1. Conceptual issues and preliminary observations

1.1 INTRODUCTION

We often hear about the resource curse, how this curse has left countries like Nigeria in economic ruins, and how the curse is preventing resource-rich countries from diversifying their economies. The resource curse, also known as the “resource trap” or the “paradox of plenty”, is a term that is used to describe a paradoxical situation in which a country that is endowed with valuable natural resources underperforms economically. While several potential explanations can be suggested for this phenomenon, the most common explanation is that it arises because too much of the country’s capital and labour force are concentrated in just a few resource-dependent industries. By failing to invest adequately in other sectors, resource-dependent countries can become vulnerable to adverse changes in commodity prices and experience long-run economic underperformance.

If the resource curse is caused by too much of a good thing (natural resources), then by extrapolation a curse would arise whenever one sector dominates other sectors of the economy. It follows that the dominance of the financial sector, like the dominance of the resource sector, should lead to a curse because of too much of a good thing: finance. The “too much” feature of the finance curse is used explicitly by the Organisation for Economic Co-operation and Development (OECD, 2015) as expressed in Policy Note 27:

Finance is a vital ingredient of economic growth, but there can be too much of it. Over the past 50 years, credit by banks and other institutions to households and businesses has grown three times as fast as economic activity. At these levels, further expansion is likely to slow long-term growth and raise inequality.

The difference between the two curses is significant. The resource curse is caused by nature where a country is endowed with natural resources, but the finance curse is the product of deliberate policy actions that facilitate the financialisation of the economy. Resource endowment does not necessarily lead to a curse, because a proper utilisation of the resources can lead, with the right policy, to economic diversification. For instance, Norway is a very happy
country where people live comfortably (without having to pay for healthcare and education) even though it has a resource-based economy that depends heavily on North Sea oil. A prerequisite for this state of affairs is that natural resources are kept under public ownership instead of granting the rights exclusively to a “foresighted entrepreneur” who extracts resources “efficiently” and sells them for private profit without paying taxes. This, for example, happens in Australia where natural resources are used to enrich some business tycoons while the middle class is taxed heavily to build the infrastructure used by the tycoons in the process of enriching themselves.

The finance curse can be reversed by reducing the dominance of the financial sector through policy action and regulation, but the resource curse cannot be reversed by giving up resources. Another difference is that resource-endowed countries realise the difficulty of diversification, acknowledge the need for it, and endeavour to accomplish that objective. Countries with a dominant financial sector, on the other hand, are typically proud of it as reflected in the motto “who needs manufacturing industry when we have the City?” in reference to the concentration of financial institutions in the City of London. In those countries, the financial oligarchs, who are the perpetrators and beneficiaries of the finance curse, are aided and abetted by politicians, policy makers, academics and free market evangelists to maintain the curse indefinitely. One has to remember that it is a curse for the majority of people but a blessing for the oligarchs and their enablers and backers. For the latter, the curse is a sign of progress and economic maturity, because mature economies are supposed to move towards services, including financial services. This is at least the message they convey.

The terms “financialisation”, “finance-dominated capitalism” and “finance-led capitalism” imply that a dominant and central role is played by the financial sector in the economy. The financial sector provides lubricants for economic activity that take the forms of credit, means of payment, risk management tools and other financial services, but too much lubricant can be harmful. A similar message is conveyed by the term “financial capitalism” (or “finance capitalism”) as opposed to “industrial capitalism”. It follows that distinction is made between financial capital and industrial capital, which sounds (more or less) like the distinction between capital in economics (a stock of capital goods) and finance (an amount of funds available for the acquisition of financial assets). Thus, the move from industrial capitalism to financial capitalism, which eventually brings with it the finance curse, is supposed to be a sign of progress, or so we are told by the beneficiaries of the curse. We have to remember that bad things happen and persist because there are powerful beneficiaries – this is true of wars and equally true of the finance curse.

Distinction can also be made between real capital and fictitious (including speculative) capital (for example, Radzievska, 2016). Real capital serves
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primarily the movement of industrial capital, which plays a decisive role in generating output and income, whereas fictitious capital is represented by financial assets. As the title of ownership of financial assets, fictitious capital does not generate output by itself, but only contributes to the redistribution of income. Radzievska (2016) also refers to “production capital”, which is the real capital that serves primarily the movement of industrial capital, suggesting that it plays a “decisive role in creating income by embodying in materials and things”. She goes on to argue that since the vast majority of financial markets belong to developed countries, these countries receive the bulk of the redistributed income of the real sector.

The term “financialisation” may be used in more than one sense to refer to globalised financial markets (Arnold, 2012), the growing significance of shareholder value in management decision making and corporate strategy (Boyer, 2000; Crotty, 1990; Feng et al., 2001), and rising financial investment and income generated from financial transactions (Orhangazi, 2008; Stockhammer, 2004). It also reflects the difference between financial capitalism and industrial capitalism. A comic but realistic description of transactions executed in a financialised economy can be presented by using the two-cow analogy (for example, https://www.sadanduseless.com/a-tale-of-two-cows-funny/):

You have two cows. You sell three of them to your publicly listed companies, using letters of credit opened by your brother-in-law at the bank, then execute a debt/equity swap with an associated general offer, so that you get all four cows back, with a tax exemption for five cows. The milk rights of the six cows are transferred via an intermediary to a Cayman Island Company secretly owned by the majority shareholder, who sells the rights to all seven cows back to your listed company. The annual report says the company owns the eight cows, with an option on one more.

A similar but real-life story is told by Shaxson (2018) about a London-based company in the business of selling digital rail tickets and charging a small booking fee for each ticket it sells. This company is owned by another company, which in turn is owned by another company, which is owned by another, and so on, to the tune of five companies above the train ticket seller. Shaxson describes how the little booking fee charged to millions of passengers is sent across the English Channel to the tax haven of Jersey, then back to London, where it would pass through five more companies, before it is sent back to Jersey on the way to the European mainland where it would enter the accounts of two companies in Luxembourg, which happens to be another tax haven. Once the booking fee has reached Luxembourg, it enters a financial tunnel where it becomes a little harder to track, but it soon surfaces in the Caribbean where it goes through three or four more mysterious Cayman Islands companies. Thereafter, the booking fee joins a multitude of other
financial streams from around the world, which come together and form port-
folios managed by a giant US investment firm. This description tells us a lot
of things. It tells us that a financialised economy is most suitable for money
launderers and tax evaders, and that most of what goes on in a financialised
economy is generating money out of money without any value added. In other
words, it is profiteering without producing. This description makes an excel-
lent dictionary-definition of the word “parasitic”.

1.2 SOME PRELIMINARY OBSERVATIONS

Although some policy makers believe that financialisation occurs naturally
as the economy moves away from manufacturing industry to services (Liu,
2005), it is far away from being a “natural development”. Rather, as Witko
(2014) argues, it is a consequence of public policy choices that occur when
large financial firms are active in politics, not for the sake of politics but by
using politics as a means to an end. Financialisation, therefore, represents reg-
ulatory and political capture, a situation where the financial oligarchy has the
power to extract concessions from politicians and public policy makers. David
Stockman, a former director of the US Office of Management and Budget,
once described financialisation as “corrosive”, arguing that it had turned the
economy into a “giant casino” where banks skim an oversize share of profits
(Bartlett, 2013).

The vast literature on financialisation deals with various aspects of this
phenomenon, covering the definition and measures of financialisation, its
effects, and the channels whereby those effects are transmitted to the rest of the
economy. According to Skott and Ryoo (2007), financialisation has led to (i)
a significant increase in the volume of international financial flows, (ii) a large
expansion of consumer credit, (iii) a reorientation of corporate objectives
towards the short-term interest of shareholders, and (iv) a greater influence of
international financial institutions in the global economy. All of these conse-
quences have served the financial oligarchy rather well and enabled financial
institutions to claim an increasingly bigger portion of corporate profit.

The weight of the financial sector has grown spectacularly in terms of
profits, size of institutions and markets, and also in terms of political influence and visibility. Finance has penetrated every aspect of the society, as everything has been financialised, including commodities, housing, healthcare and education. For example, student loans (in excess of one trillion dollars in the US) have become a lucrative business that generates fees and commissions by securitising the associated cash flows. Another example is that the prices of essential goods, such as petrol and wheat, are determined in financial markets by speculative forces, irrespective of the actual supply-demand balance in the physical market. Every aspect of daily life has underlying financial products,
to the extent that financial literacy has become a prerequisite for success in ordinary life. If the status quo does not change (or is not changed), which is highly likely, be prepared to trade derivatives on human organs, slaves, prostitutes and asylum seekers as joint ventures between foresighted financiers and shrewd traffickers. After all, these are lucrative lines of business, particularly given the market has no morals, as free marketeers proudly claim.

Financialisation represents a shift in the way wealth is accumulated. In years gone by, when the financial sector existed to support physical production, profits were generated primarily from the mass production and sale of the goods that people wanted to consume (hence, industrial or production capitalism). In a financialised economy, on the other hand, a large (if not the dominant) portion of profits comes from the trading of financial assets and from the fees and commissions charged on mostly parasitic operations that produce zero value added. In a financialised economy, the oligarchy makes money out of ordinary people and naive investors seeking the “American Dream” by pumping and dumping financial assets, even those that have no intrinsic values such as cryptocurrencies. Fine (2012) argues that mortgage finance is just one aspect of financialisation, specifically attached to housing, but symbolic as a major representative of the more general penetration of finance into ever more areas of economic and social life such as pensions, education, health, and the provision of economic and social infrastructure. He refers to the increasing extent to which finance has gained presence in areas where it had previously been relatively absent (hence expect financiers to launch joint ventures with traffickers to create futures, options and swaps on or in human organs, slaves, prostitutes and asylum seekers).

Distinction is made between financialised firms and financialised economies. With respect to firms, financialisation occurs when non-financial firms devote a growing part of their resources to financial activities in detriment to their principal activities. With respect to countries, financialisation occurs when non-financial firms indulge in financial investment to such an extent that it makes the value of financial assets in a country rise relative to real assets. Since the 1970s, the value of global financial assets has soared. Not only have financial markets grown in absolute terms, they have also expanded in relative terms as the value of global financial transactions surpassed that of the real production of goods and services. In 1973, the ratio of the value of foreign exchange transactions to global trade was 2:1, but in 2004 this ratio was 90:1. In 2022, when the last FX survey was conducted by the Bank for International Settlements, trading in FX markets reached $7.5 trillion per day. This means that 4.2 days of FX trading covers the 2022 level of annual global trade at $31.5 trillion.

Financialisation is not something that simply happened as a natural course of evolution. Political decisions, or lack thereof, enabled the process to take
off and accelerate. Policies formulated at the national and international levels encouraged activities and changes that provided the right environment for financialisation to move at full speed. Inaction, the deliberate decision to allow market forces to run our affairs, and refusal to intervene (even to regulate fraud or deal with some destabilising forces) allowed the proliferation of parasitic activities that are commonly found in a financialised economy. In short, financialisation has not evolved naturally – rather, it is the product of public policy choices motivated by a race among the political elite to serve the financial oligarchy.

The proponents see the growth of the financial sector as essentially beneficial, believing that a well-developed financial sector stimulates economic growth and that financial markets are conduits to the efficient allocation of resources (for example, IMF, 2006). This rhetoric has maintained its momentum, even in the face of recurring financial crises. In a financialised economy, however, firms aim to maximise their short-run financial values at the cost of sustainable productive investment. In a financialised economy, economic and social public policies are neglected in favour of market tyranny, with serious adverse consequences for efficiency and equity. In a financialised economy, the society is unnecessarily exposed to the volatility and crises that typically characterise financial markets.

Reinert and Daastøl (2011) note that in a financialised economy, more money is made through the appreciation of real estate than in any other way. Consequently, they wonder about the long-term consequences if an increasing percentage of savings and wealth is used for inflating the prices of already existing assets instead of boosting new production and innovation. Paul Krugman tells a story of a Russian immigrant, an engineer by profession, who said the following: “America seems very rich … but I never see anyone actually making anything.” Krugman (2011) comments that this statement became increasingly accurate over time, which led him to suggest that “Americans made a living by selling each other houses, which they paid for with money borrowed from China.”

The advent of the global financial crisis and the great recession has led to the emergence of a widespread belief that too much finance can be a drag on the economy. Crotty (2005) argues that “finance has grown in importance with the rise of neoliberalism, that financial interests have become much more economically and politically powerful, and that these trends have been coterminous with deterioration in real economic performance”. Financialisation is believed to have the following adverse economic, political and social effects: (i) weak growth and low employment levels resulting from shrinking productive investment; (ii) the dominance of capital over labour as mergers and acquisition intensify downsizing in a never ending race to boost shareholder value and profit; (iii) shifts in the structure and dynamics of class relations; (iv) a reduced
margin for public policy; and (v) increased concentration of income and rising inequality. These effects and others will be discussed in detail in Chapters 8 and 9.

Indicative of interest in financialisation and its effects is the launch in December 2011 of the project “Financialisation, Economy, Society and Sustainable Development” (FESSUD). The objective of the project, which ran for five years from 2011 to 2016, was to develop a comprehensive policy agenda for changing the role of the financial sector. The project, which was managed by a consortium of partners from 14 countries, addressed issues pertaining to the ways in which growth and economic performance depend on the characteristics of financialisation, the nature of the relation between financialisation and the sustainability of the financial system, the lessons to be drawn from crises about the nature and effects of financialisation, and the characteristics of a financial system that supports sustainable development. A large number of papers have been produced by the participants, dealing with a variety of topics such as the relation between financialisation, debt and inequality (Detzer, 2016); international and domestic financialisation (Kaltenbrunner and Painceira, 2016); the relation between financialisation and economic performance (Sawyer, 2015); financialisation and crises (Dodig et al., 2015); the effect on income distribution (Hein and Detzer, 2014); the effect on sustainability (Vercelli, 2014); financialisation in the developing world (Tyson and McKinley, 2014); and the effect on income distribution (Hein and Dodig, 2014). This list of the topics covered by FESSUD is certainly not exhaustive.

Outside the FESSUD, numerous studies demonstrate the adverse consequences of financialisation, particularly the retardation of growth and intensification of inequality, which are arguably related in the sense that inequality itself retards growth. For example, Bartlett (2013) suggests that “financialization is also an important factor in the growth of income inequality, which is also a culprit in slow growth”. Cushen (2013) explores how the workplace outcomes associated with financialisation render employees insecure and angry. Black (2011) lists the ways in which the financial sector harms the real economy, describing the financial sector functions as “the sharp canines that the predator state uses to rend the nation”. The adverse effects of financialisation are widely recognised as being mostly related to the accumulation of debt, which leads to a diversion of increasing portions of the financial resources of the corporate and household sectors to debt service.

In general, studies of financialisation can be classified into four categories. Macroeconomic studies examine financialisation as the driving force of a “finance-led” regime of capital accumulation. Critical accounting studies of financialisation demonstrate that the development of an active market for corporate control and the adoption of fair-value reporting have blended the
Financialisation of cash earnings and wealth accumulation in the corporate sector’s accounts (Gleadle et al., 2014). The sociological studies show that financialisation results from mass marketing of financial products, which have been made available to large segments of the population, and from the dissemination of specific narratives that emphasise individual responsibility alongside risk-taking and financial education (Blackburn, 2006; Langley, 2008). The geographical literature examines the spatial implications of the observed mutations in the financial sector. For example, Cloke (2010, 2013) argues that financialisation has led to the rise of ultra-capital, which he defines as a “hybrid form of circulating capital, driven by the erosion of difference at the state/private regulatory interface into a contiguous politico-financial relational space”.

1.3 FORMAL DEFINITIONS OF FINANCIALISATION AND RELATED TERMS

Financialisation is a broad term that describes and pertains to a wide range of trends, which makes it difficult to define precisely. Even though economists writing about financialisation from a political economy perspective are concerned about the rapid growth of financial activities and the increasing power of the financial oligarchy, they have not come up with a generally accepted definition of financialisation. For example, Crotty (2005) refers to a lack of consensus on a definition of financialisation among its critics.

The most widely cited definition of Epstein (2002) is that “financialization means the increasing role of financial motives, financial markets, financial actors and financial institutions in the operation of the domestic and international economies”. Expansion of financial markets is not only about the volume of financial transactions and trading but also about the diversity of transactions, assets and market participants. As a result of deregulation and financial innovation, all of these aspects of financialisation have been growing spectacularly.

Another definition of financialisation is suggested by Krippner (2005) who defines the phenomenon as “a pattern of accumulation in which profits accrue primarily through financial channels rather than through trade and commodity production”. The word “accumulation” means different things in economics and finance. In economics, accumulation refers to the capital stock, the stock of machines, equipment and structures used to produce consumer goods. In finance, accumulation refers to the stock of financial assets. In a financialised economy, profit is derived primarily from the accumulation of financial assets rather than capital stock. This is why distinction is made between industrial capitalism and financial capitalism. Early twentieth-century thinkers observed that changes in the balance between financial capital and industrial capital was
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associated with imperialism and that imperialism, as a stage of capitalism, was
reached when the export of financial capital replaced the export of goods (see,
for example, Moosa, 2019). Another definition that involves the word “accu-
mulation” is suggested by Marois (2012) who defines “emerging finance cap-
italism” as “the current phase of accumulation, characterized by the fusion of
the interests of domestic and foreign financial capital in the state apparatus as
the institutionalized priorities and overarching social logic guiding the actions
of state managers and government elites, often to the detriment of labor”.

An important aspect of financialisation that is not reflected in these defini-
tions is the over-reach of the phenomenon as it becomes an integral part of the
average person’s daily life. This aspect is referred to in the definition of Davis
and Kim (2015) that it is a “post-Fordist regime of accumulation characterised
by the proliferation of financial institutions and instruments and the increased
importance of finance to everyday life”. A Fordist accumulation regime is
a characterisation of the mass production-based economy that prevailed in the
1950s and 1960s. The term “post-Fordism”, on the other hand, refers to the
emergence of a new set of organisational, economic, technological and social
configurations to replace those of “Fordist” mass production. This definition
refers explicitly to the “increased importance of finance to everyday life”, but
it is not clear whether this increased importance is supposed to be good or bad,
useful or harmful. The ultimate form of “intrusion” of finance on everyday life
is the recent wave of fintech that aims to make everyone pay by anything other
than cash.

A definition that is intended for the non-specialist is presented by
Investopedia (2021), which goes as follows:

Financialization refers to the increase in size and importance of a country’s financial
sector relative to its overall economy. Financialization has occurred as countries have shifted away from industrial capitalism. The term also describes not just the
increase of the market and financial sector’s presence in our lives but the increasing
diversity of transactions and market players as well as their intersection with all
parts of the economy and society.

This definition encompasses several dimensions of financialisation: (i) the
relative size and importance of the financial sector, both of which are dis-
proportional to its contribution to GDP and social welfare; (ii) the shift away
from industrial capitalism to financial capitalism and from the production of
goods to the production of financial assets; (iii) the role of financial markets
in the lives of ordinary people who are not necessarily portfolio managers or
derivative traders; (iv) the rise of parasitic operations and financial products
that aggravate risk when they are supposed to be used for risk management;
and (v) the intrusion of finance on daily life.
In financialisation, daily life is emphasised by Komlik (2015) who describes financialisation as “the ascendancy of finance”, suggesting that it represents “the capturing impact of financial markets, institutions, actors, instruments and logics on the real economy, households and daily life”. Storm (2018) refers to the introduction of financial market logic into areas and domains where it was previously absent. It is not exactly clear what is meant by “financial market logic”, but I suppose that it pertains to how the market behaves. Financialisation is viewed by Phillips (2006) as “a process whereby financial services, broadly construed, take over the dominant economic, cultural, and political role in a national economy”. Phillips notes that the financialisation of the US economy follows the same pattern that marked the beginning of the decline of Habsburg Spain in the sixteenth century, the Dutch trading empire in the eighteenth century, and the British Empire in the nineteenth century. These leading economic powers of their time followed an evolutionary progression: first, agriculture, fishing, and the like; next, commerce and industry; and finally, finance – and with finance came the collapse.

Definitions of financialisation emphasise various aspects of the phenomenon, including (i) power of markets, institutions and elites; (ii) importance of financial activities; (iii) growth of financial markets; and (iv) conversion of industrial capital to financial capital. According to Sawyer (2014a), various definitions of financialisation should be taken as indicating the general scope of the phenomenon under review, then he goes on to argue that the term “financialisation” is not limited to a specific period or place and that the pace and form of financialisation varies across time and space, emphasising periods of de-financialisation as well as those of financialisation. This remark seems to have come in response to some scholars who associate financialisation with a specific time period, even in the definition. For example, Turbeville (2013) describes financialisation as “changes that occurred during the period of deregulation that began in the 1970s”.

The related terms “finance-dominated capitalism”, “finance-led capitalism”, “financial capitalism” and “finance capitalism” mean the same thing, the subordination of processes of production to the accumulation of profits in a financial system (Scott and Marshall, 2005). Johnson (2009) describes financial capitalism as a “form of capitalism where the intermediation of saving to investment becomes a dominant function in the economy, with wider implications for the political process and social evolution”. Palley (2012) argues that the predominance of finance capital has led to preference for speculation (casino capitalism) over investment for entrepreneurial growth in the global economy. Rudolf Hilferding is credited with bringing the term “finance capitalism” into prominence in his 1910 *Finance Capital (Das Finanzkapital)*, where he presented a study of the links between German trusts, banks and monopolies before World War I (Hilferding, 1910). Bideleux and Jeffries (1998) describe
Hilferding’s work as a “seminal analysis” of the transformation of competitive and pluralistic “liberal capitalism” into monopolistic “finance capital”.

Financial or finance capitalism is contrasted with industrial or production capitalism. Hudson (1998) makes a comparison by suggesting that old industrial capitalism sought profits by building factories and investing in capital equipment to employ labour in the production of goods and services, particularly in manufacturing industry. Conversely, finance capitalism seeks capital gains mainly in the form of higher asset prices. According to Hudson, the shift to finance capitalism was motivated in part by the desire to evade income taxes. For example, in the real estate sector (the economy’s dominant sector in terms of asset size) re-depreciation and over-depreciation of buildings and the payment of mortgage interest leaves almost no taxable income at all. He also refers to finance capitalism as “rentier capitalism”, which is centred in the financial sector. The objective is to recycle the economy’s savings into real estate and the stock market to bid up land and equity prices, not to create new assets. In the stock market, capital gains are achieved by downsizing the labour force and scaling back production so as to squeeze out more revenue rather than seeking to expand market share by undertaking new direct investment.

The finance curse effectively means that too much finance can make a country poorer. The Tax Justice Network (2020) makes an interesting analogy between the financial sector and a fried egg:

Consider a financial sector as a fried egg. The yolk in the middle is the useful part, helping citizens save for the future, providing loans to small businesses, and so on. The white of the egg is the harmful part. It might contain, for instance, accountants helping wealthy individuals or large multinationals set up tax haven structures to escape tax, or lawyers helping large companies merge to become dominant monopolists, or bankers engaging in the kind of financial engineering that led to the last global financial crisis.

The basic policy prescription that flows from the finance curse analysis is to shrink the financial sector back down to its useful core.

Coming up with a precise definition of financialisation is secondary to understanding what it looks like, how it has evolved, and the means whereby its negative consequences can be dealt with. Even in the absence of a universally acceptable definition, the critics agree that too much finance is bad for the health of the economy. In general, however, financialisation can be understood to imply the dominant place that shareholder value has taken in non-financial corporate governance, the growing role of financial markets in the economy, the rising financial and economic power of the financial oligarchy, and the explosion of financial trading and “innovation”. It is more important to recognise the symptoms of financialisation, including a monetary policy oriented almost exclusively to price stability, a significant increase in the volume of
international financial flows, a sizeable expansion of consumer credit for households, a reorientation of corporate objectives towards the short-term interests of shareholders, and a greater influence of international financial institutions in the global economy.

It follows that financialisation must be perceived as a fundamental transformation of the financial sector, which has been consequential for the whole economy. Sawyer (2014a) argues that Epstein’s definition “provides the object of study and in itself does not specify the time period or geographical space to which it applies; nor does it provide any analytical framework for its study”. It is fair to say that a one-sentence definition is not supposed to say something about the time period or geographical space – otherwise, the whole concept can be dealt with in a definition.

1.4 CHARACTERISTICS OF THE FINANCIALISATION PROCESS

Financialisation is a process that exhibits several characteristics. The first is the spectacular growth of financial markets, which is emphasised by Fine (2012) who refers to the large-scale expansion and proliferation of financial markets, particularly in the post-1980 period, marked by Thatcher-Reagan wholesale deregulation of everything under the sun. Indicative of this growth is what a McKinsey Global Institute (2010) report says: “The global capital market has never been larger, more dynamic, or more diverse – nor its power greater to shape the wealth of nations.” The report goes on to say that “the global financial stock has grown faster than world GDP, indicating that financial markets are becoming deeper and more liquid”. It is of course far-fetched to claim that the wealth of nations is shaped by financial markets, unless the word “shaped” implies the redistribution of income from the public at large to the financial oligarchy. The proponents argue that growth of the financial sector makes the process of risk management “more efficient”, enabling the diversification and control of risk. In reality, the growth of finance has been accompanied by the emergence of new, hard to measure kinds of risk, given the insatiable appetite for short-run profit and the tendency of those running financial institutions to ignore long-run survival and overlook social values and concerns. A remuneration structure in which a “performance-related” bonus is a major component of overall pay encourages excessive risk-taking and short-termism.

The second characteristic is deregulation of the financial system and the economy at large, which is highlighted by Fine (2012) who suggests that “the process has been closely interwoven with deregulation of the financial system itself and the economy more generally”. Deregulation is intended to allow businesses to operate more freely, without any or minimal restrictions that can be circumvented easily. The proponents claim that deregulation stimulates
economic activity, improves innovation and boosts market growth for the benefit of consumers. In the US, for example, banks were deregulated when the Glass–Steagall Act was repealed in 1999. The legislation was initially introduced in 1933 to prevent banks from using deposits to buy risky securities for fear of losing their clients’ money. It was intended to separate investment banking from commercial banking, not only to safeguard customers’ interest but also to prevent conflict of interest (for example, when a bank grants a loan conditional upon the use of part of the loan to participate in an Initial Public Offering (IPO) that is arranged by the same bank). The fact of the matter is that deregulation enables fraud, particularly in the finance industry that is already infested with fraudsters, and leads to financial instability and crises. To the detriment of financial stability and social welfare, this cause and effect mechanism has been demonstrated over and over again.

The third characteristic is the emergence of new financial institutions, markets and instruments. Fine (2012) describes this characteristic by observing the “birth of a whole range of financial institutions and markets, and corresponding acronyms, that are bewilderingly complex”. The recent wave of fintech (financial technology) has resulted in the creation of thousands of new firms providing financial services by using state-of-the-art technology. Before that, shadow banking institutions, which are unregulated or lightly regulated, proliferated and used by traditional financial institutions to circumvent regulation, sell their products and commit fraud. A wave of financial “innovation” led to the creation of exotic financial instruments, primarily derivatives that are rather difficult to understand except by those who know as much mathematics as Einstein did (and even they get it wrong as exemplified by the failure of the hedge fund Long-Term Capital Management in 1998).

The fourth characteristic is the appearance of a culture oriented to the individual, the market and the alleged rationality. It has become accepted that it is fine for the executives of financial institutions to earn several thousand times what the average worker earns and to be granted bonuses and golden parachutes irrespective of performance. In 2009, a failed insurance company called AIG paid some of its employees bonuses out of taxpayers’ financed bail-out money because they were cleaning up the mess that they created in the first place. That incident, which triggered outrage, sounds like rewarding an arsonist for putting out a fire that they had started. It has become acceptable that financiers like Jeffrey Epstein could afford a private jet and an exclusive island out of salary and bonuses. One hedge fund manager received $3.7 billion (yes, this is a billion with a “b”) in just one year of “work”, roughly 74,000 times the average US household income. That “work” involved the design of some financial instruments, which were bound to fail, and taking a short position on them (see, for example, Anderson, 2008). In this culture, which has been promoted by some finance academics who are beneficiaries of the status quo,
the market is always right, to the extent that bubbles and mispricing do not exist. Fine (2012) notes that financialisation is strongly associated with market mechanisms, complemented or even reinforced by policies that have underpinned rising inequality.

More or slightly different characteristics of financialisation are identified by Fine (2012). At a systemic level, he suggests, financialisation has been located in terms of the dominance of finance over industry. Another characteristic of a financialised economy is that consumption is typically sustained by the extension of credit, not least through the use of capital gains in housing as collateral. He describes as a striking feature “the penetration of such financing into a widening range of both economic and social reproduction, including housing, pensions, health, and so on”. Last, but not least, he refers to the association of financialisation with a particular culture, encompassing a set of practices reflecting an attitude of anti-statism, adherence to the neoliberal ideology, and firm belief in market efficiency. Fine correctly suggests that the state has played a major role in promoting financialisation, which is not surprising, given that the very concept of free market would not have evolved in Victorian England without the active support of the state.

On the other hand, Radzievska (2016) identifies three trends associated with financialisation. The first one is seen in the activities of industrial and commercial enterprises, which refrain from investing their free capital in their own production and go instead for lucrative financial transactions, in the process becoming financialised firms. The second trend can be observed at the level of banks that begin to pay more attention to operations in financial markets and business with households. The third trend is manifested in the active household participation in financial operations. On this last trend, Storm (2018) put it elegantly as follows:

Working people, for instance, increasingly have their (pension) savings invested in mutual funds and stock markets, while their mortgages and other debts are turned into securities and sold to global financial investors … At the same time, the “under-banked” poor have become entangled, or if one wishes, “financially included”, in the “web” of global finance … More generally, individual citizens everywhere are invited to “live by finance” … that is, to organize their daily lives around “investor logic”, active individual risk management, and involvement in global financial markets.

On social issues, he writes the following:

Citizenship and rights are being reconceptualized in terms of universal access to “safe” and affordable financial products … Financial markets are opening “new enclosures”, deeply penetrating social space – as in the case of so-called “viatics”, the third-party purchase of the rights to future payoffs of life insurance contracts from the terminally ill … or of “healthcare bonds” issued by insurance companies.
to fund healthcare interventions, in which the payoff to private investors depends on the cost savings arising from the healthcare intervention for the insurers. And what are we to think of “humanitarian impact bonds” used to finance physical rehabilitation services in countries affected by violence and conflict … ?

Yet another characteristic is the transformation of banks. The driving force of this transformation has been declining reliance of large corporations on bank loans. Corporate enterprises in developed countries have been financing investment (on a net basis) primarily through retained profits. As far as external finance is concerned, they have been relying increasingly on direct borrowing in open markets. Banks have responded to narrowing profit opportunities by turning to the personal incomes of ordinary people as a source of profit and by indulging in investment banking functions. Banks have developed new revenue streams coming from extortionist fees, commissions and other non-interest sources. Greedy banksters have developed a healthy appetite for extracting as much as possible from ordinary people. For example, the fee charged by one Australian bank to non-customers for withdrawing cash from its ATMs is $7.50. The fee charged by the same bank to customers for late credit card payments amounts to an annualised interest rate of some 300,000 per cent at a time when the same bank was calling vigorously for the abandonment of cash and taking interest rates to negative territory so that customers can be charged for leaving their money with that bank. A story went around once that a customer was sent a bill for the time spent by a “manager” having lunch with that customer, even though the customer paid for the lunch. Greedy banksters have gone as far as stealing from dead people (Dennis, 2018).

1.5 EVOLUTION OF FINANCIALISATION

In the early twentieth century, speculative activity prevailed in US financial markets, which were largely unregulated, culminating in the stock market crash of October 1929. The crash and the ensuing Great Depression witnessed the failure of a large number of banks and significant misconduct on Wall Street. As a result, the Franklin Roosevelt Administration took the brave but necessary decision to implement a series of regulatory measures intended to curtail the power of the financial oligarchy. The objective of regulation was to ensure financial stability and support growth and capital accumulation. It was felt that a stable financial sector was needed to provide low-cost credit to the non-financial corporate sector and support the production of goods and services and investment in physical capital. In essence, those measures were taken to restore the function of the financial sector of providing support for the production of goods and services rather than making money out of money.
As a result, a new financial structure emerged, with the following key features. The Federal Deposit Insurance Corporation (FDIC) was established to provide deposit insurance for consumer protection and avoid bank runs. Separation between investment banking and commercial banking was put in place via the Glass–Steagall Act for the purpose of insulating depository institutions from capital markets. Accordingly, depository institutions were prohibited from underwriting and placing securities and from holding speculative assets. Regulation Q was introduced to put limits on deposit interest rates to limit excessive competition among banks and to ensure low lending rates. The FDIC and the Comptroller of the Currency were empowered to ensure the prudence of the banking sector and limit competition in and entry to the sector. The Securities Act of 1933 regulated financial markets by establishing the Securities and Exchange Commission (SEC). The Commodity Exchange Act of 1936 was intended to regulate the exchanges for commodities and futures trading. Specific regulatory measures were put in place to deal with different parts of the financial sector. In 1933 federal home loan banks were established to supervise savings and loans associations, whereas the Bureau of Federal Credit Unions supervised credit unions. The international financial system was subsequently regulated by establishing fixed exchange rates against a gold-convertible dollar.

The new set of rules and active macroeconomic management produced high economic growth rates during the “golden age” of capitalism. Conditions, however, changed in the 1970s when the phenomenon of stagflation emerged, coupled with the collapse of the fixed exchange rate system when the convertibility of the dollar into gold was abolished in August 1971. Those conditions were conducive to the rise of neoliberalism, which received support from right-wing academic economists, most notably Milton Friedman and members of the Chicago School in general. Keynesian macroeconomic management policies were rejected and a wave of deregulation ensued.

The regulatory measures of the 1930s were opposed by the financial oligarchy right from the beginning. However, the oligarchy had to wait until the 1970s for the process of deregulation to start and gain momentum subsequently. The 1970s witnessed a tendency towards “liberalising” finance and the rise of financial innovations aimed at circumventing financial regulation. The collapse of the fixed exchange rate system and the removal of capital controls made exchange rates highly volatile. Interest rates also became volatile when in 1979 the Fed abandoned the policy of interest rate targeting in favour of money supply targeting. Increased level of financial volatility provided the incentive to use derivatives and other fancy financial products, allegedly for the purpose of risk management.

In his influential book, *The Transformation of Corporate Control*, Neil Fligstein (1990) argues that the financialisation of the firm could be traced
back to the late 1950s and 1960s. As he later put it, “all of the financial forms of reorganization including mergers, divestures, leveraged buyouts, the accumulation of debt and stock repurchasing were invented or perfected in this period” (Fligstein and Markowitz, 1993). A large number of economists, influential and otherwise, followed suit, pointing to the growing financial orientation of firms since the 1960s (for example, Zorn, 2004). By these accounts, corporate decision making became increasingly determined by the financial bottom line.

The increasing power of financial institutions over time enabled them to demand and obtain deregulation as they extracted significant concessions from public officials who are supposed to serve the public good. Following the oil price hikes of the 1970s, oil producing countries found themselves with more money than what they could spend immediately, so they began to “recycle” vast amounts of “petrodollars” by depositing them in “Western” banks. Those banks became more powerful as a result of the newly acquired financial muscles while searching for profitable investment outlets for the petrodollars. They lobbied for open international investment opportunities – in the process they put pressure on countries all around the world to privatise, liberalise and deregulate. By using carrots and sticks, the International Monetary Fund (IMF) and World Bank convinced and/or pressured developing countries to open up and financialise their economies to provide those investment opportunities. In the “West”, politicians and policy makers were more than happy to be compliant with the demands made by banks and the financial oligarchy at large.

By the early 1980s, the financial sector was playing a central role as industrial capitalism was gradually replaced with financial capitalism. Governments were complicit in this transformation, which the financial oligarchy had aspired for. The two major political parties, particularly in the Anglo sphere, competed with one another to serve the oligarchy. In the UK, for example, it was the Conservative government of Margaret Thatcher that pushed the deregulation (and financialisation) agenda, but Tony Blair’s “New Labour” was just as sympathetic with the cause of the oligarchy (and this is why it was “New”). When Jeremy Corbyn tried to turn the clock back, he was sent to oblivion by a conspiracy that involved some of his own party members. He has since been replaced with a new leader who is more business friendly (and NATO friendly) than his predecessor. In the US, it was the Democratic administration of William Jefferson Clinton that abolished the Glass–Steagall Act in 1999. In Australia, the difference between the two major parties (Liberal and Labor), when it comes to being “business friendly”, is like the difference between tweedle dee and tweedle dum.

In 1983 an agreement was reached between the Thatcher government and the London Stock Exchange to settle a wide-ranging antitrust case that had been initiated during the previous government by the Office of Fair Trading.
against the London Stock Exchange under the Restrictive Trade Practices Act of 1956. Those restrictive practices included the “single capacity rule”, which enforced a separation between brokers, acting as agents for their clients on commission, and jobbers who made the markets and theoretically provided liquidity by holding securities on their books. Other restrictions include the requirement that both brokers and jobbers be independent and not part of any wider financial group, and the stock exchange’s exclusion of all foreigners from stock exchange membership. The outcome was the birth of the Big Bang on 27 October 1986, which was effectively a series of deregulatory measures, whereby the system of open-outcry was replaced with electronic, screen-based trading. The Big Bang led to significant changes in the structure of financial markets in London as many of the old firms were taken over by large banks, both foreign and domestic. The following years witnessed further changes to the regulatory landscape, at a time when manufacturing industry was being decimated. No wonder, then, that the motto “who needs manufacturing industry when we have the City?” has survived the test of time.

The abolition of the Glass–Steagall Act was so significant that it deserves more attention. Even before the introduction of the Gramm–Leach–Bliley Act (GLBA), which replaced the Glass–Steagall Act, regulatory restrictions in the US were undermined by lenient regulatory interpretations and the use of loopholes. The repeal of the Glass–Steagall Act was justified on the grounds that it would enhance financial stability by allowing financial institutions to diversify their product offerings, and consequently their sources of revenue, which would put them in a better position to compete in global financial markets. In effect, the GLBA was no more than the ratification and extension of changes (favourable to the financial oligarchy) that had already been made because the Office of the Comptroller of the Currency (OCC) had the authority to grant banks the powers they sought.

It is not only the Anglo, Five-Eye sphere where governments emboldened the financial oligarchy by accommodating their demands and meeting their wishes. Japan, which at one time emulated European imperialism by adopting its own Monroe Doctrine, was so inspired by the British Big Bang that the Japanese embarked on their own Big Bang. On 11 November 1996, Prime Minister Hashimoto Ryutaro instructed the Minister of Finance and the heads of other related government agencies to “reform” the financial system as a top priority. Osamu (1997) believes that the Japanese Big Bang was wider in its scope than the British Big Bang, as it was intended to overhaul every bank, securities broker and insurance company, whereas Britain’s Big Bang was essentially a securities “reform”. As a result, the Japanese financial oligarchy indulged in a massive wave of cross-sectoral mergers and acquisitions. One has to say, however, that the Japanese were wise enough not to follow the British in decimating manufacturing industry.
As a result of these developments, the financialisation of the economy took off. Financial innovation and deregulation led to a rapid growth of the financial sector, involving not only big banks, but also non-bank financial institutions, such as pension funds and investment funds, and more speculative institutions such as hedge funds and private equity funds. The process involved the development of a wide range of new and complex financial instruments. The strengthening of the financial sector put pressure on non-financial firms to give top priority to achieving the highest possible financial return for shareholders, in the pursuit of the so-called “shareholder value”. For those firms, failure to sustain high dividend payments to shareholders brings about the risk of big institutional investors selling off their holdings, making the underlying firm exposed to the risk of a hostile takeover. In response to the changing conditions, non-financial firms embarked on repeated rounds of “rationalisation”, such as outsourcing parts of the work, closure of the least efficient plants and cost reduction, particularly labour cost. Furthermore, non-financial firms strived to raise their own returns by engaging in financial investment rather than investment in real capital (buying stocks and bonds rather than new machines, and using the proceeds from the selling of a factory for the same purpose). No wonder then that we started to witness “jobless growth”.

1.6 CLOSING REMARKS: KEYNES ON FINANCIALISATION AND CASINO CAPITALISM

The financial sector is important for growth and development because it provides the means of payment and credit facilities, which are necessary for the production and exchange of goods and services. However, too much of a good thing is bad, and this is valid for financial services. When the financial sector becomes too big, it turns from a hero to a villain, as described by Libich and Lenten (2022). On the other hand, Strange (1983) describes a highly financialised economy as “casino capitalism”. She notes that the difference between an actual casino and the economy-wide casino in a financialised economy is that people choose whether or not to take risks at the Black Jack table, whereas casino capitalism drags us all into the game involuntarily. In his review of Susan Strange’s book, Minsky (1987) commented as follows on the similarity between Casino Royale and the casino found in a financialised economy.

When a position in a batch of principal-only mortgage securities can cost a firm as disciplined as Merrill Lynch about a quarter of a billion dollars on literally the turn of a card, the economic order’s resemblance to a gambling den becomes striking. Furthermore, when exchange rates and financing terms emulate a yo-yo, as they have during the past fifteen years of floating exchange rates, with serious consequences for jobs, prices, asset values and investment, the gambling den is unsavory.
Had Minsky lived to witness the devastation of 2008, he would have changed his mind about describing Merrill Lynch as “disciplined”. Similarity between activity in a financialised economy and a real-life casino was mentioned by Keynes in *The General Theory* (Keynes, 1936):

> Speculators may do no harm on a steady stream of enterprise. But the position is serious when enterprise becomes a bubble on a whirlpool of speculation. When the capital development of a country becomes a by-product of the activities of a casino, the job is likely to be ill done.

Keynes recognised financialisation long before contemporary economists and social scientists started writing about the phenomenon in the past 20 years or so, or particularly in the aftermath of the global financial crisis. He was more widely known for his contributions to macroeconomics than his work on the impact of finance on economic activity (Guevara et al., 2019). Keynes observed that the functioning of capitalism in the early twentieth century had changed dramatically since its mid-nineteenth-century version. During the interwar period, Keynes (1936) observed a shift in entrepreneurial mentality and decision making towards the pursuit of speculative short-term profit. In nineteenth-century capitalism, entrepreneurial decision making was largely characterised by long investment horizons, while finance served merely as a vehicle for these long-term projects, as it should do.

Keynes’s observation of increasing speculation in financial markets reflects to a certain extent his early conception of financialisation as the domination of the financial sector and obsession of policy makers with price stability. More importantly, Keynes (1930) was able to trace the disconnection between financial activity and real production:

> The volume of trading in financial instruments, i.e. the activity of financial business, is not only highly variable but has no close connection with the volume of output whether of capital goods or of consumption goods; for the current output of fixed capital is small compared with the existing stock of wealth, which in the present context we will call the volume of securities.

Lapavitsas (2013) considers the concept of financialisation to be closely associated with Marxist political economy, whether implicitly or explicitly. Three reasons are put forward by Lapavitsas to rationalise this proposition. The first is that the literature hints at “an epochal change of capitalism”, which has traditionally invited Marxist analysis. Second, it suggests systemic, or aggregate, transformation of the economy and society, which has similarly attracted Marxist interest. Third, the literature carries a whiff of disapproval by suggesting a problematic relationship between finance and the rest of the economy.
The casino analogy can be used to describe the global financial crisis and the associated moral hazard. The banking oligarchy gambled with depositors’ money, lost almost everything, and gave the receipts to the depositors in their role as taxpayers. The Ponzi scheme of “fractional reserve banking” meant that it was rational for banks to engage in risky financial transactions while keeping minimal capital, knowing that the lender-of-last-resort (that is, the taxpayer) would foot the bill. Only banks can gamble, keep the proceeds when they win, and have someone else cover losses when luck abandons them. No wonder that financialisation is a profitable enterprise, even though it instils a curse.