No. 25

The Political Economy of Europeanized Financial Regulation[1]

Universiteit van Amsterdam,
The Netherlands

Daniel Mügge
d.k.muegge@uva.nl

Please cite this working paper as:
Mügge, Daniel (2012), 'The Political Economy of Europeanized Financial Regulation', *GR:EEN Working Paper, No.25*
www.greenfp7.eu/papers/workingpapers

[1] The author gratefully acknowledges research assistance by Bart Stellinga, support the Harvard University Center for European Studies (CES), and the comments of anonymous reviewers for the CES working paper series and the *Journal of European Public Policy*.

This research acknowledges the support of the FP7 large-scale integrated research project **GR:EEN - *Global Re-ordering: Evolution through European Networks***
European Commission Project Number: 266809

Abstract

Over the past two decades, the European Union (EU) has become a central actor in financial regulation and developed complex institutions to govern financial markets. Recent scholarship has detailed the functioning of these institutions and revealed their inner dynamics. At the same time, however, the political-economy embeddedness of financial regulation, which had inspired early research on European financial integration, has increasingly dropped out of the picture.

This essay makes the case for putting this embeddedness central once again and exploring how the Europeanization of financial regulation has affected the political-economy make-up of Europe. To do so, scholars need to study finance not only as a service sector, but also as that facet of the economy that creates and allocates credit and financial investments. Beyond the evolution of socio-economic orders inside Europe, a focus on such links provides novel avenues for making sense of the European role in global financial governance.

Introduction

In the decade prior to the financial crisis, European Union (EU) institutions such as the Commission have become central players in financial regulation, both vis-à-vis member states and on the global stage.[2] In response, EU financial regulation has emerged as a distinct field of study that has analysed regulatory and institutional reforms and the drivers behind them. A first wave of research had asked who supported EU financial integration, on which terms, and why; it mostly drew on comparative political economy for answers.[3] Once supranational actors had been installed, scholars zoomed in on them to unravel the real-world functioning of EU regulatory policy and the influence of the newly established institutions on policy output.

This scholarly focus on policy-making institutions de-emphasized how financial markets relate to and co-evolve with other facets of socio-economic orders – for short, the political-economy embeddedness of financial regulation. The financial crisis has been a powerful reminder, however, that this embeddedness still mattered enormously to the evolution of European capitalism, even if it had dropped out of the policy discourse. Thus, while early scholarship had asked how the political-economy make-up of Europe had affected EU financial integration, it is time to reverse the question: how has the Europeanization of financial integration affected the political economy make-up of Europe?

This essay will suggest two conceptual steps to address this question: first, scholars of EU financial regulation should take finance more seriously. Much recent scholarship in this area has treated finance primarily as a business sector,

---

[2] To aid legibility, I use 'financial crisis' through this article to denote of financial malaise of the past years even if the strength of the causal links between the subprime, banking, and sovereign debt crises as its components are still an open question.

[3] Unless specified otherwise, EU financial integration refers both to the cross-border integration of European financial markets (for a range of relevant indicators, see e.g. European Commission 2007 and subsequent versions of the Financial Integration Reports) and to the concomitant supranationalization of financial governance in the EU.

comparable to other service sectors. In spite of the important insights thus generated, it is time to emphasize once more that the financial sector creates and channels debt, credit and investment in contemporary capitalism and that financial regulation shapes how it does that. The study of European financial regulation had become overly removed from the substance of what was being governed.

The second step follows directly: comparative political economy traditionally had charted how particular economic institutions, including financial markets, fit into wider institutional ensembles that were analysed for example as social systems of production or varieties of capitalism. Changes in financial markets then mattered because they reverberated throughout economies. While in and of itself, this perspective has continued to thrive over the past years (e.g. Glyn 2006, Krippner 2011), it has mostly been divorced from scholarship on the overhaul of EU financial regulation and governance (Macartney 2009 is an exception). This essay suggests avenues for bridging this gap.

This shift in perspective from finance as a business sector to finance as credit creation and allocation also opens new avenues for studying the role of Europe in global financial governance. The global standard setting literature commonly suggested that the substance of international standards followed from countries' avoiding adjustment costs for domestic firms. The focus on credit creation through the financial sector points in different directions to explain its international position, for example to the dependence of European economies on private sector credit creation. It offers an alternative way of thinking about the "purpose" (Posner and Véron 2010) that may underlie position-taking in global negotiations than the one now common in studies of EU financial regulation.

The spirit of this essay is to suggest what it sees as fruitful and pertinent avenues for future research. Intriguing questions, rather than definitive answers, is what it seeks to provide. To do so, it first traces the shift in emphasis from political economy to institutional analysis in this field over the past two decades. The sections

that follow first make the theoretical case for re-embedding financial regulation and then propose ways in which this embeddedness has mattered to the real-world evolution of European capitalisms and the EU role in global financial governance. In keeping with the mission of this essay, it will be left for future research to determine just how relevant and strong the causal links suggested here are.

Studying EU financial regulation: from political economy to institutional analysis

The first wave of EU financial integration came in the wake of the single market programme of the mid-1980s (Sandholtz and Zysman 1989). Charged with designing a European regime for financial services, member states initially made little progress. The Second Banking Coordinating Directive of 1989 implemented EU-wide what had already been agreed in the Basel Accord under US pressure a year earlier (cf. Oatley and Nabors 1998). Common rules for capital markets proved almost impossible to attain (Steil 1993). National financial models differed too much to agree on a single template (cf. Coleman 1996), and the "battle of the systems" produced a relatively weak compromise replete with loopholes only in 1993 (Story and Walter 1997, cf. Brown 1997).

Scholarship of these developments was firmly rooted in political economy analyses: member state governments battled each other over market access abroad for their own firms (Underhill 1997, Moravcsik 1998: 355). The intellectual point of departure was the embeddedness of national financial systems and sectors in nationally idiosyncratic ensembles of economic institutions (Zysman 1983). Even though the emphases differed, comparative political economists commonly acknowledged that national financial systems had co-evolved with different modes of government intervention in economic affairs and national economic profiles (Crouch and Streek 1997, Hollingsworth *et al.* 1997, Kitschelt 1999, Hall and Soskice 2001)

and that they were governed with an eye to these institutional links (e.g. Loriaux 1997, Deeg 1999). [4]

Embeddedness mattered in other respects, too. Financial sector interests were largely organized on a national basis (cf. Coleman 1996, Josselin 1997), and governments functioned as conduits to channel these interests into international negotiations (Filipovic 1997). This “anchoring” of financial institutions in home countries implied relatively unambiguous regulatory and supervisory responsibilities for national authorities. [5] And internationally, the segmentation of financial sectors along national lines meant that there was no European voice to speak of. In the Basel Committee for Banking Supervision or the International Organization of Securities Commissions the United Kingdom sided with the United States in key debates, confronting Germany and France in particular (Underhill 1995, Filipovic 1997, Oatley and Nabors 1998).

The second wave of EU financial integration began in the mid-1990s. Financial firms from across the continent favoured pan-European expansion, requiring more integrated governance and a shift to the more profitable capital market activities hitherto concentrated in the City of London (Mügge 2010). Many governments looked at apparent US economic successes in the mid-1990s in envy and concluded that financial market overhaul in Europe might yield similar results (Bieling 2006). The EU Financial Services Action Plan, endorsed in 1999, spawned several dozen new directives to enshrine this vision in EU rules. With the establishment of the Lamfalussy process two years later, financial regulation was

[4] For the remainder of this essay, the “varieties of capitalism”-label will be used to denote nationally specific and often complementary economic institutions. Usage of label does not imply endorsement of the more specific conceptual claims advanced by the VoC-approach as proposed by Hall and Soskice (in particular, the CME/LME dichotomy) or its superiority over approaches, such as the French regulation school. For the purpose of this essay, it is the shared emphasis of various CPE-approaches on the embeddedness of institutions that is important, and the “varieties of capitalism”-label is the most established and least unwieldy one to highlight this point.

[5] The collapse of the Bank for Credit and Commerce International in 1992 triggered intensified international cooperation in this field.

effectively pooled in Brussels, even if collectively, national authorities retained much influence (Quaglia 2007, De Visscher *et al.* 2007). With the roll-out of the common currency around the same time, wholesale financial activity increasingly integrated across the continent, and governance had effectively become Europeanized.[6]

This development triggered a shift in scholarly emphasis. The supranationalization of financial regulation encumbered strictly comparative work with its emphasis on domestic institutions and cross-national variation. That said, the difficulty to accommodate finance in institutionalist depictions of contemporary capitalism went beyond a level-of-analysis problem. The disembedding of financial markets concerned not only their governance, but also their mode of profit generation (e.g. Das 2006). Certainly since the late 1990s, the growing importance of financial accumulation through purely financial means, for example the exponential growth in credit derivatives, has meant that finance as a social and economic sphere followed a trajectory that was increasingly detached from the rest of the economy – or so it seemed until the recent financial meltdown shook up national economies in their entirety.[7] It was (and is) not obvious how financial markets, and the influence their gyrations can have on the evolution of political economies and the institutions in them, can be integrated into models of the political economy that have essentially seen it as an ensemble of institutions that co-evolve over time in dialectical fashion (e.g. Streeck 2011).

On top, the rise of regulation as a particular mode of governance (Majone 1996, cf. Levi-Faur 2011) diverted attention from the political economy facets of financial regulation. Traditionally, CPE analyses had emphasized what Jayasuriya (2001) had called the "positive coordination" of economic institutions: individual institutions' place in a larger institutional ensemble was the key to understanding

[6] In contrast to wholesale activity, retail banking and insurance remained fragmented along national lines, much to the chagrin of the Commission (Grossman and Leblond 2011).
[7] Consider for example the record profits of Wall Street investment banks during the economic slump that followed the bursting of the dot.com bubble in 2000.

them, not least because scholars expected governance of these institutions to reflect such complementarities.

The dawn of "negative coordination" in the second half of the 1990s completely changed the perspective. Financial regulation was not only partially shifted to Brussels. It was also increasingly delegated to regulators whose task it was to administer markets not with an eye to national economic idiosyncrasies but in line with abstract and seemingly self-evident precepts such as market efficiency and consumer protection. From a facet of an integrated national economy, finance became a business sector to be regulated competently, and it was increasingly studied as such. Scholars put the new institutional arrangements under the magnifying glass to elucidate their inner workings (Moloney 2010, 2011a, 2011b, Quaglia 2010). As the European institutional web grew thicker, their emphasis shifted towards conceptual apparatuses common in other fields of EU regulatory competence, such as airlines, telecoms, and environmental, health and safety standards (e.g. Quaglia, De Francesco and Raedelli 2008).

This institutionalist scholarship revealed new drivers behind and obstacles to the further evolution of regulatory integration (Thatcher and Coen 2008): rational institutionalism highlighted veto players, and historical institutionalists pointed to path dependency and sequencing (e.g. Bach and Newman 2010). In new expert committees bargaining was partially supplanted by genuine deliberation about appropriate answers to regulatory challenges (Quaglia 2008). And as many institutional innovations defied categorization as either EU committees or inter-governmental bodies, their study as (transgovernmental) regulatory networks gained traction (Baker 2010, Posner 2010, Maggetti and Gilardi 2011).

While financial regulation was increasingly studied as the administration of a complex business sector, the political economy linkages that earlier comparative work had emphasized mattered as much as ever. Regulation still interacted with other facets of economic governance such as industrial or fiscal policy. It still had

clear distributive consequences. Public authorities remained responsible for safeguarding financial stability of their economies, and they still tried to make their voice heard on the global stage. With the inner workings of EU financial regulation now well charted, times has come to focus once more on the embeddedness of financial markets and ask how the Europeanization of financial regulation has left its mark across all these fields.

Putting "finance" back into the study of EU financial regulation

Analyses of these links begins with heeding a lesson that (re-)emerged from the crisis: finance is special. Financial markets may increasingly have been regulated with a mind-set that saw them primarily as markets for financial services not fundamentally different from, say, air transport. In that sense, analyses that conceptualized the sectorial politics as comparable to those in other service sectors may have been right on target. At the same time, the idea that finance as an economic domain is mainly a services sector is the regulatory equivalent to the view that money is just a neutral veil covering an underlying real economy, which has no other effect than influencing nominal price levels. As Keynes and many since him have stressed, the management of money is part and parcel of how economies are structured and evolve.

For the appreciation of EU financial integration, several economic effects of financial regulation are particularly important, and for each, we have to ask how it has been affected by the Europeanization of financial regulation. Most fundamentally, financial regulation shapes the creation of financial instruments and thereby the creation of credit. A credit default swap (CDS) – effectively an insurance against losses as a consequence of debtor default – makes a good example. On the one hand, a CDS can indeed be seen as insurance, and hence as a service like many others. On the other hand, a CDS creates an "investment" out of thin air. It is a

promise to pay in the future (contingent on a default) and once it becomes tradable, a CDS can circulate like any other financial instrument. In effect, a party issuing a CDS creates credit – money – where none existed before. The same is true for other complex derivatives that mushroomed before the crisis, most notoriously collateralized debt obligations. Private financial activity as a source of credit in turn has direct bearing on fields such as monetary policy and social policy, for example by providing private credit to compensate for welfare state retrenchment (Crouch 2011).

Financial regulation affects not only the creation of credit, but also its distribution: who can get it, and on which terms? The risk-weightings banks are required to attach to their loans influence the interest they will charge their customers, benefitting some and disadvantaging others (e.g. Claessens *et al.* 2008). The ability of lenders to parcel out and redistribute financial risks, as happened with real-estate loans in the subprime mortgage crisis, affects the availability of funds for prospective house-owners (Aalbers 2008). And the ease with which deposit-taking institutions can invest their customers' funds abroad influences how closely domestic savings match domestic investment and hence how international imbalances evolve.[8] We do not know how important these effects are, both across countries and compared to other factors, but it is clear that they matter.

Going beyond the financial sphere narrowly considered, financial regulation influences the relative attractiveness of competing investments. For example, financial regulation may allow, or even encourage, banks to use customer funds for cross-shareholdings rather than proprietary trading in bonds, stocks or derivatives, which may in turn buttress or undermine particular economic structures (Deeg 1999, Morin 2000). The conditions under which banks are allowed to lend into real-estate booms is particularly relevant: not only may they fund asset bubbles which have

[8] The obvious example here is the Eurozone crisis and the importance of cross-border integration of financial firms for the emergence of imbalances and for the difficulty to solve the crisis. While available evidence suggests clear links, these are as yet poorly understood and documented.

deleterious consequences when they burst (Schwartz 2009). Other economic sectors may face relatively higher borrowing costs than they otherwise would because of the apparently attractive yields in real-estate lending. On top, accounting standards and taxation regimes for financial gains may encourage or discourage long-term investments (cf. Perry and Nölke 2006).

In this way, financial regulation also has indirect distributive dimensions: for example, the availability of “patient capital” to German manufacturers generated job-security and stability for blue-collar workers in manufacturing; financial liberalization weakened both. Such distributive questions about financial regulation arise around the globe, but Europe is particularly fruitful to explore them: comparable rules have been rolled out across the continent over the past decade. With the diverse political economies it combines under one regulatory roof, the EU is a perfect environment to study comparatively the impact of regulatory reforms and the factors that condition it. The identification of net winners and losers is an important part of that agenda.

EU financial regulation and the transformation of European capitalism

Along all the dimensions outlined in the preceding section, the liberalization of financial services in Europe has reshaped the European economy. For the United States, this development has been analysed as financialization. Krippner (2005, 2011) has detailed how a succession of legislative changes has not only unshackled the financial sector itself (cf. from a different angle Johnson and Kwak 2011), but also changed the profile and modus operandi of many non-financial corporations as well as the channels through which wealth is accumulated and distributed (cf. Lazonick and O’Sullivan 2000, Epstein 2005, Froud *et al.* 2006).

Financialization has also received growing attention in Europe (for an overview, see Stockhammer 2007). But hitherto, European integration, and financial integration in particular, has remained disconnected from that research agenda, even

though EU financial regulation has been central to the financial reshaping of Europe (see, however, Bieling 2006, Macartney 2009). Here lies largely uncharted territory. What role has European financial regulation – which since the 2000s mostly meant EU rules – played in the reshaping of the European political economy? Has it spawned dynamics comparable to those in the USA? Why (not)? And how have the institutional specificities of European law-making, which institutional scholarship has drawn out so well, influenced the substance of rule output and hence its wider economic impact? For example, (how) has it mattered to the French economy that rules for the Paris bourse are no longer made by French authorities but European ones?

EU financial integration has been about creating markets both across and within borders. These twin projects have been two sides of the same coin: effective cross-border integration necessitated a "disengagement" of governments from their own financial sectors, and hence their governance in line with generic precepts to replace nationally idiosyncratic ones – the shift from positive to negative integration outlined above. In this way, the supranationalization of EU financial regulation has been intimately connected to "regulatory liberalism" (Gamble 2009) as a reform programme (Mügge 2011a). The supranationalization increasingly removed financial regulation from citizen control. Governments often outsourced depoliticized regulation to expert committees, not least to forestall politically costly battles. Regulatory networks as detached policy spaces flourished in this environment. Agreement on the merits of "innovation" allowed European regulators to coordinate regulatory details while sidestepping principled debates about the appropriate place of finance in contemporary societies, such as resurfaced after the crisis. And as the EU bureaucracy had a clear mandate to further integration, the shift of regulatory competences has had a self-reinforcing quality: it put people in charge who often had a mission to push integration even further.

The prevailing pro-market climate coupled with little external scrutiny – the EP proved ineffective as a check on regulatory reform – fostered dense ties between policymakers and the financial industry. Such ties had also existed when policy communities had still been largely national. But financial sector contribution to wider economic management, at least on the Continent, had been the flipside of financial firms' privileged access to government policy. In contrast, in the strong ties that developed between supranational actors and the financial industry such encompassing considerations played no role. Now, it was all about private sector advice for boosting the efficiency and "innovative" capacity of European financial markets.

The supranationalization of financial governance detached it from other facets of economic governance. To take just one example, publicly owned German wholesale banks – the *Landesbanken* – had been important facilitators of regional industrial policy, and they had linked local savings banks to global capital markets. But the new European regime had no room for government intervention in and support for financial firms. Reluctantly, regional German governments had to disengage their *Landesbanken* to ensure more "equal" terms of competition with private sector banks.

To be sure, EU financial integration has not only influenced the big European economies that have been the mainstay of CPE analyses (Zysman 1983, Schmidt 2002) and from which most examples in this essay are drawn. But we know very little about its impact in for example Scandinavian countries, Greece, Portugal, Ireland or Spain. With the integration of wholesale financial markets cheap credit could reach corners of Europe where hitherto it had been hard to come by, especially in those Mediterranean countries that also introduced the euro. Instead of having to rely on local savings, banks in the Southern periphery could now tap into international money markets to finance long-term loans to local customers. Such integration was an explicit policy goal, and the Commission presented it as a clear sign of policy

success (European Commission 2007). The results, now well-known and documented, were unsustainable booms in consumption and construction in countries where interest rate drops were most pronounced. The common currency added to overly optimistic risk assessments among investors. And the positive economic effects of the initial surge in available credit, due in this case to European financial integration, attracted more investors and funds, creating a financial bubble.

Taken together, these points not only suggest exploring how EU financial integration has transformed European capitalisms. It also raises the question to what degree such integration – both in markets and in their governance – has been wound up in the build-up of financial vulnerabilities that were unsustainable and would necessarily collapse. If the pre-crisis evolution of EU financial governance was part and parcel of the spread of financialization throughout Europe, the crisis may not have been an exogenous shock but an endogenous one. In addition, the same institutions that have intensified the financial vulnerability of European economies have proven inept at addressing the crisis once it emerged (High Level Group on Financial Supervision in the EU, 2009). The poly-archic nature of European governance hindered quick policy-adjustment, and regularly prevented bail-outs and border-spanning deposit insurance where they were needed. Was the pre-crisis mode of governance *necessarily* unsustainable because it systematically generated overly lax and ineffective policy?

Analysis of these issues will require varied data, conceptual steps and tools. We need to understand better how regulatory changes affect the behaviour of financial firms as well as debtors and investors. How has EU financial integration shaped the business models of banks throughout the EU? And how have changed business models affected the provision and distribution of credit? Answering these questions calls for a deeper engagement with (financial) economics (e.g. Baldwin and Wyplosz 2012), business studies (e.g. Berger *et al.* 2000, Slager 2004), and scholars from law and economics (Ferran 2004, Moloney 2010), who have often

asked questions pertinent to the transformation of European finance while remaining in a detached scholarly universe. Quantitative studies can use across-case variation between EU member states to establish the impact financial regulation has had on specific facets of national economies while qualitative scholarship can trace how a changed regulatory environment has affected behaviour of diverse economic agents.

On top, we will want to understand better to what degree and with which motivation public actors have supported or obstructed regulatory reforms. Past studies have tended to put business interests and the avoidance of adjustment costs central when explaining variation of governments' regulatory preferences (e.g. Mügge 2010). The depth of changes to the European economic landscape that the crisis has now exposed challenges us to take a hard look again: who has shaped EU regulatory overhaul, to what effect, and why? If the transformation that EU financial integration has wrought on European capitalisms is as significant as this essay suggests, it will be worthwhile looking beyond the immediate preferences of relevant actors and exploring their embeddedness in the structural transformation of the European economy. At the same time, we will have to ask how ideas and commonly held beliefs have mattered to battles over EU financial integration (Quaglia 2011, cf. Woll 2008, Abdelal, Blyth and Parsons 2010). Had it been inspired by a particularly "neoliberal" understanding of the world, and if so, does widespread criticism of these ideas in itself change the thrust of contemporary regulatory politics? Post-crisis EU reforms provide an excellent opportunity to assess the importance of (perceived) material interests, policy-making institutions, ideas and structural economic transformations for regulatory overhaul.

The global context

The political economy approach to EU financial regulation also opens fruitful avenues for making sense of the EU's role in global financial governance. Extra-European

relations in finance require a somewhat different approach than the intra-European research agenda laid out so far. For the latter, institutionalist scholarship has supplied a thorough account of how policy-making operates, allowing scholars to build on these insights when asking for the wider effects of Europeanized financial regulation throughout the European economy. In contrast, our understanding of the EU's role in global financial governance is less advanced, not least because it emerged much more recently and because we do not have a rich heuristic, like that provided by comparative political economy for intra-European developments, to understand what animates the EU in its global actions, what determines its relative success, and how we should assess the effects of such governance.

What exactly is to be won or lost in global cooperation? Singer (2007) has modelled the policy preferences of financial regulators as a trade-off between relatively lax standards that benefit domestic financial firms and tighter rules meant to boost financial stability. International cooperation, he argues, arises when international competition makes it impossible to achieve both goals at the same time unilaterally. International minimum standards prevent a regulatory race to the bottom. What then shapes the substantive preferences of negotiating parties? Ceteris paribus, they favour the internationalization of domestic rules to minimize adjustment costs or of regulation that, at the margin, privileges domestic firms in international competition (e.g. Oatley and Nabors 1998). In such an analysis, the political economy embeddedness of financial markets apparently plays no role.

The EU has seen its international profile wax over the past decade or two. The regulatory one-way traffic that transatlantic rule harmonization used to be (Simmons 2001) has given way to rules travelling in both directions – from the US to Europe and vice versa (e.g. Posner 2009, Eberle and Lauter 2011, Leblond 2011). Much scholarship investigating this shift has taken market size as its starting point (cf. Drezner 2007): states' control over domestic market access is their principal bargaining chip in international regulatory coordination. The concentration of

European regulatory competences in supranational hands substitutes one giant financial market for more than two dozen much smaller ones (Posner 2009). EU bargaining power rises, even if the relationship is not linear (Mügge 2011b).[9]

What has the EU done with this newly-won influence? Posner and Véron (2010) found the EU's motivation to seek international regulatory influence unclear – it had accumulated "power without purpose". The absence of a clear European policy agenda may seem in tension with our intuition that great powers secure seats at the negotiating table with unambiguous goals in mind. Many observers had expected the EU to promote a radically different blueprint for global rules flowing from the more coordinated market model prevalent on the Continent. But the overall thrust of EU policy has not been to unseat financial markets from the dominant position they had acquired in Europe. Why not?

Once we tie EU financial regulation to the overhaul of European capitalisms more broadly, the question is not merely one about the ability of the EU or the USA to play cannily a coordination game in international standard setting. Instead, we ask for the willingness and ability of the EU to reverse both the disembedding of financial markets from other facets of economic policy and the financialization of European economies more generally. A range of hypotheses emerge: maybe European economies have become so dependent on private sector credit creation that a return to financial repression is unappealing? Or maybe disembedded and globally integrated financial sector interests dominate in the end, ensuring a convergence of regulatory preferences across the Atlantic?

Most intriguing for the purpose of this essay, as well as most troubling, are those explanations that draw directly on the Europeanization of financial regulation itself to explain the inertia in EU regulatory policy: maybe the key factor is that the EU who represent the EU globally have an institutional bias in favour of negative

[9] Note that the concentration of regulatory competences swings free of its success in spawning actual market integration (Grossman and Leblond 2011).

coordination of policy, and hence against re-embedding financial markets, as that has been the model of EU institutional development for the past two decades? In addition, the on-going sovereign debt crisis in Europe has exposed the inability of European institutions to address trouble in financial markets effectively, among others because national fiscal authorities have political difficulties supporting financial firms that are integrated across borders. Hence, the EU has been relatively ineffective in taming its home-grown financial crisis, and it may well be this lack of a capacity to act forcefully internally that prevents a more encompassing overhaul of the European economic model and hence also explains regulatory inertia in international reforms.

Adjudication between these claims will require much more detailed empirical analyses than we have so far, and the methodological challenges they present are formidable. But if we want to make sense of what the Europeanization of financial regulation means for the EU's global role and its ability and willingness to push financial governance in a different direction than that pursued over the past decades, it will be fruitful to reconnect such analyses with the embeddedness of financial markets in contemporary capitalism.

Conclusion

Financial regulation shapes credit creation and distribution, financial flows, banks' business models and through these channels affects the evolution of economies at large. This essay has argued that the study of EU financial regulation stands to gain from reengaging scholarly perspectives that put such effects of central. In a nutshell, it has suggested analysing how the Europeanization of financial integration has affected the political economy make-up of Europe. The research questions and fields that belong to such a research agenda should not be understood as substitutes for the institutional scholarship that has dominated the study of EU financial regulation in

recent years but as complements. Institutionalist work holds many insights that will be indispensable for answering the questions raised in this essay.

If the links between EU financial regulation and political economies at large are as relevant as suggested here, scholars of such regulation will have contributions to make that go beyond their own field, European Studies or research on financial regulation itself. Arguably, comparative political economists have insufficiently incorporated (the politics of) financial regulation in their analyses of continuity and change in contemporary capitalism. Economists who study financial markets and firms and their evolution over time need to appreciate financial regulation as a structuring force. Law and economics scholarship has made valuable contributions here. But it is scholars of European financial regulation and the politics surrounding it who are uniquely placed to analyse and demonstrate how the evolution of European finance and its governance are two sides of the same coin and matter for the evolution of European capitalism as a whole.

References

Aalbers, M. (2008) 'The Financialization of the Home and the Mortgage Market Crisis', *Competition & Change* 12(2): 148-166.

Abdelal, R., Blyth, M. and Parsons, C. (eds) (2010) *Constructing the International Economy,* Ithaca: Cornell University Press.

Bach, D. and Newman, A.L. (2010) 'Transgovernmental Networks and Domestic Policy Convergence: Evidence from Insider Trading Regulation', *International Organization* 64(03): 505.

Baker, A. (2010) 'Deliberative international financial governance and apex policy forums: Where we are and where we should be headed', in Underhill, G., Blom, J. and Mügge, D. (eds) *Global Financial Integration Thirty Years On*, Cambridge: Cambridge University Press, pp. 58-73.

Baldwin, R. and Wyplosz, C. (2012) *The Economics of European Integration,* 4th ed., Berkshire: McGraw Hill.

Berger, A., Bonime, S., Covitz, D. and Hancock, D. (2000) 'Why are bank profits so persistent? The roles of product market competition, information opacity, and regional/macroeconomic shocks', *Journal of Banking & Finance* 24: 1203-1235.

Bieling, H. (2006) 'EMU, financial integration and global economic governance', *Review of International Political Economy* 31(3): 420-448.

Brown, P. (1997) 'The Politics of the EU Single Market for Investment Services: Negotiating the Investment Services and Capital Adequacy Directives', in Underhill, G. (ed.) *The New World Order in International Finance*, Houndmills: MacMillian, pp. 124-143.

Claessens, S., Underhill, G. and Zhang, X. (2008) 'The Political Economy of Basle II. The Costs for Poor Countries', *The World Economy* 31(3): 313-344.

Coleman, W. (1996) *Financial Services, Globalization, and Domestic Policy Change,* Basingstoke: MacMillian.

Crouch, C. and Streek, W. (eds) (1997) *Political Economy of Modern Capitalism: Mapping Convergence and Diversity,* London: Sage.

Crouch, C. (2011) *The Strange Non-Death of NeoLiberalism*, Cambridge: Polity.

de Visscher, C., Maiscocq, O. and Varone, F. (2007) 'The Lamfalussy Reform in the EU Securities Markets: Fiduciary Relationships, Policy Effectiveness and Balance of Power', *Journal of Public Policy* 28(1): 19-47.

Das, S. (2006) *Traders, Guns & Money. Knows and unknows in the dazzling world of derivatives*, London: Financial Times Press.

Deeg, R. (1999) *Finance Capitalism Unveiled: Banks and the German Political Economy,* Ann Arbor: University of Michigan Press.

Drezner, D. (2007) *All Politics is Global. Explaining international regulatory regimes,* Princeton: Princeton University Press.

Duménil, G. and Lévy, D. (2011) *The Crisis of Neoliberalism*, Cambridge MA: Harvard University Press.

Eberle, D. and Lauter, D. (2011) 'Private interests and the EU-US dispute on audit regulation: the role of the European accounting profession', *Review of International Political Economy* 18(4): 436-459.

Epstein, G. (ed.) (2005) *Financialization and the World Economy,* Cheltenham: Edward Elgar.

European Commission (2007) *European Financial Integration Report*, Brussels.

Ferran, E. (2004) *Building an EU Securities Market,* Cambridge: Cambridge University Press.

Filipovic, M. (1997) *Governments, Banks and Global Capital,* Aldershot: Ashgate.

Froud, J., Johal, S., Leaver, A. and Williams, K. (2006) *Financialization and Strategy. Narrative and Numbers,* London: Routledge.

Gamble, A. (2009) *The Spectre at the Feast. Capitalist Crisis and the Politics of Recession,* Houdmills: Palgrave MacMillian.

Glyn, A. (2006) *Capitalism Unleashed. Finance, Globalization and Welfare,* Oxford: Oxford University Press.

Grossman, E. and Leblond, P. (2011) 'European Financial Integration: Finally the Great Leap Forward?', *Journal of Common Market Studies* 49(2): 413-435.

Hall, P. and Soskice, D. (eds) (2001) *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage,* Oxford: Oxford University Press.

Helleiner, E. and Pagliari, S. (2011) 'The End of an Era in International Financial Regulation? A Postcrisis Research Agenda', *International Organization* 65(1): 169.

High-Level Group on Financial Supervision in the EU (ed) (2009) *Report [De Larosière Report],* Brussels.

Hollingsworth, J.R. and Boyer, R. (eds) (1997) *Contemporary capitalism: the embeddedness of institutions,* Cambridge: Cambridge University Press.

Jayasuriya, K. (2001) 'Globalization and the changing architecture of the state: the regulatory state and the politics of negative co-ordination', *Journal of European Public Policy* 8(1): 101-123.

Johnson, S. and Kwak, J. (2010) *13 Bankers. The Wall Street Takeover and the Next Financial Meltdown,* New York: Pantheon.

Josselin, D. (1997) *Money Politics in the New Europe. Britain, France, and the Single Financial Market,* Basingstoke: MacMillian.

Kitschelt, H., Lange, P., Marks, G. and Stephens, J. (eds) (1999) *Continuity and Change in Contemporary Capitalism,* Cambridge: Cambridge University Press.

Krippner, G. (2005) 'The financialization of the American economy', *Socio-Economic Review* 3(2): 173-208.

Krippner, G. (2011) *Capitalizing on Crisis. The Political Origins of the Rise of Finance,* Cambridge MA: Harvard University Press.

Lazonick, W. and O'Sullivan, M. (2000) 'Maximizing shareholder value: a new ideology for corporate governance', *Economy and Society* 29(1): 13-35.

Leblond, P. (2011) 'EU, US and international accounting standards: A delicate balancing act in governing global finance', *Journal of European Public Policy* (3): 443-461.

Levi-Faur, D. (2011) *From Big Government to Big Governance?* Jerusalem Papers in Regulation and Governance No. 35, Jerusalem.

Loriaux, M. (1997) 'Socialist Monetarism and Financial Liberalization in France', in Loriaux, M., Woo-Cumings, M., Calder, K., Maxfield, S. and Pérez, S. (eds) *Capital Ungoverned: Liberalizing Finance in Interventionist States*, Ithaca: Cornell University Press, pp. 120-161.

Macartney, H. (2009) 'Variegated Neoliberalism: Transnationally oriented fractions of capital in EU financial market integration', *Review of International Studies* 35(2): 451-480.

Maggetti, M. and Gilardi, F. (2011) 'The policy-making structure of European regulatory networks and the domestic adoption of standards', *Journal of European Public Policy* 18(6): 830-847.

Majone, G. (ed.) (1996) *Regulating Europe,* London: Routledge.

Moloney, N. (2011a) 'The European Securities and Markets Authority and Institutional Design for the EU Financial Market - A Tale of Two Competences: Part (1) Rule-Making', *European Business Organization Law Review* 12(1): 41-86.

Moloney, N. (2011b) 'The European Securities and Markets Authority and Institutional Design for EU Financial Markets - A Tale of Two Competences: Part (2) Rules in Action', *European Business Organization Law Review* 12(2): 177-225.

Moloney, N. (2010) 'EU financial market regulation after the global financial crisis: "more Europe" or more risks?', *Common Market Law Review* 47(5): 1317-1383.

Moravcsik, A. (1998) *The Choice for Europe. Social purpose and state power from Messina to Maastricht.* Ithaca: Cornell University Press.

Morin, F. (2000) 'A transformation in the French model of shareholding and management', *Economy and Society* 29(1): 36-53.

Mügge, D. (2010) *Widen the Market, Narrow the Competition. Banker interests in the making of a European capital market,* Colchester: ECPR Press.

Mügge, D. (2011a) 'From pragmatism to dogmatism. EU governance, policy paradigms, and financial meltdown', *New Political Economy* 16(2): 383-402.

Mügge, D. (2011b) 'The European presence in global financial governance: a principal-agent perspective', *Journal of European Public Policy* 18(3): 383-402.

Oatley, T. and Nabors, R. (1998) 'Redistributive Cooperation: Market Failure, Wealth Transfers, and the Basle Accord', *International Organization* 51(1): 35-54.

Perry, J. and Nölke, A. (2006) 'The political economy of International Accounting Standards', *Review of International Political Economy* 13(4): 559-586.

Posner, E. (2010) 'The Lamfalussy Process: Polyarchic origins of networked financial rulemaking in the EU', in Sabel, C. and Zeitlin, J. (eds) *EU Governance: Towards a New Architecture?*, Oxford: Oxford University Press, pp. 43-60.

Posner, E. and Véron, N. (2010) 'The EU and financial regulation: power without purpose?', *Journal of European Public Policy* 17(3): 400-415.

Posner, E. (2009) 'Making Rules for Global Finance: Transatlantic Regulatory Cooperation at the Turn of the Millennium', *International Organization* 63(4): 665-699.

Quaglia, L. (2011) 'The 'Old' and 'New' Political Economy of Hedge Fund Regulation in the European Union', *West European Politics* 34(4): 665-682.

Quaglia, L. (2007) 'The politics of financial services regulation and supervision reform in the European Union', *European Journal of Political Research* 46(2): 269-290.

Quaglia, L., De Francesco, F. and Raedelli, C. (2008) 'Committee governance and socialization in the European Union', *Journal of European Public Policy* 15(1): 155-166.

Quaglia, L., Eastwood, R. and Holmes, P. (2009) 'The Financial Turmoil and EU Policy Co-operation in 2008', *Journal of Common Market Studies* 47(Annual review): 63-87.

Quaglia, L. (2010) *Governing Financial Services in the European Union,* London: Routledge.

Quaglia, L. (2008) 'Financial Sector Committee Governance in the European Union', *Journal of European Integration* 30(4): 563-578.

Sandholtz, W. and Zysman, J. (1989) '1992: Recasting the European Bargain', *World Politics* 42(1): 95-128.

Schmidt, V. (2002) *The Futures of European Capitalism,* Oxford: Oxford University Press.

Schwartz, H. (2009) *Subprime Nation,* Ithaca: Cornell University Press.

Simmons, B. (2001) 'The International Politics of Harmonization: The Case of Capital Market Regulation', *International Organization* 55(3): 589-620.

Singer, D. (2007) *Regulating Capital. Setting Standards for the International Financial System,* Ithaca: Cornell University Press.

Slager, A. (2004) *Banking across Borders,* Rotterdam: Erasmus Research Institute of Management.

Steil, B. (ed) (1993) *Competition, Integration and Regulation in EC Capital Markets,* London: Royal Institute of International Affairs.

Stockhammer, E. (2007) *Some Stylized Facts on the Finance-Dominated Accumulation Regime,* Amherst, MA: Political Economy Research Institute WP 142, University of Massachusetts Amherst.

Story, J. and Walter, I. (1997) *The Political Economy of Financial Integration in Europe: The Battle of the Systems,* Cambridge: MIT Press.

Streeck, W. (2011) 'Taking capitalism seriously: towards an institutionalist approach to contemporary political economy', *Socio-economic review* 9(1): 137-167.

Thatcher, M. and Coen, D. (2008) 'Reshaping European Regulatory Space: An evolutionary analysis', *West European Politics* 31(4): 806-836.

Underhill, G. (1995) 'Keeping governments out of politics: Transnational securities markets, regulatory cooperation and political legitimacy', *Review of International Studies* 21(3): 251-278.

Underhill, G. (1997) 'The Making of the European Financial Area: Global Market Integration and the EU Single Market for Financial Services', in Underhill, G. (ed.) *The New World Order in International Finance*, Basingstoke: MacMillian, pp. 101-123.

Vogel, D. (1995) *Trading Up. Consumer and Environmental Regulation in a Global Economy,* Cambridge: Harvard University Press.

Woll, C. (2008) *Firm Interests. How Governments Shape Business Lobbying on Global Trade,* Ithaca: Cornell University Press.

Zysman, J. (1983) *Governments, markets, and growth,* Ithaca: Cornell University Press.