‘This must never happen again.’ That is the typical reaction of policy-makers and the general public to the global and euro area crises. Yet there has been ample previous experience with financial crises in advanced and emerging market economies. How is it that the lessons were not learned, and that many economies – supposedly the most sophisticated – have been saddled with a rise in public debts that is unprecedented in peace-time?

The origins of the crisis lay in mistakes on a grand scale that embraced monetary, fiscal, and regulatory policy. Policy-makers were ‘captured’ not just by industry interests but by ideas – including an exaggerated faith in unfettered markets. Political, economic, and technological influences played a major role. The challenge in the wake of the crisis is to explore how reformed institutional structures can help underpin more sustainable growth – and prevent similar cycles in the future.

The PEFM programme was created to fill a gap by approaching these issues with a multi-disciplinary approach, and by bringing together researchers from academia, private institutions and government. The aim is to understand better the role of financial markets in society, to promote discussion, and ultimately to foster better policies.

Max Watson

Main goals and activities of the programme

The Political Economy of Financial Markets programme (PEFM) aims to shed light on the way in which institutions, including macroeconomic policy frameworks, interact with financial markets. In the wake of the global and euro area crises, it seeks to promote a better understanding of financial markets and to contribute to improved policy formulation in the future.

Its main activities are to carry out research, hold seminars, and publish findings in outlets that range from academic articles and books to policy briefings and op-ed pieces in the international press. Three initial research groups were set up at the outset, bringing together academics, officials and market participants:

- The first research topic is Financial Integration in Europe – why this has not lived up to expectations, and the implications for banking and fiscal union.
- The second research topic is Regulatory Capture. This explores how relations between the financial sector and regulators interacted with political and ideological influences in the ‘regulatory space’, during the run-up to the crisis.
- The third research topic is Macroeconomic Policies and Financial Stability – asking how monetary and fiscal policy regimes can respond to instability in the private sector, without jeopardizing policy transparency.
- Several future research priorities have been identified. These include shadow banking; macroprudential measures; and the impact of advanced economy policies on emerging markets.

Mission

Through a network of academic, official and private market experts, we aim to foster research into the political-economic drivers of changes in financial markets, in light of the global and euro area financial crises.

The programme focuses in particular on issues situated at the intersection of macroeconomics and financial studies, and it is concerned with the institutional setting in which policy towards financial markets is formed at the national and European levels.
The work of PEFM is overseen by an Academic Steering Committee whose members are Christopher Adam, Professor of Development Economics; Othon Anastasakis, Director of the European Studies Centre; Kalypso Nicolaïdis, Professor of International Relations; David Vines, Professor of Economics; and Max Watson, Director of PEFM.

Christopher Adam

Christopher Adam is Professor of Development Economics and a Fellow of St Cross College, Oxford. He is a Visiting Professor at CERDI, at the Université d’Auvergne, Clermont-Ferrand. From 2003-05 he served as External Macroeconomic Adviser to the Policy Division at DFID, and he continues to represent DFID as Vice-Chair of the African Economic Research Consortium. He is co-editor of the Oxford Bulletin of Economics and Statistics, and the Oxford Review of Economic Policy. He is a member of the editorial boards of Oxford Economic Papers and of Oxford Development Studies. His current research addresses three main themes: the macroeconomics of Africa; growth and structural change in low-income countries; and the political economy of aid. In 2011 he was appointed Special Advisor to the Inquiry into Aid Effectiveness of the House of Lords Economic Affairs Committee.

Othon Anastasakis

Othon Anastasakis is Director of the European Studies Centre, Director of South East European Studies at Oxford (SEESOX), and a Fellow at St Antony’s College, Oxford. He teaches South East European politics. Previously he was Researcher at LSE, and Advisor on EU matters at the Greek Ministry of Foreign Affairs. His recent books include ‘From crisis to recovery: Sustainable growth in South East Europe’ (co-edited with Jens Bastian and Max Watson, SEESOX 2011), ‘In the Shadow of Europe: Greeks and Turks in the era of post-nationalism’ (co-edited with Kalypso Nicolaïdis and Kerem Oktem, Brill, 2009), and ‘Greece in the Balkans: Memory, conflict and exchange’ (co-edited with Dimitar Bechev and Nicholas Vrousalis, Cambridge Scholars Press, 2009). He has published many articles on comparative democratization in South East Europe, EU-Balkan relations and EU conditionality. He is General Editor of the Palgrave Macmillan-St Antony’s College series.

Kalypso Nicolaïdis

Kalypso Nicolaïdis is Professor of International Relations, Chair of South East European Studies at Oxford (SEESOX), and a Fellow of St Antony’s College, Oxford. During 2012-13 she is Straus Fellow and Jean Monnet Fellow at the Law School, New York University. She is Chair of the Global Trade Ethics project and a Member of the ECFR Council. During 2008-10 she was a member of the ‘Reflection Group on the Future of Europe’ set up by the European Council and chaired by Felipe Gonzalez. She teaches theory of international relations, European integration, international political economy, negotiation, game theory and research methods. She is a founding member of the Spinelli Group. Her recent publications include ‘European Stories: Intellectual Debates on Europe in National Context’ (co-edited with Justine Lacroix), and ‘The Idea of European Democracy’, in Philosophical Foundations of European Union Law (edited by Julie Dickson and Pavlos Eleftheriadis).

David Vines

David Vines is a Professor of Economics at the University of Oxford and a Fellow of Balliol College. He is Director of the Centre for International Macroeconomics at Oxford. He is also an Adjunct Professor in the Centre for Applied Macroeconomic Analysis at the Australian National University; a Research Fellow of the Centre for Economic Policy Research in London; and Scientific Coordinator of the European Union Framework Seven PEGGED Research Programme on ‘The Politics and Economics of Global Governance: the European Dimension’. From 1994 to 2000 he was Director of the Research Programme on Global Economic Institutions of the Economic and Social Research Council. He is a trustee of the Oxford Policy Institute. He formerly held the Adam Smith Chair of Political Economy at the University of Glasgow. He acts as Advisor to Fair Observer, an online magazine covering global issues from a plurality of perspectives, on all economic matters. He has published numerous academic articles in the fields of macroeconomics and of economic governance.
Development priorities

The initial activities of the PEFM programme have been funded by a grant from the Financial Market Policies Foundation. This has allowed the establishment of an office for the programme at the European Studies Centre at St Antony’s College, Oxford. It has also covered the costs of workshops and other key activities for a period of two years, with a plan to extend this to three years. On this basis the programme has created a research network, and has initiated a series of research projects, workshops, seminars, and publications.

There are several directions in which it is planned to expand activities as further funding is identified:

- The programme currently has no funding for full-time research positions at the European Studies Centre, such as research fellows or post-doctoral research associates. Creation of such positions would greatly strengthen the programme’s capacity to pursue research issues that require in-depth study over an extended period.

- The committed and anticipated funding is projected to cover three years of core operations. The goal, however, is to extend the programme to five years, and ultimately to make it a permanent programme.

- As research papers are completed, there are plans to bring a number of these together in an edited volume on ‘The political economy of financial markets’. The preparation of major publications, however, depends on adequate additional funding.

- The longer-run goal is to secure endowment funding to provide a permanent footing for the programme, and for researchers based at the European Studies Centre.

The programme is embarking on a fundraising effort to support these goals, and in doing so will work closely with the development office at St Antony’s College.

The Financial Market Policies Foundation

Core funding for the programme has been assured by a grant from the Financial Market Policies Foundation (www.fmpf.org). The Foundation supports and publishes academic research into the role and impact of financial markets in contemporary and historical society; the relations between governments and financial markets; and their impact on the public good. The Foundation seeks where possible to place the results of such work in the public domain through journals, seminars, presentations and the internet. The Foundation and its programmes are supported by advisors who are academically or professionally eminent in their own fields internationally. The Foundation was incorporated in January 2012, and is registered as a charity in England and Wales.

Programme Director

Max Watson is a Visiting Fellow at St Antony’s College, Oxford, and Director of the Political Economy of Financial Markets programme. He also co-ordinates political economy work on South East Europe under the SEESOX programme. He was until recently a director of the Central Bank of Ireland, and research director at the consultancy John Howell & Co Ltd. His career began in the Bank of England, where he was a manager in banking supervision and adviser on international affairs. He was then chief of the IMF’s International Capital Markets Division; a mission chief to countries in emerging Europe and the euro area; and later a Deputy Director of the Fund. He spent five years at the European Commission, as adviser to the Director-General of Economic and Financial Affairs. He is also a fellow of Wolfson College, Oxford, and a Trustee of the Foundation for Law, Justice and Society.
People at PEFM

Adam Bennett

Adam Bennett is a Senior Associate Member of St Antony’s College, and also an external lecturer at Cardiff University. He worked for 24 years at the IMF, until 2011. He was Senior Advisor (Deputy Director grade) in the IMF’s European Department in 2009-11, with responsibility for the Western Balkans, as well as mission chief for Italy. Before that, he was Senior Advisor in the Middle East Department. During the second half of the 1990s he was chief of the IMF’s Stand-by Operations division. In his early career, he worked for the UK Treasury and for two investment banks. His published work has ranged over macroeconomics, monetary economics and post-conflict economics. He is a past member of the editorial board of the journal of Economic Modelling. Bennett was educated at Cambridge University and the London School of Economics.

Gillian Edgeworth

Gillian Edgeworth, a senior member of St Antony’s College, is Chief European Emerging Market Economist at Unicredit Bank. She joined the bank in 2010 and is responsible for economic analysis of regional economies ranging from Turkey, Russia, Poland, Ukraine and Hungary to smaller countries such as Latvia, Kazakhstan and Serbia, as well as recent EMU entrants such as Estonia and Slovakia. She also covers developments in Ireland and Greece. Prior to joining Unicredit, she spent 8 years as a member of the economics team at Deutsche Bank, responsible for coverage of Poland, Hungary, Czech Republic, Slovakia, the Baltics, Greece and Ireland.

Stewart Fleming

Stewart Fleming, a senior member of St Antony’s College, is a journalist and writer on international economics. In the 1970s and 1980s he was Financial Times Bureau Chief in New York and Frankfurt. He was then FT economics correspondent in the USA, and its US Editor. In 2003-2008 he lived in Brussels, writing a column on international economics for European Voice, the Economist Group’s Brussels weekly. His recent publications include “Europe, China and the Group of Twenty” (in “China, the EU and Global Governance”, Edward Elgar, 2012).

Gene Frieda

Gene Frieda, a senior member of St Antony’s College, has served as a senior global strategist for Moore Capital since May 2007, focusing on global macro policy issues. Previously, he was Global Head of Emerging Markets Research and Strategy and a proprietary trader at RBS between 2002 and 2007. Between 1995 and 2002, Mr. Frieda ran Global Emerging Markets research, Asian research and Latin American research for IDEAGlobal and 4Cast from bases in New York, London and Singapore. Mr. Frieda earned his M.Sc. in Economics from the LSE, and holds B.A. degrees in Political Science and Economics from the University of Oklahoma.
Valerie Herzberg

Valerie Herzberg, a senior member of St Antony’s College, is a member of the Cabinet of Herman van Rompuy, President of the European Council. Her focus is on economic questions, including notably the eurozone. Previously, she worked in the IMF’s European Department; at the European Commission; the European Investment Bank; the National Bank of Belgium; and the Bank of England. Her experience includes work on monetary policy and financial stability issues in emerging and advanced economies. A German national, she holds an MSc in Economics from the LSE.

Russell Kincaid

Russell Kincaid, a Senior Associate Member of St Antony’s College for 2013-14, was until recently a Director at the IMF, where his responsibilities included risk management, control, and governance processes, and the secretariat for the risk management committee. Earlier, he held senior positions in the Strategy, Policy and Review Department and the Secretary’s Department. He has published on macroeconomic and financial policies, exchange rates, sovereign debt, and financial markets. He has been on the Editorial Board of IMF Staff Papers, taught at Columbia University, and was a visiting fellow at the European Commission. Mr Kincaid graduated from UCLA and holds a Ph.D. from Columbia University.

Thomas Mayer

Thomas Mayer, a senior member of St Antony’s College, is Senior Fellow at the Center of Financial Studies of Frankfurt University and Senior Advisor to Deutsche Bank. Before that, he was Chief Economist at Deutsche Bank, and earlier held positions at Goldman Sachs, Salomon Brothers and the International Monetary Fund. His latest book on the euro “Europe’s Unfinished Currency” won praise from central bankers and senior policy makers. His PhD is from the University of Kiel.

Julie Adams

Julie Adams joined PEFM in 2012, and has been administrator of South East European Studies at Oxford (SEESOX) since 2004. As well as dealing with all the administrative matters, and organising events, Julie also designs and creates promotional material for PEFM and SEESOX, such as brochures, newsletters etc. Julie is also responsible for editing the PEFM and SEESOX websites. A qualified English language teacher, Julie previously ran her own business providing English language courses throughout England to students sponsored by the Spanish government. She lived in Greece for seven years where she taught English. She speaks Greek fluently.
Current research projects

Financial integration in the Euro Area

This research group, led by Gillian Edgeworth and Gene Frieda, has been exploring the pattern of capital flows in the euro area and neighbouring countries during the run-up to the crisis. Flows to euro area countries that later experienced financial stress were dominated by portfolio and other debt-creating flows, with Foreign Direct Investment (FDI) being a net negative item in these years. It seems these flows tended to increase financial vulnerability, and did not strongly serve to enhance debt-servicing capacity. The pattern in emerging Europe was somewhat different, with FDI accounting for around half of net inflows; but, outside Central Europe and Turkey, a substantial proportion of these flows appears to have been destined for the non-traded goods sector. The research suggests that several drivers of these flows – including the adjustment process of economies within the euro area – were not exceptional, and may recur. ‘Rebooting EMU’ thus requires stronger fiscal backstops than currently envisaged. The preliminary report was presented at a joint regional seminar hosted with SEESOX and the Central Bank of Bosnia and Herzegovina.

From regulatory capture to regulatory space

This project, led by Max Watson, was inspired by suggestions that banks ‘captured’ regulators before the crisis. A Policy Brief explores how various influences triggered changes in regulatory philosophy and practice. It confirms earlier findings that the notion of ‘binary’ capture of an agency by an industry is too simple a framework. (www.sant.ox.ac.uk/pefm/publications.html)

The run-up to the crisis in fact saw complex interactions in the ‘regulatory space’ between influences that included changes in ideas; shifts in the power of interest groups; and political, economic and technological changes. These influences had a mutually-reinforcing impact, favouring deregulation and a greater dependency on private sector risk assessment techniques. An exaggerated faith in efficient markets and rational expectations contributed to the crisis not only by supporting less intrusive regulation but also by laying an intellectual basis for macro policy regimes that largely ignored private sector imbalances. This work benefited greatly from a workshop hosted by the Foundation for Law, Justice and Society. (www.fljs.org)

Macroeconomic policies and financial stability

Several studies are being prepared in this work-stream, including a reassessment of monetary policy – ‘The Power of Credit’ – by Michael Biggs and Thomas Mayer, an analysis of ‘Fiscal Policy under EMU’ by David Vines and Max Watson; and ‘Macroprudential Markets and Policy Coordination’ by Russell Kincaid and Max Watson.

Further research is planned on the role of macroprudential instruments, with Valerie Herzberg, Gillian Edgeworth and Russell Kincaid being among the contributors.

There is a particular focus on the role of national policies under EMU. Preliminary work was discussed at the PEFM macro workshop in mid-May, and publication of discussion drafts will follow. Follow-ups to this work will focus on the spillovers of advanced economy financial policies to emerging markets in Europe.
Larger countries avoided commitments to co-ordination, and with France and the USA significantly undervalued this was a fatal weakness of the system.

David Vines discussed the difficulties that even Keynes experienced in trying to understand the nature of the economic problem in the 1930s, which went far beyond reparations, and the kind of policy recipes that might be promising. The problem was one of restoring simultaneously external and internal balance to economies. The inadequate global supply of reserves was acting as a constraint on the system; wages were downwardly rigid in countries such as the UK, which had fixed exchange rates and were overvalued; and surplus countries (such as France) were not expanding demand in a way that would facilitate adjustment by deficit economies. He saw direct lessons for euro area policy-makers today. The burden of adjustment is falling on deficit economies, which have downwardly rigid wages and locked exchange rates; and there is a shortage of aggregate demand.

The launch of PEFM took place on 28th November 2012. Patricia Clavin, Professor of International History and Fellow of Jesus College, and David Vines, Professor of Economics and Fellow of Balliol College gave a seminar on issues in the 1920s and 1930s that seem most relevant today. A podcast of the seminar event will be found on the PEFM website www.sant.ox.ac.uk/pefm.

Patricia Clavin noted that governments raised social expectations during the First World War, but were unable to satisfy these in the Peace. Reconstruction without aid led to inflation, and thence to a revival of the Gold Standard. Seeking to meet commitments, states saw a rise in economic nationalism (not just among extremist parties) and a ‘permanent condition of quasi-emergency’. Trade controls proliferated. States became obsessed with population policies. The first IMF-style programme – with fiscal monitoring, phased disbursements, a resident representative – was put in place in Austria in 1922; successful financially, it was deeply resented politically. This became a model for Hungary, Greece, and Bulgaria.
The European Studies Centre

The European Studies Centre is dedicated to the interdisciplinary study of Europe. It has particular strengths in politics, political economy, history and international relations, and also brings together sociologists, social anthropologists and students of culture. The Centre is a meeting place and intellectual laboratory for the whole community of those interested in European Studies at Oxford. Beside its permanent Fellows, the Centre has Visiting Fellows from several European countries, as well as graduate students from around the world working on European affairs. The Centre also participates in several collaborative international research projects. Seminars and workshops on a wide range of topics are held regularly at the Centre. These involve Oxford scholars from all disciplines and their counterparts from abroad, often with the participation of students. A number of special lectures and international conferences, bringing both leading academics and distinguished practitioners to Oxford, are offered to a wider audience under the auspices of the Centre.

Co-operation with other programmes

Through its Academic Steering Committee and other channels, PEFM is committed to developing strong and productive links with other programmes at Oxford, at other UK universities, and abroad. It is hosting joint activities on emerging Europe with South East European Studies at Oxford (SEESOX). It has plans to hold seminars jointly with the Global Economic Governance programme at University College, Oxford, and with the International Economics Programme at Chatham House.

Publications

PEFM publications, powerpoint presentations, and podcasts are posted on the programme website (www.sant.ox.ac.uk/pefm). Recent items posted there include the podcast of the PEFM launch seminar; a discussion draft on political and economic sources of the financial crisis; and a policy brief on ‘Regulatory Capture’.

Colleagues and guests at the PEFM launch event on 28 November, 2012.