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The reinvention of prudence: household savings, financialisation and forms of capitalism

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Abstract

Increasing levels of personal debt, soaring house prices and a looming pensions crisis have recently stimulated considerable interest in household financial behaviour. Using macro data from the financial accounts of the four largest economies in the EU from 1980 to 2003, we observe that the bourgeois virtue of prudence needs to be redefined because, in an era of financialisation, in all four countries household portfolios converge towards riskier investments. At the same time, household reactions to the major economic events of the last twenty years are more complicated than the existing literatures on financialisation and varieties of capitalism would suggest.

Keywords

Household assets, Financialisation, Varieties of capitalism, Household financial behaviour

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The reinvention of prudence: household savings, financialisation and forms of capitalism

> I could at all events be certain that my future was fully provided for. I had entrusted the round sum of eighty thousand marks to the city bank; the interest – these are poor times, heaven knows!- amounted to about six hundred marks a quarter, and this was enough to permit me to live decently, to buy books, to go the theatre now and then – not excluding an occasional lighter diversion.
>
> Thomas Mann *The Joker* (1897)
>
> while her family's debts (including £20k on credit cards) were 'horrendous', the equity in her two London houses and two flats, plus the 'fabulously chic' flat in Paris she rents to tourists, easily outstripped the money owed. It was because she was 'pretty happy with risk' that she had invested early on in a big house in the capital which had risen in value and enabled her to have the family and life she wanted
>
> Rosie Millard, journalist, quoted in the *Guardian* (5 April 2005)

This paper is about how prudence is being redefined and reinvented in a period of financialisation, when households increasingly own a range of assets and are faced with complex choices between asset classes. The empirics about household savings in several European countries in turn raise interesting questions about the adequacy of conventional supply side ways of thinking about varieties of capitalism. If the paper starts from a question about what prudence is or might be, the business press shows that prudence is continuously being politically redefined. Prudence is something our political leaders apparently have because, according to the *Economist* (10 February 2005) George W. Bush's recent proposal for privatising US social security are based on a preference for prudence over ideology. Yet, prudence is something which still needs to be maintained by restrictions on the general population because in George Bush's individual retirement accounts 'there will be rules to guard against risky behaviour and individuals will have limited investment choices'. But the boundaries on acceptably prudent saving are also being continuously extended, as when the UK authorities consider whether to include investment in holiday homes abroad in the basket of tax-deductible savings for retirement or when to allow retail investment by small investors in hedge funds (*Financial Times,* 10 June 2005).

Just what has changed and how over several decades? The average bourgeois has never been able to heed Shakespeare's abstentionist advice to 'neither a borrower nor lender be' and has instead practised prudence which, as our opening quotes illustrate, is a bourgeois virtue manifest through different behaviours in various contexts. From the mid nineteenth century onwards, prudence used to be defined for the respectable working class and petit bourgeoisie as holding down a job, saving cash in deposit accounts and avoiding debt by always keeping income below expenditure. If there was some capital available, prudence implied putting it into something secure such as bonds or house property, which brought modest income with very little risk to capital. The positive values were predictability of capital and income, confidence in the financial intermediaries (which were almost exclusively banks with their local branches) and understanding of the risk/return characteristics of different investments with clear contractual arrangements. Thomas Mann, the quintessential man of letters on bourgeois values, vividly depicts an example of this commonly accepted form of prudence in his 1897 story *The Joker* (Mann, 1993). In our first opening quotation, the hero of the Mann story contemplates, at the age of twenty-seven, a prudent and cultured life until his last days after depositing his inheritance of eighty thousand marks into a bank account and counting on a quarterly interest income of six hundred marks.

The second quotation from a recent newspaper story illustrates the rather different calculations of a bourgeois of our own time, the BBC's former arts correspondent. Journalist, Rosie Millard and her husband owed £20,000 to credit card companies and their bank but also owned two houses and three flats as part of 'a property portfolio extending well beyond the £1 million mark' (*Guardian,* 5 April 2005). Here the old bourgeois values are more or less inverted because increasing debt covers expenditure which is greater than income because of purchases like £800 dresses. Increasing debt is explicitly not a problem because 'risk' has been embraced and the journalist has assets in the form of property whose capital value is increasing. The deficiency of income is being covered by the appreciation of capital so that this bourgeois now becomes a gambler in a world of uncertain future capital values where it will only come good if the value of his/her risky assets increases.

If Rosie Millard is perhaps an unusual case, it is clear that there has been a more general reinvention of prudence which has increasingly broadened the legal and professional definition of prudent investment, which now increasingly includes alternative investments like hedge funds (Crawford, 2002, p. 12). This point emerges very clearly from Crawford's history of how the definition of prudent investment has evolved in the US since the court case of *Harvard College v. Amory* in 1830. In 1934, five years after the 1929 crash, investing in stocks was condemned by the court as speculation verging on gambling whereas in 1986, in the early years of the bull market of the last two decades of the 20th century, a court imposed liability on a bank for failing to include stocks in a portfolio (Crawford, 2002, p. 9). According to the Uniform Prudent Investor Act (UPIA) in the USA, what becomes customary practice in the investment community is also, by definition, the required practice.

This reinvention of prudence and the resultant change in patterns of household assets and liabilities could be analysed and mapped from several different points of view and needs to be set in a social science context. However, the reinvention of prudence is not well suited to relational analysis by a mainstream economics that tries to find general or universal relations across variables (with different countries figuring as observations). This is because the empirical evidence on European countries summarized in later sections of this article shows rapid shifts in household behaviour, feedback and ricochet effects as well as path dependency. Over the past twenty years in all the high income countries, households have shifted between asset classes so that it is difficult to generalize about behaviours and relations that stay the same. Part of this change could be rationalized ex post as the pursuit of optimality, but the concept of an optimum portfolio is slippery because it pre-supposes more certainty of risk and reward than is often the case given the conditions of various asset markets and the limited financial literacy of many consumers (Erturk *et al*., 2005); for these reasons, ex post labelling may not be very enlightening.

On the other hand, time series and cross section differences in behaviours and relations are in themselves interesting and in this paper we analyse them by considering how the changing patterns of household savings over the past twenty years in several European countries extend and modify our understanding of the varieties of capitalism and the broader processes of financialisation. As we argue below, issues about varieties of capitalism have been generally understood in supply side terms by considering bank and market interaction with productive firms which have shareholders and stakeholders. How then does the bank versus market distinction appear from the different point of view of households and savers' decisions about asset classes? Is there a distinction between households in the Anglo-American economies and the rest? And how does behavioural change fit with the idea of a 'model of capitalism' (e.g. Rhenish v Anglo American), which would imply fairly stable behaviour and identity within institutional frames that do not change, so that we could distinguish bank-based from capital market-based economies in 1985 and 2005.

We would also wish to make the connection with the financialisation literature where there is a need to broaden out existing discussion. Aglietta (2000) has written about a patrimonial

society where ordinary households hold assets as well as selling labour. But a flurry of discussion around 2000 at the end of the bull market both increased and narrowed discussion insofar as it elided financialisation with shareholder value and the stock market. Consequently, researchers with interestsin the role of capital markets in European countries (see for example Boyer, 2000 and Schmidt, 2003) work with a narrow definition of household participation in financial markets and look at share ownership alone. In contrast, Froud *et al.* (2002) argue for the importance of examining all coupon-like investments, and this has an obvious rationale when equity does not necessarily dominate household financial portfolios and housing markets are important in a Europe where net wealth per household is increasing because assets are increasing faster than liabilities.

The paper which takes up these questions and issues is organized in a relatively straightforward way into three sections. The first section surveys the existing varieties of capitalism and financialisation literatures and develops the argument that both literatures limit our understanding of the dynamics and trajectory of present day capitalism if our concern is with (changing) household behaviour. The second section presents and analyses the available empirical data on household asset portfolios since 1980 in the four largest economies of the European Union - Germany, France, Italy and the UK. The third section returns to the literatures on forms of capitalism to examine the notion of household capitalisms; this is followed by a concluding section that argues for an agenda of further research into the re-invention of prudence in present day capitalism. The empirical results of this article are interesting in several respects. The empirics on household savings suggest the end of the old bank versus market divergence for households because bank deposit saving has become less important in mainland Europe over the past twenty years. But this change does not imply a new convergence when financialisation has not so far established a uniform logic of investment behaviour among the households of Europe, partly because the financial services conglomerates push different products in various countries and the resulting pattern is one of variable and unstable flows of funds.

Varieties of capitalism, financialisation and limits on the field of the visible

The varieties of capitalism and financialisation literatures both raise issues about how and why ideas succeed and about the limitations of the resulting conventional wisdoms. The varieties of capitalism approach has been very popular because it represents a strong, simple way of conceiving the role of institutions in generating productive efficiency and welfare differences. These ideas have been appropriated and developed in a variety of ways but they generally offer a (fairly static), supply-side view of the differences between national capitalisms. The financialisation literature rests on a rather different assumption of change that was often represented in cartoon terms as an epochal shift from production to finance. The problem here is the way in which the general concept of financialisation became mixed up with shareholder value which was simply one (ephemeral or ambiguous) late 1990s manifestation of the new influence of the capital market on firms and households. Here again, we would argue that the new concepts of the later 1990s immediately moved things on intellectually by establishing longer term limits on the field of the visible and thinkable, but that these new concepts now need to be developed.

The varieties of capitalism literature proposes structural categorization of individual countries or groups of countries based on various configurations of institutional complementarities and hierarchies. According to this view such configurations determine the behaviour of the economic agents (Shonfield, 1964; Berger and Drache, 1996; Hollingworth and Boyer, 1997; Crouch and Streeck, 1997; Hall and Soskice, 2001; Amable, 2003; Morgan, 2005). Practically, the strategic preferences of firms and actors are influenced by supply side institutions like state, banks, financial markets and trades unions, which co-ordinate economic activity and structure a particular set of opportunities. This becomes a varieties of capitalism

approach because institutional differences between the capitalist countries or groups of countries are then used to identify economic models which help develop an understanding of how modern capitalism varies across nations. Hall and Soskice (2001) define two broad idealized categories that form the opposite poles between which all observed examples can be pegged: these are liberal market economies (LMEs) of the US and the UK type and co-ordinated market economies (CMEs) of the German and Swedish type. The same capitalistic polarity is expressed in terms of the opposition between 'institutional' economies versus 'free market' economies by Crouch and Streeck (1997), who trace the origins of this literature back to Andrew Shonfield's *Modern Capitalism* (1964) and his political quest for alternatives within capitalism. This two varieties dichotomy has of course been subsequently expanded by other authors who distinguish three or more variants. Thus, Amable (2003) expands the theoretical dichotomy of Hall and Soskice's LME and CME, into a model of five geographically distinguishable types of capitalism including the market-based, social-democratic, the Continental European, the Mediterranean and the Asian.

The underlying theoretical question is whether the models are converging, while the political question is whether a mainland European social market system can compete successfully against the Anglo-Saxon form of market capitalism. The consensus is that convergence of different varieties towards the market based model is not taking place because structural differences survive despite developments such as globalisation and collapse of communist east European regimes, both of which bring more liberalisation and deregulation of financial markets, privatisation and free flow of capital. Schmidt (2003) argues that the process labelled globalisation has not caused a convergence of varieties of capitalism in Europe: for example, it has helped France to remain as a third 'statist' alternative to the German model of 'corporatism', and the UK model of 'liberalism', models. Navarro *et al.* (2004) argue that globalisation wave between 1980 and 2000 did not alter the political character of the welfare states of Europe with social public expenditures and public employment continuing to expand. These authors find no evidence of convergence. The changing record of relative performance colours views about the competitiveness of the European social market system which have varied along with changes in the growth, productivity and unemployment rates of European economies relative to those of the USA. On this basis, the German and Japanese alternatives were much more credible in the early 1990s economic recovery than in the late 1990s period of the new economy or in the early 2000s period of apparent success for the flexibilized. But there is no consensus about one best way or even about unique configurations. Amable (2003), for example, suggests that institutional complementarities and hierarchies from each of his five forms can be strategically rearranged to achieve a new politically acceptable and desirable optimum capitalist system.

The limits of the orthodox approach to varieties of capitalism are increasingly evident. The approach samples institutional differences in a fairly stadardised way which focuses attention on product market and labour market and incidentally credits institutions like banks with behavioural consistency in a national context. The resulting approach to capitalism can be partial, static and focused on supposedly enduring differences; thus, non-convergence is perhaps not so much an empirical result as an a priori of the varieties form of analysis. This seriously underestimates the general dynamism of capitalism which the varieties approach is not theoretically equipped to deal with (see for example Strange, 1997 and Morgan, 2005). In the mid 2000s this dynamism might specifically be understood as an indeterminacy in the relations between key national institutions in different European countries as they confront common problems such as the pension crisis, housing market bubble and household indebtedness which are all consequences of the generally low interest rates that prevail after the defeat of inflation. Social democrat Sweden, Mediterranean Spain and Anglo-Saxon Britain all share similar asset price problems in their housing markets that leave policy makers and academics alike twitching (European Central Bank, 2003; OECD, 2004a; *Economist*, 3 March 2005; Borsch-Supan and Brugiavini, 2001; Borio and McGuire, 2004; Rosenborg, 2004; Ball, 2004). In focusing on differences, the varieties of capitalism approach has a

tendency to underestimate the sources of novelty and new behaviours in national economies and the dynamics of the impulses regenerating and destabilising capitalism. It is all of course partly a matter of focus and emphasis because it could be argued that the study of stability and coherence arising from different institutional structures complements the study of change and that the two are connected by the notion of path dependence which explains how surviving institutions and previous behaviours determine the nature and direction of change. However, if we want to understand change across households, the varieties of capitalism literature on its own does not provide an adequate framework.

In contrast to the varieties of capitalism focus on the product market, the financialisation literature is centred on financial markets as key determinants of the behaviours of economic actors and the trajectory of capitalism. The financialisation literature can be considered in a number of phases which include: first, the late 1980s and early 1990s work in finance and economic sociology by US scholars (Fligstein, 1990; Jensen, 1993; Useem, 1996); second, the 1999-2000 work in political and cultural economy by European and American authors (Boyer, 2000; Froud *et al.*, 2000; Lazonick and O'Sullivan, 2000); as well as more recent and innovative work by Stockhammer (2004) and Krippner (2005). Most of these works are concerned with the UK and USA as the locus of change but other researchers have explored the uneven geographical diffusion of financialisation outside the Anglo-Saxon economies from France and Germany to Turkey and Japan (Morin, 2000; Jürgens *et al*., 2000; Ertürk, 2003; Morgan and Takahashi, 2002). All the different literatures are one way or another concerned with change (not stability) but the presuppositions about how capitalism works are much more varied in the financialisation literature than in the varieties literature. One of the more obvious lines of division here is between those like the Regulationists Aglietta and Boyer, who are concerned with the restoration of coherence, and those like the cultural economists Froud *et al*., who emphasise contradiction and discrepancy. Thus, Boyer (2000) investigates whether widespread share ownership can form the basis of a new growth regime, replacing the earlier Fordist growth regime and establishing a long-term macro-economic stability where labour's purchasing power could increase with rising stock market prices after a fall in wages. By way of contrast Froud *et al.* (2000) originally observed that the gap between corporate performance and stock market expectations encouraged management as cheap tricks, subsequently developing a much more cultural 'narrative and numbers' approach to corporate strategy (Froud *et al*., 2006).

Against a background of the bull market and the new economy, the late 1990s financialisation literature analysed how the relationships between managers, shareholders and labour were being reconfigured under the influence of capital market pressure for shareholder value. The most widely read and influential writers here were almost certainly Lazonick and O'Sullivan. Their institutionalist presuppositions about the stock market fitted with those in the varieties of capitalism literature; just as their story line about a shift in US corporate behaviour from 'retain and reinvest to 'downsize and distribute' fitted with what many wanted to believe about complex evidence. According to Lazonick and O'Sullivan (2000) the pursuit of shareholder value disconnects top management from the workforce in a capitalist enterprise and hence throttles the innovative forces that sustain economic growth. Managerial behaviour changes and the management shifts its alliance from shop floor to the trading floor of the stock market. Labour force downsizing then becomes a reliable source of boosting cash balances needed for higher dividends and share buybacks. The institutional investors - pension funds, mutual funds and insurance companies - which have come to rely on such payouts are accomplices to the 'downsize and distribute' strategy of the management.

More recently, the empirics underlying this interpretation have been challenged and the debate about financialisation has been broadened out so that the (temporary) elision of shareholder value and financialisation is being corrected, allowing us to begin to understand financialisation as a more complex, longer term process. Thus, Froud *et al.* (2006) challenge the assertions about increased distribution by arguing that, if dividends to shareholders and

interest payments are added together, disbursements to capital in the US giant firms in the S&P 500 show a pattern of cyclical variation without secular increase since 1980. Meanwhile Krippner (2005) has broadened the frame around the argument by proposing a new methodology to measure financialisation and empirically demonstrating that US (non financial) firms have acquired financial assets and come to rely increasingly on profits from financial activities (as opposed to product market activities) through changes which predate the 1990s. At this point, our argument is simply that the frame can be broadened again by considering households as well as firms. The financial behaviour of households has recently attracted a great deal of popular, academic and policy interest due to the increasing levels of debt across nations, soaring prices in housing markets and the problems about funded pensions and state welfare, But the financialisation literature remains largely preoccupied by firms and their interaction with the capital markets. The productive systems approach, similarly, concentrates on labour and wages and does not problematize the wealth and income dynamics embedded in household finances, which may have significant implications for aggregate demand, welfare state and political behaviour in financialized capitalism.

Increased financialisation brings fundamental and complex changes

In this section we present an empirical analysis of the changing stocks of household financial assets since 1980 in the largest four economies in the EU - Germany, France, Italy and the UK. These four European countries were selected because they are individually important and together illustrate a range of different capitalisms. Our analysis is then constructed by building information from a variety of different sources. We have used macro data from the national financial accounts and created time-series data over a twenty-three year period between 1980 and 2003 (the UK data is available only from 1987). The European System of Accounts (ESA95) is a useful source but provides data for the EU countries only from 1995 onwards. National financial accounts provide the most consistent and comparable data but differ in how they calculate the current market value of un-quoted stocks and bonds, and in how they disaggregate non-equity securities and insurance technical reserves. Christensen and Mathiasen (2002) provide a useful survey of the statistical methodologies in the EU countries which explains such important differences. To examine the distributional aspects of household finances, liabilities as well as financial assets would need to be considered and micro-data is also needed. However such micro data currently is not available as readily and consistently as macro-data and is collected through infrequent panel surveys often have distributional biases, including under sampling the wealthiest households. Guiso *et al.* (2002) have examined the available micro-data in Germany, Italy, Netherlands, the UK and the USA and demonstrated the potential of such sources. Thus, it is difficult but not impossible to discuss the balance sheet of assets and liabilities in European countries and beyond: indeed, this article does include some basic information about household liabilities to avoid a one-sided asset-based view of financialisation. From this point of view, our current article can be considered as a pilot study which could and should be followed by a larger scale study of more countries and gives equal attention to liabilities as well as assets.

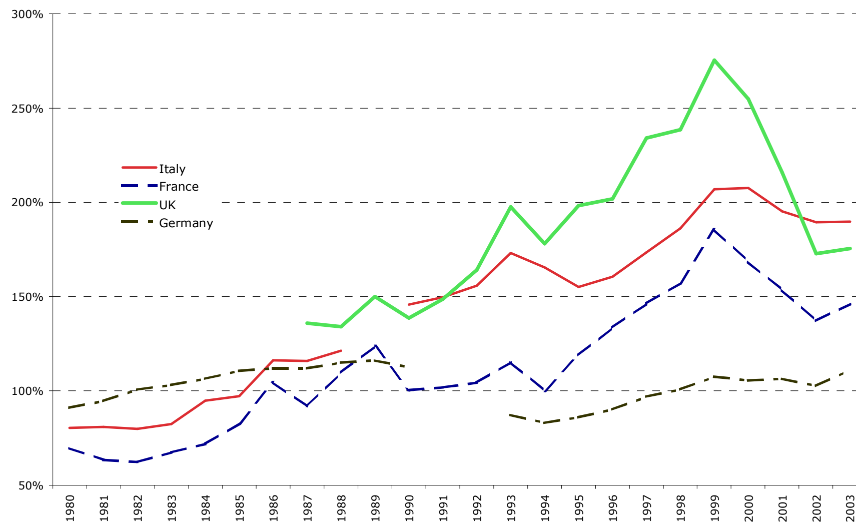
The analysis in this second section of the article develops a narrative of change by highlighting and commenting on six key changes in household asset portfolios over the past 25 years; the next section builds the story by presenting a complementary analysis of changes in household behaviour. As previously explained, the narrative form of the analysis is determined by the evidence (or more exactly is appropriate for the evidence). The graphs in this section illustrate rapid and complex changes which our narrative tries to encapsulate by focusing on several key aspects of the dynamics. In our view, the implication is that changes since 1980 have extended and intensified financialisation of the household in all four European countries in ways which have undermined a bank-based household capitalism as households across Europe expand their holdings of risky assets whose capital value can go up or down. But while these important changes abolish an old divergence between the UK and

the mainland, they do not establish convergence because important differences persist, especially those arising from direct or indirect ownership of capital market investments. The end result is an analysis which highlights a complex pattern of similarities and differences in household capitalisms in various European countries; it is also one that does not fit with existing generalisations about productive varieties of capitalism. If that interpretation is novel and perhaps controversial, we would ask our readers to consider the six changes summarized below.

Change 1: A measurable increase in financialisation insofar as household wealth in all four countries is increasingly held in the form of financial assets, which have become more important on a per capita and as a percentage of GDP basis over the past 25 years.

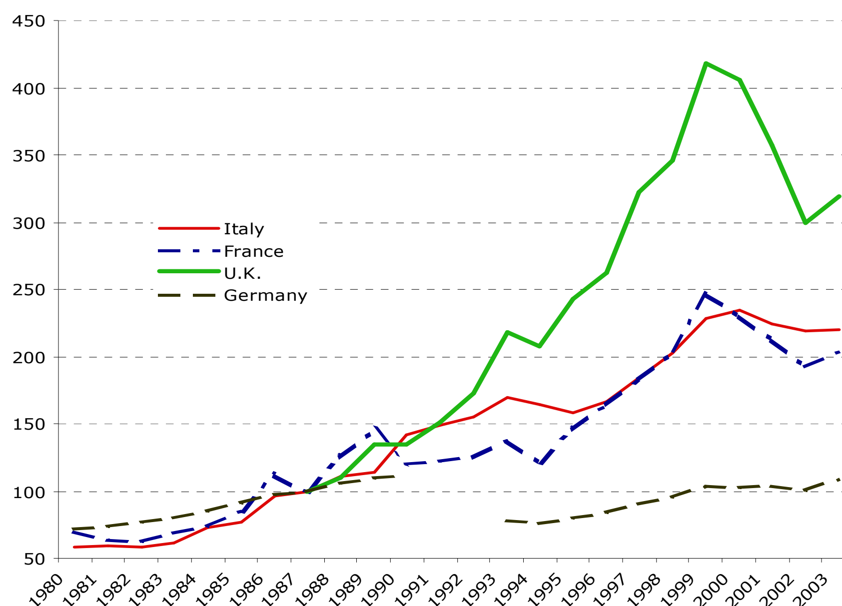
We observe in all four countries a secular increase in financialisation insofar as both net household financial assets as a percentage of GDP and financial assets per capita have increased in all four countries (see Figures 1 and 2). The increase is quite significant except in Germany where reunification in 1991 led to a step-like reduction in the significance of such assets, followed by a resumption of growth. In the German case, the impact of reunification is considerable as Germany had higher levels of net financial assets than both France and Italy in 1980. Although the UK data is not available between 1980 and 1987, it is possible to observe (and, given our stereotyping of varieties of capitalism, it is hardly surprising to find) that the level of financialisation is on our measure highest in the UK. But what is striking is the transformation in Italy where financialisation in the context of shareholder value and the stock market was never important. If household financialisation is measured extensively, Italy leads both France and Germany; moreover the Italians (and the French) increased their net financial wealth more than the British and the Germans. As a percentage of GDP, the net financial wealth of the Italians increased from 80.5% to 189.7% between 1980 and 2003 (see Table 1).

Figure. 1. ***Net household financial wealth (as a percentage of GDP)***



Sources: Banca d'Italia, Banca d'Italia (2005), Banque de France, Deutsche Bundesbank (2004a, 2004b), International Statistical Year Book (2004), National Statistics Office of the UK

Figure 2. ***Net household financial wealth per capita (1987 =100)***



Sources: Banca d'Italia, Banca d'Italia (2005), Banque de France, Deutsche Bundesbank (2004a, 2004b), National Statistics Office of the U.K., Eurostat, International Statistical Year Book.

Table 1. ***Household portfolios and wealth (as a percentage of GDP)***

	ITALY					FRANCE				
	1980	1987	1995	2000	2003	1980	1987	1995	2000	2003
Deposits and cash	55.8	50.9	74.3	58.5	60.5	56.7	54.5	57.9	58.1	58.1
Bonds	15.0	39.9	48.8	43.7	49.3	8.8	9.7	10.3	4.8	4.6
Government bonds	*11.8*	*36.2*	*40.8*	*16.5*	*15.2*	*n.a.*	*n.a*	*0.7*	*0.5*	*0.4*
Stocks	8.7	12.1	27.2	66.2	49.3	15.7	37.4	36.4	73.9	49.8
Quoted stocks	*n.a*	*n.a.*	*5.5*	*16.5*	*10.5*	*3.2*	*5.8*	*6.4*	*8.0*	*4.7*
Mutual funds	0.0	7.1	7.4	39.4	27.4	2.1	13.3	18.1	18.7	16.6
Insurances and Pension funds	5.2	6.6	18.6	28.3	35.9	6.9	11.9	33.8	53.0	58.6
Other assets	2.2	7.3	1.8	1.7	1.2	6.7	3.0	4.1	5.8	6.2
Total financial assets	87.0	123.9	178.1	237.8	223.6	96.8	129.7	160.6	214.3	194.0
Financial liabilities	*6.5*	*8.1*	*22.8*	*30.2*	*33.9*	*27.3*	*37.9*	*41.6*	*45.7*	*47.8*
Net financial wealth	80.5	115.9	155.2	207.6	189.7	69.5	91.8	119.0	168.6	146.1
Housing wealth	121.8	97.8	154.8	139.9	161	131.0	124.0	117.6	117.5	118

	U.K.				GERMANY					
	1987	1995	2000	2003	1980	1987	1993	1995	2000	2003
Deposits and cash	59.6	65.2	67.5	73.4	52.9	57.9	65.8	62.6	60.8	65.7
Bonds	7.1	6.5	5.1	4.5	11.8	17.3	17.9	19.3	17.9	20.8
Government bonds	*4.2*	*3.5*	*2.9*	*2.5*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*
Stocks	28.2	42.7	58.7	30.5	4.8	6.8	16.6	16.6	28.2	18.5
Quoted stocks	*21.1*	*23.7*	*33.8*	*18.7*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*	*n.a.*
Mutual funds	4.0	10.2	16.2	10.9	7.3	5.9	8.2	10.6	20.1	21.8
Insurances and Pension funds	92.8	138.3	176.8	144.5	16.7	24.9	36.3	39.1	49.9	54.4
Other assets	8.6	9.3	8.7	8.2	7.3	9.9	1.5	1.6	2.2	2.8
Total financial assets	200.3	272.2	333.0	272.0	100.9	122.7	146.4	149.8	179.2	184.1
Financial liabilities	*64.3*	*74.0*	*78.0*	*96.5*	*9.7*	*10.7*	*59.2*	*63.8*	*73.6*	*72.8*
Net financial wealth	136.0	198.2	254.9	175.5	91.1	112.0	87.2	86.0	105.5	111.2
Housing wealth	n.a.	151.2	198.2	253.6	n.a.	n.a.	187.2	191.0	190.3	189.0

Sources: Banca d'Italia, Banca d'Italia (2005), Bank of England (2005), Banque de France, Banque de France (2005), Brandolini et al. (2004), Deutsche Bundesbank (2004a, 2004b), International Statistical Year Book (2004), INSEE, National Statistics Office of the U.K.

Change 2: the end of a household capitalism based on bank deposits in the mainland European countries which, in this respect, increasingly come to resemble the UK where bank deposits were much less important in 1980.

In all four countries gone are the days where households, like the character from the Thomas Mann story, keep substantial amounts of their financial wealth in bank deposits. As far as the households are concerned it was possible to talk about a bank-based system in mainland Europe around 1980 but things have since changed quite radically. As Table 2 shows, in all four countries by 2003 bank deposits, cash and government bonds account for no more than around one-third of household financial assets. The households in bank-based Italy dramatically reduced their holding of safe financial assets in their total portfolio of financial assets from 77.8% in 1980 to 33.8% in 2003. This is a change of a staggering 44 percentage points in Italy, far outstripping the French reduction of 28.5 percentage points and the German 16.7 point decline in holdings of safe financial assets. As a result of these varying changes, by 2003 all four European countries more or less have converged onto holding just one third of their assets in savings accounts or coupons whose capital value is secure. The stark 1980 difference between bank-based, risk averse household capitalism in the continental European countries and a different Anglo-Saxon way has diminished by 2003, thereby, making a 'bank-based' classification in the household sector almost redundant.

Table 2. ***The share of safe and risky financial assets in household portfolios (percentages)***

	ITALY					FRANCE				
	1980	**1987**	**1995**	**2000**	**2003**	**1980**	**1987**	**1995**	**2000**	**2003**
Safe assets	77.8	70.3	64.6	31.5	33.8	58.5	42.0	36.5	27.3	30.2
Risky assets	22.2	29.7	35.4	68.5	66.2	41.5	58.0	63.5	72.7	69.8
Intermediated	*6.0*	*11.1*	*14.6*	*28.5*	*28.3*	*9.3*	*19.4*	*32.3*	*33.4*	*38.8*
Non intermediated	*16.3*	*18.7*	*20.8*	*40.0*	*37.8*	*32.2*	*38.6*	*31.2*	*39.2*	*31.1*
	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

	U.K.				GERMANY					
	1987	**1995**	**2000**	**2003**	**1980**	**1987**	**1993**	**1995**	**2000**	**2003**
Safe assets	31.9	25.3	21.1	27.9	52.4	47.2	45.0	41.8	34.0	35.7
Risky assets	68.1	74.7	78.9	72.1	47.6	52.8	55.0	58.2	66.0	64.3
Intermediated	*48.3*	*54.6*	*57.9*	*57.1*	*23.9*	*25.1*	*30.4*	*33.2*	*39.1*	*41.4*
Non intermediated	*19.8*	*20.2*	*20.9*	*15.0*	*23.7*	*27.7*	*24.6*	*25.1*	*26.9*	*22.9*
	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Derived from Table 1.

Notes: Safe assets are bank deposits and government bonds. Risky assets are direct and indirect stock market investments and corporate bonds.

Change 3: the rise of a household capitalism based on risky assets (whose capital value can go up or down) as the mainland European countries increasingly come to resemble the UK in this respect

The flip side of the decline in bank deposits is an increasing household dependence on risky assets (where capital values can go up or down) as a per cent of total financial assets. What is interesting is that this development happens against a background of increasing ownership of financial wealth in all these four countries. As the Europeans become richer in financial wealth they allocate significantly more of it to riskier financial assets. Without going into a technical debate on credit and market risk of financial instruments, we used a simpler definition of risk and put bank deposits and government bonds together, denoting them 'safe assets'. (Strictly, they might be termed *safer* assets because in the EU only the first €30,000 of bank deposits are legally protected and there is no explicit central bank commitment to bailing out failing banks, just as the market value of government bonds is sensitive to interest rates changes before maturity.) Equities, mutual funds and insurance products are included in the risky assets category because the principal can be expected to go up or down. Table 2 shows that in all four countries the share of risky financial assets in household portfolios has

increased significantly and now constitutes more than fifty percent of financial assets in all four countries. There is a revolutionary shift to risky assets in Italy between 1995 and 2000 and a significant one in France. Another interesting observation is in terms of the percentage share of total holdings, where French households align more with those in the UK, rather than their Italian or German counterparts, in holding risky assets.

Change 4: the importance of enduring national differences between direct and indirect ownership of capital market investments because direct ownership remains important in Italy and France, whereas intermediation is important in the UK and Germany

By 2000, a distinction between direct and indirect ownership of capital market investments seems more appropriate than the bank-based versus market-based distinction. On this basis, if intermediation of increasing investment in risky assets is the criterion, Italy and France form a separate group from Germany and the UK. Thus, the French hold their risky assets more directly through mutual funds, insurance policies and stocks whereas the British hold them indirectly through pension funds as part of a national system of funded provision under professional management which concentrates on investment in liquid giant firm stocks. This enduring difference reflects different supply-side evolution of financial markets, institutions and government policies and regulations within each country. There are also significant associated differences in household attitude to personal holdings of illiquid investments (British households are illiquid through institutional arrangements such as funded pensions). As Table 1 shows, the Italians and the French voluntarily hold a significant amount of unquoted shares which could not be easily converted into consumer expenditure in economic recession. Institutionalized saving, relevant group schemes and maybe individual trust in financial intermediaries are strong in Germany and the UK; whereas a capitalism of personal connection is alive and well in France and Italy where households are willing to hold non quoted shares.

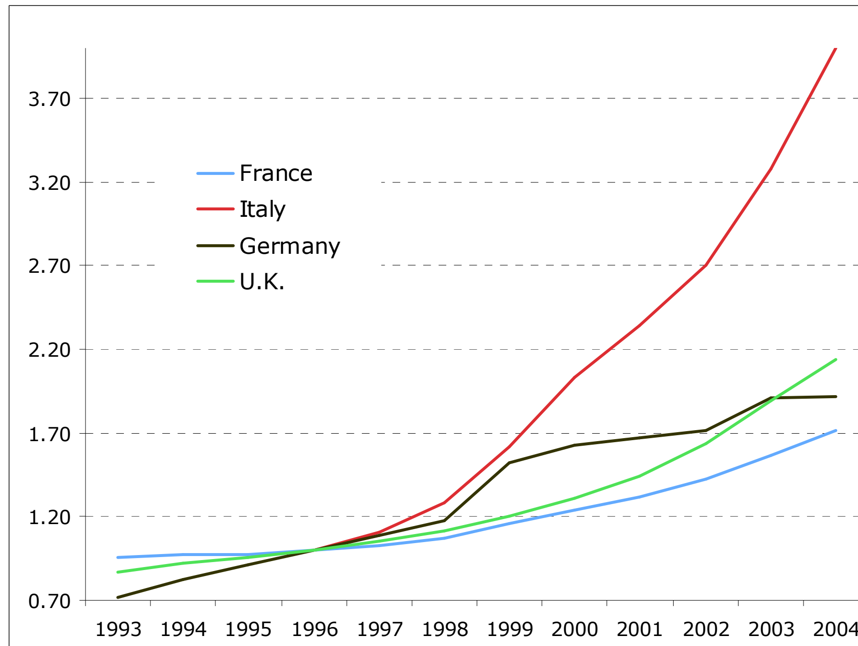
Change 5: if we consider both sides of the balance sheet, households have become more financialized in all four countries insofar as they have increased debt and accumulated more liabilities which offset their assets.

It is misleading to concentrate exclusively on the asset side of the household balance sheets because assets need to be considered in the context of liabilities. We cannot cover liabilities comprehensively but do need to make some basic points so that our story is not biased by its concentration on assets. In current public discussion, consumer debt is an issue in most European countries. Table 1 shows that the households in the four European countries use significantly more debt now than they did in 1980. It is important to note that Germany after reunification is more similar to the UK than to France and Italy when judged by this measure. An increase in financial wealth is accompanied by a greater increase in financial liabilities in countries like Italy and France between 1980 and 2003. The British have always had a significant level of liabilities (96.5% of GDP in 2003) but what is surprising perhaps is the higher levels of household liability in Germany. Unification and the inclusion of non-profit organisations in German statistics complicates the reading of the German figures but, at face value, household liabilities in Germany stood at 73% of GDP in 2003, double the Italian figure and almost one-third more than the French one. On the asset side, the Germans have the lowest ratio of financial assets to GDP (see Table 1), which can be described as unfinancialized Rhenish behaviour; but, if we consider liabilities as well as assets, the Germans are closer to the Anglo Saxons than to other continental European countries.

Increasing levels of household debt are correlated with soaring prices in the housing markets all over Europe (except maybe in Germany). This is relevant on the asset side because the official data on household wealth is biased towards financial assets. Data on real estate wealth is not as readily available. However, households seem to have included real estate in their portfolio of investments especially after the stock market crash of 2000 and banks seem to be very willing to extend loans to households for this purpose (see European Central Bank, 2003;

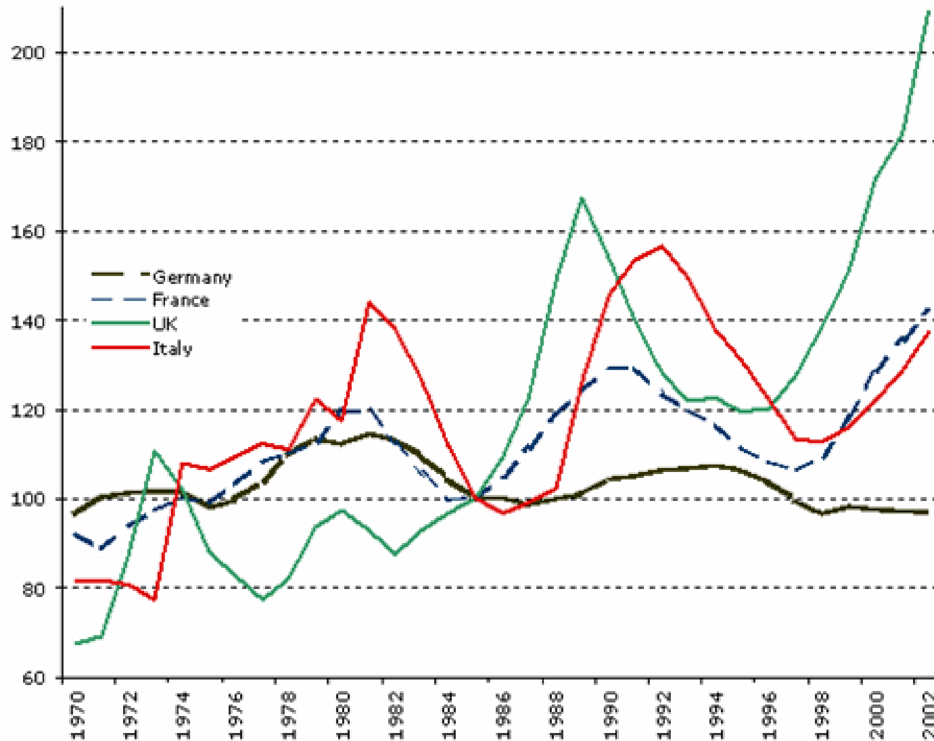
Borio and McGuire, 2004; Tsatsaronis and Zhu, 2004). Figures 3 and 4 illustrate these developments in the four countries that we examine. Higher levels of net financial assets do not necessarily make households immediately wealthier as most of these assets are illiquid, like insurance and pension funds, which put the British in the same boat as the French and the Germans. When wealth is illiquid access to debt becomes important. The French are the least liquid as they hold substantial amounts of unquoted shares, while the Italians are the most liquid as they hold less insurance and pension products but more bonds and mutual funds, shorter term investments which presumably reduce their need for debt.

Figure 3. ***Index of the value of house loans (1996=100)***



Sources: *Banca d'Italia, Banque de France, Deutsche Bundesbank, National Statistics Office of the U.K.*

Figure 4. ***Real residential property prices (1985=100)***



Source: Bank for International Settlement (2004)

Therefore the current dynamics of household finances across Europe are such that households are taking an asset and liability approach which includes real estate in the asset portfolio and should consider maturity and type of debt in the liabilities. More generally, with increased financialisation household wealth has become more sensitive to the movements in interest rates, stock markets and house prices as households are faced with ever more complicated financial calculations and decisions. Thus, in an ideal world of financialisation, households would be following the financial market news about interest rates and asset prices to estimate their debt burden and capital gains/losses, and this information would have serious implications for their current and future consumption decisions. Attanasio and Banks (2001) point out that the replacement of socialized pay-as-you-go (PAYG) systems by individual funded pensions would require households to be familiar with many savings products and to make complex financial calculations which greatly complicate any definition of life cycle income and saving. As Erturk *et al.* (2005) demonstrate, increasingly complex choices have already outrun the calculative capabilities of ordinary households. In response to concerns about the existing capabilities of citizens and the requirement for more individual decisions about financial products and services, including for security in retirement, national governments such as those in the US and UK and the OECD have recently embarked on initiatives to improve the level of financial literacy across society (OECD, 2004b; FSA 2004; Federal Reserve Board, 2004).

Varieties of (financialized) prudence

In this section, the narrative focus shifts from household assets to household behaviour as disclosed by the shifts in asset stocks. Here again we encounter complexity because the similarities and differences in household behaviour are difficult to categorize and consequences are not as easily predictable as a varieties of capitalism approach might suggest. For example, as pointed out above and as demonstrated in Table 2, Italian households have increased the share of risky financial assets in their portfolio more than the other countries in our sample between 1980 and 2003, with a three-fold increase in share from 22.2% to 66.2% of total assets. But, Italian households are the most prudent of all when it comes to the ratio of financial assets to debt (see Table 4): the financial assets of Italian households cover their liabilities 6.6 times whereas in the north of Europe the 'imprudent' Germans have a ratio of just 2.5. The Italians are also more liquid than other countries as they hold more bonds and mutual funds in their portfolios (see Table 3). Table 4 also shows that although the French households, as discussed above, participated in the financialisation process by increasing their ownership of risky financial wealth, they are the only nation that has actually become less risky in terms of leverage. The French ratio of financial assets to financial liabilities increased from 3.6 to 4.1 between 1980 and 2003. Naturally this ratio has much to do with the sensitivity of the value of financial assets to market price movements as the UK ratio before and after the market crash of 2000 demonstrates: for example, the British have 53% of their financial assets in market sensitive pension funds (see Table 3). But such observations nevertheless underline the unpredictability of outcomes under financialisation which, from this point of view, takes us further away from coherence.

Table 3. ***Share of financial assets in household portfolios (percentages)***

	ITALY					FRANCE				
	1980	**1987**	**1995**	**2000**	**2003**	**1980**	**1987**	**1995**	**2000**	**2003**
Deposits and cash	64.2	41.0	41.7	24.6	27.0	58.5	42.0	36.0	27.1	30.0
Bonds	17.2	32.2	27.4	18.4	22.1	9.1	7.4	6.4	2.2	2.4
Government bonds	13.6	29.2	22.9	6.9	6.8	n.a.	n.a.	0.4	0.2	0.2
Stocks	10.0	9.8	15.3	27.8	22.0	16.2	28.8	22.7	34.5	25.7
Quoted stocks	n.a.	n.a.	3.1	6.9	4.7	3.3	4.5	4.0	3.7	2.4
Mutual funds	0.0	5.7	4.1	16.6	12.3	2.2	10.3	11.3	8.7	8.6
Insurances and Pension funds	6.0	5.3	10.5	11.9	16.1	7.1	9.2	21.0	24.7	30.2
Other assets	2.6	5.9	1.0	0.7	0.5	6.9	2.3	2.5	2.7	3.2
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

	U.K.				GERMANY					
	1987	**1995**	**2000**	**2003**	**1980**	**1987**	**1993**	**1995**	**2000**	**2003**
Deposits and cash	29.8	24.0	20.3	27.0	52.4	47.2	45.0	41.8	34.0	35.7
Bonds	3.6	2.4	1.5	1.7	11.7	14.1	12.3	12.9	10.0	11.3
Government bonds	2.1	1.3	0.9	0.9	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Stocks	14.1	15.7	17.6	11.2	4.8	5.6	11.4	11.1	15.7	10.0
Quoted stocks	10.5	8.7	10.2	6.9	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Mutual funds	2.0	3.7	4.9	4.0	7.3	4.8	5.6	7.0	11.2	11.8
Insurances and Pension funds	46.3	50.8	53.1	53.1	16.6	20.3	24.8	26.1	27.9	29.6
Other assets	4.3	3.4	2.6	3.0	7.3	8.0	1.0	1.1	1.3	1.5
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Derived from Table 1.

Table 4. ***Ratio of household financial assets to debt***

	1980	1987	1995	2000	2003
France	3.6	3.4	3.9	4.7	4.1
Germany	10.4	11.5	2.4	2.4	2.5
Italy	13.4	15.3	7.8	7.9	6.6
U.K.	n.a.	3.1	3.7	4.3	2.8

Source: Derived from Table 1

Unpredictability and surprises can also be observed by considering the different reactions of households in various countries to the same major financial events. After the stock market crash of 2000, households in France, Italy and the UK reduced their ownership of mutual funds but German households, who hold the least financial assets, increased their holding of mutual funds (see Table 5). This increase could be due to the fact that mutual funds in Germany include relatively lower proportions of stock market investments and thus have a more limited exposure to share price falls, although there is no data at this level of detail which could confirm this hypothesis about mutual funds, which are by definition subject to capital market price uncertainty in one way or another. Even more interesting is the behaviour of Anglo-Saxon households which bought less equity on the upswing of the bull market and sold off less after the crash. During the bull market period of 1995 to 2000, the British households raised their investment in the stock market least, with an increase of 9.3 percent against 22 percent, 17.7 percent and 12.2 percent increases by the Italians, the French and the Germans respectively. Then, after the market crash of 2000, British households switched sharply to safe bank deposits: between 2000 and 2003, the switch to safe bank deposits and currency by the British was of a magnitude of 6.8 percentage points whereas the switch to safety in continental European countries was half this figure, at about 3 percentage points on average (see Table 2). This dramatic change in the UK is also influenced by the impact of the revaluation of financial assets after the stock market crash but so were the weights in other countries. Table 5 supports this observation and shows the difference is not an artefact produced by a concentration on percentage shares as bank deposits and currency per capita increased in the UK in the aftermath of the market crash more markedly than in the other countries.

Table 5. ***Real per capita growth rates (at 2003 prices and in percentages)***

	ITALY				FRANCE			
	1980-89	**1990-94**	**95-2000**	**2000-03**	**1980-90**	**1990-95**	**95-2000**	**2000-03**
Deposits and cash	1.2	1.4	-2.6	2.0	0.7	3.0	2.2	0.7
Bonds	17.8	5.0	-0.1	5.0	0.8	5.7	-12.4	-0.7
Government bonds	*18.6*	*0.6*	*-14.8*	*-1.8*	*n.a.*	*n.a.*	*n.a.*	*-2.9*
Stocks	7.7	2.0	22.0	-8.6	13.9	-5.0	17.7	-11.7
Quoted stocks	*n.a*	*n.a*	*27.1*	*-13.3*	*11.0*	*-3.2*	*6.8*	*-15.2*
Mutual funds	n.a	21.6	42.8	-10.7	26.7	-0.5	2.8	-3.1
Insurances and Pension funds	6.5	n.a	11.0	9.2	11.8	14.5	11.8	4.1
Other assets	n.a	n.a.	1.2	-10.6	-8.7	13.3	9.6	2.8
Total financial assets	7.8	3.7	8.2	-1.2	6.1	2.4	8.2	-2.6
Financial liabilities	*7.6*	*3.3*	*8.0*	*4.8*	*7.3*	*-1.6*	*4.1*	*2.2*
Net financial wealth	7.8	3.7	8.3	-5.9	5.5	4.0	9.5	-4.0
GDP	3.0	0.7	2.3	1.0	1.7	0.6	2.2	0.7

	U.K.				GERMANY			
	1987-90	**1990-95**	**95-2000**	**2000-03**	**1980-90**	**1993-95**	**95-2000**	**2000-03**
Deposits and cash	4.9	1.6	3.3	3.2	2.3	-0.8	0.4	2.6
Bonds	-11.1	8.0	-2.3	-0.9	8.3	5.6	-0.6	5.3
Government bonds	*-25.2*	*17.8*	*-1.4*	*-1.2*	*n.a.*	*n.a.*	*n.a.*	*n.a.*
Stocks	9.9	5.4	9.3	-11.0	7.3	1.7	12.2	-13.1
Quoted stocks	*n.a.*	*3.8*	*10.1*	*-9.8*	*n.a.*	*n.a.*	*n.a.*	*n.a.*
Mutual funds	6.2	19.6	12.5	-6.3	-1.4	15.3	14.9	2.6
Insurances and Pension funds	2.9	9.3	7.7	-2.6	6.9	5.6	6.0	2.9
Other assets	5.9	0.8	1.2	0.2	5.5	5.9	8.0	8.0
Total financial assets	4.3	6.4	6.8	-2.6	4.3	2.9	4.7	0.9
Financial liabilities	*7.5*	*1.1*	*3.7*	*5.8*	*3.6*	*5.6*	*3.9*	*-0.4*
Net financial wealth	2.7	8.9	7.9	-5.9	4.4	1.0	5.2	1.8
GDP	2.1	1.4	2.6	1.4	2.2	1.7	1.0	0.0

Sources: Banca d'Italia, Banca d'Italia (2005), Bank of England (2005), Banque de France, Banque de France (2005), Brandolini *et al.* (2004), Deutsche Bundesbank (2004a, 2004b), International Statistical Year Book (2004), INSEE, National Statistics Office of the U.K.

Notes: The table shows geometric averages**.**

Thus, there is at least a suspicion that households in the UK have developed more sophisticated behaviours in response to market signals, so that increases in asset prices encourage cashing out; this behaviour would need to be analysed in the context of higher levels of home ownership in the UK. Does the Anglo-Saxon model increase the uncertainty of wage income but offset labour market losses through wider availability of mortgages, which is expansionary in effect when prices in the housing market are rising strongly and interest rates are low? In seven OECD countries Barrell and Davis (2004) found that ease of access to bank credit and the housing equity withdrawal cause short run income elasticities to decline and short run wealth and interest rate elasticities to increase. Therefore wealth distribution and the aggregate demand from households in a financialized economy may be nowhere near as straightforward as most models of capitalism would predict.

Conclusion: 'eppur si muove'

This article aimed to move discussion of financialisation forwards by analysing household savings and asset portfolios. In doing so, it has highlighted an important aspect of financialisation as ongoing process by presenting evidence on how households in four European countries have over the past 25 years increased their level and sophistication of interaction with financial markets. On the whole, the empirics on European household assets and behaviour generally support those who have argued that financialisation has contradictory effects (especially in France and Germany). Thus, the French who voted to defend their social model in the EU constitution referendum hold almost exactly the same percentage of risky assets in their portfolio as the British. There are also added complexities arising from increasing levels of household debt and soaring prices in the housing market in most European countries that highlight economically significant dynamics which are outside the bank versus market opposition, as conventionally understood in the existing varieties of capitalism literature. Of course, the productive systems and household portfolio approaches are (or should be) complementary not alternative forms of understanding like Ptolemaic or Copernican accounts of the cosmos. But, we can use the evidence on changing household assets and behaviour to raise serious questions about the comparative static bias in some of the existing varieties of capitalism literature, where the preoccupation with firms, labour and financial institutions may have produced serious underestimates of the scope and pace of change in present day European capitalism.

The analysis in this paper represents a first attempt to discuss the idea of household capitalisms. The purpose is not to seek to identify a schema of types which represent individual countries or groups of countries, but instead to explore similarities and differences, as well as paradoxes and interesting findings. Such explorations are a necessary first step in understanding the variable extent to which households have become more financialized, where our expectation is that there is no unique measure of financialisation but rather a series of changes in assets, liabilities and net wealth that together help provide a complex picture of the dynamics of household behaviour and the outcomes in terms of changes in portfolios and risks. Such analysis is likely to identify distinct differences between countries in the nature and rate of change, but the preliminary analysis in this paper suggests that simple models of household capitalism, that for instance distinguish bank-based from other forms of savings, are unlikely to emerge. More research is clearly needed to explore such complexities and paradoxes further, but the findings in this paper suggest that this is a fruitful area for research. If financialisation is partly or mainly about creating new kinds of economic subject and behaviours, the analysis in this paper confirms that we should not neglect changes around the household.

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