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“Consequences of the financial Crisis“.

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Introduction

As the title of this article indicates, I want to explain the consequences of the financial crisis.

Because the crisis came from the US to Europe I will also discuss some of the consequences of the financial crisis in the US.

The most obvious results of the Crisis in Europe, but also in the US, were the following:

I The new Regulations in Europe and in the US, like the Banking Union, the Frank-Dodd Act and EMIR regulation in order to trying to avoid a new crisis. Connected with the banking Union are the monetary politics of Draghi to reduce the interest rate to a historical low just to „stimulate the economy“.

Related to this policy are the notions inflation and deflation. This has to be studied as well.

These notions will also be discussed in connection with the views of the Austrian School. That indicates Von Mises’ and Hayeks point of view, but also the opinion of Jesus Huerta de Soto, adherent of the youngest Austrian School will be explained, because they have a totally different view on the mainstream financial policy of today.

II The Frank-Dodd Act and the EMIR regulation in order to trying to avoid a new crisis will be discussed separately.

III The new role of Europe’s Leaders and the shift of power.

IV Europe’s citizens’ changed attitude towards the whole European concept. It sounds very contradictory, but on the one hand the ideal of the Euro-crats of an ever-closer Europe seemed to come closer and on the other hand European

citizens revolted against this evolution and voted likewise: they are often referred to as the Euro-sceptics.

While previously the European citizen did not care about what happened in „Brussels“, now they want to have a say in that.

In the conclusion the future of Europe and some suggestions how to handle that, will be discussed.

I The new regulations as a result of the Crisis.

I.I The Banking Union

Introduction and explanation of the existing situation

During the last months, leading auditors were invited to deliberate how to put the balances of the big banks of the Euro-zone under the microscope, as it has never been done before. A patchwork of financial supervisors will be a matter of the past. Because of the ongoing crisis, this is –according to the EU officials- absolutely vital. Only when the balance is clean, can the banks provide the economy with credit and as a consequence enhance growth in order to revitalize the labor market.

Since it concerns a lot of money, States, investors, banks and the ECB struggle for power and influence. The auditor will pay particular attention whether loans, securities and derivatives are actually worth as much as the banks indicate in their balances. In case a bank fails, it has to provide for additional capital, but this can have a side- effect for banks that meet the minimal legal requirements. Also, because the supervision mechanism is still under construction, a lack of human resources and skills perpetuates the likelihood of the national supervisors being the evaluators of the balances. *Such in other words, means that the process of rehabilitation for banks will be essentially and necessarily the responsibility and duty of the nation state.*

In order to protect the tax-payers, the shareholders and creditors of the banks should be taken into duty in case of a crisis. Such a scheme is planned for 2016. Italy alone needs 25 billions in capital. The Special Representative of the ECB for the Audit, Ignazio Angeloni, had to make a decision this summer, but the problem cases have been identified: the *Commerzbank* in Germany, *Belfius* in Belgium and several others banks in the Euro-zone. It seems plausible to close the equity gaps without the help of the governments. That would be the most comfortable and optimal solution: the Germans would not have a debate about allocating the taxpayers' money for bankrupt banks, the southern countries would have no new EU requirements and the bankers no State intervention.¹

The banking Union is also an instrument through which to take affirmative steps towards “an ever closer Union”². As Jose Manuel Barosso said in his speech for the “*Jean Monnet*” conference on November 14, 2013: “In order to achieve such European-wide political consensus, a banking and a fiscal union must be constructed”. This is an obvious example of using an economic tool for a political goal.

¹ This information has been taken from the article “Und raus bist du” of Mark Schieritz and Arne Storn in “Die Zeit” dd 24 October 2013, p. 24

² Jose Manuel Barosso in his speech for the Jean Monnet Conference 2013: “The Political Implications of European Economic Integration- Towards a Political Union-” dd November 14, 2013.

“In this context, the final link in the European integration after the establishment of the economic and monetary union, would be in fact a *political union*. Claire Davenport and Robin Emmott³ referred to the remarks of Mario Draghi: “Today marks a real step forward in setting up a banking union”. President Mario Draghi added, that the central bank would push ahead rapidly with hiring the staff and building the institutional capacity to supervise the banks.

The Banking union, conceived as a three-stage process involving a single bank supervisor, a single resolution authority and a single deposit-guarantee scheme, is the most ambitious project launched since the region’s debt crisis and is designed to provide a stronger underpinning to the single currency project. It marks a new phase of deeper integration among the euro zone countries.

However, such strategy produces a variety of complex issues regarding sovereignty. Most notably Germany, the euro zone’s most powerful member state, is becoming increasingly concerned about an over-centralization of powers. Berlin already accused the European Commission’s proposal for an independent authority as being contrary to EU law and has publicly criticized the plan in a potential setback.

“The single supervisory mechanism is a linchpin of a deeper economic and monetary union”, European Commission President Jose Manuel Barroso said after the vote. “Now our attention must turn urgently to the single resolution mechanism,”⁴.

Another opinion is the following: "A first lesson is that a ‘banking union’ is more important than a ‘fiscal union’ in Europe⁵. The second lesson is that the current state of integration in the Euro-zone represents the worst imaginable combination:

- Any losses in the banking sector fall on the national governments, which are overwhelmed when a strong local boom turns into bust.
- The euro made the wholesale liquidity and funding market cross-border, so a system-wide liquidity crisis arises whenever a local banking system becomes insolvent.

The system cannot be sustained as it is. Europe must either move forward to a full banking union, or it will be pushed backwards into nationally segmented financial markets. At this present moment, the tendency towards the latter is clear. Unless a more integrated system is established, financial integration will have to move backwards⁶.

So far the (official) information in die “Zeit” and other sources have dominated the discussions.

Mr. Schulz, President of the European Parliament, said the banking union would only work if there was a European approach instead of leaving it up to member states, which would make it difficult to make a quick decision when a bank was experiencing difficulties. “If a bank cannot be wound up within a weekend in order to prevent a run on the banks, the system is too complicated,” he said. “The Commission must play a central role here, rather than not transparent bodies

³ Claire Davenport and Robin Emmott “ Europe clears critical hurdle on road to banking union” in “Business International news”

⁴ Idem

⁵ Wyplosz, Charles (2012), “The Eurozone’s May 2010 strategy is a disaster: Time to pay up and end this crisis”, Vox EU.org, 20 June.

⁶ Wyplosz, Charles (2012), “The Eurozone’s May 2010 strategy is a disaster: Time to pay up and end this crisis”, VoxEU.org, 20 June.

with not transparent interests – otherwise it will ultimately be a case of ‘Operation successful, patient dead’.

The EP president also criticized plans for a resolution system based on national funds instead of a single resolution system for the transition phase: “Ultimately, the taxpayer will once again have to come to the rescue after all. That contradicts the fundamental idea of the banking union, which is, that banks should come to the rescue of banks!”

I.2 What would be the opinion of the adherents of the Austrian School⁷ on this subject?

Ludwig von Mises and F.A. Hayek were adherents of the Austrian School. They proposed measures totally different from the ones taken today; Hayek had a different approach than Von Mises and Huerta de Soto⁸ has a totally opposite opinion.

- **Hayek** proposed the Denationalization of Money as an instrument to get a clean banking system. Such a theory has as principle that the creation of money is no longer in the hands of the national government, but that private banks can create money⁹.

- **Von Mises** on the other hand spoke of “sound money” and the means to achieve this goal, was to (re) introduce the Gold Standard. The Gold Standard has been in use for a very long time until 1971 and the times were prosperous. There was never so much trade between the different countries and continents as right before the First World War.

According to von Mises “the Gold Standard lost popularity because for a very long time no serious attempts were made to demonstrate its merits and to explode the tenets of its adversaries”¹⁰. The sound money principle has two aspects:

- "It is affirmative in approving the market's choice of a commonly used medium of exchange."
- "It is negative in obstructing the government's propensity to meddle with the currency system. The sound-money principle was an experience that could be perceived by a much larger public than the narrow circles of those conversant with economic theory. Hence the sound-money idea became one of the most popular points of the liberal program. Friends and foes considered it one of the essential postulates of a liberal policy”¹¹.

The position of the opponents is the following: “What the foes of the gold standard are asking for is not to reverse a prevailing tendency in the determination of prices, but to intensify very considerably the already prevailing upward trend of prices and wages. They simply want to lower the monetary

⁷ Ludwig von Mises and F.A. Hayek were adherents of the Austrian School

⁸ Huerta de Soto, adherent of the younger Austrian School.

⁹ F.A. Hayek: “Denationalization of money. An analysis of the Theory and practice of concurrent Currencies”, London Institute of Economic Affairs. Hobart Special Paper, no. 70

¹⁰ Ludwig von Mises “ The theory of money and credit” Orlando (1913)2009, p. 248

¹¹ Idem p. 247

unit's purchasing power at an accelerated pace". But what the people are really asking for is a rise in the prices of those commodities and services that they are selling while the prices of those commodities and services which they are buying remain unchanged".¹²

Huerta de Soto.

According to Jesús Huerta de Soto, the Euro has the same effect as the Gold Standard. In his article "The Euro as a "Proxy" for the Gold Standard". An additional aspect of the Euro, related to the Banking Union" he explained his point of view as follows.

"It forces governments to keep the budget in balance. "Only when exchange rates are fixed are governments obliged to tell citizens the truth. Hence, the temptation to rely on inflation and flexible rates to avoid the political cost of unpopular tax increases is so strong and so destructive. So, even if there is not a gold standard, fixed rates restrict and discipline the arbitrariness of politicians: "Even in the absence of a pure gold standard, fixed exchange rates provide some insurance against inflation which is not forthcoming from the flexible system. Under fixity, if one country inflates, it falls victim to a balance of payment crisis. If and when it runs out of foreign exchange holdings, it must devalue, a relatively difficult process, *fraught with danger for the political leaders involved*. Under flexibility, in contrast, inflation brings about no balance of payment crisis, nor any need for a politically embarrassing devaluation. Instead, there is a relatively painless depreciation of the home (or inflationary) currency against its foreign counterparts" (Block 1999, 19).

Huerta de Soto continues: "As we have seen, Austrian economists defend the gold standard because it curbs and limits the arbitrary decisions of politicians and authorities. It disciplines the behavior of all the agents who participate in the democratic process. It promotes moral habits of human behavior. In short, it checks lies and demagoguery; it facilitates and spreads transparency and truth in social relationships. No more and no less."

Perhaps Ludwig von Mises said it best: "The gold standard makes the determination of money's purchasing power independent of the changing ambitions and doctrines of political parties and pressure groups. This is not a defect of the gold standard, it is its main excellence"¹³

The result of inflationary policy on interest rates.

De Soto continues: "The introduction of the euro in 1999 and its culmination beginning in 2002 meant **the disappearance of monetary nationalism and flexible exchange rates** in most of continental Europe. Now what interests us is to note that the different member states of the monetary union completely relinquished and lost their monetary autonomy, that is, the possibility of manipulating their local currency by placing it at the service of the political needs of the moment. *In this sense, at least with respect to the countries in the euro zone, the euro began to act and continues to act very much like the gold standard did in its day. Thus, we must view the euro as a clear, true, even if imperfect, step toward the gold standard*". "This means limiting monetary nationalism as far as possible, eliminating the possibility that each country could develop its own

¹² Ludwig von Mises 1969, 251-253. The notes in the text are from Huerta de Soto.

¹³ Ludwig von Mises "Human Action" Chicago (1949) 1966 , 471

monetary policy, and restricting inflationary policies of credit expansion as much as we can", by creating a monetary framework that disciplines as far as possible economic, political, and social agents, and especially, labor unions and other pressure groups, politicians, and central banks.

It is only in this context that we should interpret the position of such eminent Austrian economists (and distinguished members of the Mont Pèlerin Society) as von Mises and Hayek. For example, there is the remarkable and devastating analysis against monetary nationalism and flexible exchange rates which Hayek began to develop in 1937 in his particularly outstanding book, *Monetary Nationalism and International Stability*¹⁴. In this book, Hayek demonstrates that flexible exchange rates preclude an efficient allocation of resources on an international level, as they immediately hinder and distort real flows of consumption and investment. Moreover, they make it inevitable that the necessary real downward adjustments in costs take place via a rise in all other nominal prices, in a chaotic environment of competitive devaluations, credit expansion, and inflation, which also encourages and supports all sorts of irresponsible behaviors from unions, by inciting continual wage and labor demands which can only be satisfied without increasing unemployment if inflation is pushed up even further. Thirty-eight years later, in 1975, Hayek summarized his argument as follows: "It is, I believe, undeniable that the demand for flexible rates of exchange originated wholly from countries such as Great Britain, some of whose economists wanted a wider margin for inflationary expansion (called 'full employment policy'). They later received support, unfortunately, from other economists¹⁵ who were not inspired by the desire for inflation, but who seem to have overlooked the strongest argument in favor of fixed rates of exchange, that they constitute the practically irreplaceable curb we need to compel the politicians, and the monetary authorities responsible to them, to maintain a stable currency".

It can be concluded that representatives of the Austrian School were fervently against inflation, but the ideas of Keynes, (who was pro inflationary measures) are still propagated as in the *Economist* (alas!) It writes, "none of this means that inflation will not one day be a risk. But it is not a today's problem. All the sound money fanatics, might reconsider whether Western policymakers did too little, not too much"¹⁶. *Alas: Keynes said about the same: "In the long run we are all dead". We know how his inflation policy worked out.*

I.3 The Interest rate, inflation and deflation.

Connected with the monetary policy is the policy concerning the interest rate, inflation and deflation.

Interest rate

Manipulating interest rates and inflation is part of the Keynesian politics, just as Draghi is nowadays using it.

Von Mises explained the following, concerning lowering interest rates and credit expansion: "At the beginning, the popularity of credit expansion was due to the

¹⁴ F.A. Hayek *Monetary Nationalism and International Stability*, Genève 1971 [1937]

¹⁵ Though Hayek does not expressly name them, he is referring to the theorists of the Chicago school, led by Milton Friedman, who in this and other areas shake hands with the Keynesians.

¹⁶ The Economist "The perils of falling inflation. In both America and Europe central bankers should be pushing prices upwards", November 9, 2013 p. 14

idea that it is a blessing for every country and for the whole world to have a low interest rate. Credit expansion was considered a vehicle to lower the rate of interest. The politicians wanted prosperity for his country, and for the people; even Coolidge in 1924 wanted low interest rates". He added to this: "The crash was the necessary outcome of the attempts to lower the rate of interest by credit expansion. Institutional unemployment was the inevitable result of the policy of minimum wage rates"¹⁷

Inflation and deflation

Inflation was/is one of the instruments used by the opponents of the Gold Standard. "From time immemorial inflation has been recommended as a means to alleviate the burdens of the poor worthy debtors at the expense of rich harsh creditors"¹⁸. "A government always finds itself obliged to inflationary measures when it cannot negotiate loans and dare not levy taxes. " But according to von Mises "inflationism is inadequate and technically regarded bad policy"¹⁹

He added to this: "The crash was the necessary outcome of the attempts to lower the rate of interest by credit expansion. Institutional unemployment was the inevitable result of the policy of minimum wage rates"²⁰

Historically the episodes of inflation correspond with periods of poor economic growth.

We have seen the result of trying to use the introduction of the Euro in order to achieve a political union. It failed. That is to say: the public opinion is more divided now than ever before.

Deflation or inflation, that is the question.

Referring to the previous remarks on Inflation, some reflections on Deflation.

Reason to treat this topic is that the ECB (Draghi) is afraid of the possibility of a deflation and already lowered the interest rate to under zero lately.

The eventuality of a possible deflation was also discussed in the article "Kommt jetzt die Deflation?" in "Die Zeit"²¹.

As a matter of fact the inflation was so high the last years, that a lowering of prices was more than welcome. Hence the aim to refute the general opinion, that deflation is a very bad and ugly thing.

Definition of Deflation

In economics "*deflation*" is a decrease in the general price level of goods and services²². Deflation occurs when the inflation rate falls below 0% (a negative inflation rate. This should not be confused with **disinflation**, a slow-down in the inflation rate (i.e., when inflation declines to lower levels). Inflation reduces the real value of money over time; conversely, deflation increases the real value of money – the currency of a national or regional economy. This allows one to buy more goods with the same amount of money over time.

¹⁷ Ludwig von Mises " Human Action" p. 849

¹⁸ Ludwig von Mises, idem p. 249

¹⁹ Ludwig von Mises " The theory of money and credit" Orlando (1913)2009, p. 119 and 124

²⁰ Ludwig von Mises " Human Action" p. 849

²¹ Kommt jetzt die Deflation?" in "Die Zeit" dd 3-4-2014, p. 1

²² Robert J. Barro and Vittorio Grilli (1994), "European Macroeconomics", chap. 8, p. 142. ISBN 0-333-57764-7

The official/mainstream version of deflation is the deflationary spiral according to the mainstream politicians. An answer to falling aggregate demand is economic stimulus, either from the central bank, by expanding the money supply, or by the fiscal authority to increase demand, and to borrow at interest rates which are below those available to private entities.

In more recent economic thinking, deflation is related to risk: where the risk-adjusted return on assets drops to negative, investors and buyers will hoard currency rather than invest it, even in the most solid of securities²³.

This can produce a liquidity trap or it may lead to shortages that entice investments, yielding more jobs and commodity production. A central bank cannot, normally, charge negative interest for money, and even charging zero interest often produces less stimulating effect than slightly higher rates of interest. In an autarky (a closed economy), this is because charging zero interest also means having zero return on government securities, or even negative return on short maturities. In an open economy it creates a carry trade ((investment), and devalues the currency. A devalued currency produces higher prices for imports without necessarily stimulating exports to a like degree.

In monetarist theory, deflation must be associated with either a reduction in the money supply, a reduction in the velocity of money or an increase in the number of transactions. But any of these may occur separately without deflation. It may be attributed to a dramatic contraction of the money supply, or to adherence to a gold standard or other external monetary base requirement.

However, deflation is the natural condition of hard currency economies when the supply of money does not grow as quickly as the population and the economy. When this happens, the available amount of hard currency per person falls, in effect making money more scarce; and consequently, the purchasing power of each unit of currency increases. Many people accept inflation as a fact of life. However, under certain economic situations, the opposite phenomenon actually takes place, and is known as “deflation.”

The official version sees deflation rather as an indication that economic conditions are deteriorating. Deflation is usually associated with significant unemployment, which is only corrected after wages drop considerably. On which the reply could be, that –if the prices go down–and the loans diminish, the result will be the same.

Furthermore, businesses’ profits drop significantly during periods of deflation, making it more difficult to raise additional capital to expand and develop new technologies. So far, the official (“mainstream”) version of deflation.

“Deflation” is often confused with “disinflation.” While deflation represents a decrease in the prices of goods and services throughout the economy, **disinflation** represents a situation where inflation increases at a slower rate. Although that might be presumed, disinflation does not usually precede a period of deflation. *In fact, deflation is a rare phenomenon* that does not occur in the course of a normal economic cycle, and therefore, investors must recognize it as a sign that something is severely wrong with the state of the economy.

What Causes Deflation?

²³ Hussman 2010

Deflation can be caused by a number of factors, all of which stem from a shift in the supply/demand curve. Remember, the prices of *all* goods and services are heavily affected by a change in the supply and demand, which means that if demand drops in relation to supply, prices will have to drop accordingly. Also, a change in the supply and demand of a nation's currency plays an instrumental role in setting the prices of the country's goods and services.

There are several definitions of Deflation²⁴.

I.4 Von Mises' version of the notion of deflation is as follows: "The notions deflation and inflation are not praxeological concepts. They were not created by economists, but by the mundane speech of the public and the politicians. They implied the popular fallacy that there is such a thing as neutral money or money of stable purchasing power and that sound money should be neutral and stable in purchasing power. From this point of view the term inflation was applied to signify cash-induced changes resulting in a drop in purchasing power, and the term deflation to signify cash-induced changes resulting in a rise in purchasing power. But purchasing power never remains unchanged and consequently there is always either inflation or deflation"²⁵.

As von Mises put it: "The terms inflationism and deflationism, inflationist and deflationist, signify the political programs aiming at inflation and deflation in the sense of big cash-induced changes in purchasing power. The semantic revolution has also changed the traditional connotation of the terms inflation and deflation. What many people today call inflation or deflation is no longer the great increase or decrease in the supply of money, but its inexorable **consequences**, the general tendency toward a rise or a fall in commodity prices and wage rates. This innovation is by no means harmless. It plays an important role in fomenting the popular tendencies toward inflationism"²⁶ "Credit expansion is a boon for the banks, contraction is a forfeiture. There is a temptation in inflation and expansion and a repellent in deflation and contraction"²⁷. Deflation in the Austrian definition would not include episodes of a falling price level due to, say, accelerated productivity growth or business cycle fluctuations where there was no accompanying monetary shortage.

I.5 Economic crises, Business depressions and Free Banking.

Let us consider what von Mises said about this topic. He looks at the problem from a totally different angle.

*"Many **socialist** authors emphasize that the recurrence of economic crises and business depressions is a phenomenon inherent in the capitalist mode of production. On the other hand a socialist system is safe against this evil according to them. As already has been obvious, the cyclical fluctuations of business are not an occurrence originating in the sphere of the unhampered market, but a product of government interference with business conditions designed to lower the rate of interest below the height at which the free market would have fixed it."²⁸ True, governments can reduce the rate of interest in the short run. They can issue additional paper money. They*

²⁴ Brendan Brown "The Global Curse of the Federal Reserve" Palgrave Macmillan, 2011 p. 53

²⁵ Ludwig von Mises "Human Action" 1966, The Ludwig von Mises Institute, Alabama p. 419

²⁶ Ludwig von Mises "Human Action" 1966 p. 420

²⁷ Ludwig von Mises idem, p. 565

²⁸ Ludwig von Mises "Human Action", 1966, p. 562

can open the way to credit expansion by the banks. They can thus create an artificial boom and the appearance of prosperity. But such a boom is bound to collapse sooner or later and to bring about a depression.”²⁹

Von Mises explains free banking as follows: “For the most part the banks with good repute are blamed for their conservatism and their reluctance to expand credit. However that is responsible behavior. In the eyes of people not deserving of credit such restraint appears as a vice. But it is the first and supreme rule for the conduct of banking operations under free banking.

The majority of liberal politicians simply surrendered to the popular hostility against money-lending and interest taking. *They failed to realize that the rate of interest is a market phenomenon that cannot be manipulated ad libitum by the authorities or by any other agency.*

Von Mises continued: “I want to conclude with a last line: Free banking is the only method available for the prevention of the dangers inherent in credit expansion. The governments interfered precisely because they knew that free banking keeps credit expansion within narrow limits”.³⁰ *In the eyes of the public opinion however free banking is mostly compared with “free trade in swindling”.* Von Mises is right to oppose to the continuing manipulation of the interest rate and to warn against the credit expansion. Also his interpretation of free banking is a right and surprising one.

To conclude: the fact that banks are going to be audited is a good thing, but to use the Banking Union as a political instrument to achieve an “ever closer Union”, is very wrong.

II The Regulation in the USA. A Wall Street Reform: The Dodd-Frank Act. The EMIR in Europe;

Introduction

The Dodd-Frank Act and the EMIR Regulation aim at the same target and are therefore discussed together in this article.

First of all I will describe the **official** American version of the financial crisis and the reasons for drafting the Dodd-Frank Act³¹.

II.I

“In the fall of 2008, a financial crisis of a scale and severity not seen in generations left millions of Americans unemployed and resulted in trillions in lost wealth. The broken financial regulatory system was a principal cause of that crisis. It was fragmented, antiquated, and allowed large parts of the financial system to operate with little or no oversight. And it allowed some irresponsible lenders to use hidden fees and fine print to take advantage of consumers.

To make sure that a crisis like this never happens again, President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act into law. The most far reaching Wall Street reform in history, Dodd-Frank is supposed to prevent the excessive risk-taking that led to the financial crisis. The law also provides common-sense protections for American families, creating new consumer watchdog to prevent mortgage companies and pay-day lenders from

²⁹ Ludwig von Mises “Omnipotent Government. The Rise of the Total State and Total War” Spring Mills Pa Libertarian Press (1944) 1985 p. 251

³⁰ Ludwig von Mises “Human action” idem, p. 440 and 444

³¹ <http://www.whitehouse.gov/economy/middle-class/dodd-frank-wall-street-reform3>

exploiting consumers. These new rules are meant to build a safer, more stable financial system—one that provides a robust foundation for lasting economic growth and job creation.

Holding Wall Street Accountable

According to **proponents** of the Dodd-Frank Act, “the financial crisis was the result of a fundamental failure from Wall Street to Washington. Some on Wall Street took irresponsible risks that they didn’t fully understand and Washington did not have the authority to properly monitor or constrain risk-taking at the largest firms. When the crisis hit, they did not have the tools to break apart or wind down a failing financial firm without putting the American taxpayer and the entire financial system at risk. Financial reform includes a number of provisions that will curb excessive risk taking and hold Wall Street accountable.

The idea is that taxpayers will not have to bear the costs of Wall Street’s irresponsibility: If a firm fails in the future, it will be Wall Street – not the taxpayers – that pays the price.

The regulation separates “proprietary trading” from the business of banking:

The “Volcker Rule” will ensure that banks are no longer allowed to own, invest, or sponsor hedge funds, private equity funds, or proprietary trading operations for their own profit, unrelated to serving their customers. Responsible trading is a good thing for the markets and the economy, but firms should not be allowed to run hedge funds and private equity funds while running a bank (something like the former Glass-Steagall Act ³²)

The Volcker rule, named after United States Federal Reserve Chairman Paul Volcker, is meant to restrict United States banks from making certain kinds of speculative investments that do not benefit their customers³³. Volcker argued that such speculative activity played a key role in the financial crisis of 2007–2010. The rule is often referred to as a ban on proprietary trading by commercial banks³⁴, whereby deposits are used to trade on the bank's own accounts, although a number of exceptions to this ban were included in the Dodd-Frank Act³⁵. The rule's provisions were scheduled to be implemented as a part of Dodd-Frank on July 21, 2012, with preceding ramifications but were delayed. On December 10,

³² See my article on the Glass-Steagall Act “Should we return to the Glass-Steagall Act after the Credit Crunch?” of January 2009, where the pro’s and cons of this regulation have been discussed.

³³ en.wikipedia.org/wiki/Volcker_Rule#cite_note-2

³⁴ (also “prop trading” or PPT) occurs when a firm trades stocks, bonds, currencies, commodities, their derivatives, or other financial instruments, with the firm's own money as opposed to its customers' money, so as to make a profit for itself. They may use a variety of strategies such as index arbitrage, statistical arbitrage, merger arbitrage, fundamental analysis, volatility arbitrage or global macro trading, much like a hedge fund. Many reporters and analysts believe that large banks purposely leave ambiguous the amount of non-proprietary trading they do versus the amount of proprietary trading they do, because it is felt that proprietary trading is riskier and results in more volatile profits

³⁵ en.Wikipedia.org/wiki/Volcker_Rule#cite_note3and4en.wikepedia.org/wiki/European_Market_instructure_Regulation#cite_note-1

2013, the necessary agencies approved regulations implementing the rule, which were scheduled to go into effect April 1, 2014. However, as of December 30, 2013, the final Volcker Rule regulations had not been published in the Federal Register, and the agencies had stated they were evaluating several issues.

Ending bailouts:

Reform will constrain the growth of the largest financial firms, restrict the riskiest financial activities, and create a mechanism for the government to shut down failing financial companies without precipitating a financial panic that leaves taxpayers and small businesses on the hook.

Protecting American Families from Unfair, Abusive Financial Practices

Before the crash that devastated America's economy, there were seven different regulators with authority over the consumer financial services marketplace. Accountability was lacking because responsibility was diffuse and fragmented. In addition, many mortgage lenders and mortgage brokers were almost completely unregulated. Too many responsible American families have paid the price for an out-dated regulatory system that failed to adequately oversee payday lenders, credit card companies, mortgage lenders, and others, allowing them to take advantage of consumers. That's why President Obama overcame the big bank lobbyists to protect and empower families with the strongest consumer safeguards ever.

President Obama's Wall Street reform law created an independent agency to set and enforce clear, consistent rules for the financial marketplace.

The Consumer Financial Protection Bureau (CFPB) is setting clear rules of the road and will ensure that financial firms are held to high standards. Like a neighborhood cop on the beat, the CFPB supervises banks, credit unions, and other financial companies, and will enforce federal consumer financial laws.

For example:

- For families who want to buy a home.
- For families caught by unexpected overdraft fees.
- For families with credit cards.
- For families considering student loans.

As a comment regarding the line "loans they didn't need or couldn't afford" the following can be said. Actually also the Federal government encouraged the ownership of houses ignoring whether the buyers could afford that or not, or were buying bonds and shares with borrowed money.

A reaction came from Rep. **Scott Garrett**, who explained in the "*The Cato Report*"³⁶ the following: "The law (the Dodd-Frank Act) creates two separate agencies ³⁷ that are granted essentially unlimited power to define and regulate nearly every conceivable financial transaction in the country. *Worse yet, they are accountable to no one. Put together, they are basically the judge, the jury and unfortunately, the executioner of the economy.* On top of that the Courts are not authorized to review and rule on whether or not FSOC has correctly interpreted

³⁶ Rep. Scott Garrett in the "The Cato Report" in the "Policy Forum" of September/October 2013, p. 10.

³⁷ The Consumer Financial Protection Bureau (CFPB) and the Financial Stability Oversight Council (FSOC)

the provisions of Dodd-Frank” The courts have no authority in this area. This means that the Separation of Powers, so dear to the Americans is wiped out by this regulation.

Imagine, that European courts were not allowed to judge the righteousness of the laws and regulations, because that is exactly what happens in Germany with the decisions from the Bundesverfassungsgericht!

II.2 The European Market Infrastructure Regulation (EMIR)

The European Market Infrastructure Regulation (EMIR) on the other hand is a European Union regulation designed to increase the stability of the over-the-counter (OTC) derivative markets throughout the EU states. It is designated Regulation (EU) 648/2012, and it entered into force on 16 August 2012.³⁸

Derivatives play an important role in the economy but are associated with certain risks. However a lot of enterprises and multinationals use this tool to finance the subsequent production phases.

The crisis has highlighted that these risks are not sufficiently mitigated in the over-the-counter (OTC) part of the market, especially as regards credit default swaps (CDS). Since the beginning of the financial crisis, the Commission has been working to address these risks.

On 19 December 2012, the European Commission has adopted nine regulatory and implementing technical standards to complement the obligations defined under the Regulation on OTC derivatives, central counterparties (CCPs) and trade. They were developed by the European Supervisory Authorities and have been endorsed by the European Commission without modification.

The adoption of these technical standards finalizes requirements for the mandatory clearing and reporting of transactions, in line with the EU's G20 commitment made in Pittsburgh in September 2009.

There are more points to consider.

Grosso modo those two laws are not so different from each other. In fact they have the same aim: protect the consumer, but do they achieve this aim?

The fact that via the Dodd-Frank Act so much power, unlimited power has been given to CFPB and the FSOC, is unforgivable, but understandable. Given the circumstances and the gravity of the Financial Crisis, the regulation was an understandable reaction. Von Mises assumed, that people can and will act in a responsible way and I wish I could agree with that.

Somehow the possibility should be created to mitigate these acts and allow more freedom. Accountability and responsibility are all good features and should be allowed to be exerted by the bankers and traders. Taking away this possibility is in the end not a good thing.

II.3 The European Legislation.

Connected to the above discussed themes the European regulation should be considered. Indeed, legislation concerning Europe should be transparent and understandable. *Like James Madison said: “A law is bad not only when it is unconstitutional, but also when it is so voluminous that it can not be read; so*

³⁸ en.wikipedia.org/wiki/European_Market_Infrastructure_Regulation#cite_note-1

*incoherent that it cannot be understood*³⁹ *Not only the Treaty of Lisbon is an example of bad legislation, but a more important element is missing: the Trias Politica Rule.* The separation of powers does not exist in Brussels: the Commission exerted until now the legislative power and the executive power in one. The European parliament has now more (legislative) power than before.

Edmund Stoiber, who presided “The High Level Group on Administrative Burdens” said the following during a conference in Brussels on June 25, 2014 “Cutting Red Tape in Europe- Vision and Results”: “There have been attempts to promote “Deregulation”, Better Regulation”, but I propose to introduce “Smart Regulation”(intelligente Gesetzgebung”).

In a newspaper article about Stoibers work on Red Tape⁴⁰, it has been explained that the Group examined 74 legal documents, 300 proposals for improvements and has saved the EU a 50 million € for the “Zentralverband des Deutschen Handwerks”.

In the same article a range of absurd regulation has been explained.

Together with all these regulations, the Euro-skepticism has increased as has been shown in the European elections.

III The new role of Europe’s Leaders and the shift of power.

Verdrossenheit, Krisen Lethargie/Fretfulness, dissatisfaction: Europe should serve the European Citizen.

In this context the word “Verdrossenheit” has been used, because it describes so well the mentality that has started to prevail in Germany and also in parts of Brussels. The enthusiasm for Europe is gone, because most people do not want to chase the chimera: “an ever closer Union”.⁴¹

It is not difficult to find arguments against “Europe”. The greatest reproach is, that there is a huge bureaucracy and that the Eurocrats live in an “ivory tower” and do not want to listen to the arguments and reproaches of the “normal/average” citizen, because that would equal Populism.

For Inigo Errejón of Podemos, *la casta* and “Brussels” have reached a union against the people, against the nations.⁴²

On conferences in Brussels everybody agrees with everybody. A dissident opinion was unthinkable until recently and it was not listened to, ignored or worse: ridiculed.

For example in the UK the situation is the following. “Studies of voters show that they are drawn to UKIP (and other Euro-skeptic parties), not only because of dissatisfaction with the mainstream parties, but because of a general disillusionment with the political establishment. Based on the experiences of other European countries, these voters appear unlikely to return to supporting

³⁹ Rep. Scott Garrett quoting James Madison in Cato Policy Report Sept/Oct. 2013, p. 11

⁴⁰ “Sein Vermächtnis” Matthias Krupa in “Die Zeit”, dd May 8, 2014, p. 30

⁴¹ As Jochen Bittner says in “Die Zeit”: “Wenn Europa eines nicht mehr braucht, dann sind es die Verfechter einer ever closer union, die sich gegenseitig mit Karlspreisen behängenden Integrationisten”. Die Zeit 5 Juni, 2014 p. 1

⁴² Gero von Randow “Hunderte gehen in Europa auf die Strassen, um gegen den Euro zu protestieren, gegen Brüssel oder Angela Merkel. Hat diese linke Bewegung eine eigene Theorie? Wer sind die Vordenker? Und warum paktieren die Empörten sogar mit rechten Populisten?” in “Die Zeit”, dd 26 March 2015, p. 5.

the traditionally dominant Conservative and Labor parties in the foreseeable future.

About half of the voters of right-wing populist parties in Western Europe are former supporters of mainstream centre-right parties who grew disillusioned with their purportedly pro-European and liberal policies. Trying to counter this trend, the French and Dutch conservative parties have adopted substantial parts of the populists' agenda regarding the EU and immigration⁴³.

Now that David Cameron is re-elected as prime minister, he will try to renegotiate Britain's status within the EU and could put the issue up for a national referendum. However, major European powers such as Germany and France appear unwilling to renegotiate the fundamental basics of the European treaties.

That would be an argument more to be against the Eurocrats and an argument more to bring about, that those civil servants should change their opinions.

In case some countries would leave the EU, the rest will continue to persecute their goal in a rapid speed, like travelling in a TGV; and that goal is: "an ever closer Union".

That vision and ideal will continue to recede like a mirage. This ideal will never suffice and it will never be reached. *The most urgent question will be: Who is deciding, when there is enough Europe?* "More Europe" means for most of the European citizens more regulation, more centralization. Indeed, the last time has shown a shift of power from the national level to the European level,

These questions were very urgent in the past elections in 2014, because they not only concern the election of the new European Parliament, but also of the President of the European Commission and the position of the President of the European Council and of the High Representative for the EU on Foreign Issues, formerly Lady Ashton, now Federica Mogherini.

The President of the Commission:

As mentioned before there has been a shift of power and emphasis of national influence to a European level. Instead of former Prime Ministers, who had their day, the national governments send now heavy weights to "Europe".

There were several candidates for the function of the president of the European Commission: Jean-Claude Juncker for the EPP-ED Group, Guy Verhofstadt for ALDE, Martin Schulz for the Social Democrats, Alexis Tsipras for the "Left Parties and José Bové and Franziska Keller for the Greens.

In the end it was Juncker, who won.

In "Die Zeit" several candidates have been judged. One conclusion was, that if we look more precisely, then the candidature of Junckers was absolutely not unavoidable, because Juncker represents the past, not the future.

On the contrary, he even seemed backward-looking, like a quotation dating back from a time, when Europe was still manageable and Europe still a promise.

⁴³ Timo Lochocki "Three reasons why UKIP matters" edited by the German Marshall Fund dd 5-5-2015. (consequently right before the elections in the UK)

Juncker was considered unequivocally the wrong person to lead the EU in the upcoming years. There are the following items to consider.

“The Union has grown in the last decades and is more focused on the East, the money has become scarce and dealing with each other has become more direct. More important: the doubt has increased that the Integration, such as “the old ones” have operated, would be irreversible”⁴⁴. The person who has taken over the responsibility in the EU, will have to live with these vibrations. He must be prepared and willing to question some certainties. Juncker has to convey what he wants to do in the upcoming years and how he sees Europe in the future. Now that Juncker has presented his team, it looks like he did understand the criticism of the past. The last chance to convince the European citizens, that “Brussels” hears their criticism and anxieties and that it has more to offer than some superfluous rules, like to decree how much time coffee can be kept in a thermos flask.⁴⁵

The President of the European Parliament.

Schultz has said some true things, like: “Instead of taking care of the really important topics, the EU takes care of showerheads and olive oil jugs. We should stop to irritate the people. We will have to put the whole EU upside down”⁴⁶. “Reform instead of renationalization” he says.

The President of the European Council, now Donald Tusk, seems to be a right choice.

The High Representative for the EU on Foreign Issues, formerly Lady Ashton, now Federica Mogherini is - according to *Die Zeit*- “an Italian without any experience”⁴⁷. Indeed she invited Putin for a conference at the height of the Ukrainian crisis. Her point of view is, that the EU is a project of peace. Certainly, but the EU has grown in importance and in such a situation other rules prevail. The choice of Ms. Mogherini as the successor of Lady Ashton is a disastrous decision. She is inexperienced and naive.

The President of the European Central Bank. His name has been added, because Draghi has managed to make his position a most important one, although he has not been elected. His decisions, like the lowering of the interest rate, influence European politics in a far reaching way⁴⁸. Since a few years, Mario Draghi is the **fifth** power in Europe.

All those politicians are pro-Europe of course. The most important criterion for the future leaders is to act in the interest of the European citizens, because all those politicians speak about the “project Europe” and not about the European citizen. I think that that is exactly the point: instead of aiming at an “ever closer Union”, try to reach EU citizens and show them the advantages again of the EU, of being a part of it.

⁴⁴ Mathias Krupa in *Die Zeit* “Der Mann der zu viel weiss”, February 13, 2014 p. 8

⁴⁵ Mathias Krupa in “*Die Zeit*”, “Juncker will stürmen” September 18, 2014 p. 12

⁴⁶ Mathias Krupa in “*Die Zeit*” “Mister Europa?”, February 20, 2014, p. 9

Rep. Scott Garrett quoting James Madison in *Cato Policy Report* Sept/Oct. 2013, p. 11

⁴⁷ *Die Zeit* “Europa ist nicht im Krieg. Im Frieden aber auch nicht”, dd September 11, 2014 P. 3

⁴⁸ *Die Zeit* “Mario Tragisch”, dd September 18, 2014, p. 24

The Eurocrats often dream of a kind of a “patriotism à l’ Américaine”, but we will never have that, because the immigrants who went to the United States, left their country and their family behind them because of various reasons and needed new patriotism, while in Europe the citizens stay (mostly) in their own country.

The most important aspect is, that the individual citizen should be in the center, not the European ideal. The citizen can never be sacrificed to that ideal. The results we have seen in the Soviet period. Europe is there for the citizens, not the citizen for Europe. That should be the leading thought during the next years.

IV Europe’s citizens

The last decade the big fear of almost all the established parties, was euro-skepticism. All those mainstream political parties, like the Christian Democrats, want more Europe, the Social-Democrats want even more Europe and the Greens want more, more Europe. That asks for reactions. People feel the influence of Europe’s regulations in their daily life and feel that they have no participation in the discussion.

Several questions can be posed.

► The **first** question is of course: do we need “more Europe?” What are the implications? According to the Euro-crats, more centralization of course, never decentralization. Also indirect democracy, never direct democracy, because that would result in euro-skepticism. If for example there is decentralization cq. subsidiarity, if we do not try to impose the same rules to everyone then there is more flexibility. Then for example Turkey could fit in to the European concept. Of course they would have to fulfill the required criteria, but there would be more freedom of interpretation. Not like the rules that are set now by the European Commission on insignificant daily things⁴⁹. On the contrary, if the European leaders want to impose uniform rules everywhere in Europe, it will not be feasible.

Federalism or co-federalism, nation states or a European superpower? These questions are still not replied to. The politicians who want more Europe, aim at centralization and that is different from integration, because in the latter case the participant/citizen can decide on his own tempo. It is also a fact, that one can not speak of a global centralization or decentralization. There will be centralization in some parts and decentralization in other regions.

The political union desired by the Euro-crats is a vision of a future form of Europe. To be more precise, such a vision is for countries, who want to impose themselves this aim. The view that this union could be the tool to solve the actual crisis of the Euro-zone, lacks every logic⁵⁰. It is even dangerous.

► The **second** question is: “what kind of Europe do we want? *Grosso modo*: a socialist Europe or a free market one? This will be the galling issue for years to come. Until now a kind of balance has been reached between the two extreme political views, but it will never be solved for good. There are propositions, not even from Euro-skeptics: “It is time to check the relation between the base and the Institutions on their liberal durability. Instead of occupy themselves with the

⁴⁹ Die Zeit “Sein Vermächtnis”, May 8, 2014, p. 30 “Von der Schnullerkettennorm (52 pages) or Feuerzeug verordnung”

⁵⁰ Die Zeit “Jeder Muss Sich Selbst Helfen”, Otmar Issing, August, 2012, p. 23

structural reforms on the labor market of separate countries and compare them with the Lisbon Treaty, the legislative competence should be given back to the national capitals. Because flexibility creates more competition and nobody ever complained about that.”⁵¹

► The **third** question is: It is not possible to ignore the Euro-Skeptic parties anymore⁵², because of the elections, but that is not such a bad thing, because all those established political parties should have a kind of opposition. These Euro-Skeptic parties could act as a counter weight against those, who enforce the rules and globalization from “Europe”.

Of course those parties do all have non -admissible ideas.

The **AfD** looked quite reasonable in his demand to change the Euro-saving politics, but turns out to be pro-Russian and pro -Putin. Frauke Petry insisted on a politics not based on sanctions, but on constructive negotiations with Russia. This party offers shelter to people who consider news from “Russia Today” as objective news, while they think that “Die Tagesschau” is part of a western conspiracy.⁵³

NV-A is not anti-Europe, but they want to split Belgium. Now that they are part of the ECR, they might start to think differently.

The party of **Wilders, the PVV and of Marine le Pen, Front National** are anti-immigrant and xenophobe.

Nigel Farage has not been taken seriously either, but did gain a lot of votes before the recent elections in the UK.

Alas, so the reality is more complex than it looks at first sight. It is equally possible, that because there was no room for criticism and euro-skeptics were not listened to, the euro-skeptics became sharper in their critique.

After all, every institution fares better when it listens to constructive criticism. For example, most **British** think that they are not euro-skeptic, but on the contrary good Europeans because they are skeptical.⁵⁴. In fact the British want to change the EU and its laws and treaties. They are the real (and realistic) opposition.

Conclusion

I. The fact that banks are going to be audited is a good thing, but to use the Banking Union as a political instrument to achieve **an “ever closer Union”, is very wrong.**

Also the interest policy of Draghi is a very dangerous instrument. Von Mises was right to oppose to the continuing manipulation of the interest rate and to warn against the credit expansion, practiced in his days as well. Also his interpretation of free banking is a right and surprising one.

⁵¹ Die Zeit “Ein Pfund für Europa”, John F. Jungclaussen, June 18, 2014, p. 22

⁵² Die Zeit “Europa braucht Schonung”, October 24, 2013, p. 3

⁵³ Die Zeit “Putin spaltet die AfD”, dd 28 August, 2014, p. 8

⁵⁴ Die Zeit “Schön gestört”, Jochen Bittner, June 5, p. 1

The most pressing question is however: did we need all those new regulations?

II. The role of the European leaders should be changed and put more under the control of a really democratic Institute. Perhaps the European parliament?

It is a fact, that (until now)

- ▶ the European Commissioners are not elected at all, not directly, nor indirectly.
- ▶ The MEP's are not accountable and in my view, the rotating presidency should be abolished due to the fact that we now have Donald Tusk as the "President of the European Council" and Federica Mogherini as the High Representative for the EU on Foreign Issues.
- ▶ Also Viviane Reding said in her interview with "Die Zeit", that it would be palatable if people want to join the discussion and want to take part in the decisions.
- ▶ According to "Die Zeit" this contrasts how these diverse opinions cannot be solved by an intensified and accelerated Europeanization in the "Brussels way". Europe needs to be spared in the next future. Get a healing sleep, get used to the new rules, to the new reality.

The new reality is at the moment that there is a strong Germany, a centralized, overregulated France with a weak President (and an overprotected labor market) and an opposition, who makes clear, that Brussels/Europe cannot act without the consent of the common citizen.

Here the question should be: what are we going to do about the changed opinion towards the European Leaders?

111 How should the structure of Europe look like?

Federalism or co-federalism. The principle of subsidiarity, mentioned in the Lisbon Treaty, should be the future instrument.

The whole legal structure of Europe should be changed and scrutinized.

In an interview with Stefanie Weiss, Charles Grant⁵⁵ stated the following⁵⁶.

"Germany will also, of course, play a crucial role in helping the British to stay in the EU, Merkel will be the dominant figure in any UK renegotiation.

What if anything can the EU do to help the British in the run-up to their referendum on EU membership?

Some countries in the EU are fairly relaxed about the possibility of Brexit – notably Spain, France and Austria, to name just a few. My line would be that Brexit would have very serious consequences for the EU: the prevailing economic philosophy would be less liberal; the foreign and defence policy would be less serious; the EU-US relationship would be weakened; and Germany would be left even more exposed as Europe's hegemon. So Germany, which sees these potential problems, should encourage other countries to be helpful to the British. That does not mean sacrificing key principles like free movement. It does mean listening carefully to British ideas, when they are sensible, as some of them are (at least in the views of several EU governments), e.g. on safeguards for the single

⁵⁵ Charles Grant is director of the Centre for European Reform

⁵⁶ N°4 – May 2015 "Listen carefully to the British", an interview of Charles Grant by Stefanie Weiss, the Bertelsmann Stiftung p. 3

market vis-à-vis the eurozone, or on enhancing the role of national parliaments in policing subsidiarity. Cameron needs a deal that he can present to the British people as showing that something has changed in the EU, for the better”.

IV The role of the European citizen should be taken seriously and enlarged.

The most important aspect is, that the individual citizen should be in the center, not the European ideal. The citizen can never be sacrificed to that ideal. The results we have seen in the Soviet period. **Europe is there for the citizens, not the citizen for Europe.** That should be the leading thought during the next years. With the upcoming referenda in the UK and even in Germany and a Bundesverfassungsgericht, that has already indicated that future changes of the European contracts should be limited- we can expect a very interesting time to come!