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A General Financial Transactions Tax: A Step Towards a Better Global Governance

Stephan Schulmeister

European Parliament

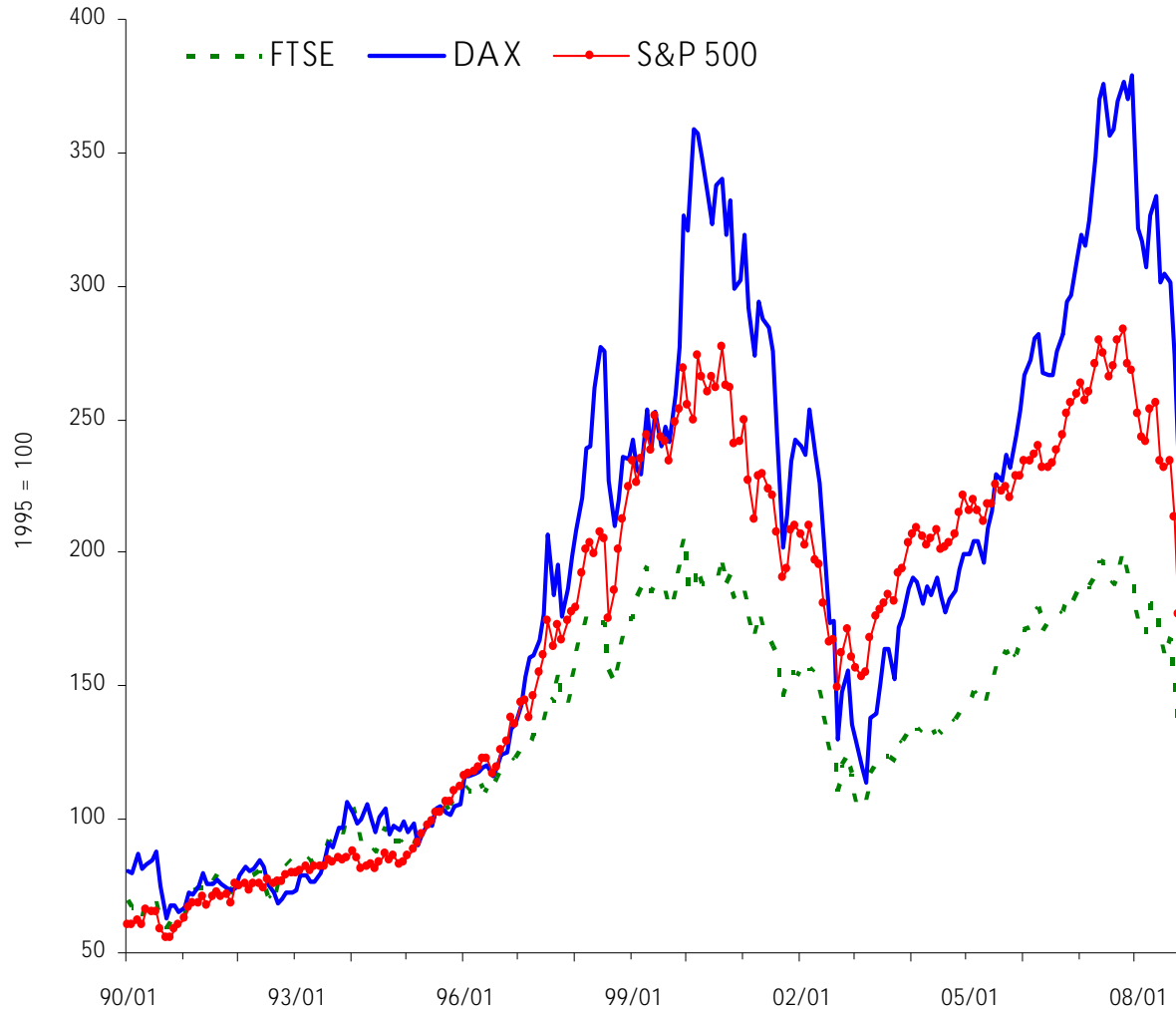
Special Commission on the Financial, Economic and Social Crisis

Public Hearing on Global Governance in Brussels on March 25, 2010

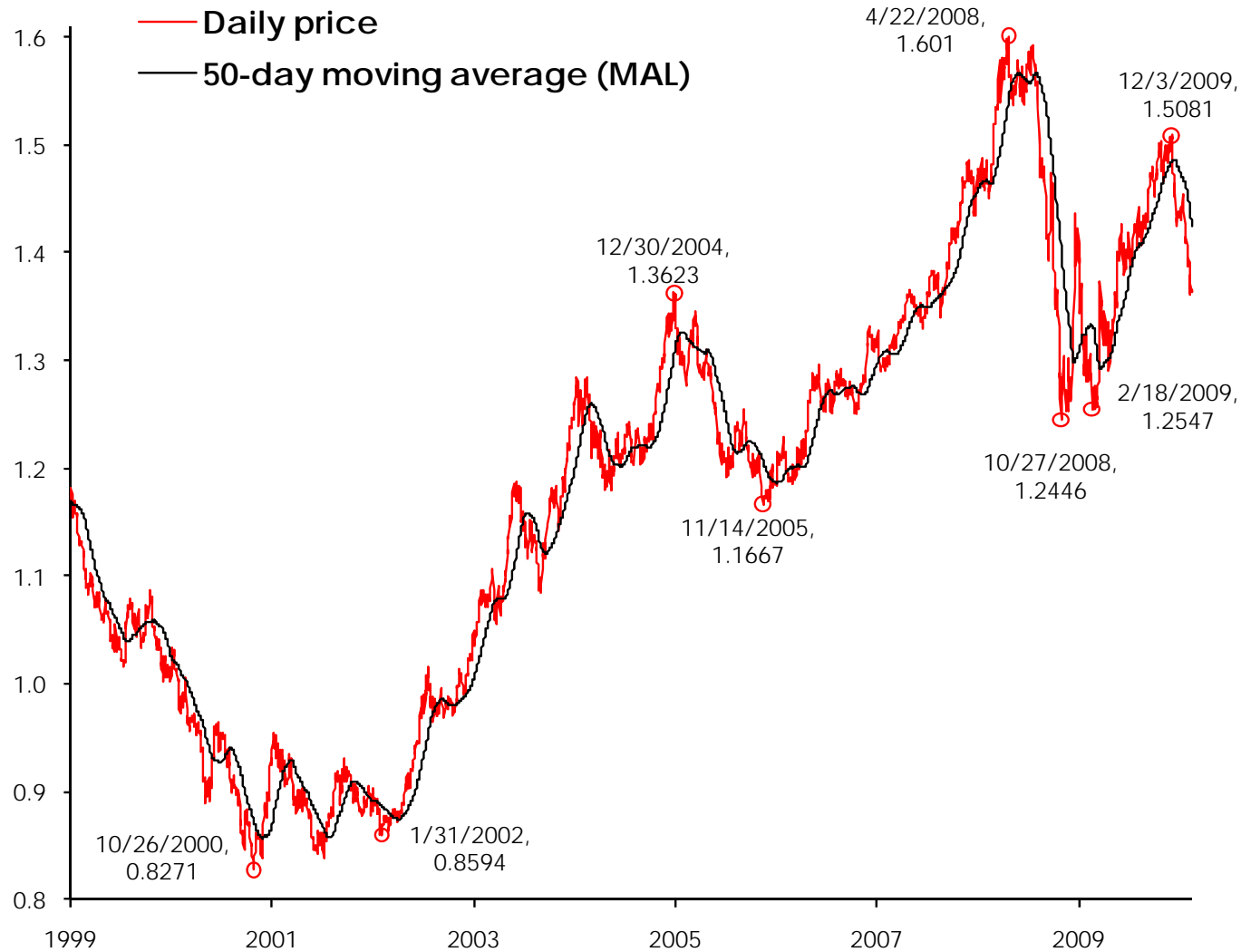
- The “long cycle” in economic and social development
- Driven by three “fundamental” interests:
- Real capital, finance capital, labour
- Bottom phase: Depression of the 1930s >
- Long-term upswing (~1950-1970s): Real capital & labour
- Long-term downturn (1970s-???): Real & finance capital
- Current crisis: Beginning of a new bottom phase
- Real capitalism/Finance capitalism:
- Two different “regimes” of a capitalist market economy
- Characterized by two combinations of many different features

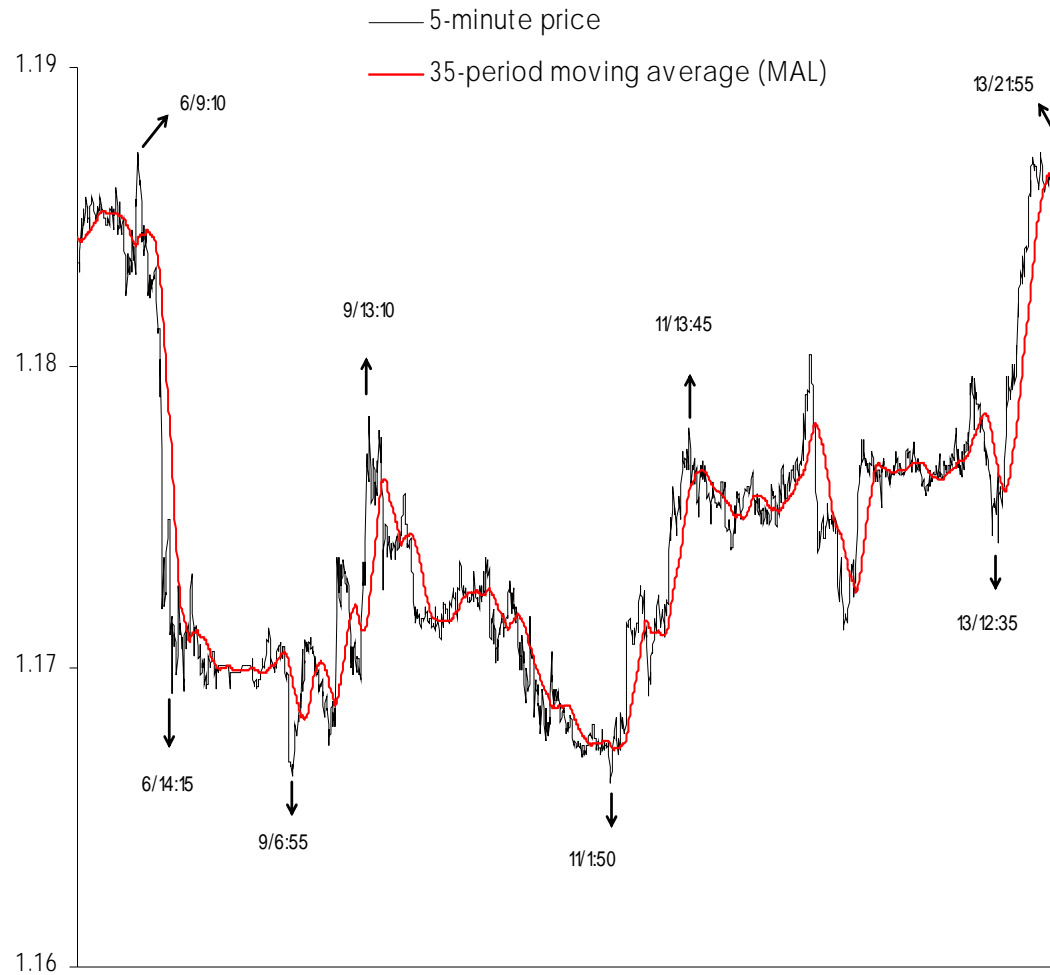
- Dynamics of stock prices, exchange rates and commodity prices
- Investment behaviour of non-financial business
- Stock market valuation and “real” net worth of corporations
- Monetary policy >
- Rate of interest and rate of growth
- Exchange rate system and focus of globalization:
- Real versus financial transactions

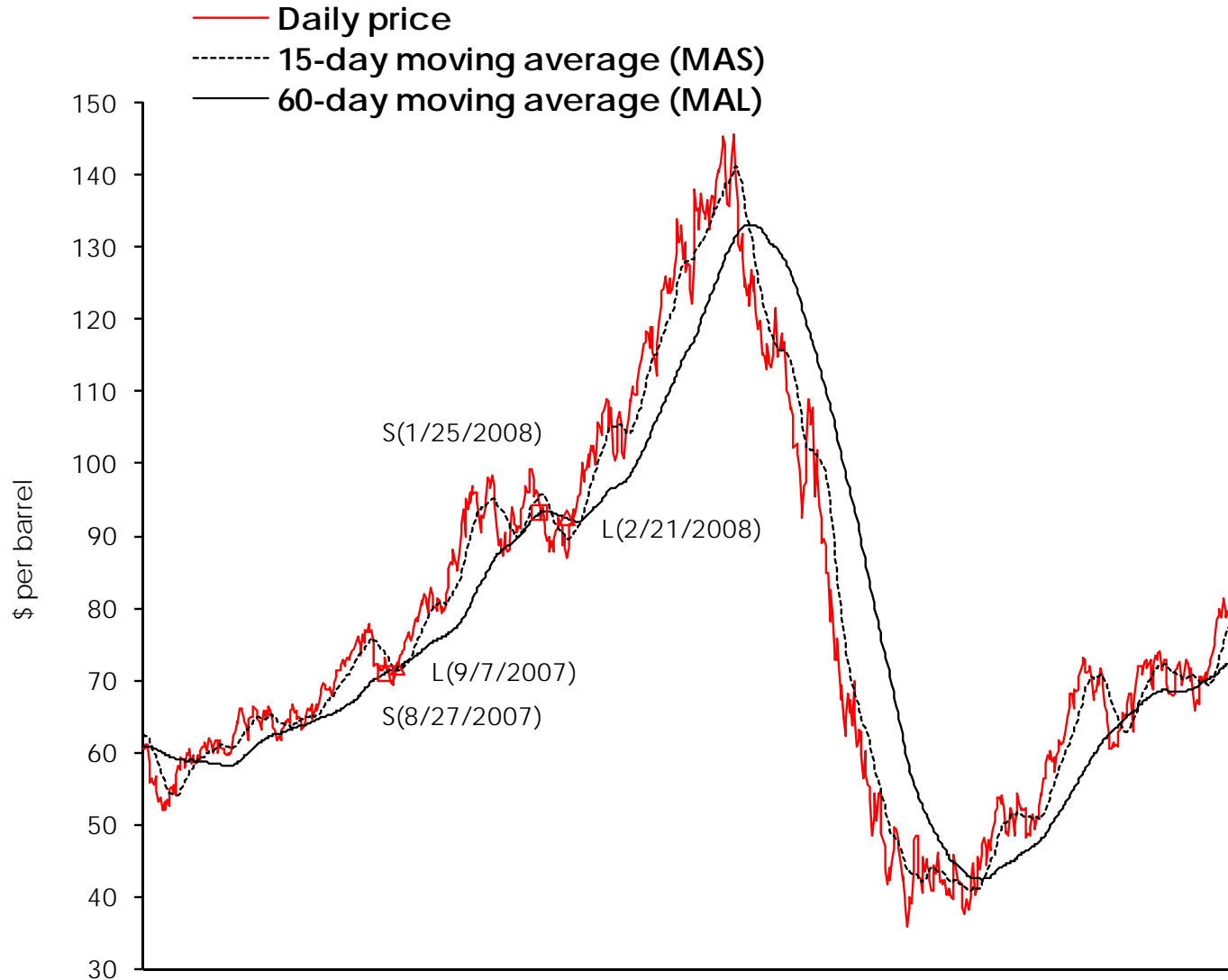
Stock price fluctuations in Germany, the United Kingdom and the US

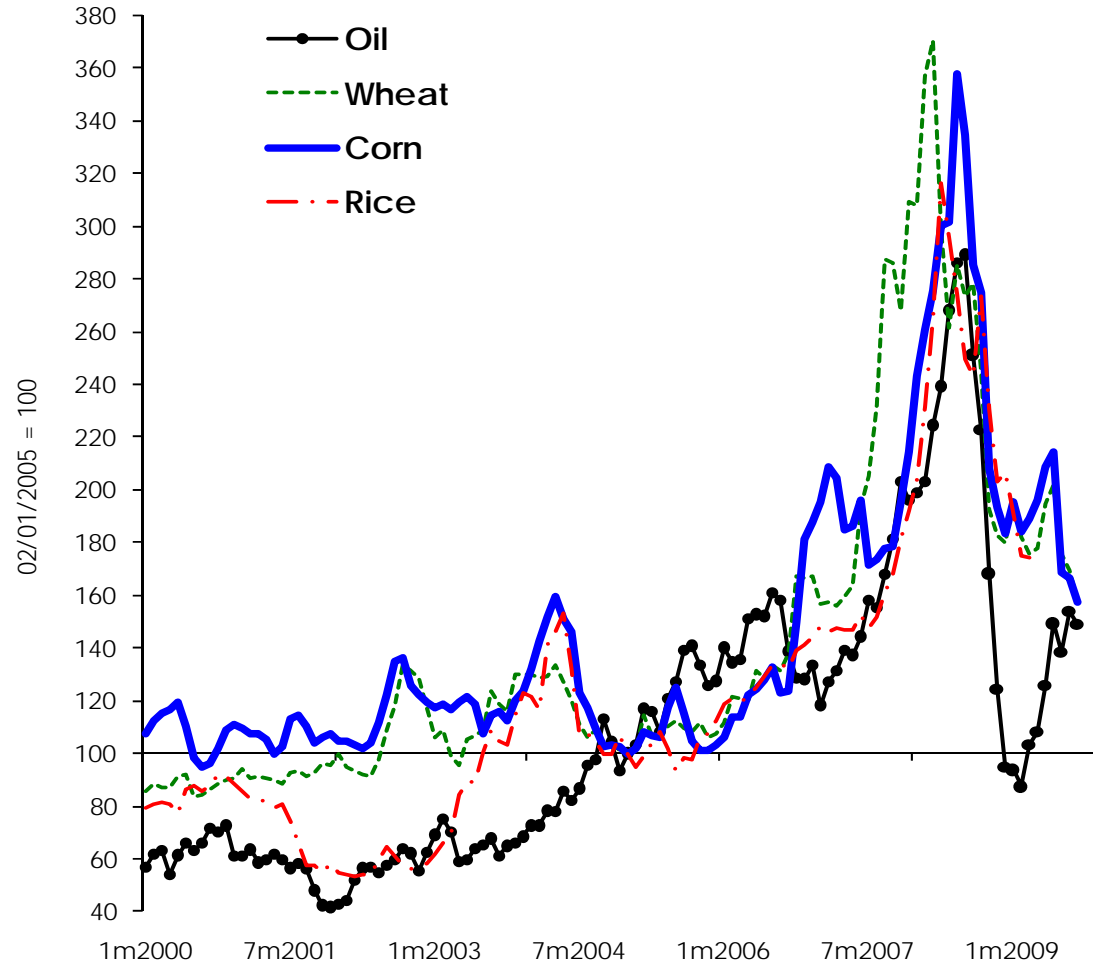


Dynamics of the dollar/euro exchange rate

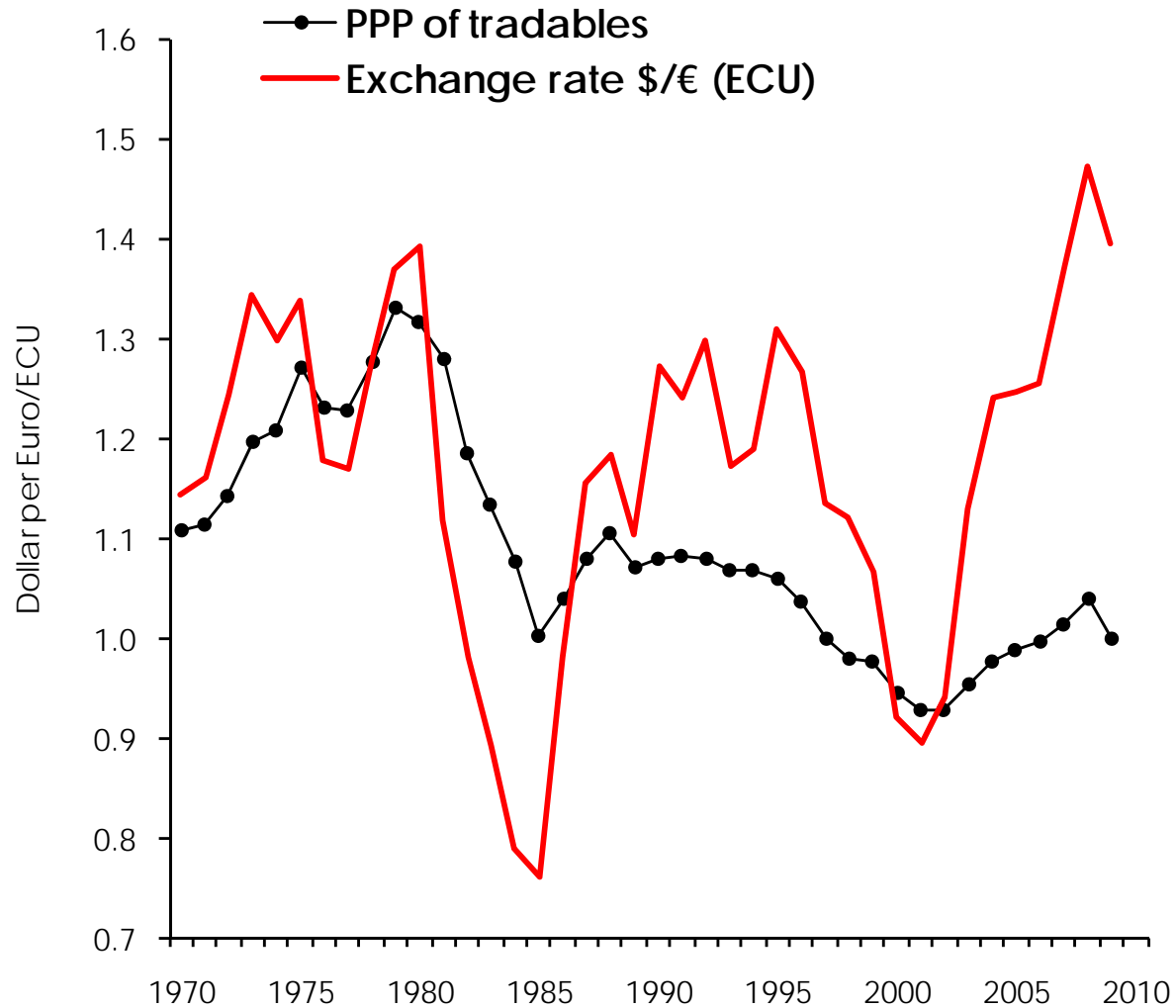




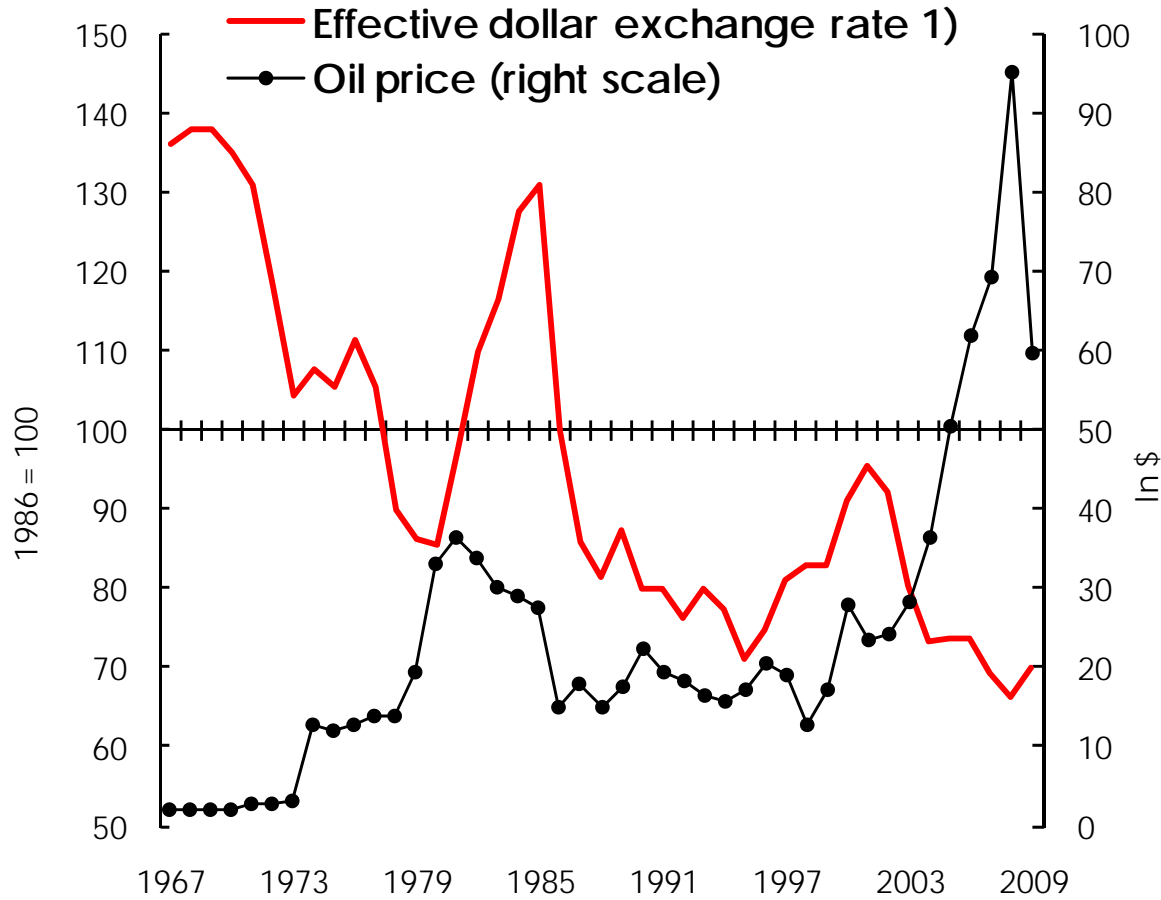




Dollar/euro exchange rate and purchasing power parity

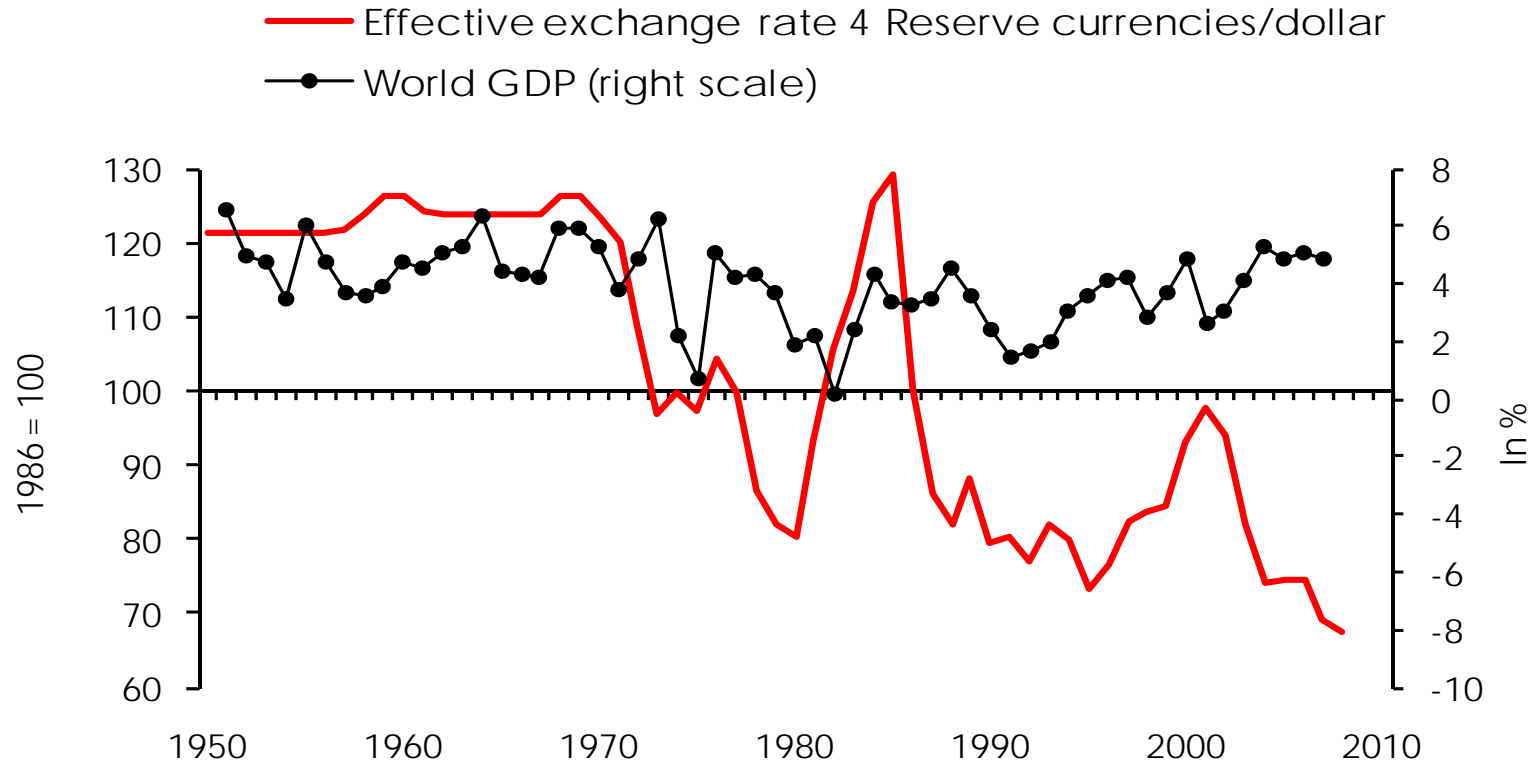


Dollar exchange rate and oil price fluctuations



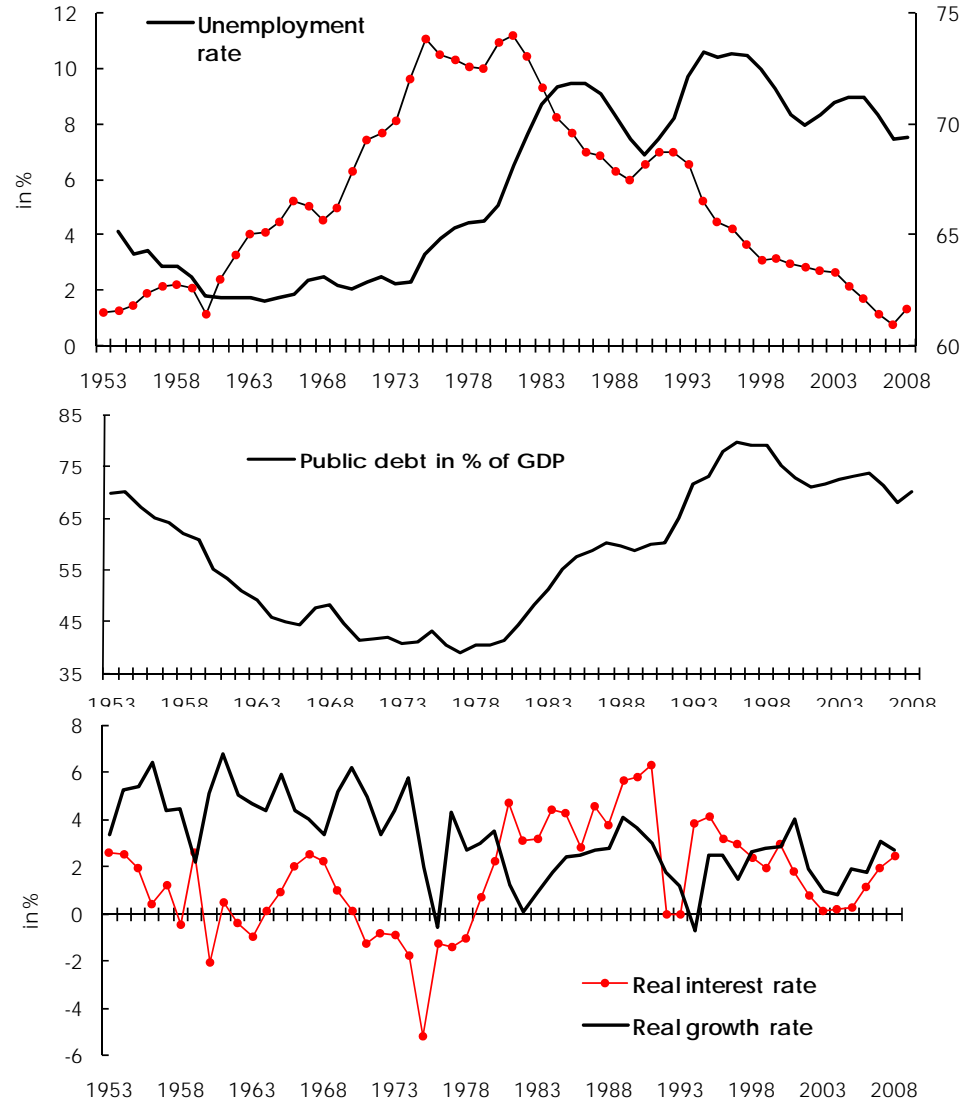
1) Vis-a-vis DM, Franc, Pound, Yen.

Exchange rates and global economic growth



Source: OECD, WIFO.

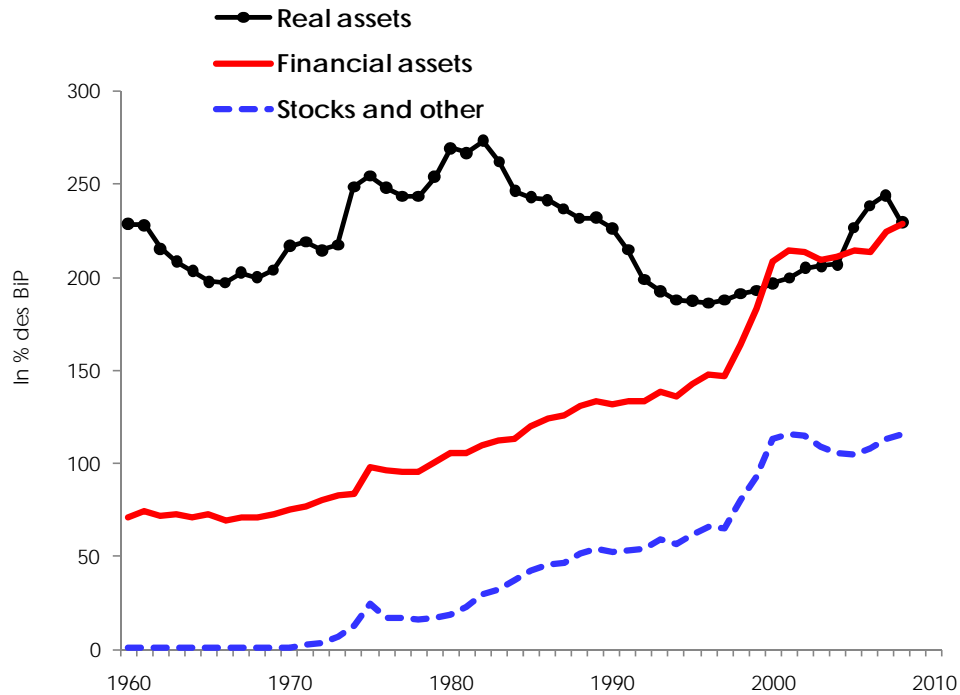
Long-term development in Western Europe



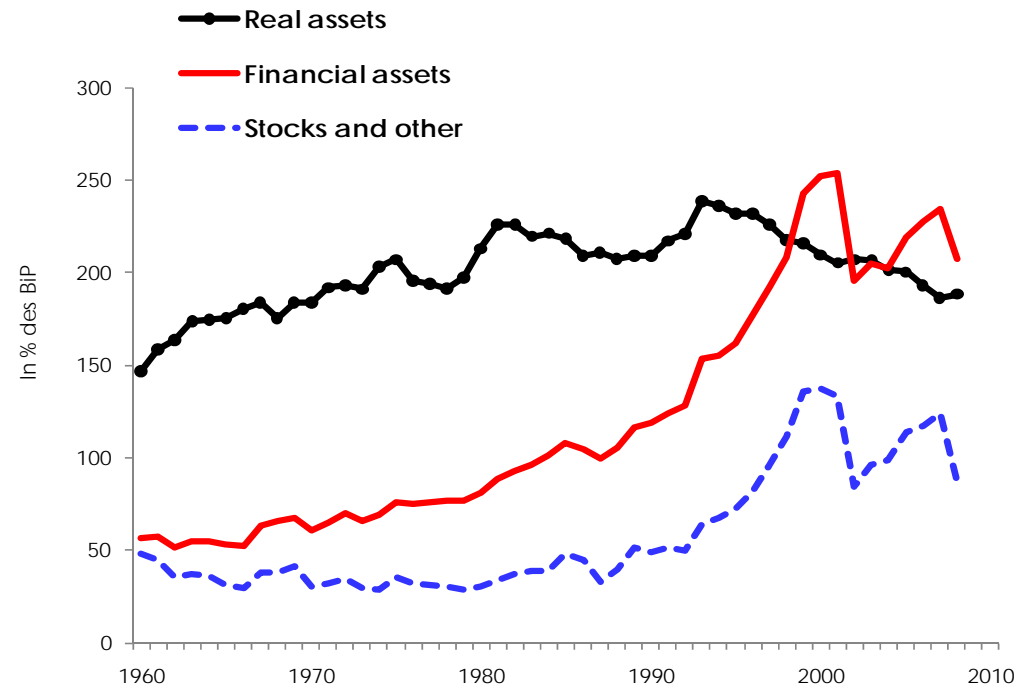
Quelle: Wifo-Datenban

Real and financial assets of non-financial business

USA

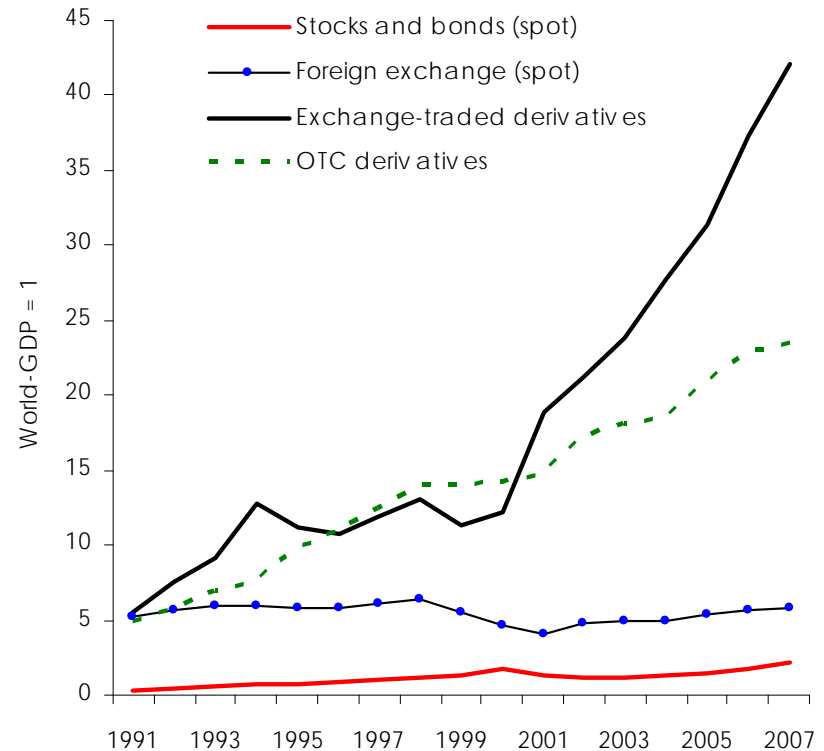
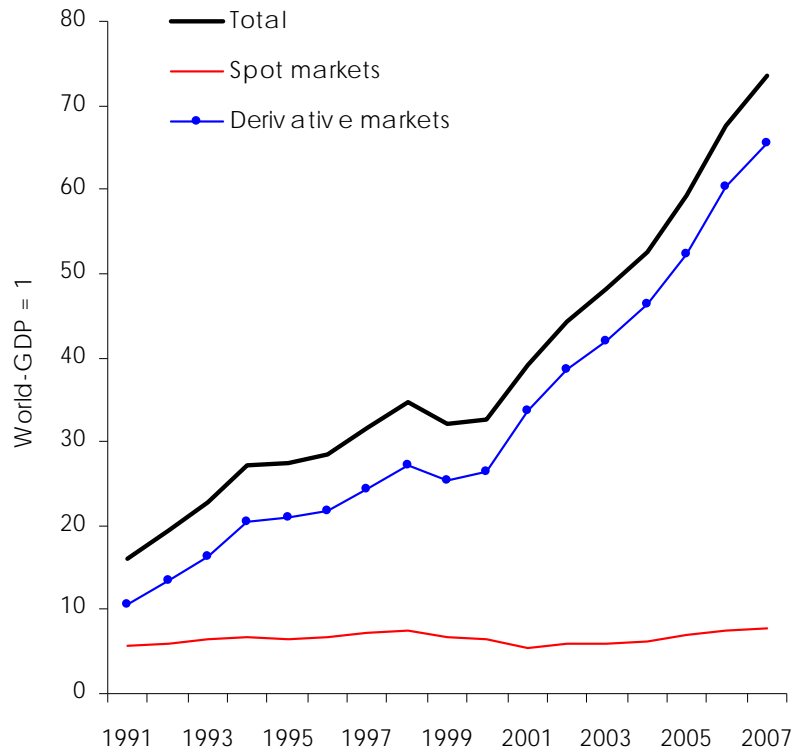


GERMANY



Source: Fed, Bundesbank, WIFO.

Financial transactions in the world economy



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- Growing discrepancy between real and financial transactions.
 - Asset prices fluctuate in a sequence of „bulls“ and „bears“.
 - Due to the accumulation of short-term runs.
 - A FTT would affect specifically very short-term transactions with high leverage >
 - Dampens long-term asset price fluctuations
 - Most important aspect: FTT as first step >
 - Re-directing the striving for profits from the financial to the real economy

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- Generalizes the Keynes-Tobin-concept:
 - All financial assets treated equally
 - Three tax rates: 0,1%, 0,05%, 0,01% of (notional) value >
 - Higher leverage > higher tax burden on cash requirement (margins)
 - Implementation through electronic settlement systems (Fedwire, TARGET, CLS Bank, CHIPS)
 - Revenue estimates: Three scenarios about the reduction of trading due to the FTT (differentiated by types of instruments)

Hypothetical FTT receipts in % of GDP at a tax rate of 0.05%

	World		Europe		North America		Asia and Pacific	
	In % of GDP	In Bill. \$	In % of GDP	In Bill. \$	In % of GDP	In Bill. \$	In % of GDP	In Bill. \$
Spot transactions on exchanges	0.11	60.9	0.12	21.2	0.18	28.3	0.16	10.3
Derivatives transactions on exchanges	0.65	358.1	0.69	122.7	1.28	198.7	0.51	32.8
OTC Transactions	0.44	242.0	0.82	145.1	0.33	50.8	0.67	43.6
All transactions	1.21	661.1	1.63	289.0	1.79	277.8	1.34	86.7

	Labor	Real Capital	Finance Capital
Economic interests	Full employment Real wage increases	High Profitability of real investments: - Low interest rates - Low exchange rates - Stable financial markets	High profitability of financial investments: - High interest rates - High exchange rates - Unstable financial markets
Conflicts of interests	Rising wages	←-----→	←-----→ Rising interest rates ←-----→ Rising exchange rate
Potential coalition partners	Real capital	Labor or finance capital	Real capital
Economic interest in state/government	Full employment policy Social security Education Public services	Anticyclical policy Growth policy: Infrastructure Education, etc.	Strong central bank Restriktive monetary policy Privatisation of social security
Political interests	Strong welfare state Strong trade unions	Weak welfare state Weak trade unions	No welfare state No trade unions

	Real capitalism	Finance capitalism
Implicit coalition	Labor & Real capital	Real capital & Finance capital
Business/unions	Corporatisms	Conflict
State/market	Complementary	Antagonistic
Targets of economic policy	Many: From full employment, high growth to social security and „fair“ distribution	Price stability, „sound“ public finances, regulation of policy, de-regulation of markets
„Power center“ of economic policy	Government	Central bank
Economic paradigm	Keynesianism	Monetarism/Neoliberalism
Diagnosis/Therapy	Systemic	Symptom-oriented
Financial conditions	Interest rate < growth rate, „calm“ stock markets, stable exchange rates and commodities prices	Interest rate > growth rate, boom und bust on stock markets, unstable exchange rates and commodities prices
Striving for profits focuses on	Real economy (Positive-sum game)	Finance economy (Zero-sum game)
Economic model	Social and regulated market economy	„Pure“ market economy

	Europe	USA
Long-term development path	Citizens embedded in social contexts (feudal system, communities, interest groups, welfare state)	Citizens as (former) immigrants: Mentality of adventurers, Competition as dominant form of social interaction
Pursuit of interests	Mainly through organisations (unions, etc.)	Predominantly as individuals in markets
Fundamental values	Individual freedom <u>and</u> social justice ("Liberte, egalite, fraternite")	Individual freedom ("pursuit of happiness")
Importance of trade unions and organisations of entrepreneurs	Great	Little
Labour relations	Corporatism	No institutionalized cooperation
Labour markets	Regulated	"Hire and fire"

WIFO ■ European Social Model versus US Model II

	Europe	USA
Insurance against illness, old-age Poverty, unemployment	Provided by welfare state	Mainly private (or no) insurance, unemployment benefits modest
Education system	Primarily run by welfare state	Mainly private
Relationship market/state	Complementary	Antagonistic
Importance of the welfare state	Great	Little
Importance of the financial sector	(Traditionally) Little	Great
Role of (stock) exchanges	(Traditionally) Less important	Very important
Focus of making profits	(Traditionally) Real economy	Real and Financial Economy
"Economic culture"	"Real capitalism" combined with welfare state	"Real and financial capitalism" ("Silicon Valley culture" combined with "Wall Street culture")