RESTORING TRUST IN THE SYSTEM - CORPORATE GOVERNANCE

Remarks by David Begg, General Secretary, Irish Congress of Trade Unions at the OECD Forum, Paris May 24, 2011

I want to talk about the power of ideas. As Keynes famously remarked, ideas are dangerous for good or evil.

Ideas shape governance institutions and because of path dependency make it difficult for people to look at the world in a different way. As the Harry Chapin song had it: "There's no need to see things any other way than the way things always have been seen!"

The truth of this was brought home to me very forcefully at the EU Economic Conference in Brussels last week. The representatives of the international institutions – including the OECD – framed their contributions in orthodox, neoclassical terms.

It is surprising how resilient (neo) liberalism is. After all, it is less than three years since Alan Greenspan famously declared to a House Committee session in Washington that: "I have found a flaw. I don't know how significant or permanent it is. But I have been very distressed by that fact."

This was Ben Bernanke's mentor, former Chairman of the Federal Reserve and prophet of deregulation speaking. Such a frank admission from such a source might have been expected to signal the end of neoliberalism, the ideology that shaped the last 30 years.

Greenspan had repeatedly claimed that self-regulation was the only basis for a modern financial system; that far from being a danger, the pursuit of self-interest by bankers was the most effective self-defence mechanism in the market system.

Since the early 1990s, Governments in the US, the UK, and the Eurozone pursued inflation-targeting policies designed to smooth out cyclical ups and downs. They used low interest rates to stimulate a debt-driven recovery after the dotcom crash in 2001. The flood of cheap goods from China helped to suppress inflation. It was Bernanke who coined the phrase 'The Great Moderation' to describe this period.

It appeared that stability had been achieved by policy alone. It is now clear that this was not the case. Stability was sustained by the deflationary impact of China, the relentless rise of cheap credit and an altered balance of power between labour and capital.

Now that the cheap credit model has collapsed, and the deflationary impact of China appears to be transitory, we are left with just the capital-labour mismatch. The collapse of the Soviet Union, the decision of China to go capitalist by decree and the marketisation of India after 1991 added an extra 1.5 billion workers for capital to employ. This massively tilted the balance of power in favour of capital, strategically weakening the bargaining power of workers in every country.

It may take a long time for this imbalance of power to play out. But already its effects are evident.

Last week the High Pay Commission in the UK reported that the FTSE 100 Chief Executives are on average paid £4.2 million annually or 145 times the median wage. By contrast the earnings of someone in the middle of the income distribution rose at less than 0.7% year over the period 1996/7-2007/8.

The interesting thing about these data is that they indicate that in the liberal market economies at least, the very rich are soaring ahead of not just manual workers but the middle class as well. We are talking here of doctors, teachers, solicitors, academics, civil servants and so on. These are the people who internalised the values of individual aspiration.

What will the long term effects of this growing inequality be on society? Corporate governance as exercised by board remuneration committees is not likely to make a difference. And for all the talk of reform, the European banking system too remains substantially unaltered. The hedge funds remain unregulated; there has been no reinstatement of the equivalent of the Glass-Steagall Act to separate retail and investment banking. The ratings agencies still pronounce on the soundness of banks and countries as if they had no part in the crisis. And, of course, the bonus culture operates as it always did. Reform then is for the little people. Why would anyone want to trust a system like this?

To reflect specifically on the theme of governance we know that the institutional architecture of the Eurozone is not fit for purpose. This problem can be traced back to unresolved debates between so called 'Monetarists' and 'Economists' in the 1960s and 1970s. The original 1969 Werner blueprint for the EMU contained proposals for institutions to manage both economic and monetary union. The Delors Report in 1989 recommended only the creation of a European system of central banks.

I cannot see how the Euro will survive the crisis without creating institutions for fiscal and economic coordination. But the deeper integration which this implies is out of line with the political mood music in many Eurozone countries as evidenced by the increasing electoral success of nationalist parties campaigning on Eurosceptic platforms.

Speaking as someone who broadly favours deeper European integration I do not find this surprising. On the evidence of what I heard in Brussels last week the existing European institutions, apparently cowed by the intense intergovernmentalism between France and Germany, are driving a programmatic response to the crisis that is redolent of harsh Thatcherite neoliberalism.

If we were to pick one acute manifestation of this it is the proposal for *reverse qualified majority voting* where penalisation of a country for non compliance with the so called 'Europe Plus' Competitiveness Pact arises.

Apart from the Parliament the European institutions lack popular political legitimacy. They have always operated on a sort of permissive consensus from European citizens. In other words, they were left alone to pursue their objectives so long as they did no harm.

They are doing harm to peoples' lives now. In my own country, where the first electoral verdict on austerity was delivered, the party which dominated Irish politics from the foundation of the State was reduced to a rump party.

Is it possible for the institutions of the EU to insulate themselves from popular anger where people are suffering from their policies? It is irrational to think that they can because national politicians everywhere will transfer the blame to those institutions. Even in good times they have done this. Why would they stop now?

Let me try to encapsulate what austerity means in practice in Ireland. For most people it is a loss of personal economic security. People are afraid of losing their jobs, afraid of losing their homes, afraid of losing their pensions. Old people are afraid of not having anyone to look after them because the money to fund nursing homes has had to be spent on medicines. People who work in low wage sectors of the economy are afraid that statutory protection of minimum standards will be removed.

These fears are entirely real and justified. The austerity programme imposed by the EU/ECB/IMF has imparted a huge deflationary shock to the economy. This means that there is no growth. Without growth it is impossible to generate the primary surplus necessary to pay down debt.

The whole thing is self defeating but such is the power of ideas that it will be persisted with regardless of the consequences – ultimately to default probably.

It need not be so. In key areas the Irish economy is doing well. Exports are booming and this year we will have a balance of payments surplus.

But the combination of private and public debt is simply so enormous that demands to discharge it in a short time period at exorbitant interest rates are not capable of being accommodated by an otherwise viable economy.

There are reasonable alternatives being canvassed. In particular the concept of a Eurobond developed by Professor Paul DeGrauwe of Leuven University has much merit. It does require people to accept that we are dealing with a systemic problem of the Eurozone rather than just the problems of individual peripheral countries. As DeGrauwe puts it:

> 'A monetary union creates collective problems. When one Government faces a debt crisis this is likely to lead to major financial repercussions in other member countries. This is so because a monetary union leads to intense financial integrities'.

(DeGrauwe, 2011:26).

In any event it is obvious that the Eurozone policy response to the crisis is not working. Nor can it ever work because it is based on narrow ideas about economics which, as Greenspan acknowledges, are flawed.

This is not really a question of economics in the first place. It is a question of political economy. A political economy approach is a completely different way of looking at things. It holds that the economy is embedded in society and not the other way round.

Ideas are important. But where peoples lives are concerned you cannot expect to restore trust in the system unless people can see that the institutions are working for them and are not in the service of ideas promulgated by some long dead scribbler.

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