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Against (the idea of) financial markets

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ABSTRACT

The difference between bank-based and market-based financial systems is a longstanding and influential conceptual staple of the interdisciplinary literature on finance. This dualistic model has been subjected to wide-ranging critiques over the past decade. Yet, while those critiques productively problematize the relationship between banks and markets presumed by the model, they fail to address the underlying distinction between banks and markets that is also presumed by the model. This article questions that distinction. It argues that financial markets are best understood not as places or platforms where banks and other financial actors come to interact – and thus as essentially separate from banks – but, instead, as, in large part, their interaction; as constituted by it. The article further argues for the political as well as scholarly importance of reconfiguring our ideas of what financial markets are. The idea of markets as separate, reified phenomena not only underpins the scholarly model of bank- and market-based financial systems – it does political work in the wider world, with the appeal to financial markets or, more nebulously, "the market" to rationalize and justify political decision-making having become a commonplace of contemporary public policy discourse.

1. Introduction

A conceptual mainstay of the vast interdisciplinary literature on finance has long been the basic distinction between bank-based and market-based financial systems. In a stylized bank-based system, banks represent the primary conduits and directors of financial flows. Corporations secure financing from banks; and those banks play the dominant role in aggregating savings, allocating capital, and managing financial risk. In a market-based system, banks are much less prominent, although not absent. Financial markets, rather than banks, are the principal sources of financing for corporations and serve as society's main vehicles of capital allocation and financial risk management. In the literature in question, these two alternative models are commonly used to describe and classify the financial systems of different countries.

During the past decade, a variety of criticisms have been levelled at this dualistic figuring of financial systems (e.g. Adrian and Shin, 2010; Allen et al., 2004; Hardie et al., 2013; Song and Thakor, 2010). This article seeks to deepen and extend this critique. It does so by problematizing a distinction that the existing critique has failed adequately to question, but which is nonetheless fundamental to the bank-based versus market-based dualism. This is the underlying, prior distinction between banks and markets per se.

At the heart of the differentiation between bank-based and market-based financial systems is the premise that banks and markets belong to different orders of things – that they are ontologically distinguishable. On the one hand there are things called markets; on the other hand there are banks (or, more generally, financial institutions). To be sure, the two can and do interrelate: banks and other financial institutions are said to be active *in* financial markets, alongside other economic actors. But, the very notion that one (the bank) can operate in or on the other (the market) implies separability and difference. Indeed, if banks and markets were *not* essentially different things, then it would be pointless to categorize financial systems on the singular basis of the distinction between them.

The article suggests that this distinction relies on and reproduces a problematic notion of what financial markets are and of what happens in them, and it argues for an alternative figuring of markets, particularly vis-à-vis their relations with banks and other financial institutions. In the literature on financial systems, and in most critical readings of it, markets are depicted as sites where competitive and chiefly anonymous economic transactions occur. But it is misleading to think of financial markets this way. First, even in nominally market-based financial systems, banks and other financial institutions frequently wield substantial influence, manifesting inter alia as power over and hence the capacity to "move" the very markets whose prominence – according to the stylized model – ostensibly obviates systemic bank promi-

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nence. Such markets are seldom anonymous or perfectly competitive; they are more often institutionally concentrated and hierarchical. Second, and more importantly, this depiction of markets – as sites for transacting – sets those markets apart ontologically: it gives them a reality and vitality of their own, including a purported capacity to "discipline" (Lane, 1993) the financial institutions that come to them, from elsewhere, to engage. The article suggests that financial markets are more accurately and productively figured not so much as the (separable) location or context for the interaction of such institutions (and others), but *as*, in large measure, such interaction.

This is not meant to suggest that the concentrated nature of the banking sector is not already widely recognized. It clearly is, both in scholarship and in public policy discourse. The post-financial crisis regulatory and scholarly debates about "too big to fail" (TBTF) financial institutions are exemplars of such recognition. Yet, crucially, such debates invariably posit TBTF *as and only as a banking problem,* and not (also) as a financial-market problem; markets are bracketed out and left largely unquestioned. Similarly, post-crisis debates about financial markets typically bracket out banking in turn. The prime example of this has been economists turning their guns, belatedly, on the "efficient market hypothesis" (EMH), which asserted that financial markets always correctly price assets given the available information. In now dismissing this hypothesis, economists have appealed to behavioral finance and its critique of traditional assumptions about the small, anonymous investors of market lore, who, it transpires, "bear little resemblance to the cool calculators of efficient-market theory: they're all too subject to herd behavior, to bouts of irrational exuberance and unwarranted panic"; and who, even when trying "to base their decisions on cool calculation often find that they can't, that problems of trust, credibility and limited collateral force them to run with the herd" (Krugman, 2009). In other words, just as TBTF is conceived as a banking problem unrelated to financial markets, financial market inefficiency seemingly had nothing to do with banks.

These post-crisis debates, in short, both reflect and reinforce the tenuous but deeply-entrenched distinction between markets and banks. The particular contribution of the present article lies not in diagnosing the concentrated nature of the banking sector, but in insisting that structural banking-sector issues such as concentration are at once structural financial-market issues, and vice versa: institutional concentration is a feature of financial markets, just as it is of financial *services* markets (Christophers, 2013).

That the figurative separation of banks and markets characterizes not only academic convention but public policy discourses such as that relating to TBTF banks, meanwhile, underscores a central reason for critiquing that separation in the first place. As well as being analytically misleading, the idea of "the market" as being somehow detached and distinct from the banking and other financial institutions that dominate it *has power* insofar as this abstracted ideational market does political work in the world. Specifically, the increasing tendency for "the market" or (financial) markets to be invoked as the ultimate arbiter of public policy is among the most striking politico-discursive developments of recent times. When governments contemplate policy interventions they openly wonder and predict how the market will respond. Similarly, once decisions have been taken, the markets' reaction is viewed as a measure of the wisdom of the chosen course; sometimes markets "cheer" such decisions while on other occasions, more ominously, the market gives a "thumbs down." More generally, the market's judgement – real or anticipated – steers policymakers in certain directions and threatens to punish them when they veer off-course. This phenomenon exemplifies the wider "logic" of market-based justification and rationalization of social action and worth elucidated by Boltanski and Thévenot (2006), the logic of the "market world" representing, in their schema, one of six principal such logics. This particular logic, as Taylor (2004: 6) avers, has come to assume an almost spiritual quality; "omniscient, omnipotent, and omnipresent," the market, Taylor claims, "has become God."

The positioning of the market as touchstone of policy suitability is problematic in at least two senses. First, there is the simple question of the grounds for policy appraisal. The more the financial markets become the arbiter of political sense and possibility, the more it is the case that what the state elects to do is based not on, say, democratic acceptability, or utilitarian considerations, or even on what is considered "right" and just, but on financial terms. The second problem relates to accountability. When the market is the yardstick for evaluation of public policy, such evaluation becomes unattributable and, therefore, unaccountable. Instead of a definable and broadly "locatable" socio-spatial constituency – the "American public," or the United Nations, or foreign governments – serving, willingly/wittingly or otherwise, as source of political legitimation, such legitimation is tied to an amorphous "market" notable precisely for being socially and spatially *un*moored, characterized as that market putatively is by "an invisible hand that works through self-interested, dispersed participants who adjust their choices to price signals" (Knorr Cetina, 2012: 115). Rhetorical referencing of "the market" ultimately conjures an accountability black-hole. With the buck being metaphorically passed to an all-powerful, but never tangible, political–financial master, it becomes impossible to determine *who* is adjudicating on public policy, or, therefore, to call them to account.

To the degree that the market appealed to in this public policy discourse is ever specified, it tends to be the (sovereign) bond and foreign exchange markets – such markets determining the value and viability of sovereign debt and currency – or the stock market – stock prices having become something of a general barometer for the economic future. The post-crisis period, as well as featuring debate around (separate) banking (TBTF) and market (EMH) issues, has of course seen an intensification of the discourse of market arbitration. Numerous governments have justified austerity policies with the explicit rationale that "the market" would exact retribution (i.e. downgrading sovereign debt) were a contrary course of action pursued. While this discourse warrants unpacking on several grounds – it is, for example, overtly gendered, commentators routinely seeing fit "to ask Mr. Market what he thinks of all this" (Peston, 2014) – it is the imputation of agency to (reified, godlike) markets that is of central interest here. Markets come to appear, in Langley's (2014: 68) words, as "a known thing or object," regarded even by practitioners "as independent and external to them, as having an agency and 'life of their own'." In the process, the agency of those who participate *in* markets is actively veiled. The discourse of "Mr. Market" gives no sense, in particular, that major financial institutions feature in market dynamics, still less that they frequently play a dominant role.

All of this may seem to take us a considerable distance from the academic market-versus-bank distinction that underwrites the categorical duality of market-based and bank-based financial systems, and that this article aims to deconstruct. On the one hand we have public policy discourse; on the other, a scholarly model. The academic distinction between markets and banks does not necessarily underwrite or actively figure in the public discourse that reifies the market and obscures banks. It would clearly be fanciful to imagine, therefore, that deconstruction of the academic distinction can directly contribute to challenging the reified market of contemporary governance and the problematic political work that this discursive construct performs. Yet, neither is it certain that the scholarly model and the policy discourse are entirely disconnected, or will necessarily remain so. Dismantling the academic distinction likely will not disturb the caricatured market of political rhetoric;