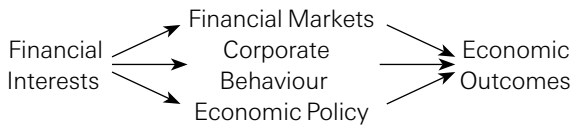
These trends were in effect complementary, since financial engineering produced high risk/yield financial products, while access to credit was made easier even for those who could not afford it. Further, during this time the use of information technology – including computers, communications equipment, scientific and engineering instruments, software and related services, etc. – has provided the type of productive technology necessary for the fast expansion of the financial services sector on a global level. In particular, Dellheim (2013) argues that microelectronic technologies, initially invented for military purposes, provided the 'technical foundations of the financial world' (Dellheim, 2013).[21]

In fact, by the late 1990s, finance capital had overtaken industrial capital, as the main driver of the economy, thus going beyond Hilferding's prediction regarding the growing power of finance! This is the era known as 'financial neoliberalism' or 'financialisation'.

17 Rudolf Hilferding, *Finance Capital. A Study of the Latest Phase of Capitalist Development* (1910), ed. Tom Bottomore, Routledge and Kegan Paul, London, 1981. **18** As Minsky has remarked, 'Keynes' lesson that policy can establish an equitable distribution of income has not only been ignored, it has also been "turned on its head" by the rich and powerful' (Minsky, 2008: 158). **19** Hyman Minsky, 1992, *The Financial Instability Hypothesis,* The Jerome Levy Economics Institute of Bard College, May 1992. **20** The expression 'superstars' has been used by Thomas I. Palley, 2007, in *Financialisation: What It Is and Why It Matters,* The Jerome Levy Economics Institute of Bard College, WP no. 525, N. Y., December 2007. **21** Judith Dellheim, 2013, 'Working on strategies against financialisation and capital oligarchies', Rosa Luxemburg Foundation, November http://kapacc.blog.rosalux.de/2013/10/26/judith-dellheim-working-on-strategies-against-financialization-and-capital-oligarchies/.

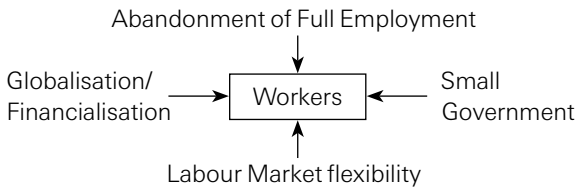
Gerald Epstein (2001) has given us a succinct definition of the term: 'Financialisation refers to the increasing importance of financial markets, financial motives, financial institutions and financial elites in the operation of the economy and its governing institutions, both at the national and international level'.[22] Richard Peet (2011) has an even more vivid description: 'Over the last thirty years, capital has abstracted upwards, from production to finance; its sphere of operations has expanded outwards, to every nook and cranny of the globe; the speed of its movement has increased to milliseconds; and its control has extended to include "everything". We now live in the era of global finance capitalism'.[23] It is David Harvey who first used the term 'the financialisation of everything' with regard to the spreading and deepening control of the economy by finance.[24]

Figure 1: Conduits of Financialisation



Source – Palley, 2007: 15

Figure 2: The Neoliberal Box



Source – Palley, 2007: 22

Thomas Palley (2007) has depicted the conduits or channels through which financialisation is transmitted to the rest of the economy and the neoliberal context (or 'box') within which it takes place, graphically, as shown in the figures above.[25] Thus, financialisation is linked to the end of the era associated with the pursuit of full employment and the unfolding of the era of financial deregulation, privatisation and market – including labour market – liberalisation. Further, as finance has strengthened its position, financial rentiers have pervaded the workings of the economy, and of policy formulation, in much the same way as the 'captains of industry' are assumed to influence Kalecki's 'political business cycle'. The higher rate of unemployment, which became common during this period by comparison to the post-WWII period, and the declining share of wages in total production, together with a host of other factors, such as the hiding of wealth in off-shore centres, the de-unionisation of workers, the weakening of the welfare state, etc., have made for an increasing rate of inequality in the distribution of income and wealth, aggravating the tendency inherent in capitalism towards long-term stagnation.[26] At the same time, the ease of access to credit, made possible by financial deregulation and engineering, as well as central bank policy, has allowed households, corporations, even countries to fund their consumption through increased borrowing, thus adding to the fragility of a ballooning financial sector.

Overall, neoliberalism and especially finance-led capitalism have dominated the global economy and society since the late 20th century. The dynamics they spearheaded turned finance from an enabling factor into an agent of destruction. The financial crisis of 2007/2008 was part of this destruction, while the ensuing economic crisis is indicative of the structural, underlying causes of finance-led capitalism.

2.3 Insights from the current crisis

Neither distribution, nor the role of money and finance are discussed outright, much less connected to each other, by the prevailing school of thought in academia, or by policy makers. This is not a practical omission or theoretical short-sightedness. Rather, it is the result of the current economic, social and political balance of forces, favouring the interests of the dominant fraction of capital. Finance and those associated with it – such as investment bankers, upper-level bureaucrats and mainstream economists – are the components of this fraction.

On the other hand, increasing income and wealth inequality in combination with the length and depth of the current crisis have stimulated growing academic and political interest in distributional issues and their relationship to financialisation. Most of this literature is to be found in the sphere of 'heterodox' economics, which encompasses various schools of thought, going beyond the 'universal truths' sustained by the faithful.[27] Not surprisingly, 'heretics' such as Keynes, Minsky, even Marx, are being revisited. Here are some of the questions raised in the past few years:

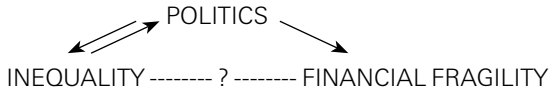
In June 2012, Joseph Stiglitz published his 'Price of Inequality' as a counterargument to both Democratic neoliberalism and Republican laissez-faire theories in the USA.[28] Stiglitz is a prominent member of an intellectual insurgency within the mainstream challenging the dominant economic orthodoxy. His argument is not only that inequality violates moral values, but that

22 Gerald A. Epstein, 2001, *Financialisation, Rentier Interests and Central Bank Policy,* Department of Economics, University of Massachusetts, Amhurst, MA, December. **23** Richard Peet, 2011, 'Contradictions of Finance Capitalism', *Monthly Review,* Vol. 63, Issue 7, December. **24** Quoted by Peet, 2011. **25** Thomas Palley, 2007, *Financialisation: What it is and Why It Matters,* The Jerome Levy Economics Institute of Bard College, WP no. 525, N. Y., December 2007. **26** Joan Robinson, writing in the early 1960s makes the following observation: '… it is remarkable that when Beveridge was writing *Full Employment in a Free Society* in consultation with a number of young Keynesians, an *average* of unemployment of three per cent seemed quite a daring objective to propose. The idea that for more than twelve years we should not touch that figure, indeed that two per cent should come to be considered dangerously high, would at that time have seemed extravagant wishful thinking' (Robinson, 1974: 88; first published in 1962). **27** To be fair, organisations such as the OECD, even the European Commission, are paying renewed attention to distributional issues, albeit mainly through the lens of welfare economics, i. e., in isolation from the workings of the economy as a whole. **28** Joseph Stiglitz, 2012, *The Price of Inequality,* W. W. Norton & Company.

it also interacts with a money-driven political system to grant excessive power to the most affluent, who enjoy favourable tax treatment, a government-protected market share, and other forms of 'rent seeking'. Furthermore, he argued that inequality undermines productivity and retards growth, whereas a more egalitarian society would result in a more stable economy. Thus, while Stiglitz does not doubt the usefulness of the market mechanism per se, he points to the need for government regulation and oversight for it to remain functional, singling out inequality as a central area for government intervention.

Stiglitz draws on the under-consumption strand of Keynes' thinking in proposing the increasing of demand by redistributing income from the high-saving rich to the low-saving poor. Paul Krugman is sceptical on this score, arguing that while inequality and macroeconomic vulnerability may have a *common causation* – e. g. neoliberal ideology – this does not necessarily amount to *actual causation,* as shown in the diagram below.[29]

Figure 3:



More particularly, Krugman holds that 'debt exploded because the Great Depression was receding into the mists of forgetfulness and both lenders and borrowers, enabled and encouraged by financial deregulation, forgot the dangers of leverage' (Krugman, 2013). To a certain extent, Krugman's view resonates with that of Galbraith, who has noted that '.. a speculative outbreak has a greater or less immunizing effect. … With time and the dimming of memory, the immunity wears off. A recurrence becomes possible' (in Galbraith, 1992: 188–189 – first published in 1954).

However, the two views of the origins of the crisis, under-consumption or collective forgetfulness leading to fresh speculative outbreaks, are not necessarily mutually exclusive; they can be reconciled through the combination of growing inequality, on the one hand, and deepening financialisation, on the other. That is, as the rich get richer, they undertake greater risks on the financial markets, while as the poor get poorer (or the middle classes face a declining standard of living), they turn to credit to supplement their income. As discussed above, the two tendencies reinforce each other in the direction of financial fragility.

Under-consumption has also been taken up by another school of thought – generally known as Post-Keynesian – in connecting inequality to finance and to the current crisis.[30] For example, Stockhammer (2010) believes that income polarisation, which had financial expansion as one of its key building blocks, was a fundamental cause of the recent financial crisis, while the flaws in the financial system constitute immediate causes.[31] Furthermore, Stockhammer et al. (2008) have found that the Eurozone is a 'wage-led' demand regime, insofar as a long-term policy of wage moderation dampens demand in the area as a whole, even if it improves the rate of competitiveness of particular Member States vis-à-vis the rest.[32] Onaran et al. (2011), investigating the relationship between financialisation, income distribution, and aggregate demand in the US, came to approximately similar conclusions.[33] More specifically, they found that the macro economy is 'wage-led', such that income is redistributed in favour of profit and at the expense of wages, suppressing consumption and negatively affecting growth and distribution.

These findings were corroborated by a further study by Onaran and Galanis (2012), carried out on behalf of the International Labour Office, which looked into the effects of a declining share of wages in GDP in both the developed and developing world during the neoliberal era of the post-1980s.[34] They concluded that (a) domestic private demand (i. e., the sum of consumption and investment) is wage-led in all countries; (b) foreign trade forms only a small part of aggregate demand in large countries, so that the positive effects of a decline in the wage share on net exports do not suffice to offset the negative effects on domestic demand; and (c) even if there are some countries which are profit-led, the planet earth as a whole is wage-led. Their main policy recommendation is the need for a recovery led by domestic demand and an increase in the wage share in the global economy as well as in individual countries.

It is, however, not only academics that are revisiting the theoretical and empirical aspects of the relationship between distribution and finance. In fact, social movements have been mobilising against the 'dictatorship of the financial markets' since the late 1990s, contributing to debates organised on the local, regional and global levels[35]. Following the financial crisis which revealed both the excesses of finance and the extreme inequality trends in all countries, the link between inequality and finance is being directly addressed by such movements and organisations. For example, Positive Money, which describes itself as 'a movement to democratize money and banking so that it works for society and not against it', has produced a report dealing with 'Banking, Finance and Income Inequality'.[36] Similarly, OXFAM International, a leading char-

29 Paul Krugman, 2010, 'Inequality and Crises: Coincidence or Causality?' – Keynote lecture, LIS Conference on Inequality, Luxembourg. **30** This school of thought is influenced not only by the work of Keynes, but also of Michal Kalecki, Joan Robinson, Nicholas Kandor, Paul Davidson, and others. **31** Engelbert Stockhammer, 2010, 'Neoliberalism, Income Distribution and the Causes of the Crisis, Research on Money and Finance', DP no. 19, June. **32** Engelbert Stockhammer, Özlem Onaran, and Stefan Ederer, 2008, 'Functional Income Distribution and Aggregate Demand in the Euro Area', *Cambridge Journal of Economics* 2009, 33, 139–159. **33** Özlem Onaran, Engelbert Stockhammer, and Lukas Grafl, 2011, 'Financialisation, Income Distribution and Aggregate Demand in the USA', *Cambridge Journal of Economics* 2011, 35, 637–661. **34** Özlem Onaran and Giorgos Galanis, 2012, ÐIs Aggregate Demand Wage-led or Profit-led? National and Global Effects', *Conditions of Work and Employment Series* No. 40 , International Labour Office. **35** For example, in the various World and European Social Fora of that period. **36** Graham Hodgson, 2013, 'Banking, Finance and Income Inequality', *Positive Money,* October http://www.positivemoney.org/publications/banking-finance-and-income-inequality/.

ity organisation, has produced a report, which points to the 'unprecedented bailout of Europe's financial institutions', on the one hand, and the 'short-sighted, regressive taxes and deep spending cuts, particularly to public services, such as education, health and social security [which] have dismantled the mechanisms that reduce inequality and enable equitable growth', on the other (Oxfam, 2013: 3).[37]

Overall, inequality and more generally the question of income and wealth distribution are coming out of the shadows of economic theory. The financial crisis of 2007–2008 and the ensuing economic crisis are forcing the 'hidden agenda' out into the open. The mainstream view is being challenged by new ideas and research into areas that were considered unimportant until recently. Furthermore, social movements and organisations are becoming aware of the deeper structural flaws of capitalism, which include inequality and financialisation, as well as the interaction between them.

37 OXFAM International, 'A cautionary tale – The true cost of austerity and inequality in Europe', *Briefing Paper,* September 2013 http://www.oxfam.org/en/policy/cautionary-tale-austerity-inequality-europe.

PART II – THE EU FINANCIAL SERVICES POLICY FRAMEWORK AND STRUCTURES

3 EU FINANCIAL SERVICES POLICY: DEREGULATORY HARMONISATION – CRISIS RESPONSE –REFORMS

3.1 EU financial services policy prior to the crisis

EU financial deregulation is embedded in the liberalisation and privatisation thrust of the 1980s. As early as 1983, a White Paper on financial integration by the European Commission called for greater liberalisation in the area of European finance.[38] This was followed by the 1986 Single European Act and the 1988 Council directive on the liberalisation of capital controls. At that time, a number of directives were adopted, introducing the so-called 'single passport' for financial services in the EU, on the basis of the mutual recognition and home country control principles.[39] Thus, products or services that are produced and marketed in one Member State are granted free access throughout the EU internal market, while the authorities of the Member State where the goods or service provider has its seat are responsible for carrying out regulation and supervision of the entity, mainly relating to risk monitoring. Host country authorities, on the other hand, retain responsibility in the area of liquidity. This is the framework that enabled the massive entry of European banks into the financial services sector of the central and eastern European countries in the 1990s.

The 1992 Treaty on the European Union and the introduction of the single currency in 1999 strengthened the tendency toward a more market-led financial system in the EU. For example, Danthine et al. (2000) found that the increased rate of activity in the EU capital markets signified a 'shift from banks to markets', benefiting the more market-based asset management and investment banking activities, by comparison to the traditional deposit and lending business of commercial banks.[40]

The advent of the euro in 1999 produced a new sense of urgency, as EU policy makers intensified their efforts to emulate the US financial industry model. This led to a new regulatory phase, beginning in the late 1990s with the Financial Services Action Plan (FSAP), which was implemented by 2005. This phase involved the further deregulation of financial services on the national level, with financial integration a key component of the Lisbon Strategy. The measure of success was explicitly stated to be lower transactions costs; according to the European Commission, 'business and citizens in the European Union need a regulatory environment which is clear, effective and workable in a rapidly changing, global market place. This is a key element if the European Union is to become the cheapest and easiest place to do business in the world.'[41]

By 2007, it appeared that the deregulatory policy followed by the EU was bearing fruit. According to the McKinsey Global Institute, Western European countries accounted for 56 % of the growth in global capital flows between 1980 and 2007, while the goal of deepening financial integration had been achieved in the money and government bond markets, and it was steadily approaching realisation in the rest of the financial services sector in the EU. However, these were the markets that were worst hit by the outbreak of the financial crisis in 2007/2008, as the money market dried up, while the government bond market went into gyrations that have repeatedly threatened the existence of the single currency since 2010. Furthermore, 72 % of the collapse in global capital flows since 2007 is accounted for by the Western European countries.[42]

The emphasis of the EU financial services policy prior to the crisis was on integration, a code word for deregulation, while its approach to the obvious danger of destabilisation relied on the exchange of information and on the existing, largely diverse, national supervisory models. The deficiencies of the supervisory regime were amply revealed by the crisis. As we shall see, the crisis revealed the true nature of EU financial deregulation, which favours the private sector at the expense of the public, the large players at the expense of the smaller ones, and capital – especially financial capital – at the expense of large segments of society, mainly the waged and salaried sectors.

Thus the 'success story' of EU financial integration was demystified. In the words of Jean-Claude Trichet, the former ECB president, 'Comparing the ex post returns with the considerable costs of the current turmoil, we have to realise that our financial system as a whole, including its non-regulated and non-listed entities, was neither strong nor efficient. It did not allocate capital properly and it did not manage risks well. … We have to put reserves and buffers back into the system; they are the protection against serious damage in a downturn and they are an integral part of sound finance.'[43]

38 European Commission, 1983, Financial Integration: Communication from the Commission to the Council, COM(83)297 final, 20 April. **39** The Single European Act gave rise to three groups of directives: (a) the Second Banking Directive (1989), the Investment Services Directive (ISD, 1993) and the Third Life and Non-Life Insurance Directives (1992) established the right of financial institutions to provide their services across the EU on the basis of a single license; (b) the 1985 UCITS – Undertakings for Collective Investment in Transferable Securities – Directive enables fund managers to provide investment funds across the EU, while the 1989 Prospectus and Initial Public Offerings Directives (IPO) harmonised the information that firms have to supply when offering securities to the public; (c) the 1989 Solvency Ratios Directive harmonised the capital standards for banks in the EU, implementing the Basel I Accord, while the 1993 Capital Adequacy Directive set minimum standards for banks and investment firms. **40** Jean-Pierre Danthine, Francesco Giavazzi, and Ernst-Ludwig von Thadden (2000) 'European financial markets after EMU: a first assessment', CEPR, *Discussion Paper* series No. 2413, Brussels. **41** European Commission, 2001, 'Realising the European Union's Potential: Consolidating and extending the Lisbon Agenda'. **42** Susan Lund, Toos Daruvala, Richard Dobbs, Philipp Harle, Ju-Hon Kwek, and Ricardo Falcón, 2013, 'Financial Globalisation: Retreat or Reset?', McKinsey Global Institute, March. **43** Keynote address at the Committee of European Securities Regulators, 23/2/2009.

3.2 Response to the financial crisis

In the autumn of 2008, as the full impact of the crisis was realised, the European Council reaffirmed '… its commitment that in all circumstances the necessary measures will be taken to preserve the stability of the financial system, to support the major financial institutions, to avoid bankruptcies and to protect savers' deposits. Inter alia, such measures aim, in conjunction with the central banks and supervisory authorities, to ensure sufficient liquidity for financial institutions, to facilitate their funding, and to provide them with capital resources so that they can continue to finance the economy properly. The European Council considers that measures to support financial institutions in difficulty should go hand in hand with measures to protect taxpayers, to secure accountability on the part of executives and shareholders and to protect the legitimate interests of other market players.'[44]

In the event, between October 2008 and October 2012, the amount of EUR 5.1 trillion was approved by the Member States for the support of the financial sector, corresponding to 40 % of the EU GDP (E. C., 2013: 16 & 19).[45] This was contingent taxpayer support individually financed by the Member States. Of this amount, more than two-thirds (26 % GDP) were actually disbursed between October 2008 and October 2011, with three Member States accounting for approximately 60 % of the total aid – UK (19 %), Germany (16 %), and Ireland (16 %). Furthermore, this aid was concentrated in a few financial institutions. For example, the three top banks in the UK and in Ireland absorbed more than 80 % and in Germany more than 50 %. The forms such aid took are shown in Table 1.

In adopting the above measures of support for the financial sector, the EU violated its own principles in relation to competition rules. In particular, it violated the 'principle of the firm's owners'/shareholders' primary financial responsibility' at a time of crisis, as stipulated in the 2003 Memorandum of Understanding on Crisis Management and further confirmed by the ECOFIN Council of October 2007, which stated that '(i) the objective of crisis management is to protect the stability of the financial system … not to prevent bank failures; (ii) in a crisis situation, primacy will always be given to private sector solutions, and (iii) the use of public money to resolve a crisis can never be taken for granted' ECB (2008: 82–83).[46]

Thus, there is a clear moral hazard contained in the EU's approach, which it chooses to ignore in rescuing its financial system. Furthermore, it burdened European taxpayers, especially the salaried and waged segments, with very high guarantees of the debt incurred in this respect. It may in fact be argued that the European Council Decision of October 2008 marks the beginning of the euro crisis, which erupted in 2010, starting from Greece and gradually encompassing an increasing number of EU Member States.

Monetary policy too was mobilised in support of the European banks. More specifically, the ECB responded to the crisis by adopting a number of exceptional or 'unconventional' measures, thus flooding the European financial system with liquidity, as well as reducing its key interest rate from 4.25 % in July 2008 to a record low 0.50 % in October 2013. These measures were

Table 1

Types of financial support given to EU banks

	Bank liabilities				Bank assets		Other		
	Increase deposit insurance	Guarantee or buy bank debt	Inject capital	Nationalise	Ring-fence bad assets	Purchase toxic assets	Fund commercial paper	Fund ABS	Ban or restrict short-selling
Germany	#	#	#			#			#
France		#	#						#
Italy	#		#						#
UK	#	#	#	#	#		#	#	#
Austria	#	#	#						#
Belgium	#	#	#						#
Denmark	#	#	#					#	#
Finland	#	#	#				#		#
Greece	#	#	#						
Hungary	#	#	#						
Ireland	#	#	#	#					
Luxembourg	#	#	#						
Netherlands	#	#	#	#					#
Slovak Rep	#								
Poland	#		#						
Portugal	#	#	#						
Sweden	#	#	#					#	
Spain	#	#						#	#

Source: OECD Economic Outlook, Interim Report, March 2009;
Note: The sign '#' indicates type of financial support provided by a country.

44 E. C. Conclusions, 15–16 October 2008, p. 2. **45** E. C., 2013, 'European Financial Stability and Integration Report 2012', SWD(2013) 156 final, April 24. **46** European Central Bank, 2008, 'Developments in the EU. Arrangements for Financial Stability', in *Monthly Bulletin,* April.

primarily addressed to the European banks, which obtained access to unlimited amounts of liquidity. As we can see in the figures below, the size of the ECB balance sheet more than doubled over the period 2008–2012 (from less than EUR 1.5 trillion to over EUR 3 trillion), while ECB lending to banks accounts for most of this increase. The balance sheet of the European Central Bank and the Eurozone's 17 national central banks currently stands at EUR 2,340 trillion euros.

Figure 4 (euro million)

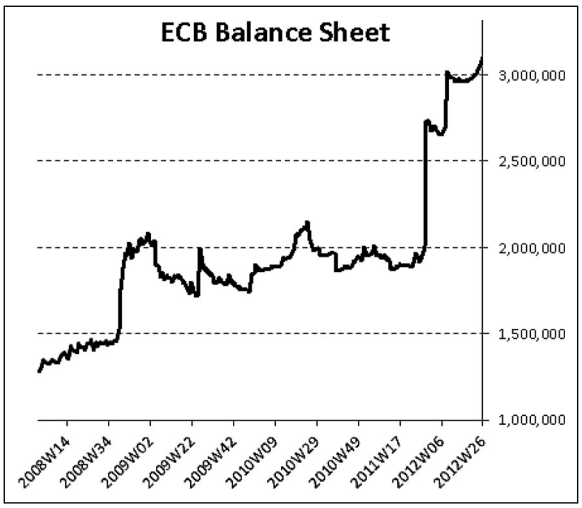
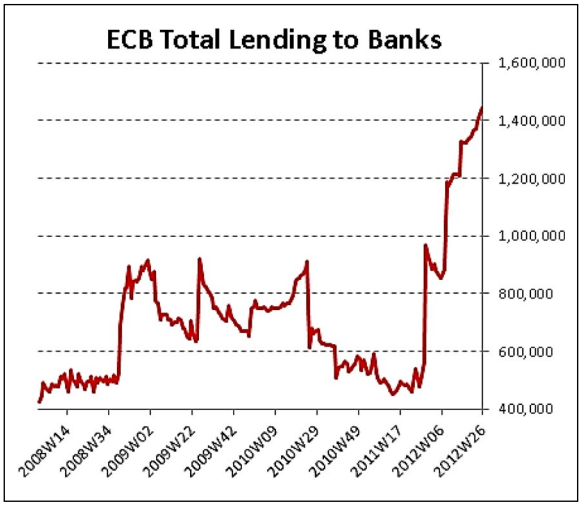


Figure 5 (euro million)



Source: ECB

By contrast, the role of the ECB as a lender of last resort vis-à-vis the European public authorities – the essence of central banking – is curtailed by the Treaty of the Union, as well as by the ECB statutes (art. 124.1 of the Treaty and art 21.1 of the Statute). This asymmetry in monetary policy, clearly favouring the financial sector, is one of the building blocks of the euro architecture and a significant component of the current economic crisis and worsening of inequality.

3.3 Financial policy reform

Following the collapse of Lehman Brothers in September 2008, the G20 was revived.[47] It met in Washington in November 2008, where it reaffirmed its commitment to free market principles, also agreeing on common principles for reforming financial markets. The reforms pertain to the following financial areas: credit rating agencies, hedge funds, OTC ('over-the-counter') derivatives, capital standards, and crisis management. The target date for implementation was set for the end of 2012.

In typical Community fashion, the response of the EU Council and the Commission to the crisis was to set up a high-level expert group to look into the problem and suggest necessary policy adjustments. The group was headed by Jacques de Larosière, a former Bank of France president. It submitted its report in February 2009. However, the reform of the EU financial services policy has been hesitant and slow, lagging behind that of the USA, in contrast to the immediate, unconditional and generous support in terms of both fiscal and monetary policy, which was extended to the EU financial services sector. The main areas covered so far include the following:

1. The establishing of three *European Supervisory Authorities* (ESAs) for each of the sectors: banking, securities, and insurance. These are executive committees under the control of the European Commission. Their task it is to promote the 'single rulebook'. These committees were originally set up in the mid-2000s as part of the Financial Services Action Plan, in order to provide technical advice to the Commission. The links between them and the financial industry are quite close, given that industry representatives participated as members when these authorities were first established.

2. A *financial transactions tax* was adopted on 22 January 2013 by eleven countries (Belgium, Germany, Estonia, Greece, Spain, France, Italy, Austria, Portugal, Slovenia, and Slovakia), to be implemented by 2014. The aim is to ease the fiscal burden rather than to put 'sand in the wheels of finance', to use the famous phrase of James Tobin. Thus it only applies to particular financial products, and the rate has been set quite low. Specifically, the tax rate has been set at 0.1 % on the exchange of shares and bonds and 0.01 % on derivative contracts.

3. *OTC derivatives,* practically unregulated until 2008, have been only partially regulated since August 2012, and transactions involving them must be cleared via central counterparties and registered in trade repositories to which the regulators have access.[48] However,

47 The group of twenty major industrial countries organised in the late 1990s to deal with the financial crisis of the period. **48** Related to these changes is the new practice of 'collateral transformation', in which banks help funds pledge their illiquid securities in exchange for more liquid collateral, which can then be used to back derivatives trade (practice of lending and repurchasing). The risk is that the new business could create longer and more complicated chains of collateral, more susceptible to vicious feedback loops when market values begin to slide.

no position limits – which could hinder speculation on food prices – have been placed on derivatives for commodities. Furthermore, decisive action is needed in the direction of (a) banning speculative/risky derivatives; (b) limiting them all to regulated and centrally cleared markets; and (c) introducing a clearance procedure so that new derivatives are consumer friendly (e. g. through a licensing system). Overall, shadow banking is to be brought out into broad daylight.

4. The Directive on *Alternative Investment Fund Managers,* which regulates managers of any unit undertaking investment, such as hedge funds and private equity, has come into force in 2013.

5. The *Short–Selling Regulation* went into effect in November 2012. Accordingly, significant short positions with regard to shares and sovereign debt must be notified and disclosed. Furthermore, naked CDSs (Credit Default Swaps) on EU sovereign debt instruments have been prohibited.[49]

6. As fears grew that the euro crisis could contaminate big Eurozone countries such as Spain and Italy, the idea of an EU *Banking Union* gained ground. This was decided at the June 2012 Euro Area Summit. It will cover three areas of common interest: supervision, deposit guarantee, and resolution. A single supervisory mechanism for the oversight of banks and other credit institutions was agreed on by the European Council at its October 2013 meeting. This confers specific tasks on the ECB and the European Banking Authority. However, it is not clear how the proposed Deposit Guarantee Scheme is to be backed, nor by whom – the European Stability Mechanism, the ECB, some form of debt mutualisation? Without any arrangement for a common fiscal backstop, a banking union cannot come into existence. The decision on this score is unlikely to be taken any time soon, as the Member States hold differing opinions. For example, Germany, Sweden, Poland, and the Netherlands wish a banking union only for the big banks, while France envisages one for all banks.

7. Other ongoing reform areas include market abuse, statutory audit of public entities, consumer protection, transparency and accounting, shadow banking, production, and the use of indices as benchmarks (e. g. LIBOR).

8. In addition to the above, the following reforms are being put into place within the global policy framework decided by the G20.

9. A *Third Basel Accord,* which maintains the current risk-weighted capital ratios system subject to a stricter definition of capital. In addition, new risk-weighted ratios for liquidity, leverage and net stable funding, as well as a surcharge for large, systemically important financial institutions, are being introduced. The new rules are to be put into effect from 2014 until 2019. However, the multiplicity of ratios – there are seven different ones – and the divergent implementation deadlines are likely to cause friction as to when/whether a bank is Basel III compliant. Further, Basel III maintains the calculation of risk-weighting on the basis of ratings assigned by the credit rating agencies or by internal risk models, both of which were instrumental in the 2007/2008 financial crisis.

Basel III is being transposed into EU Law on the basis of the Capital Requirements Directive IV (CRD IV) and the Capital Requirements Regulation (CRR). The CRD IV also includes clauses on (i) remuneration, whereby after 2014 the variable component of total remuneration are not to exceed 100 % of the fixed component (bonus – basic salary) and 200 % in exceptional circumstances; (ii) governance; (iii) gender balance (diversity) in board composition, and (iv) transparency. Without underestimating the significance of these measures, the fact that five years into the crisis putting caps on the remuneration of top bankers is still under discussion is indicative of the resistance of the financial industry to change. The same is true of the banks' governance structures and patterns, which remain largely unchanged.

With regard to *bank restructuring,* the USA has adopted the Volcker rule, in which trading by commercial banks on their own account was restricted as of July 2012. France and Germany have also taken measures on the national level. On the EU level, the issue is currently being discussed on the basis of the LIIKANEN Report,[50] which recommends the following: (a) proprietary trading and other significant trading activities should be assigned to a separate legal entity over a certain threshold, to involve two stages: the trigger for the first stage would be that assets held for trading exceed EUR 100 billion or 15–25 % of total assets; in the second stage supervisors would determine the need for separation; (b) the hierarchy of debt instruments that can be 'bailed-in' is stipulated; (c) capital requirements on trading assets and real estate loans should be reinforced; and (d) the remuneration of the top management are to include 'bail-inable' debt instruments – and be subject to disclosure. Generally, the recommendations of the Liikanen Report are a step forward, albeit a hesitant and inadequate one. The holes left are too big to ensure the adequate protection of retail banking, the taxpayer, and the economy from trading activities. As Peter Wahl has noted, this is a 'half-hearted attempt to solve the too-big-to-fail problems'.[51]

Overall, EU financial policy reform has been a slow and piecemeal affair, while the targeted actions are unlikely to mitigate the dominance of finance over labour and the economy at large. Much less do they address the fundamental problems of finance-led capitalism, amongst which inequality takes the lead. A case in point is the way the EU has dealt with the credit rating agencies, which we shall look into in some detail by way of an illustration of the intertwining of power

49 A credit default swap (CDS) is an agreement that the seller of the CDS will compensate the buyer in the event of a loan default. A CDS in which the buyer does *not* own the underlying debt is referred to as a *naked credit default swap.* **50** Submitted in October 2012. **51** Peter Wahl, 2012, 'Liikanen Report: Half-hearted attempt to solve the "too-big-to-fail" problem', in SOMO & WEED, *EU Financial Reforms Newsletter,* Issue no. 15, 7/12/2012. **52** The Parmalat scandal (known also as

between the financial elite, the political class, and the European bureaucracy.

The *credit rating industry* is a global business, controlled by three firms, Moody's, Standard & Poor's, and Fitch, which control more than 90 % of the global market. Their penetration into the EU financial services sector is profound. The EU has in fact created a captive market for the credit rating industry insofar as (i) the Capital Requirements Directive (CRD) implementing the (previous) Basel II agreement gave national supervisors the power to use a rating agent in order to set the CRD risk weights, and (ii) the credit assessment of eligible collateral for the ECB's liquidity-providing operations is predominantly based on a public rating. Both the CRD and the ECB explicitly apply the rating structures of the CRAs to determine risk weighting. It is worth noting that the USA does not have any of these practices, while the recent Dodd-Frank Act – overhauling US financial policy – requires regulators to remove any references to the rating of securities from their rules.

The EU debate on the CRAs goes back to the early 2000s. In particular, following the dot.com bubble, where the role played by the CRAs was notorious, the European Parliament passed a resolution on the basis of MEP Katiforis' report on the role and methods of credit rating agencies. This report called on the European Commission to submit, by 31 July 2005, its assessment of the need for appropriate legislative proposals to deal with the CRAs.

Finally, in March 2004, following the Parmalat scandal and the adoption of the Resolution by an overwhelming majority of the European Parliament, the Commission asked for the technical advice of the Committee of European Securities Regulators (the predecessor of the European Supervisory Authority for the securities market).[52] The latter ruled that no legislation was needed since the CRAs' self-regulation was considered adequate!

It took yet another and a much bigger crisis – the 2007/2008 crisis – for the EU to pass the first legislative measure dealing with the CRAs in 2009 (Reg. 1060/2009, 16 Sept 2009). This requires CRAs to register and to disclose potential conflicts of interest, methods, models and rating assumptions. However, it does not alter the fundamental problem of the CRAs from a public policy perspective, i. e., in relation to (a) the oligopolistic structure of industry; (b) the potential conflict of interest inherent in the issuer-pays principle, and (iii) the public-good aspect of private rating. Therefore, the European Council adopted a directive and a regulation amending the EU rules on CRAs (E. C., 13/5/2013). Although the new rules alleviate some of the problems of the CRAs, they fall short of the proposal by the European Parliament, which has demanded that all references to 'external ratings' in EU Law be deleted by 2020.

Generally, the treatment of the CRAs by the EU institutions is indicative of the close links between finance and politics. Although the CRAs have been universally recognised as one of the culprits behind the current financial crisis, they still have the upper hand in government bond markets, dictating terms to governments. Efforts to control them so far in the EU have been 'too little, too late'. Nor do these efforts address the need (a) to release the CRAs' hold on the EU financial services sector, by delinking them from the CRD requirements and the use of external ratings by the ECB; (b) to set up public CRAs alongside private ones, and (c) to incorporate social and environmental criteria in the models applied.

The EU treatment of the CRAs is symptomatic of the laxity with which regulators, politicians and mainstream academia treat the role of finance in contemporary capitalism. As a result, the lobbying business in Brussels has become ever larger and more competitive, attracted by the fact that the EU collectively forms the world's largest economy, as well as the weak ethics in Brussels, which, among other things, allow former government officials to begin exploiting their connections as soon as they leave office.[53] The fact that justice moves very slowly if at all encourages such behaviour. Even the *Economist* is protesting about 'Blind Justice', asking 'why have so few bankers gone to jail for their part in the crisis?'[54]

4 EU FINANCIAL SERVICES STRUCTURES – DEEPENING FINANCIALISATION

4.1 Size and structure of the EU financial services sector

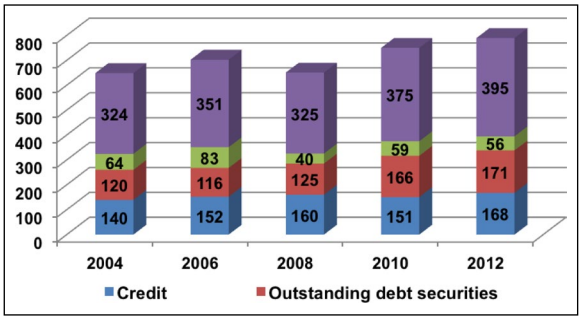
Financial deregulation and the liberalisation of capital flows at the global and European levels in the 1970s and 1980s led to the fast expansion of the EU financial services sector, as well as to its transformation from a bank-based system to a market-led one. For example, in 1980 the financial sector in the original (twelve) Member States of the Eurozone was equal to 78 % of GDP, as opposed to 179 % in the USA and 200 % in Japan.[55] Furthermore, the sum of shares and debt securities in these countries amounted to 35 % of their combined GDP, as opposed to 105 % in the USA and 103 % in Japan.[56] Even the UK, more financially advanced than the rest of the EU, fell behind the USA and Japan on both counts.

This was the challenge that European capital had to rise to, which it did via the steady deregulation of the sector and of the economy as a whole, as well as the introduction of the single currency. The 2007/2008 crisis signalled a temporary setback, which was overcome one year later. As shown in Figure 6, in 2012

'Europe's Enron') refers to the discovery in 2003 of a $ 14bn black hole in the finances of Italy's milk-processing giant Parmalat, which triggered an eight year marathon of court cases in Europe and America. **53** See Eric Lipton and Danny Hakim, 2013, 'Lobbying bonanza as firms try to influence European Union', *The New York Times,* 18 October. **54** 'Prosecuting Bankers: Blind Justice', *The Economist,* 4 May 2013. **55** Eurozone countries: Austria, Belgium, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain. **56** Marica Frangakis, 2009, 'Europe's Financial Systems Under Pressure', in John Grahl, *Global Finance and Social Europe,* Edward Elgar, London.

the sum of credit (168 %), debt securities (171 %) and stock market capitalisation (59 %) amounted to 395 % of EU GDP, which was higher than even the 2006 level (351 %) on the eve of the outbreak of the financial crisis.

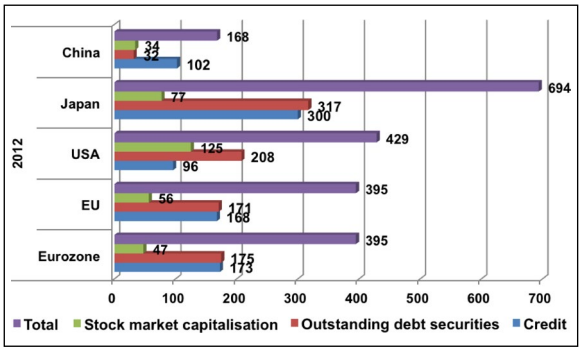
Figure 6
Size and structure of the financial services sector in the EU (% GDP), 2004–2012



Source: ECB Data Warehouse; Financial indicators

As a result, the size of the financial services sector in the EU, as well as in the Eurozone, has approached that of the USA, as shown in Figure 7, which also includes Japan and China. Although the EU appears to be behind Japan in terms of size, the long recession Japan is facing should be borne in mind. On the other hand, China is a late-comer on the financial scene, which explains its relatively small financial sector at the present time.

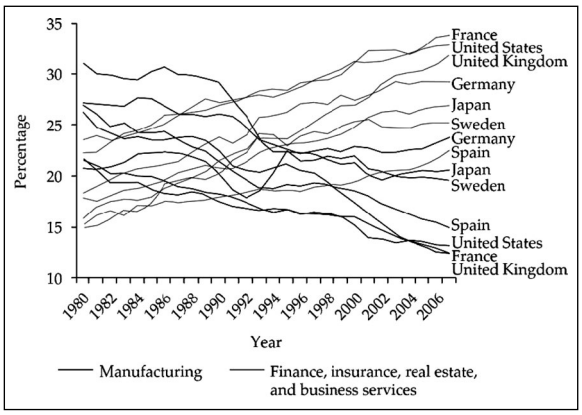
Figure 7
Comparative size and structure of the financial services sector, 2012 (% GDP)



Source: ECB Data Warehouse; Financial indicators

The rising share of the financial services has been the concomitant of the declining share of manufacturing in the major economies of the EU and in the USA as well as Japan, as shown in Figure 8 (Bermeo & Pontusson ,2012: 25).[57] This trend continued over a quarter of a century, and it can be safely assumed that the global financial crisis has not reversed it.

Figure 8
Manufacturing versus financial sector value added as a percentage of GDP



Source: http://www.russellsage.org/node/4004

The increasing size and share of the financial services sector in the economy has gone hand in hand with its transformation from a relationship-based system to a market-based one, as increasing volumes of finance are raised and exchanged on the financial markets. These include the money, bond (private and government), equity and derivatives markets, as well as the currency markets.

As mentioned above (section 3.1), the ultimate goal of EU financial policy in the 1990s and 2000s was the integration of each of these markets across the EU Member States. This was largely achieved in the case of the money and the government bond markets. However, it is these very markets which were most disrupted by the financial crisis, pointing to the lop-sided EU policy of integration, and the issue of financial stability was overlooked in the name of greater financial depth.

In particular, the money markets (pertaining to assets of up to one year) completely seized up at the start of the crisis, while they currently absorb much of the liquidity provided by central banks. Similarly, the government bond markets are profiting from the increased liquidity provided by the central banks as they increase in size, and the public debt level is rising both in the EU and in the USA. The equity markets had their heyday in the late 1990s, which however led to the bursting of the dot.com bubble and to the slowing down of their rate of expansion. During the present crisis they have not been in the limelight, although they were not as disrupted as other markets. Derivatives, mostly of the OTC, or unregulated, type, are a major financial market globally, in which the EU is dominant. Until the crisis, these markets were only lightly regulated, if at all, as they were perceived to be allocating resources rationally. The fallacy of the Efficient Market Hypothesis and its dangers became only too plain during the

57 Nancy Bermeo and Jonas Pontusson, 2012, *Coping with Crisis,* Russell Sage Foundation.

2007/2008 financial crisis.

With the expansion of the financial markets came the increasing significance of institutional investors, viz. organisations which pool large sums of money, which they invest in various assets, such as securities, real estate, etc. These include insurance companies, pension funds, hedge funds, investment companies and mutual funds, and they are often interconnected by belonging to the same financial group.

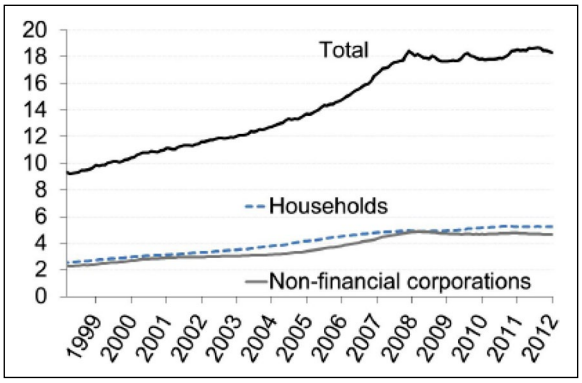
These are especially sophisticated organisations, which influence not only the way financial markets work, but also the solvency and conduct of the companies in which they hold shares. The aggressive expansion of finance in the 1990s and 2000s is closely linked to the increasing dominance of financial markets and the involvement of institutional investors.

4.2 Trading: the changing nature of banking and finance

The low inflation – low interest rate environment fostered both by the ECB and by the US Federal Reserve over a long period of time provided incentives for moving away from relationship-based towards market-based finance. Furthermore, it encouraged the search for ever higher yield/risk products. Not surprisingly, most of the growth in bank balance sheets was driven by intra-financial business rather than by actual lending. For example, according to the McKinsey Global Institute, over the period 1995–2007 the financing of households and non-financial corporations accounted for only 25% of the increase in global financial depth.[58] A similar phenomenon took place in the EU, where, according to the Liikanen Report, in March 2012, loans equal to only 28% of the total assets of the aggregate bank balance sheet were given to households and non-financial corporations by banks.[59] As shown in Figures 9 and 10 below, loans by Eurozone Monetary Financial Institutions as a share of their assets has been steadily declining since the late 1990s, even though the nominal value of these loans has been increasing.[60]

Figure 9

MFI loans in the Euro area (EURtn)



Source: EFSIR, 2013: 28 Source: EFSIR, 2013: 28

Figure 10

MFI loans in the Euro area (% of total assets)

Source: EFSIR, 2013: 28 Source: EFSIR, 2013: 28

The expansion of European banks into financial areas other than banking is further facilitated by the dominant regulatory and legal model for banking groups, that of the 'universal banking model'. Accordingly, EU universal banks typically combine retail and commercial banking activities and wholesale and investment banking activities in one corporate entity, with other activities, such as insurance, carried out in wholly owned but separately capitalised subsidiaries.

The current EU financial system is characterised by relatively few large, interconnected and diversified banking groups. As shown in Table 2, the size of the EU banking sector, both in absolute and relative terms, is greater than that of the USA and of Japan.

Table 2

Size of EU, US and Japanese banking sectors (2010)

	EU	USA	Japan
Total bank sector assets (EUR trillion)	42.9	8.6	7.1
Total bank sector assets/GDP	349%	78%	174%
Top 10 bank assets (EUR trillion)	15.0	4.8	3.7
Top 10 bank assets/GDP	122%	44%	91%

Source: Liikanen Report, 2013: 12

There is of course variation in the size of the banking sector across the EU Member States. In absolute terms the largest sectors are in the UK, Germany and France and in relative terms (in relation to GDP) in Luxembourg, Ireland, Malta and Cyprus, which are offshore financial centres.[61]

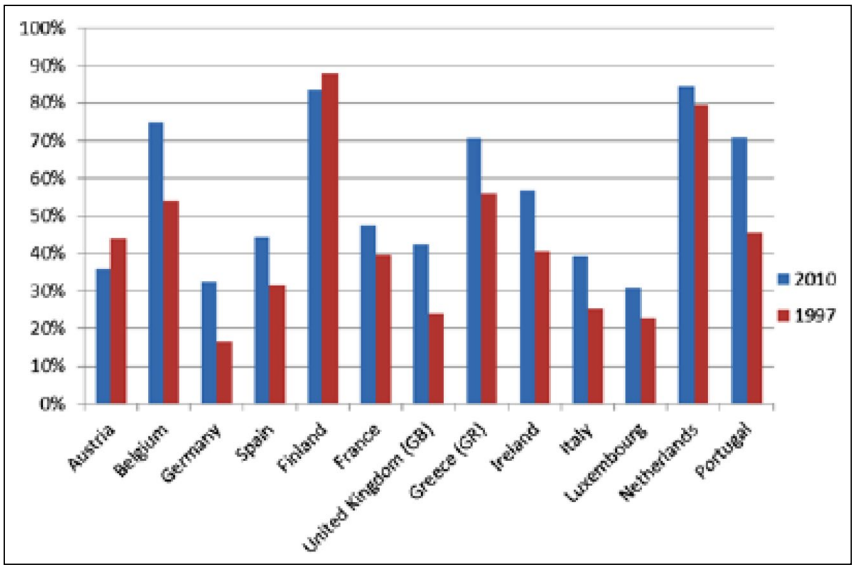
The EU banking sector is, moreover, highly concentrated by comparison to the USA and Japan, as shown in Table 2 above. Such concentration has been increas-

58 McKinsey Global Institute, 'Financial Globalisation: Retreat or Reset?' *Global Capital Markets* 2013. **59** EC, 2013, *European Financial Stability and Integration Report,* Commission Staff Working Document, SWD (2013) 156 final. **60** According to the ECB, MFIs are 'resident credit institutions as defined in Community law, and other resident financial institutions whose business is to receive deposits and/or close substitutes for deposits from entities other than MFIs and, for their own account (at least in economic terms) to grant credits and/or to make investments in securities' www.ecb.europa.eu/stats/money/mfi/index.en.html. **61** Appendix I presents data on the monetary financial institutions by country as of 2012.

ing over time, as we can see in Figure 11 below, which shows the market share of the top five banks in the EU countries with a relatively large banking sector in 1997 and 2010. Furthermore, according to the latest Banking Structures Report of the ECB, over the period 2008 to 2012 there has been a net decrease in the number of credit institutions, due primarily to within-group consolidation, raising the concentration of EU banking to even higher levels.[62]

Figure 11

Concentration ratio (market share of top 5 banks in total assets)



Source: Liikanen Report, 2013: 18

The dominance of the EU banking sector in the economy is not solely numerical. Even more importantly, it signifies a regime shift from the 'originate and hold' model, which was prevalent before the 1980s, to the 'originate and distribute' one – in which granted loans are pooled, securitised and sold to investors – which came to dominate the business of banking ever since.[63] While the first type of model focuses on building long-term customer relationships and on generating net interest income, the second type focuses on activities in the financial markets and on deriving income from fees and trading.

A further fundamental difference between the two models concerns their funding. Whereas the 'originate and hold' model relies on insured deposits, the 'originate and distribute' model relies on capital markets for funding. The inherent risks in the post-1980s banking model were made clear by the 2007/2008 financial crisis, in which the majority of the large and complex EU financial institutions that received state support had above average trading income to total revenue ratios.[64]

The shift in the banking model has encouraged the growth of shadow banking, defined as 'the system of credit intermediation that involves entities and activities outside the regular banking system'.[65] Such entities include securitisation vehicles, money market funds, investment funds, finance companies providing credit, and insurance and reinsurance undertakings, and the activities they engage in include securitisation and securities lending and repurchase transactions ('repo'), both at the heart of the 'originate and distribute' business model of the EU banking groups. It is estimated that the size of the global shadow banking system was approximately EUR 46 trillion in 2010, having grown from EUR 21 trillion in 2002. This represented 25–30 % of the global financial system.[66] Shadow banking has been increasing in importance in the EU, as opposed to the USA, where it is declining, although it accounts for a much larger share of the financial sector there. For example, in 2012, shadow banking accounted for 48 % of the total financial sector in the USA, down from 61 % in 2007, and for 20 % in the Eurozone, up from 19 % in 2007.[67]

Overall, the changing nature of the banking business and the deepening of the financial markets in the EU have had repercussions on the workings of the financial sector in relation to the rest of the economy and, by extension, to society at large. More specifically, the increasing competitiveness of the financial services sector has shifted the focus of company objectives towards short-term profits, higher risk-taking and risk-shifting, accommodationist accounting practices, and intense lobbying. This is true of the various types of financial enterprises, as well as of non-financial enterprises with active financial departments or subsidiaries.

That is, corporate governance has adjusted by adopting new norms both in the market place and outside it. For example, the short-termism of finance is closely associated with short-term performance-based managerial compensation schemes, on the one hand, and the formation of an elitist group of financiers on the global level, on the other. Both tendencies lead to a widening of the income distribution gap not only between capital and labour (functional distribution), but also within both capital and labour (personal distribution). Thus, the wealth amassed by the top 1 % income bracket is largely the result of the extraordinary financial engineering of a tightly knit elite, which

62 ECB, 2013, *Banking Structures Report,* November. **63** Appendix II presents the stages of a mortgage securitisation package. **64** EFSIR, 2013. **65** Financial Stability Board, 2011, *Shadow Banking: Strengthening Oversight and Regulation.* **66** EC, 2012, Green Paper: *Shadow Banking,* Brussels, CLM(2012) 102 final, March 19. **67** ECB, 2013, *Financial Integration in Europe,* April.

has been taking place in the global and in the European economy in the past few decades.

A further outcome of the dominant role of finance is the fact that the links between the financial elite and the political class have become particularly strong, to the point where former financial executives become prime ministers, as was the case with Lucas Papadimos – former ECB vice president and Prime Minister of Greece in 2011–2012 – or of Mario Monti – former International Advisor at Goldman Sachs and Prime Minister of Italy in 2011–2013 – while the reverse is also true, for example the current head of the ECB Mario Draghi is a former Goldman Sachs executive and former governor of the Bank of Italy.

The financial services sector returned to growth shortly after the largest global financial crisis in nearly a century broke out, while financial policy reform has been notoriously slow, especially in the EU. The dominance of finance in economic and political terms and its implications for the economy and for society at large – especially labour – go a long way towards explaining the current state of affairs.

PART III – DISTRIBUTION OF INCOME, POVERTY AND WEALTH IN THE EU

5 FUNCTIONAL DISTRIBUTION OF INCOME

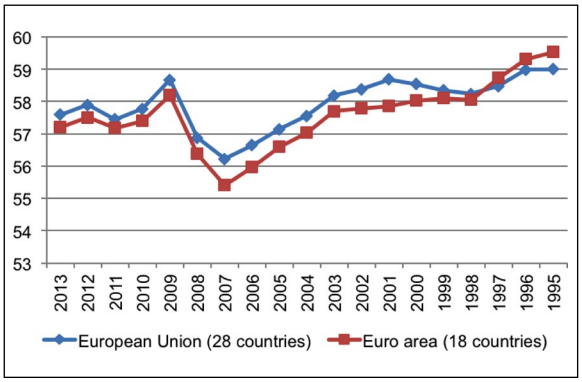
5.1 Adjusted wage share

The functional distribution of income is the archetypal problem in political economy. It is what the classics fought over and what the neoclassics chose to ignore or to dilute within the general framework of economic analysis. Since the collapse of the Bretton Woods system and the liberalisation of capital, the share of labour in the distribution of income has been declining, a phenomenon that has been observed both on the global and on the European level. Our analysis pertains to the EU and Eurozone levels over the period from the mid-1990s to the present.[68]

Fig. 12 below shows the share of wages in GDP in the EU28 and in the Eurozone 18 during the period 1995–2013. As we can see, the income share of labour has been steadily declining. In 1995, it was equal to 59 % of GDP in the EU and 60 % in the Eurozone, falling to 57 % and 56 % respectively in 2007. As in previous crises – e. g. the dot.com crisis of the early 2000s – the series shows a short-lived rise immediately after the crisis, as capital was the first to be hit, resuming its downward course soon after. Thus in 2013, the share of wages in GDP was equal to 58 % in the EU28 and 57 % in the Eurozone.

Figure 12

Adjusted wage share in EU28 and Eurozone18 1995–2013 *(compensation per employee as percentage of GDP at current market prices per person employed)*



Source – E. C., AMECO statistics

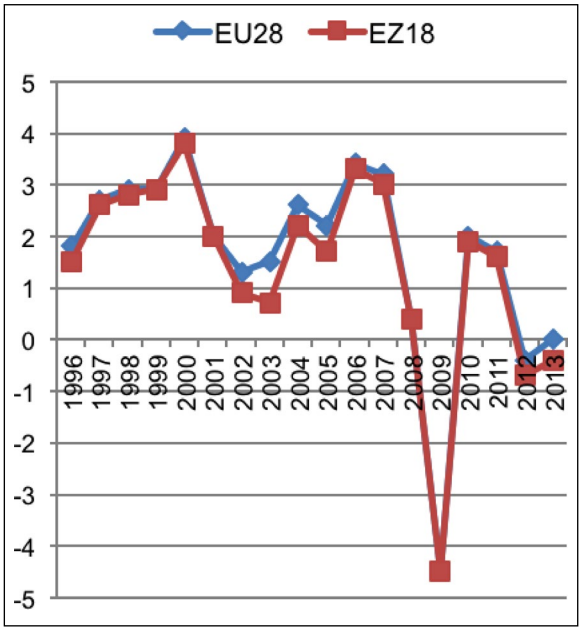
It is interesting to note that since the late 1990s, the share of labour in Eurozone GDP has been consistently below that in the EU27, even though it was in a more advantageous position in the mid-1990s. This reflects the fact that the single currency has been built on the assumption of 'wage moderation', i. e., restraining labour costs and in particular wages. To this end, EU labour policy has long favoured labour market flexibility under the so-called 'flexicurity' system, whereby flexible job arrangements are promoted, while transitions between jobs are assumed to be secure. Of course, such security is scarce in a slowly growing or even stagnating economy.

5.2 Repercussions on growth and employment

The dual nature of wages – wages as a cost of production and as the material basis of workers' consumption – was underestimated by the architects of the Eurozone in economic terms, while serving wider goals in political terms à la Kalecki. This was at the cost of slow and declining rates of growth of the EU economy, a phenomenon that was especially evident in the Eurozone, as shown in Figure 13. Similarly, investment (Gross Fixed Capital Formation) remained subdued throughout this period, becoming negative after the crisis erupted, a trend from which it has not yet recovered (Figure 14). In both instances – growth of GDP and investment – the performance of the Eurozone was below that of the EU as a whole, again pointing to the suppressive nature of the euro project. During this time, the financial sector was on the rise in terms of size and social and political influence, as discussed above.

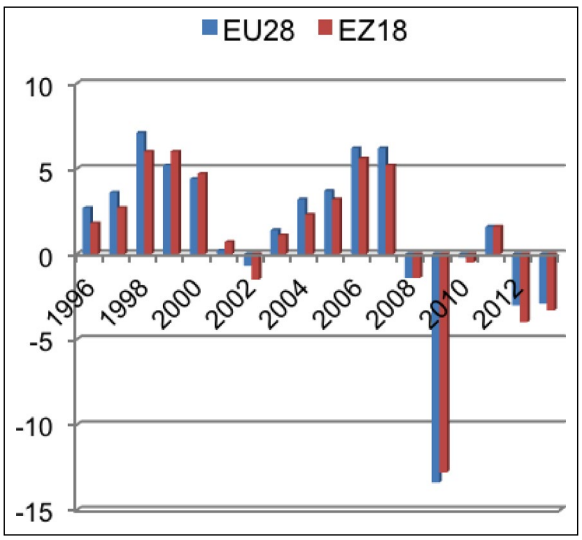
Figure 13

GDP at 2005 market prices (annual % change)



68 EU28 – or EU27, i. e., before the accession of Croatia – and Eurozone18 – Eurozone17, i. e. before Estonia joined – depending on data availability.

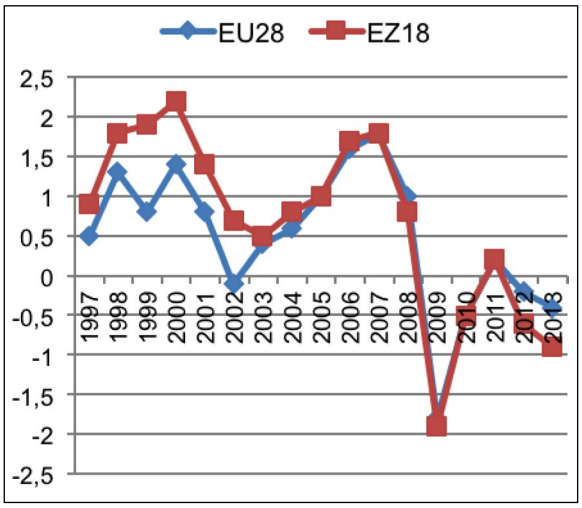
Figure 14
GFCF at 2005 market prices (annual % change)



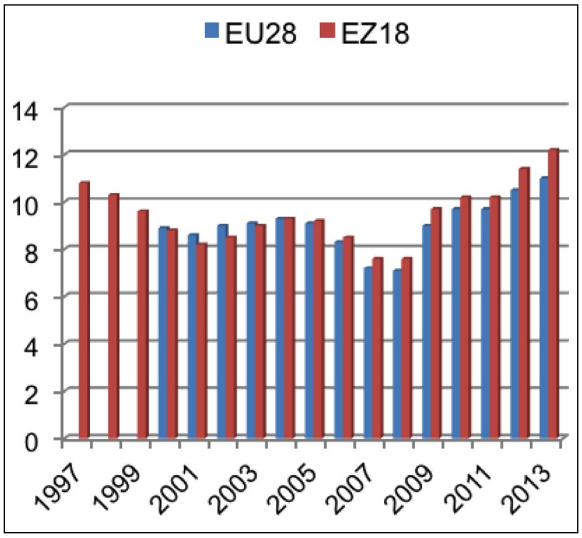
Source: Statistical Annex of European Economy Autumn 2013

The slow and declining growth rate of the EU economy and, especially, of the Eurozone, are reflected in the slow rate of increase in employment and in the high rate of unemployment during this period (Figures 15 and 16 respectively). Furthermore, the financial crisis has led the employment rate into negative territory and unemployment to new highs. The latter reached 11 % of the labour force in 2013 on average in the EU, surpassing the 9 % level of the early 2000s following the dot.com crisis. Such averages, it should be pointed out, hide significant variations amongst EU Member States. For example, in 2013 the rate of unemployment varied from 5.1 % in Austria and 5.4 % in Germany to 27 % in Greece and 26.6 % in Spain.

Figure 15
Employment: annual % change Figure 15 Unemployment rate (% labour force)



Source: Statistical Annex of European Economy Autumn 2013



Note: Data for EU28 before 2000 not available

Despite the negative developments on the level of growth and employment, the EU's policy of wage restraint through labour market reforms has been continued, aiming at increasing the flexibility of the labour market still further. Such a policy is felt to be a major component of the 'ambitious' reforms deemed necessary for the overcoming of the present crisis. Thus, the report on Labour Market Developments in the EU in 2013 concludes that: 'European countries have shown an increased commitment to tackle the structural weaknesses built-up over the last decade. Substantial reforms aimed at improving the resilience of the labour market, introducing more internal and external flexibility and facilitating the transition between jobs have been introduced in several Member States, and more are planned in the years to come' (E. C., 2013: 60).[69]

The EU policy of wage restraint and labour market deregulation will reduce further the income share of labour, as underemployment and other types of 'soft unemployment' rise and wages decline. The opposition by the trade unions has so far been ineffective in stopping, much less reversing, these trends. In fact, the European Social Dialogue, instituted in the Maastricht Treaty of 1992, excludes wages from the areas of negotiation between employers and employees.

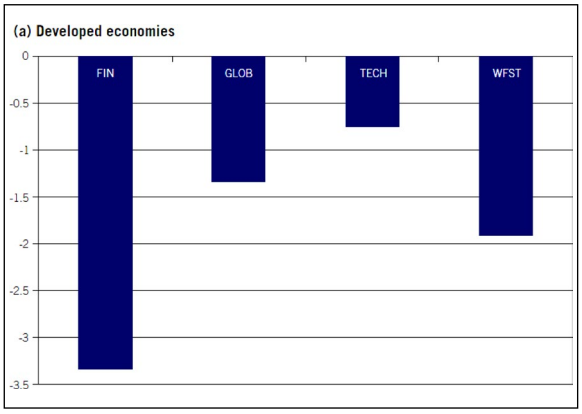
The European Trade Union Confederation (ETUC), representing European workers, had no objection to this state of affairs until recently. It is only in 2008 that the ETUC organised the first European demonstration, with the slogan 'increasing salaries and better sharing of profits'. In addition, at its May 2011 Congress in Athens, the ETUC declared its opposition to EU policies, demanding the stop of anti-salary measures. While trade union opposition remains weak and uncoordinated, the bulldozer effect of EU policies on labour income will continue.

69 E. C., 2013, 'Labour Market Developments in Europe, 2013', *European Economy* 6/2013.

5.3 The contribution of finance

As argued earlier, financialisation is a significant driver of the increasing inequality in income distribution. In particular, the International Labour Office has estimated that, in the developed countries, financialisation was responsible for 46 % of the fall in labour income shares between the periods 1990–1994 and 2000–2004, compared to 19 % of it being caused by globalisation, 10 % by technology, and 25 % by changes in government spending and union density (Figure 16).[70]

Figure 16
Factors contributing to changes in the average adjusted labour income share between 1990–1994 and 2000–2004



Source: ILO, 2013, *Global Wage Report 2012/2013,* Appendix III – Notes: FIN: 'financialisation'; GLOB: 'globalisation'; TECH: 'technology'; WFST: 'welfare state measures and labour market institutions'. 'Developed countries': Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Italy, Japan, Luxembourg, Netherlands, N. Zealand, Norway, Poland, Portugal, Slovakia, Spain, Sweden, Switzerland, UK, USA.

Although the above estimates refer to the global level, it is worth noting that of the 28 countries included in the sample, 20 are members of the EU. Hence, it may safely be assumed that the role of finance in the declining income share of labour in the EU has been equivalent to that on the global level.

6 PERSONAL INCOME AND WEALTH DISTRIBUTION

6.1 Measures of income inequality in the EU

There are sharp inequalities in the distribution of personal income within the populations of the EU, as well as between its Member States. Such inequalities undermine social cohesion, and they bear directly on the extent and depth of poverty. Figure 17 below depicts income inequality in the EU and in the Eurozone in terms of the income quintile share ratio (ratio of total income received by the 20 % of the population with the highest income to that received by the 20 % with the lowest income), while Figure 18 shows this in terms of the Gini coefficient (ranging from 0 – perfect equality – to 1, where one individual receives all of the income and the others none)[71].

Figure 17
Income quintile share ratio (S20/S20)

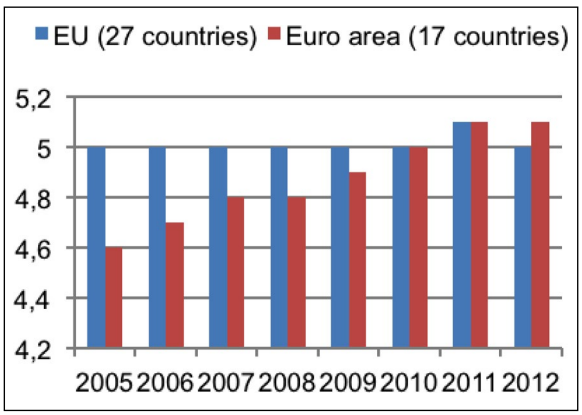
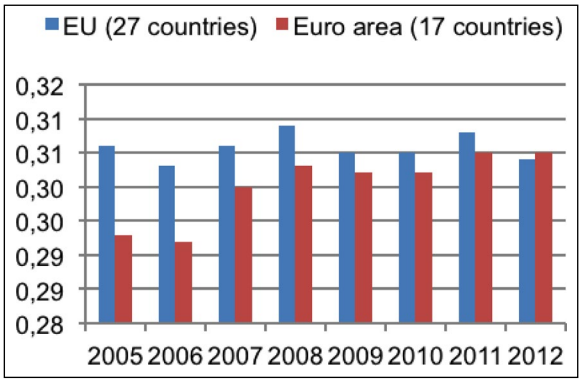


Figure 18
Gini coefficient (equivalised disposable income)



Source: Eurostat – Note: 'Equivalised' disposable income is adjusted for household size and composition.

In terms of the quintile ratios, inequality is greater in the EU by comparison to the Eurozone, where it has however been rising faster. Thus, in 2005, the S20/S20 ratio was equal to 5 in the EU and to 4.6 in the Eurozone, while by 2012 it had reached 5.1 in the Eurozone although it remained at 5 in the EU. That is, the 20 % of the population with the highest equivalised disposable income received 5.1 times as much income as the 20 % of the population with the lowest equivalised disposable income. This ratio varied considerably across the Member States, from 3.5 in Slovenia and the Czech Republic, to at least 6 in Greece, Romania, Bulgaria and Latvia, peaking at 6.8 in Spain.

Similarly, in terms of the Gini coefficient, income inequality was equal to 0.31 in the EU and to 0.29 in the

70 'The switch in the 1980s to corporate governance systems based on maximizing shareholder value and the rise of aggressive returns-oriented institutions, including private equity funds, hedge funds and institutional investors, put pressure on firms to increase profits, especially in the short term' (ILO 2013: 50). **71** Many inequality measures exist. They are either one-number statistics, such as the Gini coefficient, or shares of income, i. e., percentile ratios, whereby the former measures the income distribution as a whole, while the latter provide a measure of income inequality at specific points of the distribution (see Peter Hoeller, Isabelle Joumard, Mauro Pisu, and Debra Bloch, 2012, *Mapping income inequality across the OECD,* WP 924).

Eurozone in 2005, slightly declining to 0.30 in the EU by 2012, albeit increasing to 0.31 in the Eurozone. In 2012, this varied from 0.22 in Norway to 0.35 in Latvia.

By way of a broader comparison, it should be noted that in the late 2000s, income inequality in the 34 Member States of the OECD amounted to 0.31 in terms of the Gini coefficient and to 5.4 in terms of the quintile ratio, while the USA's equivalent figures were equal to 0.38 and 7.7 respectively[72]. Thus it appears that the EU figures are close to the average OECD ones, although they are below those of the USA.

6.2 Unemployment, underemployment and poverty

Personal income distribution is closely linked to the functional income distribution, as well as to the dispersion of wages across different types of work. More specifically, it has been found that there is a negative correlation between the Gini coefficient and the labour income share, while a positive correlation links it to wage dispersion.[73] That is, a rise in the labour income share leads to a decrease in income inequality. By contrast, a wider wage dispersion results in greater income inequality. Finance intervenes in both of these areas, exacerbating the unequal distribution of personal income.

As regards the labour income share, finance contributes through its overbearing presence in the economy and its implications for the allocation of resources between productive uses and financial, speculative ones. As discussed in Section 5 above, the ILO estimates that nearly one-half (46 %) of the decline in the income share of labour is due to the workings of finance. In particular, the continuous decrease in the share of income enjoyed by labour since the 1980s has led to the slowing down of the rate of growth of the economy and to a high rate of unemployment, as discussed in Section 5.2. Both of these developments increase inequality, as employment becomes more and more precarious, with wages tending to concentrate at the low-end of the scale. These phenomena are clearly evident in the case of the EU, and the crisis has intensified them.

It is estimated that 26.6 million persons are currently unemployed in the EU, of whom 19.4 million are in the Eurozone (11 % and 12 % of the labour force respectively).[74] To these one must add three further types of unemployed persons: underemployed part-time workers, jobless persons seeking a job but not immediately available for work, and jobless persons available for work but not seeking it. In 2012, these three forms of 'soft' unemployment amounted to 8.4 % of the EU labour force.[75] Thus, nearly one-fifth of the EU labour force suffers from some form of unemployment, while nearly one-half of the unemployed have been out of work for over a year (45 % in the EU and 46 % in the Eurozone in 2012, by comparison to 37.2 % and 39.3 % respectively in 2008).

In addition to unemployment and underemployment, the EU labour market contains a large and increasing segment of 'flexible' employment. In particular, part-time employment constitutes approximately one-fifth of total employment – 19 % in the EU and 21 % in the Eurozone in 2012 – having increased from 17 % and 19 % respectively in 2008. Furthermore, temporary employment reached 14 % of total employment in the EU and 15 % in the Eurozone in 2012 (from 14 % and 16 % in 2008). Such employment is often precarious, i. e., poorly paid, insecure and unprotected, depressing the labour income share still further.

As might be expected, the crisis of 2007/2008, the recession that followed it, and the ongoing austerity policy of the EU have led to losses of jobs and earnings, which are largely concentrated in low-skilled, low-income households. In particular, the unemployment rate of persons with a low educational level (International Standard Classification of Education, 1–2) in the EU was equal to 18 % in 2012, considerably higher than the average rate (11 %). Furthermore, the proportion of low-wage earners was equal to 17 % of all employees in the EU and to 14.8 % in the Eurozone in 2010, while the highest proportion was registered in Latvia (27.8 %) and Lithuania (27.2 %) and the lowest, less than 8 %, in Sweden, Finland, France, Belgium and Denmark.[76]

Minimum wages, on the other hand, do not provide enough of a backstop to the pressure exerted on low pay. Thus only 21 of the EU's 28 Member States have national legislation setting a minimum wage by statute or by national collective agreement, while the rate of the minimum wage in relation to average monthly earnings – approximately 30–50 % across countries – has been declining in the past few years.

It is asked: 'if a rising tide does not lift all boats, how will they be affected by an ebbing tide?' In fact, the crisis and the strict adherence of European leaders to austerity are feeding not only into widening inequality, but also deepening poverty, both absolute and relative, in which the former correlates closely with the rate of employment and GDP growth, the latter with changes in the underlying income distribution.

In 2011, 119.6 million persons (24.2 % of the total EU population and 22.6 % in the Eurozone) suffered from poverty. The highest share of persons at risk of poverty or social exclusion were recorded in Bulgaria (49 %), Romania and Latvia (both 40 %), Lithuania (33 %), Greece and Hungary (both 31 %), and the lowest in the Czech Republic (15 %), the Netherlands and Sweden (both 16 %), Luxembourg and Austria (both 17 %).

The situation is further exacerbated by the over-indebtedness of European households. 'Households are considered over-indebted if they are having – on an ongoing basis – difficulties meeting (or are falling behind with) their commitments, whether these relate to servicing secured or unsecured borrowing or to payment

72 OECD, 2011, *An overview of growing income inequalities in OECD countries: Main findings.* **73** E. C., 2012, *Employment and Social Developments in Europe 2012,* November. **74** As of April 2013. **75** Eurostat, 2013, 'Underemployment and potential additional labour force statistics', April. **76** Eurostat, 2013, 'European Social Statistics, Wages and labour costs', July.

of rent, utility or other household bills' (E. C., 2013).[77] On the basis of this definition, European households are divided into four different categories. Of the 28 EU Member States, households in only four – the Netherlands, Sweden, Luxembourg and Germany – had 'low' arrears and a 'low' inability to meet its commitments. In all other countries, households had varying degrees of difficulty in keeping up with their commitments. Furthermore, an increasing number of middle-income households find themselves in dire straits.

6.3 Wage dispersion

Generally, developments in the EU labour market have tended to aggravate the polarisation trends in wage distribution. It is estimated that in the long run, employment creation will be characterised by job growth at the top and bottom of the pay scale, leading to greater segregation of the labour market.[78] Interestingly, though not surprisingly, employee compensation in the area of 'finance and business support' exceeds the national average in most EU Member States, displaying considerable resilience during the crisis, as shown in Table 3 below. Furthermore, industry and construction competed with finance in relation to employee pay in a small number of countries only – Ireland, Netherlands, Austria, and Sweden, in addition to Germany and Spain – as did the public sector in Spain, Italy, Portugal and Slovenia (shaded areas in Table 3).

Thus it may be argued that the role of finance in shaping personal income distribution in the EU has been both indirect – via the labour income share – and direct, in terms of wage dispersion. This is all the more so in view of the hefty bonuses paid to the Chairmen and CEOs of banks and other financial institutions, the so-called 'golden boys', whose shine was only slightly tarnished by the crisis. For example, European bankers could be paid bonuses of up to 250 % of their fixed pay under a further relaxation of new EU pay rules due to come into effect in 2014. According to Reuters, banks are already devising plans to work around the bonus cap.[79]

Overall, personal income distribution in the EU is driven by changes in the extremes. The large and increasing share of the low-paid and precariously employed, on the one hand, and the excessively high rewards of capital and finance, on the other, have meant that top income brackets capture an increasing part of the income generated by the economy, while the poorest sections of the population are losing ground. These trends are accentuated by the fact that top income tax rates have come down considerably over time, while capital gains, stock options, and other financial rewards benefit from preferential tax regimes. Thus, the share of the top 1 % of income recipients has increased substantially since the 1980s, as shown in Figure 19.

Table 3

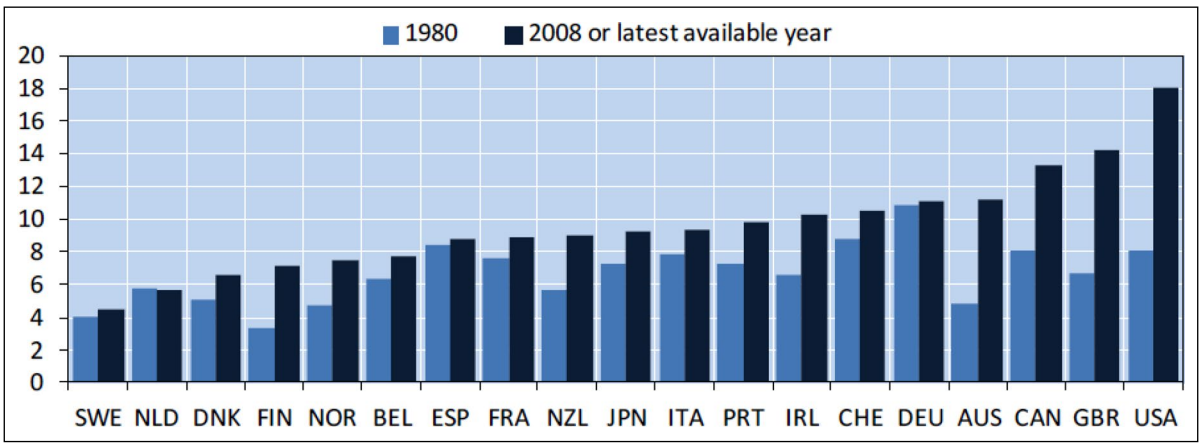
Relationship of nominal employee compensation within sectors to national average compensation (%)

	Agriculture		Industry		Construction		Basic services		Finance & business sector		Public services	
	2001–2007	2008–2011	2001–2007	2008–2011	2001–2007	2008–2011	2001–2007	2008–2011	2001–2007	2008–2011	2001–2007	2008–2011
Belgium	40.0	41.6	118.6	119.4	89.1	89.9	89.3	91.6	107.0	101.6	96.9	98.6
Bulgaria	59.5	63.3	96.6	93.0	81.8	80.2	91.2	87.6	139.5	134.4	111.1	121.5
Czech Republic	77.6	77.9	101.2	102.0	86.5	84.6	88.0	85.8	120.9	121.1	111.6	112.9
Denmark	59.7	58.0	108.6	110.1	112.6	108.4	88.0	84.8	111.0	110.6	100.2	103.5
Germany	57.8	56.1	128.7	131.2	97.1	99.1	77.1	76.7	97.5	95.6	99.6	100.0
Estonia	66.1	74.2	91.0	86.2	98.1	106.7	97.6	92.8	163.8	158.2	97.3	100.5
Ireland	63.8	72.1	95.7	98.0	123.7	123.2	73.3	74.8	112.6	115.4	117.0	112.6
Greece	54.7	55.4	103.3	106.5	69.7	69.7	83.8	82.6	137.4	126.2	115.9	116.4
Spain	34.3	33.2	107.5	109.3	90.0	100.6	89.7	86.0	108.0	99.5	116.7	118.5
France	54.4	57.3	109.6	111.3	100.8	100.6	88.7	88.8	116.5	115.8	96.5	96.1
Italy	48.0	47.8	99.6	99.7	79.3	82.6	93.6	91.2	108.4	105.6	114.2	117.2
Latvia	49.1	70.2	93.5	90.4	91.0	110.1	89.6	89.8	142.0	125.9	118.7	111.2
Lithuania	61.5	67.1	105.7	102.0	94.7	98.7	97.9	97.9	128.0	113.7	97.9	101.7
Hungary	51.7	64.0	89.7	91.8	74.2	67.8	91.8	91.0	161.0	152.8	112.2	109.0
Netherlands	66.0	70.2	120.6	122.3	117.9	121.5	81.2	79.6	107.7	108.5	100.2	100.3
Austria	55.2	52.1	114.3	117.8	100.7	96.0	78.8	78.6	110.0	108.5	108.6	108.3
Portugal	53.4	52.1	81.9	83.2	71.4	74.1	86.2	85.6	121.7	118.2	145.8	141.3
Slovenia	78.6	74.6	92.5	94.9	81.0	80.2	94.0	94.2	110.9	108.2	120.1	116.8
Slovakia	72.4	86.2	102.1	110.8	107.7	108.4	100.3	86.9	116.7	104.6	94.6	101.0
Finland	65.5	62.3	116.9	110.2	107.1	110.8	86.1	87.3	113.9	114.4	94.6	97.1
Sweden	87.3	84.8	115.2	115.0	113.6	107.9	97.1	95.2	111.1	111.1	88.6	90.7

Source: E. C., 2012, *Employment and Social Developments in Europe 2012,* chapter 5

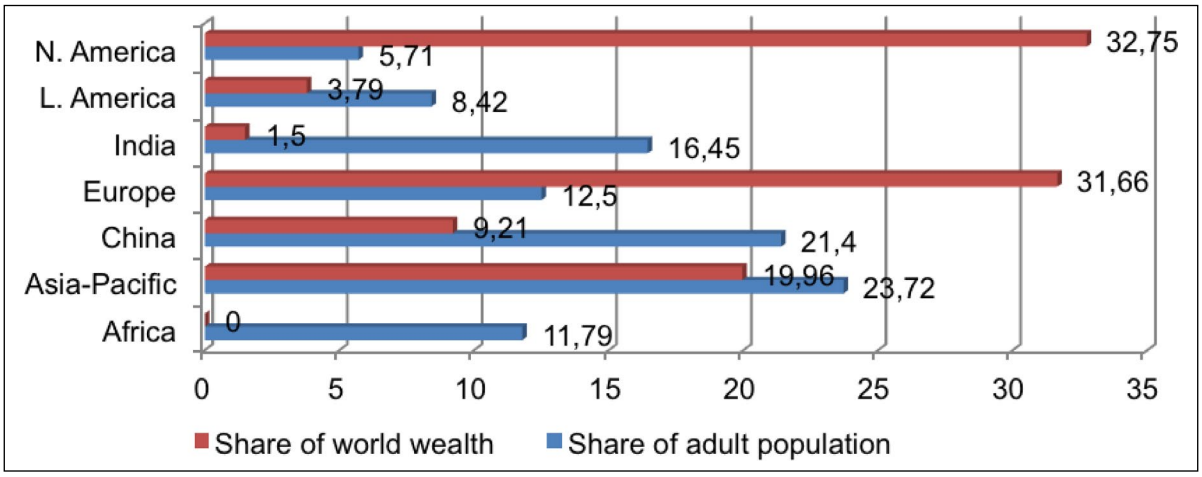
77 E. C., 2013, 'The over-indebtedness of European Households', CIVIC Consulting. **78** E. C., 2012, 'Employment & Social Developments in Europe 2012'. **79** http://uk.reuters.com/article/2013/10/23/uk-eu-banks-bonuses-idUKBRE99M14I20131023.

Figure 19
Share of top 1 % income recipients in total income



Source: OECD, 2012, *Less income inequality and more growth – Are they compatible? Part 1 Mapping income inequality across the OECD,* WP 924

Figure 20
Wealth and adult population by region, 2013



Source: Credit Suisse, Research Institute, *Global Wealth Databook 2013*

6.4 Wealth distribution

The stock and distribution of wealth is important in understanding the implications of social inequality. This is especially true in view of the sharp rise in stock and house prices prior to the crisis and the shrinking of the welfare state, shifting the risk from governments to individuals in such areas as health and education. Thus, wealth is a source of finance for future consumption and for reducing vulnerability to shocks such as unemployment, ill health, or natural disasters. Wealth also enhances opportunities for business activities either directly or as collateral for loans.

One of the main difficulties in analysing wealth is the lack of data. This is especially the case for statistics that are comparable across countries, due to differences in definitions, as well as in measurement conventions. While a number of reports are published by private entities – research departments of big banks or international consultancy firms – such data has not yet been systematically made available by the EU statistical authorities. Hence our sources for this section rely mainly on the *Global Wealth Report 2013* and the *Global Wealth Databook 2013,* published by the Credit Suisse bank, which is the most comprehensive in terms of contents and the most explicit in terms of the method employed.[80]

North America is the region with the highest share of total household wealth (32.8 %) and the lowest share of adult population (5.7 %), while Europe ranks a close second with 31.7 % share of total wealth and 12.5 % of adult population, followed at a great distance by Asia-Pacific (not including China), China, Latin America and India.[81] The share of Africa in global wealth is just 1.13 %, while its share in adult population amounts to nearly 12 % (Figure 20).

80 Other reports in this area include the Wealth-X and UBS *World Ultra Wealth Report 2013* and the Capgemini & RBC Wealth Management's *World Wealth Report 2013,* while the European Social Situation Observatory's analysis of *Income distribution and Living Conditions* also offers interesting information on wealth.

Global wealth is very unequally distributed. According to the *Global Wealth Report 2013,* the bottom half of the global population own less than 1 % of total wealth, while the richest 10 % hold 86 % and the top 1 % account for 46 % of global assets.[82] The high rate of inequality is further confirmed by the elevated value of the Gini coefficient, approaching the value of 1 on the world level. The distribution of wealth in Europe is also highly unequal, even though it is slightly less so than in other regions (Table 4).

Table 4
Composition of wealth, top percentiles and Gini coefficient, 2013

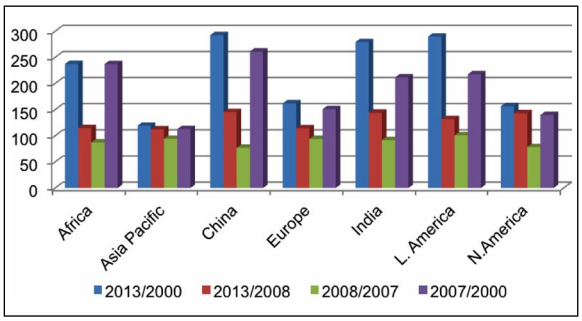
	Share of gross wealth (%)		Top percentiles (%)			Gini coefficient
	Financial	Non-financial	Top 10%	Top 5%	Top 1%	
Africa	48.3	51.7	76.4	64.5	39.9	0.85
Asia-Pacific	50.7	49.3	83.9	69.4	39.3	0.89
China	45.5	54.5	60.8	50.7	33.0	0.69
Europe	43.3	56.8	68.5	53.8	30.1	0.83
India	14.0	86.0	73.8	65.3	48.7	0.81
L. America	37.7	62.3	70.4	58.9	38.1	0.81
N. America	66.7	33.3	73.8	61.0	35.8	0.84
World	52.2	47.8	85.9	74.0	46.4	0.90

Source: Credit Suisse, Research Institute, *Global Wealth Databook 2013*

In terms of composition, more than 50 % of global wealth consists of financial assets. This is especially the case in North America, where financial assets make up two-thirds of total wealth, while in Europe they make up 43.3 %. Furthermore, according to the Wealth-X and UBS *World Ultra Wealth Report 2013,* finance is the main source of wealth for the very rich individuals – whose wealth is greater than US$ 30 million (the so-called Ultra High Net Worth individuals) – whether they have inherited their fortune or have made it themselves.

Inequality has been rising over time. As shown in Figure 21, the growth in wealth was especially strong during the period 2000–2007. In 2008/2007, it declined slightly, while it resumed its pre-crisis pattern soon after. The growth in wealth was especially strong in those areas whose share of global wealth is relatively low. That is, there is an ongoing catching up process amongst regions, although this is not expected to change the global wealth profile for a long time in view of the great differences between the USA and Europe, on the one hand, and the other regions, on the other.

Figure 21
Growth in wealth per adult at constant exchange rates (%)



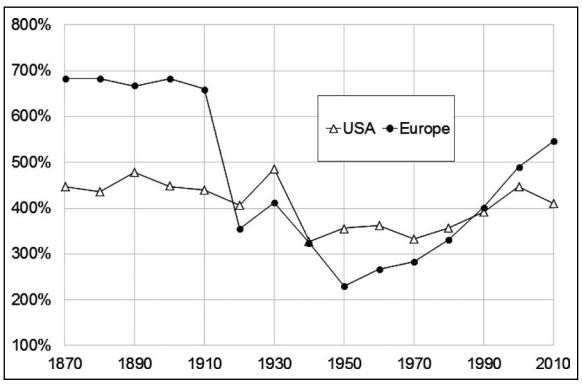
Source: Credit Suisse, *Global Wealth Databook,* 2013

Wealth in both the USA and in Europe has also been rising significantly in relation to income. Piketty and Zucman (2013) have found that in eight developed countries – USA, Germany, UK, Canada, Japan, France, Italy, and Australia – there has been a gradual rise in wealth-income ratios in recent decades, from about 200–300 % in 1970 to 400–600 % in 2010, pointing to a return to levels of wealth-income ratios unknown since the 19th century in Europe.[83] As shown in Figure 22, the wealth-income ratio in Europe reached a peak in the late 19th century, declining after this largely as a result of the world wars of the first half of the 20th century. By the 1950s it had started to rise again, and since 1990, the wealth-income ratio in Europe has overtaken that of the USA.

These developments are explained by the long-run asset price recovery – especially due to the deregulation policies of the period after the 1970s – and by the slow growth in income. Should these tendencies continue, a return to 19th century wealth inequality patterns appears likely. As Piketty and Zucman argue, 'capital is back because low growth is back' (Piketty & Zucman, 2013a: 2).[84]

81 Where 'Europe' includes 27 countries, of which 18 are Member States of the EU; see Table 1-1 of the *Global Wealth Databook, 2013* for the country coverage of wealth data. **82** According to the *Global Wealth Report,* the '… estimates for mid-2013 indicate that once debts have been subtracted, an adult requires just US$ 4,000 in assets to be in the wealthiest half of world citizens. However a person needs at least US$ 75,000 to be a member of the top 10 % of global wealth holders and US$ 753,000 to belong to the top 1 %' (Global Wealth Report 2013: 10). **83** Thomas Piketty and Gabriel Zucman, 2013, *Capital Is Back: Wealth-Income Ratios in Rich Countries 1700–2010,* CEPR Discussion Paper 9588, August. **84** Thomas Piketty and Gabriel Zucman, 2013a, 'Rising Wealth-to-Income Ratios, Inequality and Growth', VOX, September 23.

Figure 22
Private wealth/national income ratios, 1870–2010



Source: Thomas Piketty and Gabriel Zucman, 2013; Note – Europe: unweighted average of France, Germany and the UK; private wealth defined as the sum of non-financial assets, financial assets, minus financial liabilities in the household and non-profit sectors

As discussed above, the growth rate of the European economy was slow even before the crisis, from which it has not recovered largely due to the austerity policies implemented by European leaders. Furthermore, finance remains dominant in Europe, while financial policy reform is hesitant and slow to take effect. These tendencies do not augur well for the future. Increasing inequality in the distribution of wealth will aggravate inequality in the distribution of income in Europe, which in turn must undermine social cohesion and democracy within and between the Member States of the EU. The signs are clear for anyone who cares to see them.

The trends in Europe and the EU policies supporting them have to be stopped as a matter of urgency and to be reversed, as far as possible. This is the challenge faced by the left in Europe. How this challenge is met will shape the future of Europe and of the world, insofar as the impact of European affairs extends well beyond Europe itself.

A POSTSCRIPT: THE NEED FOR FURTHER RESEARCH

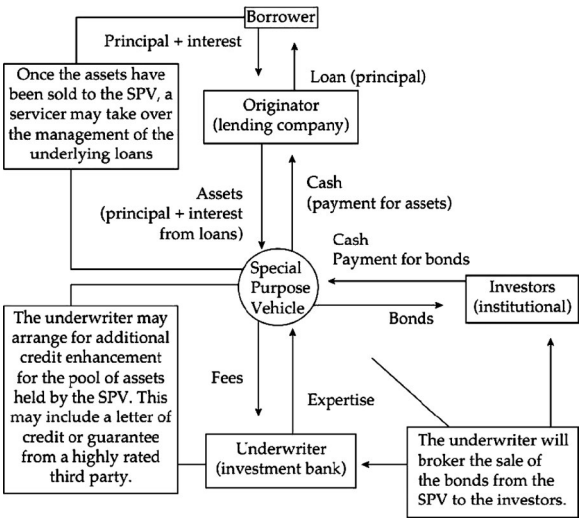
In this survey, we have looked into the notions of distribution and financialisation, the linkages between them and the way these apply to the EU. Our focus on financialisation is based on the conviction that it is a major driver of inequality. At the same time, this study is of necessity limited, as it excludes the other factors underpinning inequality. Analogously, our focus on the EU is justified on the basis of the overall trends taking place within this economic, social and political space, but the impossibility of taking account of developments on the regional and/or national levels in detail is yet another necessary limitation of our work. Lastly, this study has been concerned with diagnosis, that is, with analysing the current situation and providing the tools for a better understanding. Although diagnosis implies prescription, formulating detailed policy recommendations is not part of our aim here. Indeed, these avenues of investigation – into the other factors making for inequality, how these play out on the EU regional/national level, and proposing of policy recommendations – are crucial areas for further research.

APPENDIX I
Total number and assets of monetary financial institutions by country
(March 2012)

Bank	Country	Assets/ National GDP (%)	Assets/EU GDP (%)	% Change in Assets 2007–2011
Deutsche Bank	DE	84.8	17.4	12.4
HSBC	UK	119.8	15.8	22.2
BNP Paribas	FR	99.8	15.8	16.0
Credit Agricole Group	FR	95.4	15.1	22.0
Barclays	UK	113.9	15.0	12.0
RBS	UK	109.8	14.5	-28.0
Santander	ES	118.2	10.1	37.1
Societe Generale	FR	60.0	9.5	10.2
Lloyds Banking Group	UK	70.7	9.3	141.5
Groupe BPCE	FR	57.8	9.1	-
ING	NL	161.5	7.7	-3.3
Unicredit	IT	59.4	7.4	-9.3
Rabobank Group	NL	122.9	5.9	28.3
Nordea	SE	197.4	5.8	84.1
Commerzbank	DE	25.9	5.3	7.3
Intesa	IT	41.0	5.1	11.6
BBVA	ES	56.5	4.8	19.1
Standard Chartered	UK	28.1	3.7	104.5
Danske Bank	DK	193.7	3.7	2.6
DZ Bank AG	DE	15.9	3.3	-5.0
Landesbank Baden-W	DE	14.6	3.0	-15.9
KBC	BE	80.5	2.3	-19.7
Handelsbanken	SE	75.9	2.2	40
SEB	SE	73.1	2.1	6.9
Banca Monte dei PS	IT	15.4	1.9	48.5
Erste Bank	AT	71.2	1.7	4.7
Swedbank	SE	57.4	1.7	22.5
RZB AG	AT	50.9	1.2	9.2
UBI	IT	8.3	1.0	6.8

Source: Liikanen Report, 2013, Table A.1.2

APPENDIX II
A mortgage securitisation package



Source: David B. Grusky, Bruce Western and Christopher Wimer (eds.), 2011, *The Great Recession,* Russell Sage Foundation, New York

Judith Dellheim

WORKING ON STRATEGIES TO OPPOSE FINANCIALISATION AND CAPITAL OLIGARCHIES

Marica Frangakis has written an excellent study of great interest for those working on societal alternatives and left political strategies. In this perspective, the key question is how to identify, how to activate, and how to bring together protagonists and formations sufficiently powerful to resist and overcome those forces which have repeatedly prevented any effective launch of a process of socio-ecological transformation. This question also implies a second one concerning the way the forces operate that have been able to orchestrate and renew the existing majority consensus, which opposes any meaningful socio-ecological transformation, because it is deemed dangerous and costly – despite the fact that blocking it means the destruction of humanity's conditions of existence and the continuation of violence perpetrated amongst human beings. These questions imply a third one, that is, how these questions apply to the EU and its Member States: What does this all mean for those who live in a specific EU Member State and are struggling for socio-ecological transformation in that framework?

Before the beginning of the current global financial crisis, the academic and political mainstream has generally understood the concept of oligarchy in connection with massive property in natural resources, in particular oil and gas in North Africa and Latin America. Since 2007, the concept of oligarchy is also increasingly used in describing Wall Street's 'finance oligarchs'. That there is a new oligarchy debate in the European Union should not really surprise anyone after the US rating agencies Standard & Poor, Moody's and Fitch – the 'Big Three' – downgraded more and more government bonds to junk status.

Behind the modern 'discourse on oligarchies' or, rather, behind the problematic of capital oligarchies we find the actually existing relationship between the current capitalist forms of impersonal rule, huge wealth, and the power of a small group of actors, which has the power to decide key social developments.

The economic basis for these capital oligarchies originated in the 1870s. At that very time, Marx analysed the rise of joint-stock companies:

An enormous expansion of the scale of production and of enterprises, that was impossible for individual capitals. At the same time, enterprises that were formerly government enterprises, become public (*Capital* III, chapter XXVII, iii,1).

The dynamic co-operation of dividend receivers of the new and massive corporations has led to *de facto* common forms of capital and to the emergence of the function of a 'mere manager, administrator of other people's capital' (*Capital* III, chapter XXVII, iii,3). It has even transformed the typically organising actors into salaried managers.

Maximising he profits of capital accumulation, destructive exploitation of the environment, colonialism, militarisation, and war have been widely discussed before World War One, in particular by Luxemburg, Lenin and Hilferding. Their point of departure was Marx's analysis of the joint stock companies:

I call bank capital … which is actually transformed in this way into industrial capital, finance capital … An ever-increasing proportion of the capital used in industry is finance capital, capital at the disposition of the banks which is used by the industrialists (Hilferding 1947: 305–306).

By critically taking a lead from Marx and Hilferding, we can understand finance capital as a specific interdependent relationship between capital owners, who activate interest bearing capital, and those capital owners who organise social surplus labour within the social production of goods and services. The latter task has in the meantime gained such massive importance that it can only be accomplished in a kind of dynamic co-operation. The necessary minimum of capital can be raised and exploited only by these two groups working together. This need for co-operation brings about a new division of functions in capital accumulation as a social process in which the capital owners – as co-operation partners without being equals – are able to appropriate the results of the labour of third parties, by exercising power over them. These third parties also work within the financial sphere but predominantly in the sphere of the social production of goods, which ultimately produces energy related and material use value.

The partners are internally differentiated and they are linked to their respective nation-state, and to the EU, in different, if not contrasting ways. The capital oligarchy is thus a group of actors that relies on the accumulation of finance capital, which occurs through the co-operation between capital owners, politics, the military, culture and science, the media, law, consulting and accounting, and civil society. The capital oligarchies determine the direction of societal development and the way this it occurs. They dictate living and working conditions to others and redistribute additional resources, property, wealth and salaries, alongside their capital accumulation.

The available attempts at analysing this complex pattern show that in particular since World War Two, the changes in, and transformations of, US capital oligarchies have not only affected developments in the USA, but have strongly influenced global developments – and still do. Therefore, the development of capital oligarchies within the European Union is closely con-

nected to the corresponding US developments. Their structures of correspondence are determined by the accumulation of finance capital, and their differences can be explained by the different conditions and different societies in which they exist.

The development of the US capital oligarchies is closely connected to the development of the following interlinked complexes:

– the military industrial complex ;
– the energy sector;
– the transportation industry;
– the globally oriented agro-business industry.

Materially, these closely interlinked sectors together decisively shape production and consumption patterns, as they exist within contemporary societies.

This group of four, taken together, is the largest consumer of the earth's surface and resources, the largest generator of air, water, and soil pollution, of pressure on the ecosystems. This quartet determines the kind of production and the way of life – that is, ways of life, nutrition, mobility, work, leisure time and 'co-habitation' – and thereby creates the basis of a socially and ecologically disastrous social consensus. The quartet's destructive dynamics are driven and exponentially increased by a continuously immense flow of money, finance, and bonds. State budgets, state contracts, the financial industry, and 'financial innovations' are closely intertwined with this quartet. Their own development is linked to that of the high tech sector. Microelectronics, modern information and communication technologies, biotechnologies, and nanotechnologies are only a few of the key words in the ongoing turnover of technologies, infrastructures and the related processes of development, which are mainly based on the reproduction demands of this quartet and which seem to function as drivers for the quartet in its penetration of increasingly new areas of society.

The transformation of US capital oligarchies and the associated social transformations began in the US in the 1970s. This transformation has been closely linked to financialisation. The unending production of goods and the generation of surplus without limits, the movement of capital and its realisation, as well as the life of people, are increasingly influenced, mediated and determined by financial market transactions, and thus by protagonists who are part of the capital oligarchies. Financialisation is thus a specific form of the socialisation of labour, of social production, and of the reproduction of societies. Together with the division of labour, the incomes and property of increasing members of society are involved in the accumulation process of specific forms of financial capital. This involves the development of relatively independent financial markets.

Put in a more specific and also more comprehensive way, we can say that after the US's loss of the Vietnam War and facing deep crises and a new global power structure, contradiction-ridden processes of co-operation among the '4 plus 2' ruling elites have triggered three major innovations: (a) Microelectronic technologies, initially invented for military purposes, have found broader entry into social practices; these innovations particularly have changed the technical foundations of the financial world. (b) The 1974 Employee Retirement Income Security Act allowed pension funds and insurance corporations to invest in the stock market. (c) Since the mid-1970s, stockbrokers have been legally mandated to orient their useable capital according to the rating agencies' assessments of what is 'investment grade' or 'non-investment grade'. Since then, the experts of the 'Big Three' have become consultants and partners of governments and members of parliament, and of state, public, and private institutions.

In this way, new possibilities for capital accumulation were able to emerge and expand. Increasingly, anonymous capital oligarchies have mobilised against the legal regulations of economic activities within sectors or rather within confined markets. Their successes in imposing deregulation and the subsequent drastic increases in direct investment possibilities abroad have resulted in expanding the role power of transnational corporations, in particular of those among the '4 plus 2'.

Therefore, at the end of the 1970s, emerging transnational corporations (TNCs) have expanded and become the major recipients of traditional credits from banks and various other actors in the financial sector. However, the credit-providing banks have also developed. With expanding investment banking, stepped-up 'securitisation' and the growth of shadow banking, banks have transformed themselves; new actors such as special-purpose entities have emerged and developed in the financial sector. Society itself has begun to be transformed.

Alongside these developments, there has been a massive process of concentration in the banking and financial sector. The twenty biggest funds now own on average 40 % of the capital shares in the biggest one thousand US corporations (Windolf 2008: 518). The changes in the symbiosis of capital oligarchies and their increase in power are manifest in the Financial Services Modernization Act (Gramm-Leach Bliley Act), which the US Congress passed in 1999. (This act has replaced the already increasingly weakened 1933 Glass Steagall Act, which was a pillar of the New Deal and provided for transparency in the financial markets.)

With regard to the European level, the story of the euro crisis is inseparably linked to the story of the Big Three. 'Their owners are … are simultaneously shareholders of all investment banks and of all US corporations named on the index of the 500 most important corporations …' (Rügemer 2012: 61).

In order to make use of increasing financialisation and to secure their position, the economically leading actors, and predominately those within the financial sector, enter into new co-operations. Swiss scholars (Vitalie, Glattfelder, Battiston 2011) have demonstrated that a highly networked core group of 147 companies controls almost 40 % of worldwide market operations. Among the 'top 50 control holders 22 are from the US,

eight from the UK and 17 from the EU, out of which four are from France, and two respectively from the Netherlands and from Germany. The top 50 are almost exclusively financial institutions that accept the role of the Big Three and which presumably benefit from this.

The capital oligarchies have changed contemporary society on a worldwide scale, by transforming others and by being transformed themselves. They have changed the everyday life of populations, including those of the European Union. They have been able to organise the respective social consensus for their initiatives, even in the midst of the current global financial and economic crisis. In this regard, Leif Johannsson, chair of the European Round Table of Industrialists and of Ericsson, has concluded: 'The economic crisis may have given us the chance to change things in the right direction. There is no time to waste. I am optimistic about Europe's future but we must urgently carry out the necessary reforms to improve the investment climate' (ERT 18.3.2013).

'To improve the investment climate' means in real terms to implement the interests of the TNCs headquartered in the European Union. Their interests are:

- security of energy and resource supply, security of their capital accumulation process, protection of property, internal or domestic security, international or global security;
- availability of a qualified, mobile, highly motivated, and yet cheap labour force according to contemporary industrial demand;
- constant demand for products and services ensuring calculated profits;
- availability of necessary finance and financial services;
- sufficient space for, and profitability of, investment.

The Member States in which TNCs are based and the EU institutions are being asked to serve these interests specifically. And they have made use of the current crisis by:

- working on the realisation of the EU2020 goals, especially in the areas of industrial policy and infrastructure development;
- reducing the cost of the labour force;
- reducing democratic and social standards, while reinforcing repression;
- improving the financial architecture in the direction of enabling quick profit making;
- stabilising the euro monetary system;
- accelerating the negotiation and realisation of free trade projects;
- reinforcing privatisation processes in various directions;
- marginalising ecological concerns and reinforcing a new extractivism.

The way the EU Member States have so far proceeded, along with the foreseeable combination of the dominant approaches to crisis management, show the direction in which industrial and infrastructure policy will be realised. These are oriented towards the aims of global competiveness and of 'security' (including its military dimension), surveillance, and repression. Stabilising the EMU and improving the financial architecture are not bad in themselves. They are, of course, necessary tasks to be addressed. But the actual 'package' proposed will mean increasing social, ecological, and global problems – it will strengthen the destructiveness of the '4+2' actors, and it will further reinforce financialisation.

The problem is that although some necessary steps towards a truly functioning EMU have been taken, these have involved a compromise with the main actors who have effectively caused the current financial crisis. Thus some of the main causes of the crisis have not been addressed or not been addressed in such a way as to find sustainable solutions. The main causes of the crisis are a number of factors resulting in an overaccumulation of capital:

- the deregulation and liberalisation of financial markets;
- the aggravation of discrepancies in the distribution of income and wealth and hence of liquid funds on a grand scale;
- imbalances in the balance of trade and in the balance of payments;
- extensive privatisation – especially of social security systems (Huffschmid 2009: 10–21).

These causes of the crisis constellation are at the same time strong drivers of financialisation. The crisis management package proposed (and implemented) reinforces financialisation, especially through:

- megaprojects incurring new debts;
- the EU2020 Project Bonds initiative focusing on privatisation of social security systems, aimed at further enabling investment for private capital accumulation;
- the mutual insistence on deregulation in the context of the ongoing free trade negotiations between the US and the EU;
- the EU's financial sector being (still) more weakly regulated that that of the US.

Given the number and extent of the problems, it would already be a significant achievement simply to put a halt to these processes at first, creating breathing space through a moratorium, and then perhaps even realize some small step that could symbolize the political will for, and possibility of, the needed further and deeper changes. This moment should be conceptualised and realised in such a way that it is capable of further expansion, so that the necessary and possible follow-up steps will become clearer in advance.

In seeking possibilities of political action within these contradictions, and taking account of the defensive position in which left forces find themselves, it is possible to identify three principal interconnected political areas of action:

1. The political struggle for democratic, for social as well as ecological standards – in particular, poverty-proof minimum social security standards;

2. the political struggle for the defence and democratisation of the public sphere, above all of public finance;
3. and the political struggle for a constructive and sustainable local and regional development.

Participatory processes are an essential bridge connecting these three. These three areas delineate really existing or potential possibilities for people to appropriate knowledge and capacities for solidarity-based co-operation and for dealing with the existing and identifiable causes of social, ecological, and global problems. These three areas – with their mutual interlinkages – offer starting points for a struggle against the ongoing processes of privatisation and financialisation, as well as against the '4 + 2' and the capital oligarchies behind them.

These areas offer sufficient space for the political and societal forces struggling for an emancipatory alternative to simply meet and build political alliances that may build the capacity to change the goals and means of contemporary societal development. This approach will have to be connected to a struggle for a deeper change in the current framework of social development in the EU and, therefore, with a new kind of European constitutional process as a reflection, and as an instrument, of social change.

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