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FROM MARKET TO TRANSITION ECONOMICS: THE INSTITUTIONAL ROAD TO ECOLOGICAL ECONOMICS

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➔**Purpose:** Offering a few principles for a possible transition of capitalist market economies to sustainable ecological economies.

➔**Methodology:** Drawing upon the *Institutionalist tradition and focusing on the financial dynamics of economic evolution that leads to disaster and prevents any structural and durable change.*

➔**Plan of work:**

- ➔1st section: **Special focus on financialization:** one of the main concerns that shapes the functioning of the economy in a wrong and harmful direction. Financialization of the last four decades exacerbates the ecological, economic and social degradation of the sources and resources of life on earth.

- ➔2nd section: A relevant alternative approach is related to the identification of common objectives according to a common order (coordination) and to the organization of collective action (cooperation). The structural transformation of the economy that seeks a sustainable future is a **twofold issue** lying both in **climate change** concerns and **financial instability.**
  - ➔Regulatory framework must be designed to allow the financial system to support the eco-transition process in the long run.

➔Definitions:

Capitalist market economy: a specific organization of life and people that is built on the rule of the primacy of the person over society, the latter being assumed to be an arithmetical result of the former.

- Mainly relying on decentralized (no central plan) private individual decisions and actions;
- Decisions and actions seeking private wealth accumulation without taking into account or being aware of the consequences of these actions on the rest of society and on future generations;
- Time horizon and the assessment scope of private decisions are limited to the peculiar individual horizon of decision-takers and stockholders that are relying on their own limited perspective (plans, knowledge, information, means, goals).

Ecological economics: any economy that is organized according to a few collective rules such as no polluting, no environment harming economic activities, supported by durable and long-term financing mechanisms.

- Those rules are directed towards a common goal, the preservation and improvement of live on Earth.

- **Motivation:**

  1. Ineffective actions taken by institutions and markets over the last decades with regard to the environment and development issues.

  2. Compulsory measures that should have been implemented many decades ago are postponed in the name of economic efficiency and political stability.

  3. **The Doomsday Clock** is set at 90 seconds to midnight as the planet is at a crossroads, between a point of no return if radical measures are not taken immediately, and an opportunity to change our destiny towards a possible sustainable future: "*The Clock can move away from midnight. As we wrote last year, "In this time of unprecedented global danger, concerted action is required, and every second counts.*"" (Mecklin, 2024).

     Yet, such a warning had already been issued five decades earlier: "*Science and technology, as part of their contribution to economic and social development, must be applied to the identification, avoidance and control of environmental risks and the solution of environmental problems and for the common good of mankind.*" (*Stockholm Declaration*, United Nations,1973).

I. Financialization as a source of mass destruction

- World-wide economic **liberalization** of the 1980s supported by a massive withdrawal of public-hand regulation from the economy.

- Through radical institutional changes, public regulation and collective action mechanisms were reduced to their (im)possible minimum level and governance of the economy was left to **self-regulation rules**.
- Market-led self-regulation and loose public supervision replaced tight and restrictive regulation.

- This institutional evolution allowed many various financial innovations that led market players to drastically multiply the number, the quantity and the variety of products, processes and operations in financial markets, affecting performance and efficiency of the banking sector both at individual and holding levels (Stiroh, 2000).

I. Financialization as a source of mass destruction (continued)

- The so-called **Schumpeterian innovation dynamics** was used as a theoretical reference to champion the optimality of **self-regulated financial innovations** and the retreat of the public hand from market regulation (Barredo et al. 2022).

  ! Market strategies became closely relying on **short-sighted return-on-investment criterion**, increasing the role of financial institutions and financial efficiency criteria in the functioning of economies.

- These innovations contributed to the transformation of the economy into a **global financial gambling arena**, relying much more on rapid returns on investments without no direct effective link to the industrial content and societal objectives that would underpin such activities.

- The *"New Economy"* of the late 20th century and the early 21st century: "*The New Financialized Economy*", mainly driven by financial aims and criteria, moreover supported by governments and institutions.

The main criterion of financialization

➔ **Financialization** exacerbates the "return only" rule in the behavior of economic agents as the core financial efficiency criterion enters in direct opposition with any other social and societal efficiency criterion that would be focusing on the "good for life" (and not on the "good for me").

➔ The performance of economic activities is usually measured in terms of net gains that the activity can generate for the owners and stockholders (The rule of "*Après moi, le déluge - After me, the flood*").

➔ Financialization is a process only aimed at ensuring capital accumulation that does not (cannot) take into account the public/common goods like the preservation and improvement of life on Earth.

➔ Such **common goods are global, holistic concerns while the capital accumulation is the source of private wealth**.

! The bridge between private wealth and public wealth is not a invisible bridge that could be brought forth thanks to free market mechanisms.

The main criterion of financialization (continued)

- As the performance in financial investments is the capacity of an investment to provide the investors with higher and rapid returns, when the financing of enterprises is relying on financial investors' willingness, the speed and the amount of net returns become the main rule to assess the quality of economic commitments.

  With the liberalization process, **the financial operations gain ground** and constitute a major field of battle in economic strategies.

- Therefore, the **decision of financial actors** as well as the behavior of corporations converge **toward the financial efficiency criterion**.

  In such an environment, economic, political and social decisions are related to financial efficiency criterion that was supported by the financial market efficiency hypothesis and then, by the public intervention inefficiency hypothesis.

- However, the positive results asserted to support financial markets liberalization are not there and **financial innovations often provoke huge instabilities** without enhancing real innovations and economic growth.

- On the contrary, many works argue that **financial sector would hurt innovation** and **innovation-led growth** (Xiaoyang, Asimakopoulos, and Jaebeom, 2020) since the credit expansion, related to financial innovations, may have harmful effects on resource allocation, both on physical and human capital (Cecchetti and Kharroubi, 2015, Borio et al., 2016).

De-institutionalization VS institutional revolution

- This private-interest-led regime relied on ***de-institutionalization* of governance structures** (regulation, supervision and incentivization of markets) and led to the 2007-08 financial crisis.

  The overall evolution of societies then took an unsustainable path regarding environmental, ecological and social issues. Environmental and resources depletion and hysteresis of inequalities are some of the consequences of this episode.

- So, in the face of growing instabilities and insustainabilities, the necessary **transition** of the market economy **to a viable society** calls for an **institutional revolution** that would offer **an alternative organization of economic and social dynamics in favor of collective action**, apt to make private actors' behavior consistent with societal coherence.

Such a process requires radical institutional change, which could provide the right environment to break out of the financialization of economies and help shape the behavior of individuals and markets in line with sustainability goals.

A relevant regulatory alternative requires the identification of common objectives according to a common order (coordination) and to the organization of collective action (cooperation).

Climate change *and* ***financial stability*** *are the two major concerns that should be considered in a new regulatory framework to be built on smooth coordination/cooperation mechanisms for an effective eco-transition process.*

II. Climate change, financial stability and new regulation

- Any proposal aimed at providing an appropriate collective action schema for a sustainable provision of eco-transition and its financing is obviously linked to a specific regulatory framework that is consistent with the features of the public/common good.

The core issue is then to know **what room is there for a systemic regulation** that might be relying on an efficient flexible supervision process that could deal with the complexity of the global eco-transition.

- **The structural transformation of the economy that seeks a sustainable future is a twofold issue lying both in climate change concerns and financial instability since any regulatory framework must be designed to allow the financial system to support the eco-transition process in the long run**.

Two major questions can then be put forward:

- Climate change (environment and energy transition process) and
- Financial stability (financial regulation and financing of the transition process).

- In a monetary capitalist society, these two questions are interconnected; they both form the "**eco-transition**" as a **process of radical change of the societal infrastructure** (Ülgen and Klapkiv, 2023), given by an appropriate financial organization of sustainable economic activities according to the goals of societal evolution at the global level (the Sustainable Development Goals, SDGs).

A global question

- So the lack of a global institutional infrastructure is in total opposition to the specific features of the most critical issue of all time, namely a possible and dignified future. For instance, United Nations' ***Sustainable Blue Economy Finance Principles*** (https://www.unepfi.org/blue-finance/the-principles/), launched in 2018, is a specific initiative that seeks to provide a guiding framework for banks, insurers and investors to finance a sustainable blue economy. Financial Institutions are expected to provide the financing, investment and insurance required to power ocean-linked sectors.

- Lack of information, lack of certainty and vested-interest campaigns, among others, can pollute the democratic debate and prevent citizens from being committed in collective action.

A global question is underlying today's difficulties at the international level:

What solutions could be imagined in a sustainable and feasible manner to deal with the major systemic problems that are endogenously generated by our economic system's dynamics?

- More accurately, the COP 29 in Baku in November 2024 points out the criticalness of the way we could build up sustainable financial support for the eco-transition.

Concerns related to the "Collective Action"

- A second critical issue: When the problem is system wide and goes beyond the cognitive ability of (limited) groups of people, deep reflections on an alternative "**Collective Action**" framework, i.e. public-handed global governance and regulation, become compulsory.

So, **eco-transition and its financing prove to be critical public goods since they concern "global" society and its viability conditions beyond individuals, communities, and nations**.

- Although decentralized regulation mechanisms may contribute to the efficiency of the transition process, a general framework for the organization, management and supervision of the provision of financial stability and eco-transition as global public goods fall under the responsibility and competence of public governance mechanisms (Ülgen, 2025).

A large variety of (potential and effective) risks may come into picture and require special attention.

- These risks may take the form of climate risks that are transition risks and physical risks. The former are related to policy and regulation, technology changes, consumer preferences, while the latter are related, for instance, to global warming, floods, precipitations, drought, wildfires, etc. affecting agriculture and environment.
- On the other side, financial risks can come from credit risks, market risks, underwriting/insurance market risks, operational risks, and liquidity risks (ECB, 2020).
- Climate risks and financial risks are closely related to each other not only because of the consequences of environmental concerns for economic activities but also because of constraints that the new rules and obligations that could reshape the private actors' strategies.

Feasibility and stability as conditions

- To prevent any **eco-transition related Minsky moment** and to ensure a smooth long-term reform process, **supervision of the financing mechanisms** must be designed and implemented at the global level in the same way than a consistent macroprudential approach to financial regulation must be organized from a holistic perspective (Almawi and Ülgen, 2024).

- The smooth working of monetary and financial systems is essential for a well-functioning and viable economy, just as a healthy natural and social environment is a prerequisite for a sustainable future.

  In other words, **the feasibility and stability of the eco-transition process and the stability of financial markets are the two sides of the same coin and must be handled at the global level within a macro-regulatory framework.**

- Such a framework has a twofold objective that is preventing recurrent systemic financial crises and dealing with climate change issues (NGFS, 2021).

- Long-lasting discussions around the net-zero goals, ESG models of corporations and the control over the global warming at 1.5-3°C cannot result in effective decisions and actions without building up a global regulatory framework that could give the common direction toward a common good.

Conclusion

Two points of attention:

→ The necessity of concerted action

→ The search for the common good to design and implement a relevant eco-transition process.

- ✓ The transition process is a global economic, energy, environment, and society transformation and then requires a **holistic approach** and **collective action**.
- ✓ The organization and management of such a framework must be regarded as a process of provision of **global public goods**.
- ✓ This process has also to provide answers to **a fundamental social dilemma** that is the opposition between private interest (and micro-rationality and market efficiency) and public interest (common good, macro-stability, society viability).
- ✓ For a smooth transition process against potential financial instabilities, it is necessary to **decouple eco-transition financing** and **market's financial efficiency criteria** in transition funding.
- ✓ This calls for **a new global regulatory framework** to treat climate change and financial stability as linked global issues, the response to which will determine our ability to survive (or not) the adverse consequences of our model of economic and societal organization.