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Global Finance, Industry and Shareholder Value

6.1 Introduction

A key reason why the UK persisted with a pronounced pro-market stance – even after the Thatcher-Major years had delivered no increase in trend growth – was the intellectual climate that paralleled the emergence of a finance dominated global economy. We outline in section 6.2 how financial globalization shaped ideas on economic policy from the 1980s, and in particular macroeconomic and industrial policy. In section 6.3, we deal with the crucial question of how market orientation affected the institution of the firm so that the corporation as an institution no longer plays the relatively independent role in economic development that it once did.

6.2 Finance and the global environment

Throughout the twentieth century, Britain’s economic policy has catered to the interests of the City of London. Nevertheless until at least the early 1980s, industry constituted a powerful counterweight. Firms tended to be financed out of retained earnings (Mayer 1988), so that decisions at company level were to some extent autonomous, especially when weak competition facilitated this. Finance was powerful but even in the UK for a great many years it was just one pillar of the economy.

All of this was to change in the 1980s and 1990s, not just in the UK but internationally as well. To understand this we must separate out the domestic fact of a finance-dominated industrial structure in the UK from the global forces that were making finance more powerful everywhere. The key was the increasing international mobility of capital.
that had been heavily constrained during the fixed exchange period up to the early 1970s. An important rationale for this early constraint was that a contrary policy – under fixed exchange rates – would have enforced common monetary policies on all countries – similar to the operation of a gold standard. An extreme form of globalization was thus avoided and countries were free, at least up to a point, to develop along separate capitalist lines with different institutional approaches to issues in finance, labour relations and industrial policy. Once flexible exchange rates were established after the break-up of the Bretton Woods agreement, capital controls were no longer seen as a necessary part of the framework resulting in a different and more highly globalized system (Rodrik 2011).

**Capital mobility**

Capital controls were lifted very early in the first Thatcher government to open up London to US investment banks. A decade later, by the end of the 1980s capital flows were unrestricted in all major European countries. The US and the UK, with their large financial services industries, were to the fore in pressing for further liberalization and they lobbied successfully for capital mobility to be a condition for OECD membership. Towards the end of the 1990s the IMF also committed itself to removing restrictions on capital flows internationally, something that up to then had not been part of the globalization programme which had focused more narrowly on traded goods. Trade negotiations had by then also become focussed on liberalizing services trade, in particular banking and business services which would particularly benefit those industries in the US and UK. The environment in which these changes operated is known as financialization.

The international capital markets were now dominant, but they did not work as economic theory had predicted; they proved highly volatile, with real exchange rates failing to regulate flows between debtor and creditor countries. Capital imports, often recommended for developing nations, became a feature of some developed ones, particularly after the Asian crisis of the late 1990s. Some countries such as the US and UK were permitted to run current account deficits, spending more than they produced and exporting less than they imported. Others such as Germany, Japan and China ran large surpluses. For some developing countries, current account deficits were possible to sustain as long as international capital markets were willing to underwrite the necessary capital inflows. Overall however these large imbalances contributed to global uncertainty.