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A world where transactions rule

Book review

John Plender examines a very European critique of a process of 'financialisation' that has sown distrust and damaged co-operation, creativity and loyalty

Two years ago, a book that launched an out-and-out assault on the financialisation of the economy and of society would have encountered a high degree of incomprehension in the English-speaking countries where the capital market-based model of capitalism holds sway. Today, Paul Dembinski, a University of Fribourg academic and director of the Geneva-based think-tank Observatoire de la Finance, can safely declare that finance wreaks socio-economic havoc without fear of blanket dismissal. The financial debacle that began in August 2007 clearly calls for a fundamental rethink of the role of finance, and this book is a provocative, very continental European place to embark on that journey.

The nub of Mr Dembinski's thesis is that financialisation has become predominant through the economy-wide replacement of relationships with transactions. This process creates distrust, generates supervision costs and

makes co-operation, creativity and long-term commitment almost impossible. It is also inimical to the notion of the common good – not least because finance has been allowed to become not just a means but an end.

The corporate sector, he argues, is hostage to an excessive preoccupation with shareholder value and return on equity. Managers think of their companies as a portfolio of businesses that are there to be bought and sold. One result is that trust between capital and labour has been undermined. Certainly, what English-speaking economists call implicit contracts between management and the workforce have increasingly been breached as a result of hostile takeovers and the relentless urge to improve the bottom line.

One of the trumpeted advantages of the Anglo-American model is flexibility. Mr Dembinski turns this on its head, declaring that in a more transactional economy, people so distrust their counterparties that transaction costs increase and the potential for co-operation in long-term investment is undermined – all to the point where the economy and society are deprived of their adaptive capacity.

In banking, the ethically based fiduciary principle has indisputably been eroded by the transactional ethos. The "originate and distribute" approach to bank lending has made the process more anonymous, as well as irresponsible. And, as the book rightly argues,

the asymmetry of information between parties to many market transactions is an invitation to predatory behaviour in the absence of fiduciary restraint.

This leads on to a revised version of the Marxist theory of alienation. Where Marx's workers were alienated because the pursuit of industrial efficiency denied them contact with the end product of their labour, Mr Dembinski's financial workers feel an exaggerated technical responsibility for their partic-

Finance: Servant or Deceiver?

Financialization at the Crossroads
By Paul Dembinski
Palgrave Macmillan, £60

ular segment of the business but no responsibility for the overall result. The very complexity of modern finance encourages a division of responsibility that insulates players from the consequences of their acts.

Such people work in a closed environment where they feel more powerful than other economic players. Ethical alienation becomes a habit for them, says Mr Dembinski, especially when the rewards are so high.

All of which merits attention in the light of the huge losses announced by banks in recent weeks. And it is hard to argue with the proposition that the manic pursuit of shareholder value and

personal profit by bankers operating within flawed incentive structures has been extraordinary damaging for the economy and for society at large.

Yet many readers may baffle at the view that the loss of a sense of the common good has left us mired in a market battlefield where all players pursue remuneration as a spoil of war and then "swiftly transfer it to the private sphere in order to build a fortress of lonely individual happiness".

The idea that modern finance, with its promise of future purchasing power for the individual, leaves us all more exposed to existential anxiety is likewise contentious. For many, credit is liberating as long as it is well-managed. Nor, I suspect, will many people share Mr Dembinski's nostalgia for family and social risk pooling in preference to financial insurance.

Some of the book's proposals, such as taxes on financial transactions, and the use of golden shares, boil down to the far-from-novel notion of throwing sand in the wheels. More interesting, if undeveloped, are suggestions that incentive structures should be changed to reward loyalty, whether to place, individuals, ideas or projects. The one thing that looks very untimely in this otherwise timely book is a call for a return to frugality and self-restraint. When we flirt with a potential depression, this is no way to address Keynes's paradox of thrift.

The writer is an FT columnist