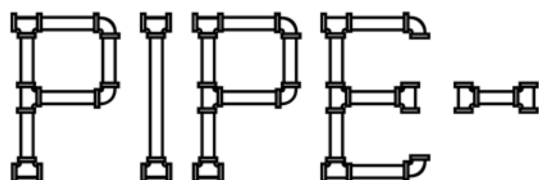

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Hrsg. von Prof. Dr. Susanne Lütz

Sebastian Schneider

Varieties of capitalism, varieties of crisis response
Bank bailouts in comparative perspective

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Abstract

Given recent history it may be necessary to recall that the so-called Great Recession we have been witnessing for more than five years now was, first and foremost, a crisis of financial markets. One reason for rising debt levels at the outset of the crisis have been massive government expenditures to bail out struggling and even failing banks. Yet, I argue that it falls short of a satisfactory explanation to simply view political action as a rational response to "objective" political and economic problems.
Therefore, the fundamental question that underlays this study is: How did different institutional settings influence diverging policy reactions to the financial crisis? To answer this question, this study compares bank bailouts in France, Germany and the United Kingdom. Drawing upon the Varieties of Capitalism literature, I identify four central, national institutions that have influenced political decision-making during the financial crisis: the political system, traditions of market intervention, economic discourse and banking and financial systems.
The French president, Nicolas Sarkozy, reverting to France's *dirigiste* tradition and resorting to a dense elitist network, used bank bailouts to support the French financial industry and to create "national champions". This sort of policy was accompanied by a non-liberal discourse criticising "excessive" financial markets. In Germany, on the other hand, the government deliberated with a broad coalition of political and market actors to create a bailout programme aiming at sustaining bank lending to the industry. However, market actors were criticised on a moral and ethical basis and the ordo-liberal state was considered as a necessary corrective safeguarding true economic freedom. Finally, the UK's "elected dictator", Prime Minister Gordon Brown, used his political power and involved his close political allies to carry out a bailout programme that was predominantly designed to defend the international competitiveness of the British financial industry. Albeit market intervention was inevitable it was announced as being temporarily and leaving as much problem solving as possible to the markets.

Zusammenfassung

Angesichts der jüngeren Geschichte scheint die Erinnerung notwendig, dass die derzeitige Wirtschaftskrise zunächst als Bankenkrise begann. Zur Beilegung dieser Krise und zur Rettung zahlreicher Kreditinstitute, setzten die Regierungen in Europa und Nordamerika Summen bisher ungeahnten Ausmaßes ein. Diese Bankenrettungsprogramme waren jedoch mehr als nur eine rationale Lösung für bestehende wirtschaftliche Probleme.
Wie diese Arbeit zeigt, hatten nationale Institutionen großen Einfluss auf politische Entscheidungen im Rahmen der Bankenrettung. Ein Vergleich zwischen Deutschland, Frankreich und Groß-Britannien zeigt, welche historisch gewachsenen Institutionen dabei eine entscheidende Rolle spielten und wie sie das taten. Vier zentrale, nationale Institutionen lassen sich mithilfe der *Varieties of Capitalism*-Literatur identifizieren: Das politische System, des Verhältnis Staat-Markt, der ökonomische Diskurs sowie das Banken- und Finanzsystem.
Die deutsche Regierung verhandelte die diversen Bankenrettungen mit einer breiten Koalition politischer und Marktakteure, mit dem Ziel, die Kreditvergabe an die heimische Industrie zu stabilisieren. Begleitet wurde dieses Vorgehen von einem ordo-liberalen Diskus. Die Bankenrettung in Frankreich hingegen wurde durch den Präsidenten dominiert, welcher dabei auf ein Netzwerk aus politischen und Wirtschaftseliten zurückgriff, um „nationale Champions“ zu schaffen. Hinzu kam ein kapitalismuskritischer öffentlicher Diskurs. In Großbritannien spielte Premier-Minister Gordon Brown eine beinahe ebenso dominante Rolle. Mit dem vorrangigen Ziel, die Wettbewerbsfähigkeit des Finanzstandortes London zu erhalten, griffen in Groß-Britannien vor allem Marktmechanismen und ein neoliberaler Diskurs.

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Abkürzungsliste

CC	Comparative Capitalism
CEO	Chief Executive Office
CME	Coordinated Market Economy
EC	European Commission
EU	European Union
GDP	Gross Domestic Product
FMSA	Bundesanstalt für Finanzmarktstabilisierung
HRE	Hypo Real Estate
IKB	IKB Deutsche Industriebank AG
IPE	International Political Economy
KfW	Kreditanstalt für Wiederaufbau
LB	Landesbank
LME	Liberal Market Economy
RBS	Royal Bank of Scotland
SFEF	Société de Financement de l'Economie Française
SMB	Small and Medium-sized Businesses
SME	State-influenced Market Economy
SoFFin	Finanzmarktstabilisierungsfonds
SPPE	Société de Prise de Participation de l'Etat
UK	United Kingdom
UKFI	United Kingdom Financial Investments
U.S.	United States
VoC	Varieties of Capitalism

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Introduction

The so-called Great Recession[1] we have been witnessing for more than five years now has been, first and foremost, a crisis of financial markets. Yet, today's political discourse is dominated by warnings about “excessive” sovereign debt and how it depresses economic growth (Reinhart & Rogoff 2010). However flawed Reinhart's and Rogoff's study might have been, the vice-president of the European Commission, Olli Rehn, the British Chancellor of the Exchequer, George Osborne, and Germany's minister of finance, Wolfgang Schäuble, all quoted it to motivate austerity policies and programmes (European Commission 2009a; *Die ZEIT,* 27 June 2013; *The Guardian,* 18 April 2013).

In the light of this reinterpretation of a crisis of financial markets into a crisis of sovereign debt it may be easily forgotten that one reason for rising debt levels at the outset of the crisis have been massive government expenditures to bail out struggling and even failing banks. In my study, I intend to focus on this aspect of the Great Recession. Therefore I analyse bailout programmes in France, Germany and the United Kingdom (UK). The impact of the crisis on these countries' national economies diverged as significantly as their economic recovery in its aftermath. This aspect may serve as a first point of reference to better understand political reactions to the crisis. Yet, I argue that it falls short of a satisfactory explanation to simply view political action as a rational response to “objective” political and economic problems. Thus, the fundamental question that underlays this study: How did different institutional settings influence diverging policy reactions to the financial crisis?

An economic crisis of this extent is a one-of-a-kind event that eludes itself from being an object of simple solutions (and explanations). Rather, the “New Age of Uncertainty” that we are living in may produce “a larger degree of uncertainty about the trajectory of policy within any one country, and variability in policy between countries” (Coen & Roberts 2012: 8; see also Blyth 2013a). What, then, forms the basis of political decision-making in times of crisis? What should be assumed to influence policy in today's complex political economies?

One approach to better understand the pathways of political decision-making emphasises the importance of political and economic institutions. However, if we accept that institutions influence decisions we still need to clarify how they exert this influence and how far it goes. Drawing upon the literature on Varieties of Capitalism (VoC) and comparative capitalisms (CC), I argue that political economies are complex entities comprised of historically grown and socially constructed institutions that influence political decision-making. To understand the political reaction to the Great Recession, it is necessary to take these institutions in consideration. Furthermore, I draw on Schmidt (2008, 2009, 2011) when I identify political discourse in these countries as a decisive explanatory factor in addition to the political system, state-market relations, and the financial system.

Outlining the historical development of these institutions in France, Germany and the UK makes it feasible to generate well-grounded hypotheses about a probable pathway of bailout policies. An empirical analysis of the actual bailout programmes in these three countries shows that such hypotheses indeed are useful to predict and assess policy outcomes. The French president, Nicolas Sarkozy, reverting to France's

[1] For a “brief etymology” see *The New York Times,* 11 March 2009.

dirigiste tradition and resorting to a dense elitist network, used bank bailouts to pamper the French financial industry and to create “national champions”. This sort of policy was accompanied by a non-liberal discourse criticising “excessive” financial market behaviour. In Germany, on the other hand, the government deliberated with a broad coalition of political and market actors to create a bailout programme aiming primarily at sustaining bank lending to the industry. However, market actors were criticised on a moral and ethical basis. The ordo-liberal state was considered a necessary corrective safeguarding true economic freedom. Finally, the UK's “elected dictator” (*Spiegel-Online,* 14 October 2008), prime minister Gordon Brown, used his political power and involved his close political allies to carry out a bailout programme that was predominantly designed to defend the international competitiveness of the British financial industry. Albeit market intervention was inevitable it was announced as being temporarily and leaving as much problem solving as possible to the markets.

This paper is organised as follows. In the first part I locate my theoretical approach within the general academic debate and set out my concrete research objectives. The second part introduces my theoretical framework and describes how it may be applied to comparative political economy. The subsequent chapter identifies the institutions that constitute a national economic system according to my theoretical approach. Part 4 elaborates on my methodological course of action. The following section consists of the historical case studies and develops hypotheses. Part 6 presents the empirical analyses of the respective bailout programmes conducted by the French, German as well as the British government. Section 7 sums up and puts the empirical cases in comparison. A final section concludes.

1. The debate

1.1 IPE and the Great Recession

According to Katzenstein & Nelson the field of International Political Economy (IPE) has been "curiously silent" (2013a: 1101) about the Great Recession. One reason for that can be seen in the disciplines' "intellectual monoculture" (McNamara 2009) and its one-sided focus on rationalism and quantitative methods. Rationalist approaches are said to have unnecessarily narrowed our perspective and to have failed to make sense of the causes of the crisis (Cohen 2009). Quantitative methods, on the other hand, are of limited use to interpret unique phenomena, such as a global financial crisis, that "come in such small numbers that statistical treatment is not an option" (Johnson *et al.* 2013: 1014).

What can be done about these shortcomings? Kirshner's (2011) answer is to put political science back into the centre of attention instead of purely economic explanations. One possible starting point for this may be "Analytic Eclecticism" (Sil & Katzenstein 2010). Two aspects characterise this approach. First, it advocates focusing on real-world developments, without "excessively simplifying such problems simply to fit the scholarly conventions or theoretical boundaries established by any one tradition" (ibid.: 10). Second, it suggests using insights from different bodies of research (Katzenstein & Nelson 2013a, 2013b: 251).

I intend to contribute to this discussion by incorporating rationalist as well as constructivist arguments in my study[2]. I argue that it is insufficient to view political actors as purely rational. Rather, actors should be understood as being "embedded" in a specific institutional environment and social relations (Granovetter 1985). Therefore, I present an approach to identify these institutional environments and to illustrate their explanatory power.

1.2 Research Objectives

Drawing upon the literature on VoC and CC, my main objective is to illuminate differences in government's policies during the early stages of the recent financial crisis. Specifically, I intend to explore the political economy of bank bailouts in France, Germany and the UK. I argue that diverging national economic and political systems are a key factor to explain differences between these countries' reactions to the financial crisis. Historically grown and socially constructed institutions are the building blocks of these different national systems. National institutional systems can be regarded as filters that "process similar, or even the same, problems each in their specific ways, resulting in characteristic policy outcomes and dynamics in different countries" (Busch 2008: 238). Politicians can be viewed as being influenced by as well as interacting with these institutions.

Three questions arise from this theoretical stance that need to be clarified. First, what are institutions? Second, which institutions constitute national economic and political systems and how do they influence political decision-making? Third, to what extent do these national systems differ from each other?

2 Although there is a debate that views these two approaches as being mutually exclusive, they can also be viewed as complementing each other (see Fearon & Wendt 2002).

2. Comparing national economic systems

Studies that compare institutions and national economic systems are legion (for an overview see Streeck 2010). In this chapter I will introduce one of the most important approaches, VoC, and illustrate how this approach has been developed further.

The main achievement of approaches that identify and compare different varieties of capitalism has been "to demonstrate that capitalism exists in a number of different institutional forms, not as just the single model implied by neoclassical economic theory" (Crouch 2005: 4). Jackson & Deeg identify three analytical assumptions that "inform and unify the diverse analytical frameworks within the […] literature" (2006: 11).

First, economic action goes beyond what transaction cost economics describe as coordination by markets or hierarchies (Williamson 1985, 1991). Rather, economic actors, being embedded in "structures of social relations" (Granovetter 1985: 481), need to be "coordinated or governed by institutional arrangements" (Hollingsworth *et al.* 1994: 4). These arrangements go beyond formal mechanisms that simply enable markets to function effectively.

Second, institutions within a national political economy do not randomly emerge but are the outcome of interdependencies. Institutions influence each other in their functionality. Over time this leads to "increasing returns" resulting in institutional arrangements that follow specific paths of development (Pierson 2000a, b). This argument disagrees explicitly with convergence theories. These theories assume that, as an answer to global competitive pressures, capitalist economies converge on a single, neo-liberal model of economic organisation. By contrast, the CC literature argues that these competitive pressures further accentuate differences in economic organisations and institutional configurations (Hancké 2009).
Third, institutional arrangements are compared to identify differences and similarities between national political economies. Here the main concern is to understand how these arrangements affect economic performance. It is argued that different economic systems feature different economic strengths in regard to innovation, economic equality and other outcomes.

2.1 Varieties of capitalism

Hall's and Soskice's (2001a) seminal study on the "Varieties of Capitalism" shall here serve as a first point of reference. Drawing upon classic accounts by, e.g., Shonfield (1965) and Katzenstein (1978), they develop an approach that centres on the firm as the main actor. Hall's and Soskice's argument is that economic institutions are necessary to and diverse in how they solve coordination problems between firms. Their concept of institutions follows North's classic definition of institutions as consisting of "both informal constraints […] and formal rules" (1991: 97).

Firms, it is argued, face coordination problems in different spheres (Hall & Soskice 2001b: 6)[3]. In any political economy there exists a set of institutions that help firms to resolve these problems. Firms can control the character of these institutions only partly. Still, these institutions "offer firms a particular set of opportunities" they can take advantage of (Hall & Soskice 2001b: 15). Therefore, it can be expected that firms develop certain strategies that benefit their purpose most. Consequently, Hall and Soskice argue that "there are important respects in which strategy follows structure" (ibid.).

As a result of historical "institutional developments in the wake of successive waves of socio-economic challenges" (Hall 2007: 40), these institutional settings differ from country to country. Therefore, VoC assumes corporate strategies to differ from country to country as well (Hall & Soskice 2001b: 15).

3 Namely industrial relations, vocational training and education, corporate governance, inter-firm relations and their relationship to their employees (Hall & Soskice 2001b: 7).

Hall and Soskice (2001b: 8) identify two ideal-types of economies, both of which are characterised by a specific set of institutions. On the one hand, there are *liberal market economies* (LMEs) that are preliminarily coordinated through hierarchies and markets (see Williamson 1985). The United States (U.S.) serves as the archetype of a LME. Relations between firms are dominated by competition and arm's-length transactions. On the other hand, there are *coordinated market economies* (CMEs) that are characterised by an important element of non-market coordination. Relations between firms are dominated by collaboration and strategic interaction. Germany serves as the typical case of a CME.

Each of these ideal-types features certain institutional complementarities. This means that some institutions facilitate the functioning and outcomes of other institutions and institutionalised practices and the other way round (Hall & Gingerich 2004; Milgrom & Roberts 1995). Consequentially, Hall and Soskice argue that nations "converge on complementary practices across different spheres" (2001b: 18).
The final aspect of this approach is what the authors call "comparative institutional advantage" (Hall & Soskice 2001b: 37). The fundamental assumption of this concept is that specific sets of institutions foster specific economic activities. For example, the institutional environment in CMEs is assumed to be advantageous for carrying out incremental innovation, while the institutional environment in LMEs supports firms carrying out radical innovation (Hall & Soskice 2001b: 38–39). This further promotes a path dependent development of national institutional systems (see also Pierson 2000a, 2000b).

To sum up, Hall and Soskice understand institutions as influencing actors' (i.e. firms) behaviour. These institutions differ from country to country and are the result of a historical development. Institutional complementarities make national political economies converge on two ideal-types each of both coming with certain comparative institutional advantages.

2.2 Agency, change and comparative political economy

Although the VoC approach had substantial influence on the discipline of comparative political economy, it has two major shortcomings worth considering. On the one hand, its focus on institutional stability fails to account for institutional change (Howell 2003). On the other hand, agency and diverging actors' preferences remain largely unnoticed (Allen 2004).

I argue that in order to resolve these issues, it is necessary to use an enhanced conceptualisation of institutions. First, institutions do more than just constrain actors' incentives and determine their action. Institutions may also be the object of action. Second, a closer analysis of institutional stability shows more subtle ways of how institutions change. Third, to fully understand how and why institutions change it is necessary to incorporate *ideas* into the analysis.

2.2.1 Conceptualising Institutions

The VoC approach has a rather narrow concept of institutions and how they affect individual actors. I argue that this concept is too limited for two reasons. First, VoC over-simplifies how institutions influence actors. From this point of view, "institutions determine actor strategies" (Deeg & Jackson 2007: 159). This conceptualisation of institutions is not able to explain actor strategies that are aimed at diverging from or even changing institutions. Second, VoC focuses solely on economic actors and, thus, "downplay[s] the role of politics and power" in creating institutions (ibid.).

Targeting these shortcomings Hall and Thelen introduce the concept of "institutions as resources" (2009: 10). From this point of view, institutions do not directly constrain and determine action but are "providing opportunities for particular types of action" (ibid.). This approach allows for institutions to also become "the object of such action" (Deeg & Jackson 2007: 159). Such a less deterministic conceptualisation of institutions focuses not on functionalist mechanisms of institutions but on "their distinct 'logics' and the different (and sometimes irreconcilable) set of values that govern them" (ibid.). Such an understanding of institutions allows conceding more autonomy and capacity to actors.

I understand institutions here as a historically grown "non-deterministic context for action" (Jackson 2010: 80). "While institutions may reduce uncertainty for actors, institutions do not fully circumscribe action" (Deeg & Jackson 2007.: 160). Yet, this does not mean that institutions are completely pliable. Rather, they may be seen "as a focal point for actors within an arena" (Jackson 2010: 81). Even if these actors decide to try to get rid of or to change these institutions, they make this decision within the existing institutional context.

2.2.2 Institutional Stability and Change

A common feature of institutionalist approaches to political economy is their general difficulty to (theoretically) account for change (Steinmo 2008: 129). Especially historical accounts usually focus on explaining rather long phases of institutional stability instead of change. If change occurs it is mostly understood as radical triggered by so-called "critical junctures", rare events such as wars or economic or financial crises (Capoccia & Kelemen 2007)[4]. In "normal" times institutional complementarities and path dependency are supposed to lead to stable institutional equilibria. Actors facing uncertainty over their prospects under alternative sets of institutions "may prefer the status quo to change" (Hall 2010: 207).

However, in complex environments such as national political economies institutions from different spheres often overlap and influence actors simultaneously (Hall & Thelen 2009; Jackson 2010). Gaps may arise between what a certain situation demands and what kinds of rules and uncertainty reduction an institution can provide. "[T]his suggests that actors respond to changing competitive economic pressures by regular experimentation with the institutions that govern them" (Deeg & Jackson 2007: 161). Institutions may change incrementally over a long period of time. Yet, change can be transformative nonetheless. Furthermore, institutional change may not necessarily implicate that old institutions are abolished and replaced by new ones. On the one hand, existing institutions may be adjusted towards new ends. On the other hand, new institutions may be built to safeguard existing objectives (Thelen 2003; 2004).

To sum up, institutions and their functions cannot satisfactorily be understood as merely representing an institutional equilibrium fulfilling an objective function at a specific moment in time. Rather, institutions are in a constant process of change. They are interpreted and reinterpreted by actors. Their functions cannot solely be derived from their formal rules. Rather, institutions permanently interact with their environment. Thus, effects and processes of change of institutions may best be understood, by applying a historically informed long-term perspective (Jackson & Deeg 2012).

2.2.3 Ideas and Institutions

Hall (1989) shows that economic ideas can be powerful indeed. Hall and his co-contributors describe how Keynesian and monetarist ideas influenced political agendas and institutional changes around the world. Various other constructivist authors have further specified the role of ideas in day-to-day (political) decision-making (e.g. on the financial crisis Blyth 2013a, 2013b; Gieve & Provost 2012). Thus, it can be argued that an extensive analysis of policy choices needs to incorporate the impact of ideas.

Campbell (2001; also Béland 2009) argues that ideas influence decision-making in two different ways. On the one hand they normatively constrain what actors perceive as politically acceptable. Thus, ideas and perceptions influence what actors perceive as the right and legitimate course of policy action (see also Hay 2011a). On the other hand, ideas can influence actors cognitively in that they enable actors to formulate solutions for political problems. These ideas can be "underlying theoretical and ontological assumptions about how the world works" (Campbell 2001: 170). Or they can be "technical and professional ideas that specify cause-and-effect relationships and prescribe a concrete course of policy action" (ibid. 167).

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4 However, there is plenty of evidence on institutional resilience in spite of such historical ruptures (e.g. Thelen 2003).

Furthermore, Blyth (2001) argues that ideas are of special importance in moments of crisis. Financial, economic or political crises are moments of great uncertainty. Since “such a situation is 'in a high degree unique,' agents' interests and the possible outcomes of their actions […] cannot be satisfactorily derived from structural location” (ibid.: 3). Therefore, actors need to individually interpret the situation they find themselves in. Ideas about the possible causes of and solutions to the crisis help actors to interpret their environment (Blyth 2002: 252-262). Thus, ideas reduce uncertainty by serving as blueprints for (political) action “that agents use to (re)structure their world, and the conventions that agents converge upon that give stability to that world” (Blyth 2011: 84).

Yet, an epistemological problems remains. Ideas are not easy to research since they “cannot be seen and are sometimes hard to track down” (Béland & Cox 2011: 13). Schmidt (2002; 2008; 2011) offers one possible solution to this problem. She introduces the concept of discourse defined by her as “whatever policy actors say to one another and to the public in their efforts to generate and legitimize a policy programme” (Schmidt 2002a: 210). This concept allows for an analysis of ideas and their impact on political decision-making. It understands discourse as representing the ideas policy-makers hold and exchange through an interactive process (Schmidt 2008). Schmidt does not deny the existence of a material reality. Rather, the interactive process of exchanging ideas is embedded in an institutional context (Schmidt 2011).

To sum up, ideas are an important aspect of how actors perceive the world and how it works. Thereby they reduce uncertainty for actors. Ideas affect what policies decision-makers perceive as legitimate as well as viable. Public discourse represents these ideas. Yet, this public discourse is not totally autonomous but is embedded in a specific institutional context.

2.2.4 Conclusion

I argue that capitalist economies may best be compared by taking into account their distinctive institutional settings. I understand institutions as a “non-deterministic context for action” (Jackson 2010: 80) that reduces uncertainty for actors. Institutions can change radically but in most cases institutional change is incremental and long-term. Ideas influence what kind of policy action may be perceived as legitimate as well as viable. Ideas and their influence on political decision-making can be grasped by analysing public discourse. This discourse is again embedded in an institutional setting.

3. Identifying national economic systems

In this chapter I specify how institutional systems vary. First, I argue, countries differ in their political systems. Second, countries have different approaches to market intervention and state action. Third, economic ideas that dominate the political discourse differ from country to country. Finally, there is variety between financial and banking system.

3.1 What role for the state?

In the wake of globally liberalised financial markets there has been a tendency of IPE to downplay the role of the state (Helleiner 1994, 1995). The state has been viewed as a servant of markets rather than as an actor on its own. In the CC literature the state has been denied an active role in the political economy (Jackson & Deeg 2008: 699–700). Schmidt makes an attempt to fill this gap by "bringing the state back in yet again" (2009). She defines the state as "the range of public institutions and actors that, whether alone or in interaction with private actors and institutions, can have a major impact on what happens in national political economies in a varieties of ways" (ibid.: 516-517).

First, there are "the political institutions that frame the interactions between political and economic actors" (ibid.). Schmidt identifies two different institutional settings (Schmidt 2006 2008, 2009, 2011). On the one hand, there are "simple" polities, "where governing activity is traditionally channelled through a single authority" (Schmidt 2006: 3). In this case governments are able to implement policy reforms swiftly and without having to make bigger concessions to political or regional oppositions. The main sanctioning mechanisms are elections and street protest. Simple polities are characterised by majoritarian, unitary states. In such polities the legitimising (or communicative) discourse towards the general public is assumed to be more sophisticated than the discourse coordinating different policy actors. On the other hand, there are "compound" politics, "in which governing activity is highly dispersed among multiple authorities" (ibid.). Here governments have to negotiate with a broad range of political and sometimes regionally dispersed actors before implementing policies. These systems are oriented towards consensus and the voting system is characterised by proportional representation. In such polities the coordinating discourse between policy actors is assumed to be more sophisticated than the legitimising discourse towards the general public.

Second, there are different approaches to market intervention and state action (Schmidt 2009: 521-522). The state may take up a liberal stance leaving market actors mainly autonomous. It sets the general rules and only intervenes if there are conflicts or when actors violate fundamental rules. On the other hand, the state may play a coordinating role conducting adjustment processes together with market actors. It acts as an arbitrator between market actors and leaves the administration of rules to them while being a coequal bystander in the background. Or the state may actively intervene in markets when it considers it necessary. Whereas adjustment processes in general are market-driven there are also areas where they are state-driven.

To sum up, this approach helps to analyse the role the state plays in national political economies. On the one hand, it distinguishes between different kinds of polities and their effect on political discourse. On the other hand, it helps to identify general modes of policy implementation and interaction with market actors.

3.2 Ideas and Action

Ideas influence what kind of policy action may be perceived as legitimate and viable. Although, basically, ideas are being held individually they may better be analysed as representing general beliefs that inform political action (Campbell 2004: 108–110; Schmidt 2002b, 2007). Neo-liberalism, for example, may be the

prevalent economic paradigm of our time. Yet, its specific occurrence differs from country to country (Schmidt & Thatcher 2013; Schmidt & Woll 2013). Although such an approach may not be able to explain the effect individual ideas have on individual action, it, nonetheless, may shed light on the general influence of publicly held economic ideas.

3.3 National financial & banking systems

One of the most widely used approaches to comparing financial systems distinguishes between market-based and bank-based systems (Allen & Gale 2000). It's very basic definition is that financial systems "are crucial for the allocation of resources in a modern economy" (ibid. 3). Therefore Allen and Gale classify financial systems by the main mechanism of allocation. They identify two ideal-types that slightly correlate with the ideal-types by the VoC approach (Deeg 2010). In Germany, for instance, banks are the most important financial institutions. Here financing is relationship-based with so-called *Hausbanks* keeping long-term reciprocal relationships with their corporate clients in the form of bank loans. Such a system is better suited to provide long-term investment for firms engaged in rather incremental but stable innovation (Rajan & Zingales 2003). In the US, on the other hand, capital is mostly provided by financial markets. They are dominated by arm's-length and deal-based relationships between investors and firms. Investors gain information about potential investments not from personal exchange but from market signals and publicly disclosed information. Such a system is assumed to have a comparative advantage in financing radical innovation in new technologies (ibid.).

A third ideal-type, identified by Zysman (1983), views some financial systems as being "state-dominated". *Dirigiste* France was an example for a state that strategically allocated and invested capital to promote specific firms and sectors. Yet, the significance of this third ideal-type waned since the 1990s due to the liberalisation of financial markets and a decreasing role for the state in this regard (Deeg 2010).

Lately Hardie *et al.* (2013) have criticized this dichotomy (or trichotomy) for not being able to account for recent developments in financial markets. They argue that bank-based as well as market-based financial systems have changed remarkably. In bank-based systems banks have increasingly engaged in market-based financial activities. In market-based systems banks have gained significant importance without these systems bearing resemblance to bank-based financial systems as described above. These changes have mainly been brought about by the banks themselves. To grasp these developments Hardie *et al.* introduce the concept of market-based banking (2013).

Whereas this term has been used before to describe the so-called system of "shadow-banking", Hardie and Howarth "broaden the definition to include all those parts of commercial banking that are […] dependent on the market" (2013a: 24). Although banks still provide loans to firms, "commercial banks have become more market based" (ibid.: 27). Yet, the authors do not assume a development of convergence to a single type of banking system. Although "the most important change in Europe is […] what has occurred on the balance sheets of the banks", there are still significant differences between countries (ibid.: 46).

To sum up, this concept helps to explain the impact of the financial crisis on the banking system of individual countries by pointing out not only the impact of financial market liberalisation but also the changing role and behaviour of banks in the run-up to the crisis. Furthermore, this focus sheds light on "the logic behind government policy responses" (Hardie *et al.* 2013: 17).

3.4 Short summary

The institutional setting that influenced political decision-making during the Great Recession consists of four different variables. There are, first, the organisation of the political system, second, approaches to market intervention and state action, third, ideas understood as general beliefs about rightful as well as productive policies and, fourth, financial and banking systems.

4. Methodological approach

This chapter sheds light on two methodological issues. First, I give a description how I will conduct my case studies and, secondly, I elaborate on the case selection.

4.1 Case studies

My approach is historical, qualitative, and comparative. It is historical in that I intend to "explain [specific] outcomes that have already happened" (Mahoney *et al.* 2009: 116). It is qualitative, because it generates "observations that cannot be assembled into a standardized rectangular data set but are nonetheless extremely useful fur causal inference" (Mahoney 2010: 124). And it is comparative in that I provide "narrative explanation[s] of a causal path that leads to a specific outcome" in three different countries (Vennesson 2008: 235).

The specific outcome I intend to explain is the difference in bailout programmes in France, Germany and the UK during the first years of the Great Recession. I argue that different institutional settings influenced political decision-making during the financial crisis. Thus, first, I describe the "historical context, which has a direct consequence for the decisions" made about bank bailouts (Steinmo 2008: 127). For this purpose, I give a historically informed overview on the political system, state-market relations, economic discourse and ideology as well as financial and banking systems in the run-up to the financial crisis. I then present hypotheses about possible policy outcomes based on my theoretical framework.

Thereafter, I conduct three in-depth case studies by providing a "detailed narrative" describing the events leading to the bank bailouts (George & Bennet 2005: 210). Within these case studies I intend to apply a positivist as well as an interpretivist perspective. It is my aim not only to discover a general causal relationship between institutional settings and policy action, but also to learn more about causal mechanisms (Lin 1998). In other words, I focus on the political processes that led to the specific policy outcomes to examine whether "the causal process" of my theory can be observed (Vennesson 2008: 232). Moreover, I focus on the discourse that accompanied this political process to "examine the reasons that actors give for their actions and behaviour and to investigate the relations between beliefs and behaviour" (ibid.: 233).

Finally, although generally speaking "the question of whether and how the resulting explanation might […] be generalized is a secondary concern" (Mahoney *et al.* 116) of qualitative historical approaches, I nevertheless compare the results of the three case studies to identify more general lessons that can be learned from them.

4.2 Country cases

As mentioned above, I will analyse three country cases: France, Germany and the UK. I chose these three countries because I assume them to significantly vary in their national economic systems. Therefore I expect to discover different bailout policies informed by this institutional variety.

In the VoC literature Germany and the UK each represent an ideal-type with Germany being the classical CME and Britain a clear example of a LME (Hall & Soskice 2001b: 16). Schmidt (2003; 2009) introduces France as a third ideal-type that she calls "state-influenced market economy" (SMEs). Schmidt has been criticised by proponents of typologies that adhere to Hall's and Soskice's analytical parsimony because she "conflates a distinctive mode of coordination with a different model of capitalism" (Hancké *et al.* 2007: 28). However, as I will explicate below, I find substantial evidence to assume that the institutional framework of the political economy in France, Germany and the UK varies extensively enough to

legitimise my case selection. Furthermore, inasmuch as I deviate from the parsimony that characterises the VoC approach I presume that "the gains in empirical coverage […] outweigh the losses in terms of analytical sharpness" (Hancké 2009: 15).

4.3 Empirical cases

A (bank) bailout occurs "when a government provides aid to (bails out) a financially distressed entity" (Wright 2013: 415). A bailout is a far-reaching government intervention in economic markets that even raises ethical questions (McGee 2008). Yet, during the first years of the crisis, financial sector rescue programs reached an unprecedented dimension and placed the state's "new power" at the centre of academic and political attention (Hassel & Lütz 2012).

France, Germany and the UK all conducted extensive rescue programmes to bailout financial institutions. Usually, such market interventions in European Union (EU) member states are comprehensively regulated by EU state aid law and competition policy (for a detailed account see Adriaanse 2012). However, due to pressure of time and the obvious need for action, the European Commission (EC) was willing to make concessions. Albeit a common framework for bank bailouts was agreed upon, these rules had only limited effects on national bailout policies (Russo 2012). Thus, it can be stated that the bank bailouts that occurred were "*national* solutions to a *common* problem" (Quaglia 2009: 1063). It seems therefore fit to assume that national institutions had a perceivable effect on national bailout programmes.

5. Historical case studies

This chapter compares the institutional settings in France, Germany and the UK before the crisis. First, I present the political systems. Second, I present the different approaches to market intervention and state action. Third, I give an overview of the general economic ideas informing political action in France, Germany and the UK. Finally, I describe the financial and banking systems in the three countries.

5.1 Simple and compound polities

This section classifies the political systems that characterise the country cases. Whereas France and the UK can be described as simple polities, Germany fits to the description of a compound polity.

5.1.1 France

France's political culture and system is clearly dominated by the figure of the directly elected president (for a detailed account see Gaffney 2010). The president is the main and decisive actor in policy-making. Although formally the prime minister is the head of government, the president sets the main political guidelines. Even if president and prime minister happen to be from different political parties (which has rarely been the case), prime ministers usually adhere to the president's policy-making power. Law-making is dominated by the government and leaves only secondary competences to parliament. President and parliament are elected by absolute majority voting. France is a unitary state par excellence where regions and communities have only minor competences (for a detailed account of France's political system see Kempf 2007).

5.1.2 Germany

Germany is a federal state by constitution. The so-called *Laender,* the regional states, enjoy widespread competences especially in law-making. Only a few policy areas are exclusively regulated by federal law. *Laender* and the federal state share competences in a great deal of law-making. The regional states are represented by the Federal Council that works as a counterpart to the Federal Parliament and is able to block federal law. This system results in extensive cooperation between federal and state level. Federal as well as state parliaments are elected by a proportional representation system. Thus, most of the time there are coalition governments by at least two parties resulting in the necessity to compromise in sometimes long-lasting coalition negotiations. On the federal level there has not yet been a single-party government. The president has a primarily representative function and is not directly elected. The head of government is mainly a *primus inter pares* and sets the political guidelines without having the all-embracing competences of the French president (for a detailed description of Germany's political system, see von Beyme 2010).

5.1.3 United Kingdom

Although the Queen (or King) is still the head of state in the UK, the prime minister is the central figure within the political system. One of his main sources of power is the appointment of ministers and other staff members. Furthermore, decisions by the prime minister are mostly made in intimate and opaque circles. Parliament is elected by relative majority voting resulting in clear majorities. Most of the time, governments have been single-party governments. The UK is a unitary state by constitution (see Sturm 2009 for a detailed account of the UK's political system).

To sum up, France's and the UK's majoritarian voting and unitary state systems make it possible for the heads of government to push through far-reaching political projects and reforms and, thus, they can be

described as simple polities. On the other hand, compromise between parties as well as federal and state level is central to Germany's political system. Thus, Germany can be categorised as a compound polity.

5.2 State action and market intervention

5.2.1 France

Economic policy-making in post-war France was dominated by an interventionary state as described by the term *dirigisme*. The state was heavily involved in the market by directing money to certain economic areas, centrally planning economic activity and extensive state ownership of banks and companies. This *etatist* economic system was radically reformed and liberalised in the 1980s (see Levy 1999; Schmidt 1996). Yet, "the road to a more market-centered political economy is paved with new state interventions" (Levy *et al.* 2006: 134). It can be argued that the *dirigiste* state has not been dismantled but redeployed. For example, on the one hand labour markets have been liberalised to increasingly allow firms market-led adjustment autonomous of state intervention. On the other hand, this deregulation has been met by a growing welfare state "pacifying and demobilizing the potential victims of this process" (Levy 2005: 104; Levy 2008).

Furthermore, the French state has replaced traditional industrial policy by more indirect measures to promote "national champions" and protect French companies (e.g. Clift 2013). One measure to protect French firms from foreign takeovers after the liberalisation of financial markets have been the so-called "hard cores" of major French firms "cemented by cross-shareholdings and interlocking board memberships" (Clift 2008: 201). Although these hard cores have been disbanding since the 1990s, personal networks between business and economic elites still play an important role in the French political economy. These networks are mainly a result of the common educational backgrounds of French elites. The alumni from the so-called *grandes écoles* still provide the "social cement of the French model" (ibid.; see also Schmidt 1996).

Still, French economic policy cannot be described as following a certain homogeneous conception. The structural transformation of the French political economy has, after the 1980s, been continuous and incremental (Amable *et al.* 2012). But there have been neoliberal as well as neostatist policy initiatives making French economic policy-making appear "unfocused and contradictory" (Levy 2013: 334).

To sum up, the French political economy cannot be described as *dirigiste* anymore. Yet, the state still plays a decisive role and intervenes directly if it deems it necessary. The state has moved from being "market-making" to "market-shaping" (Levy 2005: 105). Or as Howell (2009: 251) put it: "the state no longer directly organizes economic activity and its direct regulatory role has lessened […]. The importance of the French state now is its capacity to reform institutions in such a way as to encourage different practices […]." While certain tools and policies that have been associated with the *dirigist* framework have been dismantled, that is not "the same thing as dismantling that framework itself" (Levy 2006: 136).

5.2.2 Germany

In Germany, the state seldom directly intervenes in the market but rather coordinates market actors. Its main task is to set up and maintain a regulatory framework that guarantees the functioning of the market and sustains the freedom of economic actors. In labour markets, for example, the state supports the principles of codetermination and collective bargaining but leaves the concrete administration of these rules to the market actors and does not interfere directly (Wood 2001).

Furthermore, economic policy-making is characterized by a "high degree of consensual decision-making without direct state intervention" (Grossman 2006: 327; see also Cioffi 2004: 260–261). Unilateral political decisions are rare, which is also a result of Germany's neo-corporatist and decentralised political system (see also Reutter 2012). Economic reforms are embedded "within wider political compromises" with key societal groups (Schnyder & Jackson 2013). For example, "key institutions (formal rules) governing the

financial system are developed through a consensual bargaining process" that involves a variety of actors and business associations (Deeg 2005: 175). Moreover, "German banks and the federal government formed the core of a coalition" that initiated financial market reform (Lütz 1998: 166; Lütz 2005). The development and conceptualisation of a new supervisory body has also been the result of broad consultation between political and market actors (ibid.: 163). This kind of policy-making is embedded in a system of strong sectoral business associations and other "para-public institutions" (Wood 2001: 254).
Economic policy-making in general aims at sustaining "[m]acroeconomic stability, inclusive social policy and a sustained growth of industrial production" as well as a strong export-orientation (Bonatti & Fracasso 2013: 1028). These aims are supported by high public spending on infrastructure as well as research and development. Independent regulatory bodies are in charge for further policy objectives such as monetary stability or competitive markets and are removed from direct government intervention (Streeck 1997).

To sum up, the German state and its economic policy can be described as "enabling" and "coordinating" (Schmidt 2009: 519). Its ability to directly intervene in the market is institutionally constrained. On the one hand, critical policy tasks are conducted by independent regulatory bodies. On the other hand, important economic adaptations such as wage bargaining are exempt from direct government intervention. Rather, the states enables market actors to coordinate such tasks between themselves. Policy making is consensus-oriented and greatly influenced by neo-corporatist institutions.

5.2.3 United Kingdom

The British state has the potential for far-reaching institutional reforms and it has used this potential in recent decades to liberalise, deregulate and distance itself from intervention in markets. Ever since its "neo-liberal turn" the British political economy has been dominated by the prevalence of market mechanisms and is, thus, best described as LME (Hall & Soskice 2001b).

Direct intervention in markets has been almost completely disestablished. The welfare state is reduced and means-tested, public planning has been marginalised, public companies have been privatised and subsidies reduced or repealed. Most industrial sectors are left to self-regulation with the state keeping arm's-length distance (Gospel & Edwards 2012; Schmidt 2002: 160-164). The wider public sector is dominated by managerial and market-based practises. Economic policy-making is essentially monetarist with a focus on low inflation and the restricted use of active fiscal policy (Hodson & Mabbett 2009; Pollit & Bouckaert 2004: 292-299). Independent institutions serve the purpose of separating market regulation from the direct influence of politicians, thus, leading to the "depoliticisation" of economic policy-making (Burnham 2001; Froud *et al.* 2010).

The financial sector has a special significance for the British economy as well as for economic policy making. On the one hand, the financial sector and financial services contribute significantly to the UK's Gross Domestic Product (GDP) making the competitiveness of "the City" (of London) a main political priority throughout the political spectrum (Morgan 2012). On the other hand, the City and the financial sector have considerable influence on the decision-making process of the British government making "the City of London the most deeply historically rooted and the most formidable concentration of power in British society" (Johal *et al.* 2012: 68). This is not least because there have been close relationships between government, regulatory bodies and the banking sector. This concerns informal crisis-management (Froud *et al.* 2010: 28) as well as exchanges of staff (Frach 2008: 56 – 58).

To sum up, British economic policy-making is informed by a marginalised public sector and a liberalised private sector. Although the state generally has the capacity for far-reaching interventions in the market it does seldom make use of this potential. Market mechanisms usually prevail over other mechanisms of coordination.

5.3 Economic discourse

5.3.1 France

Liberalising reforms of the French political economy since the 1980s have not been accompanied by a legitimizing discourse. The French political economy was rather liberalised "by stealth" (Gordon & Meunier 2001). Neither right-wing nor left-wing parties were able to develop a discourse "that would serve to legitimize the country's liberalizing economic transformation in terms of national values and identity" (Schmidt 2002: 271). Rather, free markets remain illegitimate and economic liberalism a taboo that various presidents were unable to call into question (Culpepper 2006: 45; Perrineau 2013: 186-188). It is still more acceptable to remind the public of the "dangers of unfettered markets" (Gordon & Meunier 2001: 14).

If at all, liberalizing reforms were legitimised as a necessary reaction to the challenges of globalisation and European integration. A recurrent argument has been that if France were able to take a leading role in the EU it would be able to protect the French economy against "unharnessed globalization" (Abdelal & Meunier 2010: 363). Liberalising within the context of "managed globalization", it was argued, would enable the French state to protect its people against the "delocalization" of jobs and other dangers of unfettered markets (Abdelal 2007; Abdelal & Meunier 2010; Schmidt 2007). When French political or economic interests seem to be at stake, (indirect) state intervention remains the appropriate and legitimate means to defend these interests (Gualmini & Schmidt 2013: 359-360).

To sum up, French economic discourse remains highly sceptical of liberalism and free markets. Rather, it emphasises the role of the state as a guardian against the dangers unconfined free markets.

5.3.2 Germany

German economic thinking is informed by a body of thought that is best described by two terms: ordo-liberalism and social market economy. Ordo-liberalism incorporates a commitment to liberal values but within a social order guaranteed by the state. The state sets up a framework of rules that is seen as a pre-condition for the functioning of markets and that is able to remediate market failures (Sauerland 2012). In Sally's (1994: 463) words, "it is incumbent on the state to set up and secure the institutional framework of a free economic order, but it should not intervene in the competitive economic process". Not only is this "rule-based conception of political economy shared by most of the German political parties, it is also endorsed by most of the economic profession, domestic media and the larger public" (Berghahn & Young 2013: 775).

This order does not only include economic rules, but also a moral, social and, thus, political framework (Bonefeld 2013). Central to German economic discourse is not only stability and free competition but also moral and ethical values such as fairness and solidarity (Garrett 2001). Markets are not only seen as imperfect in that they can lead to cartelisation and other economic dysfunctions, they can also have "socially disruptive consequences" (Lehmbruch 2001: 92). Therefore, it falls to the state to protect individuals against economic risks they cannot cope with themselves while preserving values such as "the responsibility for one's fate and [the readiness] to participate in honest and free competition" (Erhard 1958: 184).

To sum up, ordo-liberal discourse views the state as a pre-condition of the functioning of markets in that it sets the rules and policies that prevent market disruptions. However, within this regulatory framework economic actors are allowed to act autonomously and without state interference. Nevertheless, economic actors are expected to abide by moral and ethical values such as responsibility, solidarity and fairness. In other words, "[o]rdoliberalism argues that economic freedom unfolds within legal, social, and moral frameworks, for which the state is responsible" (Bonefeld 2012: 651).

5.3.3 United Kingdom

The ideational turn from Keynesianism to Monetarism in the 1970s and early 1980s has sustainably changed economic thought and discourse in the UK. Thatcher's neo-liberal break with the UK's Keynesian past marked the rise of an "economic doctrine" (Hay 2001: 209) that informs economic policy making to this date (for a detailed historical account see Hall 1992, 1993). Neo-liberalism makes a roll-back of the state in all policy areas a pre-condition of economic growth. Although in the beginning it was a project of the conservative party, Tony Blair's "New Labour" made neo-liberal economic thought predominate at both ends of the political spectrum (Schmidt 2002: 301).

Fundamental to the British understanding of neo-liberalism is the assumption that the market is superior to the state in terms of the allocation of resources (for a detailed account see Hay 2007). The provision of capital for public projects (e.g. infrastructure) by private actors is viewed as being more efficient than public financing. The same holds true for the provision of public goods in general, where market and quasi-market mechanisms are supposed to be more efficient. From this follows, that the state should be limited to a non-interventionist role as a "facilitator and custodian rather than a substitute for market mechanisms" (Hay 2004: 508). This comes along with monetarist and supply-side economic policies. On the individual level economic imperatives are placed over principles of social justice. Social inequality is explained as an inevitable and worthwhile result of unequal performance. This emphasis on individualism and personal risk-taking implicates a retrenched welfare state that should avoid providing "disincentives to market participation" (ibid.).

Furthermore, British economic discourse justifies this prevalence of economic principles "in terms of the harsh economic realities of economic interdependence" (Hay & Smith 2005: 128). Globalisation, it is argued, exposes institutions on all governmental levels (from local to EU) to a "competitive audit" (Hay & Smith 2013: 296). Capital is perfectly mobile and may "exit" markets any time in search for more lucrative investments. The leaner the welfare state is and the more reluctant state intervenes in and regulates markets, the more attractive a political economy is for capital and investment. It is this neo-liberal model and its assumed competitiveness that needs to be defended against "more interventionist-inclined" European Union partners (Hay & Smith 2005: 151).

To sum up, economic discourse in the UK views market mechanisms as being generally superior and more efficient than state action. From this follows an emphasis on individualism and limited state intervention. Economic imperatives resulting from globalisation and unfettered financial markets further justify this neo-liberal stance.

5.4 Banking and financial systems

5.4.1 France

Until the 1980s the financial system was a central part of France's state-controlled economy. The state was deeply involved in financial activities through publicly owned enterprises and the state-led allocation of capital to finance particular economic activities. The state controlled big parts of the banking system. Bank debt was the most important source of corporate financing (see also Zysman 1983).

The reformation and liberalisation of the financial system was a central aspect of French economic reform in the late 20th century. One idea behind the deregulation of financial markets was that banks would provide long-term capital to small and medium-sized businesses (SMB) analogue to the "German model". Yet, the banks did not meet these expectations (Deeg & Perez 2000: 127–130). Rather, these reforms were accompanied by the markedly increasing importance of financial markets in general and equity financing in particular. Total financial market capitalization in France grew from 27% of GDP in 1975 to 186% of GDP in 2001 (O'Sullivan 2007: 398). Aggressive strategies of external expansion by leading French companies induced an increasing number of mergers and acquisition that increased the importance of financial markets even further (ibid.). Yet, banks still play a crucial role on the French financial market.

The French banking market is highly concentrated and some French banks are leading global players especially in retail and derivative banking (Hardie & Howarth 2009).

That said, these developments did not result in an "anglo-saxon style" financial system in France although financial market regulation was considerably liberalised. Rather, the "acceptance of some liberal 'shareholder value'-oriented elements co-exists with enduring attachment among French policy elites (of left and right) to 'stakeholder capitalism' institutions and norms and to co-ordinated, 'statist' French capitalism" (Clift 2009: 74). Concentration of ownership and other protective mechanisms "have erected new obstacles" that constrain foreign takeovers (Clift 2007: 563).

It is therefore not easy to categorize the French financial system, since "it contains features of the liberalized, deregulated, and more capital market-based British system but also features of the more protected, regulated, and bank-credit based financial systems of southern Europe and Germany" (Howarth 2013a: 129). The French banking system is dominated by a few global players that internationally engage mainly in retail banking. This structure and predominance is indirectly supported by the state.

5.4.2 Germany

For a long time, Germany has been perceived as having a classical bank-based financial system where banks are by far the most important sources of corporate financing (Allen & Gale 2000). The German banking system can be described as resting on three pillars: commercial banks, savings banks and cooperative banks (Hackethal 2004). The group of the commercial banks consists of a few big banks (e.g. Deutsche Bank or Commerzbank) and a number of smaller private banks. They are universal banks engaging in traditional banking business as well as investment banking. The savings bank group consists of small and (mostly) publicly owned banks that are supposed to serve a public interest, that is, support individual savings as well as providing capital to local communities. Their business activities are locally constrained. On a regional level, the so-called *Landesbanken* (LBs) serve as central banks to the smaller savings banks and provide loans and cash management to "their" state(s). Besides that, they also engage in universal banking and, thus, compete with the bigger commercial banks. The third group, the cooperative banks, consists of smaller banks that mainly provide local retail and lending services.

This banking system serves the main purpose of providing long-term financing to the industry and especially to SMBs. Especially the highly federalised savings bank system benefits from local proximity to enterprises and relational banking. This system of long-term industrial finance is an important aspect of and sustained by German industrial policy (Deeg 1999).

However, the German financial system has undergone significant reforms in recent decades (Lütz 2005; Nowak 2004). On the one hand, the close relations between banks and SMBs have stayed intact and the banking system still provides "patient capital" to the industry (Culpepper 2005; Deeg 2009). Household savings as well as investment have been equally resilient to change (Vitols 2004). On the other hand, commercial banks as well as LBs have in recent years increasingly engaged in investment banking and internationalised their business (Hardie & Howarth 2009; 2013b). By the same token did the importance of (international) equity capital rise in recent years, especially for large firms (Goyer 2007).

The German financial system stands out due to its heterogeneity and its high grade of decentralisation. It has a highly internationalised commercial banking sector while preserving its system of small savings and cooperative banks.

5.4.3 United Kingdom

In the UK, the financial sector has probably profited most from Thatcher's policies of deregulation and liberalisation. As mentioned above, the financial sector, concentrated in the City of London, is deeply entrenched within the British political economy. It always has 1been highly self-regulated and insulated

from political interventions. Close relationships between government and financial sector further supported the City's independence (Froud *et al.* 2010; Johal *et al.* 2012: 68–73).

The main impetus behind the so-called "Big Bang" that extensively liberalised financial markets in 1986 was to strengthen the competitiveness of London as a financial and banking centre. Although London already played an important role in financial markets before, it was still possible that it would be outpaced in the future by New York. The high degree of liberalisation of the British financial market and its openness to foreign investors became its main competitive advantage over its American concurrent (Morgan 2012). Over the years it gained immense significance for the British economy. In 2010 the financial industry and related services accounted for around 14% of the British GDP (Talani 2011: 16)[5].
This significance of the financial sector for the British GDP goes hand in hand with its insignificance for the industrial sector. Even before the crisis bank lending to the manufacturing sector was marginal and the financial sector has been largely uncoupled from the productive sector (ibid.: 16-20). This peculiarity of the financial sector may best be regarded as an important aspect of the so-called "'Anglo-liberal' growth model" that has marked the UK since the early 1990s (Hay 2011b: 4). This growth model is consumer-led, financed by private debt, based on swift access to credit and a de-regulated and highly securitised mortgage market. This "asset-based welfare", or "privatised Keynesianism" as Crouch (2009) puts it, is also a consequence of the limited British welfare state (ibid.: 7).

The British financial system may best be described as market-based. Financial markets are regulated at arm's-length and enjoy significant independence from political influence. However, its economic importance does not feed back into the "real economy". Furthermore, in the period since 2000 banks are increasingly engaging in equity and bond markets, making the British financial system one "that shares negative aspects of both bank- and market-based systems, with few of the positives and with additional sources of weakness" (Hardie & Maxfield 2013: 57).

5.5 Conclusion and hypotheses

This section sums up the institutional differences between France, Germany and the UK and compares them. A hypothesis is developed for each institutional feature. These hypotheses clarify the expected effect of the institutional feature on the bailout policy in each country.

Table 1: Political System

France	**Germany**	**United Kingdom**
Simple (majoritarian voting; unitary state)	**Compound** (proportional representation; federal state)	**Simple** (majoritarian voting; unitary state)

Hypothesis 1: I expect political decision-making in France and the UK to be dominated by the respective head of government without major consultation with parliament. I expect policy-making in Germany to be consensual and informed by profound consultation with parliament and regional states.

5 The manufacturing sector, by contrast, accounts for only 12% of GDP (Talani 2011: 16).

Table 2: State-market relations

France	Germany	United Kingdom
State-influenced (etatist; elitist; protectionist)	**Coordinated** (corporatist; consensual; enabling)	**Liberal** (arm's-length; deregulated; elitist)

Hypothesis 2: I expect the bailout programme in France to be dominated by the government, influenced by personal networks and having protectionist side-effects. Furthermore, I expect the German bailout programme to be consensual, informed by consultations with the private sector and to refrain from radical market interventions. Finally, I expect the British bailout programme to be as non-interventionist as possible and profoundly informed by the effort to preserve the competitiveness of London as a financial centre and influenced by the financial elites from the City.

Table 3: Economic discourse

France	Germany	United Kingdom
Etatist (non-liberal; market-sceptical; communicative)	**Ordo-liberal** (state-oriented; ethical; coordinative)	**Neo-liberal** (state-sceptical; competitive; communicative)

Hypothesis 3: I expect the bailout programme in France to be accompanied by a legitimising discourse that criticises financial markets and advocates the state as a necessary corrective. Furthermore, I expect the bailout programme in Germany to be accompanied by a coordinative discourse that advocates the state as a moral corrective that protects economic freedom from negative market excrescences. Finally, I expect the British bailout programme to be accompanied by a legitimising discourse that emphasises the freedom of markets and the significance of financial markets for the political economy.

Table 4: Financial system

France	Germany	United Kingdom
Hybrid (deregulated; concentrated; protectionist)	**Bank-based** (regulated; heterogeneous; 'patient')	**Market-based** (deregulated; globalised; "non-productive")

Hypothesis 4: I expect the French bailout programme to aim at protecting the structure and international position of the French financial sector. Furthermore, I expect the German bailout programme to aim at sustaining bank lending to the industry and to cut back the financial market activities of the LBs. Finally, I expect the British bailout programme to aim primarily at preserving the competitive status of London as a global financial centre.

6. Empirical cases

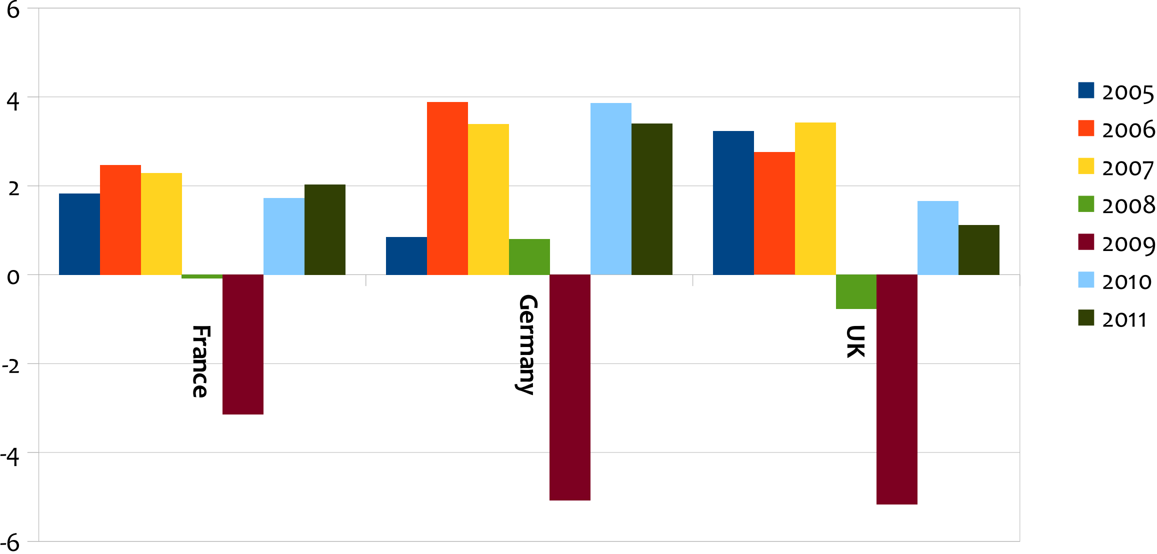
This chapter provides and analyses the empirical evidence regarding the bailout programme in each country. The first section quantitatively compares the impact of the financial crisis and government reactions to it. Sections two to four then qualitatively analyse the bailout policies by the French, German and British governments according to the hypotheses developed in the previous chapter. Section five concludes.

6.1 Overview

The financial crisis not only had an devastating impact on the financial and banking sector, but also on national economies in general and state's financial capacities. Figure 1 shows the changes in GPD in the run-up to and during the first years of the crisis[6]. Although Germany and the UK were affected most all three countries suffered significant recessions in 2009. Yet, Germany shows stronger recovery in the years following the financial crisis.

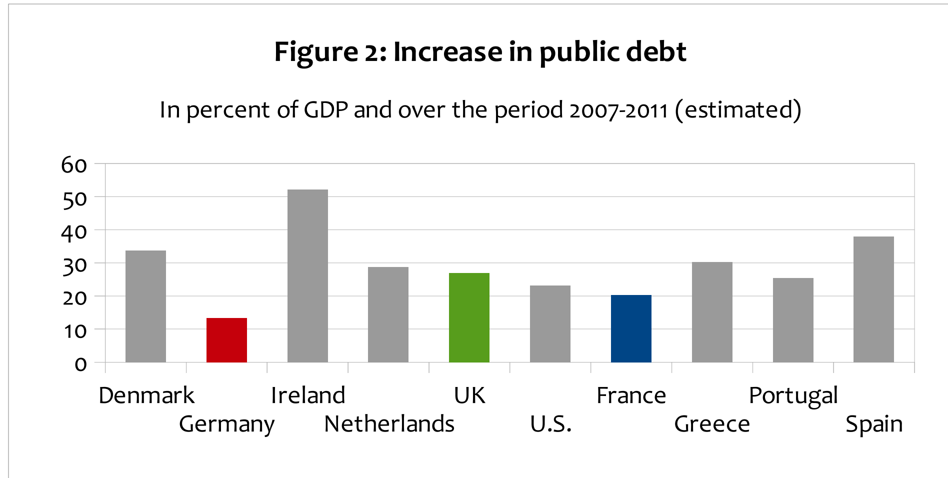
Figure 1: Gross domestic product

Percent change, constant prices

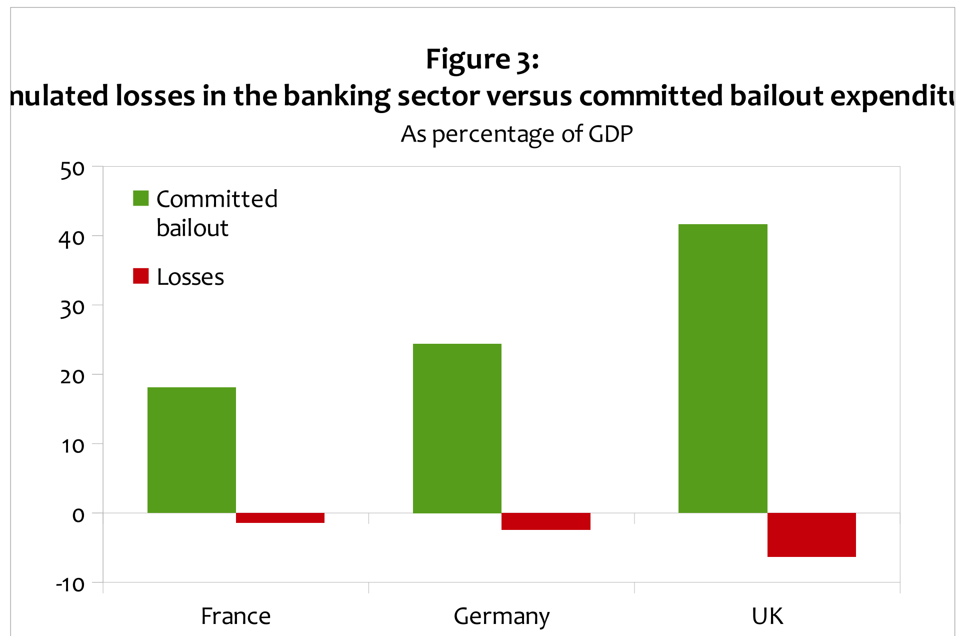


The increase in public debt may serve as a good indicator for the general impact the financial crisis had on national economies. On the one hand, bailing out banks affected by the crisis is expensive. On the other hand, there were also high expenditures due to economic stimulus packages. Both measures added to sovereign debt. Figure 2 shows the estimated increase in public debt for selected European countries that can, directly or indirectly, be traced back to the financial crisis[7]. It includes direct contributions to the financial sector as well as spending that aimed at offsetting decreased economic growth and other side-effects of the financial crisis.

6 Source: World Economic Outlook Database, October 2013.
7 Source: Laeven & Valencia 2010: 24; increase in public debt is increase in gross general government debt (central government debt if not available) over GDP, estimated over the 3 year period following the start of the crisis using WEO debt forecasts.



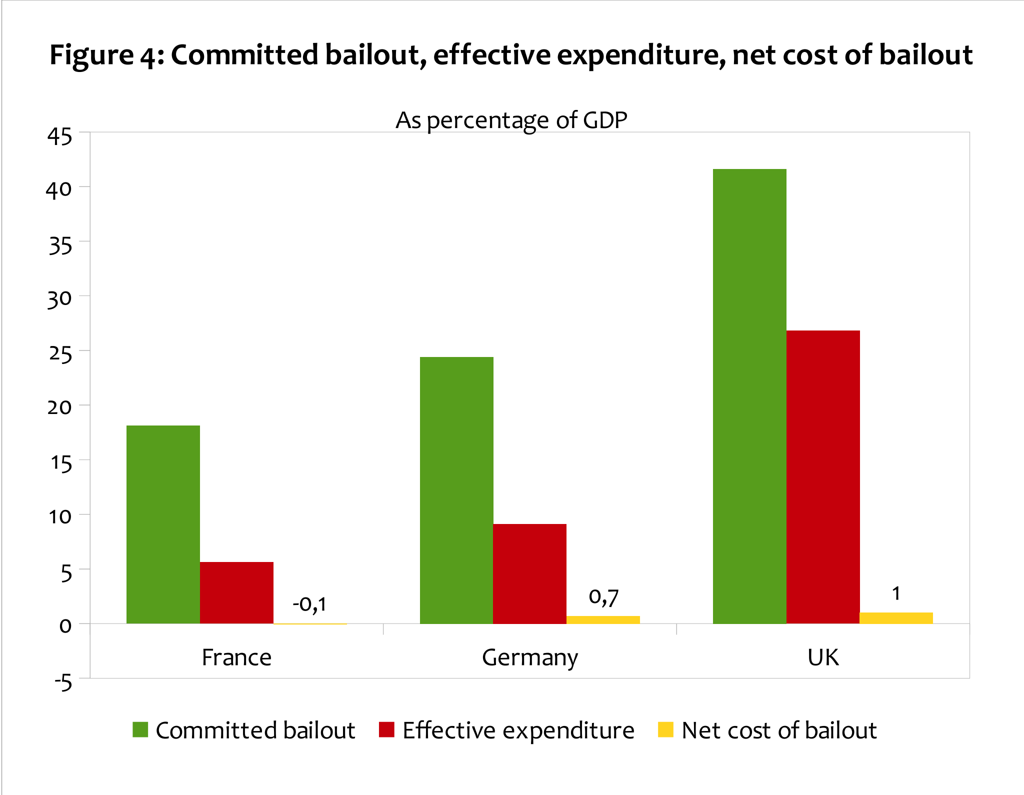
Although public debt rose significantly in all countries the impact the financial crisis had varies considerably from case to case. This holds true for the crisis' impact on the financial sector and government outlays for the banking sector shows as well. Therefore, figure 3 shows cumulated losses in the banking sector and bailout expenditures committed by governments for France, Germany and the UK[8]. Note that these are not the expenditures that governments actually paid. Yet, commitments in comparison to banking sector losses are a good indicator for the overall impact of the crisis on the financial sector. The banking sector in all three countries suffered losses although the UK has been affected most heavily. Furthermore, although committed expenditures correlate slightly with banking sector losses, figure 3 shows that the crisis and its effects have been assessed very differently from country to country.



Governments committed themselves to high amounts of bailout expenditures but not all of these have actually been used. Furthermore, not all of the money governments spend on bailouts is irretrievably lost. Public money that is provided to private banks may be paid for by an interest charge or a fee. If governments buy assets or shares from banks at one point in time they may be able to yield a return from these assets or shares later. Thus, as figure 4 shows for France, Germany and the UK, government bailouts not only differed in the amount of money committed to bailouts but also in actual expenditures as

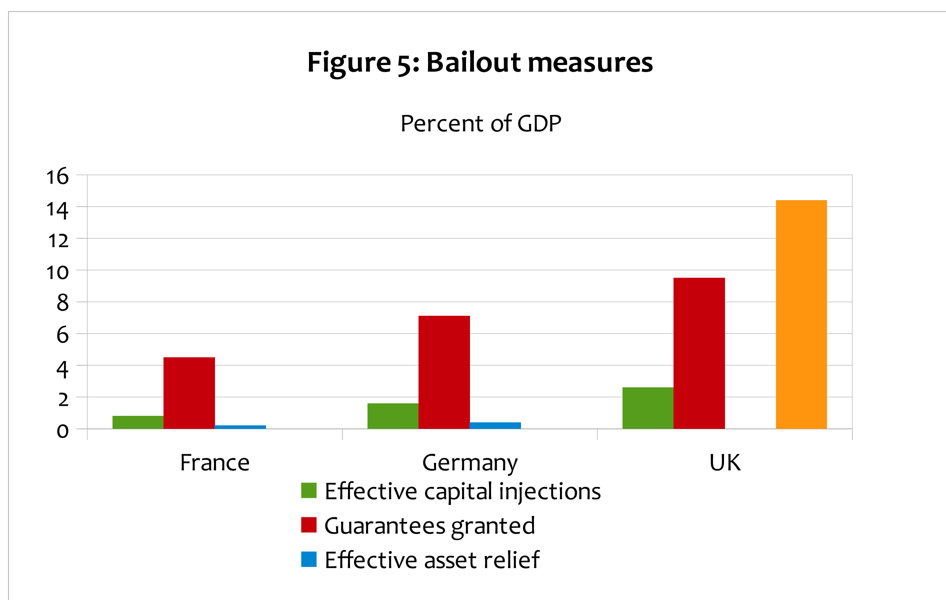
8 Source: Grossman & Woll 2014: 580; cumulated losses as a percentage of GDP from 08Q3 to 09Q1; committed expenditures as percentage of GDP up to July 2009.

well as net costs[9]. Whereas France was able to yield a small return, Germany and the UK lost up to one percent of GDP. In addition, the UK's effective expenditures amount to more than double the expenditures by the French and German government respectively.



Bailouts cannot only be distinguished by the amount spent, but can also be divided into several categories of measures. First, there are recapitalisations through capital injections and acquisitions of stakes. Second, there are guarantees on bank liabilities. Third, there are measures aiming at asset relief (e.g. so-called "bad banks"). Finally, there are further measures aiming at supporting bank liquidity (i.e. liquidity facilities at central banks). Figure 5 shows that the bailout programmes by France, Germany and the UK not only differed quantitatively but also qualitatively[10]. Whereas the UK bailout relied extensively on liquidity interventions, France and Germany did not undertake such measures at all. All bailout programmes used capital injections and granted large amounts of guarantees. Furthermore, the bailouts by France in Germany also used asset relief but only in small amounts.

9 Source: European Commission 2009b: Annex 2; Grossman & Woll 2014: 581; actual expenditures up to July 2009; net costs by the end of 2010.
10 Source: European Commission 2009b: Annex 2; actual expenditures up to July 2009.



To sum up, public debt increased in all three countries due to crisis effects. However losses in the banking sector and committed bailout expenditures differed significantly. The same holds true for effective expenditures and net costs. The UK has been affected most heavily in regard to banking sector losses as well as the costs of its bailout programme. France's banking sector suffered least and the French government was even able to yield a small return from its bailout programme. Germany stands somewhere in between the two countries with net costs almost as high as the UK's but lower expenditures. The measures undertaken by France and Germany resemble each other. The UK stands out because of its high amount of liquidity interventions.

6.2 The French Case

The financial crisis' impact on France's banking system has been significant yet "comparatively limited" (Howarth 2013a: 131; for a detailed account considering the early stages of the crisis see Xiao 2009). As figures 3 and 4 show, banking sector losses as well as effective bailout expenditures were comparatively lower than in Germany or the UK. In global comparison, the losses French banks had to suffer were lower than in most other countries. At the End of 2010 BNP Paribas, for example, the French bank that experienced the highest losses in France ranked only 16th globally as to total write-downs *(Reuters,* 24 February 2011). For 2008 and 2009, three of France's biggest banks, BNP-Paribas, Société Générale and Crédit Agricole, even reported profits (Howarth 2013a: 132).

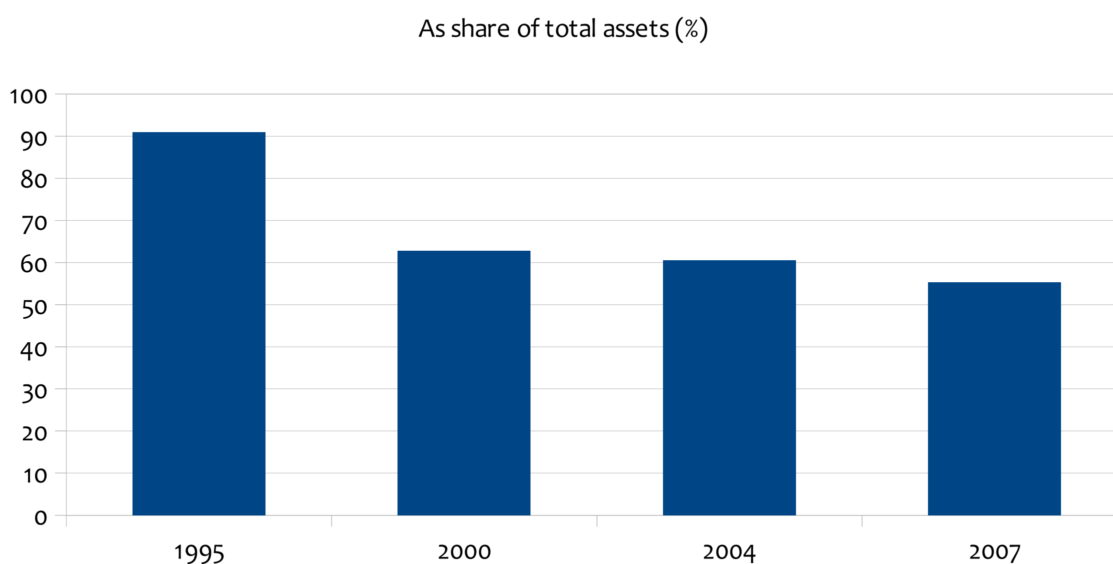
Yet, that is not to say that were not affected by the crisis at all. As table 5 shows, the largest French banks had to conduct significant write-downs[11]. As this table indicates private banks and the so-called "mutual banks" were hit alike. Mutual banks are "majority owned by their depositors and, at least in principle, operated for their benefit, rather than, as with the listed commercial banks, for the benefit of private shareholders" (Howarth 2013b: 374). Caisse d´Epargne and Banques Populaires are both mutual banks, Crédit Agricole is a part mutual bank. All three banks suffered losses through investment subsidiaries and were restructured in the course of the crisis (Howarth 2013a: 132).

11 Source: Howarth 2013b: 376; estimates based on write-downs and losses from sub-prime securities, mortgages, CDOs, derivatives and SIVs, and losses on bad loans, or non-performing loans.

Table 5: Write-downs by French banks

Bank	Total write-downs 2007–2010 ($ US)	Write-downs 2007–2010, percent of total assets (at End 2007)
BNP Paribas	28.3	1.67
Société Générale	18.6	1.74
Crédit Agricole	18.6	1.32
Crédit Mutuel	N/A	N/A
Caisse d´Epargne	Share of Natixis 6.9	N/A
Banques Populaires	Share of Natixis 6.9	N/A

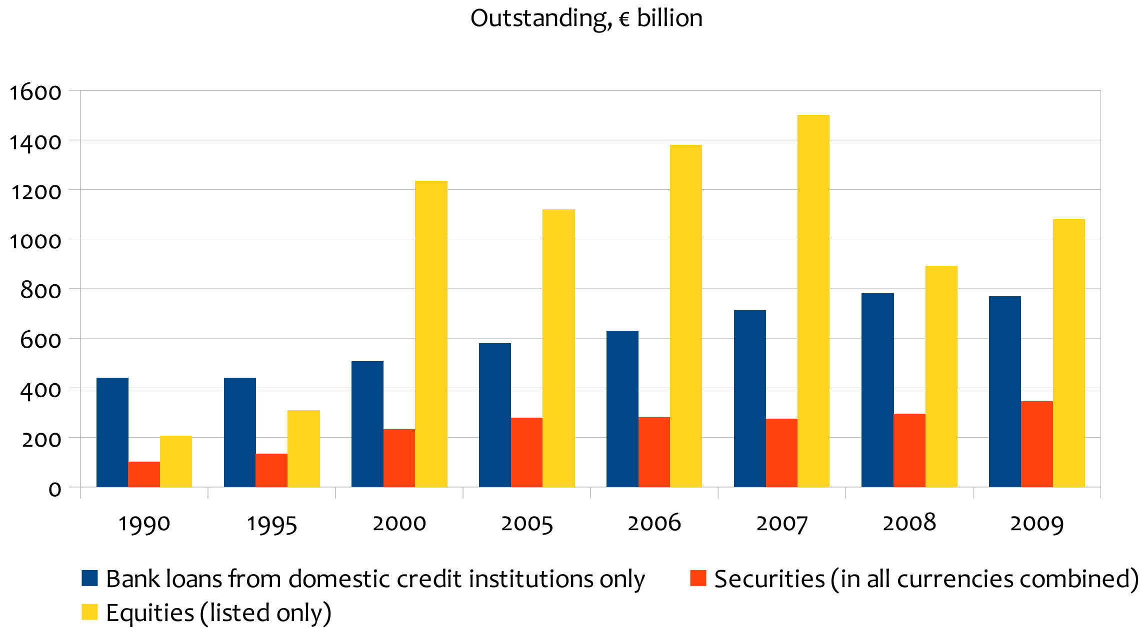
One explanation for the limited impact the financial crisis had on the French banking system is its diversification and its strong retail element (Hardie & Howarth 2009; IMF 2009). One the one hand, to a great extent France's financial system has been equity-dependent as represented by the limited share of lending in total bank assets shows (Figure 6)[12].



On the other hand, since 2000 the French financial system has become increasingly bank-based as non-financial companies more and more rely on bank loans as a source of financing in comparison to securities or equities (Figure 7)[13].

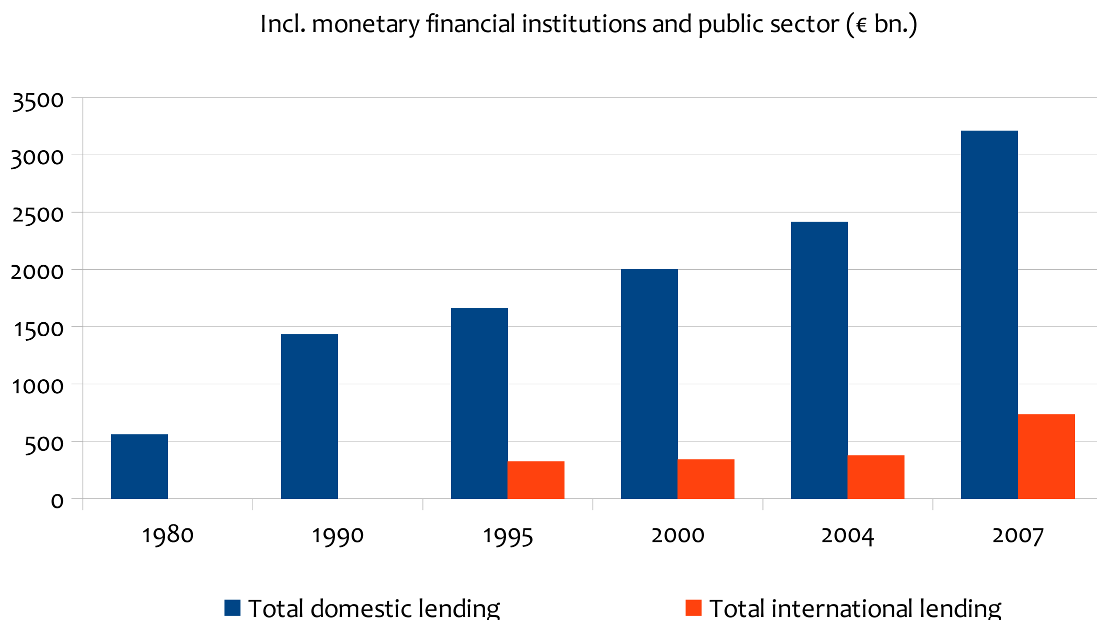
12 Source: Howarth 2013a: 134.
13 Source: Howarth 2013a: 131.

Figure 7: Finance raised by French non-financial companies since 1990



Furthermore, notwithstanding its relative decline as share of total assets, the total amount of retail bank lending increased significantly at the domestic as well as the international level (Figure 8)[14].

Figure 8: French financial institutions, total increase of retail bank lending



This development also reflects French bank's internationalisation strategy as Table 6[15] shows (see also Hardie & Howarth 2009: 1025–1028).

14 Source: Howarth 2013a: 134.

Table 6: French bank's internationalisation strategies

BNP-Paribas	Lending outside France rose from 61% in 2001 to 65% in 2007. Lending business to the rest of the European Economic Area rose from 18% of total in 2001 to 30% in 2007.
Société Générale	Lending outside France rose from 35% in 2003 to 50% in 2007. Exposure outside Europe rose from 10% in 2003 to 19% of total in 2007.
Crédit Agricole	Lending outside France rose from 18.4% 2001 to 56.3% in 2007. Lending business in the rest of the EU increased from 4.9% to 33.9%. Lending to the rest of the world increased from 14.5% in 2001 to 22.4%.

6.2.1 The French bailouts

French policies during the early stages of the crisis consisted of two key measures intervening in the banking sector. First, the *Société de Prise de Participation de l'Etat* (SPPE) was established, its main task being the provision of capital to banks in financial difficulties. Second, *Société de Financement de l'Economie Française* (SFEF) was founded, its main task being to sustain the creation of credit in the overall economy. The creation of these two new institutions paralleled another rescue package for the French car industry (Clift 2012a) and several other measures which aimed at promoting and fostering French industry (Levy 2013). Although initially there had been strong resistance by the European Commission to the French bailout programmes, it later dropped its initial demands and authorised the programme (*Financial Times,* 28 November 2008; Hardie & Howarth 2009: 1032).

6.2.2 SPPE & SFEF

France's bailout programme amounts to potential € 360 billion. € 40 billion of which can be used by publicly owned SPPE for recapitalisation of banks. To this day, there have been two tranches of € 10.5 billion each that have been disbursed to the six biggest French banks in exchange for so-called *titres super-subordonnès* without voting rights. These subordinated bonds are securities issued by the banks that have no limited term and may be redeemed any time at the issuer's will (Russo 2012, Fn. 11). However, the government earns an averaged interest of 8.2% on these instruments (OECD 2009: 22).

On the other hand, 66% of SFEF are owned by seven large French banks[16] and 34% by the French state (resulting in a blocking minority and a veto right). The SFEF issued and sold securities on the market that are guaranteed by the government[17]. Banks participating in SFEF had to sign a memorandum of understanding that imposed several conditions on them. These include increased lending activity to the industry as well as participation in the so-called "credit mediation" programme under the auspice of the French ministry of economics. This programme aims at moderating between creditors and enterprises that are denied a loan[18]. Furthermore, banks were urged to adopt a code of conduct on the compensation of executive directors (AFEP 2008; Russo 2012: 176). However, the fulfilment of these conditions was mainly voluntary (Jabko & Massoc 2012: 579). Until September 2009, SFEF had raised € 77 billion, and then ended its issuance activity (OECD 2011: 29).

6.2.3 BNP Paribas, Dexia and BPCE

Three banks stood out from the French bailout programme, namely BNP Paribas, Dexia and BPCE. BPCE is the result of a merger by Banques Populaires and Caisse d´Epargne. Banque Populaire (a mutual banking group) and Caisse d´Epargne (slightly resembling the German savings banks) merged in august

15 Source: Howarth 2013b: 379.

16 Namely Banque Populaire, BNP Paribas, Caisses d'Epargne, Crédit Agricole, Crédit Mutuel, HSBC France and Société Générale.

17 Parallel to France's general downgrading by rating agency Moody's, SFEF's rating has been downgraded from AAA to Aa1, too (*The Telegraph*, 19 November 2012).

18 See http://www.economie.gouv.fr/mediateurducredit/accueil for further information.

2009 to form BPCE, France's second largest banking group *(BPCE,* 24 June 2009). This merger had become necessary after Natixis, the common investment subsidiary of Banques Populaires and Caisse d´Epargne suffered losses amounting to € 2.8 bn in 2008 and another € 1.8 bn in the first quarter of 2009 (*Handelsblatt,* 26 August 2009).

However, this merger was not only the result of the two banks giving in to market pressure, the state also took a leading role during the process. First of all, BPCE received a total of € 7.05 billion from the SPPE[19]. Secondly, François Pérol was appointed chairman as well as chief executive of the new company in August 2009 (*The New York Times,* 27 August 2009). This measure was highly controversial since, before his appointment, Pérol was president Sarkozy's chief economic advisor (*FAZ,* 24 February 2009). Furthermore, Pérol was accompanied by two confidants that joined him on the board. François Riahi had worked as an auditor at the French Treasury between 2001 and 2005, then became Head of the Budget Policy Office and since 2007 served as an advisor to President Sarkozy (Bloomberg Businessweek n.d.). Didier Banquy had worked before as a deputy director of President Sarkozy's past ministerial staffs (Jabko & Massoc 2012: 578). Although, formally, they were not government representatives there remained a strong informal relationship and influence. This was later implicitly acknowledged by Pérol when he stated at a parliamentary hearing that "it was necessary in this business to have a neutral person, who also in some way embodied the state" (ibid.: 579).

An example for the promotion of a "national champion" is the take-over of Belgian-Dutch bank Fortis by BNP Paribas that was completed in May 2009 to form the biggest bank in the Eurozone in terms of deposits and Europe's third-largest in terms of market value (*BNP Paribas,* 12 May 2009; *The Economist,* 21 October 2010). In April 2009, the French state became BNP Paribas' largest stakeholder, now owning 17% of the company's shares. Yet, via the SPPE the French state has subscribed only to non-voting shares that do not carry seats on the board and cannot be converted into regular shares (*Financial Times,* 07 April 2009). BNP Paribas' then chairman, Michel Pébereau, a close ally of President Sarkozy, extensively participated in drafting the French rescue plan (Jabko & Massoc 2012: 577). The second tranche of the SPPE was disbursed earlier than planned due to the appeal by Pébereau. One day after this injection of capital, BNP Paribas announced that it would take-over Fortis (ibid.; Clift 2012a: 217, 2012b: 584). Even before these two measures, the European Commission had criticised the French bailout scheme for representing an "appreciable financial advantage for the beneficiary banks, which would be difficult for them to obtain from private investors under current conditions" (European Commission 2008).

Finally, in September 2008 Dexia, a Franco-Belgian municipal lender, notified the public about financial problems due to its exposure to American asset backed securities. Early in October 2008 the French government alongside its Belgian and Luxembourgian counterparts announced a bailout package amounting to € 7 billion[20]. In contrast to its Belgian counterpart, the French government only obtained non-voting shares through this capital injection (Clift 2012b: 584). At the same time Dexia's chairman Axel Miller resigned (*FAZ,* 01 October 2008). Miller was soon to be replaced by Pierre Marinai, Sarkozy's former office manager and another close ally to the President (*FAZ,* 08 October 2008; *Süddeutsche Zeitung,* 13 October 2011). A few days later, the three governments declared that they would guarantee all of Dexia's borrowing for one year. This period was later extended (*FAZ,* 09 October 2008).

In June 2010 Dexia announced that it would exit all state guarantees early (*Dexia,* 30 June 2010). However, financial problems came back with a vengeance in 2011. In November the bank received an injection of capital amounting to € 5.5 billion[21] as well as state guarantees by the three governments of up to € 90 billion. It is now planned to break up Dexia and sell the parts (IMF 2012: 36; *Süddeutsche Zeitung,* 10 October 2011).

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19 From a first tranche *Banques Populaires* received € 950 billion and *Caisse d´Epargne* received € 1.1 billion by the end of 2008. Two further disbursements were made at the end of the second quarter 2009 (€ 2 billion) as well as on 31 July 2009 (€ 3 billion). State aid was fully repaid by BPCE during the first quarter 2011 (*Moody's,* 18 April 2011).
20 € 3 billion each by the French as well as the Belgian government and € 376 million by the government of Luxembourg (*FAZ,* 01 October 2008).
21 € 2.9 billion each by the Belgian government as well as € 2.6 billion by the French government (IMF 2012).

6.2.4 Economic discourse

Although the president generally is the main political actor in France, Sarkozy's has been exceedingly present in political discourse as well as decision-making. His governing style has been described as "'hyper presidentialism" (Perrineau 2013: 182) and he was given nicknames such as "omnipresident" (Levy 2011: 15). He has been permanently at the centre of attention, "making all decisions big and small, and launching new initiatives on an almost daily basis" (ibid.). With regard to the bailout programme Jabko and Massok quote two members of parliament recalling a "'monarchical' process in which Presidential advisor 'super-Pérol' was entirely in charge, with Finance Mininster Christine Lagarde relegated to a secondary role and Parliament reduced to a 'recording chamber'" (2012: 573).

However, his actual policies fell short of his active rhetoric and public presence. First of all, Sarkozy was elected president in 2007 on a very liberal, almost 'Anglo-Saxon' platform. He promised to break with France's dirigiste past and to "pull France into the twenty-first century" (Gaffney 2012: 350; Gualmini & Schmidt 2013: 367). However, he soon turned away from this liberal stance and towards what has been described as "post-*dirigisme"* (Clift 2012a, 2012b).

The bailout programme and associated policies during the crisis were accompanied by a discourse, which can be characterised as twofold. On the one hand, Sarkozy resorted to the rhetoric of "managed" globalisation trying to establish a *dirigiste* agenda against unfettered financial markets on the international level (Abelal & Meunier 2010: 364). Whereas the governor of the Bank of France stressed the necessity of national solutions to the financial crisis notwithstanding efforts to globally regulate financial markets (Noyer 2010: 1). This rhetoric went along with a rather nationalist discourse promising to "protect the French people *in* globalization" and against the "'*delocalization,'* or offshoring, of jobs" (Schmidt 2012: 176), despite the fact that this kind of "economic patriotism" has not always proved to successfully mobilize political backing in the past (Callaghan & Lagneau-Ymonet 2012).

On the other hand, on the national level, critique centred on the "excessive" behaviour by bankers and other actors on financial markets. Yet, here the gap between political rhetoric and action was especially wide. As aforementioned, the state, when bailing out several banks, only subscribed to non-voting shares. Thus, it missed an opportunity to actively intervene in bank's business activities (Jabko & Massoc 2012). Furthermore, although Sarkozy had a very harsh stance on bankers salaries and bonuses, there only were "soft" rules and "no sanctions and few conditions were imposed on French banks in the context of the bank bailout" (Clift 2012a: 218). Regulatory reforms on the domestic level fell short of Sarkozy's "anti-liberal" discourse, too (Jabko 2012).

6.2.5 Short summary

To sum up, France's bailout policies were dominated by president Sarkozy and extensively influenced by his personal and informal network. Despite his *dirigiste* and anti-liberal rhetoric, there were no far-reaching interventions in the market or banks business activities. Rather, bailout policies were used to further consolidate the French banking market and for the creation of national and European „champions".

6.3 The German case

Germany's banking and financial system was one of the hardest hit in Europe. Yet, "German bank lending was only marginally affected by crisis and the core element of the German […] CME—patient capital—barely undermined" (Hardie & Howarth 2013: 103b). One explanation for this is that the small savings and cooperative banks with their regionally focused business activity have not been notably engaged in the kind of investments that were affected by the financial crisis. These small banks continued to provide capital to the SBE "backbone" of the German economy.

Big commercial banks, by contrast, were deeply involved in such investment activities. However, they were not the only ones. Another group of banks massively exposed to the financial turmoil were the LBs.

These banks, besides serving the public interest, have since 2000 increasingly invested in investments that were affected most by the financial crisis as table 7 shows[22].

Table 7: Exposure of selected banks to conduits and special investment vehicles (2007)

Bank	**Ownership**	**In % of capital**	**In % of assets**
Sachsen LB	Public (Landesbank)	1,126	30.3
West LB	Public (Landesbank)	542	12.7
IKB	Private	494	20.5
Dresdner Bank	Private	364	9.9
Landesbank Berlin	Public (Landesbank)	179	2.2
Bayern LB	Public (Landesbank)	170	5.1
HSH Nordbank	Public (Landesbank)	126	4
Deutsche Bank	Private	114	3.3
Nord LB	Public (Landesbank)	89	2.9
Commerzbank	Private	85	2.2

Table 8 therefore shows the losses by these banks between 2007 and 2009[23]. Although IKB Deutsche Industriebank AG (IKB) stands out, there were significant write-downs in several other banks, too. As will be shown below, most of these banks had to be bailed out and some of them (Sachsen LB, WestLB and IKB) collapsed completely.

Table 8: Selected German bank write-downs on toxic assets and bad loans (2007–9)

Bank	**Total write-downs at end of 2009 ($ bn)**	**Write-downs/total assets (end 2007) (%)**
IKB	14.4	22.68
Sachsen LB	2.5	3.69
Bayerische LB	18.8	4.52
Commerzbank	22.3 (including Dresdner Bank)	0.36 (2008); 2.01 (2009) including Dresdner Bank assets
HSH Nordbank	4.1	2
Deutsche Bank	21.4	1.89
HRE	7	1.74
WestLB	3.9	1.36
LBBW	7.8	1.75

6.3.1 IKB

One of the first banks that has fallen victim to the financial crisis, was IKB. On Monday, 30 July 2007, the Bank published an ad hoc disclosure that it would rely on refinancing due to significant losses from its engagement in the US subprime investments (IKB 2007). A few days later, banking associations and the public bank Kreditanstalt für Wiederaufbau (KfW) announced a bailout package for IKB in the amount of

22 Source: Hüfner 2010: 5.
23 Source: Hardie & Howarth 2013b: 106; as of 31 December 2009.

€ 3.5 billion. Private banks, savings banks and cooperative banks together contributed € 1 billion to the bailout package[24] (*Die WELT*, 02 August 2007).

In November 2007, it became clear that another bailout package would become necessary. KfW provided another € 350 million (KfW, 29 November 2007). Two months later, KfW again stood in and bought a convertible debenture amounting to € 54 million that was soon converted into regular shares (*DPAG,* 07 January 2008). A few weeks after that, KfW announced that it intends to sell its IKB shares, though this attempt was stopped again two months later (*KfW,* 18 January 2008; *DGAP,* 20 March 2008).

In February 2008, a third bailout package up to € 1.5 billion in connection with a capital increase by IKB amounting to another € 1.5 billion followed. Regarding the bailout package the private banks associations' president Klaus-Peter Müller highlighted: "I think that the private banks will accept their obligation" (*Reuters,* 14 February 2008). On 15 February then minister of finance Peer Steinbrück announced before parliament the details of the package. € 1 billion were to come from the federal government and another € 300 million were supposed to be a final contribution by the private banks (*Bundesregierung,* 15 February 2008). Effectively, the final package was limited to € 1.05 billion that came entirely from the federal state (*Frankfurter Rundschau,* 21 August 2008).

The IKB's capital increase was almost unanimously approved by the stockholder's meeting on 27 March 2008 (*Handelsblatt,* 28 March 2008). Although the plan to increase IKB's capital in the beginning envisaged KfW to contribute 1.25 of the € 1.5 billion, in the end KfW had to contribute more than 99% and raised its share in IKB to 90.8% (*DGAP,* 16 February 2008; *Frankfurter Rundschau,* 21 August 2008).

The final and most surprising episode of IKB's bailout happened in August 2008 when it was announced that KfW's share of 90.8% was to be sold to US-investor *Lone Star*. The price finally realised was speculated to be well below expectations (*Spiegel-Online*, 21 August 2008). The deal was finalised on 29 October 2008 (*DGAP,* 29 October 2008). Two years later, European managing director Bruno Scherrer said in an interview that *Lone Star* would put IKB up for sale and said: "Our work is done" (*Handelsblatt,* 13 October 2010). Finally, in 2012 IKB paid off the last of its government guarantees (*DGAP,* 14 December 2012).

6.3.2 FSG, FMSA and SoFFin

After the collapse of *Lehman Brothers,* it soon became obvious that German banks would need further financial help. On 17 October 2008 the German parliament passed the so-called Finanzmarktstabilisierungsgesetz. It institutionalised bank bailouts by setting up a fund that would provide recapitalisation and guarantees to banks (Finanzmarktstabilisierungsfonds [SoFFin]). A federal agency (Bundesanstalt für Finanzmarktstabilisierung [FMSA]) serves as a supervisory body to the fund. To receive a loan from SoFFin, banks have to fulfil certain conditions. These are, amongst others, "a sustainable business policy", to serve the industry and especially SMB's need for loans as well as appropriate compensation schemes (FMStFV 2008). Initially, the fund was supposed to be active only until 31 December 2009 but it has been extended two times and is now available to banks until 31 December 2014 (Tagesschau, 26 January 2012; *Die WELT,* 17 October 2012). Three committees manage and supervise the fund respectively. At present the FMSA and, thus, the SoFFin is managed by three board members: Christopher Pleister is the former president of the cooperative banks association, Günter Borgel has been a consultant before, and Karlheinz Weimar is the former minister of finance of the state of Hesse[25]. The main decision-making committee is the so-called *Lenkungssauschuss,* consisting of five members: a representative of the ministry of finance, the Federal Chancellery, the ministry of justice, the ministry of economics and the German states respectively. A parliamentary supervisory board is the third committee that controls the FMSA.

24 The private banks contributed € 500 million, the savings banks € 333 million and the coopartive banks € 167 million (*Handelsblatt,* 26 February 2008).
25 http://www.fmsa.de/de/fmsa/FMSA/B_Organisation/leitungsausschuss/.

6.3.3 SoFFin

The SoFFin is able to provide the German banks with recapitalisation amounting up to 80 billion € and guarantees amounting up to € 400 billion. Table 9 shows how much recapitalisation and guarantees it has provided to banks since its establishment[26].

Table 9: SoFFin measures 2008–2013 (€ billion)

Bank	Recapitalisations	Guarantees	Total
Aareal	0.5	4.0	4.5
Commerzbank	18.2	5.2	23.4
HRE	9.8	124.0	133.8
Portigon (former West LB)	3.0		3.0
HSH Nordbank		24.0	24.0
IKB		10.0	10.0
SdB		6.7	6.7
BayernLB		5.0	5.0
DüsselHyp		2.5	2.5
CorealCredit		0.5	0.5
Total	**31.5**	**181.9**	**213.4**

Hypo Real Estate (HRE) stands out totalling € 133.4 billion of recapitalisation and guarantees. HRE's main business activity is mortgaging for commercial customers. The bank practically collapsed in 2008 and has been completely nationalised in 2009.

After it became clear that HRE was in dire need of financial relief a first crisis meeting took place between federal government, the German central bank, the German financial regulatory authority and representatives from the financial industry and business associations between 25 and 29 September 2008. They agreed to provide HRE with a recapitalisation amounting to € 35 billion. The state guaranteed for € 20 billion, the private financial institutions guaranteed for another € 20 billion. Furthermore, it has been agreed that the banks bear 60% of potential losses although the total amount is limited to € 8.5 billion (*Der SPIEGEL*, 17 August 2009). When it became obvious that HRE will need more than the € 35 billion the banks initially withdrew from the agreement (*FOCUS,* 04 October 2008). At a second crisis meeting on 6 October 2008 the private banks agreed to provide another € 15 billion to HRE, bearing 60% of the losses up to an amount of € 14 billion (*FAZ,* 06 October 2008). A few days later, HRE was the first bank that applied for a guarantee by SoFFin in the amount of € 15 billion (*Spiegel-Online,* 29 October 2008). In November 2008, the members of the supervisory board were almost completely replaced. The new members were mostly former bankers plus one former state secretary and one former central banker (*Handelsblatt,* 17 November 2008).

In January 2009, there was first evidence of an upcoming nationalisation of HRE when SoFFin signalled that it was willing to take over more than 50% of HRE's shares (*Handesblatt,* 26 January 2009). Meanwhile, SoFFin guarantees provided to HRE amounted to € 52 billion (*FAZ,* 11 February 2009). At the end of March HRE's core capital quota fell below the regulatory threshold of 4%. Strictly speaking this would result in the close-down of HRE (*Die ZEIT,* 29 March 2009). As an immediate reaction, SoFFin bought 20 million shares on the stock market now owning 8.7% of HRE's shares (*Die WELT,* 29 March 2009). In April parliament passed a law that allows federal government to take over private banks and potentially "squeeze out" other shareholders. It is the first law in the history of post-war Germany that allows for compulsory acquisition and has been met with widespread critique from business associations and other interest groups (*Handelsblatt,* 18 February 2009; *Spiegel-Online,* 18 February 2009).

26 Source: FMSA 2013; maximum amount used.

A few days later, the federal government announced a take-over bid for HRE. However, not least due the resistance by major shareholder J.C. Flowers, the take-over bid was not successful and SoFFin was able to buy only 47.3% of HRE's shares (*Handelsblatt,* 24 April 2009; *Spiegel-Online,* 07 May 2009). Therefore, SoFFin planned to take over HRE completely via an increase of capital stock. This was made possible by the shareholder meeting on 2 June and the so-called "squeeze-out" of remaining shareholders and, thus, HRE's nationalisation was finalised in October (*NZZ,* 02 June 2009; *Tagesschau,* 05 October 2009). Yet, HRE was still in need of capital and received another recapitalisation amounting to € 3 billion in November 2009 and further guarantees amounting to € 40 billion in September 2010 *(DPAG, 0*4 November 2009; *FAZ,* 11 September 2010). Finally, the FSMA established *FMS Wertmanagement* to serve as a "bad bank" for HRE (*FAZ,* 01 October 2010).

6.3.4 Commerzbank

Another bank that needed recapitalisation and guarantees by the state was Commerzbank. It is one of Germany's biggest private banks and has been, together with Deutsche Bank*,* one of two banks that the Financial Stability Board considered "systematically important" in 2011 (FSB 2011). Yet, Commerzbank lost this status in 2012 in the course of its financial problems *(FAZ,* 01 November 2012).

In August 2008, it was decided that Commerzbank would take over its concurrent Dresdner Bank from insurance group Allianz AG. Because Dresdner Bank had suffered heavy losses during the first months of the financial crisis its purchase price was relatively low (*Spiegel Online,* 31 August 2008). The restructuring of the two banks was finalised in April 2011 *(FAZ,* 26 April 2011). The deal was politically controversial since there was a higher take-over bid by China Development Bank. Labour representatives favoured the Chinese solution since they assumed that there would be no lay-offs in contrast to Commerzbank's plans to lay off around 10,000 employees (*Spiegel-Online,* 27 August 2008). However, there is evidence that there was also political pressure that favoured the take-over by Commerzbank to form a second German bank of international importance (*Süddeutsche Zeitung,* 30 August 2008). Furthermore, it was assumed that the new bank would serve as a new big bank for the financing of German SBEs (*Spiegel-Online,* 01 September 2008).

In December 2008, Commerzbank applied for financial relief from SoFFin. It was granted a recapitalisation amounting to € 8.2 billion as well as guarantees amounting to 15 billion €. However, this came with several strings attached. Commerzbank committed to paying no accrued dividend in 2008 and 2009, providing extra loans at the usual market price to SBEs to the amount of € 2.5 billion as well as a limitation of its management's salary (*Spiegel-Online,* 19 December 2008). Furthermore, in January 2009 Commerzbank was the first German bank to issue bonds backed by the state (*Handelsblatt,* 08 January 2009). As a result, it was able to raise capital in the amount of € 5 billion (*FAZ,* 08 January 2009).

Parallel to that process there was yet another bailout by the German state. SoFFin provided a further recapitalisation amounting to € 10 billion now owning 25% plus one share of Commerzbank partly in the form of a silent partnership (*Commerzbank,* 08 January 2009). Commerzbank's spokesperson of the board, Martin Blessing stated that this recapitalisation had become necessary "because of Dresdner Bank, but not only because of Dresdner Bank" (*FAZ,* 09 January 2009, translation by author). Moreover, further negotiations and financial support by Allianz AG were also necessary to avoid endangering the take-over (*Spiegel-Online,* 08 January 2009).

In the context of its increased shareholding the state now has the opportunity to send two secretaries of state to the bank's supervisory board. Albeit the minister for economic affairs stated that he expects Commerzbank to provide more loans to the real economy, it was announced that the government did not want to exert any influence on the Bank's business activities (*Spiegel-Online,* 09 January 2009).

To get rid of its toxic assets, Commerzbank established an internal "bad bank" in March 2009 (*Handelsblatt*, 27 March 2009). Furthermore, at a press conference in May 2009, the bank published a "Roadmap 2012" wherein it announced that it wanted to downsize its investment banking and intended to become a *"Hausbank"* for private and corporate customers (Commerzbank 2009). In 2011, the Bank started to pay pack SoFFin's capital contributions. For this purpose, it carried out an increase of capital

stock. SoFFin converted parts of its silent partnership but kept its share of 25% plus one *(Tagesschau,* 06 April 2011). May 2013 Commerzbank paid back the reminder of SoFFin's capital contributions. It carried out another increase of capital stock. SoFFin's share thereby decreased to 17% (*FAZ,* 15 May 2013).

6.3.5 The *Landesbanks*

As aforementioned, the LBs were among the hardest hit financial institutions in Germany. Although they serve a public interest their business activity exposed them extensively to toxic assets and bad loans. These business activities and the subsequent bailouts resulted in a substantial consolidation. WestLB, LB of Germany's biggest state, North Rhine-Whestphalia, has been broken down and Sachsen LB has been taken over by another LB. Finally, HSH Nordbank triggered a rather emotional debate about management salaries in public banks.

6.3.5.1 Sachsen LB

Sachsen LB extensively traded securitised assets via an Irish subsidiary. These were the main reason for its financial turmoil during the early months of the financial crisis (*FAZ,* 21 August 2007). Eventually, in August 2007 Sachsen LB received a loan amounting to € 17.3 billion that was provided by a group of savings banks, primarily other LBs (*FAZ,* 18 August 2007). One condition for the loan was that the state of Saxony would search for an investor that would be willing to take over Sachsen LB. The bank had been in a weak market position for some time already (*Spiegel-Online,* 20 August 2007). For this purpose, Sachsen LB, which had been a public institution before, was then transformed into a regular stock company to facilitate a potential take-over (*FAZ,* 21 August 2007).

A few days later LBBW (Baden-Württemberg's LB) took over Sachsen LB. LBBW provided Sachsen LB with financial aid in the amount of € 250 million and administered Sachsen LB on a trust basis. It was agreed that LBBW buys Sachsen LB within a year at a purchase price between € 300 and 800 million. In return the state of Saxony and the Saxon savings banks had to obtain shares in LBBW. The agreement was made by the prime ministers and other ministers of Baden-Württemberg and Saxony. Representatives by the main political parties in Saxony were informed and involved in the decision-making process as well (*FAZ,* 27 August 2007). Yet, six days later Saxon's minister of finance resigned due to the decision-making process not involving the state's parliament. Parliament was only informed afterwards (*Die ZEIT,* 31 August 2007).

The final bailout plan was decided in December 2007. LBBW bought Sachsen LB for € 328 million. In return, the state of Saxony agreed to provide guarantees for potential loss risks amounting to € 2.75 billion. Several partners were involved in the bailout, for example the German Savings Banks Association. The German financial regulatory authority and the central bank were part of the negotiations as well (*Spiegel-Online,* 13 December 2007).

6.3.5.2 WestLB

In April 2007 WestLB informed the public about high losses in proprietary trading it suffered due to manipulated stock prices (*Spiegel-Online,* 11 April 2007). Later, in January 2008, WestLB received an injection of capital from its owners amounting to € 2 billion (the state of North Rhine-Westphalia and the savings banks) to compensate its loss (*FAZ,* 21 January 2008). In February 2008 a crisis meeting took place between WestLB's owners, the central bank and Germany's financial regulatory authority. A second bailout package was resolved upon. WestLB received a second recapitalisation in the amount of € 5 billion. Furthermore, it was planned that the bank should lay off 1,500 employees until 2010, downsize its investment business and focus on its business with SBEs. WestLB's Chief Executive Officer (CEO) stated that the job cuts were supposed to be "as socially acceptable and cooperative as possible" (*Handelsblatt,* 08 February 2008, translation by author). A merger with Helaba (another LB) was considered further. To this end, WestLB transferred assets amounting to € 23 billion to a newly established special purpose vehicle (*Spiegel-Online,* 08 February 2008). Yet, at the end of February negotiations with Helaba were cancelled (*Süddeutsche Zeitung,* 28 February 2008).

In November 2008 the savings banks developed the so-called "Masterplan" to consolidate the German LBs, though that plan did not have considerable consequences (*Spiegel-Online,* 14 November 2008). WestLB continued to transfer toxic assets to its bad bank, by April 2009 they amounted to € 77 billion (*FAZ,* 26 April 2010).

It took until March 2012 before a final decision was made on WestLB's future. In the end, the bank was going to be split up. Its business with savings banks, corporate customers and communes was going to be continued by Helaba (*FAZ,* 20 March 2012). Portigon AG, a new foundation, would carry out financial services primarily to Helaba and WestLB's bad bank (*Spiegel-Online,* 21 March 2012). The bad bank received retroactively a total of € 100 billion in assets that are to be handled until 2028 (*FMSA,* 30 June 2012).

6.3.5.3 HSH Nordbank

Until September 2009 several write-downs resulted in losses amounting to € 2.3 billion (*Spiegel-Online,* 23 September 2008). Consequently, in November 2009 HSH Nordbank received € 30 billion in guarantees from SoFFin (*FAZ,* 04 November 2008). Three months later HSH Nordbank received another bailout package directly from its two owner states Hamburg and Schleswig-Holstein. The package consisted of a recapitalisation amounting to € 3 billion and guarantees amounting to € 10 billion. Notwithstanding the crisis, July 2009 chairman Dirk Nonnenmacher received a bonus in the amount of € 2.9 million. He was severely criticised on ground of this "question of decency" (*FAZ,* 17 July 2009, translation by author). Schleswig-Holstein's prime minister stated that although Nonnenmacher may have a contractual right to his bonus, "there is no moral justification for this payment" (*Die ZEIT,* 26 July 2009, translation by author).

6.3.6 Economic discourse

The bailout policies by the German government have been embedded in an economic discourse that focused on three aspects. First, a moral and ethical debate about the responsibility as well as the compensation of bankers. Second, the role of banks in a social market economy. Third, the role of the state in a free economic order.

Bankers have been severely criticised for their actions as well as for their "exaggerated" salaries. Peter Struck, of the then governing social democrats, stated before parliament that no policy or regulation would be able to replace the necessary "moral instauration" among bankers (Deutscher Bundestag 2008a: 19658, translation by author). In the early stages of the financial crisis Josef Ackermann, then CEO of Germany's biggest bank Deutsche Bank, admitted that mistakes were made and announced that Deutsche Bank's management would voluntarily abstain from their yearly bonuses in 2008. Politicians objected that there would not have been a moral justification for theses bonuses anyway (*Spiegel-Online,* 30 December 2008). Bankers receiving bonuses in such times "discredit the market economy" (*Süddeutsche Zeitung,* 16 February 2009, translation by author). Finally, in June 2009, the German parliament passed a law on the "adequacy of management salaries". One justification for this law has been that "for the social acceptance of our economic order, it is necessary that salaries for all people are not out of all proportion to what they contribute to society" (Deutscher Bundestag 2009a: 25128, translation by author). This debate has continued for many years (*Die WELT,* 17 March 2012).

The desirable role that banks ought to play in a social market economy may best be summed up by the phrase "servant of the real economy". This demand came from politicians as well as bankers (*Der SPIEGEL,* 17 October 2011; *Süddeutsche Zeitung,* 10 September 2011). A parliamentary commission of enquiry concluded that "self-regulation by markets is not enough to guarantee a smooth functioning of financial markets that serves the public interest" (Deutscher Bundestag 2009b: 184, translation by author). Furthermore, before parliament the importance of the preservation of Germany's three-pillar banking system as a political priority was repeatedly emphasised (for example: Deutscher Bundestag 2012a: 18232). This deemed state intervention necessary. Angela Merkel, Germany's head of government, stated before parliament that "the state has been and still is the only instance that is able to restore trust between the banks, which is necessary for the protection of the public and for the protection of bank's interests"

(Deutscher Bundestag 2008b: 19349, translation by author). By the same token, SoFFin's then chief supervisor, Albert Rupprecht, declared in 2010 that the fund's main task are to protect employees, pensioners, savers and enterprises from damage (*Süddeutsche Zeitung,* 17 May 2010). Yet, it has also been cautioned against too far-reaching market intervention (Deutscher Bundestag 2012a: 18226). One member of parliament even quoted Ludwig Erhard, the "spiritus rector" of Germany's social market economy: "The deep sense of social market economy is to unite the principle of freedom on the market with the principle of social balancing and moral responsibility of every one of us" (Deutscher Bundestag 2012b: 25551, translation by author).

6.3.7 Short summary

To sum up, the bailout policies by the German government involved a broad coalition of political and market actors. The German states were necessarily involved in the bailouts of the LBs but were also part of the general decision-making process (see, for example, Deutscher Bundestag 2008a, 2008b). Private and financial markets actors were part of the decision making process as well. Furthermore, they were held accountable financially as well as politically by an ordo-liberal public and political debate. A partial return by banks on their traditional business model helped to sustain lending to Germany's "economic backbone".

6.4 The British case

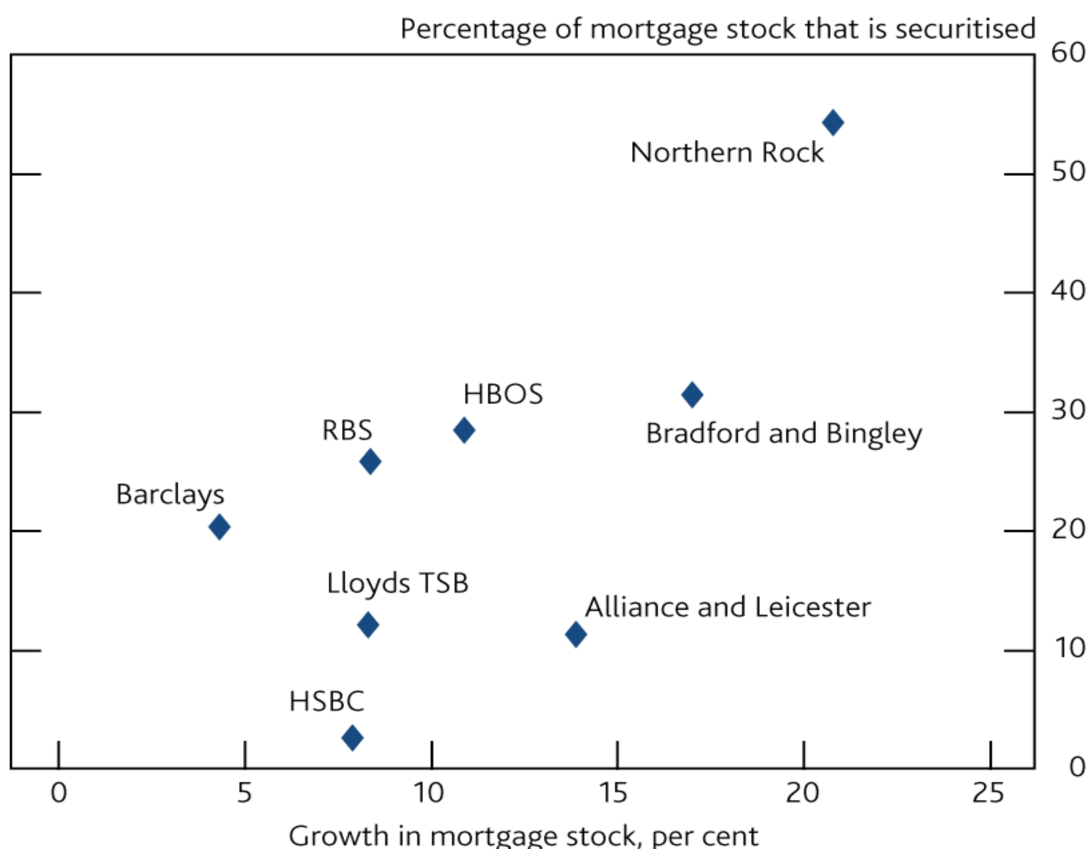
As aforementioned, the UK's financial and banking system was one of the hardest hit by the financial crisis. The British bailout programme amounted to more than 25% of the UK's GDP and consisted to a large amount of capital injections. British banking behaviour, paralleling banking behaviour in the U.S., in the run-up to the crisis featured three vulnerabilities (Hardie & Maxfield 2013: 65-75). First, the "originate-to-distribute" model or the "making of loans with the intension [sic] of selling them" (ibid.: 65). This model relies heavily on information provided by rating agencies and the like and worked relatively well due to relatively stable market conditions before the crisis. Yet, this model of banking collapsed during the early stages of the financial crisis. This collapse was additionally aggravated by the homogeneity of banking activity leading to "common market exposures" (BIS 2008: 133).

Second, "shadow banking" that "involves commercial bank lending that is wholly or partially removed from bank balance sheets as long as market financing is available" including "the reduction of capital needed to support lending" (Hardie & Maxfield 2013: 67). Short-term money markets are the "lifeblood" of these banking activities (Pozsar *et al.* 2010: 50). However, when these markets dried up in the course of the crisis, this led to "unanticipated balance sheet expansion" (BoE 2007: 14). In 2007 alone this balance sheet expansion amounted to £ 147.4 billion with far-reaching effects on bank's capital requirements (ibid.).

Third, "wholesale funding" by banks that obtain money "to make loans or purchase loans made by others, not from depositors, but by borrowing from each other" (Hardie & Maxfield 2013: 65). British banks were heavily exposed to this kind of funding and needed to raise almost 50% of their funds in the market (IMF 2010: 67). Furthermore, British wholesale funding was especially exposed to the US$ inter-bank market with external assets of British banks amounting to 54% of all assets (McGuire & von Peter 2012: 163).
Bank's investments in securitised mortgages exemplify this extreme exposure to market risks (Figure 9)[27]. With Northern Rock being an outlier, all banks except Barclays showed growth rates in mortgage stock over 5%. Furthermore, most of these banks had more than 20% of their mortgage stock securitised. As will be shown below, most of these banks had to be bailed out by the British government.

27 Source: BoE 2009a: 17; data pre-date the merger of Lloyds TBS and HBOS, which was completed on 19 Januar 2009; percentage of mortgage book securitised as at end-2007; average annual growth in mortgage stock from end-2004 to end 2007.

Figure 9:
Share of UK mortgages securitised by UK banks versus growth in stock of mortgages



Thus, not surprisingly, British banks were, alongside their American counterparts, affected most by the Great Recession. As table 10 shows, among the 15 banks reporting the greatest losses between 2007 and 2010 are in large part from the UK (four) or the U.S. (nine)[28].

Table 10: Estimated bank losses 2007 – 2010

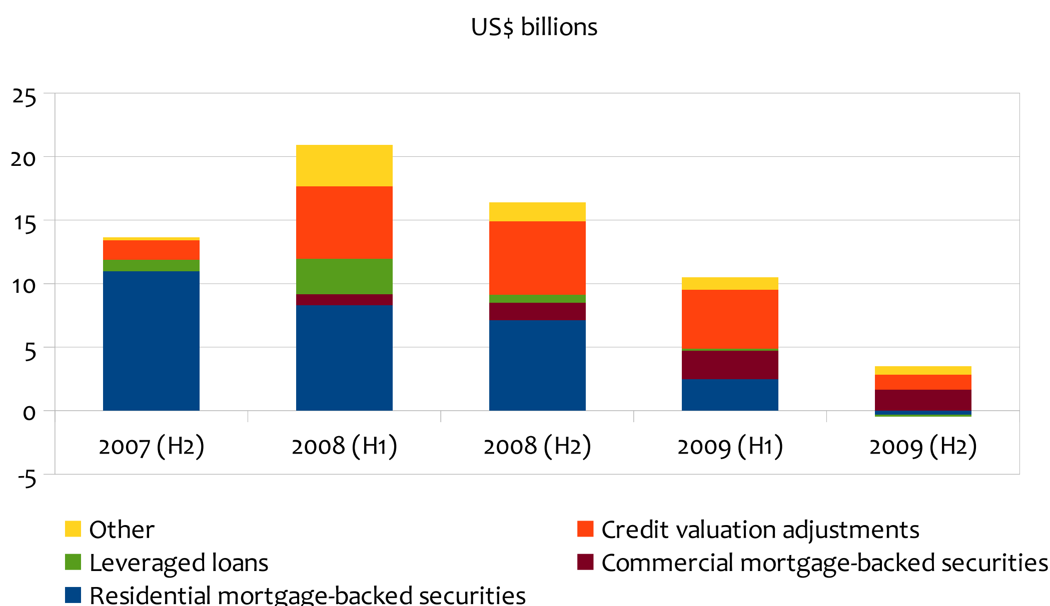
Bank	**Estimated losses ($ billion)**				
	2007	**2008**	**2009**	**2010**	**Total**
Citigroup (U.S.)	*29.1*	*63.4*	*30.7*	*30.8*	***154.0***
Bank of America (U.S.)	*12.1*	*29.2*	*35.5*	*34.4*	***111.2***
Lloyds (UK)	6.8	28.9	36.1	10.3	**82.1**
Wachovia Group[29] (U.S.)	*4.0*	*73.4*			***77.4***
HSBC (UK)	*19.3*	*30.3*	*26.4*		***76.0***
JP Morgan Chase (U.S.)	*4.5*	*10.2*	*29.5*	*24.7*	***68.9***
Royal Bank of Scotland (UK)	7.0	23.5	21.3	14.9	**66.7**
Merrill Lynch[30] (U.S.)	*25.1*	*38.6*			***63.7***
UBS (Switzerland)		*50.6*	*1.8*	*0.1*	***52.5***
Wells Fargo (U.S.)	*3.5*	*8.7*	*18.2*	*17.6*	***48.0***

28 Source: Reuters 2011.
29 Acquired by Wells Fargo at the end of 2008.
30 Acquired by Bank of America on 1 January 2009.

Fannie Mae	*4.7*	*26.9*	*15.4*		***47.0***
Barclays (UK)	7.0	16.5	12.7	9.2	**45.4**
Freddie Mac (U.S.)	*5.2*	*24.4*	*12.8*		***42.4***
Washington Mutual[31] (U.S.)	*5.1*	*36.7*			***41.8***
Santander (Spain)	*4.8*	*8.3*	*13.2*	*14.0*	***40.3***

Write-downs were comparably high for major UK banks especially in terms of mortgage-backed securities and credit valuation adjustments (Figure 10)[32].

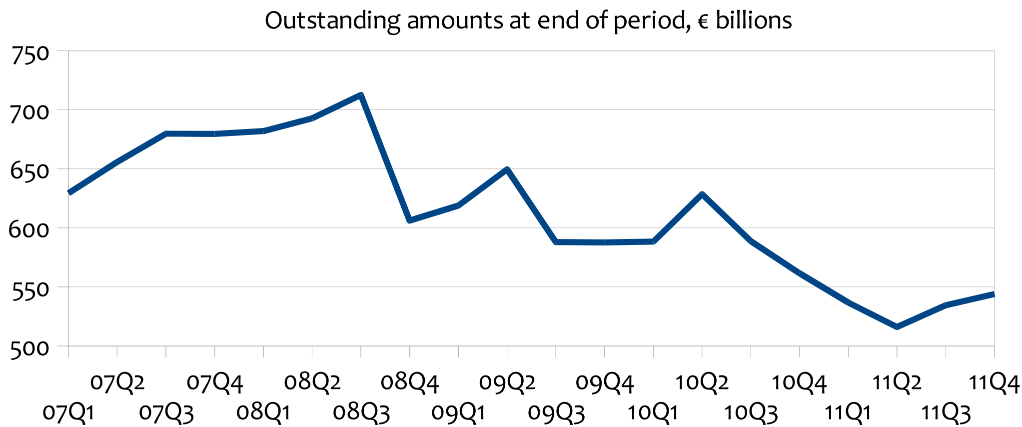
Figure 10: Major UK banks' write-downs



Finally, as figure 11 shows, lending to non-financial corporations, already relatively low in the UK (Talani 2011), practically nose-dived after 2008 and has barely recovered since[33].

31 Acquired by JPMorgan in September 2008.
32 Source: BoE 2010a: 46; includes all write-downs due to mark-to-market adjustments on trading book positions where details are disclosed by firms; credit value adjustments on exposures to monolines and other; other includes structured investment vehicles and other asset-backed securitiy write-downs.
33 Source: ECB Statistical Data Warehouse.

Figure 11: UK lending to domestic non-financial corporations



6.4.1 Saving the banks

To evaluate all policy-measures by the British government during the crisis would go beyond the scope of this thesis. Therefore, I first give an overview on the two central bailout packages announced in October 2008 and January 2009 respectively. Second, I then focus on the state's bank shareholdings managed by UK Financial Investments (UKFI), namely Lloyds Banking Group, Royal Bank of Scotland (RBS) and Northern Rock.

The British authorities also had some "first mover" advantage setting the pace by being the first country to adopt a comprehensive bailout plan. This early and swift reaction to the crisis was further facilitated by the availability of significant expertise on financial matters in crucial institutions, particularly at Downing Street as well as the treasury, and the British political system giving prime minister Gordon Brown (Labour) and his executive far-reaching authority without further consideration of parliament (Quaglia 2009: 1069-1069). Although opposition leader David Cameron offered his full support, the prime minister did not need to rely on it and could, for example, include only Labour ministers and civil servants in his economic council (*Spiegel-Online,* 14 October 2008).

Rather, Brown relied on making his measures politically acceptable to the banking industry (Moschella 2011: 88). This resulted not least in regulation reflecting a consensus between regulatory and banking elites as well as the close integration of newly established institutions like the UKFI with elite networks in the City of London (Froud *et al.* 2010: 30-34).

Table 11 summarises the two large British bailout programmes in 2008 and 2009 and gives an overview over the time frame and objectives of the measures conducted[34].

34 Source: *Bank of England,* 03 February 2009, 25 September 2009; BoE 2008: 10, 2014: 12-13; Russo 2012: 177-182; *UK Debt Management Office,* 13 October 2008*,* 22 April 2009*,* 29 March 2010.

Table 11: British bailout programmes, overview of measures

Name	Time frame	Measures	Objectives
Special Liquidity Scheme	April 2008–January 2009 (closed January 2012)	⅄ Allows banks to swap for up to three years illiquid assets they held on their balance sheets as at 31 December 2007 for UK Treasury Bills in return for a fee ⅄ Risk of losses remains with the banks ⅄ Collateral has to be highly rated and is subject to significant haircuts ⅄ Treasury Bills with face value of approx. £ 185 billion have been lent ⅄ Nominal value of securities held amounts to approx. £ 287 billion (valuation approx. £ 242 billion as of January 2009)	⅄ Tackle overhang of asset-backed securities ⅄ Improve liquidity in the UK banking system ⅄ Increase confidence in financial markets
Credit Guarantee Scheme	October 2008–February 2010 (closed October 2012)	⅄ Treasury guarantees issued debt instruments up to three years in return for market oriented fee ⅄ In order to be eligible institutions must have raised or committed to raise Tier 1 capital ⅄ Outstanding issuance amounted to £ 125 billion (as of March 2010)	⅄ Provide short-term liquidity ⅄ Make available new capital to UK banks ⅄ Maintain lending in the medium term
Discount Window Facility	October 2008–today	⅄ Allows banks to borrow highly liquid assets in return for less liquid collateral in return for a market oriented fee ⅄ Drawings have a maturity of 30 days	⅄ Aimed at banks experiencing a firm-specific or market-wide shock
Guarantee Scheme for Asset-Backed Securities	April 2009–December 2009	⅄ Treasury guarantees residential mortgage-backed securities up to five years in return for market oriented fee ⅄ Eligible institutions are the same as for the 2008 credit guarantee scheme	⅄ Improve banks and access to wholesale funding markets ⅄ Help support banks' lending in the economy ⅄ Protect the taxpayer

6.4.2 Northern Rock, RBS and Lloyds Banking Group

After having problems to finance its lending during summer, it was announced in September 2007 that Northern Rock would receive financial aid from the Bank of England. It became to first bank to be recapitalised since the Bank of England overhauled its lender of last resort rules in 1998 (*Financial Times,* 14 September 2007). Northern Rock's financing issues then were described by Treasury officials as a "temporary problem" and "nothing to worry about". The loan was to be provided at a penal interest rate, since the Bank's management was considerably to blame for the problems (*BBC*, 13 September 2007). However, a few days later £ 2 billion already had been withdrawn by savers "besieging" Northern Rock branches (*BBC,* 17 September 2007). Therefore, 22 September 2007, Northern Rock was forced to borrow about £ 3 billion from the bank of England (*Financial Times,* 22 September 2007).

Until December, government lending to Northern Rock had piled up to £ 25 billion. Yet, since the Banks financing problems continued it was considered to either sell the bank to a private investor or put it, temporarily, in public ownership with the latter being the preferred solution (*The Guardian,* 14 December 2007). Finally, on 17 February 2008, it was decided to nationalise Northern Rock completely since bids by private investors did not ensure that the government loans to the bank would be repaid duly and therefore did not "deliver sufficient value for money" (*Bloomberg,* 17 February 2008). On the same day, Alistair Darling, the Chancellor of the Exchequer, promulgated that the bank "will be run at arm's length and on a commercial basis" (*HM Treasury,* 17 February 2008).

Later in 2008 a new institution was founded to manage the Government's shareholding in diverse British banks (see also below), the UKFI. The Treasury assured that the investments will be "managed on a commercial basis by a new arm's length company" aiming at creating "value for the taxpayer as shareholder, with due regard to financial stability and acting in a way that promotes competitions" (*HM Treasury,* 03 November 2008). The latter has subsequently been affirmed by a report published by the British Office of Fair Trading saying that "public support for Northern Rock did not […] have a significantly adverse impact on competition" (*Office for Fair Trading,* 10 March 2009). Finally, on 17 November 2011, it was announced that Virgin Money would take over the Bank for £ 747 million. Yet, Northern Rock's bad bank Northern Rock Asset Management that had been split off earlier remained in public ownership (*BBC,* 17 November 2011)[35].

The aforementioned bailout programme dating October 2008 also included a recapitalisation amounting to £ 37 billion of three big UK banks, namely RBS and Lloyds Banking Group[36]. In these cases it was also asserted by government officials that the partial nationalisation resulting from the capital injection would be only temporary (*Financial Times,* 13 October 2008). It was planned that RBS would receive £ 20 billion with the remaining £ 17 billion going to Lloyds and HBOS (BBC, 13 October 2008). On the same day it was announced that four of RBS' senior board members would leave their positions. At a press conference the Chancellor of the Exchequer stated that they would be replaced by people "who understand the business" and that he therefore was "looking for people with a banking background rather than a civil service background" since "banks must be run on a commercial basis" (*The prime minister's Office,* 13 October 2008).

The result of these capital injections was that, by November 2008, the government owned just below 58% of RBS and more than 40% of Lloyds (*FAZ,* 28 November 2008). Due to further investments and a share swap, until January 2009 the government's share in RBS rose up to almost 70% (*BBC,* 19 January 2009). The government's share in RBS later rose further to 82% (UKFI 2012: 17). November 2009 then saw RBS and Lloyds selling 318 and 600 of their branches respectively due to competition concerns (*FAZ,* 04 November 2009). Furthermore, Lloyds confirmed a capital increase amounting to £ 13.5 billion to avoid joining the government's guarantee scheme for asset-backed securities (*BBC,* 03 November 2009). In February 2010, Lloyds conducted another issuance of shares whereupon the government's share in the bank dropped to 41% (*The Guardian,* 12 February 2010). Finally, in September 2013, the British

35 Alongside with the mortgage assets by former building society Bradford & Bingley (*The Guardian,* 01 October 2010).

36 Lloyds banking group is the result of a merger of Lloyds TBS and HBOS announced September 2008 and finalised January 2009 (*BBC,* 17 September 2008; 12 January 2009).

government started to sell its shares in Lloyds yielding a profit. As a result its stake in Lloyds today amounts to 32.7% *(Spiegel-Online,* 17 September 2013).

6.4.3 Economic Discourse

The quoted statements by government officials already indicate the direction economic discourse took during the bailout programmes. It emphasised three aspects. First, market discipline was supposed to be the most important mechanism to revive the British banking and financial system. Second, it was considered essential to keep the British financial system internationally competitive. Third, the economic crisis was regarded as a "crisis of (sovereign) debt".

Although bankers have been heavily criticised for exorbitant remuneration and bonuses this critique has been expressed to a lesser extent on a moral or ethical basis. Rather, high bonuses were to be disapproved when they had the potential to be "reward for failure" as the Treasury called it *(The Telegraph,* 13 October 2008). As mentioned before, managing the nationalised banks was to be conducted on a commercial, arm's length basis. The Bank of England's financial stability reports repeatedly referred to market pressure being the preferred mechanism to constrain the bank's "excessive risk-taking activities" (BoE 2009b: 37). Yet, market discipline can only work when there is "reliable, timely and granular information", thus the reform of disclosure practises (BoE 2010a: 62; on the issue of transparency and computability of information see Best 2010; Blyth 2013a). Sharpened market discipline would also improve the taxpayer's shareholder value (BoE 2010b: 53). Regulatory legislation consequentially remained very limited focussing mainly on capital requirements (Froud *et* al.: 2010, Morgan 2012).

Notwithstanding this critique, "[b]oth the government and the Conservative opposition have made it clear that financial sector reform must not jeopardize the international competitiveness of the City" (Hodson & Mabbett 2009: 1055). Rather, the government emphasised the "pivotal role" of the financial sector for the UK's economic growth and regulation as a "critical success factor" to preserve the UK's role "as a global leader in financial services" (HM Treasury 2009: 18, 23, 21). Furthermore, in a common statement, Gordon Brown and Nicolas Sarkozy highlighted the importance of "world-class financial centers such as London and Paris" (*The Wall Street Journal,* 09 December 2009). Consequentially, the UK resisted most regulatory reforms on EU level fearing that they would damage the competitiveness of its financial industry (Quaglia 2010: 524-525).

Moreover, generally speaking, economic discourse in the UK became soon a "crisis of debt" discourse focussing on the dangers of "excessive" sovereign debt instead of dangers originating from the financial sector (Gamble 2012; Hay 2013).

6.4.4 Short summary

To sum up, the British bailout programme has been mainly directed by the prime minister and his staff and under significant influence from the banking industry. Main objectives of the bailout and regulatory reforms were "value for money", perceiving the taxpayer as "shareholder" and the preservation of the UK's financial system's international competitiveness. These measures were accompanied by a liberal discourse with a focus on market mechanisms.

7. Summary and comparison

Tables 12 to 15 sum up the empirical findings and compare them to the hypotheses.

Table 12: Political System, findings

France	
Hypothesis 1: Political decision-making is dominated by the French president without major consultation with parliament	
Findings:	
⅄ „Monarchical" process of policy-making	+
⅄ Parliament as by-stander	+
Germany	
Hypothesis 1: Policy-making is consensual and informed by profound consultation with parliament and regional states	
Findings:	
⅄ Federal Council co-decided on most laws	+
⅄ Representative of regional states at SoFFin's decision-making body	+
⅄ Resignation of Saxon's minister of finance for not involving parliament	+
UK	
Hypothesis 1: Political decision-making is dominated by the British prime minister without major consultation with parliament	
Findings:	
⅄ "elected dictatorship" (*Spiegel-Online,* 14 October 2008)	+
⅄ Development of the bailout plan in opaque circles and influenced by the banking industry	+

The analysis shows that the political processes leading to the specific bailout programmes in France and Britain were dominated by the respective head of government. The involvement of regional states in the German policy-making process was at least in terms of the LBs inevitable. However, the French case shows that the personality of the head of government is also highly influential.

In compound politics the institutions of the political system may be regarded as having a more direct influence on the decision-making process since they consist, at least to some extent, of formal rules that clearly determine when and which other political actors outside government have to be involved. Simple politics leave more autonomy of choice to the respective head of government whom to directly involve in the political process.

Table 13: State-market relations, findings

France

Hypothesis 2: Bailout programme is dominated by personal networks and has protectionist side-effects

Findings:

- „Remarkable sociological unity of public and private elites“ (Jabko & Massoc 2012: 575) +
- Political allies and friends installed in important positions +
- BPCE as new „national champion“, BNP Paribas takes over Fortis +

Germany

Hypothesis 2: Bailout-programme is consensual, informed by consultations with private sector and refrains from radical market interventions

Findings

- Broad deliberative process with banks and *Laender* +
- Financial involvement of banks in bailout programme +

UK

Hypothesis 2: Bailout programme is as non-interventionist as possible, aims at preserving the competitiveness of the financial sector and influenced by financial elites from the City

Findings:

- Banking elites influence on bailout plan and institutions +
- Despite nationalisation arm's length and commercial management +
- Limited regulation on the national level, resistance to regulation on the international level +

The French case suggests a fall-back to traditional ways of state influence that has been described by Clift "post-*dirigiste*" (2012a, 2012b). Yet, German and British governments also did not break with the traditional state-market relations. This holds true for the decision-making process as well as policies themselves.

One reason for the involvement of actors from the financial and banking industry in all three cases may have been the need for expertise. Another one may have simply been vested interests investing in policies that have a direct effect on their day-to-day business. Albeit these two reasons may be generally applicable there were still specific logics of private sector involvement and policy contents. For example, British bailout policies were highly concerned with avoiding banking sector concentration whereas the French policies further strengthened French big players.

Table 14: Economic discourse, findings

France

Hypothesis 3: Bailout programme accompanied by a discourse that criticises financial markets and advocates the state as a necessary corrective

Findings:

⅄ Post-*dirigisme*	+
⅄ Managed globalisation	+

Germany

Hypothesis 3: Discourse advocates the state as a moral corrective that protects economic freedom from negative market excrescences

Findings

⅄ Moral debate about management salaries	+
⅄ State as "guardian of economic freedom"	+

UK

Hypothesis 3: Bailout programme accompanied by a discourse that emphasises the freedom of markets and the significance of financial markets for the political economy

Findings

⅄ Arm's length, money for value, no rewards for failure, market discipline	+
⅄ Crisis of debt replaces crisis of financial markets	+

Political as well as market actors in all three cases resorted to traditional discourses to make sense of and legitimise political action in times of uncertainty and crisis. However, as the French case shows, discourse is not action. This is best exemplified by Sarkozy's double minded statements, initially promising a liberal rupture with France's *dirigiste* past and soon thereafter harking back to an anti-liberal, anti-market discourse. An observation valid for all three cases is that political action fell short of a political discourse that in the beginning demanded far-reaching regulatory reforms.

Table 15: Financial system, findings

France

Hypothesis 4: French bailout programme aims at protecting the structure and international position of the French financial sector

Findings:

⅄ Demand for national solutions to financial crisis	+
⅄ Consolidation of banking market	+
⅄ No direct intervention in financial market	+

Germany

Hypothesis 4: Bailout programme aims at sustaining bank lending to the industry and to cut back the financial market activities of the LBs

Findings

⅄ Lending to industry has been sustained during the crisis	+
⅄ LBs downsized investment banking	+
⅄ Preservation of three pillar system as political priority	+

UK

Hypothesis 4: British bailout programme aims at preserving the competitive status of London as a global financial centre

Findings:

⅄ "Pivotal role" played by the financial industry	+
⅄ Limited national regulation, resistance to international regulation	+

Political action in all three cases aimed at preserving and fostering the competitiveness and advantages of specific national financial and banking systems. However, it cannot be said that this is the equilibrium outcome of a rationalist decision-making process. Competitiveness may best be viewed as a social construction, too, since political action has also been informed by the appropriateness of certain business models and the refusal of others (see also Sennholz-Weinhardt 2014; Thiemann 2014).

Although there have been institutional changes in all three countries (and especially the emergence of new institutions) these do not represent a break with the past, but rather a move to "help stabilize prior practices" (Deeg & Jackson 2007: 171). Political decision-making and how it is influenced by social institutions, cannot be understood by considering institutions "one by one, in isolation from each other, but only as elements of the larger social system to which they belong—which in addition must be conceived not as a static *structure,* but as a dynamic *process"* (Streeck 2009: 1).

8. Conclusion

The Great Recession has been a one-of-a-kind event. Yet, it did not result in an all-embracing break with our (institutional) past as a historical approach would possibly predict. Rather, political reactions to the crisis followed established logics of action guided by historically grown and socially constructed institutions. Although in the early stages of the financial crisis capitalism has been criticised harshly, this has not at all resulted in an all-embracing overhaul of how our day-to-day economic life is organised. Neo-liberalism as an ideology and capitalism as a form of political economy have remained surprisingly "resilient" (Schmidt & Thatcher 2013), its "non-death" leaving some observers astonished (Crouch 2011). It seems that neo-liberalism as an ideology has become so dominant that it is not questioned even in the face of its most shattering crisis. A narrower focus on ideas and how they directly influence (political) action may be one of the most promising approaches towards understanding this aspect of the recent economic history (Blyth 2013b).

Yet, as this study has shown, talking about "neo-liberalism" and "capitalism" as if they would be clear-cut descriptions of real-world phenomena oversimplifies things. There is not only one occurrence or two "varieties" of capitalism. Rather, analysis of capitalist political economy needs to take into account a variety of political institutions and ideas that inform and influence policy-makers in their actions.

Furthermore, the state has proved to be a decisive actor. The state has been a decisive actor in liberalising and globalising financial markets (Helleiner 1994, 1995). It has been a decisive actor in implementing neo-liberal reforms on the national level (Schmidt & Woll 2013). And, last but not least, it has been a decisive actor in managing the financial crisis. There has been no "retreat" of the state (Strange 1996). Yet, it also remains questionable if the State gained "new power" (Hassel & Lütz 2012). It rather seems that there is an ever-ongoing and interdependent process between the state influencing the market and market actors influencing policy.

Albeit a case study analysis is not able to develop universal laws or predictions on policy-making or market developments, it is able to shed light on specific events in history and possible lessons drawn from these events. By sharpening our lenses such a study may contribute to making sense of events influencing our everyday life and to transfer at least parts of our conclusions to other cases and phenomenon.

Fioretos shows how historically informed approaches on "capitalist diversity" can be applied to issues of global regulation or the EU's role in the global economic order (2010a; 2010b). Locating politicians within their national economic and political systems may allow us informed speculation about their preferences and actions on the international level. For example, German's strong stance on rule-based austerity as a solution to the European debt crisis may best be understood in the light of its ordo-liberal economic discourse and its specific growth model (Berghahn & Young 2013; Bonatti & Fracasso 2013). Howarth & Quaglia show how negotiations about the adaption of the so-called "Basel III accord" into EU legislation are influenced by national institutions (2013). Given the tendency towards inter-governmental solutions to the European debt crisis, the influence of national institutions may in the future even increase.

However, as this study has shown, politicians are not isolated and purely rational decision-makers. They are embedded in a social context that influences their preferences and decisions and that makes it necessary to take a closer look at the factors that inform policy-making. These national (and personal) factors, it seems, prevail notwithstanding all interdependencies that characterise the globalised world and the "New Age of Uncertainty" we are living in.

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