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MONDAY VIEW: Levy on financial deals threatens Europe growth

By Simon Lewis, Chief Executive Of The Association For Financial Markets In Europe

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The idea of a global tax on financial transactions was first proposed nearly 40 years ago by the late economist Professor James Tobin.

With good reason, the proposal has never been taken up. But it has recently returned to the European agenda as politicians and regulators consider how to shore up budget deficits and stabilise financial markets.

Earlier this year, the European Parliament voted in favour of a financial transaction tax (FTT), adding momentum to the European Commission's work on a Europe-wide levy of, potentially, 0.01pc to 0.05pc on financial transactions.

Making a point: Nicolas Sarkozy and Angela Merkel try to get their views across

Then last week, there was a flurry of further interest, stirred up following the Franco-German summit when Angela Merkel and Nicolas Sarkozy held their crisis talks.

The market reaction to the proposed FTT has been negative.

Unsurprisingly, this tax is not just seen as bad news for banks and other financial companies, but crucially it is seen as being bad for business overall in Europe and likely to reduce economic growth, failing to meet the proponents' objectives.

The real impact of a financial transaction tax is still not widely or fully understood.

The impact on the 'real economy' – especially manufacturers and exporters – could be severe.

Many financial transactions are carried out not as speculation for its own sake, but on behalf of businesses that would be forced to bear the extra costs of the tax.

Take foreign exchange, which underpins international trade. A tax on currency trades would increase costs for a large section of industry in the UK and across Europe.

Furthermore, there is real concern that the European Union could proceed unilaterally, without ensuring that competitive financial centres, particularly in the US and Asia, follow suit.

The risk to Europe and the UK is threefold: A loss of competitiveness for our companies trading internationally; putting our banks and financial firms at a disadvantage; and Europe's financial centres struggling to compete in a tough global market where narrow margins count. A seemingly small tax rate, designed to raise billions, can end up having a serious impact on customer costs.

And of course, nowhere will the impact be felt more than in London, the world's leading centre for foreign exchange trading, accounting for 37pc of global foreign exchange turnover last year.

It is these factors which led the President of the European Central Bank, Jean-Claude Trichet, to warn the European Parliament recently: 'Let us be sure we don't do something we might regret one day . . . If certain transactions are considerably more costly in Europe than in other parts of the world, they will be done overseas.'

The main result of introducing the FTT would not be to drive out destabilising capital flows, as some may argue. It would be to push up costs for Europe's firms and push essential business transactions overseas.

The European Commission has made clear its intention and plans to publish proposals this autumn for a European FTT.

What is also needed is a thorough analysis of the full economic impact of any proposal, and the Commission is committed to publishing such an assessment shortly.

We must also study the past carefully, and the few instances where an FTT has been adopted. Lessons can be learned from Sweden, which imposed a financial transaction tax in the 1980s and saw stock trading leave Stockholm for other financial centres, as well as witnessing a sharp drop in trading volume for Swedish government bills. Sweden then abolished the taxes.

A central point in this discussion must be around the proper role of Europe's financial sector.

The industry is already one of the largest contributors of tax revenues – and a major source of jobs and trade, which should not be taken for granted.

But what matters above all is the overall impact on competitiveness, jobs and future economic growth in Europe and the UK.

That is what is really at stake in this tax debate.

People:
Nicolas Sarkozy
Places:
Stockholm,
London,
United Kingdom,
Europe,
Asia
Organisations:
European Central Bank

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