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Re-structuring the financial sector to better serve economy and society

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Outline

- Financialisation – growth of financial system; form of changes
- Has that growth of financial system been socially beneficial ?
- What's the financial system for?
- Re structuring the financial system

Financialisation

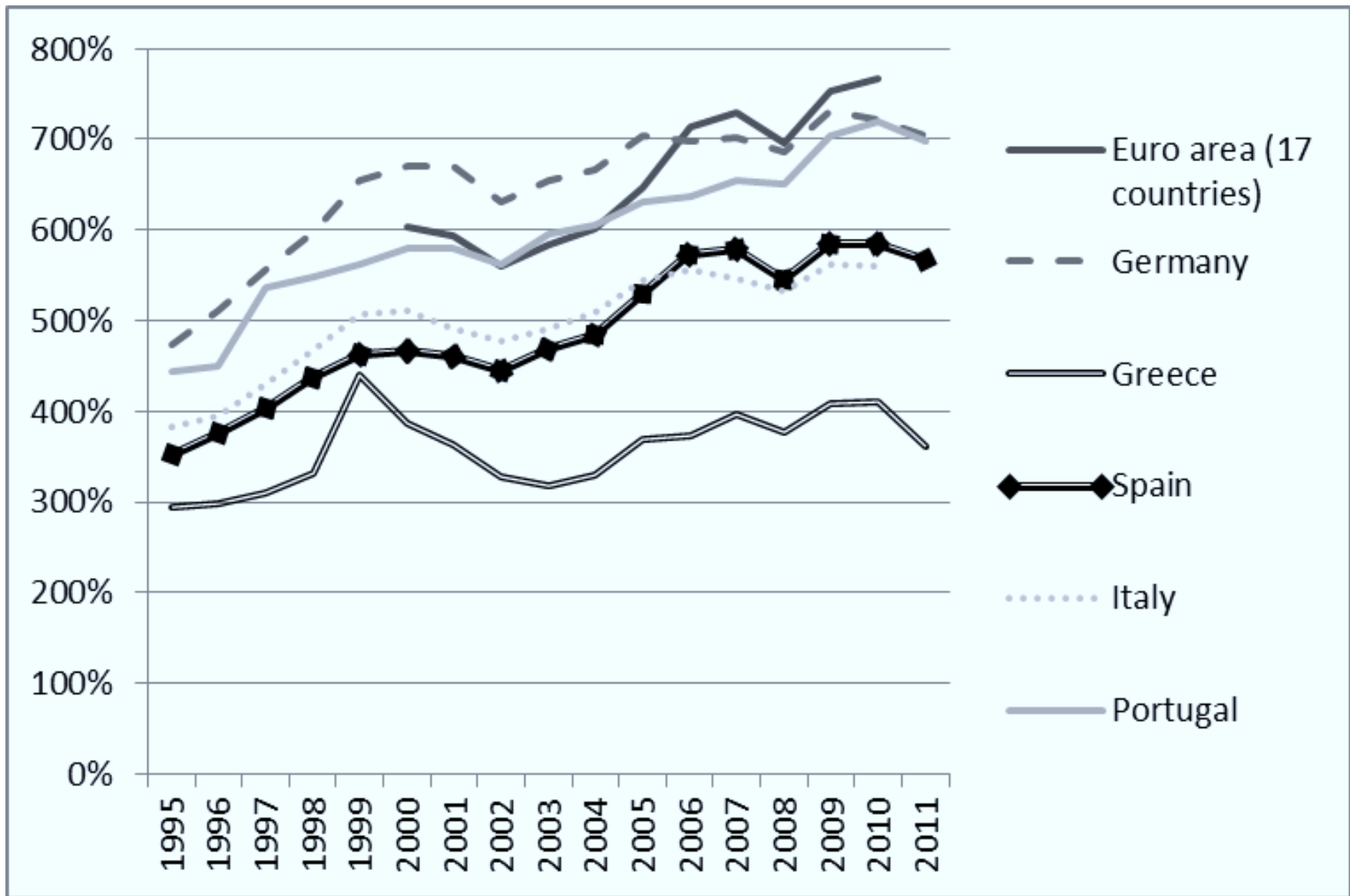
- The past four decades can be labelled an era of financialisation
- ‘financialization means the increasing role of financial motives, financial markets, financial actors and financial institutions in the operation of the domestic and international economies’ (Epstein, 2005)
- The focus here is on the growth in scale and changes in form of financial sector



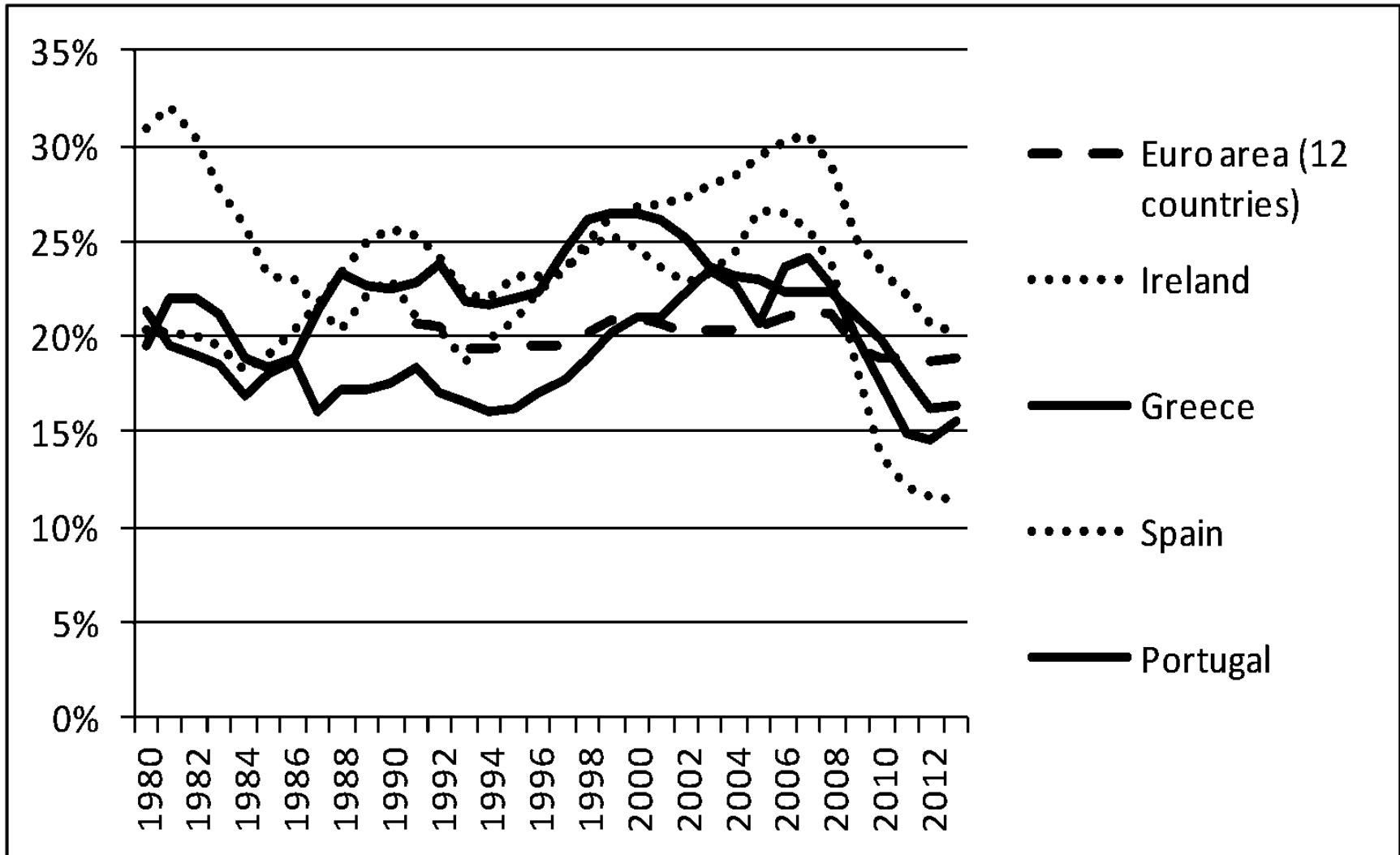
Financialisation in Portugal

- Sérgio Lagoa, Emanuel Leão, Ricardo Paes Mamede, and Ricardo Barradas
- Report on the financial system in Portugal, FESSUD Studies in Financial Systems no.9
- Available at fessud.eu
- Some indications of growth of financial sector and household debt follow: note also tendency of investment to decline.

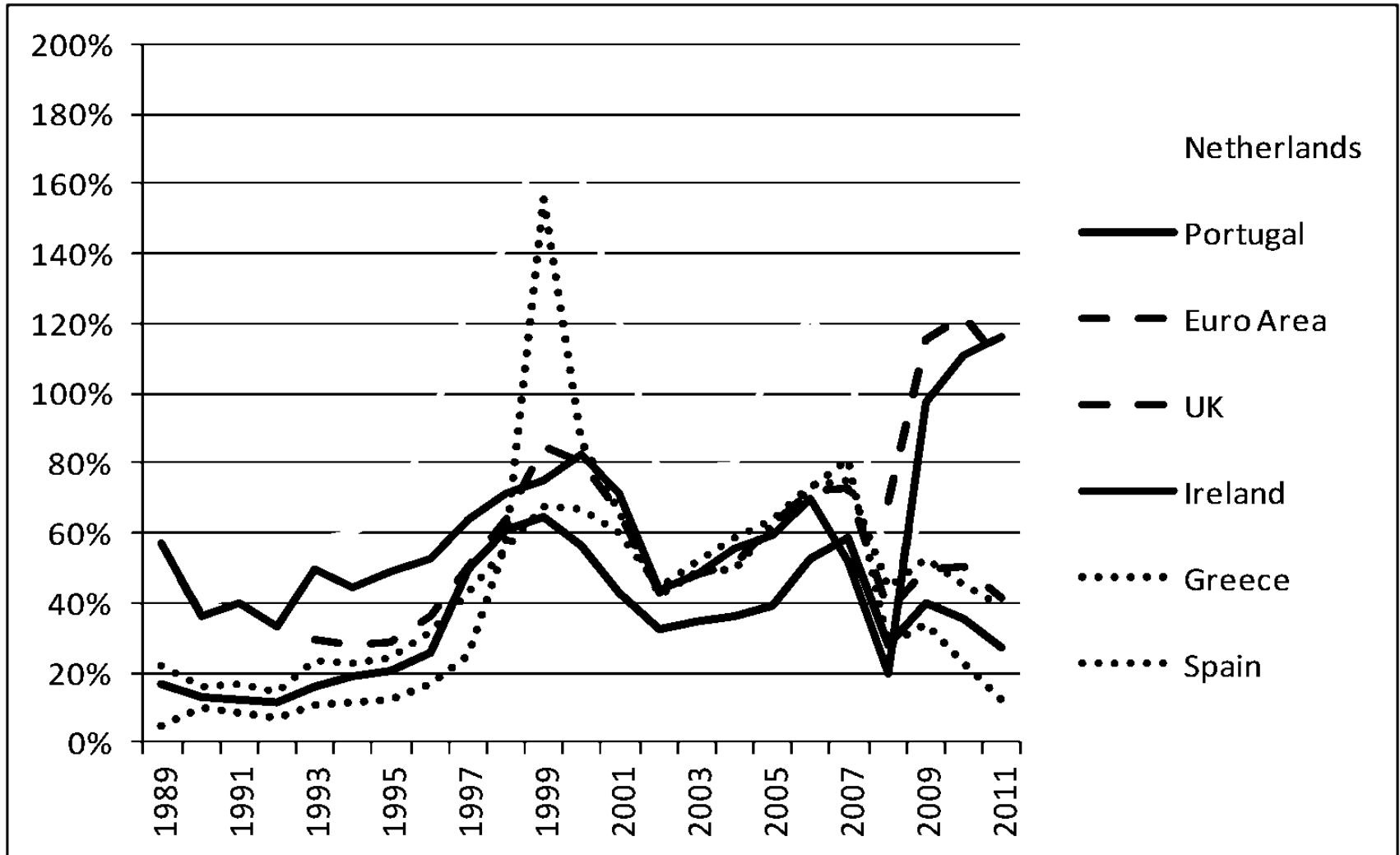
Financial assets of the total economy (% of GDP)



Gross fixed capital formation at 2005 prices (% of GDP)



Stock market capitalization of quoted shares (% of GDP)



Household's debt (% of GDP)

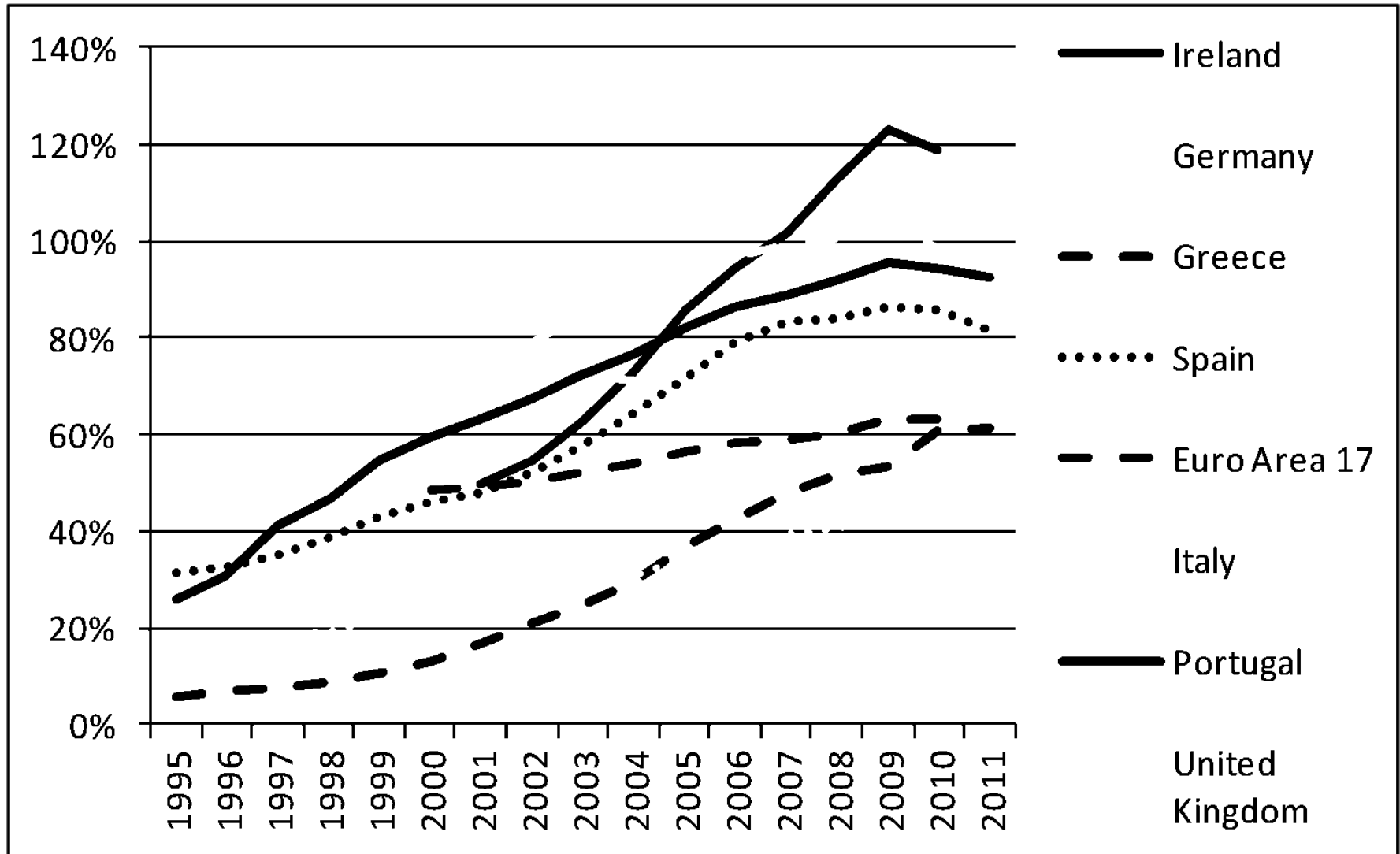


Table 12 – Financial intermediaries versus financial markets

	Stock market capitalisation (% GDP)	Debt market capitalisation (% GDP)	Financial assets of financial intermediaries (% GDP)
1995	20	7	205
2011	27	24	446
% change 1995-2011	35%	269%	117%

Source: Eurostat and ECB



Has the growth of
the financial sector been beneficial?

- What have been the effects on investment and economic growth ?
- Has the financial sector become too large?
- Financial crises and their costs on output, employment and growth
- Mis-selling and other costs



What do we expect of the financial sector?

- Provides a payments system
- Providing financial assets to facilitate saving; links savings with capital investment; allocates funds for investment, and monitors use of those funds.
- Insurance services



Re-structuring the financial sector

- The guiding principles: a financial system which effectively serves economic, social and environmental needs in a sustainable manner
- The specific ways in which the financial system could be changed are dependent on existing institutions and their history.
- In general it is not the volume of savings which needs to be raised rather it is the allocation of those savings.



Re-structuring the financial sector

- The financial sector necessarily allocates funds and is involved in ‘credit rationing’: decisions over who receives funds and at what price. How are those decisions made?



Role of taxation

- The role of financial transaction taxes to reduce the ‘casino economy’
- The clear purpose of such taxes should be the reduction in the volume of transactions, and the release of resources which are engaged in those transactions.



Re-structuring the financial system

- Stakeholder financial institutions vs. Shareholder financial institutions
- The 'double bottom' line
- The benefits of a more diverse financial system in terms of stability
- Ability of savers to influence where their funds are used



Developing financial institutions

- Financial institutions can be monitored as to the direction of lending with incentives (e.g. reserve requirements).
- ‘Guided lending’ cf. Community Reinvestment Act



Developing financial institutions

- State (green) development bank along lines of KfW in Germany
- Linked in with industrial strategy



Developing financial institutions

- Roles for
- Mutual financial organisations: savings banks
- Investment vehicles using revolving funds
- Micro finance
- Credit unions
- Ethical banking



A concluding comment

- Each form of financial institution and its operation has downsides and issues as well as benefits.
- At present time each should be judged by their abilities to fund socially desirable investments, notably environmental friendly ones ('green investment')
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