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Who does the state work for? Geopolitical considerations in the organization of (global) finance

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Abstract
States acting as lenders of last resort in the aftermath of the 2007/2008 financial crisis clearly illustrated the central role that states have in the operations of financial markets. Despite their active roles, however, states continue to be presented as passive actors that dance to the tunes of the financial markets. This paper, however, takes a close look at how states' geopolitical concerns influence financial regulation. States are perceived as serving the interests of their citizens, yet future rescue operations (as lenders of last resort) at the costs of the taxpayers remain a strong possibility – in particular, Too Big To Fail (TBTF) banks persist and their leverage-ratios have not greatly improved. To better understand why this is the case, this paper argues that geopolitical concerns influence the triangular relationships between the (democratic) state, the financial sector, and the state's citizens (and taxpayers) in favour of the financial sector. Accordingly, the paper argues that we should more explicitly ask 'what drives states (and politics) in their approaches to finance?'

Keywords: financial regulation, state finance dichotomy, geopolitics, future crises, lender of last resort, global markets

Introduction

To mitigate the economic and social costs of the 2007/2008 financial crisis, many governments, in particular in the West, have gone at great lengths to rescue their financial sectors – TARP in the Unites States, (partial) nationalizations of the RBS in the United Kingdom, ABN AMRO in the Netherlands, and the saving banks in Spain, are just a few examples of state interventions. More than six years later, this has resulted in two views: one, that 'we have done a lot' since the crisis erupted, and the other 'that we are a long way from completing the far-reaching changes that we need' (Johnson, 2014). There is more consensus, though, about the fact that it is unfair to have taxpayers footing the bill for market failure – not the least, because this is perceived to undermine democracy (e.g., Shaxon and Christensen, 2013; Streeck, 2014). Proponents of greater government intervention and the supporters of laissez-faire free market ideologies may differ in approach, yet rarely is *privatizing profits and socializing losses* voiced as a sustainable model for a more robust financial system.

This paper argues that notwithstanding political claims about protecting the taxpaying citizenry, most states tend not to meet these claims. Without doubt, states and international regulatory institutions have drafted impressive regulatory responses – hence, the argument 'we have done a lot'. But despite a large variety of regulatory changes and proposals aimed at minimizing the economic and social costs of future crises, it seems unlikely that states will not have to financially step in when finance fails again. For example, the Too Big To Fail (TBTF) issue has all but disappeared, while the current leverage-ratio of most banks hardly safeguards these banks from insolvency in the case of negative shocks (e.g., Allesandri and

Haldane, 2009; Admati and Hellwig, 2013; Johnson, 2014). Hence, although the using of (future) tax-incomes to prevent financial institutions from bankruptcy may be rejected on moral grounds, the potential to re-apply the same approach in the case of future crises has not diminished. Equally, as a result of states' financial injections and/or the decline of tax incomes, austerity measures aimed at decreasing sovereign debts and at (re)financing these debts at advantageous interests rates remain pertinent; and notwithstanding that austerity measures are characterized by a larger variety of opposing opinions, they also result from states prioritizing the opinion of financial markets.

To better understand why states have so far only limitedly relieved the (future) predicament of their taxpayers, this paper seeks to explore the relationships between democratic states, their respective citizenry, and national and international financial sectors. It particularly aims to analyse states' political balancing between geopolitical considerations and the constructing of a solid financial system that prevents citizens from suffering he burden of failing financial institutions. A central quest in the analysis, and which has so far received relatively attention in understanding state responses to the financial crisis, is 'what drives states (and politics) in their approaches to finance?'[1] How geopolitical considerations shape state responses, the paper argues, need to be explicitly addressed if we want to better understand the current state of financial regulation. The paper will, first, give a short overview of the relationships between the state and finance – more generally and with regards to the last financial crisis. After that, it will address the relationship between state and its citizens and the value of politically voiced narratives to prevent taxpayers from picking up the bill for rescuing financial institutions. Finally, the paper will focus its attention on how geopolitics influences these relationships between the state, its citizens and finance.

The myth of markets without states

Since the crisis, laissez-faire capitalism has fallen off its pedestal; the need for states to step in further highlighted the fact 'that states were necessarily involved in financial operations' (Moran and Payne, 2014: 337). In reality, prior to the crisis states were also closely engaged. The financial sector has always operated in close collaboration with states, even if the latter could be subject to a level regulatory capture: 'financial markets are not autonomous or natural, given that they always operate in a political context' (Carruthers and Kim, 2011: 244). Despite the evident influence of state (and political) involvement in financial markets, however, the dichotomy between finance and the state, with finance as an uncontrollable and faceless system, is prevalent. In the words of Lehman Brothers' last CEO, Dick Fuld (2008), for example, the 2007/2008 financial crisis was a financial tsunami – like a big storm, beyond the prevention capacity of mere mortals. Equally, politicians portrayed this image. In the direct aftermath of the crisis, the United Kingdom's then Prime Minister, Gordon Brown, said, 'this is an international economic hurricane sweeping the world and lashing our country' (Porter, 2009). While during the French 2012 presidential campaign, the current French president, François Hollande, referred to the world of finance as a faceless government (Rachman, 2012).

[1] State is used in a rather simplified manner and includes also the political spectrum. In reality state tends not to be a singular entity. Instead, most states are characterized by different competing forces, both in the everyday operations and in the political domain deciding over the state's priorities. For the analysis of the relationships between the state, its citizens and finance, however, it is sufficient to look at the dominant directions of the state and, thus, define the state (and the political domain related to it) as a singular entity representing these directions.

The dichotomy between an autonomous finance (and economics) and the state (and politics) originates, to a large extent, in longer discussion about modern finance as detached from, and overarching, other societal spheres. With modernity the conception of the economy as separate from other societal spheres was born, also resulted in the pervasive influence of markets on society. Karl Polanyi (1957) is renowned for voicing concerns about the separate but dominant position of economics and financial markets over society. He, however, also explicitly argued that this did not happen autonomously from politics. Yet, how the political spectrum and finance are interwoven receives surprisingly little attention. In many (mainstream) economic accounts political considerations hardly play a role. Accordingly, the role of the state tends to be obscured. Or states are presented as subdued to the powers of finance, with financial sectors capturing the state through their lobby efforts (e.g., Igan, Mishra and Tressel, 2009). There is little doubt that lobbying played and continuous to play a significant role, yet it portrays a picture of states as passive bystanders. Matthias Thiemann (2014: 1209) illustrates that cognitive capture as the cause for regulatory lenience prior to the crisis can hardly account for a uniform global lack of regulation of securitization activities. Instead, states are actively involved in the workings and directions of finance.

In *The Making of Global Empire: The Political Economy of American Empire* (2012), Leo Panitch and Sam Gindin illustrate the close collaboration between the (Unites States) state and its financial sector. They argue that the (powerful) narrative of states versus the markets is a false dichotomy. On the contrary, with the development of capitalism 'states in fact became more involved in economic life than ever, especially in the establishment and administration of the juridical, regulatory, and infrastructural framework in which private property, competition, and contracts came to operate' (Panitch and Gindin, 2012: 3). Besides, states also acted increasingly as lender of last resort in order to contain capitalist crisis. According to Piergiorgio Allesandri and Andrew Haldane of the Bank of England, the relationship between the state and finance has actually been reversed the last two centuries. Initially sovereign debt defaults were the biggest cause of banking collapse. Today, however, '[t]he state has instead become the last-resort financier of the banks. As with the state, the banks' needs have typically been greatest at times of financial crisis. And like the states, last-resort financing has not always been repaid in full and on time' (Allesandri and Haldane, 2009: 1). The example of Lehman Brothers is interesting in this respective, as the state did not act as lender of last resort to save the bank, this 'creating the largest bankruptcy in American history' (Davis, 2009 130–1). In a twist of faith, however, the global chain reaction this triggered may now actually serve as an example for many governments to prevent, at all (social) costs, large and systemic financial institutions to collapse.

Close collaborations between the states and their financial sectors are not a characteristic of the Unites States only, but also of, for example, the United Kingdom, Ireland and mainland Europe (e.g., Ahamed, 2014; Bell and Hindmoor, 2014; Woll, 2014). Notwithstanding, the United States are a dominant force, where all the trend-setting developments originated (Streeck, 2014: xii), and with a strong ideological narrative that the state and markets are separate entities. For example, the frequently voiced rhetoric that 'government is not the solution, government is the problem' was the loudest in the United States, even though it paints a false picture: neoliberalism may be understood in terms of the expansion and deepening of markets and competitive pressure, but it 'was essentially a *political* response to the democratic gains that had been previously achieved by working classes and which had become, from capital's perspective, barriers to accumulation' (Panitch and Gindin, 2012: 15).

In reality, the state has not withdrawn from the financial and economic domains.[2] The concept of the state and markets as separate entities may serve as useful abstraction, according to Geoffrey Underhill, but '[t]hey are part of the same integrated ensemble of governance, a state–market *condominium'* (Underhill, 2000: 129). Also, because 'states became increasingly dependent on the success of capital accumulation for tax revenue and popular legitimacy' (Panitch and Gindin, 2012: 3). It is debatable, however, to what extent the US, and also other states, had an explicit strategy in pushing a neoliberal agenda, expanding their financial sector and/or reinforcing financialization, i.e. the broad-based transformation in which profit making in the economy occurs increasingly through financial channels rather than through productive channels.

The course of events

Greta R. Krippner (2011: 3) remarks, '… financialization was not a deliberate outcome sought by policymakers but rather an inadvertent result of the [US] state's attempts to solve other problems. She supports Polanyi's dictum that 'laissez-faire was planned', as 'freeing' the markets required active state intervention. Yet, her insightful analysis shows that even though the state was absolutely central, financialization 'was subject to trial and error, and not nearly as seamless as it has sometimes been presented' (Krippner, 2011: 3). Hence, it is important to bear in mind that the relationships between states and finance are complex, can be contradictory, and are to a large extent the results of *bricolage*. With respect to the belief that certain scientific formulas and models were unilaterally adapted in the finance sector, for example, Ewald Engelen et al. (2011a) show that practices and regulation were constantly changing and grafted on existing knowledge and regulation:

> For [Claude] Levi-Strauss, bricolage is a 'parallel mode of acquiring knowledge' (1966: 13) and involves 'build[ing] up structures by fitting together events, or rather the remains of events, while science, "in operation" simply by virtue coming into being, creates its means and results in the form of events, thanks to the structures which it is constantly elaborating and which are its hypothesis and theories' (Levi-Strauss 1966: 22). (Engelen et al., 2011a: 51).

Reality turns out to be much less straightforward than is often presented. Government practices and interventions, but also innovation originating in financial markets, tend not to be the product of engineering or a rationalist grand plan, but much more the creative and resourceful use of materials at hand, regardless of their original purposes. Changes and innovations such as the repeal of Glass-Steagall Act and Basel II are illustrative of this process (Engelen et al., 2011a: 51-52). In other words, new regulatory principles are frequently created out of the materials at hand instead of solely originating in rational scientific knowledge.

Evidently, the growth of national financial sectors and of global finance could not have been possible without explicit and implicit state interventions and support, even though states – and their regulatory apparatus – could not prevent crises from happening. As Panitch and Gindin argue in another publication, state institutions were not necessarily unaware of the potential dangers: '[already in 1987, the New York Federal Reserve] saw what was happening in

[2] Apart from the driving force behind the expansion of global finance, the central role of the Unites States was also 'closely related to, and augmented by, the growing international predominance of American corporations' (Panitch and Gindin 2012: 112).

financial markets as a double-edged sword, expanding the range and cheapening the costs of financial transactions while at the same time producing such a massive increase in market volatility as to make financial crises more likely' (Panitch and Gindin, 2014: 381). Despite close involvement, many activities in modern finance seem to have been beyond the scope of the state to exercise effective control. When it spirals out of control, though, it becomes increasingly difficult for states to take their hands off:

> The "moral hazard" tightrope that the state had to walk in this respect was nothing compared with the practical hazard involved in figuring out whether allowing even a small bank to collapse might have systemic effects […] in May 1984, with "the liquidity of the whole banking system" at stake according to the Treasury, the most ideologically free-market-oriented Republican administration since the 1920s nationalized the bank and bailed out its creditors. It was when the Treasury's comptroller made it clear during Congressional hearings on Continental Illinois that the uninsured creditors of the eleven largest US commercial banks would be treated in the same fashion that the term "too big to fail" came into widespread usage (Panitch and Gindin, 2012: 179).

The 2007/2008 crisis illustrated that the TBTF issue had not but been solved. Up till today it remains a pressing concern. In July 2014, the Brussels based think-thank Breugel organized a seminar in which regulators, bankers and other concerned parties discussed the latest developments aimed at solving the TBTF issue. Notwithstanding concerns about the social costs rescuing insolvent banks may entail, all current regulatory proposals focus on technical fixes in the structures of banks, their shareholders, asset categories, and so forth. There seems little political pressure to actually decrease the size of banks. On the contrary, banks, in the US particularly, have increased in size after the crisis – or as Peter Boone and Simon Johnson state (2010: 248), the bailouts and bust amounts form an implicit taxpayer subsidy that encourages individual institutions to become larger and, as a result, the whole system to swell. If relying on regulators' historical track record, this seems to offer little relief for taxpayers. Prior to the crisis it was assumed by regulators that TBTF was solved because of regulatory measures like capital-adequacy standards and quick interventions. Regulators, moreover, believed that two prominent financial innovations encouraged by the US Treasury Department, securitization and derivative markets, had led to a 'renewed focus on responsibility and discipline in finance' (Panitch and Gindin, 2012: 266). It could not have been further from the truth, as we now know.

Current regulations targeting financial institutions leverage-ratio also provide little hope that states will not to have to act as lenders of last resort again. Financial institutions' capital requirements remain extremely low (Finance Watch, 2014: 5) and need to be simpler and more robust to avoid large banks from gaming the rules (Pagano, 2014). Anat R. Admati and Martin Hellwig's (2013) widely cited work, moreover, undermines the financial sector narrative for maintaining low capital requirements, in particular by debunking the argument that more capital means that borrowing money becomes more expensive. With regards to this paper, it is in particular about how the leverage-ratio may affect the wholesale funding that the interbank lending financial institutions to a large extent rely on. Uncertainty about each other's balance sheets, as the 2007/2008 financial crisis demonstrated, quickly halts the operations of the largest (systemic) banks. The next crisis will actually demonstrate whether financial institutions can maintain the argument that current requirements are sufficient or, more likely, whether they also go against their own arguments and quickly become suspicious about their counterparts potential to remain solvent. In the latter case, it is highly likely that states will have to step in as lenders of last resort again. In other words, implicit state subsidies seem not to have ended once and for all: '[e]ven with systemic risk reduced, the state is unlikely to be able to credibly to stand aside when future tail risks eventuate, as they are sure to do' (Allesandri and Haldane, 2009: 16).

States and their citizens

Perceptions about the state and its supposed and actual functioning are varied, yet as the previous section has illustrated the intimate relationships between the state and finance are often ignored. It does not fit well with the dichotomy between the state and finance (or the private sector as a whole), which is particularly prevalent in dominant neoliberal discourses. What is more, even when they have intimate knowledge about the contrary some of neoliberal's most ardent supporters uphold the image. William E. Simon, who was the US Treasury Secretary from 1974 to 1977, perfectly illustrates this. Simon, who had been successful as a bond dealer at Salomon Brothers before he joined the US government, '[may have] expounded neoliberal nostrums about the need for a small state more loudly than anyone else, but he was fully aware how intertwined were Wall Street and "big government" [due to his previous work at Salomon Brothers, which was highly active in trading government bonds]' (Panitch and Gindin, 2012: 146).

In the realities of the triangular relationships between the (democratic) state, the financial sector, and the state's citizens (or taxpayers), close ties between finance and the state may affect the third party, the citizenry. The 2007/2008 financial crisis is illustrative of the quick pace in which state interventions turned into democratic liabilities. Many ordinary citizens have been burdened with the social and economic costs of the crisis, while they are by and large of the opinion that they are not responsible for the crisis. Instead, as countless media reports have shown, it is commonly believed that irresponsible behaviour of bankers and other financial professionals caused the crisis.[3] Accordingly, (political) responses to the crisis are presented as minimizing the social fallout of future crises, with politicians taking turns in criticizing bankers and the like – for their greed, irresponsibility, lack of empathy, arrogance, and so forth (e.g, Hall and Daneshkhu, 2009; Beattie, Ward and Guha, 2009). While there is probably a grain of truth in these accusations, it distorts the picture of the state's role.

Democratic states tend to portray themselves as defenders of the rights and positions of their citizens. Most (financial) state support to financial institutions has been framed with regards to the economic consequences, with the economy being synonym for society's prosperity. TARP and other state interventions have been presented as rescue operations aimed at containing the social consequences of faltering financial sectors. As shown, some are of the opinion that the interventions were rather successful, while also the international collaboration between governments has been praised (e.g., Drezner, 2014). In a number of cases governments may have recouped their financial aid and there was certainly a level of international collaboration. In other cases, in particular with regard to the nationalization of banks in Europe, it remains to be seen whether governments will be able to recoup the full amount. In case they will not succeed, the bill will have to be paid for by the taxpayers. Equally, rising unemployment and austerity measures as a result of the financial crisis have hit large segments of the American and European populations. Governments seek to reduce costs by economizing on their

[3] See also the documentary *Inside Job: How Bankers Caused the Financial Crisis* (2010).

expenditures on, to name a few, medical care, old-age care, army staff and equipment, and public services more generally. These measures are politically justified by the argument that it reduces the costs for national constituencies. We should certainly not trivialize high government debts, yet it is debateable whether austerity measures are really intended to minimize the costs for (future generations of) national citizens.

Governments publicly maintain the image of putting their citizens first. As a result a distorted picture of what is really going on is maintained, thereby limiting any fundamental discussion about the relationships between the state, its citizens and finance. The focus is predominantly on technical fixes of the system as the solution 'to reduce system complexities and introduce redundancies to make the financial system more robust' (Engelen et al., 2011b: 5), with finance presented as a neutral domain operating outside of the realm of the state and politics.

A major problem with a strong focus on technical fixes is that they obscure the political balancing between the interests of (international) finance and of (national) citizens. Wolfgang Streeck, in his book *Buying Time: The Delayed Crisis of Democratic Capitalism* (2014), captures the actual situation by distinguishing between *Staatsvolk* and *Marktvolk*: the 'general citizenry' and the 'people of the market'. Apart from that one (*Staatsvolk*) is nationally organized and the other (*Marktvolk*) organized internationally, there is a substantial difference in the claims both groups can make on the state. Increasing influence of the *Marktvolk* relates, according to Streeck (2014: 80–90), to the increase in sovereign debt – the debt state. While in democratic states, the *Staatsvolk*, can express their will in periodic elections, the power and influence of the *Marktvolk* comes through their role of creditors to the state: 'as creditors, they cannot vote out a government that is not to their liking; they can, however, sell off their existing bonds or refrain from participating in a new auction of public debt' (Streeck, 2014: 81) – moreover, they have a substantial influence over setting the interests rates for sovereign debt. It is telling that after every presentation of new plans that lay out solutions to the Eurozone's sovereign debt crisis, politicians often anxiously awaited the reactions of the financial markets.

Streeck illustrates the tensions between these two groups; in particular how states balance between the interests of the two sides. He is clear, however, about which side the state favours:

> As far as creditors are concerned, they need to ensure that any future 'haircut' will affect not them but, for example, pensioners and clients of national health care systems – in other words, that governments exercise sovereignty only over their *Staatsvolk*, not their *Marktvolk*. If we think of the discussions of recent years, we can see that this principle is now already taken for granted: it is a commonplace across the political spectrum that 'the markets' must not be 'unsettled' at any costs, whereas the unsettling of citizens-as-pensioners or citizens-as-patients has to be accepted in the name of the public good (Streeck, 2014: 86–7).

The concealed reality, then, is that managing public finances is much more a response to financial markets than to the national citizenry, even though the latter may ultimately be the one feeling the consequences. As Cornelia Woll (2014) shows, it is not a one size fits all, as some states are more successful (France in her case) in engaging large financial institution in mutual rescue operations – and thus in limiting the burden for the taxpayer. Notwithstanding, Streeck is of the opinion that states do too little to serve their citizens, the *Staatsvolk*:

'Nowhere is it written that [states] can use their sovereign powers only to meet their obligations to finance markets, by increasing taxes or decreasing benefits for their citizens. The first obligation of democracies is to their citizens; they can make laws and dissolve contracts; anyone who lends them money can and must know that' (Streeck, 2014: 162). Yet, relatively few states have so far considered this a viable option. As the next section illustrates, this seems to a large extent the result of geopolitical considerations.

Geopolitical concerns

As already said, state institutions are aware of the dilemmas they face: '[t]he unresolved dilemma for all capitalist states today is how to both stimulate the economy and regulate financial markets so as to limit increasingly dangerous volatility without undermining the ability of finance to play its essential role in global capitalism' (Panitch and Gindin, 2012: 333). They have, in other words, to seek a good balance between how to best manage the (national) economy for society to prosper and how to facilitate (global) finance. This also is by and large a matter of geopolitics, as states tend to favour finance over their citizenry due to the role financial markets play in the current world order. Surprisingly, however, there is relatively little research looking at how these aspects interact and interrelate – and, thus, how it helps to understand the continuing potential for taxpayers to have to pay the costs of future rescue operations.

The Great Depression and two world wars negatively affected the legitimacy and growth of the financial sector and 'not until after 1985 did the international financial markets re-emerge as a major factor' (Sassen, 2005: 21). Today the financial system can arguably be considered a global system (Knorr Cetina and Preda, 2005: 5). *Finanscapes*, the flow of large quantities of capital at blinding speed over the globe (Appadurai, 1990), have shaped a truly interconnected global grid. With it the financial service sector has increased in size, complexity and, especially, centrality in the operations of the world economy. States learned by doing how this affected their room for manoeuvre, as the Herstatt crisis in (then still) West Germany illustrates. To avoid 'moral hazard', its central bank, the Bundesbank, had allowed Bankhaus I.D. Herstatt of Cologne, one of the country's largest private banks, to collapse in 1974. The central bank was forced to reconsider its stance, however, this marking a turning point:

> It was the Bundesbank that was taught a lesson in the internationalization of the state. By the end of the year it had agreed to assume responsibility for paying off Herstatt's creditors, giving foreign banks preference over German banks and corporations. More broadly, it was drawn into supporting the US position that "a firms and explicit commitment must be given to the marketplace that central banks would provide lender-of-last-resort to banks operating in the Euromarkets" (Panitch and Gindin, 2012: 153–4)

Finance, it shows, was gaining prominence over democratic decision-making processes. Streeck refers to it as a transition from a Keynesian to Hayekian political economy. States, though sovereign in theory, have to pursue policies and regulation in accordance with dominant economic beliefs about efficiency theory, while in the past they had much wider range of instruments for discretionary government intervention (Streeck, 2014: 110). The accompanying shift to a debt state largely contributes to this since states have to rely on the confidence of financial markets for the (re)financing of their sovereign debt. This, according to

Streeck, comes at a cost for the citizenry. In the aftermath of the latest financial crisis, for example, governments impose harsh austerity measures on themselves and their citizens '[t]o regain the "confidence" of "the markets"' (Streeck, 2014: 9).

It could be argued that finance, or capital more generally, has gained an ever more stronger influence over the state, to the extent that it seems that finance keeps the state hostage. It is assumed that capital is highly mobile and that if states do not respect the conditions set by financial markets, the capital would move elsewhere. Austerity measures certainly confirm this, as one of the main incentives for governments to strictly control their budgets is that more favourable credit ratings lower the borrowing costs. One could claim this is to the advantage of the taxpaying citizenry as the state is trying to control its sovereign debt and pay the least interests on this debt possible. The citizenry may nevertheless suffer the consequences of austerity measures. These measures, moreover, are by and large the result of a particular approach of states towards finance; namely, allowing finance to becoming increasingly more important and difficult to curtail once it fails. In the case of the United Kingdom, for example, bank balance sheets increased significantly since the early 1970s: 'By the start of this century, bank balance sheets were more than five times annual UK GDP. In the space of a generation, the insurable interests of the state had risen tenfold' (Allesandri and Haldane, 2009: 3).

The increasing importance of finance was an interaction between the state and finance, and as illustrated above could not have occurred without the active participation of states. In all cases the spread and spatial expansion of financial markets happened in close collaboration with the state. They provided legislative and administrative changes, coordinated with other states and signed treaties to accompany the extending of markets: 'The more capital became internationalized, the more states became concerned to fashion regulatory regimes oriented to facilitating the rapid growth of international trade and foreign investment' (Panitch and Gindin, 2012: 223). In a way, finance has become the new 'benign' driver for geopolitical struggles in the sense that it is geopolitics without armies. The image of geopolitics as physically fighting over territory and resources, which certainly remains prevalent, has to a large extent been overtaken by geopolitical concerns about how to please and use global finance to one's advantage; compared to Susan Strange's 1988 analysis about power in the world economy, finance has even become more significant (see for a reflection on her analysis of the state and finance also Underhill 2000). This favours, with regard to Streeck, the international position of the *Marktvolk* – equally reflected in Thomas Piketty's (2014) observation of increasing inequality.[4] Owing to international competition between states, states seem to favour finance over their citizenry. By and large, the citizenry is immobile, while finance is not. Geopolitically, one can compete in attracting large and internationally operating financial institutions. Competing over who offers their taxpayers the best guarantees may win votes domestically, yet it does very little internationally. The latest financial crisis illustrates this.

[4] It is argued that, especially in the last decade (with, for example, the economic development of the BRICS), global finance has decreased inequality between states. Within states, however, inequality is on the rise as a result of the globalization of finance.

2007/2008 financial crisis

To minimize the consequences, an urgency to address the problems internationally was prevalent in the immediate aftermath of the 2007/2008 financial crisis. Governments worked overtime to mitigate the economic costs and to draft new regulation to prevent the same from happening again. The financial sector also has not sat around idly. On the one hand, banks and other financial institutions have closely collaborated with the government. Many banks have realized that a stronger and healthier financial system would be in their advantage, as also the European Banking Authority (2014: 34) acknowledges. Nor should the impact of reputational risk be neglected since financial institutions have much to regain after the crisis spurred an increase in loss of confidence among the public. On the other hand, financial institutions have tried to influence the directions of new regulations by (openly) objecting to stricter rules. JP Morgan Chase's CEO Jamie Dimon, for example, said in 2011 that new global bank rules would be 'anti-American' and that the United States should consider pulling out of the international negotiations (Liberto, 2011). On many other occasions, financiers equally shared their dislike and, for example, threatened to depart from the City when rules would become too restricting (e.g., Barty, 2009; Mackintosh, Parker and Tait, 2009; Jenkins and Burgess, 2010). Notwithstanding outcries from financiers, however, states have so far hardly threatened the existing financial model. This may be blamed partly on regulatory capture. Placing a limit on the size of the financial sector has been suggested: 'It makes little sense for larger or mid-sized economies like the U.K., Switzerland, and the U.S. to be deriving 20 percent or so of their GNP from financial sector activities, when finance, like law and accounting, should be about facilitating economic investment, not being the investment itself' (Warwick, 2009: 7). Yet, when deconstructing states' geopolitical concerns it needs to be questioned whether 'it makes little sense' to maintain large financial sectors.

International negotiations aimed to establish a unified regulatory approach, are illustrative of the role of geopolitical concerns. There is a strong argument to be made that states have learned from the past, as they certainly see the value of international collaboration in the mitigation of the economic consequences of the crisis. At the same time, though, if it were not for national interests it would probably be much easier to design stricter global regulation. Diverging interests seem to have prevented full international collaboration, notwithstanding that is a matter of perception to what extent global coordination has been successful.[5] The G20, for example, has produced little in the way of co-ordinated action (Tett, 2010a). Neither, however, have national regulatory apparatuses really contained the size and influence of their respective financial sectors. For example, to little avail '[m]any expected the Great Recession to be followed by a new New Deal' (Davis, 2009: vi). The Dodd-Frank Wall Street Reform and Consumer Protection Act may be an impressive piece of legislation, but it is doubtful whether it will significantly change the balance between the state, finance and its citizens. Equally, sustained efforts within the European Union seem to have hardly changed the balance even though systemic risk, like in the United States, may have been reduced.

The lack of international success can partly be contributed to the fact that the defence of national interests quickly resurfaced in the aftermath of the crisis – which is not to say that international coordination does no longer play a role, nor that it has not been improved, in particular in comparison to the 1929 crash. United States regulatory responses, though

[5] Allan Beatle, in his 17 August 2014 review of Daniel W. Drezner's *The System Worked: How the World Stopped Another Great Depression*, disagrees, for example, with the analysis of how successful international collaboration was, even if he praises the author for his detailed knowledge (retrieved from www.ft.com).

certainly informed by international negotiations, shows the Unites States' tendency to unilaterally draft regulatory principles (e.g., Persaud, 2010). European officials, conversely, have been reluctant to import 'made in America' ideas, which exposes transatlantic differences (Tett, 2010b). It should be noted that these differences are not informed by geopolitical concerns only, as political and cultural traditions equally inform ideas about how to establish a robust financial system and minimize future social costs. Within Europe, however, opposing national interests clearly limit coordinated efforts to regulate finance, in particular between the United Kingdom (and its City) and continental Europe. France, for example, has been accused of trying to take advantage of the United Kingdom (Betts, 2009). While London is urged to stand up against Brussels out of fear that new European regulation will put the City at a disadvantage (Barker, 2011). Demands for a referendum about the United Kingdom's membership to the European Union seem to partly originate in conflicts over financial regulation, though ironically it has recently been suggested that a departure may actually harm the position of the City (Arnold and Fleming, 2014).

The United Kingdom's current geopolitical position relies predominantly on the global significance of the City and, thus, the United Kingdom has an interest to maintain it as one of the world's strongest global financial centres. Owing to the size of the United States' economy, New York may remain an attractive financial centre even if the United States would more strictly regulate their financial institutions. In the United States there also appears little interest in decreasing the size of its banks and/or financial sector. Also in the context of geopolitical struggles with the economic powerhouse China, it is highly unlikely that the United States will allow its banks to be substantially smaller than the Chinese ones. The implicit logic: large banks and/or financial sectors give them global advantages – 'the largest banks … have not been broken up because of fears that doing so would fatally undermine New York's and London's status as global trading centres' (Bell and Hindmoor, 2014: 360).[6] The latest conflict between the United States, the European Union and Russia over the Ukraine illustrates that states controlling global financial centres have an edge. With sovereign control over these centres you are able to block, control and survey financial flows. This indicates that states have a large potential to interfere in financial markets when they please to do so. Without doubt the boycott of Russia is circumvented, yet there appears to have been relatively little objections from the financial sector. In other words, states have many more tools at their disposal to force their will upon finance than they would like their citizens to believe.

States with significantly smaller financial sectors, due to the absence of the world's financial centres in their sovereign territory, appear to equally let geopolitical considerations influence their approaches towards their respective financial sectors. Germany, in comparison with the United Kingdom, has a much stronger industrial sector. Hence, Germany would remain economically (and geopolitically) influential even without a smaller financial sector. By forcing Deutsche Bank to become smaller, however, Germany would no longer host one of the world's largest banks. Equally, smaller states like Switzerland and the Netherlands seem to put relatively little effort in downsizing their financial institutions and/or sectors to levels that no longer requires the need for rescue operations in the case they fail.[7] Here, the narrative of

[6] International competition over tax treaties and favourable investment climates seem to a certain extent to be influenced by similar geopolitical concerns.
[7] Nicolas Véron, from the Brussels based think-tank Bruegel, for example, refers to the fact that even in the integrated European market there were incentives for banking nationalism and the support of domestic banks at the expense of financial stability and prudence (see the UK's 2014 House of Lord's inquiry on *Review of the EU Financial Regulation Framework*).

perceiving Europe, and to a lesser extent the United States, as the losers of the 2007/2008 financial crisis is of relevance. On the one hand, the more prominent role given to the G20 confirms this trend. On the other hand, the Unites States remain dominant despite the predications. And although the European Union is another story, it is equally questionable to what extent we witness a decline. This is not to say that crises cannot spell the end of certain regimes. Yet, in the current geopolitical constellation one way of preventing this from happening seems to maintain a strong financial sector and/or large financial institutes; fearing the increasing prominence of Asia may only further reinforce this. A relatively strong financial sector can serve as leverage in geopolitical struggles, while it also helps to maintain sovereign control over national and international financial flows. It may come at a cost, however, to the taxpaying citizenry and, in Europe in particular, to the welfare state. Europe, then, may not necessarily lose out as a result of the crisis, but their citizens may certainly have to pick up the bill again when the next crisis hits.

Concluding remarks

In order to maintain geopolitical power it can be argued that, in the triangular relationships, the state tends to favour finance over their (taxpaying) citizens. Or so it seems, because it is difficult to present unambiguous conclusions about the costs and benefits of geopolitical concerns. It certainly appears that the potential costs for taxpayers have all but been solved. Yet, there may also be financial benefits to maintaining geopolitical power. In conclusion of the analysis presented in this paper, three considerations are of particular concern.

First, judging from the evidence presented in this paper, states play a crucial role in the organization and maintenance of (global) finance; hence, the opposition between the state and finance is, in the words of Panitch and Gindin, a false dichotomy. Much remains unknown about the everyday realities of the operations of states, however, in particular about how state employees and institutions perceive their roles. Boone and Johnson (2010) partly blame the absence of stricter regulation on the logics of the political system, for example. Politicians, they argue, like looser regulation, because it may generate a credit boom. This may serve them when in power, while the troubles generally come later. This implies that you have to be of a strong character to be strict in times of prosperity. As a result, fundamental underlying problems in the financial system are not systematically addressed because 'the long-standing and repeated failure of regulation to financial collapses reflects deep political and operational difficulties in creating regulation for modern finance' (Boone and Johnson, 2010: 253). Following up on the concept of *bricolage*, moreover, governments, regulators, and politicians have to deal with what is at hand. Most likely, state officials and politicians do not have well-thought strategic considerations to favour finance at all costs and/or to perceive taxpayers only as tools in their geopolitical aspirations. Yet, fine-grained details about whether they explicitly discuss trade-offs remain absent; '[t]he conflict between the two stakeholder groups competing with each other for control of the democratic debt state is a new, developing and as yet hardly understood phenomenon' (Streeck, 2014: 84).

Also, there are not necessarily two clear-cut opposing blocks. On the side of the financial sector, (sovereign) bond traders, merger and acquisition bankers, analysts, institutional investors, sovereign funds, and hedge fund managers – with often different national backgrounds and a variety of geographical locations – do not necessarily have the same goals. Moreover, business interests may also differ between the financial sector and big business, even though they are strongly intertwined (e.g., Ouroussoff, 2010; Pagliari and

Young, 2014). The side of the citizenry is equally not a unified block, let alone that one can easily determine who profits and who does not from the increasing dominance of finance:

> The Occupy movement suggests that it is 1 per cent against 99 per cent. However, while it is possible to make some distinctions between the various constituencies and projects concerning the regulation of finance, there are challenges to identifying a simple division between the beneficiaries and losers of finance. The process of financialization has implications for the nature of the constituencies engaged in political processes, in some instances blurring boundaries between what might have been distinct categories of supporters and opponents of finances capital and its political projects (Walby, 2013: 502–3).

Scholars from a variety of disciplinary backgrounds, such as economics, political sciences, sociology, and anthropology, could help to further our understanding of how states perceive their relationships with finance and their citizens. This will help to enhance our knowledge on why differences and similarities between narratives and practices in defence of the taxpaying citizenry may occur.

Second, can it be calculated to what extent ordinary citizens benefit financially from the maintenance of large financial sectors? States and their political representatives may believe that remaining geopolitically significant is the best approach in the defence of their national economic (and social) interests. This begs the question whether geopolitical considerations – and the defence of finance, with all the implicit subsidies that come with it – are economically beneficial to their (taxpaying) citizenry or not? It is probably difficult to get a straightforward answer, yet it is a question that needs critical engagement since states evidently pursue the belief that there are (economic) advantages to supporting their national financial institutions and sectors. Notwithstanding, and resonating the first consideration, state officials have to maintain a precarious balance between defending the state's particular interests and not diverting too much from what is done internationally. After all, states may favour a (too) large financial sector, yet they cannot afford for their financial institutes to have a higher risk of collapsing than those of other states, as this could harm their competitive edge and geopolitical position. Furthermore, what if power more than economic concerns drives geopolitical struggles (and their related support for financial sectors)? It may even happen that national citizenries, out of nationalistic pride, defend politicians and state representatives who will not bow to international pressure, even if the result is that these politicians defend the national interests of their respective financial sectors more than that they push for a financial sector that may be smaller, more boring, less internationally important, yet demonstrable more sustainable for the citizenries' prosperity.

Finally, then, even if there is room for improving the current balance, how likely is a major regulatory overhaul? Panitch and Gindin, for example, are not very optimistic about the potential for this to happen. They point to the gap between revolutionary spirits, such as manifested by the Occupy movements, and the realities of capitalism. According to them, it is not possible to change the world without taking power:

> Whether called socialism or not, today's revived demands for social justice and genuine democracy could only be realized through such a fundamental shift of political power, entailing fundamental change in state as well as class structures. This would need to begin with turning the financial institutions that

> are the life-blood of global capitalism into pure utilities that would facilitate, within each state, the democratization of decisions that govern investment and employment. But very different movements and parties from those that carried the socialist impulse in the previous century would be necessary to see this through (Panitch and Gindin, 2012: 340).

They may be right, though it is not set in stone what directions financial regulation will take. As with the process of financialization that Krippner (2011) refers to, it is also a matter of trial and error. Openly asking fundamental questions about what kind of relationships between the state, its (taxpaying) citizenry and finance 'guarantees' most prosperity to the majority of the citizenry should be part of it. The crisis, after all, was not a natural disaster. Instead, states contributed to the present form of the global financial system. If desired, then, they can also help to change it for the better.

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