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# Note from the editor

Dear reader,

Welcome to the first *Newsletter* issue of 2011. This looks like being an important year for the political economy of Europe, during which major decisions are being debated about the future of its core currency, the euro. These debates are taking place amidst a debt crisis which embraces both states and private banks, and which is being experienced especially severely in Ireland, Greece and Spain. Some scholars and commentators have been predicting that the euro will have been fundamentally transformed – reduced in size and more tightly regulated and integrated in fiscal terms – by the time the year ends. Meanwhile, the eurozone's most significant problems – serious imbalances between Germany and other countries, large fiscal deficits in Spain, Greece, Ireland and elsewhere, and the continuing exposure of banks (including those in Germany) to unmanageable losses – show no sign of abating. Should the euro contract or even fail, the consequences will be felt far beyond its member states, indeed they will play a major role in shaping the world's monetary systems for some years to come, not only in relation to the ongoing 'wars' in which major currencies such as the US Dollar and Renminbi are embroiled, but at a local level, too, as people get to grips with the rapidly changing monetary landscape around them.

All of the papers included in this issue of the *Newsletter* have been written by eminent researchers and scholars who are well qualified to address such matters, and I hope you take as much from reading their articles as I have done. I am extremely grateful to the authors, all of whom have taken time from busy schedules to write pieces especially for the *Newsletter*. And, as always, I am in debt to Christina Glasmacher, whose unfailing good humour and efficiency make the editor's job much easier and more pleasurable than it would otherwise be.

The first paper of the issue is by Keith Hart, previously interviewed by Patrik Aspers for the November 2007 issue of this *Newsletter*. Hart's work came to prominence for his invention of the idea of the 'informal economy'. For some years now – for example, through his classic article *Heads or Tails? Two Sides of the Coin* (Man, 1986) and his highly-engaging *Money in an Unequal World* (2000) – Keith has been exploring money in a distinctive way that does not

deny its 'acidic' qualities but seeks to redress an imbalance in our conception of modern, nation-state money by emphasising its potential to empower individuals and reconfigure our communities through what he calls its 'socially redemptive qualities'. In the essay published here, Hart continues in this vein by making out a vibrant and articulate case for a more nuanced approach to money in which, partly as a response to the fact that during this latest financial crisis states' "capacity to print new money has been almost exhausted," our monetary systems are reorganized – globally – in ways that bring benefit rather than harm to the social organization of the economy.

Brigitte Young has written extensively on the political economy of Europe, in addition to her work on themes such as gender, risk and globalization, and here she looks directly at the euro crisis. Whereas Hart boldly states that he 'would not wish to return to currency controls and state-managed money', Young grapples with the future of a euro in which such controls have been placed under severe questioning since its (so-called) sovereign debt crisis began towards the end of 2009. According to Young's clearly-argued analysis, the euro zone seems to be confronting a situation in which there is a genuine prospect that two hitherto distinctive and conflicting systems of policy-making – a rules-based German model with its independent central bank, as against a French model (*gouvernement économique*) in which monetary policy is more deeply embedded in political institutions – may be coming closer together through the development of much-needed reform proposals, the 'Pact for Competitiveness'. This could be a new dawn for the euro, Young suggests, in which what is novel is that 'Germany is no longer outright rejecting economic and fiscal governance at the eurolevel'.

Christoph Deutschmann has been working on money for well over two decades, for example, through his *Die gesellschaftliche Macht des Geldes* (2002). In this highly thoughtful piece, he argues that any thorough-going solution to (rather than temporary fix for) the euro's current predicament needs to get to grips with two independent but related problem complexes: the first relates to the global financial crisis, whereby eurozone member-states appear to have been especially hard-hit by the way that the financial industry 'has managed to externalize her own problem and to transform it into a problem of the states',

while the second arises from more familiar problems of political co-ordination within the eurozone itself. Deutschman shows how these problems have been interacting in Greece and Ireland, but argues that all recommendations for greater policy and fiscal integration in the eurozone will be ineffective unless its outstanding debt problems are dealt with, and this requires a form of 'austerity' on the part of private creditors, not just states and their citizens: they 'must be brought to renounce a part of their claims'.

Peter North will be well-known to most readers for his work on local and community currencies, particularly through his excellent *Money and Liberation* (2007). Here he turns his attention to the difficulties facing the euro and asks whether these might unwittingly give birth to a new politics of money. As North points out, arguments on the political Left traditionally tend to be indifferent to money itself, focusing primarily on relations between workers and employers, or between the states and citizens during economic crises. In an intriguing analysis of various options confronting the crisis-hit eurozone states, North draws attention to the experience of Argentina and envisages a future in which countries with strong regional institutions, independent of the state, take responsibility for money issuance and produce their own currencies which supplement, rather than replace, the euro.

Such local, 'grassroots' approaches to the euro crisis obviously rest upon the engagement of people in the man-

agement of money on a more local level and in a more proactive way than may hitherto have been the case. It is striking that one of the main responses to national regulators to the financial crisis – including the UK's Financial Services Authority through its *Turner Review* (March 2009) – has been to recommend stepping up programmes to 'educate' consumers and encourage greater levels of financial capability and awareness of risk. But what exactly would this entail: savers and borrowers who are more cautious, more rational – more like the *homo economicus* that sociologists have long argued is unrealistic? Olga Kuzina's paper considers exactly this problem, drawing on her work on financial 'literacy' among Russians to show how complex the concept is, and how difficult levels of financial literacy or capability are to measure. Is financial literacy simply a question of how much we know, or does it also embrace questions of attitude and belief? And if it is the latter, what practical ways forward might there be from this crisis that promise the 'monetary redemption' that Hart called for at the beginning of this issue? These are key questions, it seems to me, which must be tackled alongside the broader-based issues that will be preoccupying policy-makers as this fascinating year unfolds.

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# The Financial Crisis and the End of All-Purpose Money

By Keith Hart

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## Introduction: the financial crisis

By taking a broader view of money than its current identification with finance, I aim to historicize the present by placing it within a long-term process of social development, in the process offering a new explanation for our economic problems. I take the financial crisis to mean the fall of Lehman Brothers in September 2008 and the subsequent attempts of leading governments to stave off economic collapse by using taxpayers' money to save the banks. Now that their capacity to print new money has been almost exhausted, the world is in the grip of a growing sovereign debt crisis where several minor European countries may be followed by the default of Japan, Britain or even the United States. This is a turning point. Its denouement may be global depression, world war, fascism or democratic revolution, but eventually the contours of a new era for the world will become clearer. One way of approaching this moment of transition is to ask not what is beginning, but what is ending. This is not straightforward either.

World history since 1945 falls into two distinct periods divided by the watershed of the 1970s. In the first, developmental states generated economic growth through extending public services and increasing the purchasing power of working people. The second saw the unfettered expansion of money, markets and communications and a general increase in economic inequality. We may label them respectively the social democracy variant of national capitalism and neoliberal globalization or one-world capitalism. In any case, the rich benefited from the switch. Some think that the neoliberal paradigm still best describes our world. I believe that free market economics has been holed beneath the water by the financial crisis. But the current break in history goes far deeper than the recent replacement of social democracy by neoliberalism. We are witnessing the end of the social form that has dominated

the twentieth century. I call it "national capitalism" and its origins lie in the political and technological revolutions of the 1860s. Its historical trajectory includes two phases of financial imperialism each lasting three decades, from the 1880s and the 1980s. The former ended in the First World War, so we had better watch out! Accordingly, I find it necessary to distinguish between money and finance. I shall argue that the financial crisis is only superficially a question of credit boom and bust. At bottom it is the unravelling of the social organization of money that the world has come to live by since its inception a century and a half ago. But as always folk models lag behind social realities.

## The origins of our times\*

The 1860s saw a transport and communications revolution (steamships, continental railways and the telegraph) that decisively opened up the world economy. At the same time a series of political revolutions gave the leading powers of the coming century the institutional means of organizing industrial capitalism. These included the American civil war, Britain's second reform act and Japan's Meiji Restoration. German unification spilled over into the 1870s through the Franco-Prussian war, the Paris commune and the formation of the French Third Republic. Karl Marx published *Capital* in the same decade (1867) and the First International was formed in 1864. This concentration of so many epochal events in such a short time would indicate a degree of integration of world society even then.

Capitalism has always rested on an unequal contract between owners of large amounts of money and those who make and buy their products. This contract depends on an effective threat of punishment if workers withhold their labour or buyers fail to pay up. The owners cannot make that threat alone: they need the support of governments, laws, prisons, police, even armies. By the mid-nineteenth century, it had become clear that the machine revolution was pulling unprecedented numbers of people into the cities, where they added a wholly new dimension to traditional problems of crowd control. The political revolutions of the 1860s were based on a new and explicit alliance

between capitalists and the military landlord class to form states capable of managing industrial workforces and of taming the criminal gangs that had taken over large swathes of the main cities.

This epochal moment in world history lacks commemoration in literature, but Martin Scorsese's movie *Gangs of New York* (based on Herbert Asbury's 1927 book of the same name) shows how the Irish gangs of Southern Manhattan were subdued in the context of the civil war by shelling from battleships in the East River. Mass protest over conscription spilled over into America's first urban riots involving poor whites and black refugees from the South. The movie's final scene fades in Manhattan's contemporary skyline over its 1860s predecessor, suggesting that capitalism today was made possible by state violence then.

"National capitalism" is the modern synthesis of the nation-state and industrial capitalism: the institutional attempt to manage money, markets and accumulation through central bureaucracy within a cultural community of national citizens. It is linked to the rise of large corporations as the dominant form of capitalist organization and governments soon provided new legal conditions for their operations, ushering in mass production and consumption through a bureaucratic revolution. What followed was in essence Hegel's recipe in *The Philosophy of Right* (1821), the idea that states, run by university-trained bureaucrats, should regulate capitalist markets with a view to containing their extreme consequences, while allowing their material benefits to accrue to the people as a whole. The national system became general after the First World War and was the dominant social form of twentieth-century civilization.

The 1970s were a watershed. US expenditure on its losing war in Vietnam generated huge imbalances in the world's money flows, leading to a breakdown of the fixed parity exchange-rate system devised at Bretton Woods during the Second World War. America's departure from the gold standard in 1971 triggered a free-for-all in world currency markets, leading in 1975 to the invention of money futures in Chicago to stabilize export prices for Midwestern farmers. The world economy was plunged into depression in 1973 by a hefty rise in the price of oil. "Stagflation" (high unemployment and inflation) increased, opening the way for neo-conservative liberals such as Reagan and Thatcher to revive the strategy of giving economic priority to "the market" rather than "the state".

In 1975, all but a minute proportion of the money exchanged internationally paid for goods and services purchased abroad. Three decades later, payments of this kind accounted for only a small fraction of global money transfers, the vast bulk being devoted to exchanging money for money in another form. This rising tide of money represented the apotheosis of financial capitalism, with the production and sale of commodities and political management of currencies and trade virtually abandoned in favour of feeding an autonomous global circuit of capital.

## Money in the national community

Money expands the capacity of individuals to stabilize their own personal identity by holding something durable that embodies the desires and wealth of all the other members of society. The modern system of money provides individuals with a vast repertoire of instruments to keep track of their exchanges with the world and to calculate the current balance of their worth in the community. In this sense, money's chief function is *remembering* (Hart 2000). People learn to understand each other as members of communities; and money is an important vehicle for this. The common people share meanings (cultural symbols) as a way of achieving their practical purposes together. If wealth was always a marker of identity, then the shift to wealth in the immaterial form of money, a process speeded up and expanded by the digital revolution, contributes to the growing volatility of identity. Once fixed or "real" property was dominant as its marker, but this function has now been split between value realized in consumption and hierarchies of value expressed as abstract quantities. Money is intrinsic to both of these.

In this way, money defines each of us by articulating the relationship between individuals and their communities. The nation-state has enjoyed such tremendous success over the last century or more that we find it difficult to imagine society in any other form. I identify five ideal types of community, all of them represented by the nation-state. The nation-state has been a *political community* capable of offering its citizens a single vehicle for relating to the world outside, as well as the framework of law regulating their internal affairs. It has been a *community of place*, resting on territorial principles of association with definite boundaries of land and sea. It has also been an *imagined or virtual community*, a constructed cultural identity relying on symbolic abstraction of a high order. It has been a *community of interest*, in both the subjective and objective senses,

uniting members in trade and war by a shared purpose. Finally it has been a *monetary community*, built by shared use of a national monopoly currency. The rise and fall of single currencies is one way of approaching national capitalism's historical trajectory. But the story of modern money goes further back than that, as the history of the dollar shows.

## The dollar: a history

The United States began life as a federation, not as a nation-state. A case can be made for its having become the latter after the Second World War launched America as a global power. But the country's history contains a more plural, decentralized model of political and monetary community. Although the US dollar is the world's reserve currency today, the Americans had to develop their own money in a world dominated by greater powers, especially Britain. Moreover, at various times in their history, they suffered from severe scarcity of currency and witnessed conflict between regions and classes over the uneven shortages brought about by centralization of money in a single form. The issue of local scrip as a temporary solution for the lack of liquidity is an American tradition more than three centuries old.<sup>3</sup>

In 1695, soon after the invention of the Bank of England and with it the national debt, Britain banned the export of precious metals (specie), even to its own colonies. So the Americans, who had no gold or silver of their own, had to use foreign silver coins, mostly of Spanish origin from Mexico. They called these "dollars", after the most common name for such coins, *talér*. The Founding Fathers were not greatly impressed with the term, sometimes preferring to talk of a "unit" of currency, but they could not think of a better name and the dollar stuck.

From the 1690s, the settlers printed various types of paper money for local use. But Benjamin Franklin did more than anyone to promote the idea, writing in 1729 *A Modest Enquiry into the Nature and Necessity of a Paper Currency*. Franklin could be said to have been an information specialist, with a preference for open source distribution of knowledge. He was basically a printer and inventor who refused to seek patents for his many discoveries, leaving them to be manufactured by whoever wished to do so. He helped to launch paper money in three colonies and travelled to London in 1766 to protest the British ban on the use of paper money there. Perhaps for this pioneering

advocacy, Franklin's head is on the largest denomination American banknote, the hundred dollar bill.

The American revolution was the first war financed by paper money. The Second Continental Congress issued paper bills of credit and imposed heavy penalties for refusal to accept them as currency. After the British gave up, the government redeemed these "continentals" at the rate of a cent to the dollar. Americans won the war with a paper currency that caused many of them to lose their shirts!

In the second half of the nineteenth century, Britain was able to impose a gold standard on world trade. Governments had the choice between restricting their money supply to whatever was backed by gold or of issuing a national scrip that was worthless in international exchange. In the United States the federal government issued no paper money, restricting itself to minting coins in specie which were in short supply. This left the money supply in the hands of states and private banks who issued their own paper. The record of these free banks ("wildcats" to their detractors) was not bad. But there was always pressure to create a central bank monopoly and the Civil War provided the opportunity for this. The National Bank Act of 1863 was followed by a tax on notes issued by the states. Three Legal Tender Acts sanctioned the issue of paper money or "greenbacks". In 1879, having won the war and built up its gold reserves, the federal government finally felt able to back its dollars with gold.

Immediately voices arose seeking to make money plural again. The People's Party (better known as the Populists) found their support mainly in the South and West, among poor farmers. They flourished during the first age of financial capitalism, when New York was beginning to rival London as the world's main money centre. They wanted the government to address the chronic cash shortage in some parts of the country by issuing more paper money and unlimited silver coins. The rising price of gold and a corresponding fall in agricultural prices squeezed America's farming communities; but the main cities enjoyed a boom in international trade, splitting the country on class and regional lines. Blaming Eastern bankers and politicians, the Populists settled on a monetary policy of bimetallism (silver coins in addition to the gold-backed currency). Their champion was William Jennings Bryan, twice defeated as Democrat candidate for president in 1896 and 1900. Bryan famously told the East Coast establishment, "You shall not crucify mankind on a cross of gold".



Also in 1900, a journalist called Frank Baum published an allegory, *The Wonderful Wizard of Oz*. A tornado lifts Dorothy and her dog out of their Kansas home and deposits them in the East. Dorothy and her companions set out on the “yellow brick” road to Oz (referring to gold, as ingots and ounces), evoking an 1894 march by the unemployed demanding more money and work for the common people. On the way she picks up a scarecrow (farm worker), a tin man (factory worker) and a cowardly lion (William Jennings Bryan). The Emerald City (New York) is controlled by the Wizard of Oz (a contemporary plutocrat), who fools the Munchkins (the people of the city) into not seeing how he and the bankers manipulate the levers of power. After the Wizard is exposed for what he is, the tin man gets a bimetallic tool and Dorothy’s magical silver slippers take her back to Kansas.

Congress passed the Gold Standard Act in 1900, committing the US to even more reliance on gold. But discoveries in South Africa, Alaska and elsewhere increased the supply of gold and commodity prices rose. So Americans had their cake and ate it, at least until the Wall Street Crash of 1929 drove everyone else off the gold standard and into a new regime of national paper currencies. Richard Nixon completed this process in 1971. Today most people just know that the US dollar rules the world economy. The Europeans have floated the euro, an enormous political blunder whose consequences are only being felt now after the 2008 crash. And *The Wonderful Wizard of Oz* is a children’s story, chiefly memorable for Judy Garland’s screen performance. Nevertheless, the Fed’s money-printing machine puts pressure on the dollar’s role as the world’s reserve currency, as does the spectacular imbalance of national accounts following the rise of China as the world’s manufacturer. So this story is far from being finished.

## Alternatives to national monopoly currency

The nation-state is such a powerful and enduring social form that, although single currencies have been with us for only a short time, were only partially realized and have been breaking up since the 70s, it is very hard to dislodge the idea of money as legal tender in a sovereign territory to which its users belong. There are plural alternatives to national monopoly money in the form of thousands of community and complementary currencies (Blanc 2010; but most people are initially reluctant to embrace new approaches to money (Hart 2006).

The situation is psychologically complex, however. On the one hand, conventional money flatters our sense of self-determination: with some money, we can exert power over the world at will. On the other hand, there is comfort in the notion that money is not in our control at all. As an exogenous force of necessity, it serves, in a manner analogous to number, to promote clarity of judgment and action, whereas otherwise things might be frighteningly wide open. If they issued their own currencies, people would not only be freer, but would have greater responsibilities also.

There is a strong parallel with slavery. The monopoly claimed by national currency is felt to be inevitable, since no-one would freely choose it. To be told that there are viable alternatives makes nonsense of a lifetime’s enslavement to an unrewarding system. So we cling to what we know as the only possibility. We often talk about wanting to be free, but we choose the illusion of freedom without its real responsibility. This is perhaps why we prefer money not to be of our own making. We spend it, but we never have enough of it because “they” keep it scarce. People have to be sold the idea of making their own money; and this involves challenging with their most cherished beliefs.

If it is difficult to persuade people consciously to adopt new ideas, another obstacle is the unconscious use of old models when they form new associations. The nation-state has successfully represented society for a century or more, so that we have internalized its principles and reproduce them whenever we construct new forms of community. It is not surprising that, when people come together to make alternatives to the national economy, they often replicate it in their design for a new association – as a stand-alone multi-purpose community of like equals rather than, say, as a federated network of unequal social entities (Hart 2006).

A stand-alone community currency is like a radio or TV that can only tune to one station, a computer with just one programme. Supporting trade between people who keep their accounts in different currencies requires that the registries can communicate with each other through a cross-clearing network. This would be operated primarily through the internet, using its own money domain naming system. This facility would be further enhanced by ‘multi-cc’ smart-card systems. The cards can currently carry up to 15 different currencies at a time, off-line and anonymous, and are designed to make community money systems easily adopted in the retail sector. The card system enables every participating business also to have a loyalty loop

specific to their own business, if they choose. Of course, co-ordination is difficult when there is no one body concerned with establishing standards. In order to provide a genuine alternative to national monopoly money, community currencies should mimic what mainstream money has already become – a multitude of monetary instruments issued by a distributed network of institutions including far more than governments and the banks.

## The evolution of money today

Georg Simmel in *The Philosophy of Money* (1900) argued that money's substantial form (precious metals, then coins and paper) would wither away and be replaced by social institutions. Its functionality (the ends to which it is put and the technical means of its organization) is emancipated from substance and money's essence (what people use it for in society) is progressively revealed. This could be identified, following Karl Polanyi (1944), as a shift from commodity to token money. Money, according to Simmel, always introduces a third party to bilateral exchange – the community that shares its use.

Simmel referred to money's function as exchange and measurement, but Polanyi, (*Money objects and money uses*, 1977), identifies the conventional four functions of money as means of payment, standard of value, store of wealth and medium of exchange. "All-purpose money" unites these four functions in one symbolic form, "modern money". Money's functions were attached to different symbols before (special-purpose monies). Similarly, multiple currencies were always in circulation before the invention of the bank rate gave teeth to central bank control. This pluralism is rapidly becoming the case again. Jane Guyer (2004) has shown that it was always so in West/Central Africa, while Akinobu Kuroda (2008) makes the same case for China and medieval England.

If finance is the management of money, "financialization" (Epstein 2005) describes the situation since the 1970s when institutions specialized in money management (banks at first) have grown in size and influence while the money circuit has become detached from production, trade and political oversight. Money is increasingly exchanged for money in another form rather than for goods and services. The digital revolution in communications has vastly accelerated and cheapened electronic transfers, allowing many more institutions specialized in particular monetary instruments to join governments and banks in a

distributed network supplying money in multiple forms (Hart 2000). Faced with the returns on using their capital for finance, firms like General Motors relegated making cars to a secondary concern. The attempt to manage state control of the economy through regulating the money supply became much less relevant.

So Simmel's prophecy of the triumph of function over substance has been realised, thanks in part to technical innovations of the last few decades. But if the essence of money is its use within a community using shared social institutions, this second leg of money's double anchor (the other being traditionally its substance) is in just as bad shape, since central bank currencies helped crucially to define where society as a community of belonging or for that matter the state are; and that is no longer so. At the same time money itself has become intuitively much harder to define, since it is breaking up (Dembinski and Perritaz 2000)! Globalization has stimulated the formation of new supra-national groupings like the EU and ASEAN, while two-thirds of the 100 largest economic units on the planet are now corporations, not countries. Digital communications support new forms of commerce and association worldwide. Local currencies have sprung up in their thousands. Corporate loyalty systems (air miles) multiply (Blanc 2010).

The financial crisis of 2008 was at one level the bursting of a credit bubble that took a quarter century to build up. What goes up comes down and all that. The larger states moved to bail out the banks, while promising to rein in their profligacy (split up investment and retail branches, curtail bonuses etc). But this didn't last and the use of financial means to solve intransigent economic problems has left the world on the edge of deeper systemic failure, now manifested as a sovereign debt crisis and the threat of a double-dip recession. Nothing has yet been done to restore consumer demand in the leading western economies and all of them look vainly to exports as their salvation. In the meantime, the banks and other corporations exploit the plurality of national jurisdictions to ensure that they are not held accountable for their financial recklessness.

When it comes to money, one size does not fit all and it never has. But the national moment in history established the strong illusion that it could be so. The Europeans adopted a single currency before they had established the political conditions for its survival and at a time when all-purpose money was breaking up. If Simmel was right and



money, having lost its substance, must be shored up by a community's social institutions, there will have to be as many monies as there are communities. The digital revolution has begun to make that technically feasible. But there is clearly a contradiction between the technical possibilities for organizing money today and the idea of society as a closed hierarchical community rather than as a decentralized egalitarian network. The break-up of both the functions and issuers of all-purpose money is reflected in the dollar's contested role at home and in emergent world society. Scores of countries flock to join the dollar's umbrella rather than maintain an independent money of account (Dodd 2005). And everyone knows that if the dollar fails, there will be no world economy left at all; so reluctant savers put their money in US Treasury notes. The French and Chinese periodically grumble about the unfair advantages conferred by the dollar's role as the world's reserve currency; but a current account deficit on the present scale is not necessarily a boon. Society has escaped from its former home and has not yet found another one. Money must be central to any temporary or lasting solution. This is the meaning of today's economic crisis. The banks have done much to ruin the financial system and little to justify their preservation. But solutions will have to go far beyond regulating them and tinkering with their form.

## Money in the making of world society

Polanyi (1944) believed that money and markets had their origin in the effort to extend society beyond its local core. Money, like the sovereign states to which it was closely related, was often introduced from outside; and this was what made the institutional attempt to separate economy from politics and naturalise the market as something internal to society so subversive. Polanyi distinguished between "token" and "commodity" forms of money (Hart 1986). "Token money" was designed to facilitate domestic trade, "commodity money" foreign trade; but the two systems often came into conflict. Thus the gold standard sometimes caused deflation that could only be alleviated by central banks printing more paper. The tension between the internal and external dimensions of economy often led to business crises.

It is, however, no longer obvious where the levers of democratic power are to be located, since the global explosion of money, markets and telecommunications has severely exposed the limitations of national frameworks of economic management. A return to the national solutions

of the 1930s is bound to fail. There are substantial parallels between the last three decades and the similar period before 1914. In both cases, market forces were unleashed within national societies, leading to rapid capital accumulation and an intensification of economic inequality. Finance capital led the internationalization of economic relations and people migrated in large numbers all over the world. Money seemed to be the dominant social force in human affairs; and this could be attributed to its greater freedom of movement as the boundaries of society were extended outwards, then by colonial empire, now by the digital revolution and transnational corporations. The main difference is that the late nineteenth century saw the centralization of politics and production in a bureaucratic revolution, while now these same bureaucracies are being dismantled by neoliberal globalization. Moreover, the immediate winner of "the second thirty years war" was a strengthened national capitalism whose synthesis of state and market; the winner of the next one will have to be truly global.

The principal function of money and markets is to extend society beyond its existing limits. Thus Malinowski's (1922) ethnography of the *kula* ring could be taken as a metaphor for the world economy of his day, with island economies that were not self-sufficient being drawn into trade with each other by means of personalized exchange of valuables between local leaders. These canoe expeditions were dangerous and magical because their crews were temporarily outside the realm of normal society. This always happens when society's frontiers are pushed rapidly outwards, as they have time and time again in the last two centuries and long before that. The recent period could be compared with previous episodes in the history of global capitalism, such as the dash to build continental railroads, the gold rush and the wild rubber boom of the mid- to late 19th century. Further back there are episodes like the "South Sea bubble" and the "Tulips craze". We have just seen a rapid extension of society's frontiers after the post-war convergence of state and market in national capitalism reached its limit in the 1970s. The quick wealth and cowboy entrepreneurship was made possible by the absence of regulation in a period of global economic expansion. The end of the bubble marks an opportunity to consider how world markets might now be organized in the general interest.

It is easy enough to harp on the irrational excess and sheer inequality of the neoliberal era – the heedless speculation, corporate skulduggery, outrageous looting of public assets, not-so-creative destruction of nature and society. But there

are lasting institutional effects, just as there were to previous booms which generated transport and communication systems; a mildly inflationary gold standard; new industrial uses for rubber; stock markets and colonial empires. The extension of society to a more inclusive level has positive features; and, before we demonize money and markets, we should try to turn them to institutional ends that benefit us all. The world economy is more integrated than ever; we need new principles of political association with which to put in place more effective regulatory frameworks. Fragmentation would be a disaster. I for one would not wish to return to currency controls and state-managed money, even if it were feasible.

Clearly, the political questions facing humanity today concern distributive justice. The long period of Western dominance of the world economy is coming to an end. New actors on the world stage will have their say about who gets what. An escalation of war and general fractiousness is quite likely. Under these circumstances, a focus on the socially redemptive qualities of money and markets might be quite salutary.

**Keith Hart** is Honorary Professor of Development Studies, University of Kwazulu-Natal, Durban and of Social Anthropology, University of Pretoria. A version of this paper was presented as a public lecture of the Institute of Public Knowledge, New York University, 22<sup>nd</sup> February 2011. His web site is <http://thememorybank.co.uk>.

## Endnotes

<sup>1</sup>This argument was first laid out in Hart (2000); a more recent version is Hart (2009).

\*I owe much of the following account to the anthropologist Jack Weatherford's *The History of Money* (1997:111-177).

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# Economic Governance in the Eurozone: A New Dawn?

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The European sovereign debt crisis was the first big challenge to the euro. After much initial doubt about the survival of the eurozone currency, the German Chancellor, Angela Merkel, and the French President, Nicolas Sarkozy, agreed on a joint Franco-German plan for the 17 members of the Eurozone to ensure the long-term stability of the monetary union. At the summit in Brussels on 4th February 2011, both leaders announced that eurozone governments would embark on coordinating their economic policies. According to Merkel, the goal of the "Pact for Competitiveness" was to harmonise the conditions of the national markets and systems in order to increase the competitiveness among the members of the eurozone. The present 17 members of the eurozone are asked to coordinate their tax, pension, labour, and budgetary policies. While the Pact includes the 17 members of the eurozone, Angela Merkel emphasized that the other 10 non-eurozone countries can join in what she called the "17 plus" Pact. Already at the time of negotiating the European Stability Mechanism in December 2010, the EU-president, Herman Van Rompuy, was given the task to draw up a permanent Financial Stability Mechanism by the end of March 2011. In consultation with other eurozone leaders of governments and head of states, Van Rompuy is to report back with concrete steps on converging national fiscal and tax policies.

That the stability of the euro was high on the agenda of both Berlin and Paris was the message Angela Merkel and Nicolas Sarkozy tried to get across at the Economic Forum in Davos in January 2011. Sarkozy warned investors betting against the European single currency. "Never, listen to me carefully, never will we turn our backs on the euro, never will we drop the euro" (NYT 27.1.2011). Angela Merkel in introducing the new economic governance mechanism unequivocally stated that "we defend the Euro not only as a currency, but as a political project" (Press conference 4.2.2011).

Despite strong initial opposition to the French-German proposal (particularly from Austria, Ireland, and Belgium), the "Pact for Competitiveness" is remarkable for several reasons. Germany has always resisted the French call for *gouvernement économique* at the EU level going back to the 1980s. As recently as March 2010, Angela Merkel qualified the French call for economic coordination during the negotiations for a Greek rescue package. Unlike France, Merkel insisted at the time that the package for Greece should only be granted as "ultima ratio". In return for accepting the strong language on monetary stability, Nicolas Sarkozy could claim partial victory in gaining support for better economic governance in the eurozone. But Merkel qualified her support for economic governance by insisting that she endorses only better economic governance. In fact, many media pundits at the time suggested that the German agreement to economic governance was a hollow promise given Angela Merkel's strong opposition to any economic coordination (Young/Semmler 2011).

The recent German-Franco "Pact for Competitiveness" raises several questions about the future institutional framework of the eurozone. Why has Angela Merkel made this U-turn and suddenly endorsed the need for macroeconomic governance at the Euro-level? Does the broad response of Germany and France to the euro crisis signal a deepening of institution building so that monetary union is finally accompanied by economic (if not political) union? Will it strengthen the EU Commission (community method) to retain the sole right to propose legislation as championed by Jacques Delors, a former president of the Commission, or would it strengthen the intergovernmental cooperation (union method) which would mean that economic governance is decided among head of states and government leaders? Most importantly, do France and Germany agree on the definition of economic governance, or does Merkel intent to force the deficit economies to follow Germany's disciplined monetary and fiscal example? The mere fact that Angela Merkel refused to discuss any details of economic convergence to boost competitiveness at the joint press conference on February 4th in Brussels indicates that differences remain between France and Germany in how they define economic convergence (FT 5/6 February 2011).

## The stony road to the “Pact for Competition”

Looking back to the initial response to stem the sovereign debt crisis erupting first in Greece in 2010, then spreading to Ireland, Portugal and even Spain, the leaders of the eurozone reacted hesitantly, uncoordinated, vacillating whether to come to the rescue at all, making sure that the eurozone did not turn into a transfer union, emphasizing that the debt crisis was a home-made problem of the peripheral countries, that the crisis had little to do with the global financial crisis, and was not the result of the eurozone imbalances between deficit and surplus countries. Given these initial fragmented, uncoordinated and national policy responses to each new turn in the sovereign debt crisis, the question arises what has changed that made Germany finally join France in providing a more cohesive policy response to the eurozone crisis in 2011.

It is worth remembering that the rescue package agreed for Greece in May 2010 did not provide a mechanism to ensure the long-term stability of the eurozone. In addition, the debt negotiations were done in the absence of the European Commission. The rescue operation was an inter-governmental affair between government leaders and head of states in which the Commission and the European Parliament were side-lined. Rather than stemming the crisis through the “community method” involving the European Commission proposing a common framework to resolve the crisis, it was Germany who largely set the tone for how to resolve the crisis. Debt ridden countries were singled out for their culture of fiscal profligacy. The discourse surrounding the rescue operation focused on the lack of domestic discipline in the peripheral countries who supposedly lived beyond their means. No mention was made that the German and French banks, in particular the German WestLB and the Commerzbank in combination with French banks, were heavily exposed to Greek public and private debts. The rising government bond spreads between the core and the periphery offered high returns to German and French banks. In April 2010, the yields on 10-year Greek bonds went as high as 7.38 per cent widening the spreads over German bonds by 435 basic points and raising doubts over Greece’s ability to service its deficit. The cost of insuring against a Greek debt default reached thus record heights. As a result, the Greek sovereign debt crisis, as was subsequently the case with the Irish sovereign debt crisis, was as much a crisis of undercapitalized European banks. For Barry Eichengreen, the renowned European economic scholar, the appropriate answer to the sovereign debt crisis

would have been to endow the German (also French and UK) banks with sufficient capital so that they can withstand a debt restructuring rather than bailing out the debtor countries (Eichengreen 2010).

Instead of providing leadership for a joint eurozone response, German euro-politics focused largely on domestic concerns and was overly nationalist in tone. The German government argued, and had the support of most of the public behind it (62 per cent of voters reject further bail-outs, and 61 per cent support Merkel’s actions) that Germany did its homework by making production more competitive, rationalizing the labour markets and modernizing the social welfare system with the Agenda 2010, and made every attempt to balance the budget up until the financial crisis. Instead of reaping the benefits for these, quite often, painful efforts, Germans were now called upon to bail out the Greeks. It is not surprising that many analysts criticized Merkel for her Euro-scepticism. Whether Merkel’s hesitancy had to do with party politics of not wanting to confront the German voters with the prospect of bailing out Greece before a critical state election in North Rhine-Westphalia in May 2010, or whether the constraints of the Constitutional Court in Germany, which had previously set strict conditions in its rulings on various aspects of the Lisbon and Maastricht Treaties, were responsible for the slow response is open for speculation. Tony Judd, the recently deceased historian, argued that Merkel’s slow reaction had to do with her East German background. “Angela Merkel having grown up in the East does not appear to have the slightest understanding of the essence of the EU and the costs which are associated with its neglect” (*Die Zeit*, 12.8.2010:44).

Finally it was the pressure of the bond markets which forced even a recalcitrant Angela Merkel into action to agree to a rescue package, since the interest spreads among the eurozone countries started to destabilize the euro currency. Angela Merkel’s hesitant intervention between February and May 2010 was criticized, since it increased uncertainties in the eurozone markets and drove the CDS swaps and yields on government securities to ever greater heights. This drove up the final price of the rescue package (Fricke 2010). The crisis was momentarily stabilized with a rescue package in May 2010. A safety net of € 750 billion was put together by the European Union and the International Monetary Fund. The rescue plan consisted of € 440 billion eurozone-backed loan guarantees for stricken eurozone members raised by a newly created European Financial Stability Facility (EFSF), in addition a €

60 billion European Union balance of payment facility to raise debt by the European Commission using the EU budget as collateral, and € 250 billion loans from the International Monetary Fund. Berlin also passed an emergency law to permit the government to lend € 22.4 billion over three years as part of the eurozone rescue plan. The ECB also was given new powers to intervene in public and private debt markets, plus extra measures to boost eurozone bank liquidity, and to buy government bonds from indebted countries starting in May 2010, which the ECB had never done before and which was controversial even among some of the members of the ECB. This exceptional activity of the ECB had personal ramifications. Axel Weber, the head of the German Bundesbank, member of the governing board of the ECB and a possible candidate for the succession of Jean-Claude Trichet resigned from his position at the Bundesbank in February 2011 citing the disagreement within the European Central Bank over its crisis management which he considered outside the Bank's mandate. The rescue measures for the indebted countries were equally controversial in Germany across the political spectrum and resulted in a number of formal complaints to the German Constitutional Court arguing that the rescue plan breaks the "no bail-out plan" of the European treaties (Sinn 2010: 10).

While the Eurozone leaders took their time to respond to the sovereign debt crisis, the national debt and budget deficit ratios in terms of GDP skyrocketed in the so-called PIGS countries (Greece national debt increased to 130 per cent and the budget deficit to 8 per cent of GDP; Ireland debt ratio increased to 94 per cent and the budget deficit to a horrendous 32 per cent of GDP, 10 times the Maastricht criteria of 3 per cent; Portugal which may still become the next default candidate has a national debt of 83 per cent and a budget deficit of 7 per cent of GDP). Ireland finally had to be bailed out by the EFSF in November 2010. In response to the Irish crisis, Angela Merkel insisted that the rescue in the amount of € 85 billion for a period of three years had to be embedded in a broader strategy to set-up a new bail-out system for future defaulting countries, to strengthen the Growth and the Stability Pact by enforcing fiscal discipline, to introduce a permanent crisis mechanism with stringent conditions, and to involve private investors after 2013 in the event of a sovereign debt crisis. Her untimely demand to involve private bold holders in any losses incurred as a result of the sovereign debt after 2013 frightening the bond markets, increasing the interest rates even further Ireland and other peripheral countries had to pay on the capital markets. As a result, the sover-

eign debt crisis worsened. Even her supporters such as the CEO of Deutsche Bank, Josef Ackermann, called Angela Merkel's remarks "very unfortunate". (Die Zeit-Online 6.12.2010a). In response to these massive critiques levelled against Germany, Wolfgang Schäuble, the German finance minister, argued in the Financial Times that the financial markets do not understand the specific construction of the euro. "We have a common monetary union, but we don't have a common fiscal policy. We need to convince the international public and international markets that this is a new form, very specific to meeting the demands of the 21st century" (Schäuble, FT 6.12.2010: 3).

Up to late October 2010, Germany rejected the notion that the stabilization of the monetary union needed more than stringent fiscal discipline. The problem of the sovereign debt countries was squarely seen in the fiscal profligacy of the peripheral countries. A puzzle remains why Germany focused on public debt as the culprit of the sovereign debt crisis. It was private debt in Spain and Ireland that was the Achilles heel of the sovereign debt crisis. Both Ireland and Spain had solid fiscal positions until the state had to bail out the banking system (Dodd 2010). Thus focusing on measures to enforce a more stringent Stability and Growth Pact targets only such countries as Greece but not countries whose debts are the result of the private banking sector.

Despite these rescue efforts, the markets remained unimpressed. Once again Angela Merkel and Sarkozy met to negotiate a mechanism to safeguard the financial stability of the eurozone. The result was a horse-trade agreed upon in Deauville in October 2010. Merkel insisted on strict fiscal discipline and thus suggested automatic punishment for those violating the Stability and Growth Pact. France was against this automatism, but in return Paris agreed on amending the EU treaties to create a permanent mechanism involving private creditors. The treaty change was necessary so that a permanent crisis mechanism could be enacted. The draft of a permanent stability mechanism was announced by the European Council on 17.12.2010. Under the leadership of Herman Van Rompuy, the European Council president, two essential elements were introduced. First, a permanent liquidity facility (the European Stability Mechanism) was created to replace the present European Financial Stability Facility put together during the Greek crisis in May, which expires in 2013. This new ESM is to help indebted countries with severe cash flow problems. However, Angela Merkel rejected at that time to raise the ceiling of € 440 of the present fund, and insisted that the

crisis mechanism can be triggered only as a last resort based “on a stringent programme of economic and fiscal adjustment and on a rigorous sustainability analysis conducted by the European Commission and the IMF, in liaison with the ECB”. Any assistance has to be decided unanimously by the Eurogroup Ministers (European Council 2010: 6-9). Second, standardized and identical collective action clauses (CACs) will be included for all new euro area government bonds starting in June 2013. This means that if a government is unable to service the debt, it will allow all debt securities issued by a Member State to be considered together in negotiations, including those who disagree with the majority vote. This is a legally binding change to the terms of payment and includes standstill, extension of the maturity, interest-rate cut and/or haircut in the event that the debtor is unable to pay (European Council 2010).

To enact these changes, a paragraph was added to Article 136 of the Treaty on the Functioning of the European Union (TFEU), which said: “The Member states whose currency is the euro may establish a stability mechanism to be activated if indispensable to safeguard the stability of the euro as a whole. The granting of any required financial assistance under the mechanism will be made subject to strict conditionality” (European Council, 2010: 6). In addition the European Council agreed that Article 122(2) of the TFEU will no longer be needed. The government leaders will meet in March 2011 for the formal adoption, which will then have to be ratified by the 27 EU member states. The permanent crisis mechanism will come into force on 1 January 2013 (Young/Semmler 2011). Germany’s insistence on fiscal discipline in these negotiations, Merkel’s refusal to raise the debt ceiling of € 440 billion, and in particular her unequivocal rejection of the Luxembourg-Italian proposal for jointly guaranteed Eurobonds to help finance the indebted countries within the eurozone led to angry attacks against Germany. Jean-Claude Juncker declared in a *Die Zeit* interview that Germany “thinks a bit simple, is un-european in how it handles business at the European level, and designates certain discussions as taboo-zones” (*Die Zeit*-Online 8.12.2010).

If the Germans had intended to calm the bond markets in the eurozone with the announcement of a permanent crisis mechanism and stem the harsh criticism against the discipline imposed on euro Member States, they were wrong on both counts. The crisis has stabilized, but Greece, Ireland, Portugal, and Spain are suffering from severe budgetary cut-backs, reduction in economic

growth, and social unrest. There is much speculation that at least some countries will have to resort to debt restructuring, since the indebted countries will be unable to service their huge debts. Nor have the critical voices against Germany subsided. Martin Wolf’s headline in the *Financial Times*: The Eurozone needs more than discipline from Germany, (22.12.2010: 9) sums up the feelings of many economists and political leaders even within Germany. The former German foreign Minister and Germany minister of finance, Frank-Walter Steinmeier and Peer Steinbrück, argue that Germany has become increasingly isolated within Europe by insisting on a “German Europe” rather than a more “European Germany”. (FT 15.12.2010). Tough fiscal discipline with limited emergency funding at high interest rates, and draconian domestic adjustments is a cure which most believe will kill the patients. Surely the question is whether “voters in Ireland, Portugal, Greece or Spain tolerate a decade of austerity just to stay in a union with Germany” (Münchau, FT 20.12.2010).

### Economic Governance: A new dawn for the Eurozone?

Two months after the ink had barely dried on the draft of the permanent European Stability Mechanism, Merkel and Sarkozy announced the “Pact for Competition” to harmonize economic governance in a joint press conference on 4th February 2011. The question is whether this is a break with the past fragmented, national-oriented, uncoordinated piece-meal response to the turmoil of the eurozone markets. Surely, the mere fact that European leaders recognize that monetary union needs to be complemented with economic governance is a huge step forward. The present configuration of the European Monetary Union has a birth defect which was discussed at the time, but only came to full bloom during the sovereign debt crisis. Centralizing and transferring monetary policy to the European Central Bank, but leaving fiscal policy in the hands of national governments meant that macroeconomic coordination was sacrificed. This divided sovereignty (Jabko 2010) between the eurozone and national governments resulted in widely diverging economic and current account developments in member states. Unlike Helmut Kohl who reminded the members of the German Bundestag in 1991 that “(T)he Political Union is the indispensable complement to the Economic and Monetary Union. The recent history, and not just Germany’s teaches us that an enduring Economic and Monetary Union without a Political Union is not going to work” (Issing 2010: 3), Angela Merkel instead



defended the prerogatives of national sovereignty over tax and fiscal policy.

Given the stony road to resolve the sovereign debt crisis, the latest reform proposal, the “Pact for Competitiveness”, can be read as a new dawn for the eurozone. It signals that two very different ideas of economic policy making practiced in Germany and France may move closer together. In other words, it may lead to greater sovereignty for economic policy coordination at the EU level. Up until now two diverging concepts and ideas of economic policy-making have prevented macroeconomic governance at the eurozone level. Germany traditionally insists on the independence of the European Central Bank, a concept which is quite foreign to the French who have always advocated a more political influence for monetary policy at the ECB. Secondly, the German practitioners of the Social Market Economy put their faith in rules as the fundamental framework for economic policy-making. Thus while many euro-watchers may look bewildered at Germany’s insistence on exact rules for the Stability and Growth Pact or rules for a rigorous debt ceiling for the European Stability Mechanism, this rule-orientation has the intent to avoid political maneuverings over which Germany has no control. Thus it is not surprising that Angela Merkel has until now vehemently rejected the French call for more discretionary and political influence over economic policy.

Nicolas Jabko (2010) argues that since 2000 there has been some rapprochement between the French notion of *gouvernement économique* advocating a more active macro-economic management and the German notion of rule-setting. Particularly, the creation of the Eurogroup in 2004, which was an informal discussion group of the European finance ministers, headed by Jean-Claude Juncker, provided the first forum outside the formal decision-making body of the Economic and Financial Affairs Council (EcoFin) to arrive at common decisions. This nascent impetus of economic coordination received a strong boost when Nicolas Sarkozy saw the financial crisis as a window of opportunity to call for more economic coordination starting in 2008. As chair of the European Council, Sarkozy called for a “European Action Plan” to introduce a rescue plan for the European banking sector. In fact, it was Nicolas Sarkozy and Gordon Brown who initially led the rescue initiative at the EU level and not Angela Merkel. In the process, Sarkozy re-defined the concept so as to make it more palatable to the Germans. Jabko argues that from October 2010 onward, Sarkozy spoke of economic governance which he defined as “the coordination and peri-

odic steering of European economic policies by national political leaders” (Jabko 2010: 33). Shifting from the stronger *gouvernement économique* to economic governance means that no new transfer of power to the EU-level is involved. Thus it is not surprising that Angela Merkel at the press conference introducing the “Pact for Competition” on the 4th February reiterated time and time again that economic coordination does not imply “new competence for Europe”. According to Angela Merkel, economic coordination means that heads of state and government leaders would coordinate their economic decisions, which would need the approval of national parliaments.

That the media pundits and analysts immediately criticized the “Pact for Competition” as moving away from the “common method” of the EU and toward the “union method” in which head of states meet to coordinate economic policy is understandable. José Manuel Barroso, the Commission’s president, in a muted response criticized the idea that no additional competence was granted to the EU to solve the debt problem. He reminded the government leaders that the EU treaty provides the right framework for coordination. Critics are also correct in pointing out that the Pact has the strong handwriting of Germany. Insisting on a constitutional amendment for a debt-brake in each eurozone country to control public borrowing (as Germany has done to take effect in 2016) surely signals that Germany continues to believe that the sovereign debt crisis is the result of a lack of fiscal discipline. Only a rule-based constitutional amendment can, so the German argument, ensure fiscal prudence throughout the eurozone.

That Germany tries to imprint its stamp of economic governance on the EU is not surprising given the asymmetry of power between creditor and debtor states. As Kenneth Dyson (2010) pointed out the power over ideas in how to solve the euro crisis and the power in shaping the outcomes lies with the creditor nation and its belief in euro rules to safeguard the principles of the stability of monetary policy within the ECB. The “EMU was designed around ‘sound money’ and ‘sound finance’ ideas that were German in origin” (Dyson 2010: 604). What is new is that Germany is no longer outright rejecting economic and fiscal governance at the eurolevel. Not surprisingly Angela Merkel has defined the “Pact for Competition” according to German ideas. Despite the criticism from many member states to this German-French proposal, the Pact may turn out to be a watershed for macroeconomic coordination at the EU-level.

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# The Euro Trouble and the Global Financial Crisis

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The problems around the Euro are still far from being settled. The trouble started with the rumor around a possible Greek insolvency in early 2010 which triggered a series of meetings of the European Governments. At the end, the principles of the Maastricht treaties were revised in two major points: First, a joint rescue fund, called "European financial stability facility" (EFSF), was created in order to help member states to refinance themselves at acceptable conditions. In practice this meant that the "no bail-out" principle of the Maastricht treaties was abandoned – at least until the scheduled termination of the program in 2013. Second, the European central bank abandoned her sacred principle of not buying state bonds and intervened in favor of Greece. At that time it had been already clear that Greece would not remain the only country having problems with refinancing its public debt; further candidates – Portugal, Spain, Italy, Ireland, Belgium – became the object of concerns and were downgraded in their credit ratings. After Greece, Ireland run into acute trouble and had to seek shelter under the European umbrella. Interest rates and risk premiums for Portuguese and Spanish bonds have risen remarkably too, and the European Commission has entered into controversial discussions with the Governments on the proposal of a further expansion of the EFSF (Der Spiegel 2011) and on the idea of introducing "Euro bonds". The strongest resistance against a further Europeanization of public debts comes from the German Government, who is not enthusiastic about the prospect of taking the role of a permanent paymaster. However, as a consequence of the lasting political discussions, unrest in the capital markets will continue and most likely will create further trouble for the Euro.

The present dilemma has reanimated the old debate on the contradictory institutional design of the Euro. It is water on the mills of the Euro-opponents who now feel fully justified in their view that a common European currency could not work without a political union or at least a political coordination of fiscal and economic policies. However, the Euro crisis must be seen also in the context of the global financial crisis after 2008. Without that earlier crisis

it certainly would not have developed in the same way. As we know today, the American subprime crisis had been only the prelude of a global crisis, resulting from a long term over-accumulation of private financial assets, which additionally had been promoted by aggressive expansionary strategies of the international finance industry. A tremendous volume of uncovered titles had been piled up which due to its dimensions and inherent "systemic risks" could not simply be written off. Therefore the crisis became a political issue. The US- and European Governments intervened by voluminous parcels of credit, credit guarantees, subsidies and public expenditures in order to prevent a deepening of the collapse. They exchanged "bad", defaulted private assets for "good" public bonds, thus actually guaranteeing the profitability of private capital by tax money. On the one hand that helped to bring about an immediate stabilization, on the other hand, public debts exploded due to the costs of the bailout programs and to the fiscal strains resulting from the economic downturn. The increase of public debt had been even more marked in the US and in Britain than in Euroland. As a result, the financial markets became suspicious about the creditworthiness of the very agency that saved them from collapse, the national states. This means that the financial industry has managed to externalize her own problem and to transform it into a problem of the states.

Both factors – lack of fiscal and economic coordination in the European monetary union (EMU) on the one hand, the impact of the global financial crisis on the other – actually are interacting in the present European crisis in a complex way. This can be shown briefly for the cases of Greece and Ireland.

At first sight, Greece seemed to be a clear case of European mismanagement which showed clearly the deficiencies of political coordination within the EMU. The public sector was inefficient and disorganized, corruption and circumvention of taxes were widespread practices, public debt was far above the Maastricht criteria even before the country joined the EMU. The access to the union had been made possible only with the help of faked statistical figures. The membership in the EMU then had the effect of an invitation to continue the inherited practices, additionally prices, wages and imports soared – until the situation finally became untenable in 2010. There is no doubt that

the Greek problems would not have reached the present dimensions, if the country had kept its own currency. On the other hand, there is no debt without credit. Without the cooperation of the international finance industry, including Goldman Sachs and even more, German private and public banks, the accumulation of such a voluminous debt would not have been possible either. For the investment banks, Greek bonds offered a profitable outlet for their idle capital. In spite of the dubious circumstances, the business appeared almost risk free, as the banks could expect to be bailed out in the case of emergency. Among the German banks, the most engaged purchaser of Greek bonds was the Hypo Real Estate bank. The same bank came into serious trouble during the financial crisis and had to ask for Government support. Because of the "systemic risks" involved, the Federal Government finally decided to nationalize the Hypo Real Estate bank. This explains why Germany – after some hesitation – took initiative for a coordinated European action in favor of Greece. A possible default of Greece would have meant a considerable additional financial burden for the German Government herself. By agreeing to the help for Greece, Germany actually rescued her own bank sector. Seen from this point, the Greek crisis does not simply reveal the consequences of the institutional deficiencies of the EMU. Actually, the Greek case demonstrates the intermingling between these deficiencies and the repercussions of the global financial crisis.

The case of Ireland seems to be completely different from the Greek one. Until the outbreak of the financial crisis, the country was a model for fiscal solidity with annual budget surpluses in the years before 2008 and an accumulated public debt of only 25% of GDP. The disaster came with the international financial crisis and the subsequent collapse of the domestic housing boom which previously had generated spectacular economic growth rates. Again German banks were heavily involved. With the economic recession and the enormous expenses, the Government had to shoulder for the stabilization of the domestic banks, the public household deficits exploded. At first sight, the Irish crisis – and also the Spanish one which shows many similarities with the Irish constellation – appears to be a direct outcome of the international financial crisis. Nevertheless it would be premature to conclude that it had nothing to do with the economic coordination deficiencies of the EMU. The housing boom itself had been possible only on the background of the central regulation of interest rates in the EMU. Given the high rates of inflation and the strong increases of nominal wages not only in Ireland,

but also in Spain, the interest rates set by the European Central Bank were clearly too low for these countries, although appropriate for Germany. The cheap financing costs were a decisive factor heating the housing boom, moreover prices, wages and import surpluses soared. Again the conclusion is that the crisis is the outcome not only of one factor but of the interaction of two problem complexes: The financial crisis as well as of the EMU coordination deficiencies.

A thorough debate on ways out of the present dilemma has to consider this intermingling of the two problem complexes. Any possible solution for one of the two problems will not necessarily provide a solution for the other one, with the likely result of an overall failure. The most radical way to solve the EMU coordination problems would be the return to national currencies (Krugman 2010), or, alternatively, splitting up the Euro bloc into a "strong" northern and "weak" southern zone. This would mean the restoration of the foreign exchange market as the key coordinating mechanism of the European Economies. However, even if such a solution could be achieved without creating a monetary chaos, at reasonable costs and within reasonable time – which is not realistic –, the key objection against it is that it would not solve the debt problems of the EMU member states. Contrarily, the debt burden, which still would be denominated in Euro, would become completely unbearable for the southern states. At the same time, the "stronger" states in the north would have to write off a considerable part of their foreign investments. Moreover, the outcome for the northern states – in particular for Germany – would be a drastic appreciation of their currencies, with corresponding negative consequences for exports, growth and state revenues. Thus, even the "strong" economies would suffer from an abandonment of the EMU. This makes it highly unlikely that the German, Dutch and French Governments will follow the populist moods against the Euro in their countries and underlines the credibility of their determination to defend the euro.

Today, almost everybody agrees about the need of an improved "coordination" of national fiscal and economic policies at EU-level. The political "deepening" of the EMU, which always has been demanded by the Euro-criticizers, now meets almost unanimous support among political and economic decision makers. Actually however, this is a thorny issue already going back to a vast discussion. The Maastricht sanctions against member states violating the budget deficit benchmarks have proven nearly inefficient in

practice. The German Government herself (besides France) had been one of the pioneers in circumventing the Maastricht stability pact in 2005. Member states getting assistance from the European rescue fund indeed have to accept a tight supervision of their budget policies and to commit themselves to fiscal austerity. However, even if the Governments are able to secure parliamentary support such unpopular measures, the key point is again that fiscal austerity is not a remedy against the overdebt problem (Spahn 2010). To the contrary, policies of raising taxes and reducing expenditures will curb economic growth and make the national debt burden even heavier. For highly indebted states it will become even more difficult to escape the vicious circle of declining tax revenues and rising interest obligations. Fiscal austerity has a symbolic function as a ritual of self-sacrifice that may calm down the capital markets for some time; however they cannot cure the real problem. The European Governments are now facing the challenge to find a viable strategy for the time after 2013 when the EFSF will run out.

According to widely discussed ideas, the European Commission should be equipped with enlarged powers to coordinate the fiscal and economic policies of the member states, including the right to intervene into national tax policies and expenditures, perhaps even to regulate trade imbalances (Dullien/Schwarzer 2010). Many of these ideas do not appear overly realistic either, as they would presuppose a cumbersome and time consuming revision process of the EU treaties. Moreover, they would further nourish the already virulent concerns about the democratic deficit of the European Union, and will meet correspondingly strong political and juridical opposition. An additional transfer of economic regulatory powers to the EU commission would also touch the delicate political balance between "small" and "large" and economically "weak" and "strong" states. The strong states will resist any arrangement that will oblige them to pay the cost of the regulations without giving them a corresponding amount of political control. Last, but not least: Even if the idea of giving more power to the European Commission would succeed, it again would hardly help to settle the overdebt problem of some member states. In short: The idea of politically "deepening" the EMU looks sympathetic and meets approval from almost all sides. In practice however, progress on this way, if possible at all, will be slow and cumbersome. What remains, are appeals to improve the intergovernmental coordination of economic and fiscal policies within Europe (Schäuble 2011). The EMU members find themselves in a situation which actually ties them

together (because the breakup of the union is no viable alternative), without being able to establish an efficient coordination mechanism in the foreseeable future. This is a constellation which is likely to breed continuing political conflicts and unrest at the capital markets.

If there is anything like a "key" for all difficulties, it lies in the debt burden which the EMU states (like other ones) had accumulated even before the global financial crisis, but which had been enlarged substantially by the latter. Without a solution of the debt problem the chances for a political deepening of the EU will be equal to nil; if a solution would be found, this would surely also improve the success chances of the Euro. The problem of overly indebtedness – to emphasize it again – cannot be cured by austerity measures. The only way out is that the private creditors must be brought to renounce a part of their claims, be it in the form of an ordered restructuring of the debt, or in the form of a general "haircut". Given the dimensions of the problem, a one-for-all tax on all capital assets could also be considered. To raise tax revenues, higher taxes on capital incomes and a general financial market transaction tax would be helpful either. However, just these potentially most efficient measures are the most difficult to be executed. The mere discussion about them is being avoided because of her negative performative effects on the markets. They would induce capital flights and meet strong political opposition from the side of the proprietors and the international financial lobby. They could be efficient only under the presupposition of a minimum of international political coordination within and beyond the EU. Given the disappointing experiences with transnational coordination of financial markets at G-20 level (Mayntz 2010), quick progress on this way again does not appear likely.

Given the prospect of Portugal joining the club of EFSF-recipients perhaps in the near future, of continuing refinancing problems of the members of this club, of interest rates and risk premiums on the bonds of further member states (Spain, Italy, Belgium, France) to rise, what will actually happen then? As Germany with its strong export economy is the main economic profitier of the EMU – the key economic and political decision makers are well aware of this – it is not a risky prediction that the German Government will give up her current resistance against a further expansion of the EFSF and perhaps even to a partial introduction of Euro-bonds during the next acute crisis. Moreover, Germany possibly will have to take steps in order to reduce its current excessive export surpluses and

to stimulate domestic demand. However, there may come a point where even the German accumulated debt, which too has already grown significantly above the Maastricht limit of 60%, might reach a critical level. To prevent or at least slow down such a development, the pressure on the European Central bank to keep interest rates low and to purchase bonds of overly indebted states will remain and increase. Clearing the problem with the help of central bank money surely would be the easiest solution, the way of least resistance, which under the given circumstances certainly has its charm for the decision makers. And there is no reason for premature alarm, because with such a policy the European Central bank would only follow the footsteps of the British, US and Japanese central banks. Actually, the monetary policy of the European central bank had been comparatively conservative and restrictive so far, so that surely there would still be some leeway on such a path. However, what would be the outcome, if a reflationary race between the key global currencies should develop? A wave of inflation, resulting perhaps in a new financial crash would annihilate the stock of global capital assets probably to a degree that would surpass by far the losses which the owners would have had to expect in the case of an ordered restructuration. Thus, again I arrive at the conclusion that the debt problem is the key for settling the trouble of the Euro. The question is only whether the solution will come about in a politically coordinated way, or via the burst of a new global financial bubble with unforeseeable social and political repercussions. Clearly it is the first option which would be preferable, but unfortunately it does not seem the more realistic at present.

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# Should Crisis-Hit Countries Leave the Eurozone?

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## Introduction: the Eurozone crisis

The economic crisis within the Eurozone has led to renewed debate about the future of monetary union. Some ask: should Greece and Ireland voluntarily leave the Eurozone, reclaim their fiscal autonomy, and re-introduce national currencies either parallel to or alongside the Euro? What does the experience of citizen-led monetary experimentation tell us about the ability of civil society or subaltern groups to create their own forms of money when that provided by states fails? This is interesting as traditionally the left has been indifferent to the form of money, focusing on the exploitative nature of the relationship between worker and employer, or between the state and the mass of people during crises. Workers should struggle for more money, and better conditions. In a crisis, working people should refuse to pay the cost of a crisis they were not responsible for. Others argue for the abolition of money in favour of co-operation. But the form of money is rarely considered: we don't often hear about struggle for 'another' kind of money, even though there is a rich but hidden history of monetary contestation which goes back to Robert Owen in the UK, the Populists in the US, and the German and Swiss Freemoney networks of the Great Depression (North 2007). Could the Eurozone crisis give birth to a new politics of money? This paper discusses the options.

## Progressive support for and critiques of the EU project

The left has always had an ambivalent and conflicted relationship with the European ideal. Social democrats in many European centre left parties have long been attracted to the internationalist and solidaristic elements of the European Union. The European ideal was of making wars between countries who had engaged in the brutal, prolonged and industrialised destruction of each other's populations within living memory impossible (Lieberman 1992).

Mechanised war over a whole continent involving the systematic aerial bombing of civilians and scorched earth policies by retreating German and Soviet troops left 61 million human beings killed and a continent devastated, and the socialists in the wartime European resistance wanted to ensure this would never happen again. They developed plans for European unity based on a brotherhood of many to replace the Europe of Nations which, many argued, merely led to endemic warfare. The new international social order would also eliminate poverty, disease and unemployment, as well as irrational belligerence and xenophobia. Economic warfare and protectionism was largely believed to have led to the Great Depression. The construction of the European Coal and Steel Community aimed at integrating France and Germany's war fighting capability, making belligerence impossible.

Now, war between European countries seems not only unimaginable, but, if theorists of economic integration are right, physically impossible when nation states do not control their national economies any longer. Other attractions for the left included the 'social Europe' of the Delors plan which was a concrete alternative to the decimation of the welfare state and opt out of the social chapter under Thatcher, a solid alternative the bleak argument that 'there is no alternative'. Post-1989, pan European internationalism expanded to the entry of former Soviet dominated-states. Thus, for the centre left, 'Europe' signifies internationalism and solidarity, as opposed to the little-England nationalism and xenophobia of the Eurosceptic right. Centuries of war have given way to a shared feeling of sovereignty, of which the euro is both "the most evident symbol and deepest material form of this shared sovereignty" (Mulhearn and Vane 2008).

More radical left voices have seen the EU more as a vehicle for corporate neoliberal forms of globalisation than as a utopian internationalist project (Baimbridge, Birkitt et al. 2005). Their concerns have focused on the single market as a tool for big business to reduce labour and environmental standards through an insistence on opening up procurement in the public sector to pan-European, to the benefit of multinationals willing to undercut local providers with higher standards. At a macro-economic level the growth and stability pact that accompanied the Euro is seen as a tool for 'disciplining' national economies that do

not sign up to the Washington Consensus of balanced budgets and fiscal 'responsibility' and 'stability' above job creation and the protection of working people's living standards. In another context, Dinerstein (2001), following Bonefeld and Holloway (1996), calls this the 'violence of stability'. Left critics argue that membership of the EU prescribes progressive nationalist projects like the Labour Left's Alternative Economic Strategy (Cripps, Griffith et al. 1981) or 'Local Socialisms' of the 1980s (Boddy and Fudge 1984; Mackintosh and Wainwright 1987), which looked to protect manufacturing industry from what we now know was the first wave of what Harvey called the 'spatial fix' of a crisis of capitalist productivity – the move of manufacturing to lower cost and lower regulated countries (Harvey 1992). The Cambridge economist Ha Joon Chang argues persuasively that weaker economies might just as much want to protect and nurture their growing economic resources from globalising pressures as a family protects and nurtures its children: we expect them to make their way independently at eighteen, but not at eight (Chang 2007).

Greens share the left's charge that the EU is more of a vehicle for neoliberal forms of globalisation than for internationalism and solidarity, but their concerns focus more on the role of the single market in privileging big, global business over smaller local firms trading in local markets and thereby contributing to local distinctiveness (Scott Cato 2005). The single market, greens argue, leads to a bland, standardised 'clone town' economy (nef 2010) dominated by global brands (Simms 2007). The benefits to ordinary citizens of a pan-European currency – more convenient European holidays – are less obvious. Greens also point to the absurdity of the carbon emissions and avoidable consumption of limited fuel resources associated with identical products been produced in one country and transported to another to be sold: for example, Dutch butter sold in the UK and British butter sold in the Netherlands (Woodin and Lucas 2004). They argue for a greater commitment to local, more self-reliant economies as opposed to avoidable global trade (Douthwaite 1996; Shuman 2001; Cavanagh and Mander 2004). Their attachment to the local should not be conflated with a commitment to autarky or to xenophobia. Rather they argue for trade subsidiarity: for producing things as close to where they are used as makes economic and ecological sense. Critics would argue that they underplay the benefits of international trade and communication associated with progressive conceptions of globalisation (North 2010).

In reality, concerns about the potentially restrictive and repressive nature of the growth and stability pact proved to be overblown as Germany and France, as well as the UK, studiously ignored its constraints by running up budget deficits and deregulating finance. In practice, no left wing or green government in the Eurozone attempted any radical alternative that required 'disciplining'. Rather, neoliberal globalisation seemed dominant. Dominant, until the financial collapse of 2007-8 beginning with the sub prime crisis in the US, spreading to the UK and thence to the Eurozone. Massive Keynesian reflation seemed to stave off financial collapse, but at the cost of huge sovereign indebtedness. Not for the first time, private greed in the financial sector led to huge losses which were socialised: private debts became sovereign debt, and the markets demanded cuts in public spending in the indebted nations to recover stability. The crisis hit Greece and Ireland the hardest, with Spain and Portugal in the danger zone. The newly elected coalition government in the UK used the threat of the market to drive through significant cuts in public spending and of working people's standard of living. Resistance across Europe varied, with significant mobilisations in Greece, Spain and Portugal, with a more muted response in Ireland and the UK. The question then raises its head: why put up with this 'violence of stability'? Should countries threaten to default on their debts and renegotiate terms on a more favourable basis, or actually default?

### The Eurozone – an optimal currency area?

At this stage it is worth rehearsing the arguments for monetary union irrespective of the claimed pathologies or otherwise of a neoliberal politics of financial stability and the effects of the growth and stability pact. Mundell (1961) argued that an 'optimal currency area' is one where the benefits outweigh the costs. The argument is that replacing national currencies with a continent-wide Euro would be more efficient by reducing transaction costs for trade across borders, leading to more trade and, it is claimed, greater welfare. It would be easier to compare prices across space, so prices will be driven down. Less uncertainty about exchange rate fluctuations leads to welfare gains, so businesses can make long term plans. The result is less uncertainty about prices. Finally, opportunities for speculation on fluctuations between competing currencies will disappear, preventing otherwise functioning markets from being disrupted by herd behaviour. A bigger, more efficient market will encourage more trade, more

inward investment, more efficient location decisions, thus more growth and improved human welfare (De Grauwe 2000). National economic sovereignty is a chimera in an age of globalisation, and the benefits of integration by far outweigh any costs. Leaving the Eurozone would forfeit these benefits.

Against this, the Eurosceptic right argue that joining a single currency means that a country loses the ability to conduct national monetary policy (Redwood 2001). Its central bank ceases to exist, or has little power. It loses the freedom to revalue or devalue, or determine the quantity of money in circulation, or to affect the exchange rate with other currencies to make imports and exports more or less expensive. It can't affect interest rates to promote or retard borrowing and job/sme creation. For Eurosceptics, the loss of a national currency is equivalent to the loss of identity and of freedom. It is part of a broader move to an integrated Europe, seen as a centralised superstate. They have a preference for a Europe of Nations and free trade, and minimal regulation at EU level. Redwood also challenges the claimed peace building credentials of a single currency and of economic integration. He argues that war has been avoided as France and Germany developed democratic, peaceful values endogenously, and that NATO, not the EU, has kept the peace. If European Governments did want a war, he argues, "a small secretariat in Brussels would not be able to stop them". Redwood argues that the benefits of peace come from trade and free markets, not from a single currency, and that the rise of Irish, Flemish, Northern Italian and Catalan nationalism shows that, if anything, people want more, smaller countries, not integrated super-states. Small countries often see a currency as an essential element of sovereignty.

Both sides agree that a single currency means that national governments lose the power to affect the extent that consumers want to by domestic or foreign goods, or take account of local cultural, legal or socio-political characteristics that have an effect on the economy such as the rate of small business set ups, labour market flexibilities, the strength of trade unions and/or protest groups, or the extent that consumers spend or save. The result, as every geographer knows, is that differences across space means that growth rates may be different in different part of a currency union, with identical economic conditions at the continent level. Green critics argue that one monetary and interest rate and money rate means it can be too loose for surging regions, too tight for struggling ones. Jane Jacobs (1984) suggests the surging ones dictate it – their econo-

mies overheat, while lagging economies struggle. Jacobs argues that more localised currency circulations act as 'surge breakers', preventing crises reverberating around a large economic area, and enabling monetary policy to fit local conditions – harder in surging regions, softer in lagging ones. A continent wide currency like the Euro and US Dollar cannot fulfil this role. Echoing Jacobs, the new economics foundation's David Boyle argues that "big currencies pervert the accuracy of economic information fed back from local economies to the centre, and the consequent devaluing of local life."

Those who argue that the Euro is an 'optimal currency area' argue that over time the relentless drive towards efficiency and growth driven by a single European currency will force local and national economies into an equilibrium. People will move to where the opportunities are, putting pressure on wages and reducing pressure on surging economies. The then British Chancellor Gordon Brown consequently set out his five 'Economic Tests for Joining the Euro'. Before agreeing to join the Eurozone he wanted evidence (1) that the UK economy was harmonised with the Euro zone, (2) that there sufficient flexibility. If the UK went into recession with no control of monetary policy and with fiscal policy limited by the growth and stability pact, could it cope? The other three tests were that joining the Euro would have a positive effect on investment decisions, on financial services (given London's pre-eminent world role), and on growth and jobs. Brown thus argues that the Euro would demonstrably be working as an optimal currency area for the UK to join. As we know, the Euro failed the test in Brown's eyes.

Critics of the Euro argue that this is as the equilibrium mechanism doesn't work as effectively as it should in theory in a Europe of nation states speaking different languages, with different local cultures, and different economic conditions. Americans share political sovereignty and language, they argue, meaning they can move in a way that Europeans find more difficult. But also this can be overblown: some people can be dependent. You do get many young people from higher regulated European countries moving to lower regulated UK for work, while many American states in the deep South have entrenched poverty that is not mitigated by emigration or economic integration (Harvey 1992). A mass of reasons might make individuals and businesses, 'locally dependent', unable to move easily (Cox 1997). So the experience is that the European economies have not come into equilibrium over the past 10 years, while monetary policy has proved too

tight for countries, struggling with sovereign debt like Ireland or Greece, be it newly socialised or more structural. So should countries like Ireland and Greece call it a day and leave the Eurozone?

### Should countries leave the Eurozone?

There are three possible scenarios. A country suffering economically within the Eurozone could leave, or be forced out through market pressure. National currencies could be re-introduced, and the country regain a measure of control over monetary and fiscal policy denied it by being within the Eurozone: either to boost the economy using Keynesian methods, or by allowing its currency to float against the Euro in the expectation that it will lose value, making that country's exports cheaper. The Punt or the Drachma would be like the UK pound: EU membership would be combined with monetary independence under the control of market surveillance. Crucial here would be the attitude of the markets. Would it be welcomed as a return to normality, as opposed to the aberration of participation in a single currency that was not in that country's interests? The parallel here would be sterling's expulsion from the ERM in 1992. The British Monetary Policy Committee and Bank of England independence operates within the same neoliberal paradigm as the Euro – fiscal rectitude and stability is key – thus providing a plausible neoliberal alternative to the Euro. Other central banks could do the same.

The other example from which to draw again is not strictly the recreation of a defunct national currency, but is worth consideration: Argentina's abandonment of the 'peg', linking the peso to the US dollar, in 1992. Here again, market pressure and a bank run forced the authorities to break the Peg and let the Peso float (Halevi 2002; Blustein 2005). It lost 75% of its unrealistic valuation against the dollar, but did provide a boost to Argentine exports, with the economy achieving credible levels of growth in subsequent years. Here, despite market disapproval, Keynesian policies worked for the country, against IMF advice. The country successfully renegotiated its debts.

A country leaving the Euro would be recreating its own banknotes and coins: a more considerable rupture than the examples above. There would be the inevitable costs of dislocation. The attitude of the rating agencies would be crucial. If they believe that the move is inevitable or beneficial, then the costs might be worth paying; but there would be a penalty to be paid if the decision to leave was

deemed to be 'irresponsible'. Argentina, a globally peripheral country big enough to be able to make its own way in the face of the opposition of the rating agencies was able to make its policies work, perhaps as many of the agencies felt that the decision to leave should have been taken much earlier than it was. In that situation, the penalty for staying in could be higher than that of leaving. This is a political and economic judgement that needs to be made. Perhaps it is easier for more peripheral countries, like Argentina. Again the extent that Ireland, Spain, Portugal and Greece are 'peripheral' in relation to a Franco-German European heartland is a political call. The EU makes formerly 'peripheral' countries more central in the eyes of the market, as their actions can have ripple on effects for large, strategically more central countries like Germany. Leaving then would be a politically charged decision with costs and benefits that would need to be weighed.

### A common, but not a single currency?

The second option would be to avoid the disruption of full withdrawal and revive a national currency or create a new national or (in larger countries) regional or more local currency to run alongside, rather than replace the Euro. This would circulate at a national or regional level alongside the Euro, allowing consumers to choose which currency met their needs better. National or regional agencies could engage in more Keynesian policies at a local scale, while the benefits in reducing transaction costs for international trade remain. This echoes calls for the introduction of the 'hard Ecu' by the Major government in the run up to the introduction of the Euro, or the situation in Argentina after the introduction of the peg in the 1990s where the Provinces, which have the right to issue currency under the Argentine constitution, did so (Cohen 1998). The difference is that the country would not leave the Eurozone, but would supplement it with its own currency.

Again, the attitude of the ratings agencies would be crucial. If they judged long term membership of the Eurozone to be problematic, and default inevitable, then provided that they felt that the new national or regional currencies were being issued responsibly and growth was restored, they might support the policy: or at least pragmatically tolerate it. The IMF tolerated Argentina's Patacones until they felt that their issuance was less local Keynesianism, but a mechanism for supporting clientelist practices (North 2007:173). There have been calls for Greece to temporarily introduce the Drachma on this basis. David McWilliams

argues that the reintroduction of the Irish Punt is the only way to avoid Irish collapse. The political call here is the extent that a national currency alongside the euro would be seen as credible, and that it would be seen as less disruptive than full withdrawal.

Given this, the likelihood of national governments reintroducing a national currency out of crises environments is low, if only as a result of fear or possible repercussions from the markets. Could other actors do so, within civil society? As Josh Ryan-Collins reported in a previous newsletter (Ryan-Collins 2010), the last twenty years has seen an effervescence of community-based local money networks from Local Exchange Trading Schemes and Time Banks to the regional Berkshares notes in the United States and Regogeld in the German Länder (North 2010). When governments failed to act, community groups have stepped into the void. However, these networks are generally small, and, while often valued by their members, it seems difficult to see them being scaled up to a level where significant levels of economic transactions are being carried out using them. LETS and Time Banks are networks of between 20 and a couple of hundred participants exchanging time and labour using a virtual currency, with no physical form. Argentina did see mass usage of similar local networks during the crisis of 2001-2 (North 2007), but this seems unique. Generally, community based currencies are too small scale to provide access to a wide enough range of goods and services that they can be considered as a real alternative to conventional money. Circulating at a small, local scale, they do not act as an 'optimum monetary area' for even small businesses that trade locally, selling locally produced goods and services. Even the more ostensibly small business-friendly 'transition currencies' in Totnes, Lewes, Stroud and Brixton have quickly come up against the limits of how little is produced locally in a globalised economy (North 2010).

There are some seeds of hope. Ryan-Collins (2010) discussed the experiences of the Swiss 'Wir' network, with thousands of business members and a history going back to the Free-work Movement of the 1930s. The EF Schumacher Society of Great Barrington's Berkshares are issued in partnership with local banks, and seem to be taken more seriously than a purely community-created currency by local businesses as a result. Germany's Regiogeld builds on strong regional and local tradition in a country that was only united from a confederation of states and city-states in 1870. The first regional currency, the Roland in Bremen, was established in 2001, followed closely by the Chiemgauer in Bavaria. In 2008 there

were 28 regional currencies across Germany, some run in partnership with local banks and co-operatives. Given that one of the fundamental characteristics of money is that they should be issued by a trustworthy institution if users are to have and maintain confidence in them, regional currencies issued by trustworthy regional institutions might be able to operate at a scale below that of the nation state, and thus avoid actual or potential surveillance and control by the ratings agencies: yet be robust enough and circulate in a large enough geographical space for them to be useful for significant amounts of economic activity. Countries with strong regional institutions, independent of the state, yet also responsible in their money issuance policies and accountable to those who spend it, might be a suitable vehicle for a new raft of regional currencies supplementing, rather than replacing, the Euro. This might be particularly appropriate for regions with a strong identity, with a tradition of independent political thinking and action, and endowed with enough locally-owned production such that a regional currency could circulate independently of national or continental currencies; Bavaria, Catalonia, Emilia-Romagna, perhaps Yorkshire, spring to mind. From small acorns, more robust local momentary institutions could emerge.

## Conclusion

Ireland and Greece could yet default on their debt to the Eurozone, yet the likelihood of either country taking serious action to regain their economic independence seems far-fetched. The 'common sense', taken for granted benefits of the Euro and European integration seem incontestable outside the Eurosceptic right. Withdrawal seems a step away from the European ideal, a step back to the failed economic nationalism of the past, or even a concession to xenophobia. On the other hand, what matters is more national policy than the form of money. Britain's continued possession of a national currency has not protected elites from the perception that radical action is needed to reassure the ratings agencies of the country's solvency. Swingeing spending cuts are the order of the day in Euroland Ireland and sterling zone Britain. There seems little appetite for the reintroduction of national currencies. It might be more appropriate, then, to work at a regional level to develop currencies that operate alongside the Euro, but at a scale large enough for businesses to find them attractive. Germany's experiment with regional currencies is worth following to see if they can pass an empirical test of usefulness that has defeated smaller scale local experiments.

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# The Level of Financial Literacy of Russians: Before and During the Crisis of 2008-2009

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## Abstract

The main goal of this paper is to address the issues of defining and measuring the concept of 'financial literacy' in all-Russian surveys as well as to reveal the changes in the level of financial literacy of Russians during the period of 2008-2010.

The main finding of these surveys is that the level of financial literacy of Russians is low. During the crisis it started growing but only in terms of self-estimation and perception. In 2009 people thought that they were more financially literate than before the crisis. However, when they answer questions in the objective tests, a substantial change in attitudes, knowledge and skills can hardly be noticed.

## Introduction

Since the beginning of the 1990s and, especially after the current economic and financial crisis, the issues of financial education have risen on the agendas of different actors in many countries in the world. The growing complexity of financial products has become one of the factors of the increased concern. On the one hand, a lot of new retail products widen the scope of tools for increasing the economic well being of individuals, on the other – it has become the responsibility of individuals to use them appropriately. However, many people still lack the basic understanding of what matters for their finances. For example, the conversion of the pay-as-you-go pension system into the current accumulative one assumes that people save and invest money for their retirement. However, it has become a common case in many countries that individuals are saving too little for

their pensions. Another example is the overcrediting on credit cards which also indicates that financially illiterate consumers are not making the good decisions for their families and are undermining their economic security and well-being.

Growing concern about the low level of financial literacy resulted in the implementation of national strategies for the promotion of financial literacy in many countries. In Russia, such a strategy is about to be announced. To make the national strategy more efficient one needs to know the existing level of financial literacy of the individuals, the areas of their strengths and weaknesses as well as their preferences and needs regarding the learning process. The main goal of this paper is to address the issues of defining and measuring the concept of 'financial literacy' in all-Russian surveys as well as to reveal the changes in the level of financial literacy of Russians during the period 2008-2009 of the current financial crisis. The first part of the paper discusses the conceptual and operational problems in measuring the concept of 'financial literacy' in consumer surveys. The second part summarizes recent trends in the level of financial literacy in Russia over the crisis period.

## 1 Defining and measuring the concept of financial literacy

Even though we can find examples of empirical research on financial literacy in the 1990s it is only in the early 2000s that the first attempts to elaborate standardized instruments to measure financial literacy were made. However, even today there is no agreement between the scholars about both conceptual and operational definitions of the 'financial literacy' concept (Huston, 2010, p.296). Let us consider some of the debates in this field.

### 1.1 Financial literacy or financial capability?

The concept of 'financial capability' was developed in the UK by the FSA which extended the concept of 'financial literacy' beyond the scope of financial knowledge only to include behaviour and attitudes of people.

The rationale for this approach was based on the idea that if people do not practice what they know they can not be considered financially literate. For example, if people know that they have to keep track of their finances but they do not do that – this knowledge could not be marked as an indicator of financial literacy. The same approach can be applied to retirement savings, provision for an unexpected expense, seeking advice from an appropriate professional adviser before buying financial products, taking individual responsibility for financial decisions and etc. So, to assess financial literacy one needs to assess the ability to apply knowledge to take effective decisions in managing personal finances.

An interesting methodological question is whether the similar approach can be used for measuring the level of financial literacy in the institutional contexts of middle and low income countries. At first sight it is obvious that this should be generally true for all countries. However, it is not so because of the peculiarity of the institutional settings of the financial markets in these countries. Weak financial markets institutions result in the lack of financial savings or the presence of paternalistic attitudes of people. However, this 'deviant' behaviour and 'wrong' attitudes do not necessarily have to be considered as signs of the financial illiteracy of people. For example, in volatile financial markets and under high inflation rate the lack of savings for retirement or not enough money provision for unexpected expenses could be motivated by individuals' risk aversion rather than by the lack of financial sophistication. When financial institutions are weak financial literate people may prefer to rely on their social networks or collective actions based on paternalistic attitudes as effective decisions regarding the use and management of money rather than individual financial strategies. For example, a lot of small investors who participated in the IPO of VTB bank later experienced rapid decline of prices on their shares. Some of them addressed the government to force the bank to buy their shares back at a price which they bought them during the IPO. In terms of financial literacy paradigm this is clearly an example of illiterate behaviour since people do not understand the individual responsibility for taking financial decisions. However, if markets are manipulated by powerful players, collective actions of minor shareholders could be considered as effective financially literate response.

Since the National Foundation for Educational Research (UK) defined financial literacy as "the ability to make

informed judgments and take effective decisions regarding the use and management of money" (Noctor et al, 1992) one has to accept the rejection to buy financial products as a sign of financially literate behavior.

## 1.2 Attitudes or preferences?

In the previous section of this paper we argued that behaviour may not be a proper indicator of financial literacy in the middle and low income countries. But what about attitudes? The term 'financial capability' was introduced to emphasize that not just knowledge, understanding, practical skills but also proper attitudes which were included into the concept.

In the light of the problem of defining the financial literacy concept it is important to understand if 'proper' attitudes (savings for the rainy days, insurance against the unexpected expenses, individual responsibility in financial issues, etc.) to financial planning and savings should be considered as part of a financial literacy concept or they should be conceptualized as preferences which economists usually assume as given and be excluded from this concept. One may argue that overcrediting or saving too little may be considered as effective financial decision for consumers which are impatient and deliberately acts in accordance with their impatient preferences. The same argument may be developed for risk tolerance and paternalism in financial issues. The main question is whether in the process of measuring financial literacy we can consider the lack of savings, risk taking behaviour or paternalistic attitudes as signs of financial illiteracy or it is better to assume that those people act in accordance with their preferences and nothing can be said about their level of financial literacy. This approach is based on the concept of rationality in Economics which assumes that individuals attain their goals with the least possible costs, whatever these goals may be. If a person aims at going bankrupt and does it efficiently with overcrediting and risky investments his or her actions cannot be considered as non-rational and illiterate.

There are two ways of dealing with these questions. We can assume that attitudes, since it is impossible to differentiate between them and preferences, should be excluded from the concept of financial literacy and the operationalisation should be based on the knowledge and skills only. However, I think that we may do more than taking into account that rational behaviour assumes

logical consistency of individual preferences. The example of a person who aims at going bankrupt on purpose and does it efficiently with overcrediting and risky investments may be considered financially illiterate if he or she nevertheless wants to secure his or her investments by the state patronizing schemes because this will prevent him or her from achieving the initial goal of going bankrupt. To conclude, given perceived opportunities, attitudes which prevent people from optimisation may be considered as a part of financial literacy whereas evaluation preferences from a normative standpoint (risk tolerance or lack of savings or insurance) better to avoid. To label behavior as financially illiterate because of the inappropriate aim we will need to evaluate his or her preferences from a normative standpoint which is difficult to justify. It is better if financial literacy will be a new enlightenment, not a new religion – we therefore need to focus more on how people seek information and make decisions rather than if their attitudes are right from the normative standpoint.

However, even if we focus on decision making process it will quite difficult to judge whether decisions people make are financially literally or not since people operate in different social and economic circumstances and their access to financial products varies. So the external observer may not be aware of the hidden costs or hidden utilities which people take into account when they make financial decisions and the survey method has no possibility to reveal these reasons.

### 1.3 Financial literacy or financial education?

Another important distinction should be made in the component of financial knowledge. Financial literacy is sometimes referred to as basics of financial education ranging from basic budgeting to financial investments. There are studies which found that people with major degrees in Economics and Finance show better results in management of personal finances. However, it is not clear if there is a genuine influence of economic education on personal finances or people who choose Economics and Finance as their university degree are different from other professionals by their social and economic characteristics. If so if economic education will be given to the general population it will not end up with the same results.

### 1.4 A concept of financial literacy and its operationalization

Huston (Huston, 2010) found out that over the last decade (between 1996 and 2008) there were 52 surveys in which financial literacy was measured. Most surveys were collected in the USA. The main conclusion of the author was that “the majority of studies (72%) did not include a definition of financial literacy. Although 15% included some discussion beyond identifying the specific elements in their measure, only 13% provided a formal definition of the construct operationalized” (Huston, 2010, p.303).

The lack of attention to the definition and the operationalization of the concept of financial literacy during the latest decade is explicable and unavoidable. Financial literacy is not an easy concept to define even though intuitively it seems to be quite clear what it is about. So during the initial stage of research it was much more useful to measure different aspects of financial capabilities in different groups and setting to accumulate this information for further conceptual work.

The model of ‘financial capability’ was developed within the Adult financial capability framework by the FSA and the Personal Finance Research Centre, University of Bristol (Measuring financial capability: an exploratory study, 2005). Following FSA methodology ‘financial capability’ covers the following aspects:

“Managing money – which was primarily concerned with being able to live within one’s means

■ Planning ahead – which was required to cope with unexpected events and to make provision for the long term.

■ Making choices – which involved being aware of the financial products that were on offer, and being able to choose those that were most appropriate to an individual’s circumstances.

■ Getting help – which had two dimensions: self-reliance and using third parties”. (Kempson, E., Collard, S. and Moore, N., 2005, p. 3)

Managing money component was operationalized by the questions on incomes and expenditures record keeping, planning for ‘lumpy’ expenditure, such as quarterly

or annual bills; and living within one's means. Planning ahead included preparations for dealing with an unexpected drop in income, or an unexpected expense, accumulating money for anticipated expenses; and savings for retirement. Making choices questions collected information about how people monitor the products that they hold; and choose products. Getting help explored how people keep abreast of changes, use information and advice, and deal with complaints.

The National Survey of nearly 1,500 American adults in 2009 which questions were partly based on the FSA methodological approach reported that nearly half of survey respondents reported facing difficulties in covering monthly expenses and paying bills (managing money). The majority of Americans do not have "rainy day" funds set aside for unanticipated financial emergencies and similarly do not plan for predictable life events, such as their children's college education or their own retirement (planning ahead). More than one in five Americans reported engaging in non-bank, alternative borrowing methods (such as payday loans, advances on tax refunds or pawn shops). Few appear to be knowledgeable about the financial products they own and 62% of individuals said that, when obtaining their most recent credit card, they did not collect and compare information about cards from more than one company (making choices). Low levels of financial literacy of Americans - lack of ability to understand basic financial concepts such as the importance of retirement savings, and poor judgment in borrowing decisions - were revealed in other surveys as well (Lusardi & Mitchell, 2007; Lusardi & Tufano, 2009).

In Australia the surveys which uses an operational definition of financial literacy in the form of a framework developed in the UK reveals that Australians generally are financially literate (ANZ Survey of Adult Financial Literacy in Australia, 2008). However, it is quite difficult to compare the level of financial literacy in Australia and US since there are very few questions to compare. The survey shows that the majority of Australians have savings and make provisions for their retirement, very few are engaged in non-bank borrowing, are well informed about their consumer rights and obligations. There are certain groups who lack knowledge on financial issues. Financial literacy was well below the total sample average among those aged 70 years or over and a bit less among those aged 18-24 years. Individuals with a university degree got higher scores than those who did not

go beyond Year 10. Financial literacy scores were lower among the unemployed, those whose main source of income was a government benefit or payment, those with less than \$2,000 in savings and investments, those with household incomes of less than \$25,000 per annum, those from areas exhibiting the greatest socio-economic disadvantage and those who do not use the internet.

Another important component of the concept of financial literacy is questions on financial arithmetic originally designed by Lusardi and Mitchell (2006, 2008) for the 2004 health and retirement survey (HRS) and later were used to measure financial literacy in many surveys across the world. The questions tested the understanding of nominal and real interest rates, compounding, and the ability to compare absolute and relative values. For example, in 2005 in the National survey in the UK respondents were asked the following question: 'If the inflation rate is 5% and the interest rate you get on your savings is 3%, will your savings have at least as much buying power in a year's time?' to assess their understanding of nominal and real values. More than one in five (21 per cent) of all respondents did not give the correct answer, this figure almost doubled amongst 18- to 20-year-olds - 41 per cent of whom did not answer correctly (Atkinson, A., McKay, S., Kempson, E. and Collard, S., 2006).

The third very important measure of financial literacy is linked to the self-assessment of level of financial literacy. Many surveys verified that consumers often think they know more about financial issues than they really do. Respondents in the United States, the United Kingdom, and Australia feel confident in their knowledge of financial issues even though when given a test on basic finance it is clear they have only a limited understanding of these issues. If they do not realise they need information, they will not be in a position to seek it (OECD, 2005). When asked to assess their financial knowledge, 37 per cent of Americans in 2009 rated their financial knowledge at the high end of the scale.

Based on the general acceptance of the idea that financial literacy is a "meaning-making process" and that financially literate individuals are able to obtain, understand and evaluate the relevant information necessary to make financial decisions with an awareness of the likely financial consequences (Mason and Wilson, 2000) it is necessary to measure knowledge and skills the lack of

which may prevent consumers from taking effective decisions. What are those indicators?

***A habit of keeping personal financial records could be one of them.*** This is a very important skill which forms the basis of financially literate behaviour. Money tracking helps to optimise spending but what is even more important – without it planning for long term goals is not possible.

***An ability to read and to understand the text of the contract before signing it.*** For example, when taking out a loan one needs to understand while reading a contract if his/her interest rate is fixed or floating, what the size of effective interest rate compared to the declared one is, what the penalties are if s/he delays the monthly payment, etc.

***A practice to shop around and compare offers from different financial providers in terms of costs and benefits of their products before purchasing.*** When people do not collect and compare information they tend to engage themselves in less profitable financial strategies. Shopping around indicates the ability to make informed financial decisions. People may not shop around for particular products if they use professional financial advice. However they need to be able to differentiate between independent advisers and those who 'hide the cost of their advice' behind the cost of the products they sell.

***An understanding of personal rights and obligations in using financial products.*** People may think that they can stop paying back their loans because of such externalities as financial crisis, or they may believe that they may cheat the bank because the bank cheated them by putting into the contract (which they did not read) of higher interest rates than they saw in the advertisements.

***Knowledge of the existence and the rules of the state deposit insurance in banks.*** If people do not know that deposits in banks are insured against the risk of the bankruptcy of a bank or think that not only bank deposits but also mutual funds' investments or savings in credit unions are covered by this scheme they may wrongly estimate the risks attached to these products.

***Ability to discern the indicators of a financial fraud if a company claims to offer high and risk-free***

***rates of return on their financial products.*** It not a sign of financial illiteracy if people are engaged in these "high yield investments" being aware of their Ponzi scheme nature. Financial illiteracy becomes obvious if they are misled by high returns which they consider to be risk-free.

***Safe usage of payment cards – not writing the PIN-code on their bank card in order not to forget it.*** In this case, they risk jeopardizing their financial well-being if, e.g. the card is stolen or lost. In Russia in 90% of cases banking plastic cards are issued by banks as a part of the contracts with enterprises which pay wages through them. Employees are given these cards but many of them do not use them except for taking their money from the ATM once a month. The problem is that they have is to remember the PIN-code. That is why they write it on the card in order not to forget it in one month period.

This is not an exhaustive list of indicators of financial literacy rather few examples of those indicators which are not interfering into the sphere of individual preferences.

It is also necessary to measure how people assess their level of financial literacy subjectively and to compare these estimates with the results of the objective tests. If the results of both subjective assessments and objective tests are low but consistent this is a minor problem. The worst situation is when the subjective grades are much higher than the objective ones. This indicates that people overestimate their abilities to control their finances.

Apart from measuring the level of financial literacy it is very important to reveal what people want to know and from whom they want to learn. These questions are necessary in the surveys for the proper targeting of the programs of financial enlightenment, especially for adults. It is difficult to teach adults what they do not want to know or what they do not think is important to know.

## 1.5 The methodology of the research

The all-Russian cross-section survey data have been collected for almost two years. The first survey was undertaken in July 2008, on the eve of the financial breakdown, the last one dates from August 2010. The wording of questions as well as the sampling design was kept

the same during the period of measurement. In each survey 1600 respondents were interviewed face-to-face at 140 sampling points in 42 regions of Russia. The total sample size has a sampling error  $\pm 3.4\%$  estimated at the 95% level of confidence. The samples reflect the characteristics of the Russian population aged 18 years or over (see Appendix 2, Table 1).

### 1.6 Some of the key findings

These are some of the key findings:

Less than half of the Russians keep systematic accounts of their individual finances and their number has fallen during the years of the crisis (2008-2009). Why? Intuitively one may suppose that in the time of crisis incomes fall and in the view of the uncertainty about the future incomes more people prefer to keep control over their finances. However, this logic contradicts the results of the observations – we observe the falling rate of individuals who keep their family budgets. One of the possible explanations is that keeping a budget is an appropriate tool for reaching long term financial goals. If incomes do not fall (which is the case in Russia) the need for budgeting is declining since people do not experience the difficulties in making the ends meet. While in the presence of higher uncertainty they postpone big purchases for better times.

**Figure 1: Keeping record of family budgets, % of all respondents (N=1600) see Appendix 2**

*The wording of the question: Is your family used to keeping records of income and expenditures? Look at the card and say which option is the most accurate description of your (your family's) practice?*

Many consumers (27% in November 2009) did not read or did not understand the text of the contract before signing it. If taken as a percentage from those who had an experience of signing the contract 2 out of 5 did not read or understand the contract before signing it. Probably the percentage of people who sign contracts without understanding is higher since we can not be sure that those who answered that they understand may be mistaken. The situation has not much changed in August 2010 when the same question was asked again. There is a slight reduction in the proportion of those who signed the contract without reading or understanding it – 21% compared to 27% - however it happened

at the expense of rising the number of people who had no experience in signing the contract or those for whom it was difficult to answer this question.

**Figure 2: Reading the contracts before signing it, % of all respondents (N=1600) see Appendix 2**

*The wording of the question: When buying financial products do you read or you do not read the contracts before signing them? Look at the card and say which option is the most accurate description of your practice?*

Before the crisis four out of ten never compared terms and conditions offered by various sellers of financial products. During the crisis this is the only one indicator that has slightly changed for the better: in February 2010 only 16% said that they never compared terms and conditions offered by various sellers of financial products. This change could be considered even more optimistic if the percentage of those who were at a loss had not doubled.

**Figure 3: Comparing terms and conditions offered by various companies when using financial services, % of all respondents (N=1600) see Appendix 2**

*The wording of the question: How often do you compare terms and conditions of the financial service offered by various companies when buying financial products?*

In case of a conflict with a financial industry organization (a bank or an insurance company) three out of four do not believe in a fair resolution of their problem. Which means that people either do not know their rights as consumers when they buy financial products or they do not think that their rights are secured by the state or market institutions. There is some positive dynamics between June 2008 and November 2009 which may be linked with the fact that those people who on the pick of this crisis wanted their money back could get it due to the existence and adequate work of the system of state deposit insurance.

**Figure 4: Having confidence in a fair resolution of a conflict when using financial services, % of all respondents (N=1600) see Appendix 2**



*The wording of the question: In case of a conflict with a financial industry organization (a bank or an insurance company) are you sure that it will get a fair resolution?*

The majority of consumers can not differentiate between a fraud scheme and non-fraudulent financial company. Only one in four was right in pointing to a company which was not a bank but offered a fixed high rate of return on the investments. During the crisis people did not manage to understand these issues better. What is also interesting is that in November 2009, a year after the beginning of the crisis, there was a bigger percentage of people for whom it was difficult to say which company to suspect. Since in February 2010 the structure of answers returned to the pattern which was similar to the one in December 2008, it means that people's answers to this question are influenced by their estimates of the market stability rather than measure their knowledge on the indications of frauds.

**Figure 5: Suspecting fraud, % of all respondents (N=1600) see Appendix 2**

*The wording of the question: Imagine that you want to invest money on financial market and while looking for a better option you found out a number of offers. Could you please say which one in your opinion looks like a fraud scheme?*

People in general do not know and do not understand how the state deposit insurance scheme works. This was completely unexpected result for me as a researcher. The highest percentage of people who reported that they had heard about it was achieved in November 2008, in the period of the liquidity crisis when Russian government tried to prevent the bank run: almost 80 per cent of Russians said that they know about the state deposit insurance system. While in February 2010 a half of consumers reported that at that moment it was the first time when they heard about this system. It means that people's estimation of knowledge and understanding is rather superficial – only a good media campaign can get people remembering about these issues.

**Figure 6: Knowledge of the State Deposit System, % of all respondents (N=1600) see Appendix 2**

*The wording of the question: How well do you know what the State deposit insurance system is?*

The lack of knowing and understanding of the state deposit insurance system is confirmed by the results of the objective test. In order to find out if people know that the state insures deposit in banks only I asked them if they know what kinds of losses are covered by the state insurance system? Only 22-23% respondents gave the right answer that only deposits in banks were insured by this system.

**Figure 7: Understanding of what kinds of losses are covered by the state insurance system, % of all respondents (N=1600) see Appendix 2**

*The wording of the question: Do you know what kinds of losses are covered by the state insurance system?*

Even though the objective tests show that the level of financial literacy has not changed over the crisis period and for some indicators it has even declined, the subjective self-assessment of the level of financial literacy has grown during the period of financial crisis. If our objective tests measure the important indicators of financial literacy this is an alarming result of the growing overconfidence of Russian consumers. Why did people start to perceive themselves as more financially literate during the crisis? I think that it comes from the growing volume of financial information which people were exposed to during the financial crisis. As this is the most important event covered by the Russian and international mass media it is more likely to catch the attention of consumers. Being bombarded by this information people started perceiving themselves as more financially literate. When the scope of information in mass media reduced the self-estimation again went down.

**Figure 8: Subjective assessment of the level of financial literacy, % of all respondents (N=1600) see Appendix 2**

*The wording of the question: Do you consider yourself to be a financially literate person? Please evaluate your knowledge and skills using a five-point system, as the one at school, where 1 stands for the complete absence of knowledge and skills in management of personal finances and 5 stands for excellent command of the subject in question.*

What do people want to know about financial matters? We asked people about the most important topics they would like to get information about to increase their level of financial literacy. The respondents were given

the long list of possible options covering different aspects of financial issues. The majority of people were not interested in getting information on stock market and specific financial products like bank credits, deposits, insurance products, mutual funds, mortgage and the like. Only three options interested more than a half of respondents (index of the interest to the topic above zero). On the top of the list people put information on consumer rights protection. The second place was given to the tips about reading and understanding contracts. The top list was closed with the information on how to make savings for the retirement.

How can we improve financial literacy of the general public? If we want to increase their financial literacy first of all we need to focus on issues of consumer rights protection and prevent programs from turning into outright 'advertising' campaigns for certain products and services. If consumers are better informed about their rights they will be more likely to take more effective decisions. Educational programs on consumer rights protection could be used as a trigger for further development of financial capability.

**Figure 9: Topics which people are interested in to increase their level of financial literacy (N=1600) see Appendix 2**

## 1.7 Conclusion

The aim of this paper was to compare and analyze the changes in the level of financial literacy of Russians during the period 2008-2010 in the period of global financial crisis. Following the idea that the concept of 'financial literacy' should not be limited to financial knowledge only and has to be extended it to include behavior and attitudes, I argued that in the institutional context of Russia the lack of financial savings or the presence of paternalistic attitudes of people do not necessarily have to be considered as signs of the financial illiteracy of people.

Based on the idea that financial literacy is a "meaning-making process" I propose to operationalise this concept by measuring knowledge and skills the lack of which may prevent consumers from taking effective decisions. For example, the lack of understanding of how the state insurance system works, or the absence of practice of keeping tracks of family expenditures and incomes, etc.

The estimations of financial literacy indicators made on the basis of all-Russian surveys show that the level of financial literacy of Russians is very low. During the crisis it started growing but only in terms of self-estimation and perceptions. In 2009 people thought that they were more financially literate than a year before. However, when they answered questions in the objective tests a substantial change in attitudes, knowledge and skills could hardly be noticed.

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## Appendix 1

**1** Is your family used to keep records of income and expenditures? Look at the card and say which option is the most accurate description of your (your family's) practice? <ONE CHOICE> Card #1

**Interviewer:** If a respondent has any problems with defining a family, then explain that a family is interpreted as a household or a group of people who share revenues and expenditures.

1.1 Yes, we keep records of everything, entering all revenues and all expenditures

1.2 Yes, we keep records of everything, but not all revenues and expenditures are entered

1.3 No, we don't keep records of everything, but we know in general how much money is received and spent during a month.

1.4 No, we don't keep records of family's resources, and we don't have even a vague idea of how much money is received and spent during a month

99 I find it difficult to answer this question

**2** When buying financial products do you read or do you not read the contracts before signing them? Look at the card and say which option is the most accurate description of your practice? <ONE CHOICE>

2.1 Sign after reading the contract carefully and making clear that I understand what it says, if it is necessary I consult with the third party.

2.2 Sign after reading the contract regardless of whether I understand it or not, do not consult with the third parties.

2.3 Sign without reading, rely on what the seller said.

2.4 Do not have an experience of signing such contracts.

99. I find it difficult to answer this question.

**3** How often do you compare terms and conditions of the financial service offered by various companies when buying financial products?

3.1 Always

3.2 Sometimes

3.3 Seldom

3.4 Never

99 I find it difficult to answer this question

**4** In case of a conflict with a financial industry organization (a bank or an insurance company) are you sure that it will get a fair resolution of the dispute? < ONE CHOICE>

4.1 completely confident

4.2 rather confident

4.3 50 /50

4.4 not quite confident

4.5 completely unconfident

99 I find it difficult to answer this question

**5** Imagine that you want to invest money on financial market and while looking for a better option you found out a number of offers. Could you please say which one in your opinion looks like a fraud scheme?

5.1 A bank which offers 12% interest rate on deposits

5.2 Mutual fund which announced about 35% increase of its shares during the previous year

5.3 Financial organisation which promises to pay a 35% interest rate on your investments in one year time

5.4 Bank mutual fund of asset management which offers certificates on share holding

5.5 Non of the mentioned

5.6 All mentioned

5.7 Difficult to say

99 I find it difficult to answer this question

**6** How well do you know what the State deposit insurance system is?

6.1 Know everything about it

6.2 Know roughly about it

6.3 Heard about it but cannot say anything specific

6.4 It is the first time when I hear about it

99 I find it difficult to answer this question

**7** Do you consider yourself to be a financially literate person? Please evaluate your knowledge and skills using a five-point system, as the one at school, where 1 stands for the complete absence of knowledge and skills in management of personal finances and 5 stands for excellent command of the subject in question. < ONE CHOICE>

1	2	3	4	5
No knowledge and skills	Unsatisfactory Knowledge and skills	Satisfactory knowledge and skills	Good Knowledge and skills	Excellent Knowledge and skills

99 I find it difficult to answer this question

**8** Currently many organizations related to capital markets declare their preparedness to deal with improvement of financial literacy of the people. What kind of trainers do you see as the most suitable to deliver financial literacy program? Card # 2 Not more than 3 choices

I would like the program to be delivered by employees of:

8.1 a commercial bank

8.2 pension fund and/or insurance companies

8.3 unit investment funds (management companies)

8.4 non-government organizations or public organizations involved in consumer rights protection

8.5 government entities regulating these markets

8.6 higher education institutions of economic and financial profile

8.7 independent financial consultants

8.8 mass media (journalists and TV presenters)

8.9 other people (what kind?)

99 I find it difficult to answer this question

**9** Can you identify any of the following as a pyramid scheme? < ONE CHOICE>

9.1 A bank which offers 12% deposit interest rate

9.2 Mutual fund reporting 35% returns over the last year

9.3 A financial organization guaranteeing 35% growth of investments per year

9.4 Bank mutual fund of asset management which offers certificates on share holding

9.5 None of the above

9.6 All of the above

99 I find it difficult to answer this question

## Appendix 2

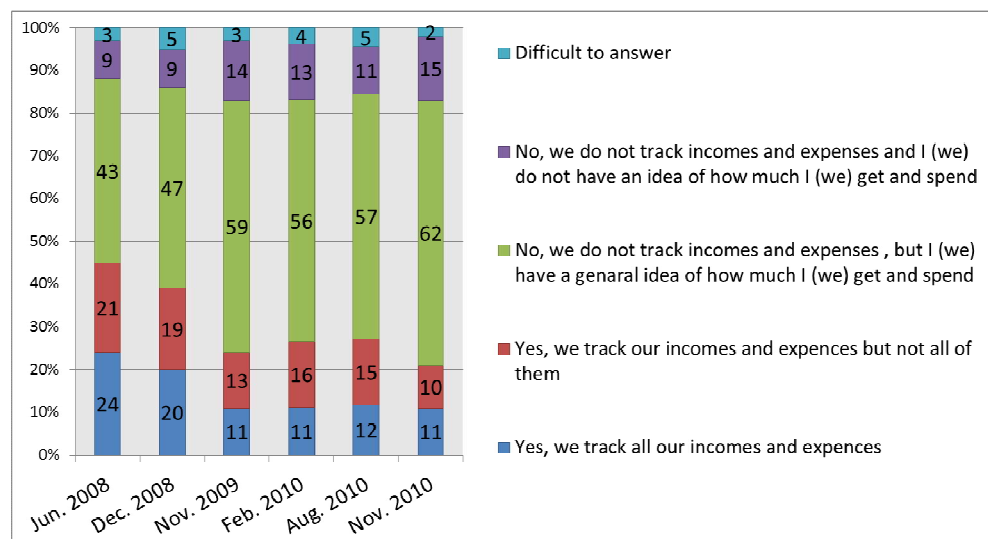


Figure 1 Keeping record of family budgets, % of all respondents (N=1600)

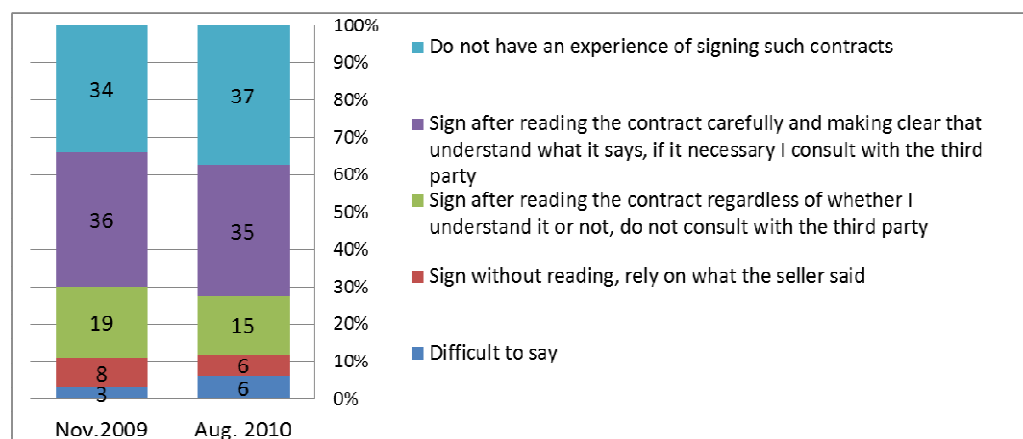
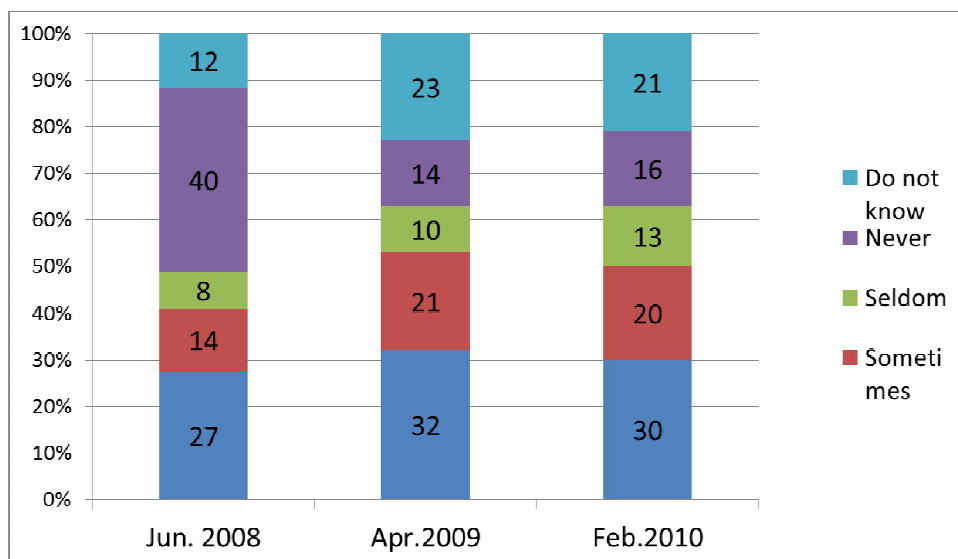
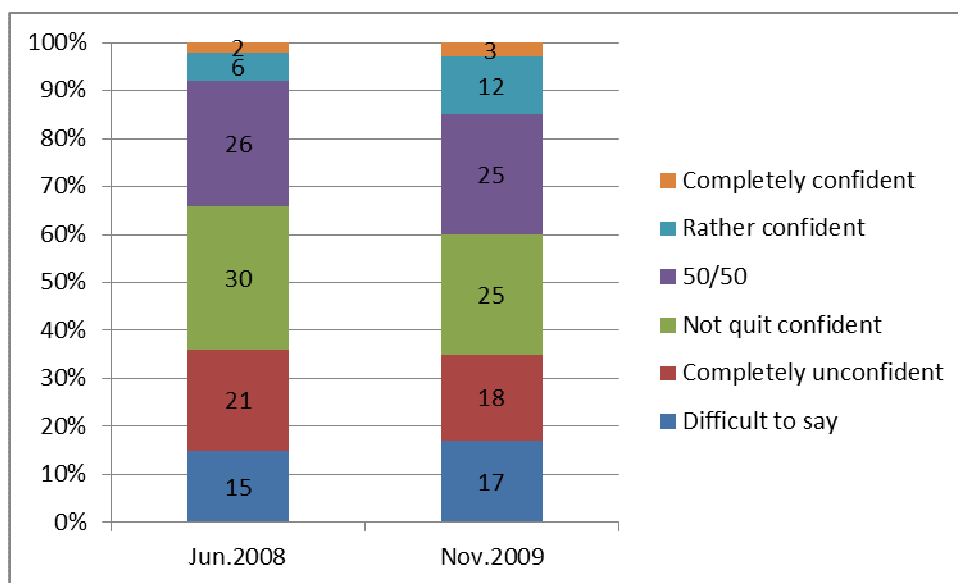


Figure 2 Reading the contracts before signing it, % of all respondents (N=1600)



**Figure 3** Comparing terms and conditions offered by various companies when using financial services, % of all respondents (N=1600)



**Figure 4** Having confidence in a fair resolution of a conflict when using financial services, % of all respondents (N=1600)



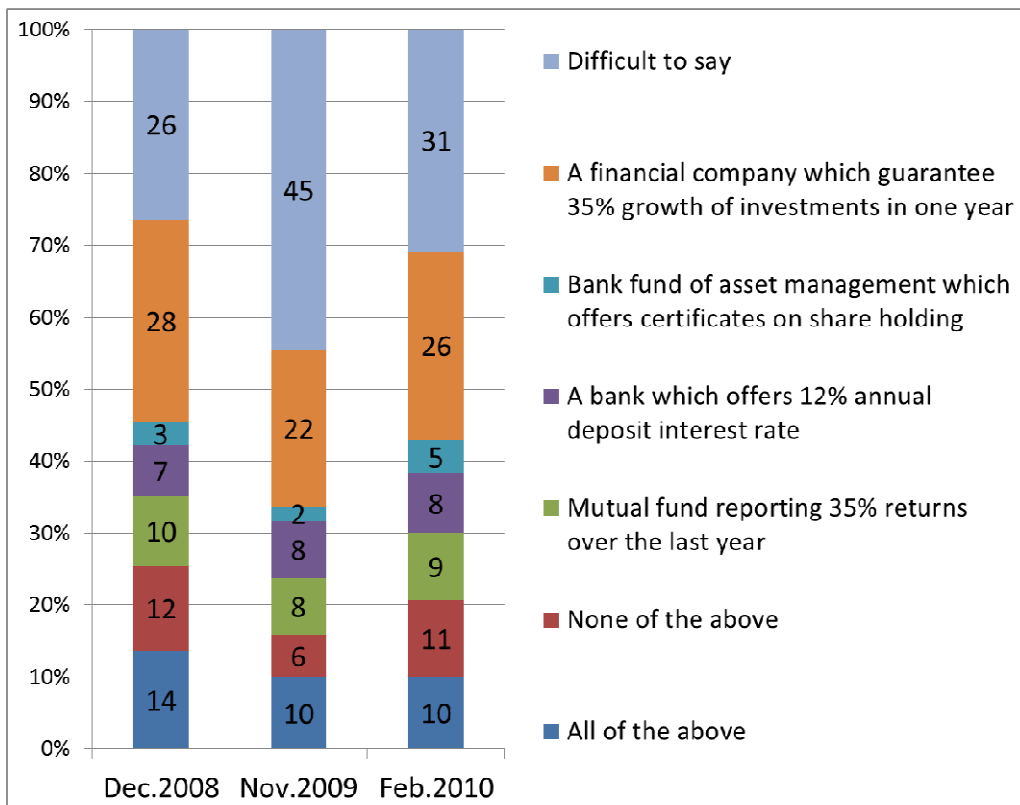


Figure 5 Suspecting fraud, % of all respondents (N=1600)

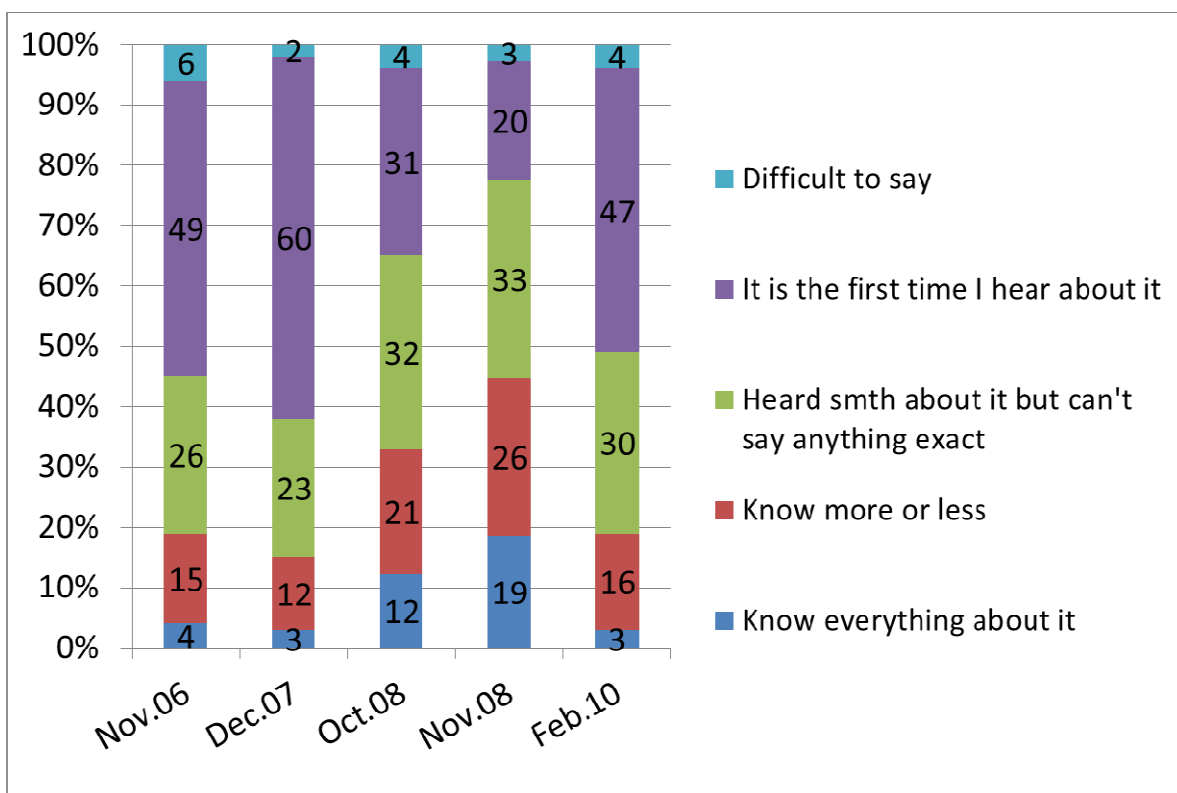
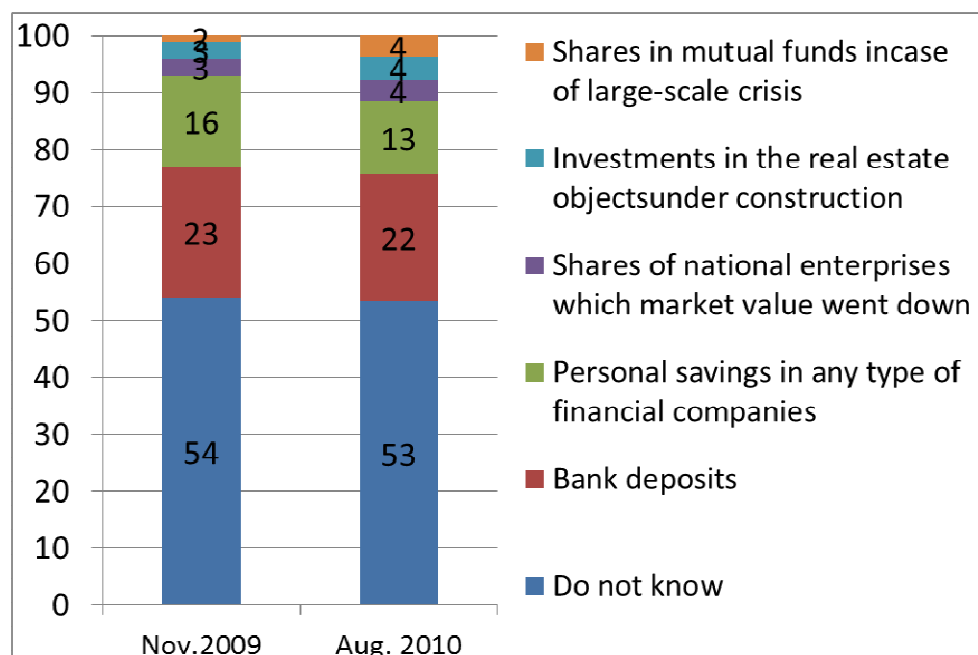
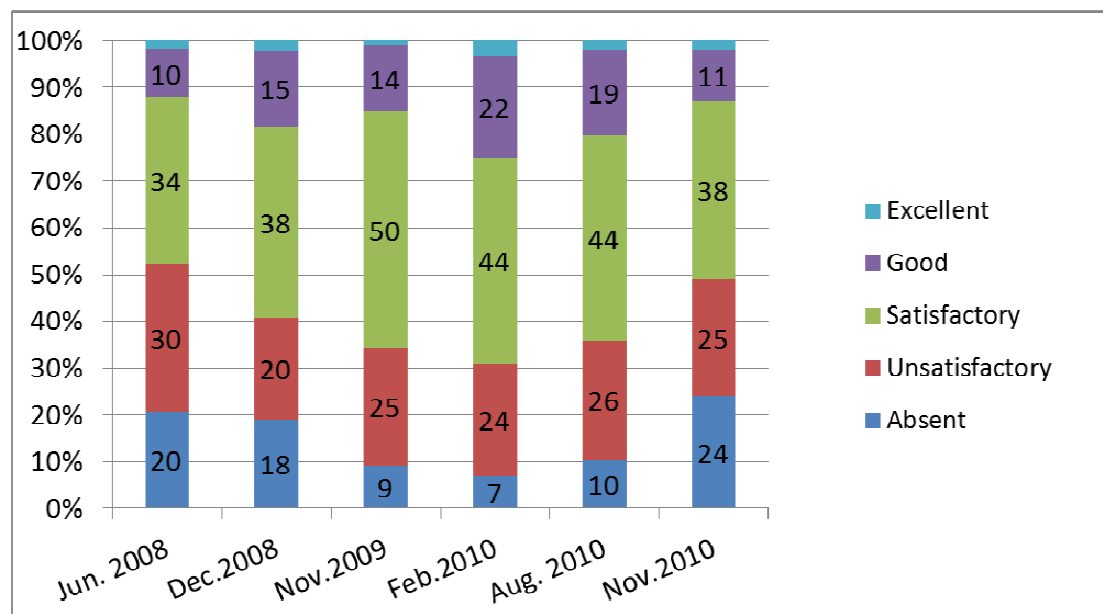


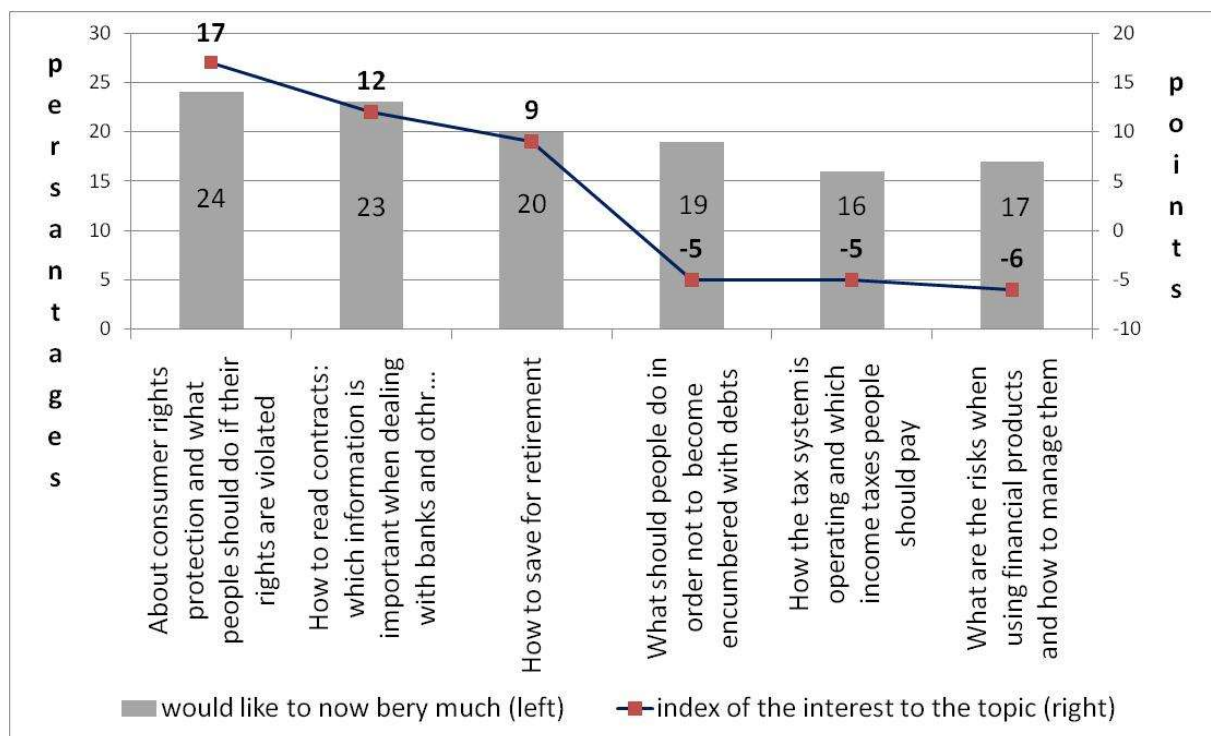
Figure 6 Knowledge of the State Deposit System, % of all respondents (N=1600)



**Figure 7** Understanding of what kinds of losses are covered by the state insurance system, % of all respondents (N=1600)



**Figure 8** Subjective assessment of the level of financial literacy, % of all respondents (N=1600)



**Figure 9** Topics which people are interested in to increase their level of financial literacy (N=1600)

**Table 1:** Final Samples by Social and Demographic Characteristics

		Official Statistics 2008	June 2008	December 2008	November 2009	February 2010	August 2010	November 2009
Gender								
	Male	46	45	46	46	45	45	45
	Female	54	56	54	54	55	55	55
Age								
	18-24	19	14	15	15	15	14	15
	25-34	18	18	19	19	19	20	19
	35-44	16	20	17	17	17	17	17
	45-59	27	27	28	29	28	28	29
	60+	20	21	21	20	21	21	20
Education								
	Primary and Post-Primary		9	10	7	8	10	8
	General Secondary		31	33	27	33	33	32
	Specialised Secondary		38	33	44	38	37	37
	Tertiary and Incomplete Tertiary		22	24	22	21	20	22
Region								
	Central		26	26	26	28	26	26
	North-West		10	10	10	10	9	10
	South		16	16	16	16	10	16
	Volga		21	21	21	21	21	21
	Ural		9	9	9	9	9	9
	Siberia		11	10	14	14	14	14
	Far East		7	8	5	3	5	5
	North Caucasus		—	—	—	—	6	—
Type of Residence								
	Moscow and St. Petersburg		11	11	11	11	11	10
	500.000+		17	19	20	18	18	17
	100.000-500.000		19	18	18	19	19	20
	Less than 100.000		26	26	24	26	25	26
	Rural Areas	27	27	26	27	26	27	27

# Book Reviews

**Book:** Aspers, Patrik, 2010: *Orderly Fashion*. Princeton: Princeton University Press.

**Reviewer:** David Dequech, State University of Campinas, Sao Paulo, Brazil, [dequech@mpifg.de](mailto:dequech@mpifg.de)

In his most recent book, *Orderly Fashion*, Patrik Aspers examines order in markets, through a detailed study of the global fashion industry, focusing on branded garment retailers, which sell clothes to final consumers. Examples include C&A, Gap, H&M, and Zara. While relying on empirical work based on observations and interviews, the book aims to contribute not only to the field of fashion studies, but also to sociological theory more generally and to economic sociology, especially regarding markets. With solid empirical research, an extensive, 20-page bibliography, and the ability of its author, the book succeeds in making valuable contributions to all these fields.

I will not summarize the book here. Aspers does it nicely, providing a summary at the end of each of the first six chapters and then discussing in Chapter 7 the findings of the book as a whole, before adding some final reflections on partial orders and their interrelations. The book also contains five appendices.

Aspers defines order 'as the predictability of human activities and the stability of social components in relation to each other' (p. 7). He studies markets as partial orders, limited in range but not necessarily local. These economic partial orders depend on other markets, as well as on noneconomic partial orders. Aspers adopts a social constructivist perspective: partial orders, including markets, are social constructions, i.e., meanings that result from social interaction and become entrenched (pp. 8-9). 'A central condition of the existence of partial order is that people perceive and act in such a way as to furnish evidence of such an order' (p. 171). This indicates an anti-realist stance, which is perhaps more clearly suggested when Aspers includes 'the realist assumptions despite claims of social constructivism' among the 'shortcomings of contemporary sociology' (p. 5. See also p. 209, n. 7). At the same time, however, Aspers acknowledges the pertinence of 'the question of ontological order', which 'remains to be addressed' (p. 166). Be it as it may, the tensions between

realism and social constructivism do indeed deserve greater attention.

The book highlights the contribution of identities, products, and values to order in the fashion industry markets. Some of these markets are classified as 'status markets', where 'order is maintained because the identities of actors on both sides of the market are ranked according to status, which is a more entrenched ... social construction than the thing ... traded in the market, namely fashion garments' (p. 16; also pp. 58-60, specifically on the branded garment retailers' consumer market).

This contrasts with 'standard markets', such as the production markets for garments, in which the branded garment retailers buy the products (pp. 144-146). The book also investigates order on the financial side of the fashion business, again focusing on the branded garment retailers, but now examining their relations with their investors in the stock market, which is another standard market. Aspers wants to bring closer together the sociological research on financial and producer markets, showing how these different markets in which the branded garment retailers operate are interconnected.

Fashion is an interesting topic for economic sociologists as well as institutional economists (even for those who consider the fashion world as vain and despise it for that), not least because it involves both imitation and stability, on the one hand, and innovation and change, on the other. Fashion is not only shared for social reasons, but, more specifically, the fact that others are wearing a given type of clothes is for many individuals a major reason for one to do the same. Aspers' work can be used here to add that this happens in the fashion consumer market when the others are of the right type (p. 53), that is, significant others (p. 52), characterized by a high status. This is a selective version of a property of conventions that we may call conformity with conformity (Dequech, 2011). The consumption of fashion garments may also involve negative network externalities, as Aspers (p. 206, n. 10) remarks. I believe this may occur after a certain number of other users has been reached, again depending on the type of these other users.

The essence of fashion is, however, to change from time to time. Oscar Wilde captured this aspect when he stated that 'fashion ... is a form of ugliness so intolerable that we have to alter it every six months' (1887: 205-206). Aspers' study intends to show, among other things, 'how order and change are interrelated' (p. 2). In my view, it does so when discussing the very notion of fashion: 'only when the social structure of identities is relatively more entrenched than the object, and when a change of garment styles takes place, can one talk of fashion' (p. 166). Conceptually, therefore, Aspers links fashion both to order based on the principle of status, in the consumer market, and to change. He has reason to hope that his theoretical ideas on this will also prove useful in the study of fashion regarding objects other than clothes (p. 166).

To conclude, this is a very stimulating, well researched and well-written book, which deserves to be read by those interested in fashion, economic sociology and/or sociology in general.

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**Book:** Karpik, Lucien, 2010: *The Economics of Singularities*. Princeton: Princeton University Press.

**Reviewer:** Monika Krause, University of Kent, United Kingdom, [m.krause@kent.ac.uk](mailto:m.krause@kent.ac.uk)

How is economic value created out of something that is unique? Lucien Karpik's new book on *The Economics of Singularities* (Princeton University Press 2010) invites us to take this question seriously and put it at the very centre of a sociology of markets. He shows us that this problem of making uniqueness marketable is a problem for actors in many fields of business and he shows that this is not a trivial problem. With exemplary care and knowledge, Karpik shows us how conventional economists have tried to explain the problem away and he makes us marvel at the devices people employ to confront it.

These devices help consumers choose between products they cannot know in advance and they help to reduce risk for producers who cannot know what people will like. Consider, for example, the guides that explain and rate fine wines, the names that brand recordings of classical works, or the advertising budgets that accompany big blockbuster movies.

Karpik writes the book about what he conceptualises as a specific kind of market: markets in singularities. Singularities, as Karpik defines them, are multidimensional and their dimensions are dependent on each other; singularities are uncertain and singularities are incommensurable.

Karpik does not tell the somewhat familiar story of how commensuration and standardization, rankings and ratings erode uniqueness. Instead, as Karpik shows, in the rise of new products – and especially the rise of new symbolic products – over the past decades, forms of standardisation and forms of singularisation have gone hand in hand within many markets.

In demonstrating the role devices play in cases where markets are constructed against the odds - the book is an important contribution to economic sociology. In the best traditions of defamiliarisation, the book is also a beautiful book.

The book raises an important question for future comparative work on markets. I wonder whether what Karpik says about markets for singularities is not an even more general feature of markets than he suggests. Karpik makes claims specifically about the economics of singularities as though that was a distinct category. But is it? Is Karpik's analysis about a specific corner of the world while we can leave the rest to more conventional modelling? If it were not, this, in some way, would make us lose the central category of Karpik's contribution, but it would make his work a basis for a comprehensive re-thinking of how empirically and comparatively different markets are constructed.

The problem of uniqueness, in some forms, seems irreducible as a property of many more markets than Karpik suggests. Any given lightbulb is unique, as one will notice if one has only one and it breaks after dark. There is some kind of quality uncertainty about that lightbulb (- but not perhaps about web content). Every person is also unique and his or her needs subject to interpretation, so that my enjoyment of any given product is to some extent contingent and unpredictable, even to me.

On the other hand, of course, lightbulbs are more similar to each other in some ways than, for example, *Sex and the City*

and *Toy Story* are to each other. And – and this is Karpik's point – my enjoyment of any given bar of chocolate is probably less uncertain than my success with any given psychotherapist.

Is singularity-ness, then, a question of degree? It might not be that easy to separate the problem of these fundamental forms of uniqueness, call them ontological, from the kind of uniqueness Karpik is most interested in. In the case of the original art painting, ontological uniqueness is central to its value as well as uniqueness of meaning. In many products the problem of uniqueness re-occurs on different levels, such as with wines in the unique bottle, the year, the brand, the producer, the type etc. Do we need to compare the lightbulb to an individual copy of "Sex and the City" or to "movies" or to "entertainment products"? If there is uniqueness on different levels within one product, how do they relate to each other and how are these managed in market-construction?

Karpik distinguishes different regimes within the economics of singularities, such as the authenticity regime, organizing the market for fine wines for example, the mega regime, operating for mega films and mega brands, or the expert opinion regime, expressed in literary prizes. We might want to build on this taxonomy of regimes to include the regimes for those products that are the least singular in the same type of analysis, rather than start from the assumption that this is a separate corner of the world altogether.

**Book:** John B. Thompson, 2010: *Merchants of Culture. The Publishing Business in the Twenty-First Century*. Cambridge: Polity Press.

**Reviewer:** Gisèle Sapiro, CNRS-CESSP, Paris, [sapiro@msh-paris.fr](mailto:sapiro@msh-paris.fr)

One of the oldest cultural industries, the book industry underwent major changes since the 1980s. John Thompson's sociological inquiry within the Anglo-American publishing world seeks to understand these changes. Based on close to 200 interviews and on a large statistical data produced by professional bodies, this inquiry fills a gap. While Pierre Bourdieu, who partly inspired this project, dedicated his last empirical survey to French publishing (Bourdieu, 1999), no in-depth research had been conducted on the Anglo-American publishing since the seminal book by Coser, Kadushin and Powell (1982). Thompson borrows freely from Bourdieu the concept of field to explore the

publishers' world. Though he makes a more interactionist use of it than Bourdieu himself, this concept allows him to describe the structure of the field, mainly the opposition between the pole of large-scale production and the pole of restricted production, as well as the mechanisms by which the belief in the value of a book is produced.

Three factors explain, according to Thompson, the major changes within the book industry. First, the growth of the retail chains: between 1993 and 2003, their share in the American book market rose twofold, from 23% to 50% of the retail sales, while the independent bookstores fell from 24% to 16% (and to 13% in 2006, because of the rise of Amazon, which had reached 11% in 2006). In parallel way, the chains abandoned their backlist policy (keeping a large supply of books published earlier) in order to concentrate on new publications and on "brand names" of successful authors.

The second factor of change is the increasing role of agents in the book market and a change in their social recruitment: new practices of "advocacy" were developed by agents coming from other fields, especially law, who claimed that the more the publishers would pay advances on fee for a book, the more he will make an effort to promote it. This policy induced a burst in the costs of the book production.

The third factor identified by Thompson is the merging of firms in large conglomerates, which tend to become international. Originally, this process was partly due to the departure of the generation of the founders in the 1960s and the problems their firms were confronting. Conglomerates function according to two idealtypical models: the centralized one, which prevailed in the first phase, and the federal one, which arose in the second one. In the latter, the objective of rationalizing the costs is limited by the will to maintain some diversity in order to guarantee a certain level of creativity: the imprints are allowed a relative autonomy in their publishing policy as far as they are profitable.

Though providing a more nuanced picture of these evolutions, Thompson confirms the idea that the strengthening of economic constraints and the overproduction lead to a reduction of the supply of books available on the market, instead of enlarging it. In a more and more risky market (the risk being intrinsic to the industry of prototypes), uncertainty is reduced thanks to brand names (such as Stephen King, John Grisham or Patricia Cornwell) and



backlist books, which still play a significant, albeit varying role according to the publishing house (from 20% to 75%, the average being around 30-40%). Publishers and agents tend to look more and more for "big books", which will be large best-sellers.

In this concentration process, the number of middle-size publishers has decreased, and they are confined to niches like health, religion or youth. On the contrary, there are more and more small publishing houses, thanks to the lower costs of access to this trade. Thus the evolution reinforces the dual structure of the field described by Bourdieu: on one side, the law of profit, on the other, what Thompson calls an "economy of favours" based on elective affinities, cooperation, voluntary work, the idea of a mission.

The role of social capital is not specific to this economy of favours. Thompson shows for instance how the social capital of the agents in the media can extend the author's "platform" (his expected audience according to his position with regards to the media). Thompson also provides indicators of the impact of methods of diffusion and of instances of consecration on sales: while the impact of literary criticism has dramatically fallen, TV shows like Oprah Winfrey in the US or Richard and Judy in the UK have the highest.

Though the author does not discuss the consequences of his findings from a broader perspective of economic sociology, much could be drawn from it. It would also have been interesting to relate the changes in the publishing industry with the broader economic evolutions, since number of the phenomena described, like merging/acquisition or internationalization of firms, are not specific to the book market. Regarding the functioning of the field of publishing, one can regret that, like in many surveys of economic sociology, there is no more reflection on the forms of in

teraction between social, cultural and economic capital. Along the same lines, beyond differences in the economic functioning, the modes of accumulation of symbolic capital at the two poles of the field would require a more systematic comparison. Bourdieu (1977) distinguishes the accumulation of symbolic capital on the long run through the recognition by the peers and by specific instances of consecration from quick sales on the short-run. Though apparently similar to the symbolic capital enclosed in the names of consecrated authors, brand names in the publishing industry are typical of the economy of the star system. Attention to the case of authors in translation, which are infamously underrepresented (not to say absent) at the pole of large-scale production in the Anglo-American book market, but highly promoted by small publishers, might have provided some insights on this question. All these questions and remarks are brought about by the richness of Thompson's analysis, by his fascinating ethnographical descriptions and by the remarkable clarity of his demonstration. It shows the benefit that economic sociology could derive from the study of cultural industries.

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