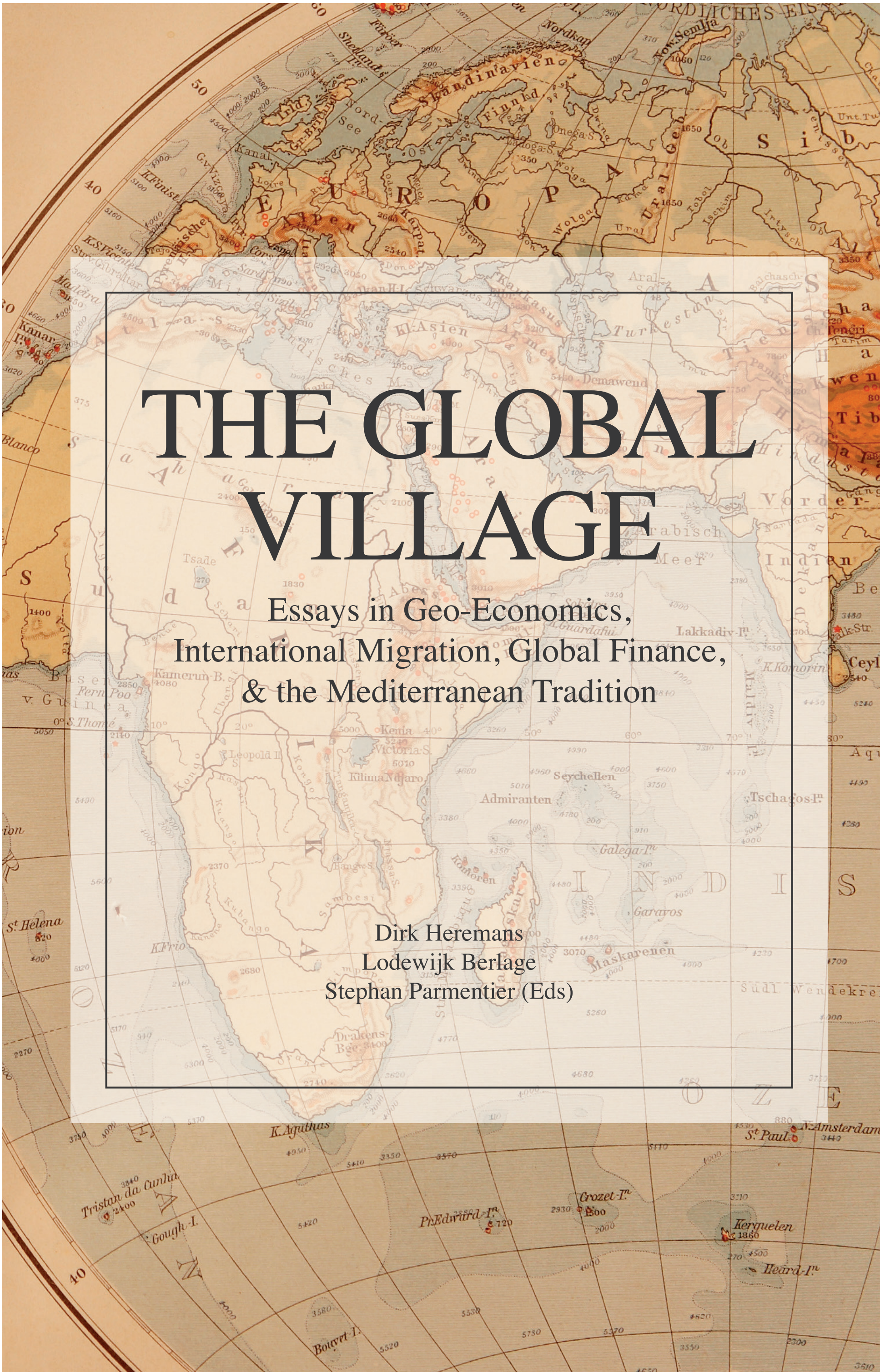

THE GLOBAL VILLAGE

Essays in Geo-Economics, International Migration, Global Finance, & the Mediterranean Tradition

Dirk Heremans
Lodewijk Berlage
Stephan Parmentier (Eds)

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Preface

The elite proclaims ‘the world is our village’. But many citizens are anxious and reply ‘our village is our world’. It refers to the trilemma that, according to Rodrik, nation states face in the globalised world: they have to make a choice between participation in globalisation, retention of national sovereignty, and the political model of participatory democracy.

Still, globalisation appears to be an irreversible phenomenon. How then to keep the tension between internationalism and nationalism manageable in Western democracies?

These tensions show up in many events and challenges, just to mention a few: on-going turmoil in the Islamic world, explosive African demography and massive migration, the aftermath of the worldwide financial crisis, a tsunami of changes in geo-economics and politics etc.

The evolving changes worldwide cannot merely be analysed as being determined only by economic and political factors, but are to be interpreted from various angles. They are also stimulated by ideological doctrines and cultural backgrounds. Is an inclusive global approach and interdisciplinary analysis not needed for a better understanding?

Moreover in order to better grasp the on-going dynamics in the world one should never lose sight of the historical dimension. Much can be learned by looking back into earlier, often critical insights on the above challenges and by confronting them with contemporary views.

Finally, the present anxiety in public opinion on these matters is increasingly a matter of (mis)perception in the present information era. Does it not underline the need to make specialized academic insights and expert opinions widely available to larger audiences by simplified and better accessible publications?

Louis Baeck Cycle of Colloquia

Following up on the previous concerns and the need to approach the global world issues from various angles, the University Foundation in Brussels – which serves as the meeting place and network for academics from various disciplines and the different Belgian universities – launched in 2018 a cycle of colloquia on the occasion of its 100 years anniversary. The Foundation was thereby inspired by the monumental work started 50 years ago by its former Executive Director Professor Louis Baeck in the area of the 'world village' as he coined it. As an economist, he did not refrain from questioning dogmas of mainstream economic thinking and ventured enthusiastically in an interdisciplinary approach.

Born in 1928, on the eve of two troubled decades, Baeck's youth was characterised by the worldwide economic crisis of the 1930s and the Second World War, before witnessing the reconstruction of the European Continent and the prosperity of the Golden Sixties.

Baeck became a true **world citizen** studying economics at the University of Leuven (KULeuven), broadening his perspectives with a Master degree in International Relations at Berkeley University (USA), and proceeded by doing field work in Africa (Congo, Rwanda, and Burundi) for his doctoral dissertation on 'Economic Development and Social Structures of Belgian Congo'. After teaching a while at Lovanium University, Kinshasa, he became an economics professor at KU Leuven in 1961, starting a new Research Centre for Development Economics as a new discipline in the Post-Colonial era. He was closely involved in policy-making in Development Cooperation leading several official missions also to South American countries. At the end of his career, given his broad interests in economic doctrines, he also ventured into the history of economic thought. His special focus was on economic thinking in the Mediterranean, mainly in the Islam and in 16th and 17th century Spain. This resulted in his book on 'The Mediterranean Tradition in Economic Thought'.

As a **homo universalis,** Baeck fostered very broad interests. His teaching included not only 'Problems of Developing Countries', but also the 'Theory of Economic Growth and Business Cycles', 'Labour Economics', 'History of Economic Thought', and even 'Introduction to Sociology' (for very large audiences). His methodological approaches were interdisciplinary which included, aside from economics, also demography, sociology, political science and ethics. He published a series of popular books in the area of development economics, as well as on globalisation and geopolitical issues.

In 1982, after serving in many executive functions at the University of Leuven, he became the **Executive Director** of the **University Foundation** in Brussels, a function he occupied successfully for 20 years. As a dynamic administrator, Baeck was involved in overseeing the major issues in university education, publishing many studies, e.g., on the cost of university education in the various disciplines, the job market for university graduates etc. He was very instrumental in bringing many needs of the university world in Belgium to the attention of political authorities. He was also responsible for managing the substantial financial portfolio of the Foundation, and succeeded in doing so in turbulent financial times. It certainly also fostered his broader interests in the financial world and his publications on the financial system crises in a geopolitical perspective.

Structure of the Publication

The Baeck cycle of colloquia aimed at a dialogue in an historical perspective between past and contemporary developments around issues in the area of 'the world village'.

Starting points were the ideas in Baeck's publications, summarizing the conventional wisdom at the time but also containing many critical reflections and original views as to the future. These ideas were presented by former close research-collaborators and colleagues of Baeck. As chairmen of the sessions, they also formulated issues and questions for the panel-members.

High-level policy-makers were invited as key-note speakers. Expert academic scholars intervened as respondents and confronted contemporary ideas and developments with earlier writings and views of Baeck.

The structure of the publication follows the themes addressed in the four colloquia spread out over 2018, reflecting in fact the four main areas of Baeck's research and writings:

- Geo-economics and globalisation
- Migration, population growth and economic development in Sub-Saharan Africa
- Global finance
- Islam and economic thinking in the Mediterranean

Acknowledgements

As a place where members of the Belgian and international university communities are happy to meet, intensive academic debate is taking place and various academic activities are welcomed, the University Foundation initiated this cycle of colloquia in Brussels being the capital of The European Union. In this respect the active support of Jacques Willems, Chairman of the Board and Eric De Keuleneer, Executive Director, is gratefully acknowledged.

The publication of the proceedings of the cycle of colloquia was made possible by cooperation between the University Foundation and the Interfaculty Council for Development Cooperation (IRO) at KU Leuven.

Louis Baeck, as the founder of the Institute for the Study of Developing Countries and the Centre for Development Planning, was also the initiator and longstanding chairman of this Interfaculty Council. IRO is an important channel through which KU Leuven makes funds available not only for research projects, but also for the formation and training of young academics in developing countries. Within the framework of 'The Global Minds Project', the IRO is instrumental in providing funds for this publication both in a digital form on open access platforms and in a print (pocket book) edition to be published jointly by Leuven University Press and the University Foundation. The aim is to make the dialogue on these very actual global issues freely accessible to students, researchers, and policymakers, in particular in the global South.

Finally Hilde Garmyn, Director for academic affairs and international relations at the University Foundation, substantially contributed to the conception and the organisation of this cycle of colloquia for a large audience at the University Foundation. She was also instrumental in setting up this publication, which was further made possible by skilful editing assistance by Isabel Fu.

To all of them many thanks.

1. Geopolitics and Globalisation

An Introduction

Frank Moss

Louis Baeck's Publications on Global Developments

Professor Baeck wrote two books on international topics that are still very relevant today. The first of these books was written already in 1984 and is entitled 'Power and Counter Power – A socio-political vision of the world'.[1] This book expands on the idea contained in one of his earlier writings, entitled 'The world is our village' which was published in 1971.[2] The underlying trend towards globalisation, which he discerned very early on, was synthesized in his 1984 publication in the following key message: the bipolar, Cold War-era world is gradually evolving into a multipolar world. However, this evolution is not the result of the emergence of new powers, but the outcome of a confluence of economic, social, cultural, and ideological factors.

As a matter of fact, the strength of Baeck's analysis of global developments has been that he was able to interpret on-going dynamics from various angles at once. His viewpoint was not merely an economic one, nor a geopolitical one. Instead, he tried to analyse evolving situations in the international domain as being determined not only by economic and political factors, but also stimulated by doctrines and cultural backgrounds.

When Baeck wrote his book 'Our rectangular globe' in 2003, it seemed that his thesis was being contradicted by history.[3] The ideology of economic liberalisation and privatisation had become the globally dominant one, after the Soviet Union and China had integrated their economies into the capitalist production and consumption processes. Geopolitically, the Western world under US leadership was dominating global developments with the expansion of NATO to the borders of the former USSR or even beyond on the one hand, and a military supremacy exhibited in the second Gulf War on the other hand.

Still, Baeck continued repeating his earlier key messages. One of his strongly held views is that globalisation is surpassing the economic dimension. It is about a global proliferation and uniformisation of techniques of production and markets, as well as of Western values, norms, and life styles. But precisely because of this multifaceted dimension of globalisation, uniformisation and convergence of sociopolitical systems will be resisted by strongly embedded cultures in other parts of the world, whose people will want to reconfirm their identities and re-establish their ethno-cultural awareness. In addition, contrary to the situation of 1984, the counter-powers to the Western economic, geopolitical, and ideological superpower had been strengthening in the period up to 2003, in absolute terms as well as in relative terms, on account of the economic growth deceleration of the US hegemon as well as the geopolitical mistakes it had meanwhile committed.

Baeck therefore continued to believe and affirm that the global asymmetry between the key nations and other groups of countries needed to be corrected in the direction of a harmonisation of their mutual interests. If not, the structural problems of the globe would remain unresolved, the world would become even more angle-shaped and hence unstable, and the US hegemon and the West more generally would suffer as a consequence.

Previous International Views and Current Developments: How Stark a Contrast?

Sixteen years after Baeck's writing on the rectangular world, his views are definitely worth revisiting. The US economy has undoubtedly lost more of its lead compared with its position one and a half decade ago. Although Baeck describes developments in China as carrying potential for catching up with the lead economies of the West, on account of its size and its pragmatic approach towards the introduction of Western modes of production, he could not fathom the tremendous economic expansion that the country has witnessed since then. Yet, his core message is proving very accurate, namely that a strongly embedded culture such as the Chinese one, and a deeply engrained ideology such as the Chinese communist party one, are able to resist the forces of Western-dominated globalisation.

With the benefit of hindsight, one could argue that Baeck was most definitely too optimistic about the development potential as a global force of such economies as India, Iran, or the African continent. But only time will tell whether such a judgment call at the current juncture was prescient or merely premature. Moreover, it is important to recall that Baeck never intended to offer a projection of the evolution of the multipolar global economy in the light of the multifaceted forces at work.

Similarly, his thesis could be viewed critically for not having foreseen that even within the communities of the Western economies resistance to the uniforming forces of globalisation would build so strongly and uncertainty about the benefits to be drawn from the 'global village' would be expressed so clearly in the form of rising protectionist forces and nationalistic movements. More relevant is to acknowledge that, of the four key actors that Baeck discerned in the process of globalisation (i.e., multinational enterprises, nation states, worldwide non-governmental organisations, and international organisations), all have either already adjusted their mode of operation, or are in the process of doing so, in the face of doubts about the earlier model of a streamlined Western-shaped globalisation.

Rodrik has illustrated in a penetrating manner the trilemma of nation states in a globalized world, having to make a choice between participation in globalisation, retention of national sovereignty, and successful continuation of the political model of participatory democracy.[4] While for some time the balance seemed to be tilting towards relinquishing national sovereignty in order to regain influence through multilateral cooperation, the pendulum now seems to be swinging in a different direction in a number of nation states. International organisations, notably the International Monetary Fund (IMF) and the World Bank, singled out by Louis Baeck for their role in the propagation of the so-called Washington consensus, have been adjusting their agendas, policy recommendations, and governance arrangements. Multinational enterprises are reviewing their global value chains and new super-firms are thriving in the services sector on account of their optimal use of information and communication technologies, allowing them to combine mass culture and individualism in a world in which the traditional social fabric has fallen prey to globalizing tendencies.

It is therefore difficult to contest that Baeck's multifaceted way of dissecting global dynamics has proven, and still is proving its validity. It is worth highlighting in this connection, from among his contributions, the following two warnings which his 2003 book contains.

First, his warning about the systemic risks contained in what he coined the increasing financialisation of the real economy. Influenced evidently by the stock market correction of the early 2000s when the tech bubble burst, he pointed to several dangers inherent in the evolving international monetary and financial system. One of its features was the rising role of non-bank financial intermediation. Another one was the rising indebtedness of the corporate sector. Still another one was the complementary, mutually beneficial, but ultimately unsustainable, combination of a consumption-based US hegemon and savings-based emerging market economies trying to catch up. Each of these three features could be seen as contributing to a growing ratio of financial over real economic transactions. Based on his recollection of historical precedents, Baeck concluded that such an increasing financialisation would ineluctably raise systemic risk. Only five years after his 2003 publication, the global financial crisis and the great recession set in, requiring an unprecedented global cooperative effort to prevent the world from sliding into a depression. The jury is still out as to whether, some ten years after, the systemic repairs undertaken will prove sufficiently resilient to cope with the next crisis. Fact of the matter is that rising non-bank financial intermediation, growing corporate indebtedness, and global external imbalances are still with us.

A second stark warning that Baeck conveyed in both his 1984 and 2003 books concerned the future of Europe. Already in his 1984 publication, he had noted that the fathers of Europe had failed in his opinion because of their insistence on economic determinism as the engine of integration and in view of their strategy of fostering European community building by means of state-led superstructures. He was strongly convinced that Europe would only succeed by means of concrete initiatives that would appeal to citizens, irrespective of their specific cultural background. As examples he quoted the monetary domain, but also innovative entrepreneurship and security.

As regards the monetary sphere, his wish materialized some five years later when European leaders decided to launch the project of Economic and Monetary Union (EMU). By the time of writing of the book on the rectangular globe in 2003, the EMU project had delivered a strong institutional setting with the European Central Bank conducting a single monetary policy for a large group of European countries. Still, Baeck seemed to have reservations about the way in which the EMU undertaking was delivering.

For what concerns European security aspects, I will leave it to the various speakers to evaluate, if they so wish, the on-going initiatives towards more security and military cooperation among EU countries. According to Baeck, already with 15 members it was difficult to achieve a common foreign policy. Hence, with 25 very heterogeneous partners (prior to the EU entries of Bulgaria, Romania, and Croatia), this undertaking would become a very long-term project at best, if not a dream, since many of the Central and Eastern European entrants into the EU have given priority to NATO membership and loyalty. Moreover, in the diplomatic manoeuvring prior to the second Gulf War, there was no trace of a European unity in foreign policy making.

Issues for Discussion from Today's Vantage Point

It would take a special colloquium to assess the extent to which the previous views, derived from a multifaceted analytical approach, remain pertinent for an interpretation of developments witnessed in the world of today. Four interesting questions can be derived directly from the 1984 and 2003 publications of Baeck. They are not put in any specific order, but each of them warrants a very deep discussion to better understand the world we currently live in.

One interesting issue would be to assess to what extent the post-Second World War institutional construction for global governance (built around a United Nations Organization, two Bretton Woods institutions (IMF and World Bank), and a World Trade Organization), remains the most suitable framework for a world with close to 200 nation states, more than 30 global cities that have more inhabitants than a country such as Belgium, and a number of global enterprises whose annual sales volume exceeds the gross national product of more than half of the world's countries. Or put differently, is the current post-Second World War institutional construction sufficiently well suited to achieve a sustainable, preferably climate-neutral growth with less inequality within and across countries and a smooth transition towards a digital economy?

A second issue would be to interpret China's increasing resistance to a US-dominated world order, as can be seen inter alia in the currently rising bilateral trade tensions, but also in geopolitical developments in Asia or in China's Belt and Road initiative which could be viewed as pursuing intrinsically similar objectives in Asia as the US Marshall Plan did in Europe some seventy years ago. The key question would then be whether these developments are demonstrations of a world becoming more 'rectangular', as Baeck would have termed it. Or, alternatively, whether we are witnessing the start of a transition process, in which evolving global forces are leading to the emergence of a new global hegemon. It is noteworthy that in 1984, Baeck did not perceive such a development possible and that, even in 2003, he did not deem feasible such a rapid rise of China toward superpower status.

A third, very pertinent issue concerns the risks faced by a global economy in which real economic outcomes seem to be determined predominantly by financial drivers and, relatedly, central banks and their policies are being perceived as the most potent actors to keep the real economy on track. In 2003 Baeck considered the state of financialisation of the global economy already well advanced, but seen from today's viewpoint, if anything, an acceleration in the process of financialisation has taken place with, as a result, record levels of indebtedness of the aggregate of governments, corporates, financial sector participants, and households at the global level.

A fourth issue would revolve around the role of Europe, or rather the European Union, in the current multipolar global context. As indicated above, Baeck was rather critical of the European project in the 1980s, as its focus was predominantly an economic one. Even in 2003, he seemed to be dissatisfied with the direction in which the European Union project was heading. The EU has further evolved since, but there are definitely dark clouds on the horizon. Brexit is only one of them, even if the most imminent one. Criticism of the EU by the current US administration or the way in which both China and Russia tend to preferably deal with individual EU Member States rather than with the EU as a whole are further demonstrations of the challenges the EU is facing. Can there be a future for such a project that, in the context of the above-mentioned trilemma of Rodrik, wants to firmly pursue the political model of participatory democracy and its participation in a globalized world, at the expense of waning national sovereignty? Again, the jury is still out, with projects such as ASEAN or the African Union pointing to the attraction of the soft powers of Europe, but many countries, also in other continents, are more impressed by the influence of hard power emanating from successful nation states, often not democratically governed.

Epilogue

Hence, it is left to the keynote contribution by Herman Van Rompuy to present contemporary views on globalisation, the tension between nationalism and internationalism, and how the European construction can help in making our part of the globe more stable and hence less rectangular in the words of Louis Baeck.

In the contribution of the panel, Mark Eyskens engages in very challenging futurology by describing 'Globalistan' and sharing his views on the labour pains of the birth of globalisation in Globalistan. Hylke Vandenbussche zooms in on a very topical subject relating to the European construction, namely the economic repercussions of the wish of the United Kingdom to leave the European Union, the so-called Brexit.

Notes

1. Baeck, L. (1984). *Macht en Tegenmacht: een socio-politieke visie op de wereld [Power and Counter Power: A socio-political vision of the world]*. Leuven: Uitgeverij Davidsfonds.
2. Baeck, L. (1971). *De Wereld is ons Dorp [The World is our Village]*. Tielt: Uitgeverij Lannoo.
3. Baeck, L. (2003). *Onze Vierkante Wereldbol [Our Rectangular World]*. Leuven: Uitgeverij Davidsfonds.
4. Rodrik, D. (2012). *The Globalization Paradox. Why Global Markets, States and Democracy Can't Coexist*. Oxford: Oxford University Press.

2. Geo-Economics and Geopolitics

Herman Van Rompuy

Globalisation, Internationalisation, and Interdependence

Globalisation is another name for internationalisation. Before the First World War, international trade was already highly developed. Colonialism also contributed to this, although this form of internationalisation was imposed on other countries in contrast to today's globalisation. The Cold War was a form of political globalisation in which almost every country had to choose between the two ideological and power blocks. The group of neutral countries was an exception, although they were mostly anti-Western.

What makes globalisation different from internationalisation? The scale of world trade certainly is greater and it is still growing. It is not centrally controlled, but it is or has been conducted within a multilateral framework of the World Health Organisation (WHO), the International Monetary Fund (IMF), G-20 and others. It concerns trade, information and communication, tourism, music and sport, climate, financial flows, multinational companies, technological transfers, and migration. Of course, national borders do not disappear and neither do all kinds of barriers to trade and investment, but the 'market crawls where it cannot go'. The movement seems unstoppable and irreversible.

This interdependence was expressed in a negative way during the financial crisis, with the global financial system just barely a few millimetres from implosion. It affected almost all countries, albeit unevenly. This global crisis provoked a global political response. The G-20 at the level of Heads of State or Government was a temporary 'countervailing power' to combat the excesses of market forces. Unfortunately, this global governance disappeared as soon as the crisis was over.

The crisis, which even became a 'multiple crisis' in Europe, further accentuated the growth differences between emerging and advanced economies. China emerged stronger from this crisis. In itself, growth differences between the two types of countries are not uncommon given that mature economies grow more slowly than those in an earlier stage of development. It is true however, that productivity growth in the West is clearly slower than just decades ago. However the reasons are not yet clear: lower increase of investments, lower capital intensity of investments, especially in the digital sector, slower than expected conversion of new technologies into economic applications, etc.

Globalisation ensured that the global income differences decreased, certainly by drastically reducing extreme poverty in Asia. However, income disparities within countries increased as competition intensified and industrial activities relocated. The pressure on the labour market meant that in the USA, for example, wages hardly increased since 1979, while productivity increased further, albeit at a slower pace. As a result, the share of profits in national income increased everywhere, but more so in the USA.

Economy-based Balance of Power

The economy now determines the balance of power much more than military power. The rise of China as a world power is due to the strength of its economy. The failure of numerous military interventions ranging from the Vietnamese War to the war in Iraq and Syria and their high budgetary cost contributed to this decline of the role of military instruments. Public opinion in the West is strongly opposed to war and the arms race; the missile crisis in the 1980s is a strong example of this. Exceptions are the military victories over the 'caliphate' and the thwarting of the takeover of power by Al Qaeda in Mali in 2013.

Obviously, the phenomenal rise of China together with the fall of communism in Europe is the biggest game changer of the past 40 years.

Communism in China has disappeared as an economic system, but the role of the communist party remains central. In fact, it is the breakthrough of the market economy, albeit with a lot of state capitalism. China represents 15% of the world economy in purchasing power parities and Russia 3%. The economic power largely determines the role of a country in world politics. China is a global player; Russia a regional one. China has a strong economy without raw materials. Russia has raw materials without an innovative economy.

The geo-economic strategy via China's One Belt One Road Initiative is motivated by domestic overcapacity in investment and, of course, by a desire to become a global player. They fill a vacuum after the withdrawal of the USA, the vanishing of the Soviet Union, and the former colonial powers.

The other emerging economies and countries have been weakened economically and politically. This is most obvious in the case of Russia, South Africa, and Brazil, three out of five members of the BRICS. India is mainly focused on its domestic challenges and on the ongoing conflict with Pakistan.

Relations between Russia and the West are at a low point. Confidence is completely lost not only through the annexation of the Crimea but through attempts to influence elections in the West through cyber-attacks. This attempt to destabilize is unprecedented.

The USA remains an economic superpower coupled with the status of the largest military power. But in relative terms it has lost much ground despite the dominant position of the GAFA companies (i.e., Google, Amazon, Facebook, and Apple) in the new economy. The dollar remains the world currency that offers the USA great advantages in foreign policy as well. The dollar does not force it to internal economic discipline. The new energetic independence of the USA through the shale gas revolution reinforces their decreased willingness to engage in the world. In the Middle East this is now very striking. Following the failure of military operations in Asia, the USA has realised that there are major risks involved and that wars in the USA itself have become unpopular. The unequal distribution of income within the States, together with these foreign wars, have led to the slogan 'America first'. Already under President Obama it was about 'leading from behind'. The domestic agenda in the USA is as important as the geopolitical rivalry with China. In a sense, the trade war against China combines both. In the eyes of American citizens, China is equated with the deindustrialisation resulting from globalisation, while at the same time the trade war tackles the Chinese dominant positions in certain global markets. China is not the only 'enemy'. President Trump needs an enemy. I fear that if there is a trade agreement with China, the EU will become the next target in the trade war. It goes so far that this domestic agenda is at the expense of solidarity within the Western camp. In fact, the West no longer exists today in the form it used to. The EU has virtually no agreement with the US President on any point. The aversion of the current American administration to international cooperation goes so far that it even left the Trans-Pacific Partnership (TPP) in 2018 although it was directed against China.

Role of the European Union

Over the last forty years, the EU has grown into an institute for 500 (or 440 after Brexit) million people. The introduction of the euro was an unprecedented form of transfer of sovereignty and enlargement to the former communist countries was a huge step. We call it: deepening and broadening the Union. However, the 'multiple crisis' since 2008 has even led to two existential crises, thus endangering the very existence of the Union. The Union overcame this once again as the EU-27 showed a surprising unity in the Brexit negotiations. But in general, the poly-crisis affected the countries in an unequal way and the theme of migration created great tensions within the Union, as well as in the USA and the UK. Over the last decade, the Union has been forced to concentrate on internal problems, as member states have focused on their own societies, with growing social and political malaise. Half of the EU countries now have a minority government. The weakened member states also make the Union weaker. As a result, the EU and its member states are lagging behind in many areas of the new economies and have so far shown too little combination of forces to meet the American and Chinese economic challenges. On the military and military-industrial front, there is the beginning of a hitherto unprecedented European cooperation, but the idea of a European army is still a long way off.

The EU is a global actor in many areas, for example, trade, climate, monetary, sanctions against Russia, partner on the Iran deal, development cooperation, etc. The EU has shown a united front on these fronts but this is not enough. More needs to be done. Unity remains an ever recurring problem and at the same time is the only possibility to be relevant on a global level. The EU is a global actor but not a world power in the absence of a military arm.

However, the focus on domestic policy has not made the EU an opponent of the multilateral order. On the contrary. Unlike China and the USA, the EU remains a believer and acts accordingly. It is gradually putting more emphasis on protecting its own interests without falling into protectionism. The EU continues to conclude free trade agreements, the most important of which it has recently approved with Japan. Within the Union there is resistance to the transfer of further national powers, but at the same time there is no strong resurgence of 'national' nationalism.

International Institutions and Cooperation

These shifts of power on a global scale only have a slow impact on the major international institutions, which are often still governed on the basis of the power relations after 1945. Strangely enough, it is the founder of the multilateral framework, namely the USA, who is turning away from this 'global governance'. The impact of globalisation made American citizens feel that global competition was a threat and that they were insufficiently protected against these new developments. The USA is withdrawing from most institutions, including numerous international agreements such as the Paris Climate Agreement, the TPP, the Iran nuclear deal, the disarmament agreements with Russia, and others. In general, we are not in favour of stronger international cooperation except in the field of climate, culminating in the Paris Agreement (2015). The United Nations Framework Convention on Climate Change (UNFCCC) decides by consensus, as does the WHO. This concerns about 190 countries!

Our world has become apolar, far from the bipolar model during the Cold War. There is no new bipolarity with China and USA yet. As a result, the world is not necessarily less secure, although it feels less stable, also to the population. Sometimes it is said that a high degree of interdependence has not stood in the way of war. But this interdependence is now much stronger than in the past. Another thesis is that the rivalry between a new global player and the old one, which in the past gave rise to war; the so-called 'Thucydides trap'. Here too, history does not have to repeat itself, certainly not in the same way.

Openness and Public Opinion

Globalisation is causing tensions in Western public opinion, which are partly at the root of the rise of populism.

We have to take into account all aspects of a human being. We need as much 'space', creating opportunities for our economic and humane development, as we need a 'place', to give us a feeling of being at home, of being protected. If there is no right balance between 'space' and 'place', between global and local, rationality and emotions, between openness and protection, hope turns into fear.

We have to better protect our people against real or perceived threats such as high unemployment rates, insecure jobs, mass illegal migration, climate change, terrorism, social, commercial and tax dumping, huge inequalities, and threats of war on our Eastern and Southern borders. If we cannot protect people, they will choose protectionism. If we fail, tribalism and nationalism will be further strengthened. If we fail, large parts of our population will turn away from our open societies, our open economies, and our open democracies. It is not only the idea of the European Union that is in danger; the liberal worldview, which values democracy and freedom is then under siege. Even though we obtained results on all those domains that citizens perceive as threatening, it is not enough. That is why openness is under pressure in parts of our Union. Protection ('Une Europe qui protège', as President Mitterrand once said) and openness are key words for our political and social models.

3. The Labour Pains of Globalistan

Mark Eyskens

Professor Louis Baeck launched the concept of 'The Global Village' when he published in the 70s of the previous century probably his most important book written.[1]

In this contribution, I would like to defend the view that the present multiple worldwide problems do still represent the birth pains of a new world – or to be more precise, of a new world community – which we might call Globalistan. Yet, the pregnancy could still end in stillbirth, if we behave in an irresponsible way.

A Tsunami of Changes

Under the ancient regime, the old order, the changes were so slow that few people noticed them; today, the changes are so fast that few people perceive them or are able to assess their scale properly. We are too often entering the future backwards, while looking in the rear-view mirror.

Fundamental and all-embracing for our future, however, is the accelerated emergence of the knowledge society, driven by information and communication technologies (ICT) and their applications, all derived in one way or another from the invention of the wonder tool, the computer. Historians used to divide world history into two parts: Before Christ and After Christ (BC and AC). Today these abbreviations BC and AC mean 'before computer' (BC) and 'after computer' (AC). Scientifically, technologically, and economically the world is becoming one, which means that countries are becoming highly interdependent. Thus a global world is emerging, our global village, which however has still remained too provincial in terms of governance. National governments are too small for the big challenges and too big for the small ones. There is a gaping asymmetry between the global aspect of the world economy and the local character of the conduct of policy via national States.

I believe that the ICT revolution has brought about critical turning points in the past 30 years. The world economy was fundamentally transformed. Worldwide political bipolarity became unstable multipolarity if not a-polarity. The fall of the Berlin Wall in 1989 led to the implosion of communism and collectivist socialism. The financial and economic crisis of 2008-2010 and the emergence of oligopolistic competition on the world markets and the digitalisation of market functioning has been seriously undermining liberal capitalism. In a numerical world private intellectual and industrial property are no longer protected. The two great ideologies which have dominated social and economic thinking over the past 250 years, liberalism and socialism (i.e., offshoots of the first and second Industrial Revolutions) are being rendered obsolete by the new scientific and technological developments.

History of mankind has indeed been steered by discoveries and scientific innovations, starting with the discovery of fire, 300.000 year ago.

Today scientific inventions are overwhelming in all domains. The acronym B.I.N.C. is useful in summarizing the ongoing scientific revolutions:

– Biogenetics, fabulous progress of medicine, average life span of 100, 150, 200 years??
– Information technology (computer apps, AI, virtual reality and physical robots, 3-D printing). Emergence of the 'robo sapiens'.
– Nanotechnology. Tomorrow, we will be able to speak to every citizen on earth in our own language, and understand all the worlds' languages thanks to Nano computers (wireless or implanted in our own body)
– Cognitive science. Human brain research and manipulation and hence steering human behaviour.

Disruption of Traditional Ideologies

The socio-economic consequences of the tsunami of scientific and technological innovations will be overwhelming and dramatic for the world community and the members of mankind. The term 'disruption' is appropriate.

Digitalisation and robotisation will considerably reduce working time, wage earners will be replaced by independent employees, the existence of world markets will go hand in hand with home work, multinationals will compete but also cooperate in lot of domains, intellectual property will no longer be protected, interconnectivity will eliminate all kind of intermediaries on the markets, e-commerce will take over from shopping. Simultaneous translation of all languages into all other languages will revolutionize learning particularly at the university level. AIRBNB, Uberisation, circular economy, pooling, personal manufacturing, on line open courses, worldwide universities will spread, cash payments will disappear. The development of solar and nuclear fusion energy will completely change the worldwide economic and political power balance. Wealth could be transformed in welfare and the pursuit of happiness will become a societal goal. A post-economic era will emerge.

Nevertheless a lot of shadows of progress will have to be dealt with: demography, aging, climate, food scarcity, antimicrobial resistance (AMR), weapons of mass destruction, the difficulty to transform multiculturality in interculturality…

A phenomenon of general *de-collectivisation* has taken place. When scientific knowledge and the innovative creativity it fuels become the most important production factors, the Marxist recipe of the collectivisation or nationalisation of the capitalist factors of production completely falls apart. Factories, machines, and raw materials can be taken over by the State and collectively managed via the communist party; human knowledge and information, numerically treated, cannot. They are in essence immaterial assets. Incomes and fortunes can and must be distributed in accordance with basic social justice. For politicians, this often leads to an embarrassing zero-sum game with winners and losers. By contrast, knowledge through communication has to be multiplied rather than divided up. Society's zero-sum game becomes a plus-sum game which only has winners, when knowledge is spread. As a consequence a new social paradigm arises: 1 + 1 = 3.

The ICT revolution confronts communism and socialism with de-collectivisation, but it has also assailed liberalism through *de-privatisation*. Nothing is private any more, and ideas, proposals, discoveries, and inventions spread around the world, often at the speed of light. Industrial and intellectual property is *de facto* left unprotected. Counterfeiting or imitation is believed to account for 25% of global production in some sectors. In a number of Asian countries, copyright is being reinterpreted as 'the right to copy'. For over two centuries, the basic paradigm of liberal capitalism has referred to the ancient Roman legal concept of private ownership. This has now lost all stability. Moreover, it is argued that discoveries and inventions represent part of mankind's intellectual heritage and should thus be accessible to all immediately. In addition, middlemen are disappearing from the markets (i.e., the phenomenon of disintermediation) so that supply and demand now come directly into contact with each other – e-Bay, internet, Amazon… are obvious examples – a development which is fundamentally altering the workings of the traditional market and which also has implications for the capacity of nation States to raise taxes through VAT and define corporate taxes of multinationals. The most important point of all, though, is that in a unified global economy, the big players have the best chance in all sectors, which is leading to *oligopolistic competition.* Competitive pressure and the enormous costs of research and development are forcing companies to upsize. This explains the frequent mergers and acquisitions, and has resulted in a worldwide life-or-death competitive struggle. World economy has now resemblance with an economic Jurassic Park dominated by what the Americans call 'the cut throat over competition'.

New forms of competition – often innovative competition – greatly diminish the advantages of market activity and sometimes eliminate them altogether (once the sale price no longer equals the marginal cost of the product). The financial sector plays a strategic role in this process, because it must be capable of financing the corporate giants on the oligopolistic markets, in which small and medium-sized companies are often turned into satellites of these businesses or sectors. As money is a homogenous commodity – money is money – the competition between financial institutions is extremely fierce. The personnel is partly rewarded with bonuses based on the recorded turnover figures, meaning that more risks are taken. Executives enjoy substantial bonuses and stock options, which lose social support when bank shares plummet. Although public opinion has proved to be less troubled about the high salaries paid to certain sports stars and all kinds of more or less questionable entertainers and singers. It is primarily the frenzied global competition in the financial sector, in which risky financing practices and products, toxic products, have been launched, that has brought about the financial and economic crisis ten years ago. As a result, a certain type of liberal capitalism has had its effectiveness and credibility undermined. The dramatic crisis of the banking sector, imported from the United States, has been countered by governments by injecting massive monetary liquidities into the financial system. This effort has undermined the solvability of State treasuries, particularly in the southern European member states of the Monetary Union and has weakened the monetary union and showed its weakness.

The global community, facing disruptive evolutions in many domains, is looking for a new, coherent social vision, which obviously needs to extend further than 'Googlism' or 'Internautism'. We should also underline that the word 'crisis', which today is more frequently used than the words 'I love you', has a Greek origin and refers not in the first place to a catastrophe but to a moment of reflection, of critical reassessment, of bifurcation for better or for worse. We have to realise that crises are also challenges and that we have to face them neither by optimism nor by pessimism. Optimism sounds naive when we look at the host of problems, confronting the world community. An optimist today would be an ill-informed pessimist.

Some challenges that transcend national boundaries are mounting: climate problems, energy supply, food and water shortages, an ageing population in Europe and China, the demographic explosion (10 billion inhabitants in 2050, of whom just 5% will be European), the multipolarisation of global politics, growing inequalities, the rejection of modernity by fundamentalist regimes, exploitation of man by man, international crime, ethnic violence and terrorism, obsolete nationalism, the proliferation of weapons of mass destruction, poverty. And even this list is not comprehensive. However history has demonstrated that humanity in the past at last succeeded in overcoming major difficulties and solving big problems. Pessimism is always paralyzing and self-destructive. What we need is 'meliorism', that means the belief and the hope that situations can be improved and problems can be solved, provided we adhere to a 'yes we can'-philosophy.

The Governance of Globalistan

Globalistan's governance needs to be devised by recalibrating the market–government pair in a totally new context. The biggest challenge for our societies and their governance is to turn the tide of change in real human progress. It is not unreasonable to suggest that 'personalism' as conceived by some thinkers of the first half of the 20th century, such as Emmanuel Mounier, could pave the way for a fundamental reflection.

The market today is largely virtual, brings supply and demand into direct contact, and is worldwide. Like all markets, world market displays the tendency to eliminate annoying competition. Thus an international authority is needed to enforce a loyal competition policy worldwide. The European Union has set an example in this respect for years with an essential role played by the European Commission's Commissioner for Competition Policy. It would make sense for the World Trade Organization to be reformed to become a sort of economic magistracy. An authority is really needed which would supervise market activity and keep it running efficiently and in doing so maximising prosperity for the greater good. However, such an authority can no longer be the nation State, which lacks the scope to regulate global economic processes. A collective policy is required which is as international as possible, which will have to be able in the future to prevent systemic crises. It therefore seems essential to me that the International Monetary Fund, the World Bank, and the World Trade Organization should start working together much more intensively, and that within the United Nations. Moreover in addition to the political UN Security Council, an Economic Security Council should be created representing the distribution of economic power in the world, for example starting with the inclusion of the G20.

Government and market, socialism and liberalism, democracy and technocracy, competition and cooperation, multiculturalism and interculturalism, nation and state, knowledge and wealth, intellectual property and the spread of the Internet, education and university, language and culture, religion and reason: all are being transformed and will bring about fundamental societal changes in turn.

Homo sapiens are now evolving into post economy. The New Economy must manage scarcity and affluence, a dual problem that is not integrated into the main classical economic theories. There will be an important shock between opulence, as already described by the economist John Kenneth Galbraith in 'The Affluent Society', and new scarcities on planet Earth. The only planet we have. There is no planet B.

A New Paradigm

The West grew strongly particularly at the beginning of industrialisation, thanks to dualism, an old paradigm stemming from Plato. This logic of contradictions was very useful because it forced the Westerners to make choices between 'either/or', between alternatives, between right or wrong in order to progress and to act. The steam engine is a good example, invented three centuries earlier in China as a piece of entertainment, but installed only in the 18th century at the heart of the industry in Europe by Westerners. Platonic dualism is at the core of creativity but was and still is at the origin of many conflicts and even wars which ranked the 20th century as the bloodiest of the human history.

Asian wisdom however teaches us another different basic paradigm: the Yin and Yang principle, the complementarity of dual oppositions which merge into a synthesis. In Chinese writing moreover, there is a single ideogram for the words 'crisis' and 'opportunity'.

This concept matches perfectly with the discovery in quantum physics that light is both a wave and a beam of particles, the photons. Niels Bohr, one of the founding fathers of quantum physics, summarized this insight by the Latin phrase 'Contraria complementa sunt', replacing the old 'either/or' logic by the revolutionary 'and/and' principle, that frees the way to cooperative solutions.

This awareness is progressively rising in Western thinking and will have far reaching consequences. It will lead us to a new holistic approach, exploring the hidden energies of diversity, divergence, oppositions and promoting synthesis, and all kinds of creative compromises, in a world of interdependence, where national governments are too small for the big problems and too big for the small ones. Economic praxis has already adopted what is coined as 'coopetition', when competition and cooperation are no longer exclusive along Darwinian principles but complementary, even inclusive according to quantum mechanical rules.

The rising of this inclusive, global approach is a challenge for political and economic leaders facing local populism emerging from fears and misunderstanding of what is going on in the global world of today and the world village of tomorrow. The nationalistic definition of 'people' has become obsolete. The 'people' has become a 'population' with multicultural features in most countries. Nationalism and populism are perfectly understandable but they have become counterproductive because they are no longer future oriented. Protectionism is the economic and cultural translation of nationalism. To a certain extent protectionism already existed before economics and politics, even before human beings: the first membranes protecting living cells, stressed in our bodies, were self protecting. This selfish vitalism is still attractive but suicidal in a changed world as soon as ego-nationalists propose to build walls instead of bridges.

In times of growing complexity, democracy is caught between web and spider. Some citizens are saying 'We have a vote, but we do not have a voice'. This is a serious warning addressed to politicians. Societal problems are extremely complex and the decision making process is most opaque. Governments and all kinds of authorities: 'they' decide, 'they' rule, 'they' legislate, 'they' impose…

There is a far reaching 'they-ification' of politics, which makes governing impersonal, abstract, and looking like a non-figurative painting. We need to reinvent democracy by introducing elements of participative decision making, by informing and explaining, and replacing demagogues by pedagogues.

Most important is to modify the democratic voting systems. One model could be the promoting of 'point voting', an electoral system by which each voter would get a plural number of votes, for instance ten votes, which he could freely cast and spread over different parties and candidates according to the intensity of his preferences. This would lead to a fine tuning of the voters choices. Also at the micro-economic level of enterprises and companies democratic cooperation between all stakeholders, transcending their exclusive interests, is at stake in the post economic era. Still more Herculean is the task of organizing steadily ways and means of international, possibly worldwide economic and political governance.

More Europe

On a much larger scale the European institutions also suffer from several functional problems and have to cope with great challenges. A European Fiscal Community should be created according to the principle 'no representation without taxation'. Today the EU Parliament has no taxation power, so it is difficult to implement new strategies and new legislation. We also need to simplify and clarify the taxation systems. Budgetary expenses with respect to defence, security, energy, development policy, integration of immigrants, research, digital communication… should be Europeanized. A strong European public budget is needed. The EU Institutions budget equals 1% versus 23% in the USA for the federal expenses.

The euro area presently, in order to cope with distortions of competition among member states, has to reduce costs of production and by consequence impose severe measures of austerity implying the reduction of public spending, of wages, of all kinds of allowances given that the management of exchange rates by individual countries is no longer possible inside a monetary zone. However, austerity measures being considered as an 'internal devaluation' make the European Union unpopular and may lead to economic deflation. Only an efficient budgetary policy conducted by the EU could stabilize the euro area.

More Europe is the only realistic approach in order to deal with the mounting challenges.

The Ethics of Change

It goes without saying that the ongoing tsunami of scientific and technological innovations will revolutionise the world community for better and for worse. As a consequence the ultimate question will be and is already the question of ethics. How to transform all these changes into human progress? How should we manage ethics in politics, in economy, in business? And what's the 'right ethic'? Who is deciding on those values? Which are the rules applicable for everyone? Do we stick and apply to the lowest common denominator?

Buddha, Plato, Jesus Christ, Kant, and other moral leaders said: 'Do not do to others what you do not want to be done to yourself'. But is this rule sufficient to improve human life on earth?

The guideline of a shifting economy and society is the quest of purpose in economy, the quest of ethics in business – with tools that can be used on the field. It is also an invitation to all decision-makers to imagine and implement new dreams to connect human beings, and transform the grief of the planetary village into human happiness.

The spread of the knowledge society is ushering in a new phase in the history of mankind. The future can only be safeguarded by promoting and developing science and technology as intensively as possible. But of course, not every change is an improvement, and a distinction should therefore be drawn between what is beneficial to human progress and what is harmful, between the good and the bad. This age-old ethical question is more topical than ever. The global community needs to be organised and transformed into an international community, based on ethical principles, confirmed by international treaties and law. And for this, the propagation and acceptance of an ethics of change is far more important than a change of ethics.

Notes

1. Baeck, L. (1971). *De Wereld is ons Dorp [The World is our Village]*. Tielt: Uitgeverij Lannoo.

4. The European Network Economy and Brexit

Hylke Vandenbussche

On 29 March 2017, the United Kingdom (UK) officially started Brexit negotiations. However, there is a great deal of uncertainty about the outcome of the negotiations the UK and the EU-27 are currently conducting. It is likely that Brexit will lead to a rise in import tariffs and a decline in trade between the two parties.

Economists are united in their belief that protectionism is not beneficial for anyone in the long run. A rise in import tariffs leads to decline in trade between the UK and the European continent, which in turn results in a loss of British and European jobs. Especially the most open countries in Europe with the closest trade relationships with the UK, like Belgium, stand to lose the most in such a scenario. As the economically most important region in Belgium, much is at stake for Flanders in particular.

In this contribution, we are examining the output and job losses in Flanders in the **optimistic** ('soft') and the **pessimistic** ('hard') **Brexit scenarios** that are now circulating in the literature. We are looking for an answer to the question how substantial the decline in export will be and **what losses in Gross Domestic Product (GDP) and jobs this will entail**. This Brexit study for Flanders builds on a previous analysis in which the output and job losses was calculated for each EU member state.[1] This study examines more closely the implications of Brexit for the three regions in Belgium: the Flemish Region ('Flanders'), the Walloon Region ('Wallonia'), and the Brussels Capital Region ('Brussels'). Our methodology is largely the same as that used in Vandenbussche et al. and can be consulted there for more details.[2]

At the moment there is a free trade policy in place between all countries of the current EU with zero import tariffs. Possible Brexit scenarios are based on an existing study of Dhringa et al. who examined what a 'soft' and a 'hard' Brexit would entail.[3] A 'soft' Brexit is described as a scenario in which import tariffs between the UK and the EU-27 remain set to zero as is the current situation, but in which other obstacles of a non-tariff nature (Non-Tariff Barriers, NTBs) would increase to 2.77%, as is now the case for Norway. In the event of a 'hard' Brexit, the import tariffs between the UK and the rest of the EU will be raised to the level of the World Trade Organisation (WTO). These so-called Most Favoured Nations tariffs (MFN tariffs) are used in the trade between, for instance, the EU and the US. Furthermore, with a hard Brexit, the NTBs would also increase to 8.31%.

We use these two scenarios as the starting point for this study to calculate how many jobs and how much output would be lost in a soft and a hard Brexit per region and per sector in Belgium.

What Makes our Brexit Study Different?

Most existing studies on the impact of Brexit base their calculations solely on *direct* trade with the UK.[4] Our methodology, by comparison, is fundamentally different and we demonstrate that taking into account only the direct export of goods will result in a significant underestimate of the trade activity between two trading partners and consequently also an underestimate of the number of jobs that will be potentially lost in the event of Brexit.

Our methodology allows us to chart the interconnectedness between the UK and Belgium (and its regions) in much greater detail. In this process, we not only consider '*direct*' export of Belgium to the UK[5] but also '*indirect*' export. Examples of indirect export from Belgium to the UK include the export of Belgian steel to Germany to be incorporated into German cars which in turn are exported to the UK. This indirect export involves Belgian jobs, too. Furthermore, direct export from Belgium to the UK includes German car manufacturers taking out a Belgian insurance policy to ship their cars to the UK. In other words, Belgian jobs in the insurance sector that would be lost as a consequence of a reduction in export of German cars to the UK after Brexit must also be included in the calculation of job losses in Belgium.

To calculate the full number of jobs that depend on export to the UK, we use the World Input Output Tables (WIOT). This database allows us to chart the entire network structure and production value chains in Europe. This means that we look at all input-output links between the various goods and services sectors in different countries. Consequently, we know which European industries are supplied by each sector in Belgium and which European industries supply each sector. In other words, in addition to the 'direct' trade with the UK, we can also establish the 'indirect' trade via third countries and sectors. This analysis takes into account all goods and services sectors in the economy and therefore offers a comprehensive picture of the interdependence between Belgium and the UK.

Hence, we find that for Belgium in its entirety, about 20% of the total impact of Brexit can be contributed to indirect channels. In other words 20% of the Belgian losses can be attributed to trade with the UK via third countries. However, there are considerable differences between the different European countries. In Slovenia, almost half of the total impact of Brexit can be attributed to indirect exports, whereas losses in Malta can be almost entirely (95%) attributed to direct trade with the UK. Also, within a country, there are significant differences between sectors, which may cause our results to deviate from those of other Brexit studies.[6] This is because we also take into account the indirect effects and these vary from sector to sector. Our study identifies these indirect effects and therefore offers a more precise picture of the impact of Brexit on each sector.

Another novelty in our study is that we only take into account added value that was created in Belgium (or more specifically Flanders) for the calculation of job and output losses. This is because gross export numbers alone do not reveal much with respect to jobs. Only the domestic added value, incorporated in the Belgian (Flemish) export is of interest since only added value represents jobs.

By meticulously charting the European production networks, our study can be considered an important addition to previous studies on Brexit. By calculating the domestic added value incorporated in the direct and indirect export of Belgium to the UK, we are able to calculate potential job and output losses in each sector, in each region in Belgium, in much greater detail than was the case before. Consequently, our results may differ from those of other Brexit analyses (see e.g., the study by Flanders Investment & Trade that was published in December 2016) which only took into account the direct gross export of Flanders to the UK in an effort to make an estimate of the effects of Brexit.

Output and Job Losses in Europe

We begin by showing the aggregated results for job losses in each European country in Figure 4.1.

Figure 4.1: Job losses in Europe as a result of a hard Brexit

Then we zoom in on the implications of a possible Brexit for Belgium, the UK, and the EU-27 as a whole. For a more detailed description of the methodology and the Brexit result, we refer to Vandenbussche, Connell, and Simons.[7]

The European, Belgian, and British losses established by this study are summarised in Tables 4.1 and 4.2. We found a Belgian job loss rate of 10.000 to 42.000 jobs, for a 'soft' and a 'hard' Brexit, respectively. This means a loss of 0.58% to 2.53% of the Belgian GDP (see Table 4.2).

The impact for the EU-27 as a whole varies from 284.000 to 1.200.000 jobs and a decline in EU GDP ranging from 0.38% to 1.54%. For the United Kingdom, we found a job loss rate of 140.000 jobs in a 'soft' Brexit scenario and 526.000 jobs in a 'hard' Brexit scenario which corresponds to a decline in the UK GDP of 1.21% and 4.47%, respectively.

Table 4.1: Job losses caused by Brexit in Belgium, the EU-27, and the UK

Brexit scenario	Job Losses		
	Belgium	EU-27	UK
Soft Brexit	-10.000	-284.000	-140.000
Hard Brexit	-42.000	-1.200.000	-526.000

Source: Vandenbussche et al. (2017)

Table 4.2: Output losses as a result of Brexit in Belgium, the EU-27, and the UK

Brexit scenario	Output Losses (in % of the GDP)		
	Belgium	EU-27	UK
Soft Brexit	-0.58%	-0.38%	-1.21%
Hard Brexit	-2.35%	-1.54%	-4.47%

Source: Vandenbussche et al. (2017)

Output and Job Losses in the Belgian Regions

Now that we have an idea of the scope of losses at the European level, we can differentiate regionally the losses for Belgium as a specific member state. So as to arrive at the results for the different Belgian regions, we ideally use regional input-output tables at the sector level with an international dimension, which is to say international production links for each Belgian region. These will enable us to chart the production structure of the Flemish economy, accounting for the way in which Flemish manufacturing is interconnected with sectors in the other EU countries and the other Belgian regions to meet international (i.e., British) demand, and to do so for each sector. Unfortunately, this information is not available in the regional input-output tables for Belgium, as a result of which we chose an alternative approach in this study.

The results for Flanders (and Wallonia and Brussels as well) are calculated as a proportion of the Belgian total results, in which the proportion in each sector is calculated as the share of Flemish employees in the total Belgian working population of that sector.[8] For instance in the food industry, the Flemish economy takes about a 70% share in the total Belgian production.

The job and output loss that we establish for Flanders, Wallonia, and Brussels, according to this method, is shown in Tables 4.3 and 4.4. It is not surprising that the greatest share of Belgian losses will be in Flanders (see Table 4.3). About 6.500 of the 10.000 jobs lost in the event of a soft Brexit are found in Flanders. Wallonia is in second place with about 2.400 jobs lost, whereas the remaining 1.000 jobs are Brussels jobs. In the event of a hard Brexit, we expect a loss of around 28.000 Flemish jobs which corresponds to 1.06% of the total Flemish working population.

In addition, with regards to output (measured in terms of regional added value), Flanders is hit the hardest (see Table 4.4). In the event of a soft Brexit, close to 1.8 billion of the 2.8 billion dollars in lost Belgian production will befall Flanders. This corresponds to a relative loss of 0.6% of the total Flemish added value. Also in Wallonia, we find the same relative loss of 0.6% which corresponds to close to 0.7 billion dollars of production. The Brussels Capital Region is affected the least in both absolute and relative numbers. Finally, our estimates indicate that about 7.4 billion dollars of Flemish production will disappear in the event of a hard Brexit. This corresponds to 2.5% of the Flemish economy, a substantial loss.

Table 4.3: Job losses as a result of Brexit in Brussels, Flanders, and Wallonia

	Job Losses			
	Soft Brexit		Hard Brexit	
	jobs	% of total number of jobs	jobs	% of total number of jobs
Brussels	-1.010	-0.15%	-3.981	-0.58%
Flanders	-6.505	-0.25%	-27.991	-1.06%
Wallonia	-2.435	-0.20%	-10.058	-0.82%
Belgium	**-9.950**	**-0.22%**	**-42.031**	**-0.92%**

Table 4.4: Output Losses as a result of Brexit in Brussels, Flanders, and Wallonia

	Loss of Added Value (AV)			
	Soft Brexit		Hard Brexit	
	million ($)	% of total AV	million ($)	% of total AV
Brussels	-347	-0.38%	-1.343	-1.47%
Flanders	-1.775	-0.60%	-7.384	-2.51%
Wallonia	-691	-0.60%	-2.778	-2.39%
Belgium	**-2.812**	**-0.56%**	**-11.505**	**-2.29%**

Brexit and the Sectors per Region in Belgium that are Affected the Most

The results achieved so far concern losses for the economy as a whole. However, the Flemish, Walloon, and Brussels losses can be split up per sector. Table 4.5 gives you an overview of the four sectors that will be affected worst by a hard Brexit for each Belgian region. As expected, these are the largest and/or most export-oriented sectors.

In terms of *employment*, the greatest losses are expected in the Flemish food industry, followed by the textile sector and two important service sectors. In Wallonia, the food industry is also the biggest loser, whereas in Brussels, it is mostly jobs in the service sectors that will disappear.

In Flanders, most of the *added value* is lost in the chemical industry, relegating the food industry to number two. Legal advice and wholesale trade complete the top four. In Wallonia and Brussels, the strongest decline in added value presents itself in the pharmaceutical and the financial sector, respectively.

Table 4.5: Most adversely affected sectors in each region in case of a hard Brexit

		Flanders	**Wallonia**	**Brussels**
Jobs	1	Food	Food	Administrative and support services
	2	Textile	Administrative and support services	Legal and acount-ing consulting
	3	Administrative and support services	Retail	Retail
	4	Legal and acount-ing consulting	Legal and acount-ing consulting	Wholesale trade
Added Value (AV)	1	Chemicals	Pharmaceuticals	Financial services
	2	Food	Food	Legal and acount-ing consulting
	3	Legal and account-ing consulting	Legal and acount-ing consulting	Wholesale trade
	4	Wholesale trade	Chemicals	Administrative and support services

Figure 4.2 shows the 15 sectors that would be affected worst by a hard Brexit in Flanders in relation to absolute job losses. It is clear that both the goods and the service sectors could be affected negatively. Within the goods industries, it is predominantly the food, textile, motor vehicles, and chemical sectors that will suffer heavy job losses in the event of a Brexit. For instance, the food industry would suffer a loss of over 3.000 jobs. Within the services sectors in Flanders, it is predominantly the administrative, legal, accounting, and retail services that would be most affected by Brexit.

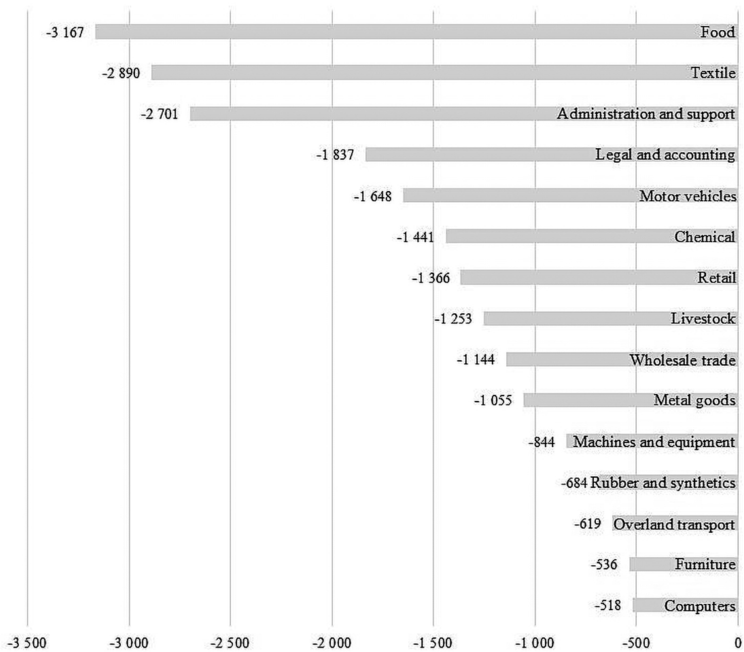

Figure 4.2: Job losses for the most affected sectors in Flanders in the event of a hard Brexit

Conclusion

This contribution analyses the consequences of a Brexit for regions in Belgium. For each sector in each of the regions of Flanders, Wallonia, and Brussels, we calculated the consequences of Brexit with respect to jobs lost as well as the generated added value that would be lost when import tariffs are introduced on both sides of the Channel.

The conclusion is that there are no winners in the event of a Brexit, only losers. Belgium, and particularly Flanders, will be amongst the biggest losers in the EU-27 in terms of jobs and local production. The findings of this study suggest stronger effects of a Brexit than other studies. The most significant reason being the strongly integrated European value chains, as a result of which Flanders not only exports to the UK directly, but is also a supplier of intermediate goods and services to a number of other EU-27 countries, which then go on to find their way to the UK. The sum total of all these effects may result in a Brexit bill for the European continent that is much higher than originally believed.

Notes

1. See Vandenbussche, H., Connell, W., & Simons, W. (2017). *Global Value Chains, Trade Shocks and Jobs. An Application to Brexit*. Leuven discussion paper.
2. See Vandenbussche, H. et al. (2017). *Global Value Chains.*
3. Dhingra, S., Huang, H., Ottaviano, G. I., Pessoa, J. P., Sampson, T., & Van Reenen, J. (2017). The costs and benefits of leaving the EU: Trade effects. *Economic Policy*, *32*, 651-705.
4. See Emerson, M., Busse, M., Di Salvo, M., Gros, D., & Pelkmans, J. (2017). *An assessment of the economic impact of Brexit on the EU27.* Briefing Paper for the internal market and Consumer Protection Committee of the European Parliament. This study provides an overview of the results from six separate studies on Brexit so far, including three academic studies and three that were carried out by international institutions.
5. The UK is Belgium's fourth most important trading partner. It represents about 8% of the direct Belgian export. As an import partner the UK is ranked fifth, with a little under 5% of Belgian import coming from the UK.
6. For Belgium, Brexit losses via indirect channels vary greatly from sector to sector. For instance, more than half of the losses for the Belgian steel sector manifest themselves through third countries. Nonetheless, most (about 95%) of the losses in the Belgian production of motor vehicles is from direct trade. A motor vehicle tends to be a final product rather than one used as input for other sectors or countries and is therefore exported directly from Belgium to the UK. Across all sectors, indirect losses from Brexit represent about 20% of the total impact.
7. Vandenbussche, H. et al. (2017). *Global Value Chains.*
8. We used the Eurostat database for the year 2010 as a source for this data.

5. Migration to Western Europe

An Introduction

Lodewijk Berlage

Louis Baeck had a lifelong interest in development problems. Starting with his early publications and throughout his career he considered development not just as matter of economic growth, but rather as a process of social and political transformation, and of a change of values and ideology underlying that transformation. In his well-known book 'The World is our Village', published in 1971, a prominent place was given to demographic change and to income gaps between rich and poor countries.[1] In his second to last book, 'Text and Context in the Thematisation on Postwar Development', published in 2000, Baeck emphasized that to comprehend the evolution of development theories it is necessary to put them in their historical context.[2]

However international migration was not given a prominent place in Baeck's publications. This was in line with early post-war mainstream research in the social sciences where international migration was an issue of marginal interest. The massive migration from Europe to the Americas and to Australia and New Zealand had been a major component of the 19th and early 20th century globalisation. But those days were long gone. After the First World War migration flows from Europe had drastically fallen. Some outmigration continued but, apart from the massive post-war population resettlement within Europe, international migration hardly got any attention from European policy makers, nor from the public at large. In the field of development economics which became a separate sub-discipline of economics during the 1950s, internal migration was given a prominent place, but international migration was hardly a research topic.

Since the middle of the 1960s there has been a substantial growth of international migration and an extensive literature on the economics of migration has been produced. Recently, attention in Western

Europe has focused on the migration flows from Sub-Saharan Africa (SSA) to Western Europe. These migration flows and their demographic and economic settings were the topic of a separate session of the lectures in memory of Louis Baeck. The questions put to the experts were:

- How can we explain the slow demographic transformation in Sub-Saharan Africa and what are its implications for emigration from SSA to Western Europe?
- What are the economic prospects for Sub-Saharan Africa? Would sustainable economic growth in SSA contribute to a slow-down of outmigration?

By way of introduction, this paper presents some of the findings of the recent literature on international migration, with a special focus on migration flows to Western Europe. We first provide some data on these flows. Subsequently we discuss determinants of migration, the effects of migration, and migration policies. In the last section we provide some conclusions.

Recent Migration Worldwide and to Western Europe

According to the UN data set on international migration in 1990 there were worldwide 153 million migrants, equivalent to approximately 2.85% of the world population. By 2015 the number of migrants had increased to 248 million or approximately 3.35% of the (increased) world population. This suggests that over a period of 25 years, the worldwide number of migrants had substantially increased, not only in absolute numbers, but also as a fraction of world population.

For a good understanding of these figures, a few remarks are useful. First, in the UN data set, used as the data source in this text, immigrants are defined on the basis of their country of birth. An immigrant is a person born in another country than his or her country of residence. Only if information on the country of birth is not available immigrants are defined in terms of nationality. (For reasons unknown to the author, data for Belgium in the UN data set are based on nationality. This results in a substantial underestimation of the number of immigrants in Belgium compared to other countries.) The use of the country of birth definition implies that children of immigrants born in the host country are not classified as immigrants. Secondly, the UN data provide information on the number of foreign born persons living in a host country at a specific moment of time. In other words they are on the stock of immigrants. An alternative statistic on international migration is the number of foreign born people entering (or leaving) a country over a period of time, usually a year. This is the migration inflow (or outflow). Stocks are the result of past in- and outflows. They are less volatile than yearly flows. Finally, the UN data set aims at providing for each year it covers a complete matrix of the number of immigrants by country of residence and by country of origin. It is likely that the quality of the data provided by a number of countries of residence is uneven and that a number of cells in the migration matrix are the results of guesswork. Worldwide immigration data are therefore likely to have a wider margin of error than data for a number of individual countries.

We now turn to migration into Western Europe, still using the UN data set on immigrant stocks. We distinguish between Central Western and South Western Europe. In our presentation the former includes Austria, the Benelux countries, France, Germany, Ireland, Switzerland, and the UK. South Western Europe comprises Italy, Malta, Portugal, and Spain. The evolution of the number of immigrants living in the two regions during the period 1990 to 2017 is summarized in Figures 5.1 to 5.6.

Figure 5.1 shows that during the period under consideration the number of immigrants both in Central Western and in South Western Europe has strongly increased. In Central Western Europe the increase was steady, from 20 million in 1990 to 37.5 million in 2017. In South Western Europe there was an acceleration during the decade 2000 to 2010, followed by a stabilisation. Figure 5.2 shows that the presence of immigrants also increased if we express it as a percentage of the population. In Western Europe immigrants made up 8.5% of the population in 1990 and more than 14% by 2017. The increase was steeper in South Western Europe where the share of immigrants increased from 2.5% in 1990 to 11% by 2017.

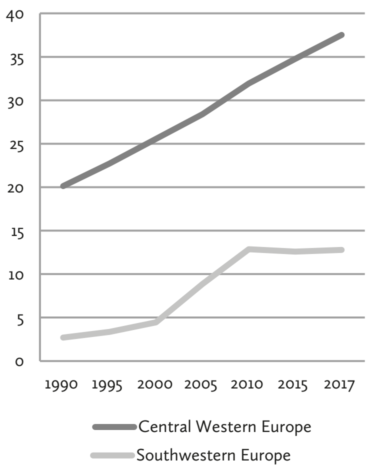

Figure 5.1: Total number of immigrants (million)

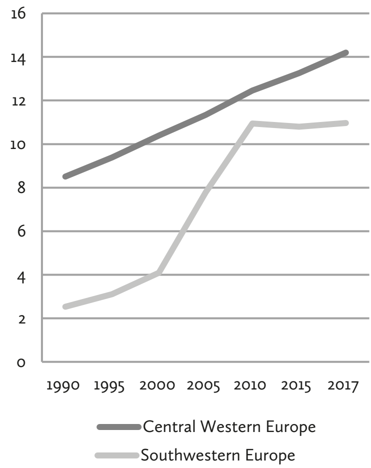

Figure 5.2: Immigrants as percentage of population

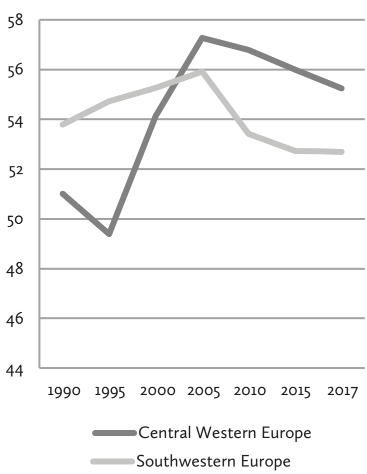

Figure 5.3: Immigrants from 'South' as percentage of total immigrants

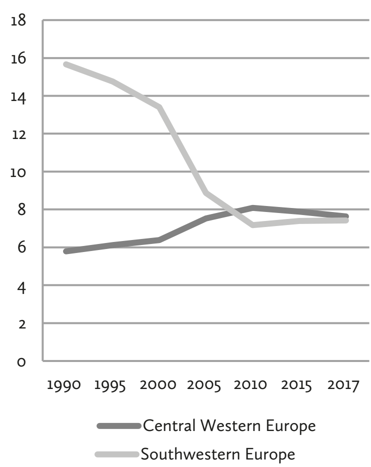

Figure 5.4: Immigrants from SSA as percentage of total immigrants

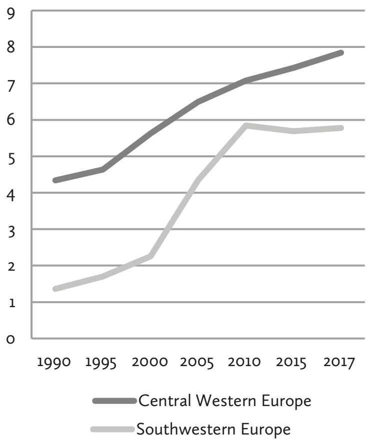

Figure 5.5: Immigrants from 'South' as percentage of population

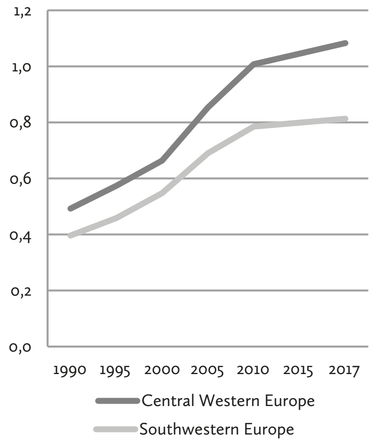

Figure 5.6: Immigrants from SSA as percentage of population

Figures 5.3 and 5.4 provide information on the composition of the stock of immigrants. Figure 5.3 shows that up to 2005 the share of immigrants from the global South (Asia, excluding Japan, Africa, and Latin America) in total immigration increased in Central and even more so in South Western Europe. However after 2005 the share of immigrants from the global South experienced a decrease. By 2017 it was approximately 55% in Central and 53% in South Western Europe. The share of immigrants from SSA in total immigration increased in Central Western Europe, from almost 6% in 1990 to 8% in 2010. Thereafter, it slightly decreased. In contrast, the share of immigrants from SSA in South Western Europe substantially decreased over the entire period under consideration, from more than 15% in 1990 to 7.4% in 2017.

However if we express the number of immigrants from the global South and SSA as a percentage of the population, as is done in Figures 5.5 and 5.6, we observe a steady increase both in Central and in South Western Europe. Remark however that the share of immigrants from SSA in the total population remains modest, in 2017 just above 1% in Central and below 1% in South Western Europe.

Summarizing the evolution over the period 1990 to 2017, the immigrant population in Central and in South Western Europe has increased both in absolute numbers and as a percentage of the total population. By 2017 the share of immigrants in the total population was approximately 14% in Central and 11% in South Western Europe. More than 50% of immigrants are from the global South, but after 2005 the share of this group in total immigration has slightly fallen. Immigration from Sub-Saharan Africa has been rising, but remains modest, both in Central and in South Western Europe.

One final remark: the fact that we have aggregated immigration data for Western Europe in two groups of host countries – Central Western and South Western Europe – does not imply that the individual countries in each of these groups share common migration characteristics or histories. To illustrate this we refer to the very different composition of the immigrant population in the individual host countries in Central Western Europe. In France the three Maghreb countries are part of the top four countries of origin. In Germany the top four is headed by Turkey, followed by Poland, Russia, and Kazakhstan. In the UK, Poland is the main country of origin, followed by Romania, Ireland, and India. And in Belgium Morocco is the top country of origin, followed by three Western European countries, namely France, the Netherlands, and Italy. In each of these host countries, a mix of historical ties, geographical proximity, and European integration explains the quite different patterns of the immigrant population's countries of origin.

Determinants of International Migration

Why do people decide to migrate from their country of birth or residence to another country? And if they decide to leave their country of origin, which country do they move to? It is evident that people can have many different motives for migrating to another country. War, civil war or unrest, persecution, joining family members who did migrate earlier, and studying abroad are some of the reasons underlying migration decisions. But no doubt demographic and economic fundamentals also play an important role.

The demographic evolution is an important determinant of international migration, both on the supply and on the demand side of the picture. Migrants are usually fairly young people. A growing cohort of ages roughly 15 to 30 years raises the number of potential emigrants. On the demand side labour shortages due to a decreasing population at working age is likely to attract migrants. As shown in the contribution of Mustapha Nabli in this volume a combination of these two tendencies may be expected to be a forceful driver of migration from SSA to Western Europe in the decades to come.

The prospect of a better life can also be expected to be an important driver of migration. Labour migration by definition consists of people in search of higher earnings abroad. But an expected higher income may also be a driver of other forms of migration. International refugees for example may decide on the country they move to on the basis of expected income. Empirical research has confirmed this. For example a study by Hatton and Williamson on the European emigration of the late 19th century has shown that the ratio between home and destination countries' wages was a statistically significant determinant of migration from the 'old' to the 'new' world.[3] More recently a number of micro-studies have shown that expected income improvements motivate people to migrate.

If the ratio between home and destination countries' (expected) incomes is a determinant of emigration, economic growth in the country of origin should reduce emigration. Empirical research has shown that this notion is only partly correct. In poor countries a number of – mainly young – people may dream of improving their situation by migrating to a higher income country. But to realize this dream they need resources to cover travel and other costs of migration. As many people do not have these resources, in poor countries there exists a reserve of potential migrants. If the average income level rises and if poor households get a share of the rising incomes, the financial constraint on migration becomes less binding and even more potential migrants are able to realize their emigration dream. Therefore economic growth first stimulates migration and only at a later stage, when incomes have risen to a much higher level, emigration can be expected to taper off.[4]

The three determinants mentioned above – a growing population, the income gap, and income growth that finances the emigration of ever more people – should stimulate migration from SSA to Western

Europe. Other factors point in the same direction: geographic proximity, common languages, and historical ties between the countries of origin and destination.

Another common finding of studies of the determinants of migration is the 'friends and relatives effect'. Migrants are attracted to places where they find people from their own village, region, or country. These people subsequently are able to provide information and support upon arrival. They may also contribute to the travel costs of new migrants. In all Western European countries there are now different diasporas that attract additional migrants.

Finally, we should not forget migration policy. In the 19th century some countries of destination, including Australia and some Latin American countries, initially provided subsidies for migrants from Western Europe. But towards the end of the 19th century anti-immigration sentiment was on the rise. Subsidies for immigrants were abolished. In the United States restrictive legislation on migration was introduced, including the Migration Acts adopted in 1922 and 1924, which introduced country specific annual quotas. More recently, especially after the first oil shock of 1973, anti-migration sentiment has been on the rise in many countries of immigration, including the Western European countries. As a result governments have tightened conditions for immigration. A side effect of more restrictive immigration regimes is the increase of non-legal migration.

Effects of Immigration in Host Countries and Immigration Policy

Public discussion of immigration policy is usually polarized. Quite often it would seem that there are only two policy options: open or closed frontiers. The reality is more subtle. Practically all countries allow some forms of immigration, either because they are obliged to by international law (e.g., the 1951 Convention on Refugees) or because of humanitarian considerations (e.g., family reunion). When we consider labour migration, there is a wide range of possible policies going from fairly open regimes to quite restrictive ones.

The second half of the 19th century was characterized by open frontiers in the countries of immigration of North and South America and in Australia and New Zealand. But that changed towards the end of the century and restrictions were gradually introduced. In the first post-World War II decades, Western Europe started facing labour shortages and individual countries started promoting immigration of low skilled labour through international agreements, first with Southern European countries and then with Morocco and Turkey (i.e., the guest worker schemes). After 1973, Western European governments have tried to reduce immigration by prohibiting immigration of labour migrants without a contract, by adopting restrictive conditions on family reunion and by tightening rules for asylum. More recently, in the framework of the European Union, resources for supervising external borders have been increased and assistance has been provided to non-member countries on the southern EU border in exchange for blocking migration to the EU.

The premise of recent Western European countries' restrictive immigration policies seems to be that immigration is harmful for natives and earlier immigrants: it has a negative effect on their economic situation, it generates fears of decreasing social cohesion, and it creates feelings of insecurity and uncertainty about the future.

At first sight the economic effects of immigration in the host countries would seem to be easy to analyse. But the extensive literature accumulated over the last 30 years and the lack of convergence of its findings suggest that the analysis of the economic effects of immigration faces many methodological problems.[5] At the peril of oversimplification we summarize the findings of this literature, focusing on three issues. First, immigration can contribute to long run economic growth. This is most evident for high-skilled immigration that may contribute to innovation and technical progress. Second, immigration can negatively affect the wages and employment opportunities of natives and earlier immigrants, especially in specific sections of the labour market. Those most affected are low-skilled native workers and earlier immigrants. But as the economy adjusts to immigration, the eventual effect on wages and employment opportunities fades out. And third, the fiscal effect of immigration is difficult to measure as fiscal contributions and costs change with age. If the stock of immigrants is dominated by recent arrivals of young people, the net fiscal contribution of immigrants in a specific year is likely to be positive. For a balanced view we should consider immigrants' fiscal contributions and costs over their lifetime. Fiscal contributions are also linked to immigrants' skills and these may be associated with their countries of origin. If we take into account fiscal contributions and costs over their lifetime, some groups of immigrants contribute positively to government income, others negatively. There are indications that immigrants from non-Western origin have lower net contributions than natives and that they are more likely to have recourse to public income support schemes.

In his well-known book 'Exodus', Paul Collier argues that the main problem with a substantial increase in the number of immigrants may be that it is threatening social cohesion.[6] Ethnic and cultural diversity may result in a loss of trust between citizens and a decreasing solidarity, which are at the core of the Western European (and other) countries' fabric of society. His argument is not so much based on past experience. Rather it is a discussion of what possibly may happen if immigration would continue to increase.

We conclude that the effects of immigration on the economic situation of natives and earlier immigrants are difficult to measure, although most likely small. Opposition to immigration must therefore be grounded in a misperception of its economic effects or on fear of the impact of immigration on social cohesion resulting in feelings of insecurity and uncertainty about the future. Ideally, immigration policy should be based on a thorough understanding of the determinants as well as the effects of immigration.

Concluding Remarks

It is highly probable that in the coming decades migration from SSA to Western Europe will strongly increase. The continuing population growth in SSA and the huge income gap will result in continuing pressure for outmigration from SSA. The paper by Mustapha Nabli in this volume provides data to illustrate this.

Even if SSA can maintain the economic growth rate it has realized since 2000, emigration to Western Europe will not decrease. Indeed income growth provides additional resources to low income groups that hitherto were not able to cover the costs of migration. Increased incomes will make it possible for them to participate in outmigration.

Immigration policies in the Western European countries can exert effects on immigration flows, but it is not likely that they can completely halt them. Between free immigration and complete prohibition there are many shades of policies of controlled immigration. Such policies may have more chances of success than prohibition.

Notes

1. Baeck, L. (1971). *De Wereld is ons Dorp [The World is our Village]*. Tielt: Uitgeverij Lannoo.
2. Baeck, L. (2000). *Text and Context in the Thematisation on Postwar Development*. Leuven: Leuven University Press.
3. Hatton, T., & Williamson, J. (1998). *The age of Mass Migration: Causes and Economic Impact*. Oxford: Oxford University Press.
4. See also the contribution of Marijke Verpoorten in this volume.
5. For OECD countries, see e.g., Burzinsky, M., Docquier, F., & Rapapot, H. (2018). The changing Structure of Immigration to the OECD: What Welfare Efects on Member Countries? *CESifo Working Paper 6992*. For a survey of studies on the effects of immigration in the United States, see National Academies of Sciences, Engineering and Medicine (2017). The Economic and Fiscal Consequences of Immigration. *The National Academies Press*.
6. Collier, P. (2013). *Exodus. Immigration and Multiculturalism in the 21st Century*. Penguin Books.

6. Europe and Africa

Facing the Greatest Migration Challenge?[1]

Mustapha Kamel Nabli

International migration has been one of the main socio-economic issues of the last quarter of the 20th and the beginning of the 21st centuries. Over this period migration into the high income countries of Europe, North America, and Oceania has drastically increased and immigration has been a prominent topic in public debates. Demographically Western Europe has changed from a net emigration to a net immigration area. Two migration corridors – from the Eastern Mediterranean into Eastern and onwards into Central Western Europe, and from North Africa into South Western Europe – have regularly dominated the news, highlighted by the death by drowning of tens and sometimes hundreds of migrants.

However what has been happening across the Mediterranean could be just the beginning of a much bigger challenge to come. Demographic and economic forces may be creating the greatest migration challenge ever, which may be playing out over the next few decades, involving Sub-Saharan Africa (SSA) and Europe. But politics is pulling in another direction, leading to much trouble ahead.

Three major forces create push and pull factors working in the same direction towards greater international migration from SSA to Europe: unprecedented demographics in SSA (and Europe), huge income differentials between these two regions, and the mismatch between supply (resulting from education) of and demand (associated with structural transformation) for skills in SSA. In the following sections we discuss each of these forces.

Unprecedented Demographics in Sub-Saharan Africa: Strong Population Growth

Taking current economic conditions constant and considering just demographic changes, huge migration pressures are to be expected. Push factors in SSA and pull factors in Europe will be acting in the same direction towards a substantial rise in migration from SSA to Europe.

In this section we illustrate this using data from the 2017 UN population projections. We use 30-year increases rather than yearly rates of growth. This makes it possible to study long term changes in the population. The 30-year increases are fairly continuous, as for successive years they are largely overlapping.

Figure 6.1 shows that over the last 40 years the population of Sub-Saharan Africa more than doubled over a 30-year period; more precisely it doubled over every 25 years.[2] The highest rate of increase since 1965 was above 127% every 30 years, reached in the years 1995-2010. The closest experience of fast population growth was reached in the Middle East and North Africa (MENA) in the 1980s, but this was the case only for a relatively short period of time. In the 1980s the 30-year MENA population growth rate exceeded that of SSA.

According to the UN population projections the SSA population will continue to increase by more than 120% every 30 years until 2030. In absolute numbers the SSA population increase will continue to rise, from 561 million between 1985 and 2015 to 1098 million from 2020-2050. This is to be compared to the largest increases in population observed over 30 years in the past: 517 million in China from 1965 to 1995 and 534 million in India from 1980 to 2010.

We now turn to the working age population, defined as the population of ages 15 to 64. In SSA the 30-year rate of increase has been accelerating from 100% every 30 years in the 1970s to more than 120% since the 1990s. The slowdown has now started. But the increase in absolute numbers is skyrocketing: from 313 million during the period 1985-2015 to a projected 755 million during 2020-2050. This increase will be larger than in any region in history: the largest increases over 30 years in the past were observed in China, 440 million from 1975 to 2005, and in India, 418 million during 1990-2020. Note the declining working age population in Europe since 2005-2010. In the future the

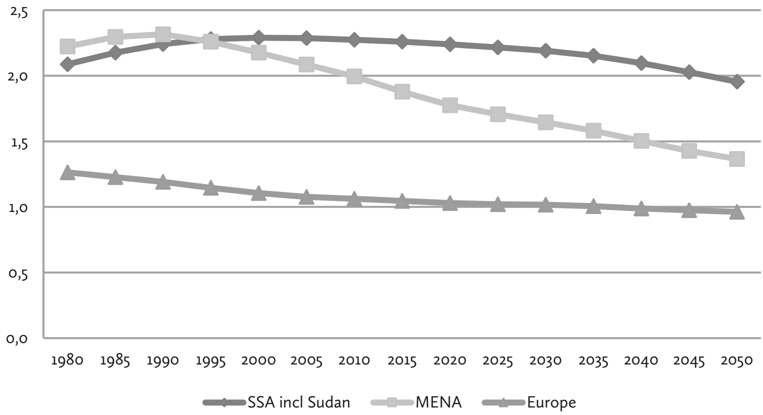

Figure 6.1: 30-year population increase, multiples

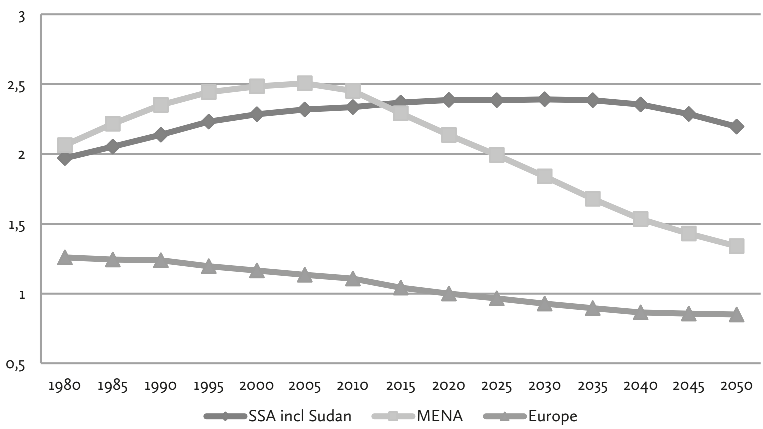

Figure 6.2: 30 year working age population (age 15-64) increase, multiples

working age population in Europe is projected to decline over 30-year time spans by 10 to 15%.

Underlying these figures for SSA is a strong increase in the number of youth (aged 15 to 24) which is projected to more than double between 2015 and 2050. At present (2018), the number of youth in SSA (198 million) is about the same as in China (182 million). But in SSA it is

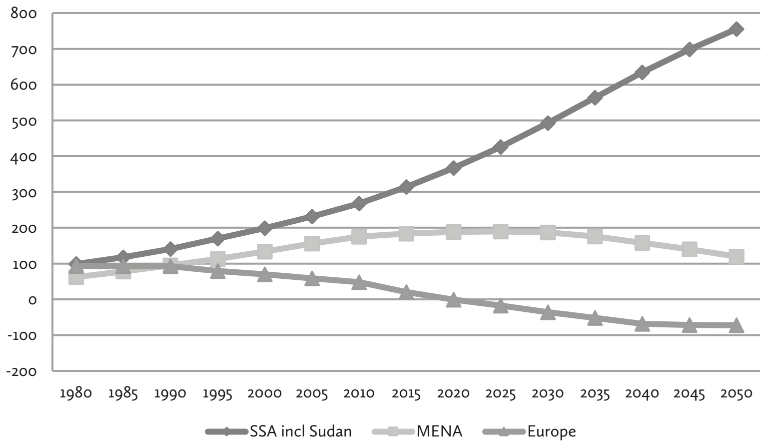

Figure 6.3: 30 year working age population (age 15-64) increase, numbers (million)

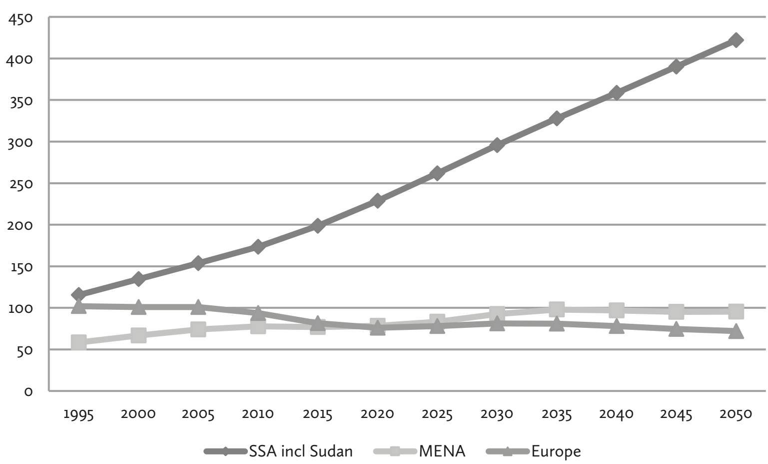

Figure 6.4: Youth population (15-24), numbers (million)

projected to rise by more than 200% (to 421 million) by 2050, whereas in China it is projected to fall to 132 million.

To project the labour force, we not only need projections of the working age population but also assumptions on the labour force participation (i.e., the percentage of people at working age who are actually gainfully employed). Based on simple assumptions about future labour force participation rates, the 30-year increase in the labour force in SSA is projected to increase from 252 million currently (2018) to more than 500 million by 2050. The number of additional entrants to the labour force, which was 10 million a year in the years 2010-2015, would have jumped to 20 million a year by 2045-2050. In all other regions of the world the rate of increase of the labour force is projected to remain stable or to decrease. In China the labour force is projected to start decreasing by 2030. The European labour force is already starting to decline.

The combination of a huge expected increase in labour supply in SSA and a decreasing labour supply in Europe is a first factor underlying the migration challenge that Europe will face in the coming decennia. In section 2 we discuss a second factor, the huge income differential between Europe and SSA.

Huge Income Differential between Europe and Sub-Saharan Africa

It is well known that there exist wide income differentials between per capita Gross Domestic Product (GDP) in European and Sub-Saharan countries. Even with substantially higher GDP growth rates in SSA than in Europe, this income differential will widen in absolute terms, strengthening the incentives for migration as never before. To illustrate this effect, we present some numbers from scenarios on economic growth produced by the Emerging Markets Forum.[3]

In all scenarios the annual GDP growth rates are substantially higher in SSA than in the advanced countries (including Europe), reflecting the opportunities of fast growth in low income countries.[4] Even with higher population growth rates in SSA, GDP per capita would rise at a higher rate in SSA than in Europe. The relative income differential (per capita GDP in SSA expressed as a percentage of Europe) would increase.

However, the absolute income differential (the difference between per capita GDP in Europe and the advanced countries expressed in money), will continue to increase in the foreseeable future. The reason is that in any year the increase of per capita GDP in dollars (corrected for inflation) is equal to the level of per capita GDP in the base year multiplied by the growth rate of per capita GDP. In 2015 per capita GDP in the advanced countries was more than 13 times that of SSA. Thus, only if the growth rate in SSA would be 13 times higher than in Europe, would the absolute income differential decrease.

According to the central scenario of the Emerging Markets Forum publication, the annual growth rate of world GDP would be 3.3%, while it would be 2% in the advanced countries and 5.1% SSA.[5] The resulting per capita GDP figures and the absolute income differential are given in Figure 6.5. Per capita GDP in the advanced countries increases from approximately 46.000 dollars in 2015 to 84.000 dollars by 2050; the implicit annual growth rate of GDP per capita is 1.7% (lower than the assumed GDP growth rate due to population growth). In SSA per capita GDP increases from approximately 3300 dollars in 2015 to 8700 dollars by 2050, implying an annual growth rate of 2.75%. This is substantially below the assumed GDP growth rate of 5.1% due to the continuing relatively high population growth in SSA. Under this central scenario, per capita GDP in SSA would rise from approximately 7.5% of advanced countries' GDP in 2015 to 10.5% in 2050. But the difference in per capita incomes expressed in dollars would rise from 42.500 dollars in 2015 to 75.200 dollars by 2050. Thus, under this scenario the faster growth of per capita GDP in SSA is far from sufficient to compensate for the substantial initial per capita income differential. As a result, the pressure for emigration would only increase.

Figure 6.6 presents the results of a more optimistic scenario under which the annual GDP growth rate would be 6.8% in SSA, compared to 5.1% under central scenario. Under this scenario the GDP growth rate in the advanced countries would only marginally be higher than in the central scenario. Figure 6.6 shows that under this scenario per capita GDP in SSA would rise to more than 15.000 dollars by 2050. The absolute difference between per capita GDP of the advanced countries and SSA in 2050 would be smaller than under the central scenario (approximately 70.000 dollars as compared to 75.000 dollars). Nonetheless this difference would still be substantial.

The conclusion must be that even in the best of cases, income differentials will be huge, creating strong pressures for migration. To limit

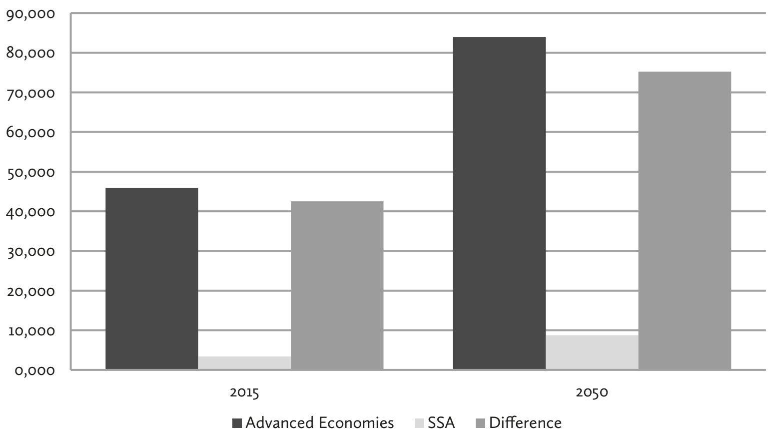

Figure 6.5: GDP per capita in 2015 and 2050, purchasing power parity, US dollars of 2011, central scenario

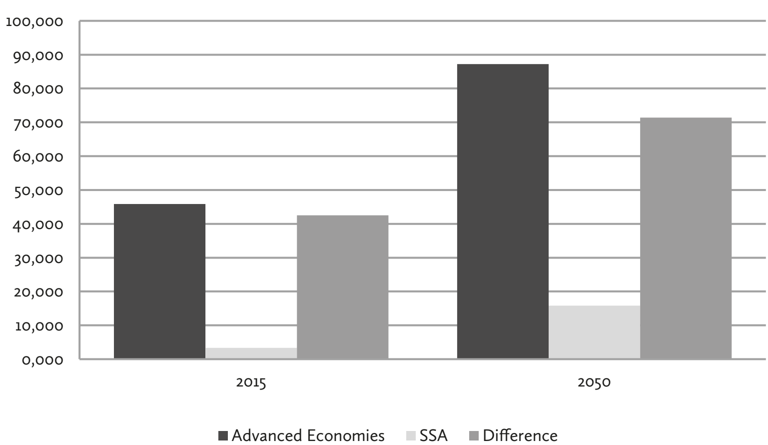

Figure 6.6: GDP per capita in 2015 and 2050, purchasing power parity, US dollars of 2011, optimistic scenario

income differentials with Europe, SSA should use the opportunities for high income growth. But achieving its high income growth potential depends on successful structural transformation. Not achieving this potential will raise income differentials. In addition, it would create incentives for migration due to the mismatch between supply and demand for skills. We discuss this in the following section.

Education, Structural Transformation, and Migration

Achieving high income growth rates and exploiting the opportunities offered by a predominantly young population (the so-called demographic dividend) depend on success in matching supply and demand for skills. The supply of skills, the availability of human capital, is driven by demography and education policies. The demand for skills is driven by structural transformation, the movement of factors of production from low to high productivity economic activities.

Nothing guarantees success in matching supply of and demand for skills. Failure in matching may produce disastrous outcomes: unproductive investment in education, a gap between expectations of young people and reality, and ensuing political unrest. It is also likely to produce increased pressure for migration. Incentives for migration are probably stronger for those with higher education and skills, due to both push and pull factors. Low returns to education in SSA are pushing emigration of skilled and highly skilled labour, while high returns in Europe attract migration. In addition to income differentials, the quality of governance and of living conditions favour migration from SSA to Europe.

In this section we compare the interplay of education, structural transformation, and migration in SSA with the experience in Asian and Middle East and North African (MENA) countries.

In most Asian countries, the supply of skills was geared towards meeting demand. The focus of education policy was more on secondary than on tertiary education. In 1985, out of a sample of six countries (China, India, Indonesia, Malaysia, Republic of Korea, and Thailand) in four countries the percentage of people aged 15 and over with completed secondary as highest level of education (henceforth called adult education) varied from 5% (in Thailand) to 18% (in Malaysia). The outliers were India, with less than 1% and the Republic of Korea with 32%. Between 1985 and 2010 this percentage increased substantially: by 2010 in four of the six countries between 19 and 25% of the adult population had completed secondary education as highest level attained.

The outliers were Malaysia which realized a dramatic increase in completed secondary education, reaching 40% of the adult population, and the Republic of Korea, where starting from a relatively high level it increased by three percentage points only.

As for tertiary education in 1985 the percentage of the adult population with completed tertiary was rather low, varying from less than 1% in Indonesia to 3% in Thailand. Again, the Republic of Korea was the exception with 8.5% of the adult population holding a tertiary degree. The increase between 1985 and 2010 was also rather moderate: by 2010 between 3 and 10% of the adult population had completed tertiary education. The exception once again was South-Korea with 35% of adults with completed tertiary education.

By 2010, all six countries had gone through a strong structural transformation with adequate demand to meet the supply of skills. Labour had moved from agriculture to manufacturing and services and the economies were moving up the ladder from low complexity and low capital intensity to more complex and more capital intensive activities.

As a result of this development there were generally low levels of unemployment for both secondary and tertiary education graduates and, with the exception of India, limited pressure for international migration.

The picture was different in the Middle East and North Africa. In most MENA countries for which data are available, we observe a very strong growth in the supply of skills, as measured by secondary and tertiary education graduates. The rapid increase of the percentage of adults with secondary (from an average of 9% in 1985 to 20% in 2010) and tertiary education degrees (on average from 2.5% in 1985 to 6.5% in 2010) was comparable to what happened in the Asian countries. Tunisia stands out as the country with the strongest increase in the percentage of the population with completed tertiary education, from less than 2% in 1985 to more than 8% in 2010.

The demand for skills in the MENA region was far less explosive. There was some movement of labour from agriculture to manufacturing and a slow increase of complexity and capital intensity of economic activities. The share of industry in employment was decreasing. The MENA economies continued to generate low productivity jobs, with weak demand for skills.

As a result, there was a mismatch between supply of and demand for skills and high and increasing levels of unemployment of both secondary and tertiary education graduates. For example, in Egypt and Tunisia the unemployment of secondary education graduates rose from respectively 14 and 13% in 1985 to 17 and 20% in 2010. Unemployment of tertiary education graduates was even higher: 22% in Egypt and 30% in Tunisia in 2010. This contributed to political and social unrest, most notably to the 2011 uprisings. It also resulted in continued pressure for migration to Europe.

The situation in SSA is more complex, as there are 49 different countries, each with their own resources, cultures, institutions, and experiences. But by and large the evolution over the past 25 years shows two common characteristics: there has been overall progress in the supply of skills, but limited structural transformation. The evolution in SSA has been more akin to the experience of the Middle East and North Africa than to that in the six Asian countries.

As to the supply of skills, the educational achievements in SSA are lower than those in the Asian countries and MENA, both at the secondary and at the tertiary level. But in most countries, there has been substantial progress.

As illustrated in Figure 6.7 in many countries there was a substantial increase in the percentage of the population with completed secondary as highest level of education. A notable exception was Zimbabwe, where the number of secondary education graduates as highest level attained fell by almost 50%. On the upper end of the distribution we observe large increases in Kenya, Malawi, and South Africa, as well as in other countries not included in Figure 6.7.

As to tertiary education, in 1985 in most countries the number of graduates with completed tertiary as percentage of the adult population was lower than 1%. Over the following 25 years the number of tertiary education graduates increased substantially in most of the countries. But given the low level in the base year, the percentage of adults with completed tertiary education remained lower than 2%. Notable high increases were realized in Kenya and Gabon (the latter not included in Figure 6.8). In the years to come large increases can be expected in many countries.

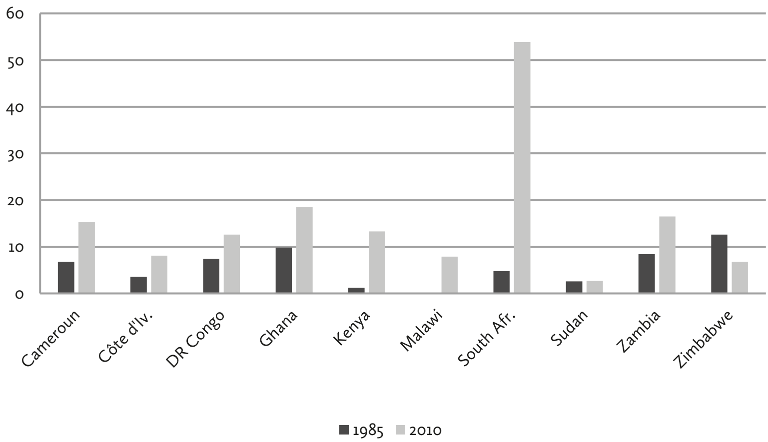

Figure 6.7: Percentage of population age 15 and over with completed secondary education as highest level attained

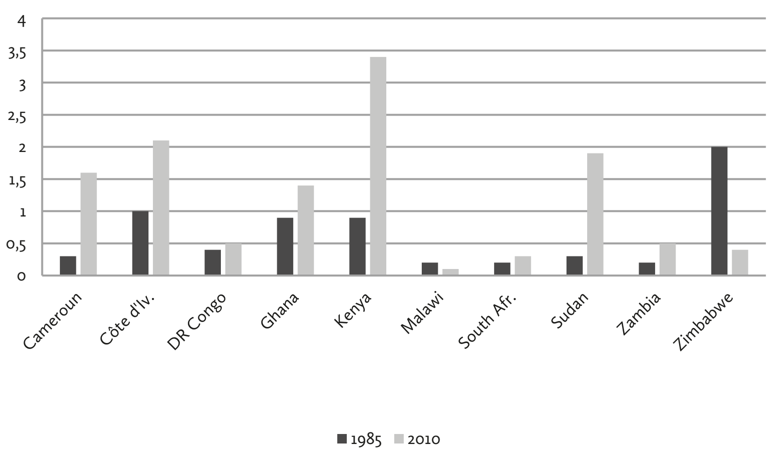

Figure 6.8: Percentage of population age 15 and over with completed tertiary education

On the demand side there has been some structural transformation. Labour has moved from agriculture into services (ICT, tourism) and capital intensive manufacturing. But most jobs are characterized by low levels of complexity. The share of industry in employment has started to decrease and there is talk of early deindustrialisation.

The outcomes of this evolution in terms of unemployment show no single pattern. In countries without significant increases in the supply of skills relative to the adult population and with limited structural transformation, no major mismatches can be found between supply of and demand for skills, and unemployment rates remain low. Some countries with both low education and low economic growth have experienced high unemployment; examples are the DR Congo and Mali. An interesting case was Kenya, which experienced high education gains and low unemployment rates. But in a few countries the combination of large increases in secondary and/or tertiary education and limited structural transformation has resulted in high rates of unemployment. Examples of high growth of graduates with secondary education as highest level attained were South Africa and Botswana with respectively 26 and 25% of the labour force unemployed. Côte d'Ivoire has a strong increase of tertiary education graduates and an unemployment rate of 27%.

What are the prospects for structural transformation in SSA? There is an on-going big debate about best pathways to structural transformation in SSA. The East Asian model of a manufacturing export-led strategy may not be available anymore with industrial revolution 4.0. A number of economists are in favour of an agricultural transformation based on Africa's comparative advantage. Their argument is that SSA has a large potential of unused arable land. Other economists are proponents of a modern services based strategy. They think of services with characteristics similar to those of manufacturing: tradable products, high productivity, economies of scale, and agglomeration economies. Examples include ICT, tourism, transport. But it seems fair to state that in SSA overall prospects for strong structural transformation are weak and that the potential for large mismatches between supply of and demand for skills is very high. Therefore, pressures on migration are likely to become stronger.

In Conclusion: a Major Challenge for Europe

Economic pressures and incentives for migration from SSA to Europe (and to North Africa) are likely to be strong over the next few decades, until the end of the 21st century. Sheer numbers, income differentials, as well as social and political unrest, resulting from the mismatch between expectations and reality, push in the same direction. Other important factors may be playing out with significant implications, such as the impact of climate change and the volatility of incomes.

The political incentives and pressures in Europe go in the other direction, towards the closing of borders and stronger restrictions on migration. Given the expected magnitude of the pressures for migration such policies may not be sustainable in the long run. Migration from Sub-Saharan Africa to Europe will be a major challenge for the 21st century which will require continued attention and innovative thinking.

There are many implications for policy actions and recommendations, both in SSA and in Europe. In Africa strong policies and strategies to reduce fertility and better manage population growth, to focus education policies on secondary education and vocational training, and to achieve strong and rapid structural transformation are required.

Europe should support African development strategies through trade openness to its exports, increased direct investment and support for diversification and technology upgrading. Europe should also develop more open and balanced policies for managed migration taking into consideration the relative supply of skills, and it should invest in and support the training and education of young people in SSA to generate the supply of skills which are in demand in Europe. This would mitigate the impact of migration of the skilled on the development of the countries of origin.

Notes

1. This paper is a short summary of a presentation at a Conference in Brussels, September 11, 2018 at the University Foundation.
2. The following data include Sudan in Sub-Saharan Africa, while UN data include this country in North Africa.
3. See Kohli, H. S. (2016). *The World in 2050: Striving for a More Just, Prosperous and Harmonious Global Community*. Oxford: Oxford University Press.
4. The data are for GDP at Purchasing Power Parity, $ 2011.
5. Projections are until 2050 and use 2015 as base year.

7. The Biggest Migration Challenge Ever

Marijke Verpoorten

Population in Africa increased almost sixfold in the past seven decades, from 229 million in 1950 to 1.3 billion today, and it will continue to rise, according to one United Nations projection ('the medium'), to around 4.5 billion in the year 2100, after which it would stabilize (see Figures 7.1.a to 7.1.d).

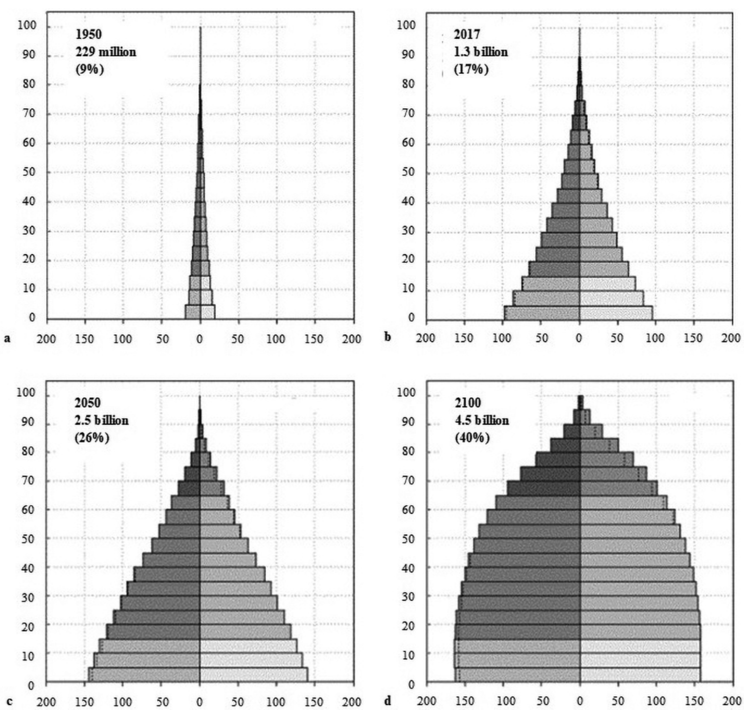

Figure 7.1: Author's compilation from data retrieved from United Nations, World Population Prospects 2017 with regards to the population in Africa in 1950 (a) and 2017 (b), and the expected population in 2050 (c) and 2100 (d). The y-axis indicates age cohorts; the x-axis gives population in millions

Africa's population structure will also change in this period: Africa will be the only region where the share of the working age population (aged 15-64) will increase, notably from 56% today to 64% in 2100. This increase will not necessarily be a demographic gift. Whether it will stimulate development will depend on the ability of the economy to absorb and productively employ the extra workers.

If the labour supply cannot be absorbed locally, the push to migrate will increase. Moreover, large numbers of unemployed youth also increase the risk of political instability, which could further fuel migration. As Professor Nabli observes in his contribution to this volume, Europe is at the eve of the biggest migration challenge it has ever faced.

Malthusian Perspective

In the popular view, the prospect of a vast population explosion is usually associated with doomsday scenarios, including poverty, famine, and war. That Malthusian perspective can be overstated: the continuation of the demographic explosion *by itself* is unlikely to make Africa poorer or more violent.

Thomas Malthus wrote that 'the power of population is so superior to the power of the earth to produce subsistence for man, that premature death must in some shape or other visit the human race'.[1] However, soon after the publication of his essay, the Industrial Revolution took off, bringing about continued productivity increases that allowed production growth to outpace population growth. In particular, since 1800 world population increased sevenfold, but production increased 73-fold, resulting in a more than tenfold increase of average per capita production.

That production outpaced population is not only true globally, but also for Africa. In the period 1800-2017, Africa's population rose more than 12-fold, but its production increased 55-fold. In the more recent period 1960-2016, when its population increased almost fivefold, GDP in Africa increased more than sevenfold. The share of its population living in extreme poverty declined, from 69.1% to 44.5%. So overall, Sub-Saharan Africa has not suffered from a Malthusian catastrophe.

However, did it experience local Malthusian catastrophes? After all, hunger and famine are still with us, as are violent conflicts.

Land Scarcity and the Rwandan Genocide

On the eve of the genocide in 1994, Rwanda was Africa's most densely populated non-island nation. It has been demonstrated both in quantitative and qualitative work that land scarcity added to the intensity of the genocide. For instance, in one of my studies on Rwanda, I demonstrate that in high density areas with many young single men, less Tutsi survived the genocide.[2]

However, the estimated effects are relatively small, and even scholars who argue that land scarcity played a role in the Rwandan genocide agree that *it did not cause the onset* of the genocidal campaign.[3] Instead, the genocide resulted from a combination of historical and macro-political factors.

Thus by itself, the continuation of the demographic explosion is unlikely to make Africa poorer or more violent. Institutions are the key, both to stimulate an economic transformation and to preserve political stability.

Institutional Perspective

The insight that institutions are key emerges from the body of research on the link between demography and conflict. The literature indeed documents correlations between a youth bulge and political conflict, and between land scarcity and conflict intensity. However these correlations are conditional in the sense that they only occur in the absence of institutions that spur agricultural innovation, that allow youth to express grievances in a non-violent way, that mitigate the sharpest (horizontal) inequalities, etc. This is not unlike the argument made by Amartya Sen that famines do not have a natural cause, but an institutional one: a sudden fall of entitlements.[4] Hence his claim that famines do not occur in functioning democracies.

Unfortunately, the democratic record in Africa is poor. Almost all of its nations are categorized as 'not free' or only 'partly free' by Freedom House. On average, Africa also scores low on the worldwide governance indicators, and has made little, if any, progress in the past decades.

At this point it is worthwhile coming back to the Rwandan case. Although Rwanda qualifies as 'not free' and scoring very low on 'voice and accountability', it has made tremendous progress on other good governance indicators, such as governance effectiveness, security, rule of law, and control of corruption.

Most likely, these improvements in governance partly account for the fact that production growth in Rwanda has greatly outpaced population growth in the past 20 years, resulting in a doubling of GDP per capita since 2000. This does not mean that violence will no longer re-occur in Rwanda. There is severe political and societal repression, and power is concentrated in the hands of the Tutsi minority. And, as in the pre-genocide era, chains of accountability are running upwards not downwards. However, the point here is that if violence again breaks out in Rwanda, it will not be because of land scarcity *per se*, but because of the absence of inclusive institutions.

Policy Perspective

According to the institutional perspective, population explosion in Africa does not imply that the continent will be poor and violent. However, when it comes to migration, even if Africa grows prosperous and becomes peaceful, the pressure to migrate to Europe will increase.

Firstly, regardless of the income levels and distribution, three billion people will be added to Africa's population. Second, contrary to what is often thought, development does not necessarily reduce migration. In fact, it has been demonstrated that the impact of income on migration is positive until countries reach a level of around 11.000 dollars per capita (PPP). Prior to that threshold, a rise in income expands the ability to migrate, mainly because greater access to networks and financing alleviates the most stringent financial constraints on migration.

Average incomes in Africa are still far below that threshold (see Figure 7.2).[5] For instance, to come back to Rwanda one last time, at

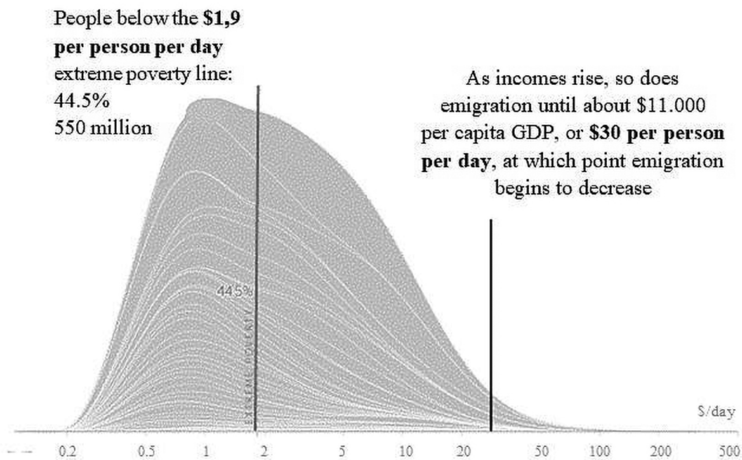

Figure 7.2: Author's compilation of the distribution of Africa's incomes in 2015, with indication of the poverty line and migration threshold, based on Gapminder, Clemens (2014), and World Development Indicators.

the country's current income of 1.900 dollars per capita, and a per capita growth rate of income of 4 to 5%, it would take over a generation (40 years) for the country to pass that threshold.

Regardless of whether Africa will be 'poor and violent' or 'prosperous and peaceful', we are at the eve of the biggest migration challenge Europe has ever faced. Our policymakers have to prepare for it, and deal with it, preferably in an organized rather than a chaotic way, in order to realize the potential for a win-win evolution. This potential is very real. After all, Europe's population will soon count many shades of grey, and adding youngsters to Europe's age pyramid can improve the quality of lives, both at the bottom and the top of the age pyramid.

Notes

1. Malthus, T. (1798). Essay on the Principal of Population as it Affects the Future Improvement of Society. *Dt.: Eine Abhandlung über das Bevölkerungsgesetz, 2.*
2. Verpoorten, M. (2001). Leave none to Claim the Land: A Malthusian Catastrophe in Rwanda? *Journal of Peace Research, 49,* 547-563.
3. Sen, A. (1981). *Poverty and Famines: An Essay on Entitlement and Deprivation*. Oxford: Oxford University Press.
4. In Verpoorten (2001), I estimate that an increase in pre-genocide population density by 100 inhabitants per km^2 resulted in a rise of the genocide's death toll by 1 to 2%, and that an increase in pre-genocide share of single men aged 25-35 by 10% led to a rise of the genocide's death toll by 2 to 3%.
5. The income threshold was measured by Clemens (2014) in 2005 PPP US$ terms. The income distribution given in Figure 7.2 uses 2011 PPP US$. For Africa, the income levels expressed in 2011 PPP US$ are about 60% higher than those measured in 2005 PPP US$. This is why the threshold as mentioned in the article (6.000-8.000) is increased by 30%. See Clemens, M. (2014). Does Development Reduce Migration? *IZA Discussion Paper, 8592.*

8. Migration Dynamics and International Partnerships

Stephan Parmentier

The keynote presentation by Mustapha Nabli provides many interesting facts, as well as challenging thoughts, about the present and future of migration flows from various parts of the world into Europe. The following short comments will focus on some aspects, particularly in relation to migration from Sub-Saharan Africa to the European Union. They do not stem from the discipline of economics, but find their sources in the fields of the sociology of crime, law and human rights. Furthermore, they have no ambition of being exhaustive, but merely wish to serve as points for further reflection and action concerning this prime topic of international relations.

Push and Pull Factors of Migration

According to Nabli, migration flows to Europe are very likely to increase in the coming decades, particularly from Sub-Saharan Africa, and will pose major challenges to politics and the economy. He identifies three major forces of push and pull factors of migration: (a) rapidly increasing demographics in Sub-Saharan Africa, (b) strong income disparities between Africa and Europe, and (c) a mismatch on African labour markets between supply and demand.

Obviously, these demographic and economic forces are very real and therefore highly likely to exert a major influence on the future of migration flows into Europe. Next to them, it seems important to sketch a broader picture of migration flows by looking more closely at a variety of factors that go beyond the realm of economics. Migration studies make a classical distinction between 'push factors' that encourage people to leave their country of origin, and 'pull factors' that draw them to a specific country of destination.[1] Push factors certainly include economic factors, like the lack of job opportunities, economic hardship, and extreme poverty. Moreover, they include social and legal factors, like intolerance and discrimination, insecurity and crime, persecution, armed conflict and extreme violence. And more than ever before do push factors relate to the intense and long-term effects of climate change in communities and regions all over Sub-Saharan Africa. On the other hand, economic conditions obviously are also pull factors, e.g., in the form of job opportunities, economic prosperity, and the possibility of sending remittances to family and relatives in the home country. Pull factors also relate to safety and security in a country, and the absence of persecution and violent conflict. The presence of family and relatives will play an important role to draw people to a specific destination, as well as the information and the image circulating about the new country. It should be highlighted that push and pull factors are dynamic, as they can change across countries and regions, as well as over time. Moreover, they are heavily influenced by differences in individual living conditions, as well as by class, race, and gender. An often overlooked mechanism lies in the intermediate structures and procedures that allow people to migrate from one place to another and one country to another. Family reunification and asylum procedures in the countries of destination constitute important legal and policy frameworks used by potential migrants, but human smuggling and human trafficking gain rapid ground as 'alternative' routes to migrate to Europe.[2]

In order to understand migration dynamics even better, it is crucial in our view to establish closer conceptual and policy linkages between two aspects, namely human rights violations on the one hand, and crime and corruption on the other hand.[3] Both aspects are interrelated, not only in Europe but also in Sub-Saharan Africa. Framing the many economic, social, and legal problems in Sub-Saharan Africa in terms of human rights violations is of course not so new: extreme poverty in certain regions, poor conditions for work, housing, health, education, and frequent violent conflicts all belong to the core violations of economic and social rights documented by many international and regional organisations. On the other hand, far less attention has been given to the existence and effects of crime and corruption issues in

Sub-Saharan Africa. The Pew Research Center has argued that crime and corruption are the top problems in emerging and developing nations, with 83% of people across 34 such economies saying that crime is a 'very big' problem, and three quarters stating the same about corrupted political leaders.[4] Specifically for 7 countries of Africa (Nigeria, Ghana, Uganda, Tanzania, Kenya, Senegal, and South Africa), the median figures are 84% and 85% for crime and corruption respectively. Corruption frequently leads to poor economic and social performance, to more insecurity, and to ineffective criminal justice systems. As such, it constitutes a major factor contributing to violations of civil and political human rights, as well as economic and social human rights. As a result, the combination of human rights violations and crime and corruption constitute crucial factors in gaining a broad understanding of migration dynamics from Sub-Saharan Africa into Europe.

Policies of Migration and Development

Nabli in his contribution advances a second key argument, namely that European politics are pulling in directions that may lead to 'much trouble ahead'. It is based on his assumption that labour migration to Europe will continue to increase in the next decades, due to the three major forces described above. He warns that restrictive European migration policies may be serving populist discourses in the short run, but are not likely to be tenable in the longer run.

While it falls outside of the scope of this short contribution to evaluate EU migration policies in greater detail, it can be argued that policies emphasising restrictive measures directed at excluding and repressing migrants from entering Europe are not likely to be successful unless complemented by other, more inclusive, policies. Building and maintaining a 'Fortress Europe' is not only very costly in monetary and human terms, but it may also lead to new human rights violations, as illustrated by recent practices of some countries to 'push back' migrants to the shores and the detention camps of Northern Africa.

Examples of additional policies aiming at investing in the development of countries and regions of origin in Sub-Saharan Africa already exist. The EU since its early years has initiated international trade policies with many regions of the world, most notably with the ACP countries (Africa, the Caribbean, and the Pacific). The current Cotonou Agreement (2000-2020) is geared at eradicating poverty and promoting sustainable development in these 79 countries, by strengthening economic links, trade exchanges, and political cooperation. For this purpose, it involves many actors in the countries concerned, including central and local authorities, the private sector, trade unions, and civil society at large.[5] A second example lies in the African-EU Partnership launched in 2000 as a political channel for economic, social, and political cooperation between the two continents in several priority areas.[6] The current four priority areas defined in 2018 include: investing in people (through education, science, technology, and skills development); strengthening resilience, peace, security, and governance; mobilising investments for Africa's structural and sustainable transformation; and migration and mobility. EU policy documents describe this Africa-EU collaboration as a strategic partnership of equals, aiming at sustainable transformation built on Africa's strengths, and including multiple partners for multiple problems.[7] Last but not least, several member states of the EU have also signed the Global Compact for Safe, Orderly and Regular Migration of the United Nations at a special conference in Marrakech, Morocco, in December 2018.[8] This UN Compact provides a cooperative framework for states to ensure that international migration can take place in a safe, orderly, and regular manner. It consists of four main parts: the vision and the guiding principles, twenty-three objectives, a section on implementation, and a section on follow-up and review. While the Compact is based on human rights, it does not add any new rights but largely refers to existing instruments and therefore is a 'codifying' instrument more than a 'modifying' one. Although non-binding in nature, and leaving lots of flexibility to signatory states for its implementation, it is likely to guide the policies and politics of several EU member states in the near and long-term future (to the extent of even provoking the collapse of the Belgian federal government in December 2018).

Migration, Development and Human Rights

That the UN Global Compact for Migration was signed on 10 December 2018 was certainly no coincidence, as it marked the 70th anniversary of adopting the Universal Declaration of Human Rights. This Compact, and many other instruments, procedures, and frameworks find firm inspiration in the elaborate human rights architecture, international and regional, as developed after the Second World War.

The same human rights framework that underlies the UN Compact has also given rise to the so-called 'human rights approach to development' (HRBAD) in academia and practice.[9] It can be argued that this approach is rooted in three major principles: (a) it encompasses all human rights covered by major international and regional instruments (civil, political, economic, social, cultural, and even third generation rights); (b) it adopts several basic values, such as equality and non-discrimination, accountability, and participation and inclusion; and (c) it tends to lean towards a 'capabilities approach' with a focus on the development of human potential.

Particularly these human rights based approaches seem very fruitful to constitute the new foundation for 21st century policies of migration and development in full respect of human dignity.

Notes

1. European Communities (2000). *Push and Pull Factors of International Migration: A Comparative Report*. Luxemburg: Office for Official Publications of the European Communities.
2. Myria (Federal Migration Centre) (2018) *Annual Report 2018. Trafficking and Smuggling of Human Beings. Minors at Major Risk*. Brussels: Myria.
3. Parmentier, S., & Weitekamp, E. (2007). Introduction: On the Double Relationship of Crime and Human Rights. In S. Parmentier & E. Weitekamp (eds.), *Crime and Human Rights*, Series in Sociology of Crime, Law and Deviance, 9, 1-8. Amsterdam/Oxford: Elsevier/JAI Press.
4. Pew Research Center (2014). Crime and Corruption Top Problems in Emerging and Developing Countries. Available at www.pewglobal.org/2014/11/06.
5. More information available at https://ec.europa.eu/europeaid/regions/african-caribbean-and-pacific-acp-region_en
6. More information available at: https://africa-eu-partnership.org/en/partnership-and-joint-africa-eu-strategy
7. European Political Strategy Centre (2017). *The Makings of an African Century. Where African and European Ambitions Meet*. Brussels: European Commission, European Political Strategy Centre.
8. For more information: Global Compact on Migration, Intergovernmentally Negotiated and Agreed Outcome (13 July 2018), at: https://www.iom.int/global-compact-migration. See also: Wouters, J. & Wauters, E. (2019). The UN Global Compact for Safe, Orderly and Regular Migration. Some Reflections. In K. Lemmens, S. Parmentier, & L. Reyntjens (eds.), *Human Rights with a Human Touch. Liber Amicorum Paul Lemmens* (375-393). Cambridge/Antwerp/Portland: Intersentia Publishers.
9. Broberg, M., & Sano, H. O. (2018). Strengths and weaknesses in a human rights-based approach to international development – an analysis of a rights-based approach to development assistance based on practical experiences. *International Journal of Human Rights, 22,* 664–680.

9. Financialisation and Policy-Trilemmas in Global Finance

An Introduction

Dirk Heremans

Globalisation, internationalisation, and openness present difficult challenges for nation states. For a better understanding they can be approached within the framework of three policy-trilemmas.

In geopolitics, a trilemma between three policy-objectives has recently been pointed out, implying that they cannot be (fully) realised simultaneously, but that one has to give: i.e., choices have to be made between participation in globalisation, national sovereignty, and participatory democracy.[1] In international monetary economics another trilemma between free capital flows, autonomous monetary policy, and stable exchange rates is since long conventional wisdom. A stable international monetary order (with currency stability) in a world with free capital flows is not achievable with autonomous monetary policies by countries. The recent international financial crisis brought a last trilemma to the foreground: financial stability is not sustainable in a world of integrated financial markets with fragmented sovereign financial policies.

These global finance issues and their relation to the worldwide financial crisis a decade ago were the topic of the fourth session of the Baeck cycle of colloquia. By way of introduction this paper first develops the earlier views of Louis Baeck on financialisation as the broader framework leading to the financial crisis. We then report on the aftermath of the financial crisis and then return to what has been coined 'the new normal' today, but also look into the remaining challenges for global sustainable financial stability. Finally, this will allow us to formulate specific issues and questions that were put to experts in the panel for a more in-depth analysis.

Financialisation and Financial System Crisis

Already at the end of the 90s Louis Baeck reported on the 1998 financial crisis in Asia[2] and on the sharp stock market correction after the high tech bubble in 2002[3]. Subsequently, in 2003 he warned about the increasing financialisation of the real economy containing inevitable systemic risks. In addition, he complained that the financial segment of the world economy functioned not only as the driving engine of the whole system, but also oriented motivations, values, and norms of our society, which now has become financialised.[4]

Baeck always framed his views on finance within the evolving world economy. Hence, in the beginning of 2008, just before the global Subprime Crisis became a reality, he wrote about system changes in a world economy with speculative bubbles[5], followed by a publication in 2009 on the 'Financial System Crisis in a Geopolitical Perspective'[6]. In particular the relation between emerging Asia and the financial crisis stricken Western economies retained his attention. The financial crisis called into serious question the Western governments precipitating an eastward shift towards Asia's economic and political power.

In all these writings, Baeck was heavily critical of what he coined as 'the exuberant turbo of the artificial financialisation of the real economy'. In fact he observed that the financial sector in many Western countries had become much larger than their real economy (e.g., in Belgium six times larger than its GDP). He puts the blame for the crisis on the 'alchemy' of financial innovations contaminating banking with many 'toxic' financial products such as mortgage-backed securities, (synthetic) collateralised debt obligations, and credit default swaps. These often highly rated assets proved in the crisis to be no better than 'junk bonds'. Due to the turbo of financialisation, finance was no longer serving the real economy. With an unlimited expansion of (synthetic) financial assets without underlying real assets, finance had created its own (highly profitable) artificial world. The real economy had become the slave and victim of the financial sector. In addition, Baeck singled out the 'Anglo-Saxon Financial Model', which emanated from the neo-liberal drive towards financial deregulation, as being at the root of the problem. This model was characterized by short-termism (i.e., short-term shareholder profit maximisation) and led to abuses of power by large institutional investors.

The New Normal after the Subprime Crisis

For sure historically the world has always been suffering from financial disruptions resulting in true crises. The International Monetary Fund (IMF) already registered 124 financial problems only between 1990 and 2007. However, the worldwide financial crisis of 2008 was the first on a worldwide scale since the Crash of Wall Street in 1929 leading to the longstanding Great Depression of the world economy in the 30s.

The Subprime Crisis, as the 2008 crisis is often called, originated from a poisonous cocktail of policy failures linked to two trilemmas. First, referring to the international monetary stability trilemma, failures in the governance of global macroeconomic imbalances provided the necessary background. Persistent trade and payments surpluses of China and corresponding deficits in the US were not adjusted by exchange rate changes and interest-rate adjustments but unlimitedly financed by massive international capital flows flooding US financial markets and investment banks with excessive liquidity. Second, a matter of the financial stability trilemma, aggressive financial innovations in the US could be launched and magnified by failures in the regulation and governance of financial institutions. Financial innovations were a way to circumvent banking regulation by shifting financial operations to non-regulated, non- bank intermediation (i.e., shadow banks). Moreover, due to international differences in bank regulation (US banks were being subject to leverage limits but not to Basel II capital requirements, whereas the opposite applied to European banks), regulatory arbitrage speedily spread US toxic financial products from shadow banks to the balance sheets of European banks.

Within global financial markets, as fragmented financial regulation and supervision failed, internationally coordinated efforts are necessary according to the financial stability trilemma to restore and maintain the health of the financial system. However, this proved to be cumbersome as financial policies cover a whole range of instruments from credible (ex post) crisis management to stop panic spreading across the world, to (ex ante) prudential and structural regulation and supervision to restore trust in banks and financial markets.

Typically, every financial crisis starts by a liquidity crisis due to a contagious bank run by depositors or more invisible by withdrawal of wholesale deposits in the wholesale banking market. When liquid funding is lacking, banks have to proceed to fire sales of assets thereby incurring large losses and eventually becoming insolvent. Central Banks can stop this process by acting as lenders of last resort, i.e., by providing as crisis managers liquidity against bank assets. Next in order to prevent failures of banks already in distress, governments have to intervene by restoring their solvency and capital base: the Treasury eventually by bailing out banks with tax money and Financial Authorities by restructuring banks eventually through mergers.[7]

In the US, the Federal Reserve Bank acted swiftly as lender of last resort by providing liquidity not only to deposit banks, but also to investment banks and the wider financial system. Moreover, in order to avoid a deep recession, the Federal Reserve shifted its monetary policy to unprecedented Quantitative Monetary Easing Policies. To regain monetary control and to start bank lending to the private sector in times of crisis, it resorted to unorthodox lending of last resort and outright purchases of private debt of different maturities. In addition, the Treasury and the Financial Authorities acted also speedily by providing funds on a large scale for bail outs, or by organizing orderly failures or restructuring of banks in distress. Moreover, the traditionally market oriented financial system was instrumental in reorganising and recapitalising banks.

In Europe, however, with traditionally fragmented policies among nation states, such crisis management proved to be more difficult. Fortunately the EU had launched the European Monetary Union (EMU) project a decade earlier for a large group of countries. In fact, this aimed at avoiding the international monetary instability trilemma threatening the integrating single market. Hence, the European Central Bank (ECB), responsible for a single monetary policy for the group of Euro-member countries, was able to coordinate the liquidity provision as lender of last resort to be executed by its member-central banks. However, the ECB did not follow the example of the Federal Reserve which was relaxing monetary policy to avoid a recession. The ECB Board remained fundamentally divided with many members being more concerned about inflation and government debt. The ECB even proceeded to restrictive monetary policies in 2010 thereby provoking a deep recession. Moreover, bail-out operations and restructuring of banks in distress to avoid a financial meltdown remained a matter for fragmented national financial authorities and national taxpayers. The EU role remained limited to supervising the implications of state aid and restructuring plans based on their effects on fair competition within the EU single market. Moreover, the complex realities of cross-border banks within the EU and of different national legal systems highly complicated this task.

As such, it was no surprise that a true Euro-crisis emerged in 2010-2012 due to a government debt crisis in several weaker member countries and provoking a true recession. Underlying reasons were that Europe was 'overbanked' compared to the more market-oriented financial system in the US and that the home-bias for national government debt inherent in bank capital risk regulation exposed EU countries overly to their sovereign debt. Normally, liquidity creation provides a backstop for the holders of government debt, but in the euro area member countries without their own currency could no longer provide such a liquidity backstop, threatening a 'bank-sovereign doom loop'. This Euro-crisis highlighted the institutional problem of a Euro-currency without (the political power of) a country, and of member countries without an own currency. Only a drastic shift of policy by the ECB by proclaiming the use of its bazooka 'the ECB will do whatever it takes' was able to stop the crisis.

Subsequently, in order to definitively restore confidence in the euro area, more cooperation and centralised decision-making has gradually been introduced by creating a Banking Union consisting of a Single European Supervisory System, a Single European Recovery and Resolution System, but not yet a Common Deposit Insurance system. In addition, further steps towards a financial market union to enhance private sector risk sharing among member countries are on the agenda. Further progress, in particular the creation of a Fiscal Union, is, however, becoming difficult as populist Euro-scepticism has been on the rise after the financial crisis.

Furthermore, in order to restore confidence in financial stability for the future, some coordinated efforts towards 'reregulation' have been undertaken by the Basel Committee on Banking Supervision operating within the worldwide framework of the Bank for International Settlements (BIS). In order to improve crisis preparation and crisis management, plans for an orderly unwinding of banks containing bail-ins for certain liabilities, have to be provided. At the level of microprudential regulation and supervision of the soundness of individual banks' new liquidity requirements were introduced and capital charges were doubled or even tripled. In addition, special oversight of systemically important banks and financial institutions has been introduced. Adjustments to bank structures were envisaged with, however, diverging views between the US and Europe. To obtain a broader helicopter view of the whole financial sector – which was notably lacking during the Subprime Crisis – a macrosurveillance system of the stability of the financial system has also been set up.

However, the fragmented supervision worldwide by many agencies in many countries (exception made for the euro area) makes the prospects for international cooperation to reinforce supervision still bleak. Whatsoever, all these changes in the financial system appear to have made the system safer; the likelihood and size of crises may be reduced.

Still, as central banks have successfully fended off deflationary forces and supported economic recovery, the path ahead for monetary policy remains unclear. With consumption price-inflation below target levels (in the euro area 2% in the medium run), historically low interest rates continue to feed asset price inflation, not only in stock markets, but more worrisome also in real estate markets, given that real estate booms and busts have been at the origin of many financial crises in the past. If central banks also have to take into account asset prices and financial stability targets, they face difficult trade-offs to balance this with their consumption-price inflation target.[8] As to a shift from the unconventional, quantitative accommodating monetary policy with low interest rates back to (higher) interest rate oriented policies, such a transition remains uncharted territory. Do recent anxieties about a looming recession lead to the central bank's balance sheet becoming a permanent tool of (quantitative) monetary policy? Can the 'new normal' then become a regime of low interest rates with low consumption price inflation, but asset price inflation, or will that eventually lead to a bubbles build-up in financial markets? Hence, the key question remains of how the financial system will operate in this environment of very low interest rates when they are maintained too long?

Financialisation and Remaining Challenges Ahead

Global macroeconomic imbalances

The global macroeconomic imbalances, that provided ample ammunition for financialisation to Anglo-Saxon investment banks operating in financial markets and that fuelled the last financial crisis, have not disappeared. According to the international monetary trilemma these imbalances may result from uncoordinated monetary policies (e.g., by China) aimed at exchange rate targets (manipulation) in order to maintain trade surpluses and financing capital outflows for strategic foreign direct investment objectives. When persistent trade imbalances show up in negative consequences for real economic activity in deficit countries (e.g., in the US), countries may be induced to retaliate by aiming their monetary policy at also depreciating their currency. It may finally result in currency wars (a race to the bottom) and international monetary instability, reminiscent of the competitive devaluations at the end of the 1920's before the Great Crisis. Moreover such instability raises concerns for 'offshore dollar finance', i.e., dollar denominated borrowing in emerging markets which doubled in recent years. How to make it safe? Whereas more international (monetary) cooperation would be needed to do so, the 'fracturing geopolitics' make such globalized finance even more difficult to deal with.

Continuing regulatory arbitrage

Shadow banking resulting from regulatory arbitrage was also at the origin of the Subprime Crisis. Paradoxically the tightening of banking regulation in the aftermath of the crisis is increasing this phenomenon even more, in particular in the US. Nearly two-thirds of the new credits – which made a rapid economic recovery in the US possible – were provided by non-bank financial institutions at the unregulated periphery. With this alternative financing amounting already to more than 43.000 billion dollars, these shadow banks are contributing most to domestic financial systemic risks in the US. A new challenge for regulation and supervision is how to address this shift and continuing expansion towards non-regulated financial market segments.

In addition, recently leveraged loans issued by private equity funds to finance risky acquisitions are funded by institutional investors in search of higher fixed income via the set-up of structured debt funds. These debt funds are rapidly expanding: in the US by 20% each year, already amounting to more than 1.1 billion dollars. As these loan funds in fact consist of illiquid paper, the question is what will happen when, in an economic downturn, their creditworthiness is impaired so that institutional investors are forced to sell? Is this artificial financialisation not comparable to the structured securitized funds which were downgraded to become junk bonds in the Subprime Crisis?

Similarly, financialisation risks are increasing with the rapid expansion of 'exchange traded funds' (ETF), being baskets of securities that trade all day on an exchange, just like stocks. Whereas initially ETFs were based on a replication by effectively holding the underlying securities, more and more ETFs have no longer such effective backing. Hence, they have no longer an underlying liquidity guarantee in times of stress in financial markets.

Banks and financial sector too big?

Paradoxically, the urgent rescue of banks in distress by merging them with other banks during the crisis gave rise to larger banks, which are even more complex in terms of managing and monitoring risks. Have these large banks of systemic importance not become too big to fail and too big to save?

Overall and more fundamentally the value added by financialisation of the economy has been critically reviewed in recent empirical research work. It is found that when finance gets too large in relation to the underlying economy, it may cease to be the 'lifeblood' of the economy and to turn into a ‘toxin’. The conventional wisdom is that normally, banks and securities markets are an essential prerequisite for economic growth. However, it is now concluded that in some circumstances finance may become too large, e.g., due to shadow banking, securitisation, low interest rates and falling credit standard etc. Finance may then become a severe threat to economic activity and involve a massive misallocation of resources. According to empirical research this would be the case when credits to the private sector in a country reach approximately 100% of GDP.[9]

Towards more inclusive interdisciplinary approaches

Our understanding of complex global economic and financial realities requires more interdisciplinary approaches. The combination of legal and economic analysis, simply coined as Law and Economics (already developing since the 70s in the US), has become one of the most innovative and influential scholarly disciplines. In its branch of ‘Law and Finance’, financial transactions and institutions are analysed as explicit and implicit (legal) contracts in imperfect markets, subject to informational asymmetries and agency conflicts. Financial crises are mainly a matter of failing corporate governance and of failing government regulation. In corporate governance – a truly interdisciplinary endeavour with research undertaken not only in economics and finance, but also in law, management, and accounting – financial crises are to be explained by ‘incentives’ for investors, asset managers, and bankers as these are determined by their contractual relationships. One of the implications of this research is that a more specific risk-based approach of the corporate governance of banks is needed. At the regulatory level, better insights are needed into the (potential) effects of financial law to better understand how misguided regulation may have been conductive to regulatory arbitrage and shadow banking via securitisation. For the future this should be avoided by (ex ante) regulatory impact analyses of the potential effects of new rules and legislation.[10]

Very recent innovative research into the legal underpinnings of finance and its consequences even demonstrates how not only bankers but also lawyers, by their legal creativity, were instrumental in creating the (legal) conditions for the Subprime Crisis. More fundamentally, this research also analyses how the 'legal code of capital' creates wealth, but also inequality.[11]

Economics, as a behavioural science, is more and more criticized that it is only guided by rational choice theory as this is a too restrictive approach towards human behaviour. Other behavioural sciences, such as psychology, claim to provide more realistic descriptions of human behaviour based mostly on experimental observations. People are only 'boundedly rational': due to limited information, high costs of processing information, and cognitive limitations, they rely in fact for their decisions mostly on heuristics (i.e., short cuts, rules of thumb etc.). Hence, a new field of 'behavioural economics' is rapidly developing based on more realistic insights in human behaviour.

In finance, the Subprime Crisis has fundamentally shaken the belief in rational behaviour of investors and in the efficiency of markets. It brings back earlier disparaging views of Keynes on animal spirits that guide investors and on financial markets as a casino. Hence, the 'behavioural finance school' already claiming for a long time that bubbles and crashes are caused by investors who are guided by irrational (or not wholly rational) beliefs is taking centre stage again. In their analysis, the rational representative investor is replaced by the phenomena of herding behaviour, time inconsistency, irrational exuberance, unwarranted panics etc. Still, in recent 'dysfunctional finance models' it is demonstrated that even individual rational actions may add up to collectively irrational outcomes, such as financial crises.

In the same vein, the macroeconomic models traditionally used by central banks and also by the ECB, are 'general equilibrium models' based on rational decision-making. Equilibrium is the rule, and is only (temporarily) distorted by external shocks. Hence, the economic system is inherently stable, financial crises are outside the scope, and the role for government policy-making is limited. These models are nowadays being challenged by 'behavioural macroeconomics' embedding bounded rationality. It implies that people follow simple rules of behaviour; if these do not work they switch to other rules which may lead to a macroeconomy in crisis. This has not yet become an alternative paradigm, however, should monetary policy not already take such behaviour into account?[12]

Issues for Discussion and Concluding Remarks

With the previous perspectives in mind, the colloquium on global finance was further structured around four questions:

First, concerning financial stability: Critical voices claim that the global financial sector is comparable to 'a cockpit without a pilot' and that banks should be controlled more than a nuclear atomic power plant. After all recent efforts for reform, is sustainable financial stability within reach or are we sleepwalking to the next financial crisis?

Second, on monetary and macroprudential policy: Have central banks not been focusing too much on macromonetary stability (i.e., consumer price inflation) and thereby neglected macroprudential stability (i.e., asset price inflation)?

Third, with respect to international monetary and currency stability: Are worldwide monetary arrangements needed between surplus and deficit countries in order to avoid foreign exchange rate manipulation and currency wars, and to prevent destabilizing international capital flows?

Fourth, about financialisation and the real economy: Do we return to the 'crisis-prone, exuberant financialisation system' of the economy, or should we better stop the dominance of this Anglo-Saxon Financial Capitalism (e.g., Wall Street, London City, Shadow Banking)?

Finally, issues remain for colloquia in the future: Are we not looking back too much in the rear-view mirror of the past financial crisis? Should we not better look forward to the new challenges of financial technology (fin-tech) in the digital age with, e.g., new private crypto-currencies in the making such as the 'Libra' by Facebook? Also new system risks may arise as cyber-attacks may break down critical digital payments infrastructure. Eventually they make provoke a disastrous loss of confidence in the financial system. Are fin-tech innovations to become game changers presenting new opportunities, or new instability for banks' business models, disrupting the financial world?

For the proximate future the likelihood and size of financial crises may be reduced. However, necessary reforms are becoming more difficult, since the aftermath of the financial crisis has turbocharged a populist surge raising questions about globalisation, job security, and income inequality especially among the lower middle class. If the system is safer, one should remain vigilant, since systemic banking meltdowns are a feature of human history.

Notes

* The author gratefully acknowledges comments by T. Peeters on a previous draft.

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10. Preserving Monetary Accommodation in Times of Normalisation[1]

Peter Praet

In the aftermath of the global financial crisis, central banks have successfully fended off deflationary forces and supported economic recovery.[2]

They have brought down policy rates to their effective lower bound and, importantly, have made use of a broad set of unconventional monetary policy measures in pursuit of their statutory objectives. In advanced economies, monetary policies have borne fruit, but their monetary policy cycles clearly differ substantially, reflecting different stages of recovery and degrees of progress towards achieving the central bank's statutory objectives.

In a number of places, central banks have already tightened their monetary policy stance; unconventional monetary policy measures have been wound down and policy rates have been gradually increased. In the euro area, however, significant monetary policy stimulus is still needed to support the further build-up of inflationary pressures and headline inflation developments over the medium term. At the meeting of the ECB's Governing Council in June 2018, we gave an important signal of a normalisation of our policy instruments. We communicated our anticipation that, subject to incoming data confirming our medium term inflation outlook, we would end net purchases under our asset purchase programme (APP) after December 2018.

Hence, I would like to address our key challenge in normalising our monetary policy instruments: preserving monetary accommodation, while switching back from net asset purchases to forward guidance on policy rates as the main instrument to steer our monetary policy stance.

While this rotation proceeds, we will continue to operate with multiple, complementary instruments, including our policy of reinvesting the principal payment of securities purchased under the APP.

The State of the Euro Area Economy

Following more than five years of increasingly broad-based economic expansion in the euro area, recent developments point to some loss of growth momentum. Preliminary data show that euro area real GDP expanded by 1.7% year on year in the third quarter of 2018, down from 2.2% in the second quarter. The slowdown in euro area economic growth since the start of 2018 has reflected in no small part a retreat from the strong growth of 2017. One-off country-specific or sector-specific factors have also contributed to slowing production in recent months. But factors related to protectionism, financial market volatility and vulnerabilities in emerging markets are creating headwinds that are becoming increasingly noticeable. Surveys of euro area business activity and sentiment indicators have softened perceptibly relative to their earlier highs, although they remain in expansionary territory and are still above long-term averages for most sectors and countries.

Overall, domestic demand continues to be supported by favourable financing conditions, as well as by the robust labour market and steady income and profit growth that these conditions have fostered.

Indeed, since we announced a combination of unconventional measures to provide additional monetary policy accommodation in June 2014, financial conditions have eased considerably. Risk-free interest rates have shifted downward at all maturities (see Figure 10.1), reducing the basis used by banks and financial markets in determining financing conditions.

This has been reflected in the sizeable reduction in bank lending rates for euro area non-financial corporations (NFCs) and households since June 2014 – which have declined by around 130 basis points and 110 basis points, respectively – as well as in the decline of NFCs' cost of market-based debt financing (see Figure 10.2).

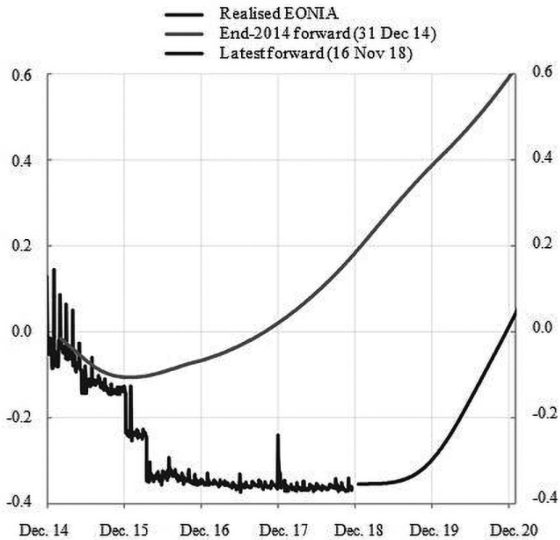

Figure 10.1: EONIA forward curves estimated from OIS (percentages per annum)
Sources: ECB
Latest observation: 16 November 2018 for realised EONIA

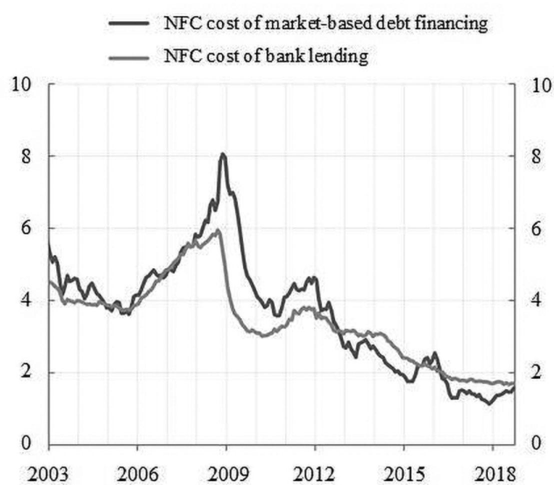

Figure 10.2: Nominal cost of debt financing for euro area NFCs by component (percentages per annum)
Sources: Thomson Financial DataStream, Merrill Lynch, and ECB calculations
Latest observation: September 2018

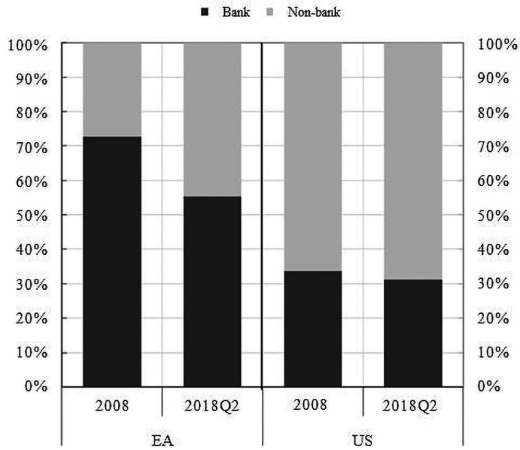

Figure 10.3: Share of bank and non-bank financing in total non-financial corporation debt financing in the euro area and the United States (outstanding amounts; percentages)
Sources: ECB, Federal Reserve System
Notes: Bank financing includes only loans granted to NFCs by banks.
Latest observation: Q2 2018

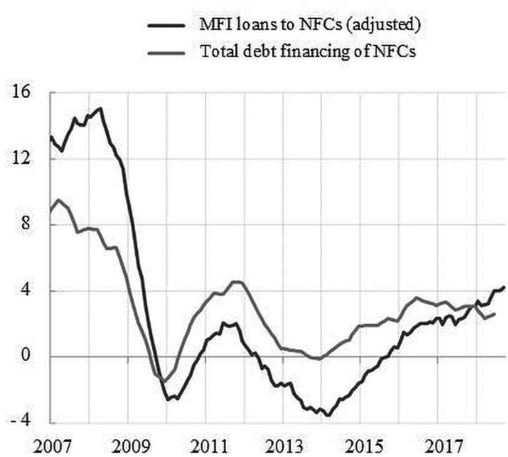

Figure 10.4: Total debt financing of NFCs and MFI loans to NFCs in the euro area (annual changes in percent)
Source: ECB
Notes: MFI loans to NFCs have been adjusted for loan sales and securitisation and cash pooling. Total debt financing is based on quarterly data.
Latest observation: September 2018 for loans and Q2 2018 for total debt financing

NFCs have also benefited from an increasingly diversified financing structure, with debt securities issuance and other forms of market-based financing substituting for bank-based sources of financing (see Figure 10.3 and Figure 10.4).

Such diversification in financing sources is good for the economy, making business investment more resilient throughout business cycles.

The underlying strength of the euro area economy continues to support our confidence that the sustained convergence of inflation to our aim will proceed. Euro area annual HICP inflation has continued to increase and stood at 2.2% in October 2018, mainly reflecting higher energy price inflation. On the basis of current futures prices for oil, headline inflation is likely to hover around current levels in coming months. While measures of underlying inflation remain generally muted, they have been increasing from earlier lows, amid high levels of capacity utilisation and tightening labour markets. Looking ahead, underlying inflation is expected to increase further over the medium term, supported by our monetary policy measures, the on-going economic expansion and rising wage growth.

Overall, though, significant monetary policy stimulus is still needed to support the build-up of domestic price pressures and headline inflation developments over the medium term.

The Rotation from the Asset Purchase Programme to Forward Guidance on Rates

At our June monetary policy meeting, we initiated a rotation of our policy instruments from the APP towards more conventional instruments of monetary policy – the policy interest rates and forward guidance on their likely evolution. We expressed our anticipation of a gradual winding-down of net asset purchases, subject to incoming data confirming our outlook for inflation. And we updated and enhanced our forward guidance on the path for interest rates, which is now expressed in terms of the expectation that key ECB interest rates will remain at their present levels 'at least through the summer of 2019 and, in any case, for as long as necessary to ensure the continued sustained convergence of inflation to levels that are below, but close to, 2% over the medium term'. In addition, we re-affirmed our intention to reinvest principal payments from maturing securities purchased under the APP 'for an extended period of time after the end of our net asset purchases and, in any case, for as long as necessary to maintain favourable liquidity conditions and an ample degree of monetary accommodation'.

This combination of policy measures aimed to preserve the degree of monetary accommodation that is necessary to ensure sustained convergence of inflation towards our aim. Clearly, the end of net asset purchases is not tantamount to a withdrawal of monetary policy accommodation. The rotation from net asset purchases towards our conventional monetary policy instruments, together with our stock of assets and the related reinvestment policy, ensure an ample degree of monetary policy accommodation. In particular, our enhanced rate forward guidance provides a strong anchor for policy rate expectations. And the reinvestment policy will ensure that the favourable liquidity conditions and duration extraction associated with the large stock of assets on our balance sheet remain in place for a long period and thereby exert downward pressures on term premia.

The mechanisms underlying the combination of instruments are duration extraction, liquidity creation, and expectation management.

Starting with duration extraction, our reinvestment policy implies that the bonds we have purchased will remain on our balance sheet for an extended period of time after the end of net purchases. Asset purchases affect interest rates mainly through the market price of duration risk, which is the interest rate risk borne by price-sensitive investors holding long-term bonds. If the central bank wants to exert downward pressures on long-term interest rates, then it can absorb duration risk from the market by purchasing securities with a relatively longer maturity. This frees up more risk-bearing capacity for investors, which they can re-allocate towards other types of risk, including investment in productive capacity. For a central bank to set this mechanism in motion, it needs to hold a large portfolio of long-dated securities embodying duration risk. Figure 10.5 shows that we have built a sizeable portfolio estimated at around 20% of the duration-equivalent stock of public debt. Maintaining such a sizeable portfolio will exert lasting downward pressure on term premia.

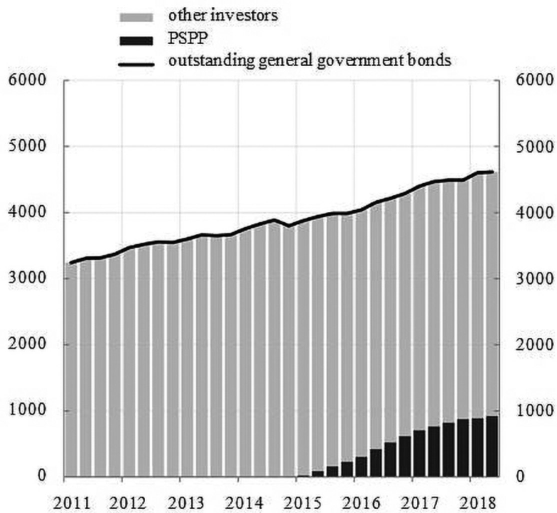

Figure 10.5: Outstanding quantity of duration: PSPP portfolio and other investors (EUR billions, 10-year equivalents)
Sources: Securities Holdings Statistics, GFS, ECB calculations
Notes: The chart shows the stock of debt securities issued by the general governments of the four largest euro area jurisdictions and the Public Sector Purchase Programme (PSPP) share of that stock in terms of 10-year equivalents. "Other investors" comprise all other financial and non-financial investors.
Latest observation: 2018Q2

Turning to liquidity creation, the roll-over of the portfolio resulting from our reinvestment policy will also continue to preserve abundant liquidity over the coming years. In the absence of reinvestments and assuming that targeted longer-term refinancing operations (TLTROs) are repaid at maturity, the level of excess liquidity would decline significantly over the coming years (see Figure 10.6).

Our reinvestment policy will contribute to maintaining favourable liquidity conditions for an extended period of time, which helps anchor expectations regarding the evolution of very short-term interest rates at the deposit facility rate. Ample volumes of excess reserves ensure that the overnight interest rate stays close to the floor of the interest rate corridor, which is provided by the deposit facility rate. This, together with forward guidance on the expected evolution of our policy interest rates, reduces rate uncertainty across maturities and thus adds to the

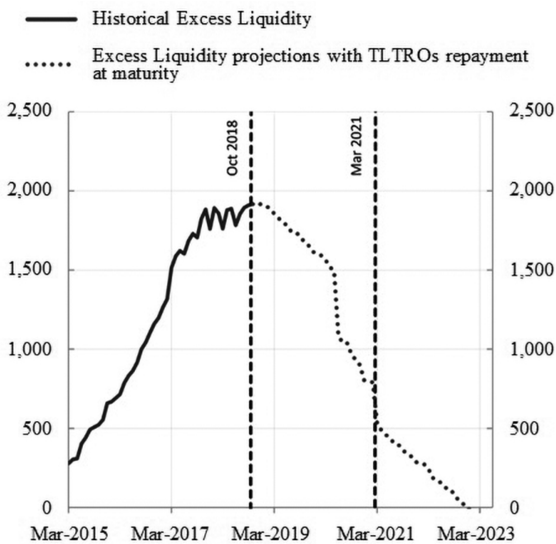

Figure 10.6: Evolution of excess liquidity under no re-investment counterfactual hypothesis (EUR billions)
Sources: ECB
Notes: The projected excess liquidity is based on a comprehensive simulation of the evolution of the Eurosystem balance sheet. For the APP it is assumed that net purchases are conducted at a monthly pace of €15 billion a month until December 2018 and then ended. In addition, the projection is constructed under the counterfactual hypothesis that there will be no reinvestments of APP maturing securities. For TLTROs it is assumed that repayments are made at the point of maturity of the respective operations. Banknotes are assumed to continue to grow in line with historical relationships. Other non-monetary policy assets and liabilities are held constant.
Latest observation: September 2018

compression of term premia brought about by the duration extraction channel.

Of course, our portfolio – even if kept constant – will tend to lose duration over time, as the securities held gradually mature. At some point, this passive loss of duration will begin to exert increasing upward pressures on the term premia. Over time, this gradual process will tend to steepen the yield curve, with our forward guidance on policy rates keeping the front end of the curve well-anchored.

Our enhanced rate forward guidance is a two-pronged statement. There is the date-based element that interest rates are expected to

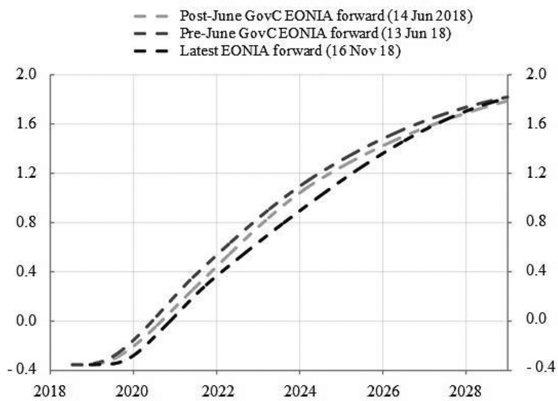

Figure 10.7: EONIA forward curves around June 2018 Governing Council (percentage per annum)
Sources: Thomson Reuters and ECB calculations
Latest observation: 16 November 2018

remain at their present levels 'at least through the summer of 2019'. In addition, there is a state-contingent element that rates will remain unchanged 'in any case for as long as necessary to ensure the continued sustained convergence of inflation to levels that are below, but close to, 2% over the medium term'. The date-based element ensures that our stimulus is not weakened by premature expectations of a rate hike. The state-contingent element, in turn, ensures that the stance will continue to evolve gradually and in a data-dependent manner.

The anchoring effect of our enhanced rate guidance was highly visible in June, when the Governing Council announced that we anticipated a gradual winding-down of our net asset purchases. Our enhanced forward guidance helped reduce the uncertainty around future short-term rates (see Figure 10.7 and Figure 10.8). Rate expectations aligned immediately to the Governing Council's rate guidance; no financial market volatility ensued.

But let me turn to the next steps for monetary policy in the euro area. The latest surveys of market participants' expectations regarding the most likely date for a first rate increase indicate that the 'at least through the summer of 2019' formulation has been solidly internalised by market participants.

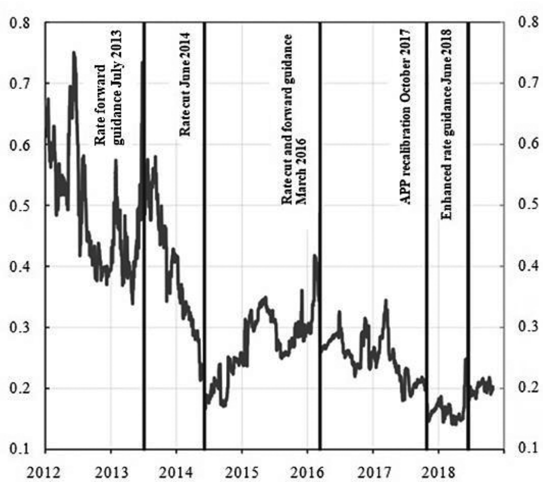

Figure 10.8: Standard deviation of three-month EURIBOR option-implied density in one year's time (percent)
Sources: LIFFE and Bloomberg, ECB calculations
Notes: Standard deviation of option-implied density of three-month EURIBOR in one year's time.
Latest observation: 30 October 2018

Looking ahead, the rotation implies that our key policy rates and forward guidance about their evolution will become an anchor for monetary policy as the end of our net asset purchases is nearing. Our communication, and the rate path itself, will be calibrated to ensure that inflation remains on a sustained adjustment path. Our policy will remain predictable, and we will proceed at a gradual pace that is most appropriate for inflation convergence to consolidate. In addition, as proved in the past, our forward guidance remains an effective firewall to insulate the euro area from unwarranted tightening pressures originating elsewhere. This protection will be crucial to ensure that, as we move along the normalisation path, euro area financial conditions remain consistent with continued progress towards our policy objective. Finally, our APP portfolio and our unconstrained provision of liquidity will continue, for the time being, to provide an accommodative environment.

I would like to make a final comment on the effects of our APP portfolio on bond yields. While, overall, our APP portfolio will continue to exert downward pressure on euro area long-term interest rates, other factors such as economic fundamentals and the creditworthiness of issuers, as assessed by market participants, remain key determinants of the levels of bond yields and spreads.

Conclusion

The winding-down of net asset purchases is not tantamount to a withdrawal of monetary policy accommodation. The ongoing rotation from net asset purchases towards enhanced forward guidance on key ECB interest rates has preserved the ample degree of monetary policy accommodation that is necessary to ensure the continued sustained convergence of inflation to levels that are below, but close to, 2% over the medium term.

Prudence, patience and persistence will continue to inform our policy decisions. The sizeable stock of acquired assets and the associated reinvestments, as well as the strong anchor for policy rate expectations provided by our enhanced forward guidance, will continue to deliver the monetary policy stimulus necessary for inflation convergence. In any event, all our policy instruments can be adjusted to ensure that inflation moves towards our aim in a sustained manner.

Notes

1. This contribution is also based on a speech given by Peter Praet in German on “Herausforderungen für die Europäische Geldpolitik 2019” at 33. Internationales ZinsForum 2018, Frankfurt am Main, 26 November 2018.
2. This speech builds on my remarks at the UBS Conference, London, 13 November 2018.

11. Potential Triggers for Financial Bubbles

Some Thoughts and Comments from Corporate Finance

Cynthia Van Hulle

Even more than ten years after the crash of 2008, awareness of the negative consequences of the bursting of bubbles is still significant among economists, governments, and even the public at large. One important question in that respect is whether or not the potential for bubbles remains important, even after the major enhancement of the oversight on financial institutions worldwide. Although corporate finance typically takes a microeconomic perspective concerning financing and investment choices by corporations, the corporate finance logic suggests that we live in an economic environment that can easily stimulate bubbles. Unfortunately, bubbles, and certainly the bursting of them, may have nasty consequences on a macroeconomic level as documented by academic research.[1] The latter has shown that in the past systemic banking crises are typically preceded by credit booms and asset price bubbles. This intervention focuses on a corporate finance view of the following three aspects that are important in today's (European) economy: low interest rates, the tax system that favours the use of corporate debt, and the changing nature of corporate investment. The discussion below argues that these factors may stimulate the overheating of (segments of) financial markets.

Does Decreasing Already Low Interest Rates Stimulate Corporate Investment?

The last several years the European Central Bank (ECB) has followed a policy of decreasing already low interest rates. Although low interest rates are beneficial to corporate investment in projects and assets, one can ask the question to what extent lowering already low rates is likely to be an important extra stimulant of corporate investment. Although the motivations of the ECB to keep interest rates low presume that this is the case, the corporate finance perspective suggests several factors may limit beneficial effects.

Interest rates in financial markets are an important driver of the cost of corporate debt. As debt is often part of the financing mix of companies, low interest rates tend to lower the cost of capital (i.e., the overall cost of funding of a project). The interest rate firms pay typically consist of the interest rate on government debt plus some extra premium for bankruptcy risk. For high quality borrowers (i.e., firms with a high rating) this premium tends to be limited to 1 or 2%, although empirical evidence shows this premium may vastly vary over time.[2] Interest rates also influence the cost of equity, the other major source of financing. The cost of equity is typically composed of the risk free rate (usually measured as the interest rate on medium to long term government bonds) to which a risk premium has been added. For listed firms, historically in Belgium this premium has averaged around about 5% in the past, with significant variation through time and across companies (the shares of some firms are significantly more risky than the shares of other listed companies).[3] For non-listed firms (i.e., the bulk of all companies), private equity players typically augment this premium with several extra risk factors such as e.g., lack of tradability of the shares (and hence illiquidity) or the extra strategic vulnerability of smaller and/or younger firms within their sector. In Belgium these extra risk factors can easily cause risk premia on equity of 15% and more for small and young firms.

When interest rates in the financial markets decrease from a high to a low level they obviously have a significant impact on the cost of capital. However when interest rates are already low, say 2%, and further decease to, say 1%, the impact on the cost of capital likely is limited, unless this further decrease in already low interest rates would also drastically decrease risk premia. However, although there is a link; practice shows that the impact on risk premia generally is not that important.[4] Furthermore, what typically is a far more important driver of investment decisions as compared to the cost of capital is the future profitability and cash generation capacity of corporate projects. Without sufficiently profitable opportunities, no investment takes place. The availability of such opportunities obviously depends upon elements such as economic conditions within the firm's sector, the capacity to compete internationally.... Only when lowering already low interest rates can influence these factors in a significant way, such a policy is important in affecting investment decisions. Although one obviously cannot guess what the economic situation would have been without the ECB's ultra-low interest rate policy, overall economic growth remains limited in Europe, which in turn dampens the availability of profitable investment opportunities.

Some sectors are more influenced by changes in interest rates than others. One such example is real estate, which is a sector that clearly has benefited from the low interest rate environment. Furthermore, investors consider real estate to be relatively safe, and tend to accept even lower risk premia on this type of investment when interest rates are low because of the 'there is no other'-effect (TINA-effect). As a result, prices of real estate assets increase (this phenomenon is called asset inflation), which in turn may lead to a bubble in the real estate market. In fact, extending to the stock market as a whole, in the past TINA has already caused asset inflation of share prices and higher stock market volatility, because asset inflation enhances the chances of bubble development and the ensuing risk of a bubble burst.

Overheating Debt Markets: Taxes and Low Interest Rates Favour the Use of Corporate Debt

The insights from corporate finance show that the tax system is an important determinant of the financing mix (i.e., debt versus equity) that companies choose.[5] The fact that interest expense (i.e., the remuneration for one source of financing – debt) can be subtracted from taxable corporate profit, while dividends (i.e., the remuneration of another source of financing – equity) cannot be subtracted, creates a tax advantage for the use of debt financing. In Europe, traditionally most of the financial corporate debt is bank financing, while in the Anglo-Saxon world market based financing (non-banks directly lend to corporations under the format of corporate bonds, commercial paper…) occurs more frequently. However over the last years the low interest rate environment has stimulated, both in the Anglo-Saxon world and in Europe, more market based financing.[6] An important driver of this phenomenon is that of the quest for extra yield in today's low interest rate environment. Similarly to the case of real estate, corporate bonds (with a sufficiently good rating) are considered to be relatively safe by investors. As a result the TINA-effect becomes more prone to edge these investors on to increase their exposure to corporate bond risk. In good economic times, companies can easily bear higher levels of debt, as high profitability encompasses the promise of sufficient future cash generation to pay for interest and redemption of the loan principal. However if a sudden drop in economic conditions occurs, this future high cash generation may not materialize, causing a decrease of quality of corporate debt and eventually the occurrence of major losses for corporate debt holders through debt restructuring and outright corporate bankruptcy.

The Changing Nature of Corporate Investment: More Uncertainty Creates More Bubble Sensitivity

The speed of (technological) change, globalization, and the increase in competition in many sectors of the economy cause the outcome of corporate investment projects to become more uncertain. Furthermore most firms are faced with the fact that, due to these former phenomena, the economic life of even successful products and services has dwindled considerably over time, thereby enhancing uncertainty, as companies need to continuously replace these successful products by new ones to keep their profitability rolling. Consequently, estimating future profits and cash generation of firms becomes more difficult, for management and outside investors alike. For listed companies this has the effect that expectations about the company's future profitability by the investing public may easily become too optimistic (thereby creating major price increases of the firms' shares) or too pessimistic (leading to major downward adjustments in stock market prices). As a result, in such an environment, the underlying (potential) stock market volatility structurally increases as well as the bubble potential. In fact, if indeed the occurrence of bubble build-up or (near bubble-build up) becomes significantly more frequent, important questions about the usefulness of the stock market as a financing mechanism come to the forefront. But such a discussion falls outside the scope of the present comments.

In Sum

The insights from corporate finance suggest that low interest rates, the tax system that favours the use of corporate debt, and the changing nature of corporate investment may each separately or in combination stimulate bubbles and overheating of financial markets. Furthermore decreasing interest rates further in an already low interest rate environment may only have a limited positive effect on corporate investment.

Notes

1. See e.g., Reinhart, C., & Rogoff, K (2009). The aftermath of financial crisis. *American Economic Review, 99,* 466-472; Berndt, A., Douglas, R., Duffie, D., & Ferguson, M. (2018). Corporate Credit Risk Premia. *Review of Finance, 22,* 419-454.
2. See e.g., Brealey, R., Myers, S., & Allen, F. (2020). *Principles of Corporate Finance*. New York, NY: McGraw-Hill Education.
3. See e.g., Damodaran, A. (2018). Country risk: determinants, measures and implications – the 2018 edition. Retrieved from https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2630871
4. See e.g., Damadoran (2018). Country risk.
5. See e.g., Brealey et al. (2020). Principles of Corporate Finance.
6. See contribution of Peter Preat in this volume

12. Quantitative Easing

For Better or for Worse

Eric De Keuleneer

I would fully agree that the very easy monetary policies of the European Central Bank (ECB) and other major central banks have had their positive consequences. The very low interest rates and abundant liquidity provided within Quantitative Easing have probably saved a number of big borrowers, and many banks, from collapse, and prevented a worsening of the economic situation after the financial crises of 2008-2011. But since then, they have probably played a part in the development of various worrying imbalances in the economy and may have delayed some necessary reforms.

Economic Activity

Quantitative Easing was meant to address the consequences of the financial crisis of 2008 on the European financial system, and the renewed Banking crisis which was looming within the euro area following the near-insolvency of Greece – to whom euro area banks had incautiously lend exaggerate amounts – a few years later. This monetary policy has since been prolonged with the stated objective to improve economic activity in the euro area, were growth remains very low ten years later. Low interest rates (real interest rates have been negative for many years, and even nominal interest rates are now negative in most euro area economies) are supposed to stimulate the economy by encouraging investment and consumption; directly by making the financing of investments cheaper, and indirectly through a 'wealth effect' if these low rates help asset prices rise in value and give households the impression of being more wealthy, thus able to spend. This seemed to work in the United States where it has been applied since 2008, although it is difficult to know if it has been a major reason for the economic recovery of the US. There are many characteristics of the US economy that could very well explain the economic growth of the last years, characteristics relating to social stabilizers, the structure of taxation and of the labour market, that are different in the euro area. Both in the US and the euro area, monetary stimulus seems to have encouraged a higher indebtedness of the non-financial corporate sector, without much stimulating investment. Most of the growth in the US came from household consumption; in the US, a major part of consumers are net borrowers rather than savers, and they very much benefited from lower interest rates. Successive rounds of Quantitative Easing have not yet succeeded in propping up growth in the euro area economies, and it might be useful to look at some of the possibly negative aspects of this monetary policy on the economic activity, and growth.

Savers, particularly modest savers who rely on savings accounts and short term bonds to get some income from their savings, thus get penalized. Since, in Europe, such savers are an important proportion of the population, this could very well negatively influence the propensity to spend, thus also **consumption,** which remains sluggish in the euro area, and hence economic activity. It could also participate in the discontent in the middle classes, which has become more noticeable. From the start of Quantitative Easing, stock prices and asset prices in general have risen substantially, which benefits mostly the wealthiest, and may also participate in the growing perception of **unfairness** of the system.

Banks and Financial Markets

The massive injection of liquidity into the banking system since 2008 has avoided the collapse of many banks, but one may fear that the banking sector has not been sufficiently reformed to take the lessons of 2008-2011 into account, and to make the European financial system more resilient during the next financial crisis. The banking system still plays a dominant part of financial intermediation in the euro area, despite not being very efficiently in many countries. Banks are still getting big subsidies: in the form of state guarantees on their deposits, with little or insufficient counterpart, and more directly by state support when approaching failure. They are also subsidised indirectly through the message that states will support them in case of need, which particularly applies to the big banks (the 'too big to fail' syndrome is still present). Banks' equity levels have improved to some extent, but the leverage ratio of many banks remains well below 5%, and for many even below 3%, meaning they can hardly absorb any meaningful losses. Their 'risk weighted' equity levels, which could sound reassuring at more than 10 or 15%, are in many cases untrustworthy, given the discretion given to banks to determine in practice themselves their risk-weighting classifications. Moreover, the zero-risk weighting given to a big part of sovereign bonds is rather illusionary, and, by encouraging sovereign bond purchases by banks, increases the vicious circle or doom loop between States and Banks in many euro area countries.

Thus, the ECB has indeed done an important job in keeping financial markets and the banking system in Europe functioning, but it has also enabled banks to keep some very bad habits. It has being propping up asset prices, but it is by no means sure that the European financial system is now on a sound footing. The asset bubbles induced by artificially low interest rates may create an additional **vulnerability**: the easy monetary conditions that prevail are pushing prices of various asset classes to high, one could say to unsustainable levels. When 10 to 20 year government bonds offer negative yields that means their price is very high, and will fall drastically once yields become positive again.

Structural Imbalances

It is almost ironic that some central banks in Europe, like in Belgium, profess a serious concern for the rise in price of **real estate**, although this is a very direct consequence of the abundant liquidity and the very low level of interest rates practiced by the ECB which is under their direct supervision. Rising prices of real estate are another source of frustration for middle-classes, the young, and in general those who need to rent or purchase their lodging.

Another consequence of the lax monetary conditions since the beginning of the crises in 2008, is that those most **responsible** for the economic crisis which has shaken the system, have rarely been held to account. Bank traders and top executives still earn often abnormally high remunerations, providing distorted incentives for doing a job that is often pretty unsatisfactory for society, and even for their employer. Rather than asking for public support, as they often do, to restore the profitability of banks, they should more often start by accepting to reduce those high remunerations. Most economies in our system suffer from an increase in inequalities and plutocracy, fuelled by perverse and excessive executive remuneration practices. There are several causes for perverse and excessive remuneration practices in the corporate sector, but many of them can be traced to the financial sector and its bonus culture which originated in trading rooms in the 80s and 90s: the liberalisation of financial markets allowed for various periods of easy profits, which alternated with crisis in one or the other segment of Finance, and in the whole of the financial world in 2008. During these periods of easy profits, bankers and traders managed to extract fat bonuses, and during the periods of crisis, they managed to get national and international public bodies and taxpayers to rescue them. This of course attracts quite a lot of financially motivated talent to the financial sector, and induces top executives remuneration-inflation in the whole corporate sector which has to compete for talent. This might be a major source of the rising income inequalities, and one that does very little to help economic growth, even to the contrary.

These easy monetary conditions have allowed many European governments to ditch necessary reforms of their economies, and of their banking system. European economies have been quite weak recently, and Quantitative Easing has provided vitamins to keep them going. However if the structural problems are not addressed, the vitamins may turn out to rather be steroids, and rather weaken the structure.

13. Mediterranean Tradition in Economic Thought

An Introduction

Marc Franco

Religion, Ethics, and Economic Thinking

Out of the box thinking, putting economics in a broader social, political, and cultural context, and never losing sight of the historical dimension was characteristic for Professor Louis Baeck's attitude as a scientist. He always questioned the dogmas of mainstream economic thinking: he never hesitated to ask fundamental questions and never neglected the wider context. This is well illustrated in his book on the 'Mediterranean Tradition in Economic Thought'[1] and in a paper on 'Mediterranean Economic Thought and Atlantic Economics' he delivered at a conference[2].

Baeck developed his interest in the topic after teaching the course 'History of Economic Theory' for many years. In such a course, the emphasis lies on the evolution of economic thinking after Adam Smith's 'Inquiry into the Causes and the Nature of the Wealth of Nations'. Preceding approaches are usually considered interesting but pre-scientific contributions (i.e., of a philosophical rather than a scientific nature).

Baeck considers the period before Adam Smith and focuses on a change in paradigm. In the Mediterranean paradigm, the community or society occupies a central place. The objective of the economy is to create a balanced society where citizens can live together in harmony and solidarity. Behaviour of the individual is subordinate to the common interest. Economic thinking is embedded in philosophical, and in particular, ethical thinking.

The Mediterranean tradition finds its origins in the works of Ancient Greek philosophers, such as Aristoles' 'Zoön Politicon', later elaborated by the Church Fathers and masterly reflected in the writings of Thomas Aquinas and Albertus Magnus.[3] In his book, Baeck describes in detail how political and economic evolution, the development of religion and religious institutions (monastic orders in particular), and the development of society and economy interact.[4]

The 'Mediterranean Tradition' is not limited to the Christian world. It is also reflected in the Islam. In Islam, society occupies a central place and the pursuance of individual interests is condemned. Redistribution of income and wealth is realised through the obligation of 'zakat' (i.e., charity: one of the five pillars of Islam) and institutions such as 'waqf' (religious charity foundation). The prohibition of interest – that was also in force in Christianity – prevents accumulation of wealth through unearned income. This doctrine is further developed by Islamic philosophers such as Al Ghazhali[5] in Persia, Ibn Rush (Averoës)[6] in Andalucía, and Ibn Khaldun[7] in North Africa.

The discoveries and political development of the 16th century shifted the centre of gravity of economic activity from the Mediterranean to the Atlantic Ocean. Production and trade developed rapidly. Producers and traders became detached from the interest of the community and pursued their own individual interest liberated from societal checks and balances. Economic development gradually occupied a more central place in society, and this stimulated thinking about the economy in its own right. Baeck mentions in this context the contributions of the School of Salamanca, the 'arbitristas', and the Flemish philosopher Leonardus Lessius.[8] On the other hand, religion also has an impact on economic development, dixit Max Weber who states that the ideology of Calvinism and its focus on the individual is an important factor in the development of capitalism.

Atlantic versus Mediterranean Tradition

Gradually, economic thinking became separated from ethics and from general philosophy and developed its own scientific methodology. The objective was no longer social welfare but the individual utility maximization of the 'homo economicus'. The market realised equality between supply and demand and social welfare is the sum of the welfare of the individual economic actors. The invisible hand of Adam Smith brought about general equilibrium and social welfare. Later on, Walras, Pareto, Debreu, and others prove that under specified conditions a market economy leads to an equilibrium that is Pareto-optimal and every Pareto optimum can be reached through the market.[9]

The social rather than individual focus of the Mediterranean thinking did however not completely disappear from economic thinking. Marxist economic thinking puts the emphasis on society and social classes rather than on the individual. It is based on the labour theory of value, which is also present in scholastic and Islamic thinking.

Moreover, the 1970s and 1980s were characterized by a revival of Islamic thinking in general, and Islamic economic thinking in particular. This evolution manifested itself not only in the Arab world but also in Turkey, Iran, Pakistan, Malaysia etc. Universities and research institutions in these countries have produced an impressive volume of publications that are little known in the Western world.[10] The question is to what extent a full-fledged Islamic economics can be developed. The difference between Mediterranean and Atlantic economic thinking (with respectively the community or the individual as the starting point) analysed by Baeck, is very relevant in this context. Many authors tend to incorporate standard economics, including mathematics and econometric tools of analysis, referring more or less explicitly to the principles of Sharia. Other authors are stuck in the Islamic jurisprudence and do not develop a scientific methodology. According to Abdul Ghafar bin Ismail, the first Contemporary Islamic Economics Conference in 1976 constitutes a watershed in Islamic economic thinking.[11] This conference gave an impetus to efforts to make the Islamic worldview the point of departure of economic theorising and analysis whereas earlier theorists started from a neo-classical paradigm that they tried to 'Islamise'. It is however necessary that Islamic economics develop beyond the work on banking and finance into a coherent school of economic thought.[12]

In the Orthodox part of Europe, in particular in Russia, one can find echoes of this approach that puts the emphasis on the society rather than on the individual. Interesting in this context is the work of the 19th century Russian economist Alexander Chayanov and his 'Theory of non-Capitalist Systems'.[13] The community feeling in the old Slavic 'mir' (village community) – linked with the traditional Orthodox religion – is contrasted with the Western decadent individualism. This approach also sometimes resonates in the thinking of President Putin.[14]

Last but not least, even in mainstream Western thinking, attempts have been made to integrate the role and interests of society, the need for re-distribution etc. in the theory. An illustration is the UN Human Development Index that intends to replace GDP per capita as a measure of development by a composite measure integrating social welfare indicators. On the theoretical level, Baeck also mentions the contributions of the Nobel Laureate Amartya Sen, in particular his 'capabilities approach'[15], and of the American moral philosopher John Rawls and his 'justice is fairness' principle[16].

Issues for Further Discussion

These important questions about the fundaments of our economic thinking, about the relation between theory and practice, and between economic thinking and economic reality were further developed in the conference cycle from three angles.

In the first place, François de Callatay analyses how the economy of the Greek and Roman world has influenced the economy of the Islamic world. In the second place, Emilio Platti analyses the relation between Islamic thinking and political Islam. He situates his analysis in the politics of present-day Egypt. In the third place Jean-Philippe Plateau was to present his recent book analysing the relationship between religious doctrines and political and economic reality in Christianity as well as in Islam.

Plateau's thinking may be summarized based on his book 'Islam instrumentalised: religion and politics in historical perspective'.[17] The starting point is Bernard Lewis' thesis that Islamic religion is an inherent obstacle for the development of democracy, modernity, and economic development.[18] This thesis is the counterpart of Max Weber's well known theory about the role of Protestantism (in particular Calvinism) played in the development of capitalism. Plateau starts his analysis from the knowledge that historically, Islam has been at the apex of human (scientific, economic, political cultural) civilisation, and he wonders how it can be true that Islam is inherently an obstacle to development.

As a conclusion of a thorough analysis of various Islamic countries, Plateau concludes that it is not Islam that is an obstacle to development. The basic problem in Islamic countries lies with the state and the political authoritarian systems, driven by the self-interest of the economic and political dominant classes. The ruling classes instrumentalise religion for their own purpose and use it as a legitimation of their wealth and their place in society. The institutions as zakat and waqf are forms of charity, realising a limited degree of redistribution but never questioning the basic inequalities in society. This analysis of the relationship between religion, state, and economy leads Plateau to questions the Weber thesis. More specifically he emphasises the fact that the state institutions promoting the development of capitalism did exist before the emergence of Calvinism.

Concluding Remarks

Baeck's contribution to the history of economic thinking raises many interesting issues about the nature and general validity of our present mainstream economic thinking, but it also raises questions about Islam, Islamic economics, and political Islam.

Two issues came up during the Q&A at the end of the panel discussion. The first question is whether the ban on interest, considered to be usury, can be maintained. This ban, rooted in Sharia (and also supported by Catholic theology until the 16th century), is difficult to maintain in the present times where financial markets increasingly dominate the global economy. On the one hand, these last decennia witnessed the development in many Islamic countries of Sharia conform banking and monetary transactions such as Islamic bonds (sukuk), the profit and loss sharing financial products (e.g., mudarabah and musharakah), or asset backed products (e.g., murabaha).[19] On the other hand, bankers in the Islamic world are increasingly involved in the new forms of financial derivative products that often not only include interest payments, but constitute forms of speculation, strictly forbidden by Sharia.[20] Will reality (and profit opportunities) overrule the strict application of Sharia – as it did with the ban on interest in 16th century Europe?[21]

A second question is related to the economic policy of political Islam. The social orientation of Islamic economic policy is mainly embodied in the two institutions of zakat and waqf that ensure a form of redistribution of wealth and income and of support for the poor. However, to what extent can these institutions be the basis of a just society? Like all forms of charity, zakat and waqf do not constitute a right to a more just society; they confirm and reinforce the existing state of affairs and have an establishment-confirming effect. Existing inequalities and injustices are not questioned. Will modern forms of political Islam be able to transcend this reliance on charity in order to solve social inequality and injustice? It seems that zakat and waqf have their place in Plateau's assessment of the instrumentalisation of religion by the ruling elites in the Islamic world.

Notes

1. Baeck, L. (1994). *Mediterranean Tradition in Economic Thought*. London: Routledge. See also Islahi, A. A. (2003). Book Review: The Mediterranean Tradition in Economic Thought by Louis Baeck. *Journal of King Abdulaziz University – Islamic Economics, 16,* 55-58. Retrieved from https://mpra.ub.uni-muenchen.de/22847/.
2. Baeck, L. (1994). Mediterranean Economic Thought and Atlantic Economics, presented at Cultural Actions for Europe, Fifth Seminar in Athens, 1994. Retrieved from http://poieinkaiprattein.org/conferences-symposiums-workshops/cultural-actions-for-europe/the-workshops/workshop-5-culture-driven-economy/mediterranean-economic-thought-and-atlantic-economics/.
3. Aristotle's ethical-political paradigm can be summarised around three axes: the community has a categorical priority over individuals; the criterion of socio-political merit has pride of place as a distributional norm; Aristotle's economy is clearly a political economy.
4. See in particular Baeck, L., Mediterranean Economic Thought, pp. 151-159.
5. A recurrent theme in Al Ghazali's analysis is a social welfare function: all goods and services are evaluated in terms of their capacity to promote social welfare or, on the contrary of their social disutility.
6. Ibn Rush is best known for his systematic interpretation and further development of the writings of Aristotle and his influence on the medieval scholastic thinkers.
7. Ibn Khaldun is best known for his analysis of social, economic, and institutional factors which influences the course of history. He is also the first Muslim scholar to produce a global picture of the economy, based on a labour theory of value. His writings aim at a renewed community spirit and efficient government to give Islam a new developmental impulse.
8. The origins of the School of Salamanca coincide with the development of transatlantic trade, the arrival of large quantities of gold and silver on the European markets, and the emergence of mercantilism. It can be considered the starting point of a subjective theory of value. In modern terms, the School of Salamanca represented a monetarist approach, the arbitristas a more structuralist approach to inflation. The ethical paradigm that reigned over the thinking about economics was gradually replaced by an approach that considered the economy as an instrument for realising practical social and political aims.

9. See e.g., Debreu, G. (1959). *Theory of Value: An axiomatic analysis of economic equilibrium*. New York, NY: John Wiley and Sons. A particular situation is Pareto – optimal (i.e., allocatively efficient) if it is impossible to change it so as to make at least one person better off without making another person worse off.
10. See e.g. Djakfar, M. (2016). Contemporary Islamic Economic Thinking: A Sharia-based Work Culture Reconstruction. *Journal of Social and Islamic Culture, 24,* 269-281; Farooq, M. O. (2013). Contemporary Islamic Economic Thought. In K. Hunt-Ahmed (Ed.), *Contemporary Islamic Finance – Innovations, Applications and Best Practices*. New York, NY: John Wiley & Sons.
11. Ghafar B. Ismail, A. (2008). *Evolution of Islamic Economic views*. Working Paper in Islamic Economics and Finance No 0906 – Research Center for Islamic Economics and Finance – University of Kebangsaan, Malaysia. Retrieved fromhttps://www.academia.edu/4417158/Evolution_of_Islamic_Economic_Views?auto=bookmark
12. See e.g., Zaman, A. (2010). Islamic Economics: A survey of literature. *Islamic Studies, 49,* 37-63.
13. Chayanov developed a theory of peasant farming, in particular substance farming, where the producers tend to produce only the amount of produce they need. Production of surplus and accumulation is avoided as it leads to destabilisation and destruction of the village community.
14. See i.a., Eltchaninoff, M. (2015). *Dans la tête de Vladimir Poutine [In the Head of Vladimir Poutine]*. Paris: Actes Sud. Eltchaninoff identified the main thinkers that have inspired Poutine: Ivan Illyine ('Putin's philosopher of Russian Fascism' as T. Snyder calls him (New York Review of Books 16/04/2018)) and Nicolas Berdaiev (conservative Russian orthodox thinker).
15. Sen, A. (1984). Rights and Capabilities. In *Resources, Values and Development* (pp. 307–324). Cambridge, MA: Harvard University Press.
16. Rawls, J. (1999). *A Theory of Justice (revised)*. Cambridge, MA: Harvard University Press.
17. Plateau, J. P. (2017). *Islam Instrumentalized. Religion and Politics in Historical Perspective*. New York, NY: Cambridge University Press.
18. See e.g., Lewis, B. (2002). *What went wrong? Western Impact and Middle East Response.* New York, NY: Oxford University Press.
19. See e.g., Farooq, M. O. (2013). Contemporary Islamic Economic Thought.

20. See e.g., 'Sharia-compliant derivatives – a contradiction in terms?' – Financial Times 11/02/2009. Retrieved from https://ftalphaville.ft.com/2009/02/11/52352/sharia-compliant-derivatives-a-contradiction-in-terms/
21. In the Divina Commedia Dante places the usurers in the inner ring of the seventh circle of Inferno. Although the ban on interest was not revoked until the beginning of the 20th century, the Church keeping up with the changing times and the needs of sovereign and of business for financial resources, from the 16th century onwards gradually changed the strict ban to a ban on 'immoderate' profits.

14. The Greco-Roman Economy at the Source of the Economy of the Muslim World?

Theory and Pratice

François de Callataÿ

The Mediterranean Tradition

'*The Mediterranean Tradition in Economic Thought*', Louis Baeck's work to which this presentation relates, was published in 1994.[1] It is a synthesis that manages to capture a broad subject in under 250 pages: producing the genealogy of the different economic thoughts in the very long run with the idea of weakening, so to speak, our mainstream assurances by demonstrating how much economic thought developed in the Muslim world could claim ancient roots. Implicitly there was a desire to emphasize how much the dominant – and at that time super-dominant – economic thinking fitted in only a short tradition, that of the children of Adam Smith, which dates back to the last quarter of the 18th century, while the economic thought of Islam was revealed to be heir of the Greco-Roman world, that is, of this classical Antiquity that we had previously so strongly claimed as our own. In this sense, Professor Baeck's book not only invited us to take more seriously into consideration a tradition that had been devalued to the point of having to be, as it were, rediscovered, but it also was meant to introduce a cultural shift. Indeed Baeck indicated to what extent what could appear to be a foreign tradition was in fact our own and this in the long run much more vitally than the hegemonic neoclassical thought process, which all but appeared to be a historical epiphenomenon. With hindsight, the book offers strong and fairly visionary arguments for an economic humanism.

What, then, is this Mediterranean tradition of which the Muslim world would be the depositary? The issue may be summarized by stating that the Mediterranean tradition is characterized by the embeddedness of the economic in the social reality; meaning that all economic acts are inevitably integrated into a set of social constraints that embody and determine them. The rationality of the *homo oeconomicus* (the tradition which Baeck calls Atlantic economics) is here subordinated to the rationality of the *homo* in the context of the group to which he or she belongs. Summarising beyond what is reasonable in order to come to my topic that results in presumed losses in terms of performance for gains, equally presumed, in terms of solidarity. To focus on emblematic examples, we may mention interest-free loans or the obligation of offering material assistance.

What to think of this relationship with the Arab world with roots in the ancient model? What should we think of the Mediterranean tradition described as placing the interests of the group above those of the individual? Taking care not to enter into a subject matter that is not mine, Islam and its economic thought, in what follows I would like to focus on the classical (or 'ancient') Greco-Roman economies: I do this because there have been remarkable changes between yesterday's and today's insights.

Primitivism and Modernism

The views on the ancient economies as described by Louis Baeck are a fair reflection of the specialists' opinions dominant in the 1980s, that is, at the height of what we call 'primitivism'. 'Primitivism' is opposed to 'modernism', and in fact, this opposition essentially covers what Louis Baeck calls the 'Mediterranean' and the 'Atlantic tradition'. The main fault line between the two is the predominance either of the group or of the individual.

The primitivist – modernist dispute is presumed to have dominated the thought of the specialists of ancient economies for nearly a century. In fact it was essentially the work of a single scholar, Moses Finley (1912-1986), who forged its genealogy up to the last third of the 19th century.[2] What is it about? In essence, it is meant to remove modernity's ingenuous and anachronistic glasses which made specialists look at ancient societies as being in no way different from ours. Following the 19th century evolutionary movements, primitivism describes economic history as if it went through different stages: on the one hand, the domestic, civic, national, and world economies and, on the other, economies embedded in society and set free from it. Finley contends that the Greco-Roman world, which he takes as a whole, did not consider economics as knowledge *per se* because the economy was presumed to be always integrated in the society. In the Greek world, the two treatises of this nature that have come to us, *Economics* ascribed to Aristotle and *Ways and Means* by Xenophon, *de facto* offer foremost on the one hand a list of stratagems and on the other a manual for the domestic economy (the literal etymology of the word 'economy': the management of the *oikos*, the house). Finley also drew arguments from the absence of words defining realities like 'budget' to postulate the absence of this reality in Antiquity.

The primitivists' vision, sometimes called 'substantivist' (a sophisticated term to describe the simple fact that economies were presumed to be mainly of the subsistence type with no large surplus to reinvest), focussed on the fate of the great majority of the population (over 85%) described as rural and living largely autarchical lives. In this context, individual profit was seen as a danger to be fought (chrematistics: the desire to possess ever more); there was insufficient money and credit was weak; the possibility of the acquisition of *terra nullius* by a non-citizen was blocked by a 'legal wall'; big business was of little importance. In short, the conditions for economic growth following the virtuous circle of liberal economics (division of labour – rising productivity – accumulation of profits – productive reinvestments) were presumed to be lacking.

For their part, the modernists, a name invented by the primitivists, focussed on another reality, residual in the primitivists' view, that of big commerce and monetised exchanges which they analysed with tools inherited from Adam Smith.

Superimposed on these diverging views of the ancient economies were other differences characteristic for the practitioners. In general, primitivists were historians – philologists, initially specialists of early periods (archaic and classical Greece), and, if we may say so, with political convictions situated rather or radically on the left. The modernists were rather historians – archaeologists, specialists of late periods (the Hellenistic and Roman worlds), and situated more to the right of the political spectrum.

In the 1980s, primitivism certainly had the upper hand. Established partly on the fertile ground of the *Ecole des Annales*, it easily fitted in a Marxist perspective, at the time still very pervasive. But in reality, in 1994 when *The Mediterranean Tradition in Economic Thought* was published, specialists of ancient economies had already partly abandoned the dominant primitivism that marked the 1970s and 1980s. Finley died in 1986. Especially the enormous contributions from field archaeology undermined considerably the Finleyan orthodoxy.

Because beyond the sensitivities of the time – the *Zeitgeist* – and beyond political opinions, one fact had clearly emerged in a quantifiable and robust manner: the ancient world, in particular the last two centuries BC and the first two AD, were characterised by economic performances that were for long time unequalled. It was not so much the data on Gross Domestic Product (GDP) – whose value is very difficult to compute for the Roman world (and illusory for the Greek city states with the exception of Athens) – which led to this observation. Rather it was the accumulation of other more robust parameters. For brevity, doubtless to the astonishment of the non-specialist, we can state that compared to England in the mid-19th century, the Hellenistic man was physically taller, lived in noticeably larger houses, had more purchasing power, and was part of a distinctively more equitable society characterised by a larger middle class. Other parameters like the number of shipwrecks in the Mediterranean, the atmospheric pollution by copper and lead, and the size of certain kinds of installations like fish tanks, confirm that the ancient world experienced an economic development that remained unsurpassed up to the modern era.

Important contributions have also been provided by epigraphic studies and the good financial records that we have of the Greco-Roman world. It is possible to identify set-ups of a financial engineering nature like interest-bearing capital investment with the components of interest specified as recapitalisation, utilisation and risk premium. The existence of credit has also been completely revised upwards, with an average usury rate of 12% per annum. The idea that people in the ancient world did not try to maximise their profits, as suggested by a reading of Plato and Aristotle, can no longer be sustained. This is clear from, amongst other works, the writings of Menander, Plautus, and Terentius, which commonly focus on the need to obtain money.

New Institutionalism

From a more theoretical perspective in recent years the dominant approach has not been primitivism but new institutionalism, with the obligatory reference to Douglass North (1920-2015), who was awarded the Nobel prize for economics in 1993 for his work in collaboration with Robert Fogel on cliometrics (new quantitative economic history).[3] At the top of the new institutionalism's agenda are choices made under constraints, transaction costs, and the two rationalities, in the short term the individual's and in the long term the group's. The newly existing hegemony of neo-institutionalism does not mean a peace of the brave at the crossroads of ancient primitivists and modernists. It is a scarcely disguised victory of the modernists in the sense that neo-institutionalism is not a frontal critique outside mainstream thought, as Veblen's institutionalism was a century ago, but rather an internal and toned-down critique: how to reintroduce the time and all constraints that turn the perfectly informed and perfectly free to choose *homo oeconomicus* into a myth?

Douglass North himself had quite bended his thinking in his later works and paid more attention to culture than to economic factors. For the non-specialist who would follow the debates, the line between – for brevity and therefore omitting the finer points – colleagues from the Anglo-Saxon world, especially Americans, like Peter Temin at MIT, who do not hesitate to apply the mainstream apparatus to the ancient economy, and the more European continental tradition in which sociological realities dominate economic factors, has recently been quite blurred.[4]

Briefly and even though we must always consider the optical distortion effects associated with the ideas of the time (largely controlled, but for how long, by mainstream economic thought), the vision of solidarity as described by Louis Baeck under the moniker of 'Mediterranean tradition' has been losing its lustre. At the microeconomic level, the individualism of the 'Atlantic tradition' is the engine that in the ancient world sustained the growth process during several centuries.

To this should be added, at the macroeconomic level, another 'black' lesson from the ancient world: the importance of war, by nature difficult to model and therefore rarely taken into account in economic models. Today's world functions with the software of growth based on technological innovation. This is a fairly recent model, let us say from the Industrial Revolution onwards. Much more frequent through the ages and on the earth's surface, growth has in the first place been predatory. The transfer of wealth from the peripheral areas of the world to the centre is a great classic. It was this transfer, and not technical improvements which later come to support it, that henceforth made possible economic growth.

Emblematically, it should be recalled that money, which is my speciality and with which I take pleasure to conclude, was not invented and coined to facilitate exchange, as has been repeated by every book on political economy, but to finance expenses that were first and foremost military. It was to finance war that over 80% (the estimate is rather on the low side) of the money stock issued in Antiquity was produced, and not or hardly to facilitate commercial transactions.

With respect to economic practice, we are thus, more than Professor Baeck might have imagined based on the information disposable to him thirty years ago, the beneficiaries for better or for worse of this Greco-Roman world, on which otherwise, on a cultural level, we have always put claims.

Notes

1. Baeck, L. (1994). *Mediterranean Tradition in Economic Thought*. London: Routledge.
2. See e.g., Finley, M. I. (1973). *The Ancient Economy*. University of California Press.
3. See e.g., North, D. C. (1990). *Institutions, Institutional Change and Economic Performance.* Cambridge University Press
4. See e.g., Temin, P. (2012). *The Roman Market Economy.* Princeton University Press.

15. Modern Egypt and Political Islam

Political, Demographic, and Religious Fault Lines

Emilio Platti

Levantine Background of Egypt

The modern history of Egypt begins with Muhammad Ali, an Ottoman general who expelled Napoleon out of Egypt. He declared himself Wali (protector = ruler) of Egypt, made the country de facto independent, although it still belonged de jure to the **Ottoman Empire**, and launched a thorough modernisation campaign. His grandson, Said Pasha, started with the construction of the Suez Channel. The successor of Said Pasha, however, accumulated international debts which led to the invasion of Egypt and the take-over of the government by Great Britain in 1882. Egypt, Cairo and Alexandria in particular, were a **melting pot** of all sorts of influences: Ottoman, Jewish, Greek, Italian, and, near the end of the 19th century, of course also French and British.

The **cosmopolitan Levantine culture** was experienced by the average Egyptian as a dominant, foreign culture, embodied by a foreign elite.

When in 1922 Egypt achieved (partial) independence under the rulership of Sa'd Zaghlul, the Levantine elite continued to rule over the Egyptian society. Egyptian nationalism has a strong secular character and became the source of legitimacy of the military coup of the colonels in 1952.

Revolution of 1952: Egypt for the Egyptians

For the first time in almost three millennia, Egypt was ruled again by an Egyptian, moreover by someone who did not belong to the privileged class.

Due to nationalisations, however, Cairo and Alexandria lost their cosmopolitan character and national elites left the country. The Jewish community and culture, which was rather active in Egypt, disappeared nearly completely, especially after the 1956 Suez Crisis.

Secular nationalism – with a socialist underpinning – became the dominant ideology. Egypt became one of the leaders of the 'non-aligned countries' (together with Yugoslavia, India etc.). Intellectuals in Egypt (and the Islamic world) accepted a new basis for legitimacy: nationalism (with the support of the military) within the framework of a Pan-Arabic (and Pan-Turkish) nationalism, not based on Islamic Law. The slogan becomes 'Revival' and under the motto of one language, one culture, with as goal one nation, reaching from the Gulf to the Oceans. Religion is relegated into the background.

The nationalisation of the Suez Channel leads to a rupture with the West, and an approachment towards the Soviet Union, which helped finance the construction of the Assouan Dam. The government also launched an industrialisation programme including among others large-scale heavy industry (iron and steel, cement etc.).

The feudal system is broken down and large land ownership nationalised. It is the end for the (feudal) large land owners and the Pasjas, being the elite of the previous regime.

Explosive Increase of Population

This evolution takes places against the backdrop of an explosive population increase: nowadays according to the Bureau of Statistics, there are more than 100 million inhabitants. This is roughly five times more than during the coup of the colonels in 1952.

It is also important to note that the median age of the Egyptian population actually is 25 years, meaning that half of the population is younger than 25 years old! For comparison, the median age of the Belgian population is 42 years.

Combined with the progression of urbanisation, the population explosion creates insurmountable problems for public spending related to health, education, housing, mobility, and job creation.

Two Revolutions

Spring 2011: the fall of Mubarak

A third ideology (not nationalism or political Islam) inspired the revolution of January 2011. The idea of a nation-state with participatory civil democracy is central to this revolution. The pride of belonging to a country as exceptional as Egypt, where Coptic Christians and Sunni Muslims live together, is an important part of the revolutionary élan. The idea of national unity without discrimination is important in a country with 90% Sunni Muslims.

Egypt is not the only country in which a revolution for civil democracy has taken place. Other countries experienced a similar revolution: Indonesia 1998 (Suharto), Tunisia 2011 (Ben Ali), Yemen 2011 (Saleh), Libya 2011 (Kaddafi), Syria 2011 (Bashar).... The evolution can be explained by the crumbling of the legitimacy of the authoritarian, post-colonial regimes (Pan-Arabic nationalism), due to wide-spread corruption, arbitrary police actions, violence, repression, forged elections....

The idea of national unity rising above differences in religion, however, faded into the background and in July 2011, Islamic political activism got the upper hand. On the Tahrir Square, radical Islamic slogans are exclaimed and during the first free elections in Egypt in December 2011, the Muslim Brothers win 50% of the votes and the Salafi 25%. In June 2012, the Muslim Brothers' candidate, Mohamed Morsi, is elected with a slight majority, against his opposing candidate Ahmed Shafik, who embodied the old regime.

The democratic legitimacy is replaced by an Islam-based legitimacy: all power comes from Allah; Shari'a is the only source of legislation and jurisprudence. Political Islam strives for a single model of the Islam way of life and this singular way of life for the people becomes: 'No other God than Allah' – 'The Koran is our constitution'.

This Islamic activism goes back to the Muslim Brotherhood founded by Hasan al-Banna in 1928 and the radical Muslim Brotherhood-ideologist Sayyid Qutb (executed by Nasser in 1966). The principles of the teachings of Qutb can be summarized in a few words: human sciences are not necessary; philosophical thinking is pagan; only

Islam is civil and human; other cultures are ignorant about the true human nature, created by God; Western capitalism is an internally organised system of usury.

A second revolution: Towards the end of President Morsi

The idea that Islam is the solution to all political, social, and economic problems leads to intolerance and conflicts in the Egyptian society. In doing so, the new legitimacy based on the political Islam is undermined. This leads to violence against Christians: on 7 April 2013 the Saint Mark's Coptic Orthodox Cathedral in Cairo is attacked; on 11 December, Saint Peter and Saint Paul's Church in Abbassiyya-Cairo is bombed. Sufi Muslims also fall victim to violence and Sufi sacred places, such as the Sheik Zayed City and the Sheik Zayed Shrine, are targeted for attacks.

The extremist Sunni movement also surfaces in other countries. In a similar vein, Shiá and Sufi shrines are destroyed in Saudi-Arabia, Iraq, Libya, Mali, Syria....

In Egypt, a popular reaction against the policy of the Muslim Brothers does not stay away. As one Imam phased it: 'the Shari'a law imposed by the Muslim Brothers is the law of al-Banna and Sayyid Qutb, not that of the Shari'a of the Holy Prophet Muhammad'. During massive demonstrations, the crowd demands the departure of Morsi.

On 3 July 2013, a declaration of the Supreme Command of the army is proclaimed by Abd al-Fattah al- Sissi in the presence of the Great Imam, the Coptic Patriarch, and the representatives of all the political parties with the exception of the Muslim Brothers.

Post-Revolutionary Era of President Sissi

The demand for legitimacy arises again: the option for Egyptian nationalism resurfaces. Sissi bases himself on his predecessors Nasser and Sadat: 'Neither the Brothers nor the Salafi: our revolution is the revolution of the Egyptians!'

General Abd al-Fattah al-Sissi wins the new elections of June 2014: he strives for a 'strong, righteous, and safe nation'.

In August 2013, the army occupies by force the square around the Râbia al-Ádawiyya Mosque, occupied by the Muslim Brothers. 'Râbi'a', which also means 'fourth' in Arabic, becomes, with four fingers held up, the symbol of resistance against Sissi; the resistance by the sympathizers of the Muslim Brothers is still continuing. Also Erdogan, whose policy is in line with that of the Muslim Brothers, holds up four fingers as a protest against the reign of Sissi.

The Al Azhar Document for Basic Freedoms of Sheik Ahmed al-Tayyib proclaims four additional freedoms: freedom of religion, freedom of opinion and the expression thereof, freedom of scientific research, and freedom of literary and artistic creativity. In a new Constitution, the role of Shari'a is revised: the legislation stands for a civilian (i.e., not a clerical or a military), democratic, and modern state, Egypt. The new legislation is accepted by means of a referendum in the beginning of 2014.

In the meantime, a law has been enacted forbidding all demonstrations. It implies in fact a strong repression against Muslim Brothers, but also against democratic youths who stand up for democratic freedoms. Hence, the final question: is this the beginning for a new legitimacy of a military nationalism?