PES

Europe: A Social Market Economy Not a Market Society

Manchester, 1st July 2008

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President
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The real economy should come first

Making Europe : (2000 & 2005)

"The most **competitive**, dynamic, **knowledge-**based economy in the World, creating **sustainable** economic growth, more and better **jobs** and with greater **social cohesion**".

March 2007

"**Energy- and Climate package**"

Social Market Economy – not a market society!

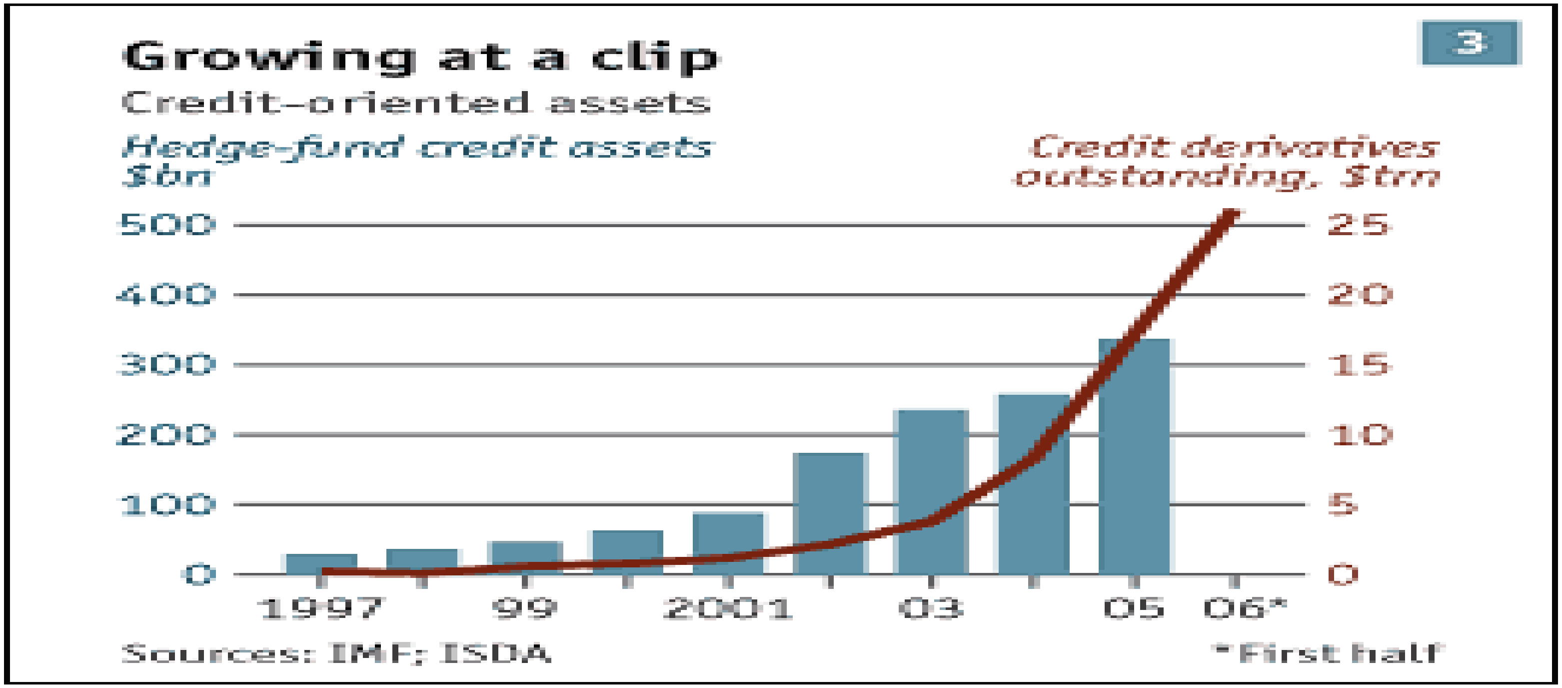
Long-term investment needs 2 trillion Euro

Who's subordinated to who?

We need well-functioning financial markets, but:

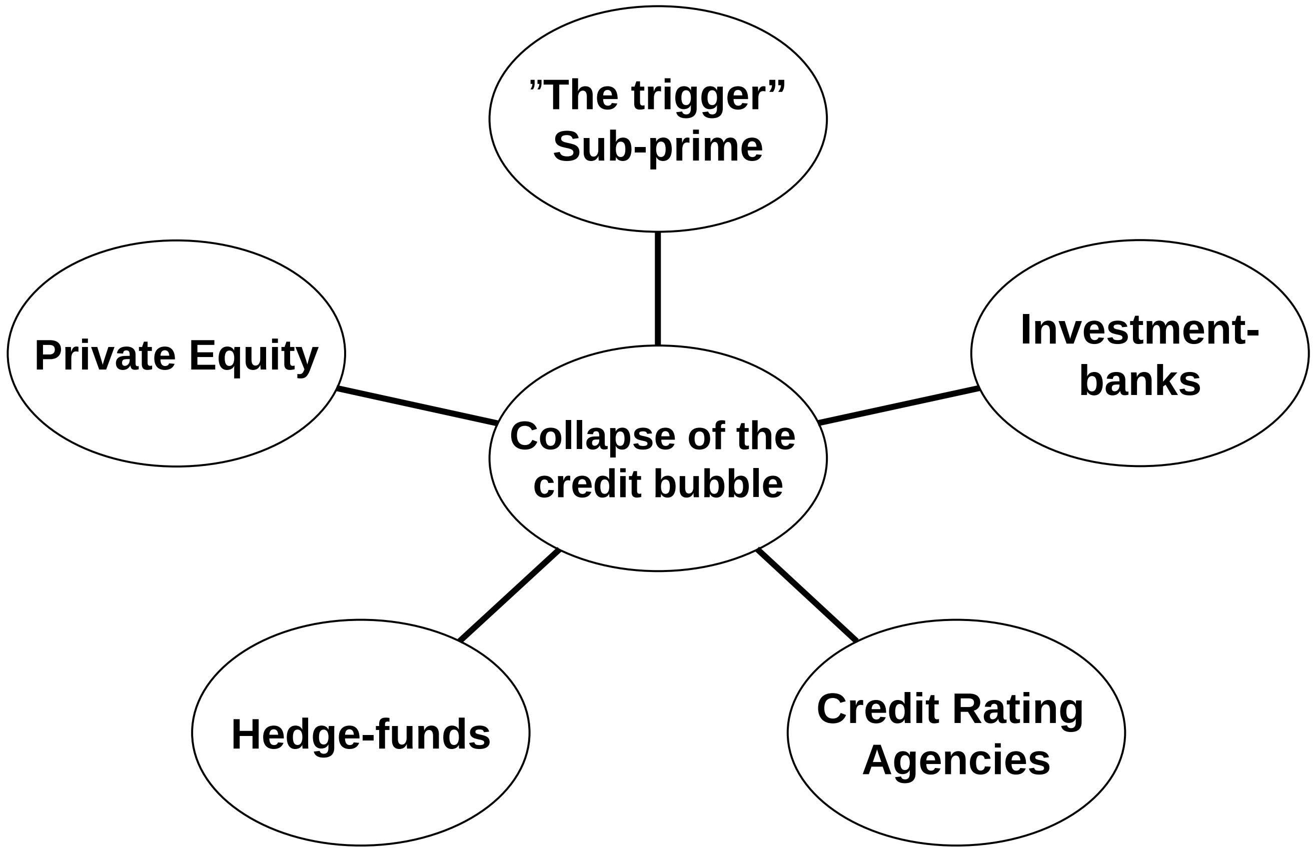
- **Cost efficient?**
- **Full transparency and disclosure?**
- **Prices vs. risks – ok? For all credit products?**
- **Financial Stability?**
- **Long-term financing?**
- **Level playing field? For all actors?**

Credit derivatives - "*Financial weapons of mass destruction*"



- 2007: Total volume of outstanding credit derivatives contracts stood at **$62,200bn**
- This is 10 times the level of four years ago !

The anatomy of the current crisis



IMF Global Stability Report (April 2008): "There was a collective failure to appreciate the extent of leverage taken on by a wide range of institutions […] and the associated risks of a disorderly unwinding"

The Big Transformation: 2002-2007

- Venture capital (only 5%)
- LBO's 60%
- No demonization
- But dominant

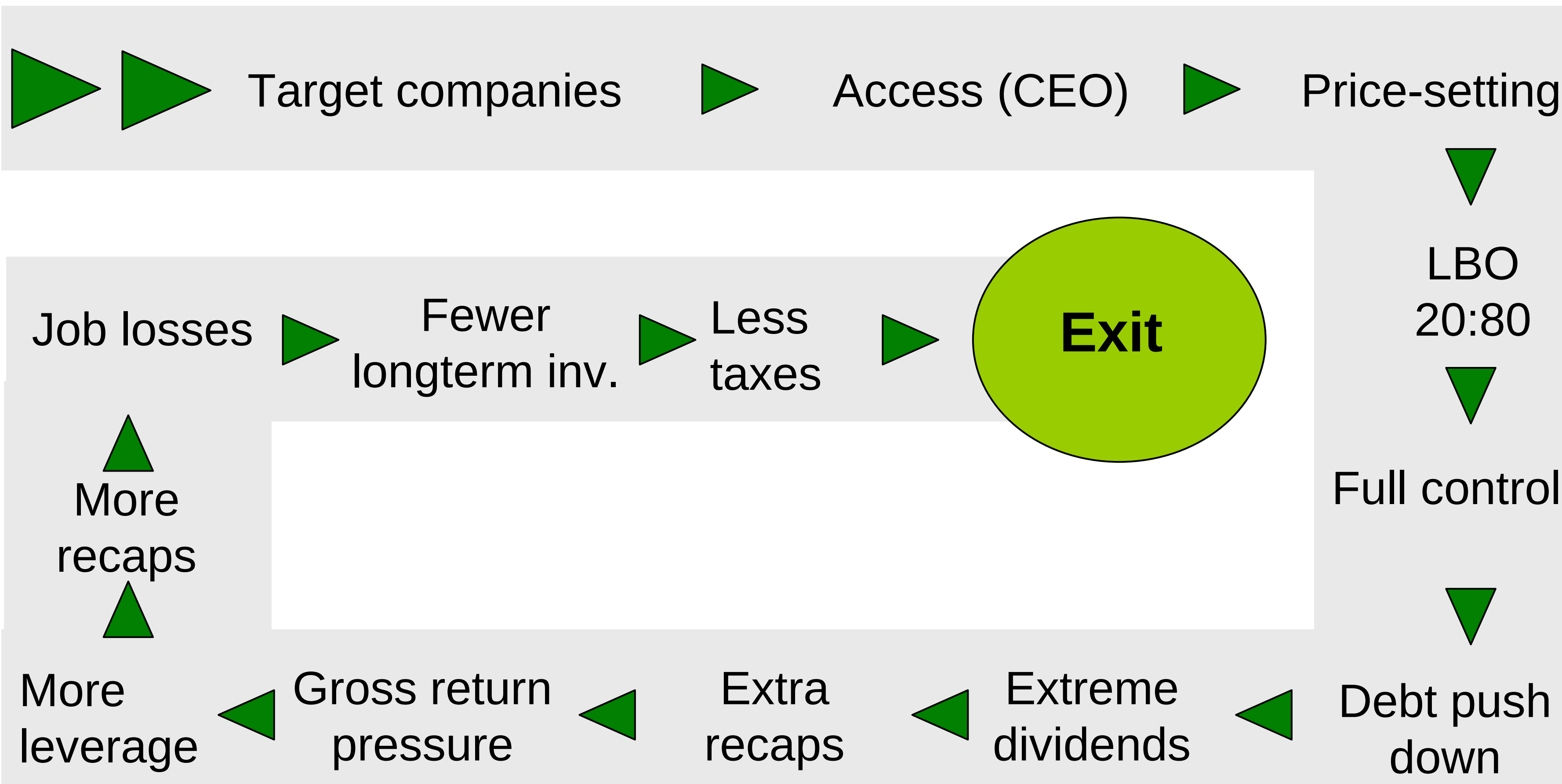
LBO's – New Employers

- **20 LBO's = 4 mio. workers**
- **5 big deals = Russia + India budget**
- **LBO 's Europe: ca. 2.000 mio. Euros**
- **LBO > IPO 2007**

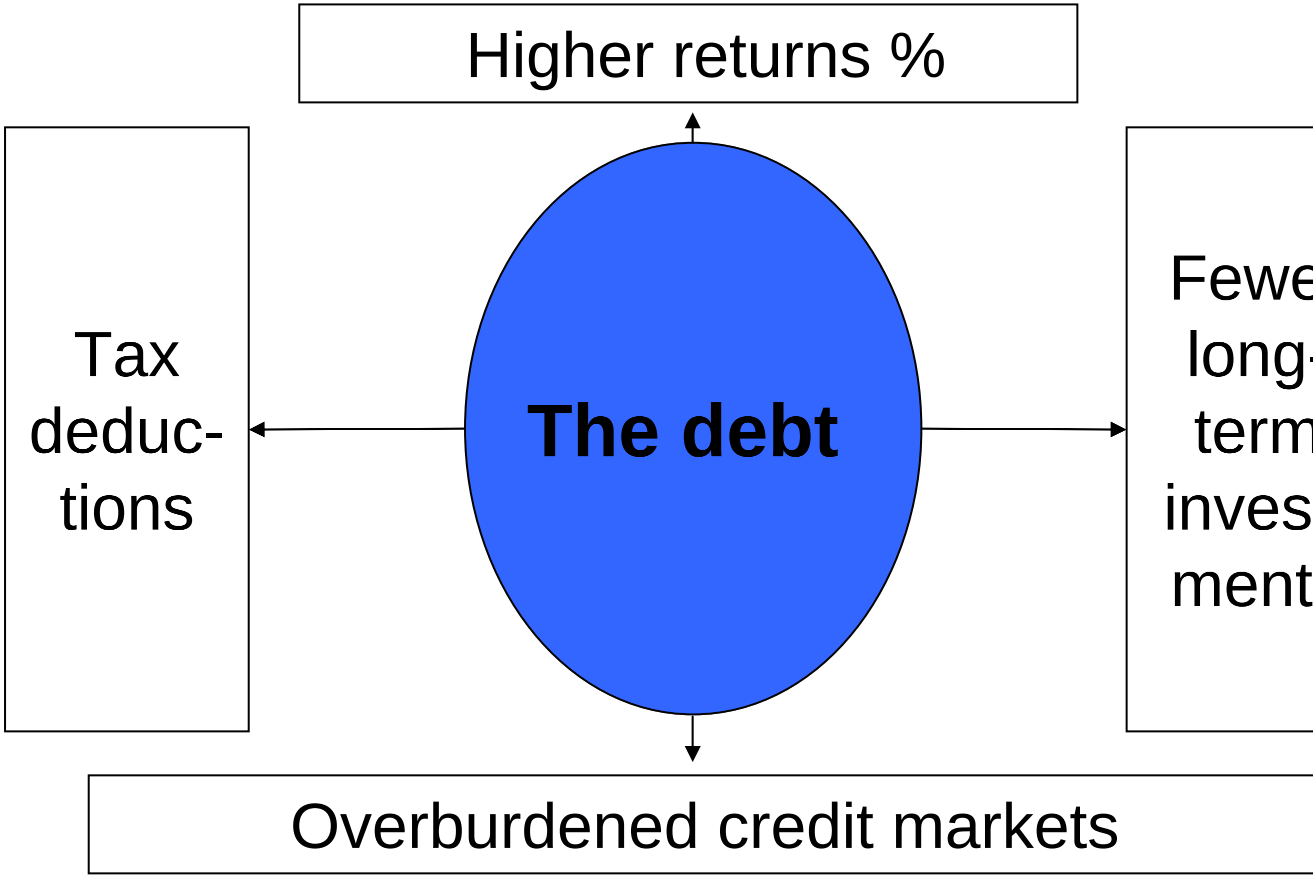
New global financial players

- **25+100+7+3 = 75%**
- **½ af global financial market**
- **Black box**
- **Financial bubbles and -crisis**
- **Short term returns**

LBO – the business model…



The debt is the key



IMF + SEC + ECB **: High risk of distressed companies**

And it continues..: S&P 6/08: ”**Lending standards continue to loosen**…”

Myth no. 1: Better performance?

Frederik Vinten, *CBS (2007):* *“The Performance of Private Equity Fund Owned Firms”*

“M*ain finding is that PE buyout fund ownership has a <u>significant negative effect on firm performance</u> relatively to similar firms. […] Post-buyout ownership concentration falls and debt does not lead to efficiency improvements.*

Myth no. 2: More jobs?

World Economic Forum, Davos (2008):

- *Workplaces taken over by PE have 7% fewer employees after 3 years and 10.3 % less 5 years following the takeover than in the control group.*

- *Companies taken over by private equity have higher rates of closure, opening, acquisition, and disposal of workplaces.*

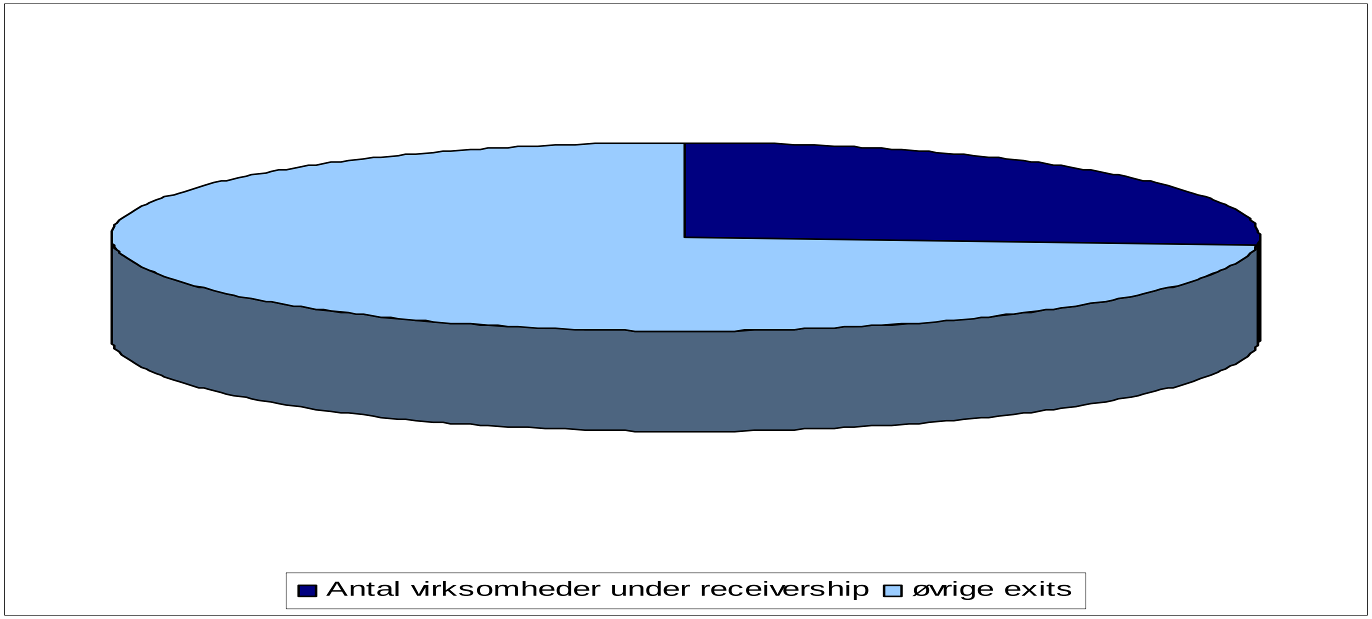
Myth no. 3: Better returns than others ?

Ludovic Phalippou & Maurizio Zollo *University of Amsterdam*: ”Net returns - adjusted for management fees and methodological errors – **3,8%** below the stock

The world’s largest pension fund CalPERS: Picking the winners? Since 1990 invested in 257 funds – 107 has given a negative return!

After the Exit: distressed companies

University of Nottingham/Barclay's Private Equity



<u>UK data</u>: More than a **quarter** of the (106 out of 400) companies disposed of by private equity in 2007 went into bankruptcy

What to do?
PES – New Financial Network

THE CHALLENGES:

- Re-linking financial markets to investments in the real, productive economy
- Emphasising quality of savings, e.g. to help those trying to safeguard their pension savings rather than making high profits quickly
- Examining commodity market repercussions (food, fuel price spikes, etc)
- Inequitable income distribution consequences of financial deregulation
- Corporate governance and workers' rights issues

What to do?
First steps in the EP

- **Financial stability, capital and Universal Regulatory coverage** (capital requirements, EU CRA, liquidity, valuation).
- **Transparency** measures (registration, prime brokers, protection of employees)
- **Excessive debt** measures (leverage, capital depletion)
- **Conflict of interest** measures (chinese walls, Investment banks, CRA's, market concentration)
- **Corporate governance and workers' rights issues**

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Who should do it?

	EU	US/JAPAN/GLOBAL
	• Transparency • Excessive debt • Conflict of interest • Capital requirements • Systemic risks/supervision • Corporate governance/Worker’s rights • Tax	• Capital Requirements • Transparency • Conflict of interest • Supervision • Tax

It’s about changing behaviour

Legislators
Labour market

Pension funds
Trade Unions

Financial market industry
(incl. PE & HF)

Way out of the dilemma!