Literatur

Brinkley, A. (1995): *The End of Reform. New Deal Liberalism in Recession and War*, New York: Knopf.
Deppe, F. (2003): *Politisches Denken zwischen den Weltkriegen*, Hamburg.
Von Hayek, F.A. (1952): *Individualismus und wirtschaftliche Ordnung*, Zürich.
Herbst, L. (1999): *Das nationalsozialistische Deutschland 1933 – 1945*, Frankfurt/Main.
Hobsbawm, E. (1995): *Das Zeitalter der Extreme. Weltgeschichte im 20. Jahrhundert*, München.
Keynes, J.M. (2008): *On Air. Der Weltökonom am Mikrofon*, Hamburg.
Keynes, J.M. (1994[1936]): *Allgemeine Theorie der Beschäftigung, des Zinses und des Geldes*, Berlin.
Mazower, M. (2000): *Der dunkle Kontinent. Europa im 20. Jahrhundert*, Berlin.
Nordmann, J. (2005): *Der lange Marsch zum Neoliberalismus. Vom Roten Wien zum freien Markt*, Hamburg.
Pribram, K. (1992): *Geschichte des ökonomischen Denkens*, 2 Bände, Frankfurt/Main.
Ptack, R. (2004): *Vom Ordoliberalismus zur Sozialen Marktwirtschaft. Stationen des Neoliberalismus in Deutschland*, Opladen.
Raeithel, G. (1989): *Die Geschichte der nordamerikanischen Kultur*, Band 3, Weinheim.
Schumpeter, J.A. (1993): *Kapitalismus, Sozialismus und Demokratie*, Tübingen (7. Auflage),
Ders. (1954): *History of Economic Analysis*, New York: Oxford University Press.
Tooze, A. (2007): *Ökonomie der Zerstörung. Die Geschichte der Wirtschaft im Nationalsozialismus*, München.
Wehler, H.-U. (2003): *Deutsche Gesellschaftsgeschichte*, Band 4 (1914 – 1949), München.
Wegmann, M. (2002): *Früher Neoliberalismus und europäische Integration*, Baden-Baden.

Quis custodiet ipsos custodes? – Who supervises the supervisors?

Kurt Bayer*

The »market failure or government failure« debate

The controversy still rages on whether the current crisis is the result of market failure or government failure. Paraphrasing former US-President Harry Truman's request for a one-armed economist,[1] I would say ›both‹. On the one hand, the tenets of the mainstream efficient mar-

* Executive Director for Austria, Israel, Cyprus, Malta, Kazakhstan and Bosnia & Herzegovina at the European Bank for Reconstruction and Development (EBRD), London.

1 President Truman, when searching for the first Chair of the Council of Economic Advisers, asked his staff to search for a one-armed economist, because the ones he knew always said: »on the one hand/on the other hand«.

ket hypothesis for explaining the functioning of financial markets, which formed the basis of their deregulation, have been glaringly shown to be wrong. On the other hand, it was the ›willing to-be-captured‹ attitude of government actors, including regulators, which aided and abetted market failure. However, expectations about the imminent demise of ›neoliberal‹ economics are premature, since to change the mainstream paradigm in economics will take a long time. This would require new curricula, new teachers, and a new generation of students, new textbooks, and new criteria for journal article acceptance. We also cannot just go back to Keynesian economics, since during the last decades many economic conditions – not least the new dominance of finance over the real economy – have changed, making some of Keynes's observations obsolete. Of course, many elements of a more realistic, less dogmatic economics exist already, viz. the essential writings of Hyman Minsky on the inherent instability of financial markets (see e.g. Minsky 1992), of behavioural economics, of institutional economics, but still unfettered belief in the invisible hand of the market persists to an astonishing degree.

Many economists, among them Paul Krugman,[2] have attributed the active dismantling of limits to speculation and risk-taking – financial market deregulation – to the argumentative force of financial economists, to their being enamoured to the elegance of mathematical models. However, grave doubts on this ›enlightenment‹ argument are in order. Think, for instance, of the revolving door policy of US financial market actors, becoming treasury secretaries or national bank governors, and after ›mission accomplished‹ going back to lucrative directorships and banking consultancies. The lobbying efforts of erstwhile Goldman Sachs CEO and later secretary of the US treasury Hank Paulson are legendary (see e.g. his effective fight against imposing stricter leverage limits on US investment banks). He is, however, by no means the only one. Similar careers can be seen in the UK, which since the 1980s has been avidly expanding London's role as the world's major financial center, vying with New York, Hong Kong and Singapore, having left continental Europe's centers far behind. But also the continentals are far away from establishing an arms-length distance between financial markets and those who are charged with reining them in, in order to safeguard the interests of the economy, the consumers and investors. The role of the »Landesbanken« in Germany, the political connections of the large commercial banks in France and Germany, the party-political and thus state influence on banks in Austria – and vice versa the influence of party-affiliated bankers on policy –, the battles in Italy between the large banks and the state: All these show an unhealthy closeness which eventually permitted massive systemic failure. It does not require sinister conspiracy theories when describing the collusion between those who profited from the immense growth rates of the financial sectors during the past 25 years and those who were supposed to oversee them in the interest of the public. Career development analysis is proof enough.

The massive failure of the financial system, coming to a head in 2008, caused the most severe economic crisis in the world in the last 60 years. Recognizing the important

2 See e.g. Krugman (2009).

role credit extension plays for our economies – and after strong lobbying efforts by failing banks –, governments came to the rescue of banks and – with the help of previously unheard-of sums – bailed them out. Estimates show that taxpayers have come to the rescue of banks to the amount of US-$ nine trillion in guarantees, cash and capital injections. This is about one seventh of World GDP! This rescue operation has propelled the deficit and debt ratios of many countries to exorbitant heights; both the US and the UK will reach GDP deficit ratios above ten percent as a result of these rescue operations and the economic stimulus packages. Other countries'[3] deficit ratios are not much lower. It will take taxpayers and citizens decades to pay these back. The irony is, of course, that the rescued banks themselves will hardly contribute to these repayments, since the respective tax codes' permission to carry forward losses – time limits for these are different from country to country: unlimited in the UK, three years in many continental European countries – will keep them out of the tax collector's reach for many years. And this despite the fact that many of the surviving banks – especially investment banks – have begun to report new profit (and bonus) records in fall 2009. The irony goes even further: Since these banks do not make their money from commercial lending – whose volume is significantly lower than before and much more expensive –, but from trading activities and from placing the bond issues which the governments had to issue in order to rescue the banks, they make revenue and profit from activities directly related to their own rescue. Should the governments, when bailing them out, not have made provisions that these triple win-win-win for banks and loss-loss-loss for individual taxpayers did not occur?

While investment banks are once more playing business as before and carving up the market among the survivors, being able – on account of government and national bank help (e.g. quantitative easing) – to refinance themselves at close to zero cost, thus reinforcing the previous market failure tendencies, the governments of the (rich) world are perpetrating another massive state failure, by letting this happen.

Early restructuring impetus by G-20

Initial announcements at the newly created G-20 summits[4] (Washington, DC; London; Pittsburgh) had analyzed quite correctly that the existing regulatory framework had allowed banks to increase their leverage ratios to irresponsible levels (e.g. 50 : 1), to grow too big to fail, to transfer risks from their books to insurance companies and consumers without their being able to account for it, to escape from remaining regulation by creating a

3 In this note I purposely speak only of rich, industrialized countries, thereby disregarding the disastrous effects the crisis is having on less developed and transition countries, especially on the poor.

4 The G-20 formation had been formed already in 1999 at finance ministers' level, with a view to have a more inclusive discussion between industrial and emerging markets on global economic policy questions. It was elevated and ›re-invented‹ at heads-of-state level after the US treasury let Lehman Brothers default – the ›official‹ start of the global financial crisis. Now this formation meets regularly both at finance ministers' and national bank governors' level in preparation for the heads of state (Bayer 2007).

huge shadow banking system, both on and off shore, etc. There was consensus that these failings had caused a gigantic inverse financing pyramid where the largest part consists of non-value creating, but fee and profit generating trading activities within the sector itself (see Turner Review – Financial Services Association 2009), and that a return of banking to its original function, i.e. to turn savings into long-term investments, was the first order of the day. Simultaneously, the International Monetary Fund (IMF) was promised more money and charged with monitoring macro-prudential risks to the global financial system, taking into account the newly globalized structure of the world economy. The Financial Stability Board was extended to include all G-20 members and asked to devise new regulatory rules. All this made sense and seemed to suggest that world leaders had come to realize that a radical restructuring of the world economy was in order. The early crisis response mechanisms, the bailouts and the following stimulus packages were the right answer to this deep crisis. They were *grosso modo* necessary, even if more consistent action could have been taken across countries, over time and across instruments.

However, while all this happened, two things occurred: a) the impetus of government regulators was weakened, and b) the surviving banks – knowing after the bailout that they really are too big to fail and thus will be rescued again next time around – have gone back to their old ways. Of course, in the meantime, they have been busy lobbying policymakers against »intrusive«, »too stringent«, »choking-off« regulation. This might help explain the reduced impetus of policymakers.[5]

At the end of 2009 there are some signs that the crisis is bottoming out, even though the effects on the business cycle, on the real economy, will be long felt. At this time it is by no means clear that the crisis will be over soon, the accumulation of non-performing loans as a result of the recession might wreak more havoc in banks' balance sheets; lending to the real sector has not yet begun; unemployment is sure to increase significantly in the OECD countries – with its concomitant effects on consumption and savings patterns and volumes.

New regulatory mechanisms are needed: The future role of citizens' organisations

Where to go from here? It has become obvious to even the most dogmatic mainstream economist and politician that the ›market‹ does not regulate itself effectively. However, if governments are (still) enthralled with – or even more seriously, captured by – financial market interests and their actors, who shall regulate them and shield us, the citizens and the economic system, from future near-meltdown crises? Both the market and the state each have their burden of responsibility to bear for making the crisis possible, for letting it evolve and for its inadequate and incomplete resolution. The state has lost an important time window of opportunity at the height of the crisis to set mechanisms in motion, combining the nec-

5 See e.g. the strong lobbying efforts by banks to have the UK government veto the new rules devised by the European Commission, as well as UK's and Sweden's efforts to prevent a truly European financial market supervisory authority.

essary rescue operations with stringent directions on the future behaviour of financial markets and their actors. Shying away from outright nationalizations; hoping that indirect incentives, like re-capitalizing private banks, would once more induce them to lend to the real sector, instead of creating state lending institutions for on-lending to consumers and businesses at refinancing costs plus margin; being too timid to put caps on bankers' remuneration, incentive and pension packages; breaking up too-large-to-fail banks – all these more direct and straightforward, consistent and radical options which could and should have been taken: today and in the future, their introduction would meet with increased resistance from an increasingly profitable (if not value-creating) sector.

There is a way out. I would propose the following steps. They are based on the premise – amply proven correct during the course of the crisis – that reliance on self-regulation by the markets is out of the question.[6] Market participants' interests have proven too diametrically opposed to those of the economy, society at large, and both businesses and consumers (savers). The interests of many financial markets actors were/are driven by personal greed, empire-building behaviour and disregard for the economies' requirements. These interests were enabled by deregulation, fascination with ever more ›innovative instruments‹ – which turned out so complex that not even their users understood their effects – and a general free-market paradigm which both financial engineers and policymakers embraced.

On the other hand, with all its shortcomings, government has democratic legitimacy[7] and – more important – unrivalled implementation capacity and experience. The question then is, how can we use the mechanisms and instruments of the state to control markets, given the above-described capture of the state by financial interests? What is needed is a change in the decision-making processes for economic policy decisions, to ›liberate‹ the state from pursuing one-sidedly the interests of financial market actors. Of course, in the final analysis, this is a question of political power. I put some hope in the fact that the citizens might be able to re-capture state authorities from the grip of financial markets interests. This requires putting effective pressure on the political system, on parliamentarians, on governments, on the judiciary. For this, the citizens cannot rely on the existing institutional arrangements, which have proved to be ›under the covers‹ with financial markets interest. They need to supplement the customary parliamentary process with much stronger grassroots activity, with a new role of civil society as ›monitor of monitors‹.

Quis custodiet ipsos custodes (Who controls the controllers)? This is the age-old question of regulation. Since existing institutions, labour organisations, business organisations, and social partners were ineffective in reining in excessive self-dealing, risk-taking and risk-shifting behaviour by financial markets, since supervisory boards – where they exist as separate entities – were unable to call management to account, since voluntary codes of conduct were not able to exert effective control, it will fall on citizen groups to supervise the

6 See e.g. the arguments advanced in Bayer ([ed.] 2007).

7 This legitimacy is afforded by democratic election processes, i.e. a formal requirement. There are discussions whether the election system, its financing, its majority-creating rules, etc. are representing the will of the populations.

supervisors and to put pressure on existing authorities to act in the interest of the economy and society. A historical reminder may be the creation of the social movements during the 1970s, of environmental movements in the 1980s and of the so-called, misnamed[8] anti-globalisation movements of the 1990s.

Such existing anti-capitalist movements, like ATTAC, or Jubilee 2000, which have wide-spread organisation, professionalism and expertise, could combine forces with those organisations which have been formed with the purpose to sue financial market actors for misleading prospectuses, inadequate information about risks and imprudent behaviour that resulted in heavy losses for many investors.[9] Such groups, at present formed exclusively to recoup some of the losses incurred, could evolve into future watchdog organisations.

Such groups, to become effective monitoring agents, need professional help and advice. This could come from academia, but also from the many disenchanted insiders of the pre-crisis financial system, whose warnings about some of the perversions were not only not heeded, but also led frequently to their dismissal. In addition, as Elinor Ostrom has shown, there are enough experts (persons) out there who volunteer their time and expertise in favour of solidarity and communal cohesion, going beyond their immediate self-interest (Ostrom 1990). Michael Thompson has shown the self-organising power, describing such diverse areas as the dwindling resource base of Nepalese Himalayan villages and the Highbury Community Association in saving living conditions in their area and finding a relocation spot for a new stadium of Arsenal Football Club (Thompson 2008: 2). Harald Müller (2009: 239) calls especially on non-governmental organisation (NGO) »mobilization capability«, in addition to substantive inputs into the decision process, as an important factor: to mobilise people to get behind a specific project.[10] Mary Kaldor (2003) has written extensively on the history, benefits and limitations of civil society involvement in decision-making, especially, but not exclusively, with respect to peace-keeping.

Historically, a parallel can be drawn to Ralph Nader's battle with the US auto industry (and other industries) in the 1960's[11], and thereafter, which has led to marked improvements in consumer protection legislation in the US, and to the establishment of the Environmental Protection Agency. With the help of new communication technologies international financial watchdog NGOs can be established and made to work. In a project financed by the Austrian Ministry of Finance I have also proposed to widen the decision-making space for policy making to include civil society (Bayer [ed.] 1997).

8 Mary Kaldor correctly points out (2003: 101) that these movements should rather be called anti-capitalist, and not anti-globalization, since they »oppose the unregulated spread of capitalism and the growing power of the market over every aspect of life«.

9 As class-action suits, or as collectives of victims, depending on the respective legal frame of each country.

10 As an example he cites their mobilizing power which put in place the Ottawa Convention against anti-personnel landmines, against the resistance of three permanent members of the UN Security Council: Russia, China, and the US (Müller 2009: 240).

11 He invented the slogan »unsafe at any speed«, denouncing the inadequate safety features of a newly-to-be introduced car by General Motors.

In order for NGOs to be able to play a stronger controlling role on government and market institutions, they need to gain credibility. This can be achieved by creating a track record of efficient intervention. But they also need to succeed to gain ›a place at the table‹, i.e. the right to be heard. The Austrian »Social Partners«, for example, have the legal right to comment on legislative bills as part of the parliamentary process; a similar right could be extended to a specialised Financial Watchdog NGO on national and international levels. If such a right cannot be achieved, the mobilising power of NGOs can be applied to have this consultation established. It is not only action-orientation which characterises effective NGO activity. The example of the establishment of the Interparliamentary Panel on Climate Change (IPPC) and its more continuous work,[12] or that of the Global Fund in health care show that also non-mass-mobilisation activities can be successfully accomplished by NGOs. However, a continuous regular monitoring role of financial market regulation would be a new state of development for a civil society organisation.

Global, regional, and national regulation

In spite of the welcome widening of global economic policy decision-making from G-7 to G-20 recently, effective policy-making and regulation require both wider (national) representation and legitimacy. I have analysed some proposals to that effect (Bayer 2007 and 2009). Wider representation could theoretically be achieved by already existing structures, like the United Nations (UN) or the IMF, both of which have universal membership. UN organisations are, however, notoriously slow and inefficient (Stiglitz Commission 2009). This leads me to the conclusion that they should delegate this economic policy deliberation and decision-making portfolio to a *Global Economic Policy Council*, comprised of the G-20, but with the inclusion of at least three to five heads of state from least-developed countries. They would join the group replacing three of the four EU members. The latter should give up their seats to a combined EU seat. This would reduce the EU's over-representation, increase the EU's clout, and at the same time gain them recognition for contributing to a more representative structure by ending the restriction of G-20 membership to the largest countries. Of course, legitimate questions can also be raised about some of the other members of the G-20. It would be important to have rich, emerging and developing countries around the table, representing all continents. Only such wider global representation would increase their legitimacy – together with delegation by the UN General Assembly –, and thus increase ownership of decisions made in the Council.

While the Council would provide political and strategic guidance and identify the topics and time frames for the most important global economic policy issues, the actual work would be done by so-called »Thematic Networks« (Rischard 2003, Bayer 2007), each of which would be established by the Council for a specific area of regulation. I would propose six areas: Macroeconomic Stability, Global Public Goods, Poverty and Development,

12 Of course, the IPCC was set up under the guidance of and with a mandate from the UN. This assures its legitimacy.

Labour and Migration Issues, Investment and Trade, and Illegal Activities. An over-arching network would attempt to close the gaps formed by interlinkages between the substance areas of the other networks, i.e. making sure that the spillovers between them are taken into account. The networks would be composed of government officials, experts and civil society representatives, in order to garner ›the best know-how in the world‹ and have opinions and interests of widely differing groups represented. The Networks would recruit their respective membership depending on the problem to be dealt with in question, in a way that the most affected countries would participate. Such a mode would also rotate membership and would avoid having the same (few and powerful) countries determining and deciding all problems. The networks, mandated by the Council, would present to it options with their various effects for decisions by the Council. Since the Council has no executive powers of enforcement, it could only lead by persuasion, ›name and shame‹ non-compliers, but essentially rely on the goodwill of all nations and actors to follow the new rules in the interest of global stability.

Regional – e.g. EU – decision-making bodies would remain, dealing with regional problems. *National* decision-making powers would continue to be lodged with national parliaments, dealing ideally with national problems and implementing some of the decisions made at ›higher‹ levels. Thus, in a cascade, decisions would be made at the most appropriate level, without jeopardizing legitimate decision-making powers. The empowerment of civil society organizations for know-how generation and inputs into decision-making would be the novel element, in order to return ›state‹ institutions to their original role, i.e. to protect the interests of citizens, society and the economy at large.

References

Bayer, K. (ed.) (1997): *Neue Formen der Erfüllung öffentlicher Aufgaben*, Ministry of Finance, Vienna.

Bayer, K. (2007): How to run the global economy, BMF Working Papers, No. 1, Vienna.

Bayer, K. (2009): *Die Governance der globalen Wirtschafts- und Sozialentwicklung*, mimeo, London.

Financial Services Association (2009): The Turner Review, London: FSA.

Kaldor, M. (2003): *Global Civil Society. An Answer to War*, Cambridge: Polity Press.

Krugman, P. (2009): How did economists get it so wrong?, in: New York Times Magazine, Sept. 2, URL: www-nytimes.com/2009/09/06/magazine/06Economic-t.html.

Minsky, H.P. (1992): The financial instability hypothesis, Jerome Levy Economics Institute of Bard College Working Paper, No. 74.

Müller, H. (2009): *Building a New World Order. The Sustainability Project*, London: Haus Publishing.

Ostrom, E. (1990): *Governing the Commons: The Evolution of Institutions for Collective Action*, Cambridge: Cambridge University Press.

Rischard, J.F. (2003): *Countdown für eine bessere Welt. Lösungen für 20 globale Probleme*, München/Wien.

Stiglitz Commission of Experts on Reforms of the International Monetary and Financial System [Stiglitz Commission] (2009): Draft, May 29, United Nations, New York.
Thompson, M. (2008): *Organising & Disorganising. A Dynamic and Non-Linear Theory of Institutional Emergence and its Implications*, Exeter: Triarchy Press.

Eigenkapital im Finanzsystem: Die Lehren der letzten, der aktuellen und der nächsten Krise

Capital requirements in the financial systems: Lessons from the last, the current and the next crisis

Peter Mooslechner*

> »[…] das vorangegangene Geld bezahlt das nächste, nein, das nächste Geld bezahlt fürs vorige […]« (Jelinek 2009)

> »The minimum hurdle that reforms should meet is whether they would have prevented the last crisis. Any feasible level of required capital would not cross this hurdle […].« (Rajan 2009)

Die gegenwärtige Finanzkrise hat ein weites Spektrum an Schwachstellen sichtbar werden lassen, die von der gesamtwirtschaftlichen Rolle von Finanzmärkten und Finanzinstitutionen über die Regulierungssysteme bis zur stabilisierenden Rolle des Staates reichen. Kurzfristig war es ohne Alternative, das Finanzsystem zu stabilisieren und negative Auswirkungen der Finanzkrise auf die Realwirtschaft zu dämpfen (Blanchard 2009, Felton/Reinhart 2009). Langfristig müssen neue effektive Rahmenbedingungen entwickelt werden, wobei die spezielle Charakteristik der Krise als eine Kombination von ›Marktversagen‹ und ›Regulierungsversagen‹ eine spezielle Herausforderung darstellt. Zentrales Anliegen muss es sein, Lücken für *regulatory arbitrage* zu schließen und die immer größer gewordenen Möglichkeiten abzuschaffen, Finanzgeschäfte außerhalb regulierter Märkte und Finanzinstitutionen stattfinden zu lassen.

Wie die Krisenchronologie zeigt, haben die Verhaltensweisen von Finanzmarktakteur|inn|en entscheidend zur Verursachung der Krise beigetragen (Borio 2008). Gescheitert ist beispielsweise ein spezifisches Geschäftsmodell (*originate and distribute*), das einen wesentlichen Beitrag zu den Krisenursachen geleistet hat. Als Folge sind zahlreiche Institute, die über keine ausreichende Einlagenbasis verfügten – wie etwa die großen Investmentbanken

* Oesterreichische Nationalbank, Wien.