Innovation
Knowledge
Development

The Open University

Financialisation: Taking stock and looking forward

Workshop on Friday 6th June 2014
9.30am – 5pm

Open University in London, 1-11 Hawley Crescent, Camden Town, NW1 8NP

Workshop outline
Since the advent of the financial crisis and ensuing recession in western economies the notion of financialisation has become mainstream and is now used in many different discourses. A rapidly growing number of references to financialisation can be found in various disciplines, such as sociology, politics, accounting and economics. The wide usage of this term, however, means that its interpretation varies significantly, and its contribution to the understanding of recent economic and social dynamics has taken many different forms.

As result the Open University's IKD Centre is hosting a workshop which aims to:

- take stock of the main contributions offered by the use of the term financialisation to the understanding of recent dynamics of capitalist societies
- identify key contributions generated by the use of the term financialisation
- look forward to identify the key issues that are likely to shape the research agenda around financialisation.

Outline workshop programme (provisional):

09:30 – 09:45 Welcome and introduction to workshop aims

SESSION 1:

09:45 – 10:30 Dimitris Sotiropoulos (OU) *Challenging and Revisiting 'Financialisation': the topology of modern finance and the key role of risk*

10:30 – 11:15 Colin Haslam (Queen Mary) *Reframing GM's Strategy 1909-1940: A Financialized Account*

11:15 – 11:45 BREAK

SESSION 2:

11:45 – 12:30 Matthieu Montalban (Université de Bordeaux) *LBO as a form of financialisation: nature, forms and consequences*

12:30 – 13.15 Janette Rutterford (OU) *Portfolio diversification pre-Markowitz: risk reduction before World War I*

13:15 – 14:00 LUNCH

SESSION 3:

14:00 – 14.45 Michael Pryke (OU) *Financialising household water: Thames Water, MEIF, and 'ring-fenced' politics*

14:45 – 15:30 Pauline Gleadle (UEA) *Divergent business models in response to financialisation: The cases of Pfizer and Eli Lilly*

15:30 – 16:10 Jeff Powell (SOAS) TBC

SESSION 4:

16:10 - 17:00 Round Table discussion, *'Financialisation: Taking stock and looking forward'*

Updated information including presentations abstracts will be made available from the IKD website: http://www.open.ac.uk/ikd/events/

Register to attend
Attendance is free, but spaces are limited. To reserve a place, or to receive further information, please email the IKD centre via: socsci-ikd-events@open.ac.uk

Food and refreshments
Lunch will be provided on the day. If you have any special dietary requirements please contact us in advance. Workshop discussions will continue over an evening meal to be organised at a local Camden restaurant. Details of the restaurant location and cost will be confirmed nearer the time.

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List of provisional titles and abstracts (* refers to presenting author):

'Financialisation' challenged and revisited: The topology of modern finance and the key role of risk

Dimitris P. Sotiropoulos, The Open University Business School*

Abstract

The term 'financialisation' has been coined and widely adopted as a description of modern finance by approaches that are critical of the research programme of mainstream financial and economic theory. The presentation revisits these discussions and attempts to capture what these approaches have in common. The majority of critical approaches usually avoid examining the nature of modern financial practices per se. Instead, they focus on outcomes and the implications that the latter may have over a range of economic and social spheres. Modern financial innovations are usually bracketed separately from other economic activities and largely considered within the context of increasing speculation. Their predatory character is taken to be to the benefit of the more sophisticated financial players. Finance is thus seen as an institutional distortion, a symptom of the deeper pathologies that current capitalism struggles with. The paper points at a different explanation. Financial practices have a particular topology in the social setting. This presentation rethinks the structure and the specificity of the co-existence between financial and other social and economic practices. The perspective offers an alternative theorization of modern finance, which is approached not as a distortion but as being innate in the dynamics of capitalist power. Regardless of its contradictions, modern financial engineering should be seen as a general technology of power that organizes the workings of social power relations and guarantees their reproduction: a genuine condition of governmentality. In this context, the role of risk along with related financial innovations is crucial, necessary and inevitable. In light of this reasoning, the presentation attempts to put forward an alternative theoretical agenda for 'financialisation'.

Reframing GM's Strategy 1909-1940: A Financialized Account

Colin Haslam, Queen Mary, University of London*

Abstract

This paper is about the Chandlers framing of structure and strategy and his legacy in contemporary business history in terms of his conceptualization of a general interpretative paradigm within which to analyse the emergence and development of modern industrial capitalism. This Chandlerian framing of the organisation of corporate resources has been employed to structure a more general position about the differences between an 'old' and 'new' financialized economy business model. This typology between old and new economy business models is then employed to describe changes in US competitiveness. In this article we argue that GMs management practices were both Chandlerian in terms of managing physical and financial resources within a decentralised co-ordinated divisional structure but also financialized during the early part of its business history 1909 to 1940. These findings suggest the need for broader framing devices

within which to capture the variety of corporate endeavours across time and space. A broader conceptualisation of strategy at GM would limit the use of stereo-types and typologies; in addition this added complexity, in terms of analytical framing, helps explain why financial transformation is less than straightforward because contradictory forces are in play.

LBO as a form of financialisation: nature, forms and consequences

Nicolas Bédu, GRETHA, Université de Bordeaux

Matthieu Montalban, GRETHA, Université de Bordeaux*

Abstract

The development of Leverage Buy-Out (LBO) since the 1980s in USA takes place in a period of mergers, financial deregulation and theoretical development sustaining the financialisation process. This article analyses the nature, the origin, the forms and consequences of LBO and its connexion with financialisation of capitalism, i.e as an institutionalised process of subordination of economy to finance capital (in the Hilferding's sense of finance capital). The aim is to show how LBO is part of this process and what are the hybrid characteristics and specificities of this kind of financialisation process. First we analyse the origin and institutionalisation of LBO, how it travels from public companies to private companies, diffusing some practices of shareholder value in SME through a non-transparent governance (opposite to stock market rules), and by lobbying States to obtain financial deregulation. Then, we examine the risk transfer from financial capital to industrial capital, and we question some classic distinctions between the types LBO. Finally, we analyse the forms of practices of parasitism by LBO, i.e. forms of value capture and predation, the mechanisms and the restructurings imposed.

Portfolio diversification pre-Markowitz: risk reduction before World War I.

Janette Rutterford, Open University Business School*

Abstract

Today, investors are assumed to want to maximize investment return, generally agreed to be the total of income and capital gain over a particular period. The measure most commonly used to quantify risk is the standard deviation of returns. The relationship between individual securities is measured by the correlation coefficient. The less correlated the securities in a portfolio, the greater the benefits from diversification.

Markowitz diversification, formally developed in 1952[1] derives the weights that securities in a portfolio should have in order to maximise the expected return of a portfolio for a given risk, and this model uses the individual securities' expected returns and risks, as well as their correlation coefficient matrix. The amount to be invested in each security depends not only on its own risk and return characteristics but on how it interacts with other securities. *Naïve diversification*, which assumes equal amounts invested in each security, achieves some benefit in the risk return tradeoff, but less than does Markowitz diversification.

This paper argues that, well before Markowitz diversification, individual investors had a good understanding of the benefits of diversification, albeit closer to naïve than to the Markowitz approach. By the 1870s, spreading risk across a number of securities was regularly promoted as a means of enhancing

[1]Harry Markowitz, "Portfolio Selection", *Journal of Finance*, 1952, vol. 7, pp. 77-91.

yield on investment although this was typically done by including a small amount of a risky, high yielding investment security. By the 1900s, the emphasis was more on naïve diversification, with investment authors recommending to both 'spread the capital over a number of concerns' and also to 'not invest more than about one tenth of the capital in any one concern".[2] Before World War I, so-called *Scientific Investment* was regularly promoted by the investment periodical, the *Financial Review of Reviews.* This promoted a top-down global diversification approach, with the world divided into ten or so regions, and equal risk investments chosen from each region. So, a higher yield portfolio could be put together with a lower correlation than available from a purely domestic portfolio.

The paper also compares theory with practice by exploring the extent of and type of diversification in actual investment portfolios held by 508 people who died between 1870 and 1902, from probate records. International diversification was more common than for 21st century individual investors, and measures of diversification were little different for pre-Markowitz investors than they are for post-Markowitz investors today.

Financialising household water: Thames Water, MEIF, and 'ring-fenced' politics

John Allen, Department of Geography, The Open University

Michael Pryke, Department of Geography, The Open University*

Since the privatisation of water in England and Wales in 1989, a shift in the pattern of ownership towards more consortia-led, global infrastructure funds has witnessed the emergence of a skewed distribution model of financialised infrastructure in the household water sector. A model of debt refinancing based largely upon the securitization of household revenue streams, we argue, has engineered benefits more towards investors than customers. Through the example of Thames Water and its purchase in 2006 by an international consortium of investors led by the Australian bank, the Macquarie Group, this article sets out a model of leveraged debt made possible through the predictable nature of revenue streams captured from households who have no choice over their water supplier or the amount that they have to pay.

Divergent business models in response to financialisation: The cases of Pfizer and Eli Lilly

Pauline Gleadle, Norwich Business School, University of East Anglia*

Stuart Parris, Department of Economics, The Open University

The pharmaceutical blockbuster model rose to become the dominant model for drug discovery and pharma industry more generally. The blockbuster model is also well suited to a financialised business environment whereby production models are optimized toward financial outcomes. Monopoly profits from patent protected products are only partially reinvested to fill discovery pipelines with future blockbusters, helping to increase share prices, yet as the same time leaving opportunity for regular dividend payment. However, in recent years the blockbuster model has faltered, it faces the perfect storm of rising R&D costs, falling productivity, and lost revenue on existing products due to the expiration of key patents. We use the pharmaceutical industry to study how firms, search for, and transition to, new business models in a financialised business environment. We compare the business models of two large pharmaceutical firms, Pfizer and Eli Lilly examining how they have conducted their business under the influence of financialisation pressures at a time when the dominant industry business model is under threat. We examine how two US

[2] W.B., *Women as Investors*, Investment Pamphlet, London 1908, p.29.

firms in the same industry show varying degrees of financialised behaviour using key indicators based corporate accounts together with supplementary materials from analyst reports and background industry data. Our analysis highlights how firms facing similar challenges have sought different strategies and responses to shareholder pressures as a result of compromise between demands of shareholders and the narratives played out by managers. Finally we consider the implications for long-term sustainability of each firm as a result of their strategic choices.