

UNIVERSITY OF SOUTHAMPTON

**DECONSTRUCTING THE TENSIONS IN
THE FINANCIAL SERVICES INDUSTRY**

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DEDICATION

To my mother

Syeda Adeebunnisa Khalidi

who laid the foundations of my education,

my father

Abdul Noor Khan Khalidi

who stimulated and encouraged my pursuit for knowledge,

and my brother

Dr. Fazal Anwar Khalidi

who set the standards of excellence and pushed me towards their realization.

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ABSTRACT
FACULTY OF SOCIAL SCIENCES
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Doctor of Philosophy
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by Manzoor Anwar Khalidi

Deconstruction is a philosophical thought (associated with the philosophy of Jacques Derrida) aimed at outlining the tensions inherent in the text, so as to be able to understand the problems connected with the text. It is after all our interpretation and understanding of the problems that forms the basis of the strategies that we develop for overcoming them. The thesis is therefore an attempt towards understanding the problems facing the regulators and their regulatory framework in the financial services industry, problems connected to the tensions emanating out of the dialectical relationship between the regulators and the regulated. The thesis is divided into five parts, the bulk of which is constituted by Parts II, III, and IV (Parts I and V being introduction and conclusion). Part II is on the tensions in the financial services industry. It involves an examination of the tensions inherent in the financial services industry, tensions that have created a crisis of confidence in the regulatory philosophy of ordering and control of the marketplace (and the ontological conditions prevailing in the marketplace) by means of a meta-framework. Part II also provides the stepping stone for a more deeper analysis of the tensions in Part III (philosophical analysis of the tensions in the financial services industry), and Part IV (the problematic of time and space compression) of the thesis. The basis of Part III of the thesis lies in Kuhn's thesis of paradigm shift. The discussion revolves round a two-part hypothesis: one, the tensions reflecting the regulatory crisis in the financial services industry may be a subset of, or a part of a much wider area of tensions/crises facing the conceptual foundations of the regulatory philosophy: the modernist philosophical thought; and two, the alternate philosophical thought which is generally described as postmodernism, may provide us with inspiration and ideas for the formulation of a regulatory strategy and regulatory framework that may facilitate the achievement of regulatory objectives while facilitating the amelioration of the tensions inherent in the financial services industry. The investigation into the first part of the hypothesis emphasizes on the problematical nature of the modernist philosophical thought: 'freedom under the guidance of reason', and the existence of the truth out there waiting to be discovered, a philosophy which encourages the development of a meta-discourse or a meta-framework that can be applied across time and space for the ordering and control of our ontological conditions. Two approaches have been applied to examine the problem: one, a historical investigation into the emergence, the development, the phases of crises and regeneration, and the present crisis facing the modernist philosophical thought. The present crisis is different from the earlier ones in the sense that unlike the earlier crises, the present crisis is connected, not simply to the change, but rather, to the speed of change of our ontological conditions. The second approach is aimed at the logic for the crisis. It involves an attack on the central dilemma of the modernist philosophical thought: the philosophy of 'becoming'. It involves a deconstructive analysis of two of the grandest of grand narratives of the modernist philosophical thought that rationalize the philosophy of 'becoming': Weber's 'Theory of Bureaucratic Rationality' and Marx and Engels' 'Manifesto of the Communist Party'. It also involves the formulation of a theory based on Schumpeter's 'Theory of Economic Development' to explain the logic for the present crisis facing the modernist philosophical thought. The investigation into the second part of the hypothesis begins with the unravelling of the confusion surrounding the concept of postmodernism, and then moves on to an exploration into the concept of postmodernism and the ideas generated within the realm of postmodern philosophical thought. Three approaches have been applied to examine the concept of postmodernism: one, the concept of postmodernism as an epoch; two, postmodernism as a reaction to, or departure from modernism; and three, postmodernism as a signifier of the problematical features of modernity. Each of these approaches provide us with a different perspective for understanding of the problems of the present era, especially in the context of the tensions in the financial services industry. This is also the basis for the investigation into the philosophy of the three most important philosophers of the postmodernist philosophical thought: Jean-Francois Lyotard, Michel Foucault, and Jacques Derrida. Part IV of the thesis which is on the problematic of time, and space compression involves: one, an examination of the concepts of time and space compression; and two, an investigation beyond the conventional concepts of mechanical time and physical space (including an examination of a few alternate concepts of time and space) in an effort to broaden our knowledge base and our ability to understand the phenomena of time and space compression, and their consequences especially in the context of the dialectical relationship between the regulator and the regulated, and the tensions in the financial services industry. The aim of the thesis is primarily metaphorical. The aim is to provide a different approach for visualizing the problems in the financial services industry. The thesis is also aimed at intellectual broadening, to serve as a direction flag for understanding the problems of the present era.

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PREFACE & ACKNOWLEDGEMENTS

I would like to apply the metaphor of ‘life as a journey’ to chart out my experience in the course of working towards my Ph.D., and at the same time acknowledge my gratitude to those who helped me in my journey through the realm of knowledge. Life as a journey is an appropriate metaphor to chart out one’s experience of the Ph.D. process because the researcher is analogous to an explorer trying to explore the unchartered territory or the realm of knowledge. This journey involves a starting point, a finishing point, cross-roads, diversions, roadblocks, etc., and at the end of the journey, one is required to submit the travelogue of his/her journey or voyage into the realm of knowledge which is the thesis.

In this journey, the supervisor plays a crucial role. S/he not only provides guidance to the traveller/researcher in the planning stage of the journey, but also periodically evaluates the progress, checks the sense of direction, and most importantly encourages and motivates the traveller/researcher, to continue the journey until the destination has been reached. During the course of the journey one may come across roadblocks and obstacles, and may therefore be required to develop strategies for surmounting the obstacles in order to reach the destination. In this journey through the realm of knowledge, sense of direction is vital, one may come across cross-roads, and may therefore be required to make a decision regarding the future the course of direction. One is always prone to take a wrong turn, which may mean getting lost, or reaching a dead end, which may require the traveller/researcher to retrace his/her steps and locate a new direction, or abandon the journey altogether. Supervisor’s input in providing necessary direction flags is therefore vital, not only in the context of the present journey, but also in the development of the necessary knowledge skills of the traveller/researcher so that s/he develops the competence and the confidence to go on future journeys independently, without the need for the guidance of a supervisor.

The end result of this journey is the Ph.D. thesis which is analogous to a travelogue mapping out the story of the traveller/researcher’s voyage through the realm of knowledge. It is also a testimony of his/her intellectual competence, and is therefore required to be examined by an expert explorer/traveller to determine whether the travelogue is worth sharing with the (academic) community, whether the explorer/traveller has achieved the competence and the confidence to undertake future journeys into the unchartered realm of knowledge independently, without the guidance of the supervisor.

My experience of exploring the realm of knowledge with the aim of achieving my Ph.D. degree can be described as a very long and arduous, yet a very fruitful journey. The journey of my exploration can be divided into two phases. The first phase was a very difficult and agonizing

experience. It involved every conceivable problem that an explorer can expect during his travels including the loss of one's bearings and breakdown. I did not have the good fortune to start the journey with Professor George McKenzie as my supervisor. It was only when I was hopelessly lost and at the verge of abandoning my journey, that George took over as my supervisor, and thus began the second phase of my journey and travels into the unchartered realm of knowledge, which although very arduous, was at the same time a very stimulating and satisfying experience. My gratitude to Dr. Jonathan Klein for helping me in the change of my supervisor.

My first meeting with George after he became my supervisor was a revealing experience. George's supervision strategy was the opposite of my first supervisor. George's approach was that of locating and encouraging the development of my strengths rather than my weaknesses. His strategy was to inspire self confidence and belief in one's strengths to take charge of the weaknesses and problem areas, so as to be able to independently chart out one's own journey. His strategy was that of providing the necessary direction flags whenever and wherever he thought the need for. His strategy was that of encouraging one to raise questions, to explore and investigate in order to appreciate and understand the problem. His strategy was that of intellectual broadening rather than limiting one's intellect within the narrow confines of a particular area of disciplinary specialization. His strategy was that of encouraging one to break out of the straitjacket or the mental prisons that seem to characterize particular areas of disciplinary specialization in order to allow cross disciplinary fertilization of knowledge, and also to develop the confidence in one's ability to interrogate the problematical facets of different disciplinary realms. At the end of my first meeting he gave me David Harvey's 'Condition of Postmodernity' to explore as a direction flag for reviewing and reexamining my ideas. This was my first encounter with a text that entered the realm of a number of disciplines including philosophy. Harvey is a geographer, and geography unlike most other disciplines appear to be undergoing a process of implosion rather than explosion (or fusion rather than fission). His book was instrumental in igniting my passion to undertake a cross disciplinary study in an effort to understand the tensions in the financial services industry. It set me on a new journey, a new process of exploration into the realm of knowledge, which though very arduous, was at the same time very inspiring and stimulating. What began with Harvey, expanded to include the texts of other major philosophers and social scientists of the modern and the postmodern era. Their texts were vital not only in broadening my intellect but also in inducing the conviction and confidence to undertake a broader and deeper rather than a narrow and surface level deconstructive analysis of the tensions in the financial services industry. In the context of the metaphor of journey, the journey progressed from an exploration of the superstructure to an exploration of the philosophical foundations of knowledge on which a number of disciplinary superstructures (each

superstructure defining a particular disciplinary realm) have been constructed. The thesis can also be visualized as a preamble for my future deconstructive investigation into the other problematical facets of our political, economic, and social realms of knowledge. This would not have been possible without the direction flags, and encouragement from George. He helped me in retracing my steps, reviewing my progress, and finding a new sense of direction - a direction that has helped me reach my destination. Thank you George.

Other than George, another person whose assistance was vital in the completion of my journey was my G.P. Dr. Catherine Ursell. I am indebted to her for the recovery from the breakdown which I suffered during the first phase of my journey. After suffering the agony of years of incorrect diagnosis and flawed drug therapy, in her I at last found a doctor with a positive attitude, a person whose medical philosophy was "if there is a problem then there must be a cure", a person who was ready to undertake all possible tests and willing to experiment with different medical and drug therapy to find cure for my headaches, a person who was willing to discuss not only the problems but also the possible therapy with the patient. The reference is to the information on therapy for headaches that I had collected from the internet sites of the various specialist headache clinics round the world. Thank you Dr. Ursell.

My thanks also to Professor Richard Dale for giving me the opportunity to do a Ph.D., and ESRC for providing the financial support for my research assistantship, and for the opportunity to work on Single European Market Project. My thanks also to Dr. Karen Piggott for extending my deadline and allowing me extra time to complete my thesis.

In the course of this journey through the realm of knowledge, I met a number of strangers and fellow travellers who became friends, whose companionship made this arduous journey bearable and in some cases even pleasurable. This section is also aimed at acknowledging my gratitude for their friendship. I would especially like to name Ali Tebrez, Saeed Ishtiaq, Shayam Dhomeja, Arshad Humayon, Aslam Pirzada, Ayub Malik, Nadeem Khawaja, Shabbhar Jafrey, Keith Terrill, Simon Wolfe, Sue Westcott, Dr. Rachel Trost, Sameera Dalvi, Yosif Basodan, Arumugam Thallaisundaram, Sofri Yahya, A Rahim A Rahman, Maria De Lordis Trevino Villarreal, Mirela Schwartz, Lei Lei Tang, and Musa Al Assad. Thank you all my friends.

PART

I

INTRODUCTION

INTRODUCTION

As to what motivated me, its is quite simple: I hope that in the eyes of some people it might be sufficient in itself. It was curiosity - the only kind of curiosity, in any case, that is worth acting upon with a degree of obstinacy: not the curiosity that seeks to assimilate what it is proper for one to know, but that which enables one to get free of oneself. After all what would be the value of passion for knowledge if it resulted only in a certain amount of knowledgeableness and not, in one way or another to the extent possible, in the knower's straying afield of himself? There are times in life when the question of knowing if one can think differently than one thinks and perceive differently than one sees is absolutely necessary if one is to go on looking and reflecting at all ... But then what is philosophy today - philosophical activity, I mean - if it is not the critical work that thought brought to bear on itself? In what does it consist, if not in the endeavour to know how and to what extent it might be possible to think differently, instead of legitimating what is already known?

Michael Foucault¹

The above quotation from Foucault is a reflection of the inspiration that forms the driving force behind the thesis. This thesis breaks away from the normal conventions² by starting on a narrow base (at the level of the regulatory framework in the financial services industry), and then broadens up as the discussion moves into the realm of the philosophical foundations of the regulatory framework. The discussion starts at the level of the superstructure (the regulatory framework in the financial services industry) and then moves into the philosophical foundations of this superstructure where the realm of investigation involves an examination of the modernist philosophical thought, as well as the alternative philosophical thought: postmodernism, which is challenging the supremacy of the modernist philosophy. In this respect the thesis may be considered (to some extent) as being postmodern³. Perhaps it is also a reflection of the intellectual development and the transformation

¹This fragment from the preface of Foucault's 'L'Usage des plaisirs' (pp.9) was read out by Gilles Deleuze at the funeral of Michael Foucault. Quoted in Eribon (1995, pp.301).

²The normal conventions of PhD. thesis entail an investigation that starts on a broad base (literature review) and gradually narrows down as it approaches completion. Furthermore, the realm of analysis in a conventional PhD. thesis generally remains confined within a particular area of disciplinary specialization.

³The reference here is to Lyotard's (1984b, pp.81) conceptualization of the term 'postmodern' as that which "puts forward the unrepresentable in the presentable itself". The reference is to that which cannot fit within confines the modernist rules of discourse formation, and hence is either denied the

in the thinking of the author from a state of mild scepticism towards the regulatory philosophy to a state of agnosticism towards it. The reference here is not to the literary concept of 'agnosticism', but that given by Lyotard in the context of the theory of language games: an unexpected move that disorients the system. This is also the basis for the use of the term 'deconstruction' in the title of the thesis⁴. The reference here is to the concept of deconstruction as a philosophical thought aimed at laying out the tensions in the text. In postmodernism the concept of text is very broad. It covers not only the work of an author, but the whole realm of human thought and action can be included within the concept of text. In the context of the title of the thesis, the whole regulatory framework in the financial services industry can be conceptualized as a text. It can be further expanded to incorporate the whole of the financial services industry (including the regulators, the regulated, the markets, and the market participants, and their activities), in which the regulator-regulated dialectic itself would be classified as a deconstructive process at work in the text. The tensions are only an indicator of the process. Deconstruction, according to Derrida (1995b, pp.413) "finds itself at the heart of what you call 'tensions'. It is a question of assuming these tensions, of 'living' them as much as of 'understanding' them". Deconstruction is not aimed at creating tensions. It is aimed at "trying to understand them, of interpreting them, so as to respond to them in the most responsible fashion possible." This is also the basic rationale of the thesis: to understand and to interpret the tensions so as to be able to respond to them in the most responsible fashion possible.

The thesis is divided into five parts, with the first and the final parts being the introduction and the conclusion. The bulk of the thesis, therefore, comprises of three parts (II, III, and IV). Part II consists of two chapters (both of which have been published in refereed journals), both of which are a critique of the regulatory framework in the financial services industry in the sense that they lay out some of its problematical facets that may be associated with the tensions in the financial services industry. The place of part II in the overall scheme of the thesis is that of providing the stepping stone, the rationale, the justification for undertaking an investigation into the philosophical foundations of the regulatory framework in the financial services industry. Part II of the thesis scratches the surface to reveal some of the tensions apparent in the financial services industry, thus providing a stepping stone for undertaking an investigation below the surface of the tensions which is the area of investigation of Part III and IV of the thesis. Part III involves an investigation into:

presence or is silenced. He describes the postmodern artist or writer to be in the position of a philosopher whose text or works are not governed by preestablished rules and cannot be judged by preestablished standards of examination. Those rules and categories are what the work itself is looking for.

⁴An unexpected move that is aimed at disorienting the system.

one, the tensions facing the philosophical foundations of the regulatory framework: the modernist philosophical thought; and two, an exploration into the alternate philosophical thought: postmodernism, with a view to provide us with ideas and inspirations that may help us in achieving the regulatory objective of a safe and sound marketplace while at the same time reducing the tensions apparent in the financial services industry. Part II of the thesis also provides a stepping stone for part IV of the thesis which involves an examination of the problematic of time and space compression. The aim is to provide a different approach for visualizing the problematic of time and space compression and its ensuing problems. Part V is the final section of the thesis. It involves drawing conclusions from the discussions in Part II, III, and IV of the thesis.

Having introduced the overall structure of the thesis, we can now provide a more detailed (chapter by chapter) introduction to the thesis.

Tensions in the Financial Services Industry: This is the theme of part II of the thesis which consists of two chapters, both of which have been published in refereed journals.

Chapter two incorporates a paper published in the Journal of Common Market Studies: "The EU Directive on Deposit Insurance: A Critical Evaluation". This paper involves a critical evaluation of the European Union Directive on Deposit Guarantee (1993) which seeks to influence the distribution of power between the banks and the depositors on one hand, and between the national regulatory authorities and the European Union on the other. The aim of the paper/chapter is to argue and lay out the tensions between the incentives induced by the directive for the depositors and the banks, and the aim of the national supervisors and the EU to foster a stable and efficient financial system. It is a fairly comprehensive paper that begins with a background outlining: one, the emergence of the concept of deposit insurance as a regulatory tool for the control of monetary stability⁵; two, features of the EU directive including some of its problematical aspects; and three, the comparison of EU Directive with the UK, German, and the US deposit guarantee schemes. This is followed by an exploration into three interrelated themes: one, the problem of moral hazard and the principle of co-insurance which requires the depositors to bear (in some instances) losses arising from bank failure. The discussion under this theme investigates into the rationale for safety net as well as its implications. The most important implication of which is the problem of moral hazard⁶, a problem that rationalizes the principle of depositors co-insurance - the depositors to share the risks,

⁵The emergence of deposit insurance as a regulatory tool can be connected to the creation of the Federal Deposit Insurance Corporation (FDIC) in 1934 to control the problem of bank runs.

⁶A problem that finds its basis in the agency cost associated with the banking industry.

in order to encourage them to monitor the soundness of the bank. The problem with this solution⁷ (it will be argued) is that it is contrary with the goals of the Deposit Guarantee Directive of a safe and sound financial system. The second theme covered in the paper involves an investigation into the principle of bank safety net procedures, and the relationship between the Deposit Guarantee Directive and the other financial market directives, especially the Bank Solvency Directive. There is an inverse relationship between the bank capital and the probability of bank failure, and the activation of the safety net of deposit insurance. But underlying this relationship are two important considerations, both of which (it will be argued) are problematical: one, the accuracy of the valuation of bank capital - tension between book value and market value; and two, the timing of the wind-up or closure - tension between solvency and liquidity, and the consequent tension between central bank and banking supervisor; The third theme of the paper relates to the 'principle of subsidiarity' which leaves the implementation of the directive in the hands of the national authorities subject to minimum standards. The discussion under this theme examines the different concepts of 'subsidiarity', and them applies Delors (1991) concept⁸ as the basis for examining five sub-themes: one, tension between the host and the home country minimum standards⁹ ; two, tension between the deposit insurance and the lender of last resort functions¹⁰ ; three, tension between the difference in treatment of foreign branches and subsidiaries¹¹ ; four, tension between the de-jure and de-facto deposit guarantee with respect to the 'too big to fail' principle; and five, tension between the private and public deposit guarantee schemes. The chapter/paper concludes by referring to the philosophy of the founding fathers of the EU: to create an environment of positive tensions in which the challenges would leads to a greater harmonization of policies eventually leading to a political unification. In this respect, the Deposit Guarantee Directive by setting the minimum standard of safety net, provides a learning period for further harmonization and consolidation. What the directive, however, ignores

⁷The reference here is to the application of depositor co-insurance as a solution to the problem of moral hazard.

⁸The smaller unit's right to act is operative to the extent, and only to the extent that it alone can act better than a large unit in achieving the aims being pursued.

⁹The EU Directive allows the branches of Foreign Banks to be regulated/covered by the home country deposit insurance, subject to the EU minimum.

¹⁰Although Deposit Insurance is aimed at solvency problem, whereas the lender of last resort facility is aimed at liquidity problem, there is a strong connection between the two. This is because the value of capital is itself problematical.

¹¹The branches of foreign bank are regulated by the home country regulator, whereas the subsidiaries of foreign banks are regulated by the host country regulator.

(it will be argued) is the fact that the behaviour of the market participants cannot be predicted. It is possible that the market participants may move quickly and implement strategies which may make future adjustments difficult to implement.

Chapter three comprises of a paper published in the Journal of European Public Policy: 'The Globalization of Banking and Financial Markets: The Challenge for the European Regulators'. The objective of the chapter/paper is to reexamine the arguments underlying the regulation and supervision of financial markets in light of the recent trends in regulatory philosophy that are shifting the burden of monitoring and supervision from the regulators to the markets themselves. The paper argues that the gradual change in the regulatory philosophy is not so much the result of the acceptance of the rhetoric of free market philosophers or the neglect of theory of market failure, rather it is a by-product of the globalization of financial markets brought about by the electronic revolution of the late twentieth century. Financial institutions by compressing time and space are threatening the supremacy of the nation-state as the basis for ordering and controlling our economic, political, and social life. The consequence has been a gradual shift in the regulatory philosophy from the regulation of markets by individual nation-states, to passing of the disciplinary function to the markets themselves. The rationale for this shift appear to the recognition by the regulators of their inability to keep pace with financial innovation and the transient and uncertain nature of market.

This is a very important paper in the context of the overall thrust of the thesis, because it directs our attention to the various forms of tensions in the financial services industry - tensions that have brought to the fore the problematical nature of the control engineering framework of the regulators - tensions that have gradually brought the regulators to the realization that: one, they have been trapped within a theoretical framework which is based on linear progress, rational choice, and a desire for unchanging social order, a framework which is inconsistent with the challenges of the dynamic market environment of the present era which is being controlled by the entrepreneur driven financial institutions; and two, in the context of Stigler's (1971) framework of demand and supply of regulations, the present market reality of global competition implies that the regulators of nation-states have lost their monopoly position as the sole supplier of regulations. It is only recently that the regulators have come to realize that they are losing this race and need to respond. Their initial reaction was harmonization of financial market regulations. The Basle Accord of 1987 is an example. The problem, however, is that these regulations are based on complex mathematical procedures which have their basis in heat temperature physics, which do not take into consideration the dynamics of the marketplace. The central thesis of the paper is that centralization of authority and harmonization will have little impact. While harmonization takes into consideration the problem of globalization, it ignores the creative destruction and the destructive construction of the entrepreneurial

forces behind the changes in the financial services industry. Since the regulators are not a part of the process, they cannot keep pace with it, and hence cannot control it. Lately, there has been a converse trend in the application of subsidiarity, not in terms of nation-states to a supra-national authority, but in terms of nation-states to the markets themselves. The paper examines this gradual shift in the regulatory philosophy in the context of four developments: one, the principle of co-insurance in the EU Deposit Guarantee Directive; two, the Fisher Report¹²; three, the Federal Reserve Board's argument for applying an open approach to regulation; and four, the New Zealand Experiment. In all these developments (it will be argued) transparency is the key to the success or failure of these initiatives. Yet despite these experiments, there are still sceptics in the regulatory community who stress on greater direct regulatory intervention instead of improving transparency. This takes us back to the start of the article: is it possible to have financial calm and order in a dynamic and competitive environment driven by the entrepreneurial forces? The only answer that one can suggest to such a question is, if the operations of financial markets are going through a paradigm shift, the researchers should also be prepared for a paradigm shift in the way they seek to understand these markets. At minimum they should be prepared to raise questions and to raise direction flags that may help us in understanding the tensions in the financial services industry. This is what part III and IV aim to accomplish.

Philosophical Analysis of the Tensions in the Financial Services Industry: This is the theme of part III of the thesis in which the discussion revolves round the hypothesis that:

- one: the tensions reflecting the regulatory crisis in the financial services industry may be a subset of, or a part of a much wider area of tensions/crises facing the conceptual foundations of the regulatory philosophy: the modernist philosophical thought.**
- two, the alternate philosophical thought which is generally described as postmodernism, may provide us with inspiration and ideas for the formulation of a regulatory strategy and regulatory framework that may facilitate the achievement of regulatory objectives while facilitating the amelioration of the tensions inherent in the financial services industry.**

The basis of the above hypothesis lies in Kuhn's (1970) thesis of paradigm shift. In the context of Kuhn's thesis, there are two possible explanations for the tensions in the financial services industry: one, at the superstructure or surface level, these tensions are an indicator of a paradigm shift in the operations of the market forces, hence the need for a paradigm shift in the regulatory framework if

¹²The reference is to the BIS (1994) report "Public Disclosure of Market and Credit Risks by Financial Intermediaries", that calls for a greater disclosure of information on market and credit risk, including the comparison of ex-ante risk profile with the ex-post performance.

the regulatory objectives of efficient, safe and sound marketplace are to be achieved. Two, at the substructure or foundational level, the tensions in the financial services industry are an indicator of the crisis of confidence facing the conceptual foundations of the regulatory framework: the modernist philosophical thought, which has become problematical in the context of the present ontological conditions where its preeminence is being challenged by an alternate philosophical thought labelled as postmodernism. It is this second of the two interpretations drawn from Kuhn's thesis that forms the basis of the above (two part) hypothesis. The discussion in this part of the thesis is covered in four chapters of which the first two (chapters four and five) involve an investigation into the first part of the hypothesis which links the tensions in the financial services industry with the crisis facing the modernist philosophical thought. The suggestion being, that the tensions that echo the contemporary regulatory crisis associated with the prudential control of banking and securities industry may not necessarily be a reflector of minor deficiencies in the regulatory tools like capital adequacy regulations which can be overcome through their correction (revision and updating). Rather, the crisis may be an embodiment of a much greater problem: the incompatibility of the regulatory philosophy with the present ontological conditions prevailing in the financial services industry. The second part of the hypothesis forms the kernel for the discussion in the last two chapters (six and seven) of part III. It involves an examination and exploration into the realm of postmodern philosophical thought for inspiration and direction flags that may help us not only in getting a better understanding and appreciation of the present ontological conditions, but also for providing direction flags towards achieving the regulatory objective of safe and sound marketplace, while at the same time reducing the tensions apparent in the financial services industry.

The storyline of chapter four is based on history. It involves a historical analysis of the emergence and the development of the modernist philosophical discourse. It covers a broad range of issues covering amongst other things, the launch of the enlightenment project; the central ideas that formed the underpinnings for the project of modernity: freedom under the guidance of reason - the rationale for the development of a universal and objective framework for the organization and control of the society; the different phases of crises and the reformulation and regeneration of modernity; the present crisis facing the modernist philosophical thought, and how it differs from the earlier phases of crises. The choice of the storyline of history lies in the two basic objectives that form the basis of the chapter: the primary objective is to connect the tensions facing the financial services regulator with the logic for the tensions and the crisis of confidence facing its conceptual foundations: the modernist philosophical thought itself. The secondary objective is to use the storyline of history to examine the emergence and the development of some of the concepts, phenomena, and governance structures connected with the tensions in the financial services industry.

In the context of the primary objective, the discussion of the chapter involves an attack on the problematical nature of the modernist philosophical thought which rationalizes the philosophy of 'becoming': the rationale for a meta-discourse or framework based on reason for the ordering and control of the ontological conditions - a framework that is rationalized as being applicable across time and space. The different phases of crises that required the revision and reformulation of the modernist philosophical discourse, point to the limits of human rationality in developing an all encompassing discourse or meta-framework that can be applied across time and space. The logic for each phase of crisis (it will be argued) lay in the changes in the ontological conditions which created a crisis of confidence in the meta-discourses (that were not only representative of, but were also rationalized by the modernist philosophical thought), aimed at ordering and control of the ontological conditions. A revision and reformulation of the discourses was therefore required for the regeneration of the modernist philosophical thought. The present crisis (it will be argued) is different from the earlier ones in the sense that it is not simply the change, but the pace of change of our ontological conditions (which is a consequence of the time and space compression engendered by the entrepreneurial forces) that is at the root of the present crisis facing the modernist philosophical thought. Now (it will be argued) it is the ability of the modernist philosophical thought to revise and reformulate its meta-discourse and regenerate itself once again, that is being questioned. The crisis therefore relates to the basic logic of the modernist philosophical thought that rationalizes the possibility of the existence of and hence the search (or the research) for the development of a meta-discourse or a meta-framework based on human rationality that can be applied across time and space for the ordering and control of the present and future ontological conditions. In other words, it is its basic presumption of the modernist philosophical thought, the philosophy of 'becoming' that is being questioned. All this points to the problematic nature of the philosophical foundations that forms the basis of the regulatory framework in the financial services industry. Hence the connection between the tensions in the financial services industry and the crisis of confidence facing its conceptual foundations: the modernist philosophical thought.

In the context of the secondary objective of the chapter¹³, the first crisis of modernity is of special importance. It was the first occurrence of the concept of business cycle, systemic risk, and cross border contagion. The collapse of the financial markets and its contagious effects on the other markets, accentuated the need for rational organization and control of the financial markets. The aftermath of the crisis is also important. It saw the launch of the first phase of globalization which

¹³The secondary objective is to use the storyline of history to examine the emergence and the development of some of the concepts, phenomena, and governance structures connected with the tensions in the financial services industry.

involved the combined initiative of the capitalist (or more appropriately, the entrepreneurial) forces and the imperialist nation-states who went on a major phase of spatial expansion. This phase is also important because it saw the development and the implementation of the meta-framework for the global standard of civilization which involved the creation of the myth of the nation-state and national societies, the system of international relations, etc.. Both these developments¹⁴ (it will be argued) are important, especially in the context of the present crisis in modernity (and the tensions in the financial services industry), which is connected to the second phase of globalization, in which the entrepreneurial forces and not the nation-states are the key players. As a consequence, in this second phase of globalization, the meta-framework of the global standard of civilization developed and implemented during the first phase of globalization, which also forms the basis of the regulatory framework in the financial services industry, has become problematical. Hence, the rationale for the tensions in the financial services industry, and their connection with the crisis of confidence facing the modernist philosophical thought.

The next chapter (chapter 5) also investigates into part one of the hypothesis which connects the tensions in the financial services industry with the crisis facing its conceptual foundations: the modernist philosophical thought. The story line here involves an attack on the central dilemma of the modernist philosophical thought: the philosophy of 'becoming' - the belief in the existence of, and hence the rationale for the development of a meta-discourse or a meta-framework (based on human rationality) for the ordering and control of the ontological conditions - a discourse, a framework that can be applied across time and space. The storyline of the chapter can be visualized as a framework with the regulators on one side and the market forces on the other, both of whom are involved in a game to control the ontological conditions. On the side of the regulators are the philosophers, the social scientists, the political forces, etc., who visualize the ontological conditions as a system, and therefore strive to develop a meta-discourse or a meta-framework based on human rationality that can be applied across time and space for the ordering and control of the system. On the other side are the entrepreneurial forces, the creative destroyers and destructive creators par excellence who in their search for profits bring about fundamental changes in our economic and social system thereby changing the basic assumptions that form the basis of any discourse or framework for the ordering and control of the system, and as a consequence creating a crisis in the meta-framework or the meta-discourse for the control of the system. This framework is also representative of the strategy adopted for the analysis of the hypothesis. It involves a deconstructive analysis of two of the grandest of the grand narratives of the modernist philosophy: one, Weber's

¹⁴The reference is to: one, the launch of the first phase of the globalization; and two, the development and implementation of the global standard of civilization.

philosophy of ‘bureaucratic rationality’ (which also forms the underpinnings of the regulatory philosophy); and two, Marx and Engels’ ‘Manifesto of the Communist Party’, as the representative of the modernist philosophical thought, in the context of Schumpeter’s ‘Theory of Economic Development’ - a theory that is representative of the contribution of the other side of the framework: the entrepreneur. The two discourses that have been chosen as being representative of the modernist philosophical thought¹⁵, are important for our analysis of the hypothesis, because they not only allow us to understand the limitations of human rationality to develop a complete system that can be generalized across time and space for the ordering and control the ontological conditions, but also and more importantly, because they allow us an insight into the force that is at the back of tensions in Weber’s bureaucratic rationality, the force that provides the explanation for the failure of socialist economic system and the crisis in modernist philosophical thought: the entrepreneur. Entrepreneur is the force of change whose contribution Weber, as well as Marx and Engels acknowledge but prefer to disregard in their rationally constructed model/system for the ordering and control of the ontological conditions. The discourse that is representative of the contribution of the entrepreneur is Joseph Schumpeter’s (1959) ‘Theory of Economic Development’. Examination of this discourse is crucial not only for understanding the tensions in the financial services industry, but also for understanding the crisis of confidence facing the philosophical foundations of the regulatory framework: the modernist philosophical thought. Schumpeter’s theory is important because it not only provides an explanatory logic for Adam Smith’s ‘invisible hand’, but also for the process of economic development (the outward shift of the production possibility frontiers) that eventually leads to a change in our ontological conditions. Schumpeter’s theory is also important because it helps us to understand the concept of ‘market mechanism’. The chapter therefore undertakes an investigation into Joseph Schumpeter’s ‘Theory of Economic Development’, and then extends his ideas to explain the present crisis facing the modernist philosophical thought, a crisis that is also apparent in the financial services industry - a crisis that is connected to the speed-up and the intensification of the development or the entrepreneurial process. It involves an examination of the variables that affect the development process. In this respect five variables have been examined: one the aggregate number of entrepreneurs active in the market place; two, the magnitude of the entrepreneurial risks; three, the pace of innovation; four, the pace of implementation of the entrepreneurial initiative; and five the pace of change in market equilibrium following the entrepreneurial initiative. It is the combined effect of these variables that provides an explanatory logic for the speed-up of the momentum of the development process, and as a consequence the speed-up of the change in our

¹⁵The reference here is to Weber’s ‘Theory of Bureaucratic Rationality’, Marx and Engels’ ‘Manifesto of Communist Party’.

ontological conditions, hence the logic for the crisis of confidence facing the modernist philosophical thought itself, a crisis that is also apparent in the financial services industry. The question arises, is there an answer to the problem represented by this crisis¹⁶? To find the answer to the question we examine the concept postmodernism given by one of the leading prophets of the postmodern epoch, Jean-Francois Lyotard (1984b): postmodernism as modernism "in the nascent state, and this state is constant", which implies a permanently revolutionary state. Modernity, by rationalizing totalizing universal theories applicable across time and space, allowed itself to be bureaucratized and ossified, and hence lost its dynamic edge. Postmodernism is therefore modernity without its totalizing and universalizing preconceptions. The concept of postmodernism as a continuously dynamic philosophical thought, suggest a possible compatibility with Schumpeter's theory of economic development, and an avenue for examination for understanding the problems of the rapidly changing ontological conditions. This is also the message of the second part of the hypothesis which forms the kernel for the investigation of the next two chapters.

Chapter six investigates into the second part of the thesis which involves an examination into the philosophical discourse that is challenging the logic and validity of the modernist philosophical discourse: the postmodern philosophical thought. The aim is to investigate into the postmodern philosophical thought for providing inspiration and ideas that may assist us in understanding the tensions in the financial services industry. However, before one can examine the concept of postmodernism, and the ideas generated within the realm of the postmodern philosophical thought, it is necessary to unravel the confusion surrounding the label of postmodernism. This is necessary because there is no precise definition of postmodernism, and the term 'postmodernism' has been used in the media as a label for a number of phenomena. Unravelling this confusion is therefore necessary in order to have a clear sense of what one is supposed to explore. This is the theme of section two of the chapter (section one being the introduction). The exploration of the concept of postmodernism is the area of investigation of section three which also forms the main body of the chapter. The approach adopted for examining the postmodern phenomenon is to classify postmodernism into three distinct but interrelated concepts: one, postmodernism as an epoch; two, postmodernism as a reaction to, or departure from modernity; and three, postmodernism as a signifier of the problematical features or the limits of modernity. First the concept of postmodernism as an epoch. Under this concept the term 'post' implies beyond, or after - a move to a new state of things, a new 'epoch'. Postmodernism as an indicator of a period of major historical transition of our society, the end of the modernist

¹⁶The reference here is to the present crisis in modernity, and as a consequence the problem facing the discourses and frameworks based on the modernist philosophical thought. The implication being, that the problem facing the regulators in the financial services industry is a consequence of the present crisis in modernity.

epoch and the beginning of a new epoch: the postmodern epoch. Within the concept of postmodernism as an epoch, three sub-themes that underlie the concept have been examined. These are one, postmodernism as a reflection of the changes in the social, cultural, and political conditions and practices; two, a shift in the way capitalism is working; three, a departure in our way of thinking about what could/should be done about the social conditions in the new epoch. This being a part of a cultural movement that is reconceptualizing our experience. It is the dynamic interaction between these three sub-themes that form the basis of our experience of postmodernism as an epoch. The final sub-section within the theme of postmodernism as an epoch relates to the implications for the financial services industry. It involves the application of the concept postmodernism as an epoch and its underlying themes to examine the tensions in the financial services industry. All the three sub-themes discussed under the concept of postmodernism as an epoch are applicable to the financial services industry, but it is the third sub-theme: postmodernism as a departure in our way of thinking about what could/should be done about the ontological conditions, that forms the main driving force behind the discussion. Caldwell (1975) essay "Managing the Transition to Post-Modern Society" fits in with this theme and has been used as the inspiration for understanding the logic of the tensions in the financial services industry. The essence of the argument discussed under this theme is that the most crucial problem facing a society during transitory periods relates to the differential rate of change between the attitude and beliefs of the general public and private sector agencies (or the governed), and the adaptive changes in the attitudes and the operational framework of the public agencies. It is this disjunction, that is at the root of the problems facing a society during a transitory period. This logic which is also applicable to the financial services industry, is the key for understanding the tensions between the regulators and the regulated. The answer to the problem according to Caldwell, lies in the reorientation of the knowledge base of the personnel of governmental agencies. The task of the managers of the public agencies during transitional periods are: reassessment of priorities, redefinition of goals, and the creation of material and intellectual environment in which all other social institutions can play their respective roles in the transition. This requires intellectual development and the broadening of the knowledge base of the public officials. Unfortunately, however, public agencies still seem to be oriented towards quantifiable, technically oriented training. They thus risk neglecting the 'essential' through their preoccupation with the 'practical', which is unfortunate, because the tasks requiring technical knowledge (technical tasks) can be out-sourced to the private sector for whom the forces of competitive market mechanism would insure against obsolescence of knowledge. Other than intellectual broadening, another crucial requirement for managing the transition from the modern to the postmodern epoch is 'societal transparency'. To be effective, and this is very important, the knowledge base of the public agencies

should be socially shared, because in a high technology society, the most knowledgeable administrators would be helpless without informed collaborators. This requires administrators who have the intellectual honesty and self confidence that is required for sharing their knowledge base with the public. The message for the regulators in the financial services industry, is the need for the sharing of their information base with the markets to improve the market mechanism.

The second approach applied to examine the concept of postmodernism, involves the use of the term 'post' as a contrast concept that implies: postmodernism as a reaction to, or departure from modernism (or modernity) which has been described as "positivistic, technocentric, and rationalistic", and "the belief in linear progress, absolute truths, the rational planning of ideal social orders, and the standardization of knowledge and production"¹⁷. Postmodernism is, therefore, a reaction to, or departure from this mode of thinking. To understand and appreciate the concept of postmodernism as a reaction to, or departure from modernism, it is necessary to examine not only the counter-concepts that characterize this concept of postmodernism, but also the source of inspiration and the underpinnings of power of this concept of postmodernism. These are the two sub-themes¹⁸ that form the area of investigation of this section. The first sub-theme involves an examination of: one, Foucault's genealogical analysis of knowledge; and two, Derrida's deconstructive analysis of knowledge. Both these philosophers and their philosophical enterprise can be described as the source of inspiration and the underpinnings of the power of the counter-concepts that characterize the concept of postmodernism as a reaction to, or departure from modernism. Foucault's philosophical enterprise involved an investigation into the history of the emergence of 'truth games' in human sciences. The reference is to the mutual development and the reciprocal ties between 'subjectification' and 'objectification', and the consequent relationship of power between the subject and the object. The power of Foucault's discourse stems from his genealogical analysis of knowledge (savoir) which involves one, his painstakingly detailed archaeologies of knowledge and two, the sheer genius of Foucault the genealogist to apply the information revealed through his archaeological research to create a knowledge of knowledge¹⁹. The power of Foucault's genealogical discourses, relates to their ability to neutralize the power that the scientific discourses acquire through the hierarchization of knowledge, power that they acquire through the subjugation of local disqualified knowledge and the historical contents of their own emergence and evolution. Foucault's

¹⁷Harvey (1992, pp.9).

¹⁸One, the counter-concepts and two, the source of inspiration and the underpinnings of power of the counter-concepts.

¹⁹Knowledge is taken apart and rearranged with the aim of controlling knowledge, rather than allowing it to control him.

genealogical discourses allow one to release oneself and one's intellect from the mental prison which knowledge based on universal and global discourses represent, and to take control of the knowledge rather than allowing knowledge to take control of one's intellect. Derrida's philosophy is very different from Foucault's because he attacks the metanarratives internally, he lays out the problematical nature of the metaphysical concepts. The significance of Derrida's philosophy is that Derrida refuses to grant the philosophers the privileged status that they have always claimed as the sovereign dispensers of reason. Derrida confronts this 'will to power' of the philosophers by deconstructing their texts. He argues that philosophers have been able to impose their various systems of thought only by ignoring or suppressing the disruptive effects of language. Derrida therefore picks out these effects by skilfully unpicking the elements of metaphor and other figurative devices at work in the philosophical texts. Derrida's deconstruction therefore acts as a liberating force in the sense that it allows one to take cognizance of the rhetorical nature of the philosophical arguments. It allows one to interrogate the rhetoric of closure, and lay out the problems that have merely been repressed or displaced rather than resolved. Derrida describes deconstruction as "an analysis which tries to find out how their thinking works or does not work, to find the tensions, the contradictions, the heterogeneity within their own corpus". Deconstruction therefore finds itself at the heart of what one calls 'tensions'. It is a question of assuming these tensions, of 'living' them as much as of 'understanding' them. Through his method of deconstruction Derrida makes a very important and positive contribution to our knowledge. By laying out the problematical features of our knowledge which we assume as truth, he helps in opening the gateway for the generation of new knowledge, as Derrida himself points out: "I try to dismantle not institutions but some structures in given institutions which are too rigid or dogmatic or which work as an obstacle to future research".

The second sub-theme associated with the concept of postmodernism as a reaction to, or departure from the modernist philosophical thought involves an examination of the counter-concepts that characterize this concept of postmodernism. The counter-concepts (to be) examined covers eight key areas that form the basis of our ontological assumptions. These are: **one**, the problematic of disciplinary research; **two**, the concept of representation; **three**, relationship between the author, the text, and the reader; **four**, the concept of subject; **five**, the concept of truth; **six**, the concept of theory; **seven**, the concept of history; and **eight**, the concept of space. Following an examination of the counter-concepts that characterize the concept of postmodernism as a reaction to, or departure from modernism, the final section of exploration under the theme involves the application of the ideas derived from the counter-concepts to examine and understand the tensions in the financial services industry.

Postmodernism as a signifier of the problematical features or the limits of modernity is the third approach applied for the investigation into the concept of postmodernism. This approach characterizes postmodernism as a concept that goes beyond modernity in the sense that it points to the limits of modernity. Here the term ‘post’ implies a reflection on modernity, i.e. ‘modernity becoming conscious of itself’. Postmodernity (or postmodernism) is therefore, modernity emancipated from its fake consciousness. Intellectuals now realize that you cannot lay out rules and standards with reference to some universal truth. Postmodernity therefore implies a renunciation of the idea of constructing a perfect rational society governed by experts. The implication is, intellectuals and experts should accept a more modest role of interpreters and brokers of culture and knowledge, to help communities understand each other. The application of postmodernism to the social sciences does not seek to ‘improve and perfect’ the social sciences, rather it attempts to make their underlying assumptions explicit, and undermine their foundational claims. This approach incorporates the works of philosophers and academics who find the project of modernity to be deeply problematical, whose endeavour is to lay out the problematical facets of modernity, while at the same time also making an effort to explore and understand the social and political codes and practices like tradition, ethnicity, etc., which were ignored and rejected by modernity (whose aim was to homogenize the social in line with the meta-discourses of the philosophers and social theorists). This approach (i.e. postmodernism as a signifier of the problematical features or the limits of modernity) is significant because it provides us the stepping stone to examine the texts of the French philosophers like Foucault, Lyotard, and Derrida, whose philosophical works brought to light the problematical features of the modernist philosophical thought, and as a consequence stimulated the development of the postmodern philosophical thought. The next chapter therefore which continues with the investigation into the second part of the hypothesis (which was also the inspiration for this chapter) by exploring the philosophy of Jean-Francois Lyotard, Michel Foucault, and Jacques Derrida.

Chapter seven continues with the investigation into part II of the hypothesis. The story line of this chapter involves an exploration into the philosophy of three of the most important philosophers of the postmodern philosophical thought (especially in the context of the hypothesis under investigation): Jean-Francois Lyotard, Michel Foucault, and Jacques Derrida. **Jean-Francois Lyotard** is best known for his philosophical work ‘The Postmodern Condition: A Report on Knowledge’ which is regarded as a pioneering work for introducing the concept of postmodernism in philosophy and social science. This work is important because it is a report on knowledge. It involves an examination of knowledge itself, its forms, and its problematical features. It introduces us to the framework of language game as a tool not only for understanding and examining the social bond, but also for understanding and appreciating the problems of the present era. Lyotard’s essay

is important because it introduces us to a number of important facets of the postmodern philosophy; one, the idea of postmodernism as modernism at a nascent stage and this stage is constant, implying a permanently revolutionary mode of philosophical thought. A postmodern philosopher is analogous to the Schumpeterian entrepreneur, but in the intellectual and not the economic realm. He creates a discontinuity in Kuhn's paradigm leading to a paradigm shift in our knowledge; two, the concept of postmodernism as incredulity towards metanarratives, a development that reflects an internal erosion of the legitimacy principle of knowledge, which itself is connected to the development of the criteria of performativity which has become the basic criteria of the operations of the market forces; three, the idea of society as a language game, a concept that has been developed by combining the concept of language as the basis of social bond and the concept of game theory, to explain the actions of the players or the participants in the language game. The concept allows us to appreciate and understand the different forms of statements, for example: denotative, prescriptive, evaluative, performative, etc., and their possible implications in terms of the possible counter-move by the receiver of the statement. It could either be merely reactional in which case it has no effect on the language game, or it could be an unexpected counter-move that disorients the system: a phenomenon described by Lyotard as the agnostic aspect of the society. Lyotard's framework of language game and the agnostic aspect of the society allows us to visualize the situation in the financial services industry where the regulatory dialectic is a reflection of the agnostic counter-moves of the financial institutions (the regulated). This framework also provides an explanatory logic for the materialization of the gradual change in the regulatory framework and regulatory philosophy that we are experiencing, the most conspicuous of which is the pre-commitment approach, which involves a change from a prescriptive approach to a performative approach towards regulation. The concept of language game also allows us to understand the contrary effect of the prescriptive approach towards regulation and its connection with terror as the basis for its application. Terror destroys the language game. The concept of the language game, also allows us to appreciate the beneficial effects of a possible change in regulatory strategy change from prescriptive to evaluative approach towards regulation, which would imply increased importance of qualitative supervision. It would also imply the introduction of an element of performativity into the regulatory game. But to achieve the desired effect on the market's self regulatory mechanism, it is essential that the results of the supervisory evaluation be shared with all the market participants. The fourth facet of Lyotard's works that comes under examination relates to the problematic nature of the theories of social science. There are two aspects of the problem, one relates to the blind use of the theories of natural science to the problems of social science. The problem has been described by Lyotard as the difference between God playing dice or bridge. While in the former case statistical probability may be able to provide a fairly

accurate answer, this, however, is not true for the latter case, where the referent is not nature but human being who is a creative animal. Hence the rationale for the use of the metaphor of 'bridge' instead of 'dice' for the latter case. The other aspect relates to the assumption of nation-state as a closed system - a notion that finds its basis in the laws of thermodynamics. This notion is problematical because: one, it encourages totalitarian thinking; and two, it encourages simplification and reductionism in modelling reality. The final aspect of Lyotard's essay that has been discussed relates to paralogy and not consensus as a source of inspiration for the future. Paralogy emphasizes on dissention and search for the unknown rather than the known thereby encouraging us to think differently, think creatively. This is also the message of Lyotard's philosophy for the regulators.

Michel Foucault's philosophical enterprise has already been introduced in the context of the discussion on the concept of postmodernism as a reaction to or a departure from modernism. Here the area of his philosophical enterprise that comes under investigation relates to his works on the problematic of power: the different forms of power - power that is connected to the truth of law, power that is connected to repression, power that is connected to knowledge, power that is connected to our bodies and their use etc., and its implications for understanding the tensions in the financial services industry. The discussion is divided into three main sections: one the circular relationship between truth and power, which implies that we either submit to the power of truth, or acquire power by producing discourses of truth; two, the underpinnings of his discourse on power, which is based on an examination of the actual practices or the application of power, rather than the juridical edifice of power. It focuses on power at the point of application; power which circulates like a net or a chain in which human beings act as a link, not only exercising power also being subjected to power. In the context of the tensions in the financial services industry, Foucault's message is quite explicit, instead of emphasizing on the legal framework of regulations, we should concentrate on its application. This implies the need for a change in emphasis from regulation to supervision. The third aspect of Foucault's philosophy discussed relates to the various forms of power, of which the two most important ones are sovereign power and disciplinary power. The power of the regulators is based on sovereign power, with law as the instrument for the application of sovereign power. The basis of power of the financial institutions (the regulated), on the other hand, is disciplinary power which is connected to knowledge and the apparatuses of knowledge. In the context of the financial services industry, the dialectic of power between the regulators and the regulated is actually the personification of the dialectical relationship between sovereign and disciplinary power. An aspect of critical importance that comes under discussion in the investigation is that the regulatory codes in the financial services industry are actually codes of normalization that were a part of (or instruments of) disciplinary power, which at a particular time in history were incorporated into the

legal codes. The incorporation of codes or rules of normalization into the legal code creates a number of problems. One avenue for bridging this problem is the supervisory tool of bank examination, which itself is a form of disciplinary power. But to have the desired effect, it needs to be combined with another form of disciplinary power: the principle of ‘panopticon: power through transparency’, which implies the need for the regulators to share the result of their bank examination with the general public.

Jacques Derrida is the third philosopher whose philosophy is explored. Two approaches were applied to examine his philosophy: one, the concept of deconstruction in the broad sense, i.e., as a philosophical thought where the aim is to achieve new enlightenment by questioning the axioms of old enlightenment, where the emphasis is on the opening up the text to reveal the tensions, in an effort to examine and understand them. This is also the aim of the thesis. Hence the rationale for the use of the term ‘deconstruction’ in the title of the thesis. The second approach involves an examination of the concept of deconstruction in the narrow sense - deconstruction as the strategy that Derrida applies to reveal the tensions in the texts of other philosophers, where the aim is open up the closures in the text to reveal the precariousness of the discourses that were revered as truth. Included within this approach is an examination of the mechanisms of Derrida’s deconstruction strategy involving the application of the concepts of ‘supplementarity’ and ‘differance’ where the emphasis is on the problems with the language in conveying meaning. In the context of the tensions in the financial services industry, the mechanics of Derrida’s strategy point to the problems with accounting as a language (the language of finance) in conveying meaning. It cautions us that the bottom line figure like capital, assets, liabilities, profits, loss, etc., should not be accepted as statements of truth. They should be placed under erasure, crossing them but allowing them to be legible, thus undermining their truth value. The message for the regulators and the users of financial statements is that accounting is also a language, we should not believe in the bottom line figures as statements of truth, we should deconstruct them in order to reveal the tensions underlying those statements.

The Problematic of Time and Space Compression: This is the theme of part IV of the thesis which is covered in two chapters. It involves an investigation into the problematic of time and space compression and its connection with the tensions in the financial services industry. The rationale for this part of the thesis is two fold: one, an examination of the concepts of time and space compression, and their ramifications especially in the context of the tensions in the financial services industry. The second rationale is related to the problematic nature of our conventional concepts of time and space themselves, which hinder rather than help us in understanding the problems of the

time and space compression, let alone facilitate us in developing a policy or a strategy for overcoming them, thus implying the need for reexamining them. Hence the rationale for examining alternate concepts of time and space for providing new insights for understanding the phenomenon of time and space compression, and its consequences. In order to give equal importance to the dimensions of time and space, each of these has been allocated a separate chapter.

Chapter eight examines the problematic of temporal compression and the tensions in the financial services industry. The discussion in the chapter has been covered under two main themes. The first theme relates to the problematic of temporal compression and its ramifications for the regulators in the financial services industry. Two approaches have been applied to examine this theme: one, the concept and the consequences of temporal compression 'at a point of time'. This approach examines the consequences of the speed-up or the intensification of our economic processes for the policy makers of nation-states in general, and the regulators in the financial services industry in particular. This includes increase in volatility and ephemerality, reduction in profit margins, reduction in time for decision making, increased risk of business failure, reduction in time for undertaking correcting action to control problems, etc.. The second approach examines the concept and the consequences of temporal compression 'over a period of time'. This approach examines the consequences of the speed-up of the change in our ontological conditions over a period of time. This approach focuses on the rationale for temporal compression 'at a point of time'. This facet of temporal compression is associated with the speed-up of the processes of knowledge generation, innovation, and entrepreneurialism all of which contributes towards the increase in the momentum of the development process and the increase in the discontinuity of the temporal flow. This approach brings to the fore the problematical nature of our mechanical concept of clock time which hinders, rather than helps us in understanding the phenomenon of temporal compression and its consequences, Hence the rationale for a reexamination of our concept of time, which is the second theme explored in this chapter. Theme two of this chapter involves an exploration into some of the alternate concepts of time in an effort to understand the tensions in the financial services industry. Within this theme, two alternate concepts of time have been examined: one, the dialectical concept of time which involves a combination of the concepts of the clock time, the social time, and the biological time into a holistic concept of time. This concept allows us to understand the dynamism of change that the concept of time represent, and the problems that arise when a static framework is imposed on the society or any societal group. The second concept of time examined relates to the concept of temporal awareness or social time. It involves an examination of Gurvitch's (1964) framework of social time to investigate into: one, the social time that is representative of the ontological conditions prevailing in the financial services industry; and two, the social times that are representative of the

attitudes and operational framework of the regulators and the regulated (financial institutions). Gurvitch's framework of social time is important because it brings to the fore the disjunctions in the temporal awareness of the regulators and the regulated, which are at the root of the tensions in the financial services industry. The overtone being the need to address this issue of disjunction in temporal awareness/social time, if the tensions in the financial services industry are to be controlled.

The aim of chapter nine is to examine the tensions in the financial services industry in the context of the problematic of spatial compression. The area of investigation of this chapter has been divided into two main themes. The first theme relates to the problematic of spatial compression and its ramifications for the regulators in the financial services industry. The discussion on this theme begins with an examination of the concept and the consequence of globalization, and then moves on to a more specific investigation into the concept and consequences of spatial compression. Although the concepts of globalization and spatial compression imply the same meaning, and are used synonymously, but here they have been discussed separately, because of the difference in the approach adopted to examine the phenomenon. While the emphasis in the discussion on globalization is on the concept and its implications, the emphasis of the discussion on spatial compression on the other hand is on explaining the basis of the phenomenon of globalization. The second major theme covered in this chapter relates to the inadequacy with the Cartesian concept of physical space in terms of allowing us to take cognizance of the dynamics of the change and the consequences of the change we are experiencing (spatial compression). This is an important reason for the tensions in the financial services industry. Hence, the rationale for a reevaluation of the concept of space. This is also the basis for examining Henri Lefebvre's concept of 'social space'. Lefebvre combines the space occupied by the sensory phenomenon, with the mental space, and most importantly, the space of social practice, to develop a single holistic concept of space, the concept of 'social space'. Metaphorically speaking, unlike the modernist concept of space which can be described as the 'stage' or the 'theatre' for the staging of the human drama, Lefebvre's concept of (social) space includes, not simply the stage or the theatre for staging of the drama (physical space), but also the actors, their intellect (covering the realm of mental space incorporating their knowledge, their ideas, and their imagination) and the products of their intellect, their relationship with the other actors, and their act (both individual and collective). The significance of social space as concept relates to its utility as a tool not only for analyzing and understanding the change we are experiencing (the phenomenon of globalization), but also for understanding and appreciating the consequences of the globalization, and has therefore been examined in detail. The concept not only allows us to take a holistic view of the space 'at a point of time', but also allows us to understand the 'process of change of (social) space over a period of time'. These two facets of the concept of social space have therefore been

examined in detail. First, the process of change in space across time: a phenomenon which Lefebvre refers to as 'production of space'. The concept of production of space implies that space is not static, it is forever in the process of evolution and change. It also points to the dynamism and creative capacity embedded within the concept of social space. The concept of 'production of space' is the key to understanding of the process of change in space of the financial services industry, and the consequences emanating from the change for the regulators. Lefebvre's thesis of production of space is important because it draws attention to the flexibility and dynamism inherent in the space of the financial institutions (regulated entities), and the inability of the regulators to alter their regulatory framework to commensurate with the scale and scope of the activities or the structure of the business organization of the regulated. The second facet of Lefebvre's concept of social space relates to an examination of space 'at a point of time' where the area of investigation relates to the 'organization of space'. Lefebvre's concept of social space allows us to go beyond the concept of simple physical space, incorporate the users of the space, and the rationale for the use of the space (by them), into the concept of social space, thus allowing us to visualize space and the organization of space in a completely new light. Social space can, therefore, be visualized as encompassing a number of networks with material underpinnings whose primary purpose is to facilitate communication/relationship between the subjects. These networks may include geographical features like roads, railways, air routes, sea routes, etc. that serve communication based on physical movements of subjects (human beings) and their material goods. These networks may also include electronic channels of communication like telephones, intranets, internet, electronic exchanges, television, radio, etc., that serve communication based on information transfer between the subjects. Each of these spaces are incorporated into the concept of social space, because the basis of their existence is to serve human interaction, and to foster human relationship. Unlike the concept of physical space which induces us to visualize space as a 'thing' bounded by physical boundaries that can only be organized by segregation and fragmentation, Lefebvre's concept of social space, organized as a network of social relationships induces us to visualize space as a 'phenomenon' that can be examined and studied with the view of discovering and exposing the actual organization of space. The significance of this concept relates to its utility as a tool for examining and understanding the organization of space of an abstract phenomenon like the space of capitalism, as well as a real phenomenon like the space of the marketplace. The concept can also be applied to understand and analyze the organization of space of a market participant (for example a financial institution), as well as that of the political forces (this includes governmental agencies like financial services regulatory agencies) that try to control the operations of the markets and the market participants. The concept of social space allows us to understand and appreciate the disjunction in the organization of space

by the regulators and the regulated. Unlike the financial institutions whose space is organized as a hierarchy of geographical and functional networks spanning a number of markets, the organization of the space of the regulators is encumbered by the limitations of physical space (whose principle of organization is segregation and fragmentation). When we combine this disjunction with the earlier discussed disjunction related to the production of space (unlike the regulators whose space is static, the financial institutions are actively involved in managing their space to take advantage of the market opportunities), the logic for the tensions in the financial services industry become apparent. These disjunctions are direction flags which have been examined in the conclusion to draw inferences and to understand the tensions in the financial services industry.

The overall aim of the thesis is metaphorical: The aim is not to solidify metaphors to achieve the semblance of truth, but to provide a different approach for visualizing the problems in the financial services industry.

PART

II

TENSIONS IN THE FINANCIAL SERVICES INDUSTRY

CHAPTER TWO

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The EU Directive on Deposit Insurance: A Critical Evaluation

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1. Introduction

The recently approved EU Directive on Deposit Guarantees (1993) seeks to influence the distribution of power between banks and their depositors, on the one hand, and between national regulatory authorities and the European Commission, on the other. Under the Directive, depositors will be guaranteed a minimum level of protection against the undesirable outcomes of asset allocation decisions taken by bank managers who, by virtue of their monopoly of information concerning the bank's portfolio, have greater power than the depositor. The implementation in the Directive of this protection involves the setting of minimum standards of coverage. In so doing, it gives wide latitude to national regulatory authorities in satisfying the minimum standards. This clearly reflects the principle of subsidiarity which characterizes the current philosophy of the EU. The purpose of this article will be to argue that incentives induced by the Directive for both depositors and banks are incompatible with the aim of national supervisors and the EU to foster a stable and efficient financial system. It is likely that both competitive distortions and an increase in financial fragility will occur as the Directive is implemented.

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In the next section of this article we will identify some of the key features of the Deposit Guarantee Scheme, together with those in the US, UK and Germany. Then three interrelated issues will be explored:

- the problem of moral hazard and the principle of co-insurance, requiring depositors to bear (in some instances) losses arising from bank failure;
- the principle of bank safety net procedures and the relationship between the Deposit Guarantee Directive and other financial market directives, especially the Bank Solvency Directive;
- the principle of subsidiarity which leaves the implementation of the Directive in the hands of national authorities, subject to minimum standards.

2. Background

The history of commercial banking is fraught with failure. Many trace the origins of banking back to the activities of London goldsmiths who offered to provide 'safe havens' for their customers. The goldsmiths soon realized that they could create loans against their customers' deposits. However, poor lending practice led to the failure of many goldsmiths and losses for their depositors. In the period leading up to the American Civil War, traders had to carry a manual to help them distinguish between the banknotes of failed and solvent banks. Prior to the Great Depression, thousands of banks were failing each year. This ceased with the creation of the Federal Deposit Insurance Corporation (FDIC) in 1934. In the opinion of Friedman and Schwartz, this 'was the most important structural change in the banking system to result from the 1933 panic and, indeed in our view, the structural change most conducive to monetary stability since state bank note issues were taxed out of existence immediately after the Civil War' (1963, p. 434). Paradoxically, today it is this guarantee of a safe haven for depositors that is being blamed for undermining the US financial system. It is argued that, since banks are not subject to the discipline of potential deposit withdrawals, they will seek to take on high-risk/high-return portfolios of assets. This is the classic 'moral hazard' problem: the existence of deposit guarantees creates an environment which provides incentives for a bank to take actions which lead to the exercise of the guarantee. This is one of the issues that we will seek to examine in detail in Section 3.

Interest in a European Union deposit guarantee scheme was first expressed towards the end of 1985 in 'the proposal for a Council Directive on the coordination of laws, regulations, and administrative provisions relating to the reorganisation and winding up of credit institutions (185/C356/10 [Com (85)

788 Final]). The Commission recommendation concerning the introduction of deposit guarantee schemes in the Community came a year later on 22 December 1986 (87/63/EEC). This recommendation laid out the basic requirements for such schemes and set up a deadline of 1 January 1990 as the time limit for all the EC Member States to set up and enforce deposit guarantee schemes within their territories. By then only six of the 12 Member States had any deposit guarantee schemes. These were Belgium, Germany, Spain, France, Netherlands, and the UK. Three members, namely Italy, Ireland, and Portugal already had plans for such schemes, while the remaining three had not even reached planning stage. By September 1993 when the Directive was finally accepted, only Greece had not implemented a deposit guarantee scheme. (A comparison of the characteristics of different national schemes is shown in Table 1.)

The specific objectives of the EC Deposit Guarantee Directive (CEC 1992c, p. 2) are:

1. to protect depositors; and
2. to reduce the fragility of the financial sector.

The issue of moral hazard has figured prominently in the discussion leading up to the adoption of the Directive. In explanatory notes, published when the Directive was proposed, concern was expressed that the 'minimum level of coverage set for the Community should not be too high in order to avoid what has occurred in the United States in particular, where the risks taken by individual depositors have been lowered so much that such depositors have become virtually indifferent to the soundness of their credit institutions' (1992c, p. 5). It is claimed that the proposed Directive has been structured in such a way as to take into account the 'anxieties, in particular of economists and financial experts who would like part of the risks to be borne by depositors, in order to encourage them to take an interest in the soundness of the institution to which they entrust their deposits' (1992c, p. 15). It appears that the Directive places more emphasis on the moral hazard problem than on the stability of the financial system (the philosophy behind the creation of the FDIC). In our opinion, however important the moral hazard problem may be, it alone cannot be the basis upon which bank safety net procedures are designed and implemented. A firm understanding of the role of banks in the economy and of the relationship between depositors, bank management, bank shareholders and the regulators is required. These relationships will be discussed in Section 3.

The key features of the Directive are noted below. There is clear emphasis on setting minimum standards in such a way that depositors also share in banking risks.

1. Home country principle – the scheme envisages a *home* country dep-

Table 1

Country (in local currency)	Coverage of Protection Extended to:			Deposits in Dom. br. of Foreign Banks	Deposits in Dom. br. of Foreign Currency	Deposits in Dom. Banks	Memb. Compulsory or Voluntary Scheme	Comp. by Deposit or Depositor	Funding Contribution or Commitment to pay	Preventative Action by Dep. Scheme Prior to Liquidation
	Maximum Compensation Limit (in ECU) (23.9.93)	Deposits in Foreign Banks	Deposits in Foreign br.							
EC:										
Belgium	BF 500,000	12,222	No	Yes	Yes	Yes	Private	Compulsory	Depositor	Contribution
Denmark	DKR 250,000	32,155	Yes	Yes	Yes	No	Public	Compulsory	Depositor	Yes
France	Fr 400,000	59,950	No	Yes	Yes	Yes	Private	Compulsory	Depositor	No
Germany	30% of bank's own funds		Yes	Yes	Yes	No	Private	Voluntary	Depositor	Yes
Ireland	< £5,000 – (80%)		No	Yes	Yes	No	Public	Compulsory	Depositor	Yes
	5000 to 10,000 – (70%)									
	10,000 to 15,000 – (50%)									
	Max coverage If 10,000	12,155		Yes	Yes	Yes	Private	Voluntary	Depositor	Contribution
Italy	< Lira 200 M – (100%) 200M to 1B – (75%)			Yes	Yes	Yes	Private	Voluntary	By deposit	Commitment
	Max coverage Lira 800M	431,055								
Luxembourg	LF 500,000	12,222	Yes	Yes	Yes	No	Private	Compulsory	Depositor	Commitment
Netherlands	Hfl 40,000	18,600	Yes	Yes	Yes	No	Public	Compulsory	Depositor	No
Portugal	< ESC 1.5M – (80%) 1.5M to 3M – (60%)		Yes	Yes	Yes	No	Public	Compulsory	Depositor	No
	Max coverage Esc 2.1 M	10,705								
Spain	PTA 1.5M	9,799	Yes	Yes	Yes	No	Public	Voluntary	Depositor	Contribution
UK	£20,000 – (75%)	19,364	No	Yes	Yes	No	Public	Compulsory	Depositor	Yes
	Max coverage £15,000/-									No
Non EC:										
Austria	OS 200,000	14,844	Yes	Yes	Yes	No	Public	Compulsory	Depositor	Commitment
Canada	C\$ 60,000	38,773	No	Yes	Yes	No	Public	Compulsory	Depositor	Contribution
Finland	UNLIMITED	–	Yes	Yes	Yes	No	Public	Compulsory	Depositor	Yes
Iceland	UNLIMITED	–	Yes	Yes	No	Yes	Public	Compulsory	Depositor	Yes
Japan	Yen 10M	80,261	No	No	No	No	Public	Compulsory	Depositor	No
Norway	UNLIMITED	–	Yes	No	Yes	No	Public	Compulsory	Depositor	–
Switzerland	SFR 30,000	17,985	Yes	Yes	No	No	Private	Voluntary	Depositor	Contribution
USA	\$100,000	85,398	No	Yes	No	No	Public	Compulsory	Depositor	Commitment
										Yes

Source: Survey on Deposit Insurance Guarantee Schemes, Banking Supervision Committee, Fédération Bancaire de la Communauté Européenne, February 1992.

Notes to Table 1:

1. In the deposit insurance/guarantee scheme for Denmark, although the limit has been specified as DKR 250,000, there is no limit for: (i) long-term depositors like pension fund accounts, (ii) trust accounts, and (iii) deposits by lawyers of clients' money.
2. For Iceland, although unlimited compensation for the depositors has been specified. Actually the total compensation to depositors is limited to four-fifths of the total assets of the insurance.
3. In the case of Belgium, if a branch of a foreign bank is covered by home country deposit guarantee which is lower than Belgium's (host country) guarantee cover, then host country top-up is provided.
4. In the case of Italy, foreign branches were invited to join the host country scheme, which they did not.
5. In the case of deposit protection for foreign branches of domestic banks, the Belgian scheme covers only that portion of deposits not covered by the host country scheme which is lower than the Belgian limit. The Italian and Danish schemes cover branches if they are not covered by the host country scheme.
6. The deposit insurance/guarantee schemes of Ireland, Italy, Portugal and UK have an element of co-insurance. The figures in brackets indicate the extent of deposits guaranteed by their respective schemes. For example, in the case of Ireland 80 per cent of the first £5,000, 70 per cent of the amount between £5,000/- and £10,000, and 50 per cent of the amount between £10,000 and £15,000 is guaranteed. The maximum total coverage is therefore £10,000/- (0.8*5000 + 0.7*5000 + 0.5*5000).

osit guarantee scheme to cover the depositors not only in home banks but also a branches in other Member States. However, until 31 December 1999, the cover in the foreign branches is to be limited up to the maximum level and scope offered by the corresponding system in the *host* Member States (1993, Art. 4.1). For foreign branches with a lower level of guarantee coverage than the host country, a top-up option has also been provided whereby the host member country will provide additional coverage to cover the competitive disadvantage of the foreign branches (1993, Art. 4.2). The effect of these provisions will be to avoid competitive distortions in each Member State, while allowing a disparity to continue on a community-wide level.

2. While the Directive requires obligatory membership in a deposit guarantee scheme, it does allow an exception for credit institutions which belong to a system which protects the credit institution itself as well as its liquidity and solvency (1993, Art. 3.1).
3. The minimum limit or floor level for the deposit guarantee has been set at ECU 20,000. However, for a transitional period up to 31 December 1999, a lower floor of ECU 15,000 has been allowed for countries with a limit lower than ECU 20,000 (1993, Art. 7.1). No upper limit on the compensation has been proposed, which means a huge disparity would exist between the German and the Italian schemes and that of the rest of the EU members (see table).

4. An option for co-insurance has been allowed at the discretion of the member countries. The minimum limit imposed by the EU is 90 per cent of deposit or ECU 20,000 whichever is lower (1993, Art. 7.4). In other words, depending upon their country's implementation, depositors may have to co-insure 10 per cent of the deposits themselves, plus any excess over the national limit. This lower limit applies to the aggregate of deposits with the same institution irrespective of the number of deposits, their currency of denomination and location within the country.
5. The Deposit Guarantee Scheme is activated when deposits become unavailable. The scheme is thus concerned with an illiquid bank rather than an insolvent one. In general, the two conditions will be uncorrelated.
6. Interbank deposits, own funds obligation (subordinated debts) and money laundering transactions have been excluded from the coverage of the guarantee scheme. Additionally a listing of the type of deposits which may be excluded or granted a lower level guarantee by the Member States has been provided in Annex 1 of the Directive. This list pertains mainly to institutional deposits. It excludes from coverage deposits denominated in currencies other than those of Member States or the ECU.
7. For branches of banks with head offices in third countries (non-member countries), the guarantee cover should be equivalent to that provided in the Directive; otherwise these branches are required to join the host country's scheme (1993, Art. 6.1).
8. Details and the extent of guarantee coverage are required to be provided to existing and new depositors. However, this information may not be used as an advertising strategy to achieve a competitive advantage over the rival bank having an inferior guarantee scheme (1993, Arts. 9.1, 9.2, 9.3).
9. A time limit of three months from the date of unavailability of deposits has been specified for banks to draw up a list of deposits to be covered and be in position to pay duly verified claims. Extension of this time limit has however been allowed for exceptional circumstances.
10. Two major items not in the Directive on Deposit Guarantee scheme are:

- (a) Legal status of the guarantee scheme – private as well as public sector deposit protection schemes have been allowed subject to the choice of the bank and the acceptability of the national supervisor. Alternative guarantee arrangements not recognized by the supervisory authorities may also be allowed if the supervisory authorities consider it to be at least

equivalent to the level of protection offered by the officially recognized schemes.

(b) Funding procedures – no specifications have been made as to whether the scheme is funded or not, i.e. whether or not a guarantee fund is to exist. Further, there is no provision for the method of funding, i.e. whether there should be a fixed premium, variable premium or no premium at all. In the last case, the guarantee scheme would be funded by commitments to pay if and when the need arises.

Existing implementations of deposit guarantee schemes in the UK, Germany and US take different approaches to the bearing of the risks inherent in banking. In philosophy the Deposit Guarantee Directive is closest to the current UK scheme. The latter was motivated by the secondary banking crisis of 1973–75 and came into force in 1982. The scheme centres on the principle of co-insurance. The coverage of UK deposit guarantee is limited to 75 per cent of the deposit up to a maximum of £15,000 (75 per cent of £20,000). Only retail deposits denominated in sterling are covered. This approach is totally different from the German deposit guarantee scheme, as German supervisors believe that the moral hazard problem can be handled by supervisory action. That is supervisors may take action to ensure that capital is adequate and monitor loan portfolios in order to ensure their soundness. Germany therefore rejects any reliance on depositor discipline via co-insurance and a fixed ceiling on coverage (Deutsche Bundesbank, 1992, p. 35). Under the German scheme, coverage is limited to 30 per cent of the liable capital of the bank per depositor. This has led the Bundesbank to comment that depositors 'are as a rule protected in full'. Thus in the case of the failure of BCCI, German depositors received the full value of their funds, whereas depositors at BCCI in the UK have been eligible for only a proportion. However, there is one potential weakness in the German scheme. A deposit guarantee scheme will be implemented when the bank is near insolvency and hence the actual value of capital will be near zero. Thus, for there to be effective implementation, the scheme must be activated when the bank is still solvent and its capital sufficiently positive to justify payments to depositors. The banks pay a flat premium (0.30 per cent) into a private scheme funded and operated as a co-operative by the banks. The premium may be raised or lowered and could even be eliminated if the supporting fund had reached a level considered to be reasonable.

Until 1992, the programme operated by Federal Deposit Insurance Corporation (FDIC) in the US offered coverage limited to \$100,000 and cost banks a flat rate premium to participate. This flat rate has now been replaced by a risk-related schedule. This is shown as Table 2. There are nine categories of banks depending upon whether they are adjudged to be well capitalized, adequately

Table 2. Assessment Rate Schedules, Second Semi-Annual Period, 1993
(Basic Points)

1. Bank Insurance Fund – Member Institution:

<i>Capital Group</i>	<i>Supervisory Subgroup</i>		
	A	B	C
1. Well capitalized	23	26	29
2. Adequately capitalized	26	29	30
3. Under-capitalized	29	30	31

capitalized or under-capitalized. Within each category, banks are divided into three groups: A, healthy; B, supervisory concern; C, substantial supervisory concern. The link here between the guarantee premium and capital adequacy is important since the greater the capital asset ratio of the bank, the smaller the probability of insolvency and any drawing upon the guarantee fund. By introducing a risk-related premium schedule, the FDIC is providing an incentive for banks to be well capitalized.

3. Moral Hazard and the Principle of Co-Insurance

The existence of safety net procedures for banks arises from the fact that banks in their pursuit of profit may act in a manner that imposes costs on other sectors of the economy and society as a whole. In the language of economists, there exist interdependencies or externalities which are not captured in the operation of markets. When this occurs, it is argued that economic efficiency can be improved through some form of government intervention, regulation and/or supervision. In the case of the banking industry there are several such interdependencies.

First, the cheque accounts at banks are used as media of exchange. Thus a bank failure affects the ability of depositors to undertake transactions if there is less than comprehensive protection. In addition, a call on loans by the receivers of a failed bank could drive the borrowers themselves into insolvency and hence lead to a further contraction in economic activity. The knock-on effects of bank failure can be substantial.

Second, given the uncertainty that inevitably characterizes the financial system, especially the fact that depositors know that they possess less information than bank management, the failure of one bank can generate contagion effects throughout the system. Depositors may extrapolate from the perform-

ance of one bank and seek to withdraw funds from perfectly safe institutions. In other words a 'run' would develop. A bank that fails to meet its obligations generates an external diseconomy into the entire banking system by reducing public confidence in the system as a whole. The key factors are quality and uncertainty. Failure of one bank leads to uncertainty as to the quality of other banks. The situation is analogous to Akerlof's (1970) famous analysis of the second-hand car market. In a world of asymmetric information, the price of 'lemons' (i.e. poor quality cars) determines the average market value for all cars. Similarly, depositor perceptions of the widely publicized problems of weak banks will influence their valuation of all banks. That is, the strongest banks will be undervalued. The existence of safety net procedures minimizes the effects of the asymmetric information and the resulting external diseconomy.

Third, the fundamental *raison d'être* for financial intermediaries in general, and commercial banks in particular, is their ability to gather and interpret investment information more efficiently than individual households or firms. Leland and Pyle (1977) refer to this as 'signal extraction'. In other words, banks have a comparative advantage in the gathering of information and hence enable greater economic specialization and efficiency than would be the case if individual lenders directly shouldered the credit risks inherent in lending activities.

However, the existence of financial institutions does not mean that risks are eliminated (for a discussion of the various risks, see Short, 1978). First, no matter how good their credit assessment and portfolio management procedures are, no bank can completely eliminate credit risks. Second, since banks fund their assets through the creation of liquid liabilities they are also subject to funding risks, especially in an institutional environment which is prone to runs. Third, they are exposed to the risks of leverage: the higher the deposit-capital or equivalently the asset-capital ratio, the greater the probability of bank failure. The capital or shareholder equity of the bank acts as a buffer stock which protects the bank, its shareholders and depositors against unforeseen declines in the value of the bank's assets. Fourth, because banking is predicated on the ability to gather and process information, the uninformed depositor may suffer from fraud or incompetent management, simply because of an inability to monitor.

Safety net procedures do not eliminate risks from the financial system. They simply shift the burden from one group or groups to others. As already noted in Section 2 of this article, it is this burden shifting which is of central concern to the authors of the Deposit Guarantee Directive. There is concern that the existence of a deposit guarantee or other procedures will induce incentives on the part of the bank to increase its risk-taking activities. Hence, there is the explicit desire, as noted in the introduction to this article, to encourage

depositors to increase their monitoring activities. This is achieved in the Directive by allowing national authorities to require that depositors bear some of the risks associated with the bank's balance sheet. If only some depositors are covered, those not covered will have the incentive to 'run' whenever there is some real or perceived problem at their bank. When failures occur, the deposit guarantee fund is placed under pressure and this in turn raises the costs of the guarantee system.

The explicit aim is to encourage depositors to monitor the behaviour of banks and hence to impose the discipline necessary to ensure that the bank acts in their interest. Depositors are expected to mobilize and to exercise a form of Galbraithian 'countervailing power', thereby enabling depositors to marshal their interests against those of bank management. To understand the costs and benefits of this approach, it is necessary to identify the *agency costs* associated with the banking industry and its regulatory structure. Our aim is to achieve an understanding of the real or potential conflicts of interest of the players involved, and the incentives created by the institutional environment in which they operate. The players relevant to understanding the banking firm are the *principals*: the owners, depositors, borrowers and supervisors and the *agent*, the bank management.

Bank shareholders and depositors empower management with the task of achieving their objectives. On the one hand, shareholders wish to achieve a return on their capital. They realize that there are risks involved and they are willing to accept them. On the other hand, depositors desire a safe haven. This conflict of objective is given formal acknowledgement in limited liability provisions that govern the operation of the bank. Should the value of a bank's assets fall below the value of its liabilities, shareholders do not have to make good the difference. In the absence of a comprehensive deposit guarantee scheme, depositors would have first claim to the value of the bank's assets in the event of insolvency. When a comprehensive scheme does exist, a third principal is introduced, the guarantor who will be concerned that bank management operates in such a way that the funds available to the guarantee scheme are not depleted.

Of course, bank management itself is not a disinterested party. They will have their own objectives. These will be largely non-pecuniary, for example relating to ambience of the workplace and time spent on interpersonal relationships during the working day. Such behaviour has been explained by expense preference theories of the firm which relate expenditure on staffing and other emoluments to the creation of a power base independent of the firm's owners. Such behaviour has been confirmed for the banking industry in several empirical tests (e.g. Edwards, 1977; Rhoades, 1980).

In order to ensure that their interests are protected, shareholders and

depositors may introduce various monitoring and control activities, e.g. auditing procedures, budget restrictions or incentive compensation schemes. It is interesting to note that under the Weimar Republic, bank managers were required to undertake a performance bond which would be repayable only upon retirement. An alternative approach would be to introduce incentives for equity holders to monitor and control more closely the activities of management. For example, in the eighteenth century, British banking was characterized by unlimited liability. Under such a system shareholders would be required to make good all losses should the value of bank assets fall below deposit liabilities. In essence, the shareholders would be guaranteeing deposit liabilities on the basis of their personal wealth. A related approach involving equity holders posting surety bonds has been discussed by Osterberg and Thomson (1991). Under such circumstances, the bank's owners have an increased incentive to monitor the activities of management. In addition, each owner would have the incentive to monitor the wealth position of other shareholders. The personal bankruptcy of one could increase the liability of others.

For the above reasons, both depositors and shareholders have the incentive to hire an auditor, or through their government require that there be a supervisory authority which undertakes the audit. Shareholders enjoy the benefits of greater leverage, i.e. a higher ratio of profit-yielding assets to equity. Hence an audit system which is responsible to the interests of the shareholders may work to the disadvantage of the other interested parties. This conflict of interest has been noted in the discussions following the failure of BCCI. Consequently there is a strong case for adopting a system whereby auditors are nominated by the regulator, and not the institution being audited. Second, the existence of such liabilities requires an explicit statement concerning the obligations of the bank's owners irrespective of whether they are managers or not.

If there exists a comprehensive deposit guarantee scheme, the burden of risk arising from the bank's levered position shifts away from the owner to the guarantor. If the guarantor is a private sector institution it will set its premiums in such a way as to reflect the probability that the guarantee will be exercised. This will depend upon the expected return and riskiness of the bank's portfolio as well as the degree of leverage. This scenario would be similar to the one now operating in the US. In terms of the issues associated with the principal-agent problem, bank owners will continue to have an interest in monitoring the activities of management. However, in addition, the guarantor has the incentive to monitor not only the activities of management but also the objectives of the owners. The latter now have the incentive to increase their leverage. Hence the guarantee fund will wish to place limits on that leverage in the form of minimum capital-asset ratios. Capital or equity not only reflects the value of the owner's investment, it also acts as a protective buffer stock against unforeseen decline

in asset values. Intuition would suggest that the higher the capital-asset ratio, the lower the probability that the guarantee fund will be drawn against. However Gennette and Pyle (1991) have shown that under quite plausible circumstances, an increase in minimum capital requirements will actually lead to an increase in the riskiness of the bank's portfolio. Thus they argue that bank capital is not a substitute for monitoring and control and, quite the opposite, may imply the need for greater surveillance of the bank's portfolio. Another principal-agent problem is introduced. The owners of the guarantee fund will have the incentive to monitor the behaviour of the managers of the fund just as bank owners have the incentive to monitor the behaviour of their management. An understanding of this relationship becomes particularly important if the guarantee fund is managed by the government or is a private company with a state guarantee. In either case, the burden of liability ends up being shifted to the taxpayer. The question then arises as to whether the taxpayer should bear the costs of monitoring the management of the deposit guarantee fund. Since the taxpayer has neither the time nor the expertise to understand financial accounts and to assess with accuracy the riskiness of the guarantee fund's position, there is an additional case for effective public supervision.

Monitoring and the implementation of control procedures to create incentives for the agent to achieve the objectives of the principal assumes that there exists information which accurately reflects the financial positions of the bank, its owners and the guarantee fund. Unfortunately this is not feasible with the current generally accepted accounting practice which is based upon historical cost or book value accounting. The objective of such practice is to ensure that the purchase price of assets is entered correctly. However, in a world where asset prices are volatile and there exists substantial credit risk or default risk on the part of borrowers, book value accounting will generate substantial inaccuracies in the valuation of bank assets. Thus, in practice, bank owners do not know the value of their equity. A bank may appear to be perfectly well capitalized from an accounting standpoint, whereas from an economic standpoint it is substantially undercapitalized or indeed has negative net worth. And the guarantor will not know the extent of its liability. Similarly, where the government acts as a lender of last resort to the guarantor, taxpayers will not know their liability.

The misrepresentation inherent in book value accounting can be reduced by increased monitoring by the supervisory authority. However, this can be expensive. Not only must the supervisor understand the balance sheet position of the bank, but also of each individual borrower. And, of course, the borrower will be utilizing historical cost accounting procedures as well, so the problem is compounded. This will be particularly true when a borrower is unable to service its loans and simply requests an additional loan to make the necessary payments. The result is a long delay between the time when a problem actually

emerges and the time when default actually occurs. The supervisory authority can request banks to make loan loss provisions, but these usually occur well after the problem arises. There are alternative accounting mechanisms based on market value or economic value methods. These are discussed in detail by Wolfe (1992).

As we have already noted, the Directive on Deposit Guarantees takes a substantially modified approach, namely depositors are expected to bear some of the risks associated with the bank's portfolio. By way of summary, this may take several forms: (i) there may be a cap on the amount of liabilities eligible for insurance; (ii) up to 10 per cent of deposit liabilities may not be insured; (iii) most wholesale depositors will not be covered; (iv) there is a time-lag between bank closure and pay-out from the guarantee fund.

The explicit aim is to encourage depositors to monitor the behaviour of banks and hence to impose the discipline to ensure that the bank acts in their interest. McCulloch (1986) has argued that the premium should be charged only on the deposits actually insured. The remaining uninsured deposits should bear a higher yield to reflect the risks to the depositor. In a perfect world, the insurance premium and extra interest charge would be the same and thus the bank would be indifferent. However, the depositor would still be subject to capital losses on the uninsured deposits. Dreyfus and Saunders (1990) have shown that where there is a cap on the level of insured deposits, the resulting increase in deposit rates will actually increase the probability of bank failure. Hence, lowering the cap could actually increase the level of claims against the guarantee fund. In addition, as Diamond and Dybvig (1986) have argued, this opens up the possibility of runs and contagion effects spreading to banks that are solvent. This is particularly relevant to large depositors holding wholesale instruments which are not covered under the Deposit Guarantee Directive. Such depositors are more aware and hence will be the first to identify signs of trouble. They will run, leaving the less sophisticated, smaller depositors exposed to loss.

The EU approach does not fully take into account the nature of the principal-agent problem as it relates to the banking industry. In this scenario, all depositors will be expected to monitor the bank management and the influence of bank owners, since these will conflict with those of both. If bank deposits were treated as debt, then deposit holders could introduce covenants in indenture provisions which would limit the portfolio decisions of management and owners. However, this does not occur in practice. In addition, depositors also have the incentive to monitor the deposit guarantee fund. For example, although the German deposit guarantee system professes to provide 100 per cent coverage, coverage is only provided on the basis of the reserves available to the fund. If these are sufficient, there is no problem. In addition, the pay-out for all sight, time and savings deposits is specifically limited to 30 per cent of liable capital. Thus as

the bank becomes weaker, the payout to depositors in the event of failure becomes smaller. In the past, the apparently extensive hidden capital reserved of German banks and the strong German economy have acted as a shield against default by a major bank. However, the uncertainties of the current worldwide recession and the economic difficulties associated with unification have altered this situation.

In our opinion, the emphasis placed on depositor monitoring is unrealistic. The new classical economic theories which have achieved prominence over the past 20 years have placed great emphasis on the information-gathering and interpretive skills of economic agents. In particular, these theories assume that economic agents are able to distinguish between systematic and random changes in economic activity. Systematic errors will always be corrected, it is argued. When applied to the monitoring activities of depositors *vis-à-vis* banks, such analysis seems highly problematic. As Merton (1977) has argued, the depositor would have to 'assume the role of a security analyst and analyse the balance sheets of the bank, its management, and overall market conditions.' For the small depositor, the costs in terms of time and prior training would be prohibitive. The only discipline available would be the withdrawal of funds. The resulting run and possible systemic contagion effects would be incompatible with the stated goals of the Deposit Guarantee Directive. There is no easy trade-off between depositor co-insurance and the avoidance of bank runs.

4. The Relationship between the Deposit Guarantee Directive and Other Banking Related Directives

The objectives of the Deposit Guarantee Scheme are related to the objectives of other actual or proposed banking and financial market directives designed to provide safety-net facilities for depositors, notably those relating to bank solvency (1989), bank supervision (1992a), winding-up (1988) and generally accepted accounting standards (1986). Unfortunately, insufficient attention has been given by the Member States to this situation. The capital of a bank not only represents the value of shareholder equity, it serves as a buffer stock against unforeseen declines in the value of bank assets. The greater the capital-asset ratio, the smaller the probability of failure of the bank and the less likely that the deposit guarantee fund will be drawn upon. The lower the capital-asset ratio, the greater the value of the deposit guarantee to the bank.

Underlying this interrelationship are two important considerations. First, the value of bank assets and liabilities must be accurately measured. Otherwise, neither shareholders nor regulators, including the managers of the deposit guarantee fund, have an accurate measure of bank capital. Under the circumstances, it is difficult for supervisors to assess whether a bank is facing liquidity

problems or insolvency. The book value of assets does not necessarily reflect their true value. Further, there are various ways of misrepresenting the actual value of assets, e.g. by postponing provisioning and write-offs.

Denmark has broken considerable ground in this respect with the introduction of a market value accounting system (cf. Pozderna, 1992). However, the cost has been greater volatility in asset and liability values and hence difficulty in ascertaining underlying trends in the structure of banks (cf. Wolfe, 1992). Second, the timing of a winding-up or closure can have a significant impact on the liability of the deposit guarantee fund. The longer a deterioration in the value of bank assets is allowed, the greater becomes that liability. This is a major theme in the 1989 Report of the Brookings Institution Working Group examining the problems faced by the US banking industry. The emphasis of the Deposit Guarantee Directive is somewhat different. This is to be activated when depositors are unable to withdraw funds. This inability could be due to a liquidity rather than a solvency problem. Hence implementation may be independent of winding-up. Time may be given for the bank to be restructured. However, there is a fine distinction between a liquidity problem and a solvency problem. A central bank may provide lender of last resort facilities to resolve the former when the latter is really the issue. Thus in a European context, use of deposit guarantees can be avoided through lender of last resort facilities. This implicit form of deposit guarantee is not addressed by the Directive.

One implication is that there should also be a directive relating to lender of last resort facilities. This raises the broader issue of the relationship between central banks and bank supervisors. A full analysis is beyond the scope of this article. However, it is important to note a potential conflict of interest. During periods of restrictive monetary policy, the level of non-performing loans increases. As a result the viability of the lending banks themselves is threatened. The probability that a deposit guarantee scheme will be activated thereby increases. Lender of last resort facilities could be utilized to avoid this. However, the expansionary effects would be counter to the objectives of the restrictive monetary policy. An alternative is that the lender of last resort facilities could be extended to the guarantee fund rather than the banks. The bottom line is that all policies relating to banks and banking supervision are interrelated.

5. The Principle of Subsidiarity

Whether or not the principle of subsidiarity is operational will depend in large measure on how specific EC directives influence market behaviour. Unfortunately, there are many definitions of subsidiarity. Some would take the rather limited view that this principle implies that decisions should be taken closest to

the persons affected. In principle, this has compelling appeal to those of liberal philosophy. It will also appeal to those who believe in the role of national sovereignty in the preservation of national culture, language and institutions. However, there is a difference between sovereignty and independence. The degree to which both can be maintained in the economic sphere will depend upon the degree to which markets are *de facto* segmented and competition is imperfect. Recognition of this dichotomy is implicit in the definition of subsidiarity offered by Jacques Delors (1991):

Subsidiarity, because it assumes that society is organized into groups and not broken down into individuals, rests strictly speaking on a dialectic relationship: the smaller unit's right to act is operative to the extent, and only to the extent (this is forgotten very quickly) that it alone can act better than a large unit in achieving the aims being pursued.

Basically Delors is raising the question, what is the optimal legislative and administrative grouping? Given that financial markets are now global and no longer have a significant geographical element, it is our view that the optimal supervisory body should be international rather than national in scope in order to minimize the possibility of competitive distortions arising from different national interpretations. Today, it is possible to undertake complex international transactions over the telephone in one's office or home. Costs are minimal. Hence with unharmonized financial regulations, one would expect regulatory arbitrage to be particularly prevalent. A country may be sovereign in the sense that it sets its own regulations subject to EU minimum standards, but that in fact it has no independence if partner countries have adopted less restrictive regulations. In such an environment it is impossible for a smaller unit to operate more effectively as an independent agent than a larger grouping that has harmonized its procedures.

It is this conjecture that we examine in the case of deposit insurance. Even though there will exist differences in coverage in national banking systems governed by the 'home country' principle, there will be the incentive for all regulatory systems to converge. But to what level? To the extent that the regulatory authorities are fully independent of political pressure and the banking industry itself, then the expectation would be that the goals of competition and safety will be pursued. However, such independence does not prevail and hence there must always be the concern that the banking industries in one or more countries will seek to achieve competitive advantage by influencing the extent and implementation of regulations. The Deposit Guarantee Directive does not take into consideration the possibility of competition in laxity.

The application of the principle of subsidiarity arises in five different forms in the Directive:

1. the minimum standards relating to co-insurance;
2. conflict between deposit insurance and lender of last resort;
3. different treatment of foreign branches and subsidiaries;
4. failure to deal with the 'too big to fail' principle;
5. funding of deposit guarantee schemes.

1. In early drafts of the Directive the level of depositor co-insurance was left up to national regulatory authorities. Thus if depositors became aware that the degree of protection provided by banks headquartered in their own country was lower than that provided by foreign banks, then they would have had the incentive to deal with the latter. The fact that deposits are denominated in the currency of the depositor's nationality will make no difference under the Directive. The final draft has eliminated this potential competitive distortion, as indicated in Section 2. However, this does not eliminate the potential international flight of funds if depositors perceive differential implementation of the Directive.

2. When a bank becomes insolvent, either it can be closed or some form of restructuring or merger can be sought by the supervisor. In the US, some economists have expressed concern that the triggering of closure or restructuring has been left too late (cf. Brookings Institution, 1989). Asset values have been allowed to continue to fall with the result that additional claims are made against the deposit guarantee fund, in that instance the FDIC, and the Federal Savings and Loan Insurance Corporation (FSLIC). The Deposit Guarantee Directive takes a somewhat different approach. The guarantee scheme would be triggered by the inability of any depositor to withdraw funds from the bank. This could occur well before a formal closure is made and would allow receivers and supervisors time to implement a restructuring or a merger. The lack of any formal closure rule would therefore seem to be unimportant. However, the problem emerges in another form involving the implementation of lender of last resort facilities. Any regulatory authority can avoid or postpone the triggering of the deposit guarantee mechanism simply by ensuring that the bank possesses sufficient liquidity to meet the demands of depositors. The issue is complicated by the fact that under the Basle Concordat, the supervision of liquidity is the responsibility of the host country rather than the home country. Thus the triggering of a deposit guarantee scheme could place national monetary authorities in conflict. In order to avoid any competitive distortion, deliberate or otherwise, it is necessary that the use of monetary policy instruments be harmonized.

3. Foreign branches are treated under the proposed Directive according to the home country principle, whereas subsidiaries are treated under the host

country principle. From a legal and supervisory position, this makes sense. However, it does provide another opportunity for a competitive distortion to arise since banks will choose the organizational structure which provides them with the best competitive advantage.

4. Superimposed upon the proposed Deposit Guarantee Directive is an unwritten principle that some banks are 'too big to fail'. Under the principle of subsidiarity, the decision as to where to draw the line between 'small' and 'large' banks would be left up to the national regulatory authorities. There is thus the possibility that different standards will be adopted. Further, it renders the Deposit Guarantee Directive irrelevant for all but small banks. Rational depositors knowing that they must co-insure will have the incentive to move funds from smaller or medium-sized banks to the large banks. The retail banking sector in each country will become more concentrated than it is currently, although such concentration is unlikely to have much effect on wholesale banking activities.

5. The existence of private insurance schemes in some Member States and public schemes in others could also create competitive distortions. Franks and Mayer (1989) have argued that private schemes may be incapable of dealing with widespread insolvency arising from systematic factors operating throughout the economy. As a consequence, depositors may lose confidence in the guarantor, thereby increasing the probability of runs for fear that the private guarantor may be unable to fulfil its obligations. In contrast, the public will perceive that a public scheme will always receive lender of last resort facilities should its funds be depleted.

6. Conclusions

The evolution of the European Community has been and will continue to be a highly dynamic process. The philosophy of the founders was to create an environment of positive tensions in which challenges would be recognized and the response would be greater harmonization of policies and hence political unification. It is against this background that the inconsistencies in practice will have spill-over effects that potentially will require greater harmonization. As the process proceeds, new tensions will develop and even more spill-over effects will occur. Of course, there is no inevitability to this process. Any policy must be evaluated on the basis of its net gains and how they are distributed. If these are substantial, then governments have the incentive to pursue greater harmonization and to abandon the principle of subsidiarity. If the perception is of net losses or only small gains, the process will slow down or stop. A period of positive consolidation might ensue, although disintegration could occur if costs are high or the existing institutional structure is unable to respond

effectively to external shocks. It is of course against such shocks that the Deposit Guarantee Directive is designed to provide protection.

The principle of subsidiarity is potentially a consolidating device. By establishing certain minimum levels of deposit insurance and then allowing countries to adopt higher standards, the Directive provides for a learning period which can set the stage for further harmonization. The problem is that market participants move quickly and hence may make future adjustments difficult to implement.

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CHAPTER THREE

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The globalization of banking and financial markets: the challenge for European regulators

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ABSTRACT

The objective of this article is to examine recent trends in regulatory philosophy that are occurring as a result of the globalization of banking and financial market activities facilitated by the electronic revolution. By compressing both time and space, this revolution is threatening the supremacy of the nation state as the basis for ordering our economic, political and social lives. In the financial services sector, the result is an increasing transfer of disciplinary functions to the markets themselves. The shift of emphasis is away from the regulation of markets by individual nation states to the provision of sufficient information to enable customers of financial institutions to create the incentives for these institutions to act in a safe and sound manner. This trend is being supported by many regulators recognizing their inability to keep pace with financial innovations and the transient and uncertain nature of market trends. The philosophy underlying the EU Deposit Guarantee Directive is such as to expose depositors to the risks of bank insolvency. Future modifications to the EU Capital Adequacy Directive will require investment firms to publish information about their risk exposures and management practices so as to enable customers to assess the credit-worthiness of these institutions. However, as global regulatory functions degenerate, there is an increased need for global harmonization of auditing procedures and reporting standards.

KEY WORDS

EU directives; financial integration of Europe; financial markets; globalization; international banking; regulations.

INTRODUCTION

The principles underlying the regulation and supervision of banks and investment firms have traditionally been based upon the economist's case for state intervention when there is a market failure. This case underpins

the European Union's philosophy towards financial markets as embedded in the Bank Solvency Directive (1989) (covering the credit risks faced by banks) and the Capital Adequacy Directive (1993b) (covering the market risks in trading books). The objective of this article is to re-examine these arguments in the light of recent trends in regulatory philosophy that are shifting the burden of monitoring and supervision away from central banks and other regulatory agencies and on to the markets themselves. We will argue that this is not so much the result of an acceptance of the rhetoric of free-market philosophers or a neglect of the theory of market failure. Rather, we see this as a by-product of the globalization of financial markets brought about by the electronic revolution of the late twentieth century. In the sphere of banking and finance this revolution, by compressing both time and space, is threatening the supremacy of the nation state as the basis for ordering our economic, political and social lives. The result is an increasing transfer of disciplinary functions to the financial markets themselves. The focus is upon improving the availability of information in such a way that it empowers market participants. The shift of emphasis is away from regulation of markets by individual nation states to the provision of sufficient information such that the market participants, no longer restricted by territorial boundaries, can regulate themselves.

Between the period of the Great Depression and the early 1960s the logical structure of the theory of economic policy achieved great sophistication. So great was the beauty and complexity of this structure that it led many social scientists and politicians to believe that economic policy could be undertaken as a form of control engineering. The hydraulic model of Almarin Phillips at the London School of Economics symbolizes this expectation. Although the premiss was that economic agents were rational, it was recognized that failures in labour, goods and financial markets could occur. The causes of these failures were processes not captured by market prices, asymmetries in the distribution of information and monopoly power. The belief was that these failures could be ameliorated through the intervention of rational policy-makers. With hindsight, however, it now appears as if these structures were narrowly conceived. First, they explicitly assumed that human behaviour was stationary and where technological change did occur, it did so gradually. Second, they explicitly assumed that the stochastic processes generating risks were also stationary. Third, it was possible to formulate policies in terms of their effects on a representative individual or firm.

During the 1950s and 1960s many economists began to question this paradigm, arguing that human behaviour was actually much richer and more complex than the stated axioms then allowed. This led to the development of behavioural theories of the firm. One theme that emerged was that individuals were driven by a sort of 'will to power' rather than a simple 'will to profit'. For example, consider similarities between a bank or investment firm and financial market regulators. In

the context of the financial firm, power could be signified by the achievement of targets relating to sales growth, market share or size of workforce, all attributes which could be inconsistent with the objective of profit maximization. However, the achievement of such objectives is seen to bestow power not only on individual managers within the institution but also on the institution itself. Similar conjectures could be extended to the regulatory agency. In theory, the objective of regulators should be the maximization of social welfare. In practice, such objectives may be tempered by the regulator's own 'will to power' which is manifested in bureaucratic structures that are larger than necessary to achieve stated objectives. In this sense the internal structures of the regulator and regulated are similar. Employees of financial institutions tolerate this since they see the sense of order as providing them with desired security, albeit at lower salary. At another level, the regulated may tolerate such behaviour on the part of the regulator since it provides a safe and secure environment.

The appropriateness of a regulatory framework and regulatory philosophy can be understood within Stigler's (1971) conceptual framework. He considered regulations to be the outcome of supply and demand relationships which, in the context of financial markets, has central banks and other regulatory agencies on the supply side, and banks and investment firms, as well as the public, on the demand side. Those who argue that regulators are prone to capture base their case upon the idea that the financial services sector is a more compact, better organized group than the public. Hence they are in a better position to influence the way that the government develops and implements regulations. In the context of the present environment in which the financial institutions strive to become global players, the situation has been altered slightly. When it is in their interest, financial institutions will submit to the authority of the regulator. When it is not, they will seek ways of avoiding the regulator, of finding a less strict regulator, or of attempting to capture the regulator.

Prior to competition and credit control in 1973, it was the practice of the Bank of England and the Big Four UK banks to meet to formulate strategy. The banks were happy to accept this discipline since it fostered a sense of certainty and order. Following Bank of England directives with respect to lending levels and interest rates reduced the need to take risk management decisions. These decisions were taken instead by the regulator. But times have changed. London is no longer characterized by a cosy oligarchy involving regulated and regulator. The protective certainty provided by the nation state is no longer a consideration for financial institutions. Since the early 1970s there has been a concerted effort internationally to increase the competitiveness of banks and financial markets. Steps to reduce the restrictions on inter-state banking and the Glass-Steagall Act (requiring separation of banking and securities activities) in the US, the abolition of exchange controls in 1979 and Big

Bang in the UK, the Single Passport Principle embedded in the European Union Banking Co-ordination (1989) and Investment Services Directives (1993a) have all changed the nature and focus of financial markets. This freeing of competition in financial markets and the resulting electronic globalization have meant that national regulators have lost their monopoly. They are no longer in demand. But regulators have only slowly come to realize that they have been trapped within a theoretical framework which is based on linear progress, rational choice and a desire for an unchanging social order.

The consequence is that financial markets are now exposed to a variety of tensions:

- tension between the power of regulatory authorities as embodied in mathematical formulae contained in regulations and the power of financial institutions that is exerted through the markets;
- tension between the constructive and destructive nature of financial innovation and the inability of regulators to keep pace with change;
- tension between universal norms contained in regulations and transient and uncertain market relations;
- tension between competition and safety within financial markets;
- tension between a desire for uniformity by regulators and a desire for difference by financial institutions;
- tension between transparency and opaqueness in the flow of financial information;
- tension between the regulators constrained by the boundaries of the nation state and the industry which now has no territorial constraints;
- tension between the regulators who are extra-market and the industry which is free to innovate within market structures;
- tension that inappropriate regulation may engender financial fragility.

It is our hypothesis that these tensions have been enhanced by the electronic revolution. Whereas, in 1960, the boundaries of a local financial community were the nation state, they are today the entire globe. The ebb and flow of these tensions is part of a complex social process that does not easily lend itself to the claims to universality generated by modern economic analysis. In our opinion, an examination of these tensions should be high on the agenda of financial market research over the coming years. Greater attention needs to be given to the causes of financial fragility rather than to what is conventionally thought to be the stable norm. The investigation should encompass both sides of the binary dichotomies. A focus that involves only one half of the dichotomies contained in the tensions just listed is bound to privilege the views of one group, either the regulator or the regulated, and lead to an incomplete and implicitly prejudiced interpretation of events. By

redirecting our research in this way, we should be better able to interpret current trends and thus enable an informed opinion about whether or not these trends will be beneficial to society.

THE TRADITIONAL THEORY OF FINANCIAL MARKET REGULATION

The traditional theory of financial market regulation finds its basis in the Cartesian logic of economic analysis. For this reason, it is appropriate to begin with a brief summary of the theory of market failures (cf. McKenzie (1995b) for a more detailed analysis). As noted previously such failures may arise in financial markets for three principal reasons.

A. Externalities. An externality is an interrelationship between individuals and/or firms that creates costs and benefits but where these costs and benefits are not captured in market prices. The standard textbook example of an externality is that of air pollution. There is no method whereby individuals whose health is seriously affected by factory emissions could extract compensation by acting on their own. In theory, government intervention could tax the polluter, thereby providing the incentive for clean-up and funding towards the health care of those affected. Alternatively, a regulator could set standards for emissions which would attract fines if there was non-compliance. In the financial services sector, the externalities attract less press coverage but are no less real or pervasive. The externalities experienced in finance are of two types: positive as well as negative, ex-post as well as ex-ante. Positive externalities relate to the social benefits provided by the banks and the investment firms in their operations. For example, banks support the payments system by cashing and clearing cheques. In their management strategies, banks will only be looking at the profits created by these activities and not at the wider social benefit which they provide in facilitating economic transactions. Investment firms play a similar role in underwriting and making markets in various financial instruments. It is argued that centralized regulation and supervision of financial institutions enables the entire economy to operate more efficiently.

A negative externality arises from the existence of systemic risk. This is the risk faced by the system from the failure of a financial institution. Unlike the examples mentioned previously, this externality does not exist continuously through time but may occur only at some discreet moment, unexpectedly. Since it is difficult to predict the timing of such an event, the amount of externalities generated by the emitter (failed financial institution) and the cost borne by the recipients are uncertain. Considering the enormous disruptive potential of the externalities emerging from the failure of a major financial institution, the test of the regulator is to minimize the probability of such an event. The most common regulatory tool applied to control failure involves the setting of minimum safety standards (as, for example, in the EU Bank Solvency and

Capital Adequacy Directives). The standard will depend upon the regulator's assessment/perception of the probability of the event *vis-à-vis* different benchmark standards (for example, levels of capital) and the extent of externalities generated from failure of an institution. The choice of the regulator *vis-à-vis* the correct/adequate safety standards will be based upon the appropriate balance of these factors against the extra cost imposed on the financial sector to protect against such an event (an eventual loss to the public) that has not yet occurred. This is not an uncomplicated problem, for it requires that the regulators not only set minimum standards of safety (capital adequacy regulations), but also back them with compensatory mechanisms like deposit guarantee schemes.

B. Asymmetric Information. A second type of market failure arises from the asymmetric distribution of information. One of the major enabling functions of banks and investment firms is their ability to marshall and interpret information about borrowers and asset price movements. By operating risk management systems and employing analysts to interpret the information flow resulting from these systems, financial institutions are able to create portfolios of loans and/or other financial instruments more efficiently than individuals operating on their own. However, the institution will view this process as proprietary. It does not wish to make it transparent, thereby enabling it to be copied by others who would then be in a position to compete away profit margins. The end result is that there is an asymmetry in the information flow between a financial institution and its customers. This asymmetry has several implications. First, many bank customers are primarily interested in a safe haven for their funds. If a bank is maintaining a risky loan book, customers will be unaware of this until it is too late and the bank has failed. As a consequence two things may happen. Customers will think that banks are inherently risky and demand a risk premium in the deposit rate. Since they have no means of distinguishing between banks which have relatively safe loan books and those which are relatively unsafe, even those banks which are safe will be forced to pay such a premium or go out of business. The result of this is that risky banks remain whereas safe banks have no incentive to stay in business or they will change their portfolio strategies to become more like the risky institutions. This process is called adverse selection.

Second, if a bank should fail, the inability to distinguish between banks may lead to runs on the banking system as a whole. Customers will extrapolate the behaviour of one bank to the system as a whole. The asymmetric distribution of information may create negative externalities as discussed in the previous section. Because of this and the fact that bank customers do not have the expertise to be analysts of the banking sector, many governments seek to redress the balance by providing deposit guarantees and ensuring that banks are sufficiently well capitalized so as to minimize the risks of insolvency. Such protection is the basis of

various international regulations including the Basle Accord of 1987 and various European Union directives, including the Bank Solvency Directive, the Deposit Guarantee Directive (1994) and the Capital Adequacy Directive for Credit Institutions and Investment Firms.

But as we shall argue throughout this article, there are no clearcut solutions. For example, the European Deposit Guarantee Directive seeks to place much of the costs of bank insolvency upon depositors. In this way they hope to induce depositors to monitor the behaviour of their bank and thence to place pressure upon it to act in a safe and sound manner. A fuller discussion of this point is contained in McKenzie and Khalidi (1994) and McKenzie (1995a). What the Deposit Guarantee Directive or the other European Union Directives related to banking and investment firms fail to do, however, is either to remove the information asymmetry between the regulators and the depositors, or to provide the depositors with information that is adequate for monitoring the prudential behaviour of their banks.

C. Monopoly Power. The third type of market failure arises from the existence of monopoly power. If only one bank or investment firm existed in any market, it would be in a position to widen the gap between deposit and loan rates or in the case of the investment firm the bid/ask spread and fees charged. Such situations could be dealt with in various ways, such as through anti-trust legislation which limits the extent of merger between financial institutions; or limits on the return that monopolies can make. In anticipation of subsequent discussion, it is worthwhile noting that there is a certain amount of market segmentation between retail and wholesale banking. Although there are exceptions, retail banking in the United States and in European countries tends to benefit from a certain 'brand' loyalty with customers unwilling to bank with foreign institutions even though the latter may be offering more competitive deposit and loan rates. In contrast, there are no such loyalties in wholesale markets where large corporate customers will deal with institutions offering the best terms irrespective of the location of the head office.

The above characterization of market failure gives the impression that all that governments and regulators need do is to turn a tap (by changing taxes or imposing penalties) or set up road blocks (by setting minimum standards). This control engineering approach needs to be tempered by the recognition that regulatory failures may exist as well. Regulatory failures may be of two types: first, those arising through the asymmetric distribution of information and, second, those arising from the behavioural characteristics of the regulators. Asymmetry in information flows may arise at two levels: first, between the financial institution and its customers and, second, between the financial institution and the regulator. If the regulator possesses only incomplete information about an institution, it is possible that any interventions may be sub-optimal, that is, they may be too Draconian but equally they could be too lenient.

Further, it enables unscrupulous management to avoid, if not evade, the spirit of existing legislation. The process of frequent bank examination and auditing reduces this possibility. At the international level, the effects of asymmetric flows of information between the regulators of different nation states may also be important where an institution has significant global operations. If one regulator, seeing that a branch is in trouble, fails to inform the regulator of the head office, one road to corrective action is closed off. This possibility can be reduced through extensive, formal international consultations.

The story which we have just been relating is based upon several assumptions:

- that individuals and firms operating in markets are rational. In terms of the calculus of economics, this means maximizing satisfaction and profits, respectively;
- that individuals and firms are prepared to submit themselves to market discipline because it enables them to achieve those objectives;
- that government intervention, whether in the form of intervention in markets or the setting of standards, is rational in the sense that it is designed to eliminate differences between private gains and costs and social gains and costs;
- that there are unique and universally accepted concepts of social gains and costs;
- that individuals and firms possess sufficient information to formulate decisions on the basis of subjective probabilities relating to possible outcomes;
- that it is possible to distinguish between fundamental mistakes and purely random errors and when the former occurs steps are taken to correct the mistake.

The overall picture is one of rational, ordered markets. Where there is the potential for market failure, governments are able to intervene in a rational and ordered way so as to reduce and perhaps eliminate the extent of the failure. This view of the world has certainly dominated financial history since the end of the Second World War. Institutions such as the International Monetary Fund and the Common Market, the return to currency convertibility in 1957, the gradual deregulation of financial markets since the early 1970s and most recently the Basle Accord of 1987 are all based on the principle that markets assisted by governments, where appropriate, would provide the basis for continuing stability and prosperity. By formalizing the single-passport principle in the Second Banking Co-ordination Directive (1989) and the Investment Services Directive (1993a), the European Union has eliminated the nation state as a barrier to competition. However, in seeking to ensure that competitive markets would also be safe for the customers of European financial institutions, the EU has retained a role for the state in the

implementation of the Bank Solvency Directive and the Capital Adequacy Directive. Because regulators were supposed to be rational and accepted the validity of the structures outlined above, it would be straightforward for the regulations to be harmonized. Indeed, in this respect the Basle Accord stands out as a truly exceptional document. Although there were important compromises in its construction, particularly to Japan, it represented an awareness that at least in the area of minimum standards for bank capital, international standards could be set which appeared to be in everyone's national interest. This document defined capital and identified broad categories of assets, each of which would require different amounts of equity support according to their perceived riskiness. The principle of risk-related regulation was thereby introduced.

DESTRUCTION AND RECONSTRUCTION THROUGH GLOBALIZATION

Many economists have been aware of the limitations of the Cartesian basis of modern economic management and regulation. Keynes was committed to the use of formal logic but only as a means of interpreting specific circumstances. He counselled against attempts at constructing universal theories and, in particular, at attempts to utilize econometric models for forecasting. In his view, the information created by markets was too transient and uncertain, with market participants, especially those in financial markets, subject to bouts of irrationality. The transient nature of financial markets was highlighted by Hyman Minsky (1957) and the Radcliffe Report (1959) who saw financial innovations as attempts by banks and investment firms to avoid stringent regulation or the effects of restrictive monetary policies. Minsky based his case on the development of the Federal Funds market in the US which enabled banks to economize on reserves and the creation of certificates of deposit which enabled banks to avoid regulations governing interest rates. The evolution of euro-currency markets found its origins in attempts by US banks to avoid controls more stringent than those in place in London. Such dynamics are captured in Goodhart's law (1989). Goodhart argued that institutions will change their behaviour in response to changing government policies so as to render these changes virtually ineffective. Although Goodhart was primarily interested in the implications of changes in the direction of monetary policies, his principle applies equally well to the effects of regulatory change. It is also appropriate to mention the Lucas critique (1976) in the light of recent attempts by regulators to encourage financial institutions to adopt quantitative risk management procedures which would serve as a basis for calculating regulatory capital. Lucas argued that as soon as a statistical model is used as a basis for policy formulation, those affected will change their behaviour so as to render the model invalid.

If we take these positions seriously, we are led to the conclusion that many assumptions of conventional regulatory theory do not hold in practice. The structure of the economy does not remain stationary over time. Banks and investment firms as they evolved from the seventeenth century onwards have been an inextricable influence in facilitating the freeing of the animal spirits which John Stuart Mill believed drove capitalist entrepreneurs. In the sense of Schumpeter, the entrepreneur is a heroic figure involved in a process of creative destruction and destructive creation, prepared to push the consequences of technical and social innovation to extremes. Similarly, the process of financial innovation is also one of construction and destruction. New financial instruments render obsolete older, inflexible savings accounts. Equity futures markets are preferred to the spot markets. Credit derivatives, call and put options and swaps enable new forms of investment and hedging which better satisfy market preferences. It is not simply the creative destruction and the destructive creation initiated by the innovative financier which is the key aspect of the change. Rather it is the surplus profit of the innovator which is the motivation behind the change. The success of the leader and his surplus profit pulls the other competitors in the field to follow him. This leads to a complete reorganization in markets and a change in the market equilibrium (Schumpeter 1959: 131).

The nature of these complementary destructive and constructive forces has not been fully appreciated by financial regulators who in the recent past have sought to set down rigid rules. Curiously perhaps, it is governments which have let the free-market genie out of the bottle. This was done on the basis that greater competition will create greater efficiency, a proposition which, as we argued in the previous section, is suspect even on its own premisses. By formalizing the single-passport principle in the Second Banking Co-ordination Directive and the Investment Services Directive, the European Union has eliminated the nation state as a barrier to competition. The Schumpeterian constructive/destructive spirits of the participants in financial markets have been unleashed. There is recognition that markets are not 'complete' in the sense that financial markets do not yet enable investors to satisfy fully their portfolio objectives. As a consequence there are profitable opportunities in moving towards completion. Concurrently, the European Union has sought to maintain the nation state as the basis for regulating financial risks. This has led to increased tension between regulators and the regulated. The regulator has remained committed to the implementation of universal norms based upon the assumption of a stationary financial environment. The constructive/destructive innovative spirits, on the other hand, are continually involved in a process of change, thereby rendering the market environment dynamic rather than static, creating a world which is both ephemeral and uncertain. Financial markets are increasing in both size and breadth while the regulatory environment attempts to extend its codification in order to keep pace

with the change. Parallel to these changes, the electronic revolution has brought about an unprecedented increase in the flow and availability of information. Markets no longer exist as physical entities. Rather, financial markets are a complex of electronic linkages organized by the former physical exchanges as well as by other bodies which never had physical premises used by customers. This compression of time and space thus poses another challenge to regulators. They are not able to keep pace with innovation, while concurrently the domain of power, the nation state, has become irrelevant. The world of financial markets and the world of the regulator are evolving in opposite directions.

All these arguments contain a common thread. They reflect the regulator-regulated dichotomy. They reflect the systems of thought which are based on binary opposition with the regulator being given a privileged position, while the regulated entities (financial institutions) have been marginalized. In the past, financial institutions have been receptive to the power of the regulator. Competition, to the extent that it existed, occurred within the boundaries of the nation state. The national regulator controlled the scale and scope of domestic financial activities and the extent of cross-border transactions. International transactions were carried out with correspondent financial institutions abroad. Communication was slow and costly. With the electronic revolution, these costs have been removed. Not only is the nation state no longer relevant in defining market boundaries, the regulated are in a position to outpace the regulator in the creation of new financial instruments, new organizational structures and new markets.

It is only recently that regulators have begun to recognize that they are losing this race and that they need to respond. The initial reaction was to seek to harmonize financial market regulations on a global, supranational basis involving not only Europe but also the United States, Japan and other major international financial centres. The first major steps in this direction were taken at the Bank of International Settlements and led to the Basle Accord of 1987 which set minimum capital standards for banks to cover credit risks. This was the basis of the EU Bank Solvency Directive. Amendments to this Accord to cover market risks associated with equities, bonds and derivatives are currently being made. However, these regulations fail to take into account the dynamics of the markets. They are based on fixed ratios and complex mathematical procedures based on duration analysis and the delta, gamma and vega of option pricing theory which have their basis in heat transfer physics. However, the scientific underpinnings of these approaches are illusory. The subjectivity and variability of these measures are not fully appreciated by market practitioners or regulators as they are by theoreticians. Some of these are discussed in Beattie *et al.* (1995) in the context of loan-loss provisioning and financial crises. In trying to force markets to adopt certain universal principles, the regulators are failing to recognize the transient and uncertain nature of those principles.

THE PRINCIPLE OF SUBSIDIARITY

Within the European regulatory framework, national regulators retain the responsibility for implementation and compliance under the principle of subsidiarity which lies at the heart of European banking and financial market directives. Basically, this means that the provisions of safety net procedures, supervision and regulation are in the domain of the nation state unless it can be shown that the European Union is better placed to carry out these tasks. We have been arguing that the nation state is no longer well placed to act as a regulator. But is the European Union any better placed? Here, too, the answer must be no. It is just as easy to carry out financial transactions in New York, Tokyo and Singapore as it is in London or Frankfurt. If there are significant differences in regulation, implementation or compliance between these centres, competitive distortions will occur. To avoid these and still maintain control over financial markets, regulators could move one step further and seek to harmonize regulations at a global level. In a sense this is happening. The Basle Accord, the genesis of the Bank Solvency Directive, involves the US, Japan and other non-EU countries. Amendments to the Basle Accord to take into account risks arising from securities trading will in the future be embodied in a modified Capital Adequacy Directive. However, it is our thesis that a greater centralization of authority will have only limited impact. Although global harmonization takes into account the globalization enabled by the time/space compression brought about by the electronic revolution, it neglects another. As we have discussed above, the electronic revolution has also unleashed the constructive and destructive energies of capitalist innovation. Since regulators are not part of this process, they cannot keep pace with it and hence they cannot control it.

More recently, there has been a converse trend in the application of the principle of subsidiarity not in the direction of the nation state to a supranational authority but from the nation state to the market. At the opposite extreme from global regulation is regulation by the markets themselves. This is being facilitated by calls for greater transparency in the operation of banks and financial markets, an approach which is consistent with the objective of enhancing financial market competition embodied in the single-passport principle. The targets here are the information asymmetries which have been enforced by the regulators in the past. Regulators require financial institutions to report vast amounts of information but not enough is actually published to enable market participants to make informed judgements about the credit-worthiness of their bank or broker. As a result, the markets are *de facto* compelled to depend on the competence or otherwise of the regulators. Various attempts at increasing transparency can be mentioned.

One is embedded in the EU Deposit Guarantee Directive (1992a, 1992b, 1994). We discuss this in detail elsewhere (McKenzie and Khalidi

1994; McKenzie 1995a). However, it is important to note that the drafters of this Directive were of the view that bank depositors should bear some of the risks should a financial institution fail. Only minimum standards for partial coverage are set down in the Directive. The idea behind this is that if depositors stand to lose money, they have the incentive to monitor carefully the strategy and management of that institution. To work, this approach means that there must be full disclosure to financial markets. Of course, even if there were, the question arises as to whether individuals would possess the skills of a security analyst to assess what is going on. Credit-rating agencies could assume some of this burden but their re-evaluations of the credit-worthiness of institutions often come only after a long lag.

Second, in the 'Fisher Report' of September 1994, the Group of Ten called for greater use of quantitative methods in the assessment of risks by financial institutions (cf. Casson 1996). The principal recommendations of this document are that all financial intermediaries, whether regulated or unregulated, should periodically disclose:

- 1 quantitative information relating to the market risks associated with their portfolios as well as the counterparty risks arising from their trading activities; and
- 2 the quantitative and qualitative procedures involved in their risk management strategies; and
- 3 comparisons of ex-ante risk profiles with ex-post performance.

Almost contemporaneously with the publication of the Fisher Report, J.P. Morgan released its risk management package RiskMetrics (1994). In doing so, they sought to fill a gap existing 'between the precision with which a firm's management can assess its financial risks and the information available to outsiders'. This asymmetry in the availability of information, they argued, could lead to an a) inefficient allocation of capital, and b) excessive fluctuations in asset prices. Further, it can lead to contagion effects and an increase in systemic risks. J.P. Morgan suggest that during periods of stress the lack of transparency can contribute to an environment in which rumours alone can cause a firm's market access and funding to be impaired as creditors and counterparties seek to avoid perceived uncertainties.

The significance of the Fisher Report is that it seeks to re-empower the regulator. The process of globalization has been enabled by the increased ability of financial institutions to process information and to develop customer relationships without regard to space. In response, regulators are seeking to monitor and control the way in which institutions manage and report this information. By ensuring that the information is presented in a consistent fashion, they believe that market participants can monitor and provide the necessary incentives for financial institutions to operate in a prudent fashion. A serious problem

with this strategy involves the quality of the information created. Econometricians have long realized that their activities are no more than a means of interpreting history. There is no guarantee that the future will be like the past, a point made emphatically in the Lucas critique summarized above.

Third, the US Federal Reserve Board has argued in favour of quantitative risk management procedures, but has warned against their mechanical use, and asserts that they must be used in conjunction with traditional methods of on-sight risk assessments. Just as every borrower may have their own risk characteristics, so every bank will be different in the way it assesses those risks. Therefore, the Federal Reserve highlights the need for monitoring and supervising financial institutions on an institution by institution basis (cf. Yellen 1996). It appears that if banks are taking an open-ended approach to their activities, regulators should as well.

The experiments in New Zealand are being watched closely as they are viewed as a test-bed for a scheme that seeks to remove the information asymmetry between the regulator, the bank and the depositor (cf. Federal Reserve Bank of New Zealand 1994, 1995a, 1995b; Lendengham 1995; Mortlock 1995). Rather than have intensive monitoring of banks as occurs in other countries, the emphasis is on public disclosure to allow customers to decide where to deposit their funds. Bank directors are responsible for managing risks and are liable for the accuracy of the information disclosed. Simplified as well as detailed financial statements would be available to all customers to make it possible for them to assess the credit-worthiness of their bank.

The principal characteristics of the New Zealand approach are:

- 1 There is no deposit guarantee scheme. If a bank fails, depositors will lose some or all of their funds depending upon the value of the bank's assets. The central bank is neither *de jure* nor *de facto* responsible for bailing out or compensating the depositors. This provides a motivation for the depositors and the counterparties of the bank actively to monitor the financial position of the bank.
- 2 There are no on-site bank examinations carried out either by the Reserve Bank of New Zealand or independent auditors. The onus for prudential control is on the bank directors.
- 3 Non-banks are also allowed to take deposits. The only legal benefit of registration is the ability to use the word 'bank' in the corporate title.

The Reserve Bank does retain the right to monitor disclosure documents, to advise and to intervene if bank distress threatens the soundness of the banking system. The principal objective of this scheme is to create incentives for bank management to monitor and manage their risks prudently. The incentive is that if they do not, they will lose depositors.

Thus, depositors will have access to information about the bank's profit and loss account, its balance sheet, the interests of directors, asset quality and loan-loss provisioning, the number of large exposures, sectoral exposure, capital adequacy including contingent liabilities and assets (e.g. options and guarantees), market risk exposures and the credit ratings of long-term senior unsecured NZ dollar debt held.

Transparency is the key to the success of this approach which gives greater responsibility to market participants. As the function of regulation declines in importance, however, there is now an increase in the remit of supervisors to ensure that published information is comprehensive and accurate. This requires a global initiative aimed at harmonizing audits and reporting standards. At the moment, supervision is based upon the home country principle. It is the Federal Banking Supervisory Office, not the Bank of England, which is responsible for branches of German banks operating in London. The nation state still remains the basis of supervision. The principle of subsidiarity is at work in two ways. At the level of regulation, we are suggesting greater responsibility for market participants whereas, at the level of supervision, greater harmonization is required, along the lines suggested by Begg and Green (1996).

Despite attempts at experimentation with greater transparency, there are sceptics within the regulatory community. Jeffrey Marquardt (1987) stated the case for direct regulatory intervention instead of improving transparency. He argued:

- 1 The role of a bank is to intermediate the information asymmetry that exists between ultimate lenders (i.e. the depositors) and borrowers. In other words, by revealing their exposures and proprietary risk management procedures, banks would be undermining their *raison d'être*.
- 2 Disclosed information would relate only to past, not future, performance.
- 3 Even if information was fully disclosed by financial institutions, it would be difficult to assess in a timely fashion.

But these arguments take us back to the introduction to this article and the question: is it possible to have financial calm and order in a dynamic, competitive environment? Indeed, financial institutions themselves may be raising this question in future strategy sessions, if they have not already done so. Having lobbied so successfully for an elimination of regulatory barriers to competition, they may find the obligations of this competitive environment so onerous that they may wish to restore the paternalistic role of the regulator that characterized the 1950s and 1960s.

In addition, there is an issue which we have not touched upon in this article: the relationship between a European monetary authority and financial market regulation. Begg and Green (1996) have raised three

points. First, effective financial market supervision is necessary for a stable monetary system. Second, it is difficult to disentangle the lender of last resort function from monetary control and prudential supervision. Third, there is an inconsistency between harmonized European monetary policies and unharmonized regulation.

CONCLUDING COMMENTS

The phenomenon of 'globalization' has brought about a paradigm shift in the operational framework of the markets. The scale and scope of the financial markets and the market participants, banks and investment firms, have been transformed from national to transnational. Because they lack roots in any one country, financial institutions have the potential to escape national regulatory frameworks. These transnational entities have harnessed rapidly evolving communication and computation technologies to reduce or remove the constraints of time and space which were the main limitations against interaction between institutions previously separated by physical distance. In the language of contemporary social scientists, they are actively involved in the 'reordering of time and space'. The development of communication technology has cut through the spatial barrier across nations, allowing on-line, real-time communications irrespective of one's location on the globe, thereby destroying physical distance which previously inhibited communication. Similarly, developments in computation technology have cut through the barriers to the processing and interpretation of data. But as these barriers collapse, there is the danger that the vast amounts of financial data which are increasingly available will bring about a paralysis in our capability to interpret that information. Overload may set in. Contemporaneously, old ways of thinking, based on ordered structures, are inhibiting our ability to cope with the change that is undermining the existing order. As we have sought to argue, financial regulators are unable to comprehend with sufficient speed current trends and the processes which underlie them. There is an inherent incompatibility between the desire for order embedded in European regulatory frameworks and the constructive/destructive forces inherent in financial market innovation.

For the regulators, this development has led to some disturbing consequences. First, the globally integrated operations of the transnational banks and investment firms have increased the systemic interdependencies between the nation states. Second, unlike the transnational financial institution, regulators are still very much constrained by their geographic boundaries. Third, the change in market environment in terms of the speed of financial innovation renders the existing regulatory tools like capital adequacy regulations suspect, if not impotent, in the context of fulfilling their regulatory objectives.

There are no simple explanations, only the complex tensions which we

have outlined in this article. Attempts to fit the facts to models purporting to represent universal norms must be tempered with an understanding that the operation of markets and of regulators and their interrelationship are part of a complex social process which is transient, uncertain and very difficult to understand. If the operation of financial markets is going through a paradigm shift, researchers must also be prepared for a paradigm shift in the way that they seek to understand these markets. At the very minimum, we must be prepared to raise questions. In our opinion, a key to understanding is the raising of flags pointing to the stresses between competitive financial markets and safe financial markets, on the one hand, and between top-down, harmonized regulation at a global level and improved transparency which enables market participants to self-regulate. Eliminating one source of market imperfection – lack of access to information – does not, however, guarantee that other market imperfections will not become more important. If there are important economies of scale in the gathering, monitoring and interpretation of information, we expect to see greater concentration in the provision of financial services globally. Attention will then turn to global anti-monopoly legislation. And, of course, it is still the case that an accurate valuation of the social benefits of financial markets is not in the self-interest of financial institutions. Hence society will continue to bear the costs of this mispricing.

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PART

III

**PHILOSOPHICAL ANALYSIS OF THE TENSIONS IN
THE FINANCIAL SERVICES INDUSTRY**

1. THE INSPIRATION:

"The salvation of knowledge (connaissance) depends entirely upon a methodological re-examination of its established forms (savoir), which congeal it by means of epistemology and seek to institute a supposedly absolute knowledge which is in fact no more than a pale imitation of divine wisdom. The only road for such a re-examination to take is the unification of critical knowledge with the critique of knowledge. The critical dimension of understanding must be brought to the fore. Collusion between 'knowledge' and 'power' must be forcefully exposed, as must the purposes to which bureaucracy bends knowledge's specialization. When institutional (academic) knowledge sets itself up above lived experience, just as the state sets itself up above everyday life, catastrophe is in the offing. Catastrophe is indeed already upon us.

In the absence of a reconstruction of this kind, knowledge must inevitably collapse under the blows of non-knowledge and the onslaughts of anti-knowledge (or anti-theory) - in short, it must relapse into the European nihilism that Nietzsche believed he had overcome"

Henri Lefebvre (1991, pp.414)

The above quote from Lefebvre (1991) provides the inspiration for this section of the thesis which aims to examine the logic underlying the tensions apparent in the financial services industry - the tensions emanating from the dialectical relationship between the regulators and the regulated (noted in Chapter Three above):

- tension between the power of regulatory authorities as embodied in mathematical formulae contained in regulations and the power of financial institutions that is exerted through the markets;
- tension between the constructive and destructive nature of financial innovation and the inability of regulators to keep pace with change;
- tension between universal norms contained in regulations and transient and uncertain market relations;
- tension between competition and safety within financial markets;
- tension between a desire for uniformity by regulators and a desire for difference by financial institutions;
- tension between transparency and opaqueness in the flow of financial information;
- tension between the regulators constrained by the boundaries of the nation state and the industry which now has no territorial constraints;

- tension between the regulators who are extra-market and the industry which is free to innovate within market structures;
- tension that inappropriate regulation may engender financial fragility;

Chapter Three (the paper by McKenzie and Khalidi, 1996) analyzed the interface of these tension and the gradual changes in the regulatory philosophy emerging as a consequence of these tensions that are shifting part of the burden of monitoring and supervision from the regulatory agencies to the markets themselves. The rationale for this shift according to the chapter/paper was the recognition by the regulators of their inability to keep pace with the financial innovation and the transient and uncertain nature of the markets, rather than a paradigm shift in the regulatory philosophy which was and still remains the modernist philosophical thought. This is the basic premise that forms the basis of part III of the thesis.

Here the aim is to investigate into the underpinnings of the regulatory framework. The aim is to examine the suitability of the philosophical foundations¹ of the regulatory framework for meeting the challenges of the rapidly changing ontological conditions² in the financial services

¹Although the literal meaning of the term ‘philosophy’ is ‘love of knowledge’, philosophy as a disciplinary domain incorporates an investigation not only into the most general as well as abstract features of the world, but also, and more importantly, the categories with which we think, for example, mind, matter, reason, proof, truth, etc.. The importance of the discipline of philosophy lies in the fact that in philosophy the concepts with which we approach the world, themselves become the topic of inquiry. Philosophy as a discipline is therefore concerned with not only an investigation into, but also and as a consequence, laying our conceptual foundations. The knowledge under investigation in philosophy not only includes generalized knowledge, but also disciplinary knowledge. The latter includes disciplinary areas such as history, physics, or law, etc. The philosophy of a discipline seeks not so much to solve the problems being tackled within the discipline, rather it aims to examine the concepts that structure such thinking, and for providing an explanatory logic for their foundations and presupposition (Blackburn, 1996, pp.286). In the context of the concept of philosophy, the aim of this section can be restated as the examination of the concepts that structure the present regulatory thinking, to lay bare their foundations and presuppositions, and to analyze the suitability of the regulatory philosophy in the context of the present era of global competition.

²The term ‘ontology’ is derived from the Greek word for ‘being’. The term ontology is also a seventeenth century coinage for a branch of metaphysical inquiry concerned with the study of ‘existence’ itself (Blackburn, 1996, pp.269-70). It has also been described as the science of ‘being’ embracing issues such as the nature of existence, and the category and structure of reality (Honderich, 1995, pp.264). It involves investigation into the different ways in which entities belonging to various logical categories (for example, physical objects, numbers, universal, abstraction, etc.) may be said to exist (Flew, 1979, pp.255-56).

Here the term ‘ontological conditions in the financial services industry’ has been used as a concept that incorporates the circumstances of the existence of the financial services industry as a whole, i.e. financial services industry as a ‘being in itself’. It includes the structure and the operational framework of the markets and the market participants (who are also ‘beings in itself’). It also includes the assumptions and the cumulative knowledge base of the market participants that forms the basis of

industry. The conceptual foundations of the regulatory thinking (and hence the basis of the design of the regulatory framework) are based on the modernist philosophical thought which assumes the existence of a truth out there waiting to be discovered - the single correct answer³ for the ordering

their actions and the effects of their actions on the behaviour of other market participants, and the operations of the markets as a whole.

The modernist philosophical discourse is a philosophical discourse of 'becoming'. It rationalizes the existence of the regulators who are extra market entities. It rationalizes the need for the existence of an extra market entity (the regulators) for the ordering and control of the operational environment of the financial services industry according to its inner logic, if the market is to be liberated from the irrationalities, imprudence, and recklessness of the market participants (who are also beings in itself). This 'being - becoming' dialectic is echoed in the regulator - regulated dialectic that is at the source of the tensions in the financial services industry.

³The overriding commitment of the modernist project was the search for the deep underlying realities that form the basis of the events and phenomenon that we experience. The aim was to develop overarching theories which could explain and give meaning to the disorder and contingency of the world. The aim was to apply this knowledge to control and change the world we live in. This, according to Usher (1997b, pp.28) was the totalizing dream of the modernist project, a dream which in the end had nothing to do with reason but something to do with desire - the desire for mastery and ultimately control. The basis of the belief that inspired this dream, lies in the positivist/empiricist epistemology (in as much as research involves about finding about the world, it is unavoidably about making knowledge claims. The term 'epistemology' refers to the way in which claims to knowledge are justified) which evolved out of the struggle against medieval church, and the authority of tradition, and their monopoly over learning and construction of truth which found its basis in the authority of divine text. Positivist/empiricists epistemology constituted a different way of grounding knowledge through the emerging natural sciences, with experiment and observation replacing tradition (Usher, 1997a, pp.2). The basis of such thinking (that forms the driving force behind the modernist philosophical thought) becomes clear when we examine the assumptions that form the basis of the positivist/empiricist epistemology (Usher, 1997a, pp.2-3):

- i. The world exists independently of the knower, i.e., the world is objective. It consists of events and phenomenon which are lawful and orderly. Through systematic observations and correct scientific methods (i.e., by being 'objective'), it is possible to know this lawfulness, which can then be used to explain, predict, and control events and phenomena.
- ii. There is a clear distinction between the 'subjective' knower and the 'objective' world. There is also a clear distinction between 'facts' and 'values'. 'Facts' belong to the objective world, while 'values' relate to the subjective knower. 'Subjectivity' involves the concerns, values, and particularity of the researcher, and therefore must not interfere with the discovery of truth.
- iii. There is an order and reason in the social world. Social life is patterned and this pattern has a cause-effect form. Things do not happen randomly and arbitrarily. The goal of research is, therefore, to develop general and universal laws that explain the social world.
- iv. Knowledge is arrived at through the use of the senses, and the application of reason. It is achieved through observation enhanced by experiment and measurement. Both experience and language are transparent, i.e. senses provide unmediated access to the world and there is a clear correspondence between our world of experience/observation and the words we use to represent it. Sensory experience must, however, be filtered through rationality. This is because reason is a universal characteristic. It allows different observers exposed to the same data to be able to arrive at the same conclusions. This is known as inter-subjective verification.
- v. All the sciences or disciplines are based on the same methods of finding out about the world. Thus, natural and social sciences share a common logic and methodology of enquiry.

and control of the ontological conditions. For the philosophers, the political scientists, policy makers, etc. whose thinking is grounded on modernist philosophical thought, such an assumption leads to two fold implications: one, it rationalizes the need for the control of the ontological conditions via an all encompassing discourse or framework. two, it stimulates the search for the single correct answer - the truth that is applicable across time and space. The consequence of such reasoning is the development of discourses or frameworks based on deductive reasoning that are elevated to the status of truth. As a result these discourses and frameworks become meta-discourses and meta-frameworks. The term 'meta' indicates that these discourses are elevated to the status of all encompassing discourses and frameworks that lay down the code of thinking and the standards of behaviour that the society should follow. The assumption is, that the philosophers, the political scientists, the policy makers, the bureaucrats, etc., know what is appropriate for the society. Hence the rationalization of the policy of rational control of the ontological conditions across time and space. This is also the basis of the regulatory philosophy in the financial services industry: rational control of the market-place according to a meta-framework⁴. The existence of a statutory regulator, and the existence of a statutory framework of market regulations based on minimum performance standards for the

- vi. Enquiry and critique into the epistemological - ontological commitments that underlie the use of methods is a pointless exercise.

These assumptions that form the basis of the positivist/empiricist methodology lead to a number of implications: one, determinacy (that there is a certain truth that can be known); two, rationality (no contradictory explanations, convergence on a single explanation); three, impersonality (the more 'objective' and the less 'subjective' the better); four, the ideal knower (that anyone whose senses are not impaired and whose faculty of reason is fully functioning can be a knower); five, prediction (that research should aim for generalization from which predictions can be made and events/phenomenon controlled); six, dehistoricisation (in order to be valid for generalization across time and space, knowledge has to be dehistoricised, i.e., detached from its source in experience and from the place where it was made. Knowledge is detached from its source in experience and hence generalizable through the application of 'reason' - reason being considered a universal attribute. Experience could only become knowledge when acted upon by reason); seven, research as a technology (research need not be reflexive or self-critical, since the focus is exclusively on methods and outcome rather than the research process itself. This ignoring of reflexivity leads to seeing research as 'technology' or technicized process).

Within the realm of generalizable knowledge, the 'best' or strongest kind of knowledge is assumed to be that which is the outcome of using scientific methods. Hence scientific methods came to be seen as the technology (consisting of a set of universal rules) for conducting research and the making of publicly licensable knowledge claims - claims guaranteeing that the world was known truly. The consequence of research becoming a technology is that most researchers in the social sciences (particularly those at the more quantitative end of the spectrum) tend to think only in terms of 'methods' or particular techniques for gathering evidence and very rarely consider the epistemological assumptions of their research. They consider the output of the research as statements of 'truth' that is generalizable across time and space for ordering and control of the ontological conditions.

⁴This statement is not necessarily a 'matter of fact', but the basic premise that forms the basis for this part of the thesis.

control of the markets mechanism, are evidence of the influence of the modernist philosophical thought on the regulatory philosophy.

The question arises: Is the basic premise of the modernist philosophical thought, of the existence of (and hence the rationale for the search of) a single universal mode of ordering and control of the operations of the society that can be applied across time and space, rational? Do the regulators in the financial services industry really know the single correct answer for ordering and control of the financial services industry? Does the present regulatory framework incorporating minimum standards like capital adequacy regulations really provide the most appropriate approach for achieving the regulatory objectives of a safe and efficient marketplace? The existence of tensions in the marketplace emanating out of the dialectical relationship between the regulators and the regulated, and the gradual changes in the regulatory framework⁵ indicate that the answer to these questions is not a definite 'yes'. This calls into question the rationality of the regulatory philosophy, especially in the context of the dynamic ontological conditions in the financial services industry. The question that needs to be investigated is, whether such a philosophy of ordering and control, is compatible with the dynamic ontological conditions of the present era.

2. THE HYPOTHESIS:

The logic or motivation for this part of the thesis lies in the following two-part hypothesis⁶:

- one: the tensions reflecting the regulatory crisis in the financial services industry may be a subset of, or a part of a much wider area of tensions/crises facing the conceptual foundations of the regulatory philosophy: the modernist philosophical thought.**

- two, the alternate philosophical thought which is generally described as postmodernism, may provide us with inspiration and ideas for the formulation of a regulatory strategy and**

⁵Discussed in chapter three (McKenzie and Khalidi, 1996).

⁶It may be noted that this is a strategic hypothesis and not a testing out hypothesis, the emphasis is therefore on evaluation and analysis of the proposition and drawing of conclusions, rather than its testing for acceptance or rejection. This can be understood in the context of Lyotard's (1984a, pp.7) argument that our hypothesis should not be accorded predictive value in relation to reality, rather it should be accorded strategic value in relation to the question raised. Strategic hypothesis according to Lefebvre (1991, pp.60), serves to centre knowledge around a particular focal point, a kernel, a concept or a group of concepts. This is also the aim of our investigation.

regulatory framework that may facilitate the achievement of regulatory objectives while facilitating the amelioration of the tensions inherent in the financial services industry.

The suggestion being, that the tensions that echo the contemporary regulatory crisis associated with the prudential control of banking and securities industry may not necessarily be a reflector of minor deficiencies in the regulatory tools like capital adequacy regulations which can be overcome through their correction (revision and updating). Rather, the crisis may be an embodiment of a much greater problem: the incompatibility of the regulatory philosophy with the ontological conditions prevailing in the financial services industry. In the context of the dynamic ontological conditions of the present era, the present strategy of the regulators involving the revision and the harmonization of the regulatory tools like capital adequacy regulations may therefore not be sufficient for achieving the prudential objectives of a safe and sound market place. It is possible that the problem may lie in the present regulatory philosophy which is grounded on the modernist philosophical thought which rationalizes the imposition of a meta-framework for the ordering and control of the ontological conditions. Such a philosophy may be workable in a static or a slowly changing society, and that too for a certain interval of time, after which a revision of the meta-framework becomes imperative. This interval of time (the period of applicability of a meta-framework) depends upon the rate of change of the ontological conditions in the society. The greater the speed of change, faster the speed of obsolescence of the meta-framework, and shorter the interval of time. In the present era, the momentum of change in our ontological conditions is so fast that it renders a meta-framework obsolete in a very short time. In the context of the financial services industry, the problem is more acute because the problem of imposition of the meta-framework interfaces not only the temporal horizon but also the spatial horizon. The regulators are faced, not only with the challenge of the rapidly changing ontological conditions in the financial services industry brought about by the innovation and the enterprise of the market forces, but also with the problem of globalization of the markets and the market participants - a problem which has severely reduced the power and hence the ability of the regulators and policy makers of nation-states to implement a meta-framework for the rational control of the markets and the market forces within their national space. This problem lies at the heart of the tensions facing the regulators in the financial services industry. This problem also lies at the heart of the tensions/crises facing the modernist philosophical discourse which is increasingly being challenged by a counter/alternative philosophical discourse referred to as postmodernism. The overtone for the regulators being:

one, the need for the re-evaluation of the appropriateness of the present regulatory philosophy (which is grounded on the modernist philosophical thought of rational control of the market place

via a regulatory meta-framework) in attaining its objectives in the context of the contemporary ontological conditions;

two, the need for undertaking an examination of the postmodern philosophical thought with a view towards analyzing its appropriateness for providing direction flags for developing a regulatory strategy that may be compatible with the present ontological conditions.

3. Analysis of the Hypothesis:

The hypothesis can be examined in the context of the argument presented by Kuhn (1970) in his influential work "The Structure of Scientific Revolutions" to explain the revolutionary changes in scientific discourse. Kuhn's thesis is grounded on the concept of 'paradigm'⁷. According to Kuhn's thesis, science during a normal period works within a framework of assumptions called a paradigm. A paradigm is only upset in period of revolutionary science, typically arising in response to an accumulation of anomalies and stresses that cannot be resolved within its framework. In such exceptionally and revolutionary periods, an old paradigm breaks down, and after a period of competition is replaced by a new one - a phenomenon he refers to as 'paradigm shift'⁸. Therefore when paradigms change, they are usually significant shifts in the criteria determining the legitimacy both of problems and of proposed solutions.

In the context of Kuhn's thesis, the tensions and stresses prevailing in the financial services industry may be an indicator of the inadequacy or inappropriateness of the present regulatory framework in dealing with the challenges of the rapidly changing ontological conditions in the financial services industry. The globalization of the industry, and the time-space compression⁹ unleashed by the electronic revolution has brought about a revolutionary change in the ontological

⁷Paradigms are frameworks that function as maps or guidelines for research communities. They define the objects, direction, and methods of research. They provide scientists and researchers not only with maps, but also with some of the direction flags essential for map making, for example, what questions can be asked, what can be researched, what is an appropriate methodology, what constitutes data, what kinds of tests enable beliefs to be counted as knowledge, etc..

⁸According to Kuhn, 'Paradigm shifts' involve major changes in the science's explanatory scheme which happens only rarely when the inadequacies of the previous framework have become limiting.

⁹The term 'time-space compression' implies the speed-up of the process of change in our ontological conditions across time and space. It also implies a reduction in the friction of distance across space. This aspect of change has been covered in part IV of the thesis where two separate chapters have been dedicated to the problem of time-space compression.

conditions prevailing in the financial services industry. The same cannot, however, be said about the regulators or the regulatory framework. The tensions and the stresses emanating from the regulator-regulated dialectic may be an indicator of the break-down of the regulatory paradigm that forms the basis of the present regulatory framework. Hence the need for a paradigm shift in the regulatory framework for achieving the regulatory objective of safe and efficient marketplace.

While Kuhn's thesis is aimed at the phenomenon of paradigm shifts in scientific research, the hypothesis under consideration is closer to the supporting argument of Kuhn's thesis. Kuhn grounded his thesis on the factors that lead to political revolutions. Two elements are essential for a revolution, firstly, the perception of a malfunction that can lead to crisis. Secondly, and more importantly, the intention behind the movements that lead to political revolutions is the resolve to change the political institutions in ways that those institutions themselves prohibit¹⁰. The germinating or the sprouting element in both, political as well as scientific revolutions, is the first element, i.e. the generation of tensions and a growing sense of unease that the existing paradigm has ceased to function adequately for the resolution of the problems. In the context of the financial services industry, the presence of tensions between the regulators and the regulated can be viewed as a symptom of the presence of the first element. The second element (i.e., resolve to change the institution in ways that they themselves prohibit), however, seems to be very conspicuous by its absence, at least amongst the regulators. However, an examination of the conceptual foundations of the regulatory philosophy reveals the presence of the first as well as the second element behind the generation of revolution. Not only are there signs of tensions in the modernist philosophical discourse, but the presence of a challenge to the modernist philosophy is also apparent. The reference is to the postmodern challenge to the modernist philosophical discourse, which aims to change the discipline of philosophy in ways that the latter prohibits.

The aim of this section is to present a case for the need for a paradigm shift in the regulatory philosophy and (as a consequence) the regulatory framework in the financial services industry. Kuhn's thesis provides us not only with the inspiration, but also the direction for undertaking an examination of the philosophical foundations of the present regulatory framework: the modernist philosophical thought. In the context of the tensions/crises facing the regulators in the financial services industry two questions arise:

¹⁰According to Kuhn, initially it is the crisis alone that weakens the role of the political institutions, but as the crisis deepens many of the populace increasingly alienated with the political life commit themselves to some concrete proposals for the reconstruction of the society as per a new institutional framework. At that point the society is divided into two opposing camps, one seeking to defend the old institutional constellation, and the other seeking to institute some new one. In the absence of any supra institutional framework for the adjudication of the conflict, this polarization finally leads the parties to the conflict to resort to techniques of mass persuasion, often including force.

- Is the current regulatory philosophy compatible with the challenges of the present era and the future?
- Is there an alternate philosophical discourse available, or can the postmodernist philosophical thought provide us with a more appropriate conceptual foundation for understanding the present ontological conditions, and for developing a regulatory framework for meeting the challenges of the present and the future?

These questions outline the theme to be explored in this part of the thesis, which is divided into four chapters (chapters four to seven). The first two chapters (Chapters Four and Five) explore the first part of the hypothesis which links the tensions in the financial services industry to the tensions facing its philosophical foundations: the modernist philosophical thought. The last two chapters (Chapters Six and Seven) explore the second part of the hypothesis which argues for the need to examine the alternate philosophical thought which is challenging the legitimacy of the modernist philosophical thought: postmodernism, with the view to provide us with inspiration and ideas for the formulation of regulatory strategies and regulatory frameworks that may help us in achieving the regulatory objective of safe and sound marketplace, while at the same time reducing the tensions apparent in the financial services industry.

CHAPTER FOUR

HISTORICAL ANALYSIS OF THE MODERNIST PHILOSOPHICAL THOUGHT: ITS EMERGENCE, DEVELOPMENT, AND CRISES

1. Introduction:

In the financial services industry, the entrepreneurial forces represented by the industry participants have brought about a revolutionary change in the market environment - a change that has decreased the coercive power of the regulators, magnified the regulatory lag, decreased the potency of the regulatory framework, and has thus created a crisis of confidence in the present regulatory framework in the context of achieving the regulatory objectives connected to the safety and soundness of the market place (i.e. the prudential objectives). The regulatory philosophy in the financial services industry is inspired by the modernist philosophical thought which rationalizes the imposition of a meta-framework for the ordering and control of the ontological conditions. The question that needs to be investigated is: can a philosophy which rationalizes the imposition of a static meta-framework across time and space, be suitable for meeting the challenges emerging from the rapidly changing ontological conditions being induced by the constant innovation of the entrepreneurial forces? This question hints at the possibility, that the present regulatory crisis in the financial services industry may be connected to the much wider crisis facing its philosophical foundations: the modernist philosophical thought. This is the central idea to be investigated in this chapter. The aim is to undertake a historical analysis of the emergence, the development, the crises, and the subsequent reformulations of the modernist philosophical thought, with a view to outline the problematical nature of the modernist philosophy itself. The aim is also to show how the changes in ontological conditions affected, as well as, were affected by the actions of the political, intellectual, and the entrepreneurial forces; how the changes in the ontological conditions affected a crisis in the modernist philosophical discourse, requiring a revision and reformulation of the discourse for its regeneration; and how the present crisis in modernity differs from the previous crises. The aim is to connect the tensions and crisis of confidence facing the financial services regulator with the logic for the tensions and the crisis of confidence facing its conceptual foundations: modernist philosophical discourse itself. Along with this primary aim, there is also a secondary aim of the chapter, an aim that is directly connected to the tensions in the financial services industry. The secondary aim relates to the use of the storyline of the emergence and the development of the modernist philosophical thought to investigate into the emergence and the development of a number of concepts and phenomena like systemic risk, cross border contagion, globalization, etc., as well

as the problematical basis of a number of our present-day governance structures that we take for granted as a priori truths, structures that are actually a part of a meta-framework developed at a point of time and a product of modernist philosophical thought, which have become problematical in the context of the present ontological conditions. The aim is to raise questions and direction flags in an effort to improve our understanding of the problems of the present era. However, prior to an investigation into the history of the modernist philosophical thought, it is necessary to restate the rationale for the choice of the hypothesis and the strategy to be applied for the analysis of the hypothesis. This is the aim of the next section.

2. The Hypothesis:

2.1. Rationale for the Hypothesis:

Analysis of the financial services industry suggests the proposition that, while the term 'revolutionary' can be associated with the change in the market environment brought about by the entrepreneurial forces, the same however, cannot be said about the changes initiated by the regulators in the context of the regulatory framework for the control of risks. Although one cannot deny the regulatory initiatives, especially those by the banking regulators under the auspices of the Basle Committee of Banking Supervision, the efforts of the securities regulators in the area of prudential control have been relatively minimal. In the case of banking regulators, there have been some initiatives aimed at ameliorating the crisis. The Basle Concordat of 1975 (and its subsequent revisions) was a major milestone in banking regulation and supervision in terms of enhancing the cooperation between the regulators of multinational banks (the home and host regulators). The other major achievement of the committee was the Basle Accord of 1988, that laid the global floor for capital adequacy requirements. These two agreements were perhaps the earliest major initiatives for dealing with the problem of systemic risk at a global level. While the Basle Accord was an evidence of the realization of the phenomenon of globalization and its ramifications, it did not represent any change in the regulatory philosophy. It was also based on the modernist philosophy of rational control of the ontological conditions via a meta-framework developed at a point of time but imposed as an all encompassing meta-discourse applicable across time and space. More recently, however there have been a few initiatives like the Fisher Report, the pre-commitment approach to capital requirements, the New Zealand initiative, etc., which show an incremental change in the regulatory philosophy¹. However, in spite of these regulatory initiatives, the reality is that the regulatory

¹These aspects have been discussed in Chapter Three (McKenzie and Khalidi, 1996).

reforms are not commensurable with the speed and extent of innovation and change being initiated by the market forces. A differential rate of change is quite apparent. The increased pace of time-space compression has increased this differential. When we add to this the differences in supervisory competence and other cross border complications², the logic for the present regulatory crisis becomes understandable.

The problem appears to lie in the present regulatory philosophy which is grounded in the modernist philosophical discourse which rationalizes the need for the rational ordering and control of the operations of market forces via a meta-framework. Such a proposition is incompatible with the present day ontological conditions, where the market environment in itself is in a state of flux. This is the crux of the problem facing the regulators. This is also the rationale for this chapter. Any framework developed at a point of time, incorporates knowledge evolved up to that point of time. Imposing it as an all encompassing rigid meta-framework may help in reducing some of the problems in the short run, but will be creating a greater problem in the long run.

Imposition of a meta-framework across time and space for the ordering and control of the ontological conditions, impedes the process of development and the evolution of knowledge by: one, creating a sense of contentment among the philosophers, political scientists, academics, etc. involved in the advancement of knowledge. The same applies to the regulators. Two, it acts as a barrier to the evolution of knowledge and the development of the market place. The financial services industry in itself is an excellent example. The reference is to the market entry barriers and other prohibitory regulations which during the time they were operational, not only created market inefficiencies but also severely impeded the market development process. Three, with the expansion of the knowledge base and the changes in the environment of the marketplace, the basic assumptions which form the basis of the meta-framework (for the ordering and control of the marketplace), becomes problematical. As a consequence, difficulties arise in achieving the objectives that form the basis of the meta-framework. Thus after every major change in the market environment, an incremental change in the meta-framework becomes inevitable. This implies that if the pace of the revision of the meta-framework does not match the pace of developments in the marketplace, a crisis can be expected. The time-space compression of the late twentieth century, which incorporates the phenomenon of globalization and the speed-up of the process of innovation, both of which can be identified with the increase in the momentum of evolution of knowledge, has created a crisis of confidence in the basic premise of the modernist philosophical thought: rational control of the ontological conditions via an all encompassing meta-framework. Since the present regulatory philosophy in the financial services industry is a subset of the modernist philosophical discourse, the

²For example, systemic risk, and cross border transfer of contagion.

present regulatory crisis in the financial services industry may therefore be identified with the crisis of confidence in the modernist philosophical discourse itself. In other words the logic for the crisis in the modernist philosophical discourse may provide the direction flags for understanding the logic for the present regulatory crisis in the financial services industry. This is the first part of the hypothesis that had been laid out in the introduction to this part of the thesis:

one: the tensions reflecting the regulatory crisis in the financial services industry may be a subset of, or a part of a much wider area of tensions/crises facing the conceptual foundations of the regulatory philosophy: the modernist philosophical thought.

two, the alternate philosophical thought which is generally described as postmodernism, may provide us with inspiration and ideas for the formulation of a regulatory strategy and regulatory framework that may facilitate the achievement of regulatory objectives while facilitating the amelioration of the tensions inherent in the financial services industry.

This chapter involves an investigation of part one of the thesis only. The strategy for investigation and analysis of part one of the hypothesis is the theme of the next section.

2.2. Strategy for the Analysis of the Hypothesis:

The hypothesis under consideration can be analyzed in terms of a framework with the philosophical discourse on one side, and the ontological conditions on the other side. In the context of this framework, the modernist philosophical thought aims at constructing knowledge in the form of an idealized meta-framework for the ordering and control of the ontological conditions in the name of reason. In other words it assumes the philosophical discourse as an independent function and the ontological conditions as the dependent function³. It rationalizes the need for the ontological conditions to be a function of the philosophical discourse, rather than the other way round. The presence of tensions is an indication of the inconsistency, and hence the disparity or incompatibility between the two sides of the framework. The presence of tensions is also an indicator of the need

³The logic for this statement has been discussed in footnote 3 in the introduction to Part III of the thesis. The overriding commitment of the modernist project was the search for the deep underlying realities that form the basis of the events and phenomenon that we experience. The aim was to develop overarching theories which could explain and give meaning to the disorder and contingency of the world. The aim was to apply this knowledge to control and change the world we live in. This, according to Usher (1997b, pp.28) was the totalizing dream of the modernist project, a dream which in the end had nothing to do with reason but something to do with desire - the desire for mastery and ultimately control.

to revise and reinvent the meta-framework in order to make it compatible with the ontological conditions. It is also an indicator of the problematical nature of a philosophical discourse that aims to order and control the ontological conditions by means of a rigid meta-framework.

Rational ordering and control of the ontological conditions by means of a rigid meta-framework is also the basis of the regulatory philosophy in the financial services industry. Tensions between the regulator and the regulated in the financial services industry are a symptom of the incompatibility of the regulatory framework with the present ontological conditions in the financial services industry. Rational control of the markets and the market forces was plausible when the pace of innovation was slow and the nation-states were governable as separate islands. In the present era of heightened pace of innovation, and global competition between the markets, as well as the market forces, such a philosophy becomes deeply problematical. Hence the need for a critical reappraisal of the philosophical foundations of the regulatory framework in the financial services industry. This is also the area of investigation suggested in Part One of the hypothesis which states: the tensions reflecting the regulatory crisis in the financial services industry may be a subset of, or a part of a much wider area of tensions/crises facing the conceptual foundations of the regulatory philosophy: the modernist philosophical thought.

The discussion to follow in this chapter aims to undertake a historical analysis of the evolution, and the development of the philosophical foundations of the present regulatory framework: the modernist philosophical thought. Using David Harvey's (1992) "Condition of Postmodernity: An Inquiry into the Origin of Cultural Change", as the basic reference for the generation of the storyline, the primary aim of the chapter is to return to time zero and to examine, one, the circumstances leading to the emergence and the development of modernist philosophical discourse; two, the problematical interface between the modernist philosophical discourse and the ontological conditions, and the effect of the changes in the ontological conditions in terms of engendering the various phases of crises in the modernist philosophical thought; three, the subsequent regeneration of the modernist philosophical thought through the revision and reformulation of the modernist philosophical discourse; and four, the present crisis, how it differs from the earlier ones. The secondary aim, as already outlined earlier is to use the storyline of history to examine and understand the circumstances behind the emergence and development of some of the concepts and phenomena, as well as the problematical basis of some of the governance structures connected to the tensions in the financial services industry that we take for granted as a priori truth.

3. Historical Analysis of Modernist Philosophical Thought:

History of modernity⁴ can be divided into two distinct phases: one, the launch of the enlightenment project which can be associated with the inception of the Renaissance era around mid fifteenth century. And two, the modernist era which can be associated with the project of modernity which according to Habermas (1985, pp.9) came into focus during the eighteenth century and developed into an extraordinary effort on the part of the enlightenment philosophers to develop objective science, universal morality and law, and autonomous art according to their inner logic. Their aim was the rational organization of every day social life.

To understand the logic for the present crisis, it is necessary to undertake a historical analysis of both these era: one, the enlightenment era, that saw the laying of the foundations of the modernist philosophical discourse which still continues to dominate the policies and the problems of the present era; two, the modernist era or the project of modernity which went through a number of phases of crises but was able to regenerate itself through a revision and reformulation of its philosophical discourse. Examination of the two era should allow us to draw inferences that may help us to understand the present crisis facing the modernist philosophical thought, and the discourses and frameworks (for example the regulatory framework in the financial services industry) founded on the modernist philosophical thought.

3.1. The Enlightenment Project:

As an epoch, the emergence of modernism can be traced to the inception of the Renaissance era (from around mid 15th century) and the birth of the ‘Age of Reason’ which later on came to be

⁴Some critics are very specific about the difference between modernity and modernism. They define ‘modernity’ as a social and political project with its emphasis of science, reason, progress, and industrialism. Whereas ‘modernism’ is specifically referred to the end of the nineteenth century cultural movement that developed as a counter culture to the foundational rationality of the technoeconomic order of modernity in favour of sentiment, intuition, and the free play of imagination (Ref: Kumar, 1995, pp.85). Here, however, both the terms are being used synonymously to refer to the concept of modernity.

known as the ‘Enlightenment Project’⁵. It was during the Renaissance era that Western history was divided into three epochs (Kumar, 1995, pp.73):

- Ancient or the classical antiquity.
- Medieval period, middle ages, or dark ages⁶.
- Modern - a time of emergence from darkness, a time of reawakening. The revival and the rebirth of culture - the ‘Renaissance’ of art, culture, and learning.

The medieval era was characterized by the arbitrary authority of the church and the monarch, who based their legitimacy on tradition and theology, both of which were given the status of eternal truth. This era sustained itself on revelation and progress founded on providence. The Renaissance was a future largely conceived in terms of the past - the era of classical antiquity. According to the thinkers of the Renaissance era, classical antiquity had set eternal standards, the endeavour of the forces behind the Renaissance was therefore the recovery of the treasures of the earlier era, the writings of Plato, Aristotle, etc.. Renaissance was based on a cyclical concept of history. It was a revolutionary break from the stagnation of the middle ages, but it was a revolution conceived on the model of the ancients, as the movement of a wheel, or the circle that returns to its beginning (Kumar, 1995, pp.74).

Although the secularism of the Renaissance was backward looking, linked to the cyclicalism of the classical model, it was the consequence of the vigour, vitality, and the confidence in their ability (at least in emulating, if not surpassing the classical era) generated during the Renaissance period that helped in the generation of new knowledge and brought about a revolutionary change in the ontological conditions of the society. It was this change that afforded the mental freedom for the

⁵The origin of modernity itself is a moot point. According to Habermas (1985), the term ‘modern’ in its Latin form ‘modernus’ was used for the first time in the fifth century to distinguish the (then) contemporary period which had become effectively Christian from their Roman and pagan past. However over the period, with varying content, the term ‘modern’ appeared and reappeared exactly during those periods in Europe when the consciousness of a new epoch was perceived. According to Cahoon (1996, pp.12-13), some critics consider the sixteenth century protestant reformation and the rejection of the monopoly of the Roman Church, and the development of a humanistic scepticism of Erasmus (1466-1536) and Montaigne (1533-1592) as the origin point of the modernity, while some consider the seventeenth century scientific revolution of Galileo (1564-1642), Descartes (1596-1650), Newton (1642-1727), etc. as the origin, still there are others who point to some other movement as the starting point of modernity. As a historical parameter, Renaissance period (from around mid 15th century) and the birth of the enlightenment project appears to be an appropriate landmark for tracing the development of modernism.

⁶Francisco Petrarch (1304-74), the ‘father of humanism’ is credited with the invention in the fourteenth century of the notion of the ‘dark ages’: a period from the fall of Rome to the rebirth of society, that he saw as beginning in his own age. The period has also been marked as the thousand years from the foundation of Constantinople in the fourth century to its fall in 1453 (Kumar, 1995, pp.73).

philosophers and social scientists of that era to question the truths rationalized by tradition and theology, that laid the foundations of a new movement in philosophy: the launch of the enlightenment project, and the age of reason.

The aim of the enlightenment thinkers was to develop a better society, the aim was to transform the medievalist society into a progressive one by removing the dogma of religion and tradition, and substituting it with reason. It was a forward looking project which aimed to change the conceptual foundations of our existence from providentialism to the belief in progress and the power of human reason to produce freedom. The fundamental achievement of the Renaissance period, according to Harvey (1992, pp.245), was the development of perspectivism⁷. This involved the conceptualization or the envision of the world from the standpoint of the 'seeing eye' of the individual. It gave prominence to the science of optics and the ability of the individual to represent what he or she sees as in some sense 'truthful', compared to superimposed truths of mythology and religion. The key is the connection between individualism and perspectivism. It is this connection that provided an effective material foundation for the Cartesian principals of rationality that became integrated into the enlightenment project.

Rene Descartes (1596-1650), the author of the Cartesian principles of rationality is generally regarded as the father of modern philosophy. Descartes was different from the other philosophers of the era in the sense that he had no reverence for the classical age. His unique ambition was not to add a contribution to the existing philosophical discourse, but to reconstruct the whole of philosophy anew⁸. He insisted on the rejection of all past systems of thought. There had to be a new beginning based on a new method for searching out the truth - reconstruction of knowledge on the basis of human reason alone. His philosophical work, 'Meditations on First Philosophy' and his famous 'method of doubt' were an attempt to rationally reconstruct philosophy afresh from scratch by ridding the mind of all accumulated preconceptions.

⁷This perspectivism was different from that presented later (around 1910) by Ortega Y. Gasset which challenged the rationalistic ideals of homogeneous and absolute space. He formulated a new version of the theory of perspectivism which insisted that there were as many spaces in reality as there were perspectives on it. He viewed that the external world is interpreted through the different alternative systems of concepts and beliefs and that there is no authoritative independent criterion for determining that one such system is more valid than another.

⁸The basis of his conviction according to Flew (1979, pp.89), was that ancient cities that have become large towns in process of time, are as a rule, badly laid out as compared to those that are laid out by a designer.

"I must once for all seriously undertake to rid myself of all the opinions which I had formerly accepted, and commence to build anew from the foundation, if I wanted to establish any firm and permanent structure in the sciences⁹."

Descartes theory of knowledge starts with the quest for certainty, for an undoubtable starting point or foundation on the basis alone of which progress was possible. The aim was to develop a discourse based upon the certainty incorporated in human reason, that would be universal across time and space. In other words the aim was to develop a meta-discourse based upon human rationality. Three facets of his philosophy that had a major impact on the development of modernist philosophical thought (and also government policies founded on it) are worth mentioning. One, his insistence on mathematical reasoning as the paradigm for his new system of knowledge¹⁰. Descartes (1596-1650) believed that the essence of science was the discovery of relationships that could be expressed in mathematical form. He argued that deductive reasoning based on mathematics should be the basis of all human inquiry including theology. Descartes shifted the emphasis away from studying the meaning of existence (ontology) to the process of knowledge formation (epistemology). His methodology of hypothetico-deductive¹¹ logic later-on became the principle rhetoric of the modern social scientist which still continues to dominate our social science research¹². Two, the Cartesian dualism, which involves the separation of 'mind and matter' or 'res cogitans and res extensa'¹³; Three, the location of the point of certainty of his philosophy "cogito ergo sum" (I think therefore I am). In other words the point of certainty that he located was the awareness of his own self. He thus gave a first person twist or an ethnocentric character to the theory of knowledge¹⁴. This may also be construed as having induced a paternalistic attitude to philosophy that still continues to dominate the modernist philosophical discourse. This paternalistic attitude is also apparent in

⁹Descartes, René (1996, pp.29).

¹⁰"Those who are seeking the strict way of truth should not trouble themselves about any object concerning which they cannot have certainty equal to the arithmetical or geometrical demonstration." (quoted in Flew, 1979, pp.89).

¹¹Deductive logic is a process of reasoning by which a specific conclusion necessarily follows from a set of general premises, as against inductive reasoning, the approach of Francis Bacon (1561-1626) which involves conclusions being drawn from a set of premises mainly based on experience or experimental evidence.

¹²McKenzie (1997, pp.10, 14-17).

¹³This facet of Descartes philosophy comes under discussion in part IV of the thesis in the discussion on the concepts of time and space.

¹⁴Blackburn (1996, pp.101).

government policies (including those related to the regulation of financial markets) inspired by the modernist philosophical thought.

A crucial ramification of Descartes pursuit of certainty in philosophical discourse was the formation of the belief that there was only one possible answer to any question. And according to Harvey (1992, pp.27), the enlightenment project took this notion that there was only one possible answer to any question as an axiomatic. From this it followed that the world could be controlled and rationally ordered if one could only picture and represent it rightly. But this presumed that there existed a single correct mode of representation, and if this mode could be uncovered, it would provide the means to enlightenment ends. And this was what the scientific and mathematical endeavour of the enlightenment philosophers were all about. The assumption about the existence of, and hence the rationale for the search for the single correct mode of representation was reinforced by the concept of physical space and mechanical time developed during the Renaissance era¹⁵. Since the conceptual foundations of the philosophers of the enlightenment era with regard to time and space were developed during the Renaissance period, accurate maps and chronometers, therefore, became the essential tools for organizing the vision of the enlightenment thinkers. While the map allowed the acknowledgement of other nationalities, it also provided a totalizing vision for environmental determinism. It led to a perception of the globe and the future spatial order, of a homogeneous society with absolute qualities that were ethnocentrically conceived. Similarly the chronometer allowed a totalizing vision of the time dimension with respect to thought and action. Time was conceived to be linear both forward as well as backwards implying retrojection and prediction as symmetrical propositions. The combination of the physical absolute concepts of time and space, with the certainty accorded by Descartes' hypothetico-deductive logic, the belief in the existence of the single correct mode of representation, and the paternalism induced by Descartes "cogito ergo sum", contributed to the development of a totalizing vision among the enlightenment thinkers with regard to the organization and control of societies over time and space. It also encouraged paternalistic tendencies among the enlightenment (and later modernist) philosophers. It encouraged their endeavour towards attaining command over the future through the powers of scientific prediction, through social engineering and rational planning, and the institutionalization of rational systems of social regulation and control. This absolute or rather the mechanical concepts of time and space which led to the totalizing vision of the enlightenment philosophers, later-on also became the central dilemma of the modernist/enlightenment project.

¹⁵Prior to Descartes' categorial separation of mind and matter dualism, there was an accepted ambiguity regarding the concepts of time and space. This facet has been discussed in detail in the chapters on the concepts of time and space in part IV of the thesis.

The central dilemma of the enlightenment project which later-on also became the central theme and hence the dilemma with the modernist project too, was its rather mechanical ideological base - the Newtonian logic of 'Clockwork Universe', according to which, if universe is made up of material objects interacting with each other through forces that obey truly universal laws, and if rules like that of action and reaction apply precisely throughout the universe, then the universe can be regarded as a gigantic machine, a kind of cosmic clockwork, which will follow an utterly predictable path forever once it has been set in motion¹⁶. Newton's logic of the universe as an ordered and logical place also implied that the behaviour of the material world could be explained in the context of the fundamental laws which had been built into the fabric of the universe. The application of this logic to social sciences and the consequent failure of this schema of thought under the pressure of time and space compression is the story behind the alterations in the enlightenment philosophy. Whenever a major change in the ontological conditions occurred, a crisis ensued, which required a revision and reformulation of the philosophical discourse to bring it in conformity with the altered state of the ontological conditions. This dilemma has very aptly been summarised by Harvey (1992, pp.252):

"Enlightenment thought operated within the confines of a rather mechanical 'Newtonian' vision of the universe, in which the presumed absolutes of homogeneous time and space formed limiting containers to thought and action. The break down of these absolute conceptions under the stress of time-space compression was the central story of the birth of the nineteenth and early twentieth-century forms of modernism."

3.2. The Project of Modernity:

3.2.1. Background:

The term modernity or modernism do not actually signify the birth of a new school of philosophical thought. It is actually the continuation, or more appropriately, the further development of the enlightenment philosophy, but with a difference. Prior to the launch of the project of modernity in the second half of the eighteenth century, cyclical concepts of history and time were dominant. Along with the story of growth and progress, the feeling of decay and degeneration persisted. In this respect Kumar (1995, pp.77-78) presents the thoughts of Bacon and Hume. Francis Bacon (1561-1626) did not believe in unending progress. He believed that learning had its infancy, its youth, its maturity, and its old age. He believed that the world had made a great progress in knowledge, techniques, trade and industry, but the time was running out. David Hume (1711-76) believed that

¹⁶White and Gribbin (1992, pp.23-24).

mankind was so much the same in all times and places, that history informs us of nothing new or strange. Its chief use was only to discover the constant universal principles of human nature. This view of history was gradually weakened in the second half of the eighteenth century leading to a new concept of history in which the moral terrorism of Christianity - the apocalyptic expectation of the end of the world was exorcized, and the Christian philosophy of 'path to salvation' was secularized to 'path to progress': the millennium became scientific and rational, the dawn of an era of unending human progress on earth. The idea of progress as elaborated by Kant (1724-1804), Condorcet (1743-94) and other philosophers of the eighteenth century became the building block of the new idea of modernity. Modernity now meant a complete new start on the basis of completely new principles - a break from the past. Past is a different country, history changes human nature, moderns are different from the ancients. One could no longer look to the past for illumination and instructions. Moderns therefore live in a new world, and are thrown back entirely for new ways of thinking and acting. Modernity implied that all cyclic pretensions were thrown off. Modernity was therefore open ended, and implied continuous creation of new things¹⁷. A major epoch in the history of modernity was the French Revolution of 1789. The French revolution changed the meaning of the word 'revolution' which lost its earlier meaning of returning to the starting point. Now it meant creation of something completely new. The French revolution took the world into a new era of history. It marked the birth of modernity¹⁸.

As a concept, although modernity is generally conceived to be open ended, and involves the rejection of the past as a source of inspiration, and stimulates towards continuous creation or revolution of new ideas and institutions, but in its formative phase, the prophets of modernity were convinced that there was a meaning to modernity. The French revolution was the principle vehicle of the new consciousness which implied the aim of modernity as the achievement of freedom under the guidance of reason¹⁹.

While French revolution gave modernity its form and consciousness - revolution based on reason, it was the Industrial revolution which provided it with its material substance. This facet of modernity has strangely been ignored by most critics and commentators of modernity²⁰. It was the British industrial revolution of the late eighteenth century that gave modernity its material form. The connection between modernity and revolution was therefore reflected not only in the political and

¹⁷Kumar (1995, pp.80).

¹⁸Kumar (1995, pp. 80-81).

¹⁹Kumar (1995, pp.81).

²⁰Kumar (1995, pp.82).

intellectual sphere, but also in the economic sphere. Industrial revolution speeded up the process of economic development to the point where it took on revolutionary proportions. It turned societies still poor and agrarian into concentrated centres of power. It not only transformed the balance of power from the feudal to the bourgeois, but also provided the material input of goods, guns, and ships for the political forces of the imperialist nation-states to join hands with the economic forces to overwhelm the resistance all round the globe and colonize the world in the name of modernity (and reason), and at the same time also facilitating the launch of the first phase of globalization²¹.

3.2.2. The Concept of Modernity:

Habermas (1985, pp.9) describes modernity as a project that came into focus during the 18th century. It was a project that amounted to an extra ordinary intellectual effort on the part of the enlightenment philosophers:

- "to develop objective science, universal morality and law, and autonomous art according to their inner logic",
- two, "to release the cognitive potential of each of these dimensions from their esoteric forms".

The aim of the modernist philosophers and social scientists was the rational organization of everyday social life using the accumulation of knowledge generated by many individuals working freely and creatively for the pursuit of human emancipation and the enrichment of their life. The logic behind the endeavour was two fold: one, the scientific domination of nature promised freedom from scarcity, want, and the arbitrariness of natural calamity; two, the development of rational forms of social organization and rational modes of thought promised liberation from the irrationalities of myth, religion, superstition, release from the arbitrarily use of power, as well as from the dark side of our own human nature. The conviction was that only through such a project could the universal, eternal, and the immutable qualities of all humanity be revealed.

It was during this period that the process of hypothetico-deductive reasoning formulated by Rene Descartes²² developed into the principal rhetoric of the modern social scientists. The modernist

²¹An epoch which I will return to later.

²²Descartes (1596-1650) believed that the essence of science was the discovery of relationships that could be expressed in mathematical form. He argued that deductive reasoning based on mathematics should be the basis of all human inquiry including theology. Deductive logic is a process of reasoning by which a specific conclusion necessarily follows from a set of general premises, as against inductive reasoning, the approach of Francis Bacon (1561-1626) which involves conclusions being drawn from a set of premises mainly based on experience or experimental evidence. Adam Smith (1723-1790) and Karl Marx (1818-1883) are perhaps the two best known examples of social scientists of the modernist era applying Descartes deductive logic, whose writings have had a powerful impact on government

social scientist and philosophers applied Descartes' hypothetico-deductive argumentation not only to understand the evolution of society, but also to develop universal frameworks for developing a better society. They laid the foundation of modernity with its emphasis on certainty, optimism, and a rationally constructed social order. It is this proposition that has continued to dominate our economic and social policy formulation (implicitly, if not explicitly, up to the present time). The application of hypothetico-deductive logic to develop universal and objective propositions to order and control the problems of the world was also the basis of the economic system formulated under the Bretton Woods Accord. It is also the basic proposition behind the regulatory framework for the control the risks in the financial services industry. Bretton Woods Accord faced a crisis of confidence in the early 1970s and ultimately collapsed under the pressure of the changing ontological conditions. The regulatory framework for the control of the risks in the financial services industry is presently feeling the pressure of the changing ontological conditions in the financial services industry brought about by the forces of globalization and the electronic revolution. The question is, can the problem of regulatory control of the financial services industry be resolved within the percepts of the modernist philosophical thought, or is a new fresh approach to the problem of regulatory control inevitable? To answer this question it is necessary to examine the history of modernism.

An examination of the history of modernism reveals that modernity as a project and as a philosophical thought went through a number of crises, but was able to regenerate itself through a revision and reformulation of its discourse(s) to continue as the conceptual foundations not only for understanding and resolving the problems of that era, but also for managing and controlling the future. The question that needs to be answered is: whether the present crisis is yet another crisis that can be overcome and the modernist philosophical thought regenerated through yet another phase of revision and reformulation of the modernist philosophical discourse? The answer to this question lies in the similarity or difference between the present crisis and the earlier ones faced by the project of modernity. It is therefore necessary to examine the earlier bouts of crises and the revision and regeneration experienced by the project of modernity. It is only then that we may be able to analyze how the present crisis differs from the earlier ones. This is the subject of analysis of the next section.

3.2.3. The Crises and the Regeneration of Modernity:

This section undertakes an examination of the cycles of crises and the subsequent phases of revision and regeneration of modernist philosophical thought, with a view to understand and explain the key difference that separates the present crisis from the earlier ones. The basic reference used for the generation of the storyline, is David Harvey's (1992) "Condition of Postmodernity: An Inquiry into

policy making during the last hundred years. Refer to McKenzie (1997).

the Origin of Cultural Change". Historical analysis of modernity shows that modernity as a philosophical movement went through a number of crises, but was able to recreate and regenerate itself through the creativity of the philosophers, although sometimes in collusion with the bourgeois entrepreneurs and the colonialist ambitions of the political oligarchy controlling the reigns of power of the imperialist nation-states. The reference is to the revision and regeneration of the philosophical discourse of modernity itself, which followed each phase of crisis faced by the modernist philosophical thought. In each phase of revision and regeneration, the term 'modern' was used to express the consciousness of an epoch that related itself to the past as antiquity, in order to view itself as the result of a transition from the old to the new. The fundamental problem with each phase of modernism/modernity was the search for eternal truth: the universal and objective framework for the organization and control of the society. The eternal truth formulated at the start of each phase of regeneration of modernity held its fort for a certain length of time until the forces of time-space compression forced a change in the ontological conditions that led to a crisis that could not be resolved within the dictates of the (then) contemporary philosophical discourse. The philosophical discourse became a liability rather than an asset. Thus, the situation was ripe for the creative destruction of the existing modernist philosophical discourse and the destructive creation of a new one announcing the heralding of a new era of modernism. In aggregate, the project of modernity can be divided into four distinct phases of crisis formation, the last of which is still unresolved. It is essentially for gaining insights for understanding and perhaps for resolving of the present crisis (the reverberations of which are also echoed in the financial services industry), that we²³ are undertaking an analysis of the earlier phases of crises and the strategy adopted for their resolution. We begin with the crisis of 1846-47.

(A) The First Crisis of Modernity: The depression of 1846-47 was perhaps the first major crisis faced by modernity²⁴. This was also perhaps the most important crisis faced by the project of modernity. Its importance relates not only to the elements of the crisis, but also to the elements of the strategy adopted for surmounting the crisis. Both aspects are important in terms of their influence on the subsequent cycles of crises faced by the modernist philosophical thought.

The Crisis: The crisis is important because it was perhaps the first recorded application of the concepts of systemic risks, business cycles, and cross border transfer of contagion. Harvey (1992,

²³The word 'we' implies the author as well as the reader.

²⁴Harvey, (1992, pp.260).

pp. 260) describes it as the "first unambiguous crisis of capitalist overaccumulation". Capitalism had matured to a sufficient degree by 1847-48. Over-production combined with reckless speculation had become rife, which had a negative effect on the financial condition of the economy and ultimately created the circumstances of a depression which began in Britain and quickly engulfed the whole of the capitalist world. The outcome was a sudden paralysis of the economy in which surplus of capital and labour lay side by side with apparently no way to reunite them in profitable and socially useful union. The situation shook the confidence of the bourgeoisie and challenged its sense of history and geography in profound ways. Three facets of this crisis are worth recounting. One, the evolution of the phenomenon of business cycles²⁵. Two, the evolution of the concept of systemic risk. The collapse of the financial markets and its contagious effect on the other markets actuated the need for the rational organization and control of the financial markets. It was only after 1850, that stock and capital markets were systematically organized and opened to general participation under legal rules of incorporation and market contract. Three, the evolution of the concept of cross border transfer of contagion. Events of 1846-47 proved that Europe had achieved a level of spatial integration in its economic and financial life that was to make the whole continent vulnerable to simultaneous crisis formation²⁶. This implied that the certainty of absolute space and place gave way to the insecurity of a shifting relative space in which events in one place could have immediate and ramifying effects in several other places. In other words systemic risk and cross border contagion had become a reality.

Resolution of the Crisis: The crisis caused by the depression of the mid nineteenth century was resolved through the combined initiative of the nation-states and the capitalist (or the entrepreneurial) forces. The strategy was time and space displacement. Nation-states went on the path of global expansion through a major phase of imperialist conquest involving 'creative destruction'²⁷ and 'destructive creation'²⁸ of other nation-states. Concurrent with the initiative of the imperialist nation-states, the capitalist sector also went on a major phase of spatial and temporal displacement. While the two complimented each other, there was a fundamental difference. While the imperialist nation-states were involved mainly in conquest, colonization and hence reordering of physical space, the

²⁵It was much later that this crisis was linked to the phenomenon of economic cycles.

²⁶This development is reflected in the synchronic nature of the political revolutions all across Europe.

²⁷'Creative destruction' refers to the deterritorialization of world spaces (other nation-states) which are stripped off their preceding specifications.

²⁸'Destructive creation' refers to the reterritorialization of the colonized nation-states according to the beliefs and conventions of the colonial and imperial administrations and for their convenience.

capitalist sector was not only involved in expansion of its markets, but also in time-space compression through the power of 'innovation'. The capitalist sector recreated itself. New organizational forms involving separation of management and ownership were developed - the birth of the corporate form of organization. Similarly new forms of credit were created - stock and capital markets were rationally organized and opened to general participation under legal rules of incorporation and market contract. These innovations coupled with technical and organizational innovations in production helped to speed-up the circulation of capital in mass market. Time and space was also compressed through innovations in transport and communications²⁹. Capitalism thus became embroiled in an unprecedented phase of massive long term investment in the conquest of space. All this changed the conception of space and time in radical ways. Not only was the relative space revolutionized through innovations in transport and communications, but what that space contained was also fundamentally reordered through the partnership of the creative and destructive forces of capitalism and imperialism.

An examination of the strategy adopted for the resolution of the crisis of 1847-48 indicates the presence of some of the elements that later became the source of subsequent crises faced by modernity. Four of these (related to the process of creative destruction and destructive creation) are worth discussing. One, the creative destruction and destructive creation launched by the imperialist forces in the process of colonization of the world spaces led to the generation of uniformity amongst the world spaces, and laid the foundations of the process of globalization we are presently experiencing. Two, it also expanded the periphery of cross border contagion and systemic risk from a European to a global phenomenon. Three, the greed, the lust for power and the passion for colonization and destruction which was the motivating force behind the creative destruction and destructive creation of the imperialist powers led to inter-imperialist rivalries, that culminated in not one but two global wars. The experience of colonization and the inter-imperialist conflicts may also be a reason for the increase in nationalist sentiments that seem to increase rather than decrease with the intensification of the globalization process. This is an important facet of the problem of national sovereignty and subsidiarity that resists against the development of a global solution for a problem of global proportion. Four, there was a key difference in the process of creative destruction and destructive creation of the imperialist forces and that of the capitalist forces. While the former relied on conquest and colonization, the essence of the latter's strategy was innovation and marketing. In the context of the present era, while the process of creative destruction and destructive creation of the imperialist forces has practically ceased, the latter forces are still not only very much active in

²⁹This included the expansion of railway network, advent of telegraph, growth of steam shipping, building of Suez canal, beginning of radio communication, automobile travel, etc..

changing the global environment, but are growing stronger. This is a crucial factor that separates the capitalist sector from the governments of nation-states. This is also a key factor that forms the basis of the dialectical relationship between the policy makers of nation-states and entrepreneurial forces. This is very much apparent in the regulatory crisis in the financial services industry where a disjunction is apparent not only in terms of their spatial reach of the regulators and the regulated³⁰, but also and more importantly in terms of their creative capacity³¹.

There is another very crucial facet of the change initiated by the nation-states after the crisis of 1846-47 that not only Harvey (1992), but most other commentators dealing with the problematic of globalization and/or the modern - postmodern debate appear to have completely missed out, with important ramifications in the context of their ability to take cognizance of the problems of the present era. The reference is to Roland Robertson's (1990) concept of 'wilful nostalgia' which forms the basis of the global standard of civilization set up during 1880-1920 period, which has become problematical in the present state of the world - a state in which, one end of the spectrum appears to reflect Marshal McLuhan's concept of 'global village'³², while the other side of the spectrum appears to show a renewed emphasis on plurality and difference. An examination of the global standard of civilization set up during the 1880-1920 period, and the concept of 'wilful nostalgia', allows us not only to appreciate and understand the basis for the existence of the two sides of the spectrum, but also the logic for the crisis facing the framework that forms the underpinnings of the contemporary global civilization.

Robertson (1990) concentrates on 1880-1920 as a period of major change. From the present day perspective, it stands out as perhaps the most crucial period of our history. It was this period that saw the laying of the foundation of the underpinnings of our present day global civilization. It was during this period that the concept of national identity was created by the national elites of the Western countries through a politically motivated contrived/synthetic/artificial wilful nostalgia. It emerged out of the 'homogenizing' requirements of the nation-state in the face of ethnic and cultural diversity. The French and the American revolutions, had already spread across the Western Worlds the belief or the idea of people living as citizens of a nationally constituted society. It was the period that followed that synthetically created nationalism was imposed as an ideal for overcoming local ethno-cultural diversity, and to produce standardized citizens whose loyalties to the nation-state

³⁰The jurisdiction of the regulators of the nation-states is delimited by their geographical frontiers, the reach of the capitalist forces on the other hand, has acquired global proportions.

³¹This aspect will be discussed in Chapter Five.

³²McLuhan and Powers (1989).

would be unchallenged by the extra-societal allegiances³³. It was during the 1880-1920 period that grandiose national symbols, monuments, and the myths about the self image of nations in the full spectrum of time (past, present, and future) were created to unify the people as one nation. Although the concept of nation-state originated in the Western world, it gradually diffused to the other countries of the world, either through the colonization process, or through the need of the natives of (actual or potential) colonies for an idea or ideal to resist the colonization process. In fact, the colonization process itself was an effort to achieve spatial expansion of the synthetically created national identities.

³³According to Lefebvre (1991, pp.111-2), there are two popular versions of the concept of 'nation' and 'nationhood':

- one, and perhaps the more popular version is the definition of 'nation' as a sort of a substance that has sprung up from nature (or more specifically from a territory with natural borders) and grown to maturity with historical time. The nation is thus endowed with consistent reality. This thesis promotes patriotism and even absolute nationalism as natural and hence eternal truths. This is the notion of 'nation' and 'nationhood' espoused by the political and intellectual elites of nation-states.
- The other view of 'nation' is that nation and nationalism are merely ideological constructs. It is neither a substantial reality nor a body corporate, rather it is a fiction projected by the politicians, and other interest groups onto their own historical conditions and origins, to begin with as a way of magnifying these in imaginary fashion, and later-on as a way of masking class contradictions and seducing the impoverished and the down-trodden public into an illusory national solidarity. It is easy, on the basis of this hypothesis to reduce national and regional questions to linguistic and cultural ones.

Actually (according to Lefebvre) there is not much difference between the two views. The latter is simply another interpretation of the former. The problem with both these arguments is that they leave space out of the picture. They are actually mental constructs about the real space. When considered in relationship to space, the concept of nation and nationhood is connected to two moments. One, the concept of nationhood implies the existence of a market gradually built over a historical period of varying length. Such a market is a complex ensemble of commercial relations and communication networks. Two, the concept of nationhood also implies violence - the violence of a military state, be it feudal, bourgeois, imperialist, or some other variety. In other words, it implies a political power controlling and exploiting the resources of the market or the growth of the productive forces in order to maintain and further its rule. Although it is difficult to pinpoint the exact relationship between spontaneous economic growth (the first moment) and violence (the second moment), and their precise respective effects, but an analysis of the history of space will indeed affirm that the two moments do combine forces and produce a space: 'the space of nation-state'. The combination of the two moments in the development of culture, languages, ethnicity (nationhood) becomes evident if we take a historical analysis of changing geographical frontiers of the space of nation-states over a period of time, and its effect on the evolution of culture and languages. The overtone is, culture, languages, and the idea of nationhood or ethnicity are not any metaphysical realities that require to fulfil a particular criteria. They evolve over a period of time and are constantly in the process of evolution and change. With the improvement of communications, and the increase in 'inter' and 'intra'-nation migration, as the geographic borders become more porous, as the different cultures and languages interact, the process of evolution of 'nation' and 'nationhood' continues.

According to Robertson, it was during this period that the wilful nostalgia among the national elites fed into the works of the leading social scientists of the era with mutually amplifying results. The consequence was the development of the grand narratives or the global discourses of Western social theory of what a modern society should look like, and how it should operate. It was during this period that the national identity became the key feature of intra-national and inter-national relations. It was during this period that the model for the organization of humanity became institutionalized as the 'global standard of civilization'. It involved four major reference points:

1. The basic constitution and state-structured features of national societies.
2. The right and modes of participation of individuals in society.
3. The conception of international relations as globe wide in their reach.
4. The increasing thematization of humankind or humanity (concretely in such contexts as the Geneva and Hague Conventions, the World Court, and towards the end of the period in question, the League of Nations).

It is this model of global civilization set up during the first phase of globalization which grew out of the wilfully created synthetic nationalist nostalgia, that has become problematical in the second phase of globalization³⁴. The reason is obvious. Unlike the first phase which was developed and launched by the philosophers and the political forces of nation-states with the aid of the capitalist forces, the second phase of globalization is primarily the consequence of the entrepreneur led capitalist forces search for profits and power. And in their search for profits and the power that comes with the increase in market share, the capitalist forces can and may shed the excess baggage of national identity which is a remnant of the wilful nostalgia and the system or the standard of intra and inter national relations created by the modernist philosophers during the 1880-1920 period. This disjunction between the political and the capitalist forces has the potential for cracking the model of global civilization established during the 1880-1920 period. The tensions in the financial services industry are perhaps an indicator of the strain facing this global model of civilization.

³⁴Robertson (1990, pp.51) refers to the present phase of globalization as the second phase of globalization. The first phase was initiated during the 1880-1920 period as a joint effort by the political forces, the capitalist forces, and the intellectual forces (the philosophers and the social scientists of the project of modernity). This phase was important on two counts: one, the extensive development of the rapid means of communications across the globe - the wireless, the airplane, and other such technological developments; and two, the development of the protocols and the various forms of international agreements for the organization of the world-as-a-whole, such as the institutionalization of World Time and the globe-wide standardization of the Gregorian calendar. This also includes the framework for global standard of civilization' discussed earlier.

(B) The Second Crisis: The next major crisis in modernity can be associated with the qualitative transformation in the preconceptions of modernism and enlightenment thought that took place during the 1910-15 period -a transformation that created a sense of confusion in the modernist philosophical discourse³⁵. This confusion was exacerbated into a crisis by the global war of 1914-18.

With regard to World War, two points stand out. One, that it was the improvements in communication and the consequent enhanced level of international cooperation between nation-states that amplified a localized conflict into a global war. Two, while modernism asserted internationalism and universalism, it could never settle its account with parochialism and nationalism. In fact, it was modernity's concept of uniform and standardized citizenship which provided the framework for the political forces to give their lust, their greed, and their will to power, the garb of a project of national salvation and a project of spatial expansion of national identity. It was this 'will to power' to expand their empires by colonizing other nation-states that eventually ended up in the collision between the imperialist/colonist empires: the World War I.

Following the episode of World War I, extraordinary intellectual attempts were made to overcome and even dominate the crisis in the experience of space and time that had built up before the first world war, and to fight off the nationalist and geopolitical sentiments that the war expressed. This endeavour for transformation of modernity came to be known as **heroic modernism** (Harvey, 1992, pp.279). Heroic modernism was basically the struggle between different currents of modernism vis.a.vis the search for an eternal philosophy which could redeem them from the formless universe of contingency and provide the impetus for a new projet for human endeavour. The aim was to show how localism and nationalism could be overcome and how some sense of global project to advance human welfare could be restored. Enlightenment thinkers had postulated human welfare as their goal. Heroic modernism was in fact the relaunch of the Enlightenment project with a difference. The central motive of the new modernists became efficiency and function. The new modernist held the view that 'form' followed 'function', and that spatial rationality should be imposed on the external world in order to maximise individual liberty and welfare, thus the philosophy of 'becoming' took the centre stage in the project of heroic modernism. The modernists of this heroic era regarded multi-

³⁵The general preconceptions about time and space were seriously challenged. Around 1910 Ortega Y. Gasset challenged the rationalistic ideals of homogeneous and absolute space. He formulated a new version of the theory of perspectivism which insisted that there were as many spaces in reality as there were perspectives on it, and that there are as many realities as points of views. Discovery of non Euclidean geometry shattered the supposed unity of mathematical language, and the concept of absolute space. The concepts of time also underwent major revisions. Einstein's special theory of relativity of 1905 and the general theory of 1916 changed the very basic concepts of time. In short the whole world of representation and knowledge underwent a fundamental transformation during this short space of time. The qualitative transformation in the preconception of modernism created a sense of confusion (Harvey, 1992, pp. 266-273).

perspectivism and relativism as the fundamental cause of the conflict that led to the World War. Their political and intellectual response was therefore the search for the eternal and the absolute qualities of modernity. As a consequence, modernism took a strong positivist turn³⁶, and through the intensive efforts of the Vienna circle established a new style of philosophy: Logical Positivism³⁷ - a style or school of philosophical thought that was to become central to the social thought after the World War II.

(C) The Third Crisis: The key problem with the project of heroic modernism was the search for 'eternal truth' which laid the foundations for the interlinking of reason with myth³⁸. One such myth created was the image of rationality incorporated in the machine, and the power of contemporary technology³⁹. It was emphasised that rational order was required to be imposed for achieving freedom and liberty⁴⁰. The problem with the approach of elevating a thought to mythological proportions was that once the myth of machine rationality was abandoned, any myth could be lodged in the central position of the 'eternal truth'. The Greeks and the Christians had already shown the way. The consequence was the amplification of the national identity already created through the strategy of 'wilful nostalgia' to mythical levels: the birth of the Nazi (of blood and soil, of race and fatherland, of destiny and place) and the Fascists (speed, power, and violent militarism) myth. The merging of these mythologies with the 'will to power' of the political forces transformed the project

³⁶Positive because it confines itself to what is positively given, avoiding all speculation. 'Positivism' is a version of traditional 'empiricism' but without the tendencies to idealism and scepticism that the position attracts.

³⁷Also called logical empiricism and scientific empiricism, it reflects the ideas and attitude towards philosophy associated with the Vienna Circle. The group which was founded in 1924 by Schlick and ended with his death in 1936, included Bergman, Carnap, Feigl, Neurath, and Waismann (Wittgenstein although associated with the group from 1927 to 1929 was not a full member). The central interest of the Vienna Circle was the unity of Science and the correct delineation of scientific method.

³⁸According to Harvey (1992, pp.35) during the inter-war years (i.e., the period of the heroic era of modernism), desperate attempts were made to search for a mythology that could somehow straighten the society out of troubled times (after all, the Greek civilization was founded on mythology, the Christians values were also built on myths).

³⁹Harvey (1992, pp.31).

⁴⁰This was also the key influence in the strong positivistic modernist philosophy of post World War II era.

of Heroic Modernism into the poisonous form of **Reactionary Modernism** which led to World War II⁴¹.

The post World War II period saw yet another transformation of modernity: the era of **High Modernism**. The foundations of high modernism were laid during the inter-war years by the efforts of the Vienna circle and their emphasis on positivism which became central to social thought during the phase of high modernism beginning after the second world war. Harvey (1992, pp.35) describes the 'High modernism' as the corporate capitalist version of the enlightenment project of development for progress and human emancipation. This form of modernism which relied on corporate bureaucratic power and rationality, was in reality a return to the myth of the efficient machine as the embodiment of all human aspirations. It was based on the belief in linear progress, absolute truths, and rational planning of ideal social order under standardized conditions of knowledge and production. The resulting state of modernism was positivistic, technocratic, and rationalistic and was imposed as the work of an elite band of avant garde planners under the watchful eye of US hegemony.

(D) The Present Crisis: It was in the mid 1960s that high-modernism started to experience the pressure of the changing ontological conditions. The foundations of high-modernism began to crack as the rebuilding of the war torn economies of Western Europe and Japan were completed. The monetary system set up under the Bretton Wood Accord started to feel the stress of change as the Japanese and German economies started to export their surplus to USA. The development of Euro Market as a financial market outside the regulatory control of the nation-states, the unforeseen events like the oil crisis, and last but not the least the electronic revolution, were some of the factors that severely strained (or more appropriately, rather cracked) the foundations of the meta-framework on

⁴¹An interpretation of the causes that led to the World War II shows that Nazism's emphasis on fatherland, Arian superiority, social progress, and national achievement although poisonous, offensive, and brazen, was not necessarily the cause of the World War II, rather it was the same cause which led to World War I. The reference is to the dialectic between 'Being' and 'Becoming' or 'place' and 'space'. As long as the sentiments were confined to a place there was no problem, the problem began when they started to impinge on the space of others. The problem began when: firstly, they began to encroach on the others right to live (the reference is to the Holocaust or the extermination of Jews), and secondly, they began to encroach on the others right to control their own destiny (the reference is to the implementation of the Nazi philosophy towards colonization of the rest of the world). This applies not only to the World Wars I and II, but to all conflicts prior to and/or after the two global wars. It was the philosophy of 'becoming' and the 'will to power' rationalized by the modernist philosophical thought that was the cause of the conflict. It is the spirit of creative destruction and destructive creation that is at the root of all the conflicts, whether it is based on the foundation of humanism, or the myth of Arian superiority, or the salvation of pagans from the doom of hell by the spread of the word of God, or even the pure imperialistic greed to rape, plunder, and colonize others and expand their empires.

which high modernism was built. Once again modernity is in crisis. The meta-framework that sustained the era of high modernism appears to have lost quite a bit of its potency. The question arises: Are we seeing, or waiting to see the emergence of yet another form of modernism to replace high modernism, or is this crisis different? To answer this question, one needs to sit back and review the logic behind the need for revision of the modernist philosophical discourse after each phase of crisis, and its comparability with the present crisis.

Examination of the emergence of the enlightenment philosophy reveals that, although, the enlightened philosophers replaced revelation and tradition with reason as the foundational logic of their discourse, the basic schema of environmental determinism, however, did not change. The schema of the modernist philosophy was based on two key assumptions: one, that there existed one ideal mode of ordering the world: the truth; and two, if the universal eternal and immutable qualities of all humanity were to be achieved, then it was necessary that the ontological conditions be controlled via a meta-framework that was representative of the ideal mode of ordering the world (assumption #1). The overtone of this logic was that the philosophers⁴² of the enlightenment/modernist era beginning with Descartes presumed their own discourse to be the ideal single correct mode of ordering and controlling the world, a discourse that was universally applicable across time and space. The philosophy of 'becoming' was, and is, therefore at the heart of the modernist philosophical thought. It is this philosophy of 'becoming' that also forms the basis of the meta-frameworks developed and implemented by the government policy makers for the ordering and control of the operations of the market forces.

The episodes of crisis formation, and the subsequent need for the revision of the philosophical discourse for the regeneration of modernity puts a question mark on the two key assumptions of the modernist philosophical thought. One, the existence of a single mode of ordering and controlling the world, and two, the need or the rationale for the ordering and control of the ontological conditions: the philosophy of 'becoming'. Instead of the modernist philosophers⁴³ controlling and ordering the ontological conditions, it was rather the changes in the ontological conditions that created a crisis of confidence in the meta-framework developed by the political and intellectual forces for ordering and control of the ontological conditions. The crisis forced the philosophers, the economists, and the political scientists to reappraise and revise their meta-narratives and their meta-frameworks in order to bring their aspirations for the future in line with the problems

⁴²This includes political scientists, economists, academics, etc. who base their discourse on the modernist philosophical thought.

⁴³This includes the policy makers and political agents whose conceptual foundations are based on the modernist philosophical discourse.

of the contemporary ontological conditions. Thus, after each phase of crisis, modernity was regenerated, either through the revision of the old meta-framework, or the generation of a new one. One of the hallmark of modernity was its ability to sustain itself by adapting its discourse/framework for meeting the challenges of the changed circumstances.

The present phase of crisis, however, appears to be different. The intense pace of time-space compression of the late twentieth century generated since the launch of the electronic revolution has led to the acceleration of the momentum of change in our ontological conditions. Now it is not simply the change in our ontological conditions, but rather the pace of change in our ontological condition, and hence the pace of obsolescence of the modernist philosophical discourses and their meta-frameworks, which is the source of the problem. Now, it is the foundational schema of modernity: 'rational control of the ontological conditions through a meta-framework' that is being questioned. The assumption that is now being challenged is that modernity has endless capacities for adaptation through the merging of rationality with progress⁴⁴. This is the view of a significant body of opinion, consisting of critics and philosophers labelled as postmodernist who hold the view that the project of modernity is deeply problematical. The implication being, that any policy framework grounded on the modernist philosophical thought may also be problematical. The tensions in the financial services industry are perhaps a symptom of this problem.

It is ironical that about five hundred years ago it was the oppressive and degenerative qualities of tradition and religion that provoked and stimulated the launch of the enlightenment project, now it is the oppressive and degenerative qualities of modernism that forms the basis for the launch of a rebellion in the form of postmodernism. About five hundred years ago, it was the inception of the Renaissance era and the knowledge generated through the voyages of discovery that not only brought about a change in the environmental conditions but also induced the confidence among the philosophers to question the discourses of the pre-modern era. After a passage of half a millennium, history has repeated itself - the electronic revolution (incorporating both the information and communication technology) has increased the pace of change in our ontological conditions (the most important component of which relates to the pace of knowledge generation) to such an extent that the rationality of the basic assumptions of the modernist philosophical thought have become questionable. The following quotes by Lyon and Harvey summarize the dilemma with modernity:

"Once providence was doubted as a means of interpreting history, but now progress, its secular counterpart succumbs to the same fate, modernity is going no where".

Lyon, (1994, pp.71).

⁴⁴Lyon (1994, pp.54)

"The tensions between internationalism and nationalism, between globalism and parochial ethnocentrism, between universalism and class privileges, were never far from the surface. Modernism at its best tried to confront the tensions, but at its worst swept them under the rug or exploited them for cynical, political advantage."

Harvey (1992, pp.24-25)

4. Conclusion: The Predicament Facing the Modernist Philosophical Discourse:

The discussion on the historical analysis of the modernist philosophical thought had two objectives: one, the primary objective was to investigate into and outline the problematical nature of the modernist philosophical thought which forms the underpinnings of the regulatory philosophy and its rationale of the need for a meta-discourse or a meta-framework for the ordering and control of the ontological conditions. The discussion involved an investigation into the crises that affected the modernist philosophical discourse and the subsequent revisions and/or reformulation that followed for the regeneration of the modernist philosophical thought, and how the present crisis differs from the earlier ones. The key difference between the present crisis and the earlier ones is that it is not simply the change in ontological conditions, but the pace of change of ontological conditions that is at the heart of the present crisis. Two, the secondary objective was to introduce the emergence and development of some of the concepts and phenomena connected with the tensions facing the regulators in the financial services industry. This also included an examination of the emergence of some of the present governance structures which we take for granted as a priori truths, which are in fact a part of the meta-frameworks developed and implemented by the political and intellectual forces inspired by the modernist philosophical thought itself. Both these objectives can be combined into a general objective of the chapter: historical analysis of the modernist philosophical thought was undertaken with a view to help us in understanding the present crisis of confidence facing the modernist philosophical thought, and its connection with the tensions in the financial services industry.

In the context of the overall objective of the chapter, the first crisis of modernity, and the strategy for surmounting the crisis are of special importance. The crisis was perhaps the first known occurrence of business cycles, systemic risk, and cross border transfer of contagion. The aftermath of the crisis is also important, because of its association with the launch of the first phase of globalization. It is also important in the context of the establishment of the global standard of civilization. This involved the application of wilful nostalgia to homogenize and integrate people

delimited by certain geographical frontiers, into one nation. The emphasis on national societal identity, and national sovereignty, has been a salient feature of all intra-national and inter-national relations following the development of the global standard of civilization which was a meta-framework for the organization of humanity based on four reference points: one, the nationally constituted society; two, the individual; three, the system of international relations (world politics); and four, the humankind. The present state of crisis in modernity is very much linked to the changes developing, and hence the tensions emanating from within the elements of this meta-framework which after all is also a product of the modernist philosophical thought:

- i. National Societies are increasingly exposed internally to the problems of heterogeneity and diversity, and at the same time are experiencing both external and internal pressures to reconstruct their collective identities along pluralistic lines.
- ii. Individuals are increasingly subject to ethnic, cultural, and religious reference points.
- iii. The system of International Relations is becoming more and more fluid and multipolar.
- iv. The idea of humankind as a species is being subjected to contested thematization and scrutiny.

What are the implications of these changes? Robertson (1990, pp.57) provides a possible answer:

"It may be that the overall form of globalization may not hold - that we may enter a qualitatively different stage in the 'evolution' of humanity. Meanwhile, nostalgic resistance to globalization - whatever its form - will continue. The global vocation of the social theorist is, on the other hand, to be positively - as opposed to negatively and nostalgically - analytical and critical."

The discussion on the different phases of crises and the consequent revision of the modernist philosophical discourse is an evidence of the limits of human rationality in ordering and controlling the future. It is limited to the ontological knowledge attained up to a point of time. It cannot and should not, therefore, be imposed as an all encompassing rigid framework for organizing and controlling the ontological conditions across time and space. The regulatory philosophy in the financial services industry which is founded on the modernist philosophical thought, and aims to order and control the financial markets by means of an all encompassing meta-framework, suffers from the same problems as its conceptual foundations.

The logic for the problems encountered by the policy makers in the financial services industry in achieving their objectives can be understood in the context of the logic for the crisis facing the conceptual foundations of the regulatory philosophy: the modernist philosophical thought. The logic for the present crisis facing the modernist philosophical discourse can be understood in the context of the crisis that led to the decline of the philosophical discourse that dominated the pre-

enlightenment era. Historical analysis of the emergence of modernist philosophical discourse suggests the possibility of drawing analogy between the modernist challenge to the pre-modern philosophy, and the postmodern challenge to the modernist philosophy. The basis of this analogy is two fold. One, it was the revolutionary change in the ontological conditions during the Renaissance era brought about by the enterprise of the bourgeois, the knowledge generated by the philosophers and the men of science, and the voyages of discovery of the explorers, etc., that created a crisis of confidence in the schema of environmental determinism based on the truth linked to tradition and religion that dominated the pre-modern philosophical discourse. A similar analogy can be applied to the present crisis facing modernist philosophical discourse, but with a difference. It is not only the revolutionary change in the ontological conditions associated with the electronic revolution and globalization, but also the pace of change in the ontological conditions generated by the entrepreneurial and the intellectual forces that has created a crisis of confidence in the modernist schema of rational control of the ontological conditions by means of a meta-framework that is universal across time and space. This analogy is also applicable to the financial services industry where the innovation and entrepreneurialism generated by the market forces (banks, securities firms, stock exchanges, etc.) have contributed to a revolutionary change in the market environment. The tensions in the financial services industry emanating from the regulator-regulated dialectic are an indicator of the crisis of confidence facing the regulatory framework in the financial services industry in achieving its objectives related to the rational control of the prudential environment of the marketplace. It is therefore safe to conclude that the pace of innovation and the pace of change in the market conditions have created a crisis of confidence in the two basic assumptions⁴⁵ of the philosophical foundations of the regulatory framework: the modernist philosophical thought.

Another possible analogy that can be drawn from the enlightenment challenge to the pre-modern philosophical thought and the postmodern challenge to the modernist philosophical thought, relates to the evolution and the progression of knowledge. It was the knowledge generated during the Renaissance era that induced the necessary confidence among the philosophers and intellectuals of that era to question the pre-enlightenment philosophy that rationalized the imposition of meta-narrative of environmental determinism grounded on the discourse of religion and tradition. In the context of the present situation, it is the increase in the pace of knowledge generation and its subsequent effect on the ontological conditions that may be associated with the growing scepticism of the modernist rationale of environmental determinism by means of a meta-framework based on

⁴⁵One, the existence of the single correct mode of ordering the world (i.e., the existence of truth waiting to be discovered); and two, the need to control the ontological conditions via a meta-framework (which is given the status of truth) if the universal, immutable, and eternal qualities of all humanity are to be realized.

deductive logic and mathematical reasoning. This analogy is also very conspicuous in the financial services industry where a growing knowledge differential in favour of the market forces (regulated) vis.a.vis the public policy makers (the regulators) is clearly evident. The effect of this ever increasing knowledge differential between the regulator and the regulated corresponds to a crisis of confidence in the former, and a growing self confidence in the latter. This is evidenced from the actions of the banks and the securities firms who appear to have moved from a strategy of indirectly pro-activating a change in the regulatory framework by prospecting for regulatory loop-holes and developing strategies for legally bypassing them, to a strategy of directly pro-activating a change in the regulatory framework by drawing attention to the inadequacies in the regulatory framework and the superiority of their own internal control framework in the context of achieving the regulatory objectives. The reference is to the initiative of J. P. Morgan and the other financial institutions to get their VAR (Value at Risk) framework models accepted as a regulatory tool for the calculation of minimum statutory capital requirements, which is an evidence of the growing self confidence of the regulated entities vis.a.vis the regulators. The increasing knowledge differential between the regulator and the regulated in favour of the latter calls into question, not only the assumption that the policy makers know the truth: the meta-framework for ordering and controlling the markets, but also the assumption that the policy makers know what is best for the market participants⁴⁶. It calls into question the suitability of imposing a meta-framework on the market participants based on the policy maker's/regulator's assessment of the most appropriate mode of ordering and control of the markets and the market participants, when their own knowledge is problematical. Another important and a potentially important ramification of the increasing knowledge differential between the regulator and the regulated relates to the relationship between knowledge and power. The difficulty facing the regulators in implementing their regulatory framework is an evidence of the increase in the power based on knowledge vis.a.vis the coercive power based on sovereign authority of the national regulator⁴⁷.

The two analogies presented above are an indicator that the resolution of the present crisis in the financial services industry within the parameters of the modernist philosophical thought is a problematical proposition⁴⁸. Both these propositions which are derived from the historical analysis

⁴⁶The reference is to the paternalistic instincts of the regulators.

⁴⁷This aspect of the problem has been covered in the discussion on Foucault's philosophy of power in Chapter Seven.

⁴⁸This inference is also supported by Robertson's (1990) exposition of the crisis facing the model of global civilization institutionalized about a hundred years ago by the modern social scientists with nation-states as the sovereign, and the centre of power and authority.

of the modernist philosophical discourse support the hypothesis which was the underlying theme of investigation of this chapter:

The tensions reflecting the regulatory crisis in the financial services industry may be a subset of, or a part of a much wider area of tensions/crises facing the conceptual foundations of the regulatory philosophy: the modernist philosophical thought.

CHAPTER FIVE

PROBLEM WITH THE PHILOSOPHY OF 'BECOMING'

1. Introduction:

The problem with the modernist philosophical thought was the topic of investigation of the previous chapter which involved a historical analysis of the emergence and the development of the modernist philosophical discourse. The conclusion derived from the analysis was that, the modernist philosophical thought went through a number of crises, but was able to regenerate itself through a revision of the philosophical discourse while still remaining within the broad confines of its basic assumptions: the existence of truth, and the need for ordering and control of the ontological conditions by means of a meta-framework that is representative (of their interpretation) of the truth. The reason for each crisis was a major shift in the ontological conditions which made the (presumed truth of the) philosophical discourse incompatible with the ontological conditions of that era. A revision in the discourse (the presumed truth) was therefore required to regenerate and sustain modernism. The key difference between the present crisis and the earlier ones is that, now it is the very logic of modernist philosophical thought that is being questioned: the existence of, and hence the rationale for the search for the truth, and the need for the development and implementation of a meta-framework based on (their¹ interpretation of) the truth for the ordering and control of the ontological condition. The storyline of the emergence and the development of the modernist philosophical thought also brought into focus the emergence and development of a number of problematical facets of our present ontological conditions including the governance structures that form the basis of the regulatory framework in the financial services industry (the existence of which is also connected to the modernist philosophical thought), which we take for granted as a priori truths. The overall aim of the previous chapter was to link the tensions in the financial services industry with the crisis facing the conceptual foundations of the regulatory philosophy and the regulatory framework: The hypothesis that formed the basis of the investigation in the previous chapter was:

The tensions reflecting the regulatory crisis in the financial services industry may be a subset of, or a part of a much wider area of tensions/crises facing the conceptual foundations of the regulatory philosophy: the modernist philosophical thought.

¹The reference is to the architects of the truth, for example, the philosophers, the social scientists, etc.. In the context of the financial services industry, the architects of the truth (in most cases) would be the regulators.

This chapter continues with the investigation into the same hypothesis, it takes the investigation a step further. Here the topic of investigation that comes under attack is the central dilemma of the modernist philosophy and of any other philosophical thought which rationalizes the philosophy of 'becoming': the need for the ordering and control of the ontological conditions by means of a meta-discourse, and the belief in the rationality of meta-discourses or the grand narratives based on human reason to withstand the test of time and space compression. The problem with such grand narratives or meta-discourses is that they are based on incomplete knowledge (knowledge accumulated by a person or a group of persons up to a point of time), and on assumptions, a priori truths, and deductive logic. As a consequence they become problematical when applied across time and space to control the ontological conditions. This is also the problem with the regulatory philosophy.

This chapter investigates into the problematical nature of two of the grandest grand-narratives (or meta-discourses) of the modernist philosophical thought:

1. Max Weber's (1864-1920) philosophy of bureaucratic rationality.
2. Karl Marx (1818-83) and Friedrich Engels' (1820-95) 'Manifesto of the Communist Party of 1848'.

The former is important because it forms the philosophical foundations of the regulatory framework in the financial services industry, and the problems evident in Weber's theory of bureaucratic rationality are very much apparent in the operational framework of the regulators too. The latter is important not only because it is perhaps the grandest of the grand narratives, but also because it directs our attention to the central dilemma with the modernist philosophical thought. Marxism (or 'scientific socialism' as it was referred to) was thought to be an ideal system that could be applied across time and space. It formed the philosophical foundations of the socialist economic system, the collapse of the system was taken by many as not only the victory of the capitalist system over the socialist system, but also as the final crisis in the modernist philosophical thought.

"The fall of Communism can be regarded as a sign that modern thought - based on the premise that the world is objectively knowable, and that the knowledge so obtained can be absolutely generalized - has come to a final crisis²."

Max Weber's discourse on 'bureaucracy', and Marx and Engels' 'Manifesto of the Communist Party' are both important to our analysis of the hypothesis, because they not only allow us to understand the limitations of human rationality to develop a complete system that can be generalized across time and space to order and control the ontological conditions, but more importantly, they also allow us an insight into the force that is at the back of tensions in Weber's bureaucratic rationality, the force

²Havel, Vaclav, (1992), "End of the Modern Era", New York Times, March 1, pp.15 (Quoted in Kumar, 1995, pp.149).

that provides the explanation for the failure of socialist economic system and the crisis in modernist philosophical thought: the entrepreneur. Entrepreneur is the force of change whose contribution Weber, as well as Marx and Engels acknowledge, but prefer to disregard in their rationally constructed model/system for the ordering and control of the ontological conditions.

Entrepreneur is perhaps the most potent force of change in our ontological conditions whose actions provide the principle logic for the present crisis in modernist philosophical thought. Entrepreneur is a the creative destroyer and destructive creator par excellence whose actions lead to fundamental changes in our economic and social system, thereby changing the basic assumptions that form the basis of any discourse or framework for the ordering and control of the ontological conditions. Unfortunately many of our social, political, and economic theorists have either ignored or given inadequate attention to the contribution of this force of change to the process of economic development, which is also the central weakness of their theories. It is also the disregard of the power and the impact of the contribution of this force in introducing and institutionalizing change, that forms the principal rationale for the present crisis of confidence facing the modernist philosophical thought - a crisis that is also echoed in the tensions in the financial services industry. This is the reason why an examination of Joseph Schumpeter's (1959) 'Theory of Economic Development' is crucial not only for understanding the tensions in the financial services industry, but also for understanding the crisis of confidence facing the philosophical foundations of the regulatory framework in the financial services industry: the modernist philosophical thought. Schumpeter's theory is important because it not only allows us to appreciate the concept of market mechanism (including the logic for Adam Smith's 'invisible hand'), but also because it helps us to understand the process of economic development (the outward shift of the production possibility frontiers) that eventually leads to a major change in our ontological conditions. The chapter therefore undertakes an investigation into Joseph Schumpeter's 'Theory of Economic Development', and then extends his ideas to explain the present crisis facing the modernist philosophical thought, a crisis that is connected to the speed-up and the intensification of the development or the entrepreneurial process - a crisis that provides an explanatory logic for the tensions apparent in the financial services industry.

The discussion to follow is divided into five sections: the next section (section two) examines the problematic nature of Weber's theory of bureaucratic rationality, and any other social or economic theory based on bureaucratic rationality. Weber's theory is important because it forms the philosophical foundations of the regulatory framework in the financial services industry, and the weaknesses and failings discernable in the theory are also conspicuous in the regulatory framework in the financial services industry. Weber's theory of bureaucracy is also important because it provides

us with an insight into the logic for the crisis of confidence facing the modernist philosophical thought. The next section (section three) involves a deconstructive analysis of Marx and Engels' 'Manifesto of the Communist Party'. The aim is to employ Marxist philosophy as an illustrative example for explaining the problematical nature of any philosophy of 'becoming' which aims to impose an ideal meta-framework for the ordering and control of the ontological conditions. Marxist philosophy is an extreme example because it involves the replacement of the entrepreneur with the bureaucrat, thereby effectively eliminating the contribution of the entrepreneur, who is the key force of change in our ontological conditions. Examination of Marx's philosophy is also important because it provides us with the spring board for examining Schumpeter's 'Theory of Economic Development', which is the area of investigation of section four. The aim of section four is to introduce the key features of Schumpeter's 'Theory of Economic Development'. This includes the concept of 'circular flow', the concept of 'development', the concept of 'entrepreneur', and the contribution of the 'entrepreneur to the process of economic development' - a process that engenders a change in our ontological conditions, and in the process, affects a change in the basic assumptions that form the basis of any meta-discourse or any meta-framework for ordering and control of the ontological conditions. Section five extends Schumpeter's 'Theory of Economic Development' to explain the present crisis of confidence facing the modernist philosophical thought - a crisis that can be connected to the speed-up of the momentum of the development process, and as a consequence, the speed-up of the process of change in our ontological conditions. This section aims to provide an explanatory logic for the present crisis of confidence in modernist philosophical thought by outlining and examining the variables that affect the development process, the change in these variables and their influence in the speed-up or the intensification of the development process - a process that also implies an increase in the momentum of the change in our ontological conditions. The final section (section six) provides the conclusions of the chapter and its connection with the first part of the hypothesis under investigation.

2. Weber's Theory of Bureaucratic Rationality:

2.1. Introduction:

The discussion under this theme aims to analyze the problematic nature of the operational framework of the regulatory agencies which is grounded on Weber's philosophy of bureaucratic rationality. The

discussion to follow, involves a deconstructive analysis of Max Weber's essay on 'bureaucracy'³, and its connection with the problematic nature of the regulatory framework in the financial services industry. Examination of Weber's discourse on bureaucracy reveals two prominent features that are not only manifested in the operational framework of the regulatory agencies, but are also at the heart of the tensions in the financial services industry. These are:

- Predisposition Towards Machine Rationality.
- Manifestation of Information Asymmetry.

2.2. Predisposition Towards Machine Rationality:

The area of investigation of this section is the operational framework of the public agencies representing the nation-states. The underpinning of their operational framework is based on Weber's concept of bureaucracy - organization as a machine. The area of investigation is therefore the problematic nature of Weber's discourse on bureaucracy, and its connection with the tensions in the financial services industry. Weber's discourse on bureaucracy is important because it outlines the schema⁴ around which the operational framework of the governmental agencies (including the regulatory agencies in the financial services industry) has been developed. Weber's discourse on bureaucracy is also important because the weaknesses and the failings of the discourse are very much conspicuous in the operational framework of the governmental agencies, including the financial services regulators. Weber's discourse is also important because Weber was perhaps the first philosopher to rationalize the need for regulatory organizations based on bureaucratic rationality:

³Weber, Max, (1967), "Bureaucracy", in H. H. Gerth, and C. Wright Mills (eds.), "From Max Weber: Essays in Sociology", Routledge and Kegan Paul Ltd., London., pp. 196-244.

⁴Max Weber (1967) refers to 'bureaucracy' as a rational-legal form of organization. Rational because the means are specifically designed to achieve certain specific goals, and legal because authority is exercised by means of a system of rules and procedures. Weber (pp.196-198) outlined six main characteristics of bureaucracy:

- I. The principle of fixed and official jurisdictional areas, which are generally ordered by rules, that is, by laws or administrative regulations.
- II. The principles of office hierarchy and of levels of graded authority.
- III. The management of the modern office based on written documents (the files), which are preserved in their original or draught form.
- IV. Office management which presupposes thorough and expert training.
- V. Official activity which demands full working capacity of the official irrespective of the fact that his obligatory time may be firmly delimited.
- VI. The management of the office which follows general rules, which are more or less stable, more or less exhaustive, and which can be learned. Reduction of modern office management to rules is deeply embedded in its very nature.

"Among the purely political factors, the increasing demand of a society, accustomed to absolute pacification, for order and protection ('police') in all fields exerts an especially persevering influence in the direction of bureaucratization."⁵

Weber viewed the essence of modernity as the application of 'dispassionate objectivity' to all spheres of life. Weber's vision of bureaucracy was based on 'rationalism' - the gradual adoption of a calculating attitude towards more and more aspects of life. He defined 'calculating attitude' as a system of procedures, rules, and regulations based on machine rationality. Weber's concept of objectivity and rationality are similar to Newton's clockwork universe⁶. He conceptualized bureaucracy as a machine for operating organizations.

"The fully developed bureaucratic mechanism compares with other organizations exactly as does the machine with the non-mechanical modes of production.

Precision, speed, unambiguity, knowledge of the files, continuity, discretion, unity, strict subordination, reduction of friction, and of material and personal costs - these are raised to the optimum point in the strictly bureaucratic administration, and especially in its monocratic form."⁷

Weber believed that nature could be tamed, workers made docile, books balanced and complexity contained, all by the application of procedures, and rules and regulations based on machine rationality. Central to the notion of 'machine rationality' are the concepts of 'objectivity' and 'calculability of rules'. Weber defined 'objectivity' as the discharge of business according to 'calculable rules' and 'without discharge for persons'. By 'without discharge for persons' he implies dehumanization⁸. To achieve dehumanization of an organization, calculability of rules and results is a necessity. This implies the development of a written set of rules and regulations within which every possible contingency is provided for. This is also the fundamental problem with Weber's concept of bureaucracy. The problem is connected to the two assumptions that form the basis of the concept of bureaucracy:

- One, it is possible to discover and locate all variables in a system, as well as the relationship between them.

⁵Weber (1967, pp.213).

⁶Discussed in Chapter Four, pp.82-83.

⁷Weber (1967, pp.214).

⁸According to Weber (1967, pp.216), "the more the bureaucracy is 'dehumanized', the more completely it succeeds in eliminating from official business love, hatred, and all purely personal, irrational, and emotional elements which escapes calculation."

- The second assumption is the existence of a highly stable system which works like a machine.

Both these assumptions are flawed. The reason being, that the concept of machine rationality cannot be applied in social sciences. Firstly, not only is it difficult to catalogue all the variables in a system, but to identify the relationships between them is almost impossible. Secondly, the concept of stable system implies, either the existence of static ontological conditions, or if dynamic, than the change is assumed to be linear, so as to allow the estimation of the future through the extrapolation of the historic data. It is this assumption of stable system, that allows one to rationalize the development of a universal framework that may be assumed to be applicable across time and space. History, however, provides us with adequate evidence regarding the flawed nature of such an assumption⁹.

The influence of Weber and his machine rationality is quite apparent in the control engineering framework of regulations in the financial services industry. Regulatory agencies conceptualize themselves as machines for controlling the operations of the industry. This explains the mechanical logic and the fixed quantitative standards of the regulatory framework (setting of minimum standards aimed at the performance control of the industry). Such an assumption can only be rationalized if the operating environment of the industry is also visualized as being operational within a mechanical framework analogous to the Newtonian concept of clockwork universe. From the design of the regulatory framework in the financial services industry, it appears that the regulators also conceptualize the market players in the industry as a machines for collecting and distributing money and money related financial instruments. In line with these presumptions, the rules and regulations of the regulatory agencies lay down the operational framework for:

- One, the mechanism for the operations of the regulatory machine.
- Two, the mechanism for the ordering and control of the market machine (the industry).

The fundamental problem here is the assumption, and hence the conceptualization of the markets (this includes the market players: the financial institutions) as machines. It is this presumption that rationalizes the development and implementation of a regulatory framework based on mechanical logic. The problem with such a governance framework based on machine rationality or mechanical logic is that, it neglects the fact that financial institution are: one, run by human beings who are creative thinkers and not machines. They are managed by professional entrepreneurs¹⁰ who are constantly involved in innovating, revising, and recreating their institutions, and as a consequence affecting the market dynamics, thereby contributing towards the transformation of the whole industry.

⁹This facet was covered quite comprehensively in the Chapter Four which involved a historical analysis of the emergence and the development of the modernist philosophical thought.

¹⁰This facet is the focus on analysis in sections four and five of this chapter.

Two, these financial institutions are not operating in parallel but are engaged in global competition with each other. The dynamics of the market mechanism which will be discussed at a later stage in the chapter in the context of Schumpeter's 'Theory of economic development' insures against the possibility of the perseverance of a mechanical environment. The implication being, that the regulators are faced with organizations that are an extension of the human brain rather than a mechanical device of the 19th century. The entrepreneurial forces are constantly involved in creative destruction and destructive creation of the system through the power of innovation and change, thereby directly influencing a change in the ontological conditions prevailing at a point of time and space. The rational thought (based on the mechanical logic) of the regulatory framework, therefore, becomes irrational when the basic presuppositions that forms the basis of the framework change. The pace of innovation and entrepreneurialism has increased substantially with the inception of the deregulation process and the launch of the electronic revolution. This is the crux of the problem facing the regulators.

The existing regulatory framework in the financial services industry is a legacy of the period when the pace of innovation was slow and markets were segregated on the basis of the geographical frontiers defining the nation state. This allowed the national regulators the sovereign power to coerce, order and control the market's competitive environment and the entrepreneurial drive of the financial institutions. The industry was, therefore, to some extent controllable by means of the mechanical framework of the national regulators. Such a situation does not exist any more. Information technology and globalization have changed the environment in the industry. The development of information technology has stimulated the speed-up of the innovation and the entrepreneurial process. The process of globalization has complicated the task of the national regulators. The markets and the market participants are networked in a global embrace, and hence extend beyond the confines and control of the regulators of one particular nation-state. These developments have strained the controls built into the regulatory framework, thereby inducing multiple tensions between the regulators and the regulated¹¹. The existence and the endurance of the tensions despite the incremental changes in the regulatory framework brought about by the national regulators, as well as the global regulatory initiatives like global harmonization of capital adequacy standards, point to the key flaw in the regulatory philosophy: the problematic nature of a regulatory framework based on machine rationality for meeting the challenges of the dynamic global environment of the present era. Inability of the regulatory machine and its mechanical framework to order and control the operations of the financial institutions and the financial market, is the story behind the tensions in the financial services industry. This is also the basis of the predicament facing the contemporary regulatory philosophy.

¹¹These tensions have been discussed in detail in Chapter Three (McKenzie and Khalidi, 1996).

Interestingly enough, Weber himself acknowledged the problematic nature of the interface between the government bureaucracy and the entrepreneur led business firms. He rationalized it as a problem of information asymmetry, which is yet another facet of the problems inherent in the operational framework of the regulators. This is the subject of examination of the next section.

2.3. Manifestation of Information Asymmetry:

In the context of the financial services industry, there are two sides of the problem of information asymmetry. One relates to the interface between the regulators and the regulated. The other side of the problem relates to the interface between the regulators and the party (the general public and the other market participants) whose welfare and protection is the *raison d'être* for the existence of the regulators. Weber discussed both sides of the information asymmetry problem. The first aspect, i.e. the problematic nature of the information interface between the government bureaucracy and the market enterprise, is echoed in the followings quote from his essay on bureaucracy:

"Only the expert knowledge of the private economic interest groups in the field of 'business' is superior to the expert knowledge of the bureaucracy. This is because the exact knowledge of facts in their field is vital to the economic existence of the businessman. Errors in official statistics do not have direct consequences for the guilty official, but errors in calculation of a capitalist enterprise are paid for by the losses, perhaps by its existence. The 'secret' as means of power, is, after all, more safely hidden in the books of an enterpriser than it is in the files of public authorities. For this reason alone authorities are held within narrow barriers when they seek to influence economic life in the capitalist epoch. Very frequently the measures of the state in the field of capitalism take unforeseen and unintended courses, or they are made illusory by the superior expert knowledge of interest groups."¹²

Weber's observation regarding the problematic nature of the interface between the government bureaucracy and the private enterprise is interesting. Although his explanation has some substance, it is at the same time, mainly an exercise towards the rationalization of the problematical nature of bureaucracy's machine rationality rather than an explanation of the actual problem. This becomes apparent when we examine Weber's observation in the context of the interface between the regulatory agencies and the regulated entities (financial institutions) in the financial services industry. In the financial services industry, the presence of information asymmetry between the regulators and the regulated, in itself, is an indicator of the existence of two concomitant problems for which the bureaucracy rather than the private enterprises, are responsible. One, the unsuitability of a framework

¹²Weber (1967, pp.235).



based on mechanical logic to meet the challenge of the rapidly changing ontological conditions. In an era in which the form and content of the information itself is changing, the fixed format regulatory reporting requirements based on mechanical logic do not make the operational performance and the operational soundness of the regulated institution completely transparent, and therefore become a problem in itself. In the case of the regulatory agencies in the banking sectors, bank examiners try to unravel the information asymmetry by complimenting their fixed format information forms with on-site bank examination which is a part of their supervisory remit. This is the second facet of the problem of information asymmetry between the bureaucracy and market participants, (i.e, between the regulators and the regulated). The key to the success of the regulatory agencies in achieving their objective of unravelling the information asymmetry and making the financial conditions, the operating performance, and the future prospects of the financial institution transparent, depends upon the efforts and the competence of the examining officers. Some of the problems that affect this facet of information asymmetry include: the disjunction between the quality of output and rewards/penalties¹³; the effect of bureaucratic rationality in dampening the creativity, imagination, and intuitive ability of the staff; the effect of the salary structure and the mechanical logic of the incentive structure on the quality and calibre of staff drawn into bureaucracy, etc.. These two problems connected to the problem of information asymmetry are important not only because they provide an explanatory logic for the presence of information asymmetry at the interface of the regulators and the regulated entities, but also because the existence of these two problems points to a third problem for which the bureaucracy is fully responsible and worthy of blame. The reference is to the information asymmetry between the bureaucracy and the public (whose interest forms the *raison d'etre* for the existence of the bureaucracy) - a problem that the bureaucracy hides behind the garb of 'official secrets'.

"Every bureaucracy seeks to increase the superiority of the professionally informed by keeping their knowledge and intentions secret. Bureaucratic administration always tends to be an administration of 'secret sessions': in so far as it can, it hides its knowledge and action from criticism. The tendency towards secrecy in certain administrative fields follows their material nature: everywhere that the power interests of the domination structure towards *the outside* are at stake, whether it is an economic competitor of a private enterprise, or a foreign, potentially hostile polity, we find secrecy.

¹³"Errors in official statistics do not have direct consequences for the guilty official, but errors in calculation of a capitalist enterprise are paid for by the losses, perhaps by its existence" Weber (1967, pp.235). The implication being, that it is the public rather than the public servant, who have to suffer and endure the effects of unsound government policies based on erroneous official statistics prepared by the public servants.

The pure interest of the bureaucracy in power, however, is efficacious far beyond those areas where purely functional interests make for secrecy. The concept of 'official secret' is the specific invention of bureaucracy, and nothing is so fanatically defended by the bureaucracy as this attitude, which cannot be substantially justified beyond these specifically qualified areas. Bureaucracy naturally welcomes a poorly informed and hence a powerless parliament - at least in so far as ignorance somehow agrees with the bureaucracy's interests."¹⁴

This critique of Weber is true even today, and is very conspicuous in the operational framework of the regulatory agencies. Neither are the fixed format periodic reports of the financial institutions revealed to the markets, nor are the results of the bank examination disclosed. The overtone being, that the regulators themselves are directly responsible for maintaining the information asymmetry in the markets, thus impeding the market mechanism from working efficiently. This is a clear case of anomaly in the regulatory framework: the existence of a disjunction between the objectives and the actions of the regulators.

In this respect, the case of the regulatory initiatives of the Reserve Bank of New Zealand provides an interesting exception. It is a case of regulators taking cognizance of this anomaly. It is a case of regulators initiating a change in their regulatory framework with the aim of aiding the market's self disciplinary mechanism by removing the information asymmetry between itself and the markets. The Reserve Bank of New Zealand took the unprecedented step of public disclosure of the fixed format periodic information provided by the financial institutions to the regulators. Interestingly enough, none of the others regulators seem to have followed suit. Perhaps the reason could be, that in the case of New Zealand, unlike the other central banks, the central bank of New Zealand does not undertake on-site examination to overcome the problem of information asymmetry of the first type (the onus of prudential control is on the bank directors). The implication being, that if the other central banks followed suit and revealed the official secrets vis.a.vis the fixed format periodic information provided by the financial institutions, there could be a possibility of the regulators coming under pressure to reveal the information related to the on-site bank examination. This may be a problematical proposition for the regulators, because unlike the fixed format information, which is purely quantitative, and where the onus is on the integrity of the provider of the financial information, the information extracted during the bank examination is dependent upon, and indicative of the competence of the examining officers. The reference is to the ability of the bank inspectors, not only to unravel the actual financial position and operating performance of the financial institution, but also to evaluate the future viability of the institution in terms of the internal control

¹⁴Weber (1967, pp.233-34).

systems in place to control the risk, and the competence of the management to keep pace with the changing market environment. This explains the logic for the secrecy of US Federal Reserve Board's CAMEL rating despite the case in favour of the public disclosure of CAMEL rating¹⁵.

In the context of the hypothesis¹⁶ under examination Weber's theory of bureaucratic rationality provided us with an insight not only into the logic for the tensions/crisis facing the modernist philosophical thought, but also for the tensions connected to the regulatory crisis in the financial services industry. The next section takes the investigation into the same hypothesis a step further - it involves a deconstructive analysis of Marx and Engels' 'Manifesto of the Communist Party', in an effort to explain the crisis of confidence facing the modernist philosophical thought, a crisis that is also apparent in the financial services industry.

3. Problematical Nature of the Marxist Philosophy: A Deconstructive Analysis of Marx and Engels' 'Manifesto of the Communist Party'¹⁷:

3.1. Introduction:

Marxist philosophical discourse provides an excellent illustration of the problematical nature of a meta-framework based on deductive reasoning that effectively eliminates the role of the entrepreneur from the economic system. In the socialist economies, the politicians and the philosophers combined to implement a meta-framework (Marxism) that effectively removed the Schumpeterian entrepreneur from the economic system and replaced him/her with the Weberian bureaucrat, thereby terminally affecting their process of economic development. The difference between the state of economic development of the socialist economies and the entrepreneur driven capitalist economies became more and more conspicuous with time. On one side, there was an economy controlled by a static meta-framework based on machine rationality, on the other side was a dynamic economy driven by the enterprise of the entrepreneurs towards a process of innovation and change. In a global economic system, it is quite obvious why the static meta-framework controlling the socialist block could not

¹⁵Shadow Financial Regulatory Committee, (1996), "Disclosure of Examination Reports and Ratings", Statement No.132, May 6, 1996, Journal of Financial Services Research, Vol.10, No.4, December 1996.

¹⁶The tensions reflecting the regulatory crisis in the financial services industry may be a subset of, or a part of a much wider area of tensions/crises facing the conceptual foundations of the regulatory philosophy: the modernist philosophical thought.

¹⁷Marx, Karl, and Friedrich Engels (1978), "Manifesto of the Communist Party", in Robert Tucker (ed.), 'The Marx - Engels Reader', Norten, New York, pp.469-500.

sustain the competition from the entrepreneur driven capitalist block. The difference between the two systems implied that the disparity between the two blocks would keep on widening with time. The only force sustaining the meta-framework of the socialist block was the coercive force of the sovereign power of the government. As soon as this force weakened, the whole edifice of the Marxist meta-framework collapsed. Interestingly enough, Marx and Engels themselves point to the logic for the collapse of their meta-framework: 'Reactionarism'.

"although the originators of these systems were, in many respects, revolutionary, their disciples have, in every case, formed mere reactionary sects. They hold fast by the original views of their masters, in opposition to the progressive historical development of the proletariat."

Marx and Engels (1978, pp. 498-99)

The collapse of the Marxist framework provides an analogy for understanding the tensions in the financial services industry. Globalization of financial institutions and financial markets has not only increased the possibility of financial institutions indulging in regulatory arbitrage in an effort towards enhancing their profitability, but has also reduced the potency of the coercive force sustaining the sovereign power of the national regulators. The response of the national regulators to this two fold problem has been the incremental upgrading and the global harmonization of parts of the regulatory framework (for example capital adequacy regulations). This strategy, however, is problematical. It suffers from the same problem as that which plagued Marxism: 'reactionarism'. It is reactionary, in the sense that it aims to hold on to the existing regulatory tools and regulatory framework instead of reappraising the whole framework anew in light of their regulatory objectives. Like the Marxist framework, the regulatory framework is also very narrowly defined and ignores a number of interacting factors. For example quantitative regulations like capital requirements do not take into consideration the quality of management, the liquidity of assets, the sophistication of internal risk management methods, etc.. Furthermore the valuation of capital is dependent upon the valuation of assets and liabilities, and hence is susceptible to window dressing. The most important problem with the present regulatory framework and/or any other framework based on the modernist philosophical thought which the deconstructive analysis of Marx and Engels' 'Manifesto of the Communist Party', brings to the fore is that, like the Marxist philosophy, the regulatory philosophy also rationalizes the application of an all encompassing meta-framework that is frozen in time. The problem, is that such a framework is static in the sense that it incorporates knowledge developed up to a point of time, and assumes the ontological conditions also to remain frozen in time. This is the reason that such a framework becomes problematical in the long run. It becomes obsolete in the due course, thereby requiring incremental revision or replacement by a new one. The increased pace of innovation and

entrepreneurialism has created a crisis for the regulators. The crisis is on account of the increase in pace of obsolescence of regulations and the decrease in the coercive power of the regulators. The problem is embedded in the regulatory philosophy of control of market forces via a meta-framework. The problem lies in the adoption of a paternalistic attitude towards the market participants: 'the regulators know what is best for the markets, and therefore have the right to order and control the market participants and the market place'. The basis of this logic has been derived from the deconstructive analysis of Marx and Engels' 'Manifesto of the Communist Party', which is the theme of investigation of the next section.

3.2. Deconstructive Analysis of Marx and Engels' "Manifesto of the Communist Party" (1848)

Deconstructive analysis of Marx and Engels' "Manifesto of the Communist Party" (1848) provides a fascinating insight into the problematic nature of their discourse of 'scientific socialism'. It draws attention to the pitfalls of deductive logic and paternalistic thinking. It also draws attention to the irrationality of the logic of imposing a meta-framework across time and space - a problem that has become synonymous with the modernist philosophical discourse and its logic for ordering and control of the ontological conditions as per a rationally and scientifically conceived meta-framework. The basis of this conclusion lies in the following two problematical features discernable in Marx and Engels' 'Manifesto of the Communist Party' - features that are also concomitant of discourses/frameworks inspired by the modernist philosophical thought.

One, the influence of the present ontological conditions in the development of the discourse/framework that is imposed across time and space. Marx and Engels' philosophical discourse can be associated with a particular epoch: the crisis of 1847-8 and the depression that followed. The ontological conditions prevailing during that period created a deep impression on the two philosophers. It induced a sense of intense scepticism against the bourgeois class. Thus, despite acknowledging the contributions of the bourgeois class in breaking the stranglehold of the feudal class and the absolute monarchies, they rationalize the need for the destruction of the bourgeois class as the only possible approach for improving the living conditions of the proletariat. They consider capitalism as a necessary but a temporary stage whose industrial development would prepare the way for the eventual communist abolition of private property. Their use of history as the basis of their conclusion is problematical on two counts: firstly, the discourse and the meta-framework proposed by them is based on the historical analysis of the changing ontological conditions up to a point of time. The overtone being that it incorporates knowledge evolved up to a point of time. Such a discourse may suffice for the present problems, but to impose it as a rigid meta-framework to cater

for the future too, increases rather than decreases the problems in the long run. Secondly, although their discourse is supposed to be based on historical analysis, the influence of the present (the depression of 1847-48) is compelling. At the time of development of the discourse, bourgeois class was considered as the foe for the proletariat, history was used as a strategic tool of deductive argumentation to rationalize the destruction of the bourgeois class. The overtone being, that it is the present ontological conditions that play an overwhelming part not only in the expectation of the future, but also forms the basis for the manipulation of the past (history) to rationalize the present thinking. Developing a framework based on the present but imposing it as a meta-framework across time and space for the ordering and control of the ontological conditions, increases rather than reduces problems in the long run. This is true of all meta-frameworks/discourses developed at a point of time but imposed over a period of time.

The second problematical feature that is very conspicuous in Marx and Engels' discourse relates to the existence of binary thinking and deductive argumentation as the basis for the rationalization of their conclusions. This is echoed in the following excerpts from Marx and Engels' 'Manifesto of the Communist Party':

"The history of all hitherto existing society is the history of class struggles.

Freeman and slave, patrician and plebeian, lord and serf, guild-master and journeyman, in a word, oppressor and oppressed, stood in constant opposition to one another, carried on an uninterrupted, now hidden, now open fight, a fight that each time ended, either in a revolutionary re-constitution of society at large, or in the common ruin of the contending classes.

.... Society as a whole is more and more splitting up into two great hostile camps, into two great classes directly facing each other: Bourgeois and the Proletariat"¹⁸

"Hitherto, every form of society has been based, as we have already seen, on the antagonism of the oppressing and the oppressed classes. The modern labourer, instead of rising with the progress of the industry, sinks deeper and deeper below the conditions of existence of its own class. He becomes a pauper, and pauperism develops more rapidly than population and wealth. Society can no longer live under this bourgeoisie, in other words, its existence is no longer compatible with society."¹⁹

¹⁸Marx and Engels (1978, pp.473-74).

¹⁹Marx and Engels (1978, pp.483).

"The lower strata of the middle class - the small tradespeople, shopkeepers, and retired tradesmen generally, the handicraftsmen and peasants - all these sink gradually into the proletariat."²⁰

In such framework of binary dichotomy, now the bourgeois was the oppressor and the proletariat the oppressed. Historical analysis suggested that those who acquired power sought to fortify their status. The logic associated with the linearity of time implied that the situation would not change. The bourgeois would become richer and richer and the proletariat would become poorer and poorer. The natural solution or the only way out of this quagmire, for the proletariat (according to this logic) was to overturn the hierarchy. The aim of Marx and Engels' philosophy as outlined in the 'Manifesto of the Communist Party', was to rationalize the creative destruction of the bourgeois class which at that time was considered as the binary opposite of the proletariat class - a simple case of deductive logic.

"All preceding classes that got upper hand, sought to fortify their already acquired status by subjecting society at large to their conditions of appropriation. The proletarians cannot become masters of the productive forces of society, except by abolishing their own previous mode of appropriation, and thereby also every other previous mode of appropriation. They have nothing of their own to secure and to fortify; their mission is to destroy all previous securities for, and insurances of, individual property."²¹

The strategy proposed for achieving the objectives consisted of two steps: **one**, "to raise the proletariat to the position of ruling class, to win the battle of democracy"²², and **two**, "the proletariat will use its political supremacy to wrest, by degrees, all capital from the bourgeois, to centralize all instruments of production in the hands of the state, i.e., of the proletariat organized as the ruling class."²³

The naivety of the logic of the two philosophers is quite apparent. The logic behind the proposal is based on a combination of binary thinking and deductive logic. When the feudal and the monarchs reigned supreme, they maintained their power by subjugating their binary opposites: the share-croppers, and the subjects, now that the bourgeoisie were the power brokers, deductive logic implied that their power was also associated with the subjugation of their binary opposite: the

²⁰Marx and Engels (1978, pp.479-80).

²¹Marx and Engels (1978, pp.482).

²²Marx and Engels (1978, pp.490).

²³Marx and Engels (1978, pp.490).

proletariat. For the proletarians, this implied that only way of breaking out of their shackles was to destroy the power of the bourgeois class.

Marx and Engels' argumentation suffers from a number of flaws, they visualize the bourgeois as a part of a social class rather than an economic agent. They ignore the difference in the power relationship of the bourgeois and the proletariat, from that of the feudal and the serf. While the feudal and the monarchs achieved and maintained power through the use of coercive force and sovereign power, the basis of power of the bourgeoisie was disciplinary power²⁴ (which is connected to knowledge and enterprise) which is an acquired and not an inherited power. Among the bourgeois community, those who inherit the property without the entrepreneurial ability of the original bourgeois face the threat of loosing out to market competition, and as a consequence loosing not only their property but also their social status. Hence the old adage: "three generations from overall to overall". The implication being, that it is not through subjugation, but rather through knowledge and the entrepreneurial drive that the bourgeois acquires and maintains power. It is a form of power which the members of the proletariat class can also acquire by educating themselves and by applying their enterprise in the business sector. The key flaw with Marx and Engels' argumentation relates to the conceptualization of the bourgeois as a 'capitalist'. They ignore the entrepreneurial trait of the bourgeoisie. The bourgeoisie were not simply capitalists but also entrepreneurs. In fact, it was their entrepreneurial ability that made them capitalist and gave them the capacity to challenge the power of the feudal and the monarchs. Although Marx and Engels acknowledge the creativity of the bourgeois in quantifying the performance of labour, and their contribution in changing the global ontological conditions, they fail to identify and understand the concept of entrepreneurialism and/or uncouple it from the capitalist function. By proposing the destruction of the bourgeois class they also proposed the destruction of the entrepreneur (the most dynamic element of change in our ontological conditions), and as a consequence, the market mechanism itself.

Marx and Engels' "Manifesto of the Communist Party" is important not only because it provides an illustration of the pitfalls of paternalistic thinking, deductive logic, and the ramifications of imposing a meta-framework as an answer to the problems of the present as well as the future, but also for providing a spring board for examining Joseph Schumpeter's 'Theory of Economic Development' which outlines the contribution of the entrepreneur in bringing about a dynamic change in the ontological conditions.

²⁴The concept of disciplinary power, and the difference between disciplinary and sovereign power will be discussed in Chapter Seven in the context of Michel Foucault's philosophy of power.

4. Schumpeter's Theory of Economic Development: Contribution of the Entrepreneur:

The key element introducing and instituting a change in our ontological condition is the 'entrepreneur'. This is the theme of Joseph Schumpeter's (1959) 'Theory of Economic Development'. This section involves an examination of Joseph Schumpeter's 'Theory of Economic Development' with the aim of understanding the concept of entrepreneur and his²⁵ contribution to the process of economic development and the success of the market mechanism. The aim of this section is to provide the springboard for the next section (section five) which involves the extension, or the further development of Schumpeter's 'Theory of Economic Development' to understand the present crisis facing the modernist philosophical thought - a crisis that is connected to the tensions in the financial services industry.

Schumpeter describes the entrepreneur as a heroic figure, a creative destroyer and destructive creator par excellence. His characteristic task, theoretically as well as historically, is the breaking up, and the creation of new traditions. Although the role of the entrepreneur applies primarily to his economic action, the implications of his actions extends to the moral, cultural, and social sectors too. The regulators, the politicians, the academics, and the philosophers, are all affected by the actions of the entrepreneur, because he breaks the mould of the circular flow. He initiates the process of development which leads to a significant change in our ontological conditions. The entrepreneur may therefore be conceptualized as the force that breaks the mould of the circular flow and initiates the process of development. To understand the concept of entrepreneur and the contribution of the entrepreneur to the process of economic development, it is necessary to understand two related concepts - the concept of 'circular flow' and the concept of 'development'. The discussion to follow has therefore been divided into four subsections:

- 4.1. The Concept of Circular Flow
- 4.2. The Concept of Development
- 4.3. The Concept of Entrepreneur
- 4.4. The Contribution of the Entrepreneur.

4.1. The Concept of 'Circular Flow':

Everyone clings as tightly as possible to their habitual economic methods, and only submit to the pressure of circumstances when it becomes necessary. Thus, under ordinary circumstances, a state of circular flow prevails in respect of the pattern of production and consumption. This is the basis of Schumpeter's argument that the economic system will not change capriciously on its own initiative but will at all times be connected with the preceding state of affairs. It may be noted that the concept

²⁵Schumpeter does not use gender neutral language in his essay.

of circular flow takes into consideration the slow and continuous changes in equilibrium or incremental changes in standards or the changes in the pattern of consumption and production that may grow out of the old one by continuous adjustments in small steps, it however, excludes discontinuous changes.

The human affinity towards standardization can also be explained in the context of the concept of circular flow. Generally the most efficient method/system developed over a period of time crystallizes into standards. Standards once developed are generally followed without making an effort towards analyzing and developing the best combination anew every time. Thus, a state of circular flow prevails. Slight revisions are generally made to adapt the methods according to the changing circumstances, as when the need arises. Economic theories assume the perseverance of circular flow, and are therefore aimed at modelling it as a standard that can be then applied for policy making. The problem with economic theories is that they ignore the contribution of the entrepreneurs. They only take into consideration the slow continual changes²⁶, and as a consequence fail when discontinuous changes in the channels of the circular flow takes place that cause a shift in the state of equilibrium. The concept of circular flow therefore provides an insight into the risks of policy making grounded on economic theories.

The concept of circular flow also provides an insight into the tensions in the financial services industry. The regulatory framework incorporating fixed quantitative standards enforced by national regulators also assumes the perseverance of circular flow. The tensions in the financial services industry are an indicator of discontinuous changes in the structure of the industry and the structure of the risks facing the market participants brought about by the actions of the entrepreneurs. Hence the need for a reevaluation and reformulation of the regulatory framework.

The concept of circular flow also explains the dilemma with the modernist philosophical discourse. The modernist philosophical thought assumes not only the perseverance of circular flow, but also aims to provide a discourse for establishing a framework for the ordering and control, and hence the sustenance of the circular flow. It neglects the possibility of the development process initiated by the entrepreneurial forces that leads to the creation of a disequilibrium in the circular flow. Hence the rationale for the crisis of confidence facing the modernist philosophical thought.

²⁶It generally explains the slow and continuous increase in terms of the national supply of the productive means and savings which are generally accounted by continual adaptation through innumerable small steps.

4.2. The Concept of Development:

Schumpeter (1959, pp.64) defines the concept of 'development' as a "spontaneous and discontinuous change in the channels of the circular flow, disturbance of equilibrium, which forever alters and displaces the equilibrium state previously existing". He (Schumpeter, 1959, pp.66) gives the following examples as illustrations of the concept of development:

- i. Introduction of a new good/product or a new quality of good/product.
- ii. Introduction of a new method of production.
- iii. Opening of a new market.
- iv. The conquest of a new source of supply of raw materials or semi manufactured goods.
- v. Changing the organizational structure of the industry, for example creation of a monopoly position through merger, or breaking up of a monopoly position.

The key to the concept of 'development' is the introduction of 'discontinuity' in the channels of circular flow²⁷. This is the reason why economic theories which are generally based on static analysis and assumption of the continuity of the circular flow, fail to model, predict, and hence control the process of development, and as a consequence, becomes a problematical proposition whenever a discontinuity in the circular flow is introduced.

4.3. The Concept of Entrepreneur:

The individuals who introduce discontinuity in the channels of circular flow, and hence engender the process of development, are characterized as 'entrepreneurs'. The concept of 'entrepreneur' includes not only independent businessmen, but also the dependent employees of a company like professional managers, executive members of Board of Directors, etc., who have the characteristics²⁸ of an entrepreneur and also have the power and the capacity to perform the entrepreneurial function. Schumpeter (1959, pp.14) explains 'entrepreneurialism' as the process of initiating the development process. Entrepreneurialism involves the achievement of commercial advantage through improvements²⁹ possible within the present state of knowledge.

²⁷New combinations that may in time grow out of the old by continuous adjustment in small steps are not included in Schumpeter's concept of development. The reason: incremental development is neither a new phenomenon nor a new development.

²⁸Characteristics of entrepreneur include initiative, authority, foresight, etc..

²⁹According to Schumpeter (1959, pp.133), introduction of new machinery is a special case of entrepreneurialism involving changes in the productive process in the widest sense, the aim of which is to produce a unit of product as a lower cost, thus creating a disparity between the existing price and the new costs. Entrepreneurialism also includes innovations in business organization as well as commercial combinations, for example, better use of the existing factors of production, a favourable choice of a location, etc.. Even when individuals do nothing but employ existing goods to a greater

4.4. The Contribution of the Entrepreneur:

Schumpeter explains the contribution of the entrepreneur in the context of three key aspects of the entrepreneurial function. **One**, entrepreneurialism relates to the **first time performance of the function**. Entrepreneur is a leader in the sense that he leads the means of production into new channels. Those who follow the leader are not entrepreneurs. **Two**, the function of a leader/entrepreneur involves "**doing the thing**", without which the possibilities are dead. Economic leadership and entrepreneurialism should therefore be distinguished from invention, because as long as inventions are not carried into practice (i.e. commercially exploited), they are economically irrelevant. It is not necessarily the function of the entrepreneur to find or create new possibilities. They are always present, abundantly accumulated by all sorts of people, often they are also generally known and are being discussed by scientific and literary writers. Entrepreneur is the individual who takes the risk of commercializing the innovation. **Thirdly**, and most importantly, it is not exactly the entrepreneur's initiative, but rather the **consequence of the entrepreneur's initiative** that effects a change in market equilibrium. Although entrepreneurs accumulate surplus profits, and are therefore abhorred by many people, they do perform a very important economic function. They are the agents of change who initiate the process of development. The success of the leader (the entrepreneur) and his surplus profit pulls the other competitors in the field to follow him. Profits slip from the entrepreneur's grasp as soon as the entrepreneurial function is performed. Schumpeter describes entrepreneurial profits as the 'child', as well as, the 'victim' of development. While entrepreneurial initiative leads to entrepreneurial profits, it also attracts other producers to follow him who gradually eat up his profits. In other words it is not the success of the leader, rather it is the consequence of

effect, they in actual fact, have carried out a new combination and are therefore entrepreneur - their gain is an entrepreneurial profit. They have triumphed over others, blazed a trial and created a model for the others to follow. In this respect Schumpeter gives a few examples that illustrate and explain the concept of entrepreneurialism.

- Establishing a business utilizing a cheaper source of supply. This may include raw materials, as well as labour (globalization therefore involves entrepreneurialism).
- Replacing of one production or consumption good with another but a cheaper one, for example, replacing wool with cotton.
- Creating a good which more adequately satisfies existing and previously satisfied needs.
- The search for a new market more inefficient than the existing one (this is another example of the thrust behind globalization).
- The case of production of a completely new good/product is a special case of entrepreneurialism. Gaining consumer acceptance for a new good/product is a very difficult proposition. It requires an input of extra resources for market development. A host of obstacles arise which may also require an input of extra resources. The implication being, that during the initial product launch and the market development stage, the entrepreneur may be required to incur costs that may be greater than the returns. However once a market has been created, the entrepreneur reaps a surplus until new competition streams in and eats up the entrepreneurial surplus.

the success of the leader which is the causal factor behind the change in market equilibrium. His success and his supernormal profits act as a magnet pulling the other competitors in the field to follow his lead. But this role (as market leader) of the entrepreneur, is against his will, because the competitors who follow him annihilate his profits gradually. This is the most significant aspect of the market mechanism (and perhaps the explanation for Adam Smith's invisible hand). The final result is a complete reorganization of the market with an outward shift in the production possibility frontier, and a new equilibrium position with a new industry cost and revenue function. This is Joseph Schumpeter's theory of economic development. The following excerpt from Schumpeter (1959, pp.131) summarizes the contribution of the entrepreneur:

"new businesses are continually arising under the impulse of alluring profit. A complete reorganization of the industry occurs, with its increases of profits, its competitive struggle, its suppression of obsolete businesses, and its possible dismissal of workers, and so forth. ... the final result must be a new equilibrium position, in which, with new data, the law of cost again rules, so that now the prices of the products are again equal to the wages and rents of the services of labour and land. ... the incentive to produce more and more products will not cease before this condition is arrived at, nor before the price falls as a result of the growing supply."

The concept of reverse engineering gives us an insight into the consequences of entrepreneur's initiative that result in introducing a disequilibrium in the circular flow. Reverse-Engineering is a process of: one, breaking the product into its basic component pieces; two, deciphering the basic linkage/processing between the component pieces within the context of the main product; three, reproducing the components parts; and finally, reassembling and interlinking them in the same way as the original to produce an imitation which has the same functional use as that of the original.

In the case of reverse engineering, the follower (or the imitator) not only saves on the preparatory cost of initial/original research and development, but also the cost of its testing and market development. In the case of financial services industry, the regulatory authorities compel the initiators of new financial products to reveal information on product design before a certificate of approval is given to launch the product. Rivals can thus free ride on innovator's investments in educating the regulators, issuers, and investors. As a result the cost of introduction for the imitation product is 50% to 75% less than that for the innovators³⁰. For the innovators, the careers of

³⁰In the case of financial services industry, Tufano (1989) estimates the cost of new product development as being from \$50,000 to \$5 million. This includes: one, payments for legal, accounting, regulatory, and tax advice; two, time spent educating issuers, investors, and traders; three, investments in computer systems for pricing and trading; four, capital and personnel commitments to support market making. In addition approximately \$1.000 million is paid to staff product development group

investment bankers and millions of dollars of the bank are put on stake even though they know that securities cannot be patented. The basic advantage that the innovating entrepreneurs get is, the head start, being the first in the field, they are able to move up the learning curve much earlier than their rivals. Their survival is therefore based on capturing a major part of the market share so as to be able to achieve economies of scale, and hence consolidate their position by becoming a cost leader in the field. In this respect, globalization has compensated for the reduction in head start available for the innovator. In other words, for the innovator, the negative implications of time-compression are countered by the positive implications of space-compression. Globalization fuels, as well as, has been fuelled by innovation.

Having examined Schumpeter's theory of economic development, we can now apply the basic concept of his theory to explain the present crisis in modernity - a crisis which is also apparent in the financial services industry.

5. Application of Schumpeter's Theory of Economic Development to Explain the Logic for the Present Crisis in Modernity:

Schumpeter's 'Theory of Economic Development' is important not only because it explains the process of development, but also because it provides an insight that can be applied to understand and explain the present crisis facing the modernist philosophical thought. This section involves the application of these insights to understand the present crisis in modernity - a crisis that appears to be different from the earlier ones in the sense that this time it is the legitimacy of the central idea of the modernist philosophical thought: the existence of, and hence the search for the truth - the meta-framework for the ordering and control of the ontological conditions, that is being challenged. The basis of this challenge lies in the speed-up of the development process fuelled by the entrepreneurs. The aim of this section, therefore, is to connect the crisis facing the modernist philosophical thought with the speed-up of the development process.

The problem with the discourses based on the modernist philosophical thought, is that they assume the perseverance of the circular flow, and hence rationalize (or rather encourage) the formulation of an all encompassing theory or framework grounded on the existing state of knowledge, and then applying it for the ordering and control of the ontological conditions across time and space. They neglect the contribution of the entrepreneur in initiating the process of

with 2 to 6 bankers. Finally the reputation of the innovator is also at stake on the success or failure of the product.

development which not only changes the status of our knowledge base but eventually leads to a paradigm shift in our ontological conditions, thereby creating a crisis of confidence in the contemporary meta-discourse. The end result of such a situation, according to Kuhn's hypothesis, is the need for a new discourse (or more appropriately, a new meta-discourse) that not only provide an explanatory logic for interpreting this altered state of the ontological conditions, but also forms the basis for the development of a meta-framework for the ordering and control of the ontological conditions.

The present crisis is special because it does not relate to the crisis of confidence in a particular meta-discourse, rather it relates to the legitimacy of the modernist philosophical thought itself, and its logic for imposing a meta-framework for organizing and controlling our ontological condition. The logic for the present crisis can be connected to the speed-up of the development process itself - a development which has significantly compressed the time frame for the survival of any meta-discourse and/or meta-framework. In other words, it is the increase in the speed of the development process which has created a crisis of confidence in the modernist philosophical thought and its rationale of imposing an all encompassing meta-framework for the organization and control of the ontological conditions. The aim of this section is to extend the insights gained from Schumpeter's 'Theory of Economic Development' to provide an explanatory logic for the speed-up of the development process which forms the basis of the present crisis facing the modernist philosophical thought.

Critical examination of Schumpeter's theory points to five variables that can be identified with the speed of the development process. These are:

- **One**, the number of entrepreneurs active in the market place. Greater the number of entrepreneurs active in the market place, greater will be the speed of the development process. In other words, there is a direct relationship between the number of entrepreneurs in the market place and the pace of the development process.
- **Two**, the magnitude of entrepreneurial risk. The level of entrepreneurial risk will have a negative impact on the development process. A higher amount of entrepreneurial risk implies a greater chance of failure. This implies an inverse relationship between entrepreneurial risk and the pace of the development process.
- **Three**, the pace of innovation. The greater the pace of innovation, greater the probability of commercialization of the innovation by the entrepreneurs for achieving a competitive advantage in the market place. This implies a direct relationship between the pace of innovation and the pace of the development process.

- **Four**, the ease, and hence the pace of implementation of the entrepreneurial initiative. There are two facets of this variable: one, the flexibility/adaptability of the organizational structure in terms of the ability of the entrepreneur to restructure the organizational structure of the corporation to fit the business strategy. The second facet relates to the flexibility/adaptability of the production process to meet the challenges of the market place and the speed of commercialization of innovation. It is after all, not the innovation, but the commercialization of innovation that leads to the development process. The increase in speed of this variable (decrease in the time for the implementation of the entrepreneurial initiative) implies an increase in the speed of the process of development.
- **Five**, the pace of change in market equilibrium³¹ following the entrepreneurial initiative. This is a very important facet of the development process. The speed of change in market equilibrium following the entrepreneurial initiative, implies that more entrepreneurial initiative is needed to hold a competitive advantage in the marketplace.

The combined effect of these variables can be presented as an equation:

$$D = f(n*i*I*E/r)$$

Where	D	is the development process.
	n	is the number of entrepreneurs active in the marketplace.
	r	is the entrepreneurial risk.
	i	is the pace of innovation.
	I	is the pace of implementation of entrepreneurial initiative.
	E	is the pace of change in market equilibrium following the entrepreneurial initiative.

The above equation provides us with a picture of the key variables that affect the development process. The above equation also allows us an understanding of the relationship between each of these variables and the development process. Employing the equation as a hypothesis, it is possible to provide a reasonable explanation for the speed-up of the momentum of the development process. Having already laid out the possibility of a connection between the crisis facing the modernist philosophical thought (a crisis reflected in the tensions in the financial services industry) and the speed-up of the momentum of the development process, we thus have a possible connection between the crisis facing the modernist philosophical thought, and the variables at the back of the crisis. Having laid out the hypothesis, we can now examine each of the five independent variables whose transformation accounts for the speed-up of the momentum of the development process, and as a consequence, the speed-up of the pace of change in our ontological conditions. Hence the logic for

³¹The surplus profit of the entrepreneur in question and his immediate followers disappears not at once, but over a period of time with the progressive increase in efficiency of the other competitors who follow the lead of the entrepreneur.

the crisis facing the modernist philosophical thought - a crisis that is also apparent in the financial services industry.

5.1. The Aggregate Number of Entrepreneurs Active in the Market Place:

The increase in the number of entrepreneurs active in the market place is perhaps the most important reason for the speed-up of the momentum of the development process. Two causal factors can be identified with the (almost) exponential increase in the aggregate number of entrepreneurs active in the market place: one, the separation of the capitalist function from the entrepreneurial function, and two, the evolution of the breed of professional manager/entrepreneur.

Historically speaking, the prior to the development of the modern banking system, the entrepreneurial and the capitalist functions were performed by the same entity: the bourgeoisie³². Separation of the entrepreneurial and the capitalist function materialized in two stages. The first stage was the evolution of the modern banking system which led to the development of the banker as a capitalist par excellence, standing between those who wished to perform the entrepreneurial function and those who had the necessary capital. The availability of bank credit made the entrepreneur, to a certain extent, independent of the inherited position, thereby allowing entrepreneurialism to ride to success on debt (borrowed money). The second stage of the separation of the entrepreneurial from capitalist function can be tied to the evolution of the public limited companies, and the institutionalization of the stock exchanges. The consequence was the shift in the ownership of the business from the entrepreneur (or his family) to the public stockholders (as in the case with public limited corporations). Corporations became artificial entities/persons in their own right, with their ownership dispersed over a number of shareholders, and the control being delegated to the professional managers.

The business enterprises of the present era are therefore composed of the professional managers who perform the entrepreneurial function, and two strata of capitalists: the shareholders who provide the equity capital, and the bankers who provide the debt capital³³. The separation of ownership and control of the modern business enterprises implies that the entrepreneurial function

³²This explains Marx's antagonism for the bourgeoisie class who combined the functions of the capitalist as well as the entrepreneur. In the context of the present economic system, the term 'capitalism' is a misnomer, a more appropriate terminology would be 'entrepreneurialism'.

³³Both these strata of capitalist forces are themselves managed by professional entrepreneurs. The reference is to the emergence of the modern professionally managed banks which control the debt capital, and the modern professionally managed insurance companies and pension funds which control/manage bulk of the equity capital.

has become (almost) completely oblivious of the need for capital, hence the development of the cult of professional entrepreneur.

The question arises: what motivated the bourgeoisie to segregate the capitalist from the entrepreneurial function, and to delegate the entrepreneurial function to the professionals? Schumpeter provides three possible explanations: one, the realization of inability of the entrepreneurs with declining powers and/or the heirs of entrepreneurs to match the market competition; two, the realization of the difference between the directing and the directed labour, and more importantly the entrepreneurial potential of the former; and three, the realization of the potential of profit participation as an instrument for activating the entrepreneurial psyche of the directing labour. Each of these is discussed in more detail below:

5.1.1. Inability of the Entrepreneurs With Declining Powers and/or the Heirs of Entrepreneurs to Match the Market Competition.

According to Schumpeter (1959, pp.156) the competitive market mechanism tolerates no permanent surplus value. The stimulus of the 'striving for profit' which is the market mechanism's driving force, annihilates not only the surplus profits in the industry, but also those with no or relatively low entrepreneurial ability. Such a fate threatens the entrepreneurs whose powers are declining, and the heirs of those who have inherited the entrepreneur's wealth without his ability. Hence, the classic American adage: "Three generations from overalls to overalls³⁴". The strategy applied for circumventing the problem, was the separation of management and control³⁵. The heirs of the previous entrepreneurs therefore became capitalist (share holders) while the entrepreneurial function was passed on to the professional managers. This is perhaps the reason for the survival of some of the business empires of yesteryears which have not only endured the test of time, but still continue to thrive.

5.1.2. The Difference Between Directing and Directed Labour, and More Importantly the Entrepreneurial Potential of the Former.

Schumpeter broadly categorizes labour into two groups: directing labour and directed labour. The distinction between the two is two fold, firstly, the directing

³⁴The overtone of the adage is that, it is the entrepreneur who builds a huge business out of nothing, his heirs may inherit his business but not necessarily his entrepreneurial ability. If that is the case, then the competitive mechanism of the market will gradually annihilate the surplus profits of the business, leading to the dissolution of their business and the wealth of the entrepreneur's family over a period of couple of generations.

³⁵This strategy in itself, is an evidence of entrepreneurial initiative, the success of which inspired and stimulated the others in the industry to follow suit, leading to a complete reorganization of the industry.

labour stands at a higher level of hierarchy than the directed labour, and is therefore involved in directing and supervising the ‘directed’ or the ‘executing’ labour³⁶. Secondly, and more importantly the directing labour has something creative in the sense that it sets itself its own ends. It is the realization of the creative potential combined with the managerial ability of the directing labour that is the key to the evolution of the directing labour into the cult of the professional entrepreneur.

5.1.3. The Potential of Profit Participation as an Instrument For Activating the Entrepreneurial

Psyche of the Directing Labour. The evolution of the professional manager into an entrepreneur may be linked to the realization of the difference between the motivating effect of wages and profits participation on the overall performance of the business. The difference between wages and profit participation is two fold: One, unlike wages, which are the expression of the contribution of the labourer towards production, profits are the expression of the value of the contribution of the entrepreneur towards production. Two, unlike wages, which are an element of cost and therefore have a braking effect on production, profits on the other hand have a reciprocal relationship with cost and therefore have an accelerating effect on production. Linking the remuneration of professional managers or directing labours to profits stimulates their creativity and motivation, and transforms them into professional entrepreneurs.

It was the combined effect of all the three factors discussed above, that stimulated the separation of the entrepreneurial function from the capitalist function and the development of the cult of the professional entrepreneur. Another factor, not discussed by Schumpeter, perhaps because it was a much later development, relates to the introduction of business education as a separate discipline, and more importantly, the change in the structure of business education from a ‘formal training’ based approach to a more ‘analytical’ approach, and the shift in the control of the higher reaches of corporate echelons from engineers to business professionals, reflecting a change in the corporate concern from production orientation to orientation towards sales, finance, marketing, and other managerial aspects related to the internal and external environment of the business. This shift has been discussed by Nelson (1995). Prior to the mid 1950s, business education followed an apprentice-journeyman model. This changed in the mid 1950s. The crucial force behind the change were two reports, one by Ford foundation, and the other by Carnegie Foundation. Both these reports called for a radical reorientation of the management education with emphasis on improving the

³⁶This lifts the directing labour out of the class of ‘labour’ into a new category and makes it a separate factor of production. While the directed or the executing labour is simply at par with the uses of land, and from the economic standpoint performs the same function as land, it is the directing labour which is in a governing position and its function is clearly in contrast with that of both executing labour and the uses of land.

analytical and problem solving skills of the business students. Another facet of the reorientation of business education, and the development of the entrepreneurial manager is the idea that managerial strategies are discernable empirically. This conviction is at the root of the rise in business related research, and in the mushrooming of management programs. The consequence³⁷ has been the emergence of the entrepreneurial manager, and the materialization of a new era in capitalism: the era of post-industrial capitalism. Nelson (1995, pp.2) explains this development:

"in recent years corporations have acquired new resources, qualitatively different from those available in the past. These resources are organizational and knowledge-based and are tantamount to a revolution in the inventory of tactics and strategies available to corporations".

The separation of the entrepreneurial function from the capitalist function, and the increase in the quality and quantity of business education (for developing the entrepreneurial manager) provides an explanation for the increase in the aggregate number of entrepreneurs active in the market place and the intensification of the development process.

5.2. The Magnitude of the Entrepreneurial Risks

The magnitude of risks involved in the performance of the entrepreneurial function is another variable affecting the development process. The relationship, however, is inverse, i.e the increase in the pace of development may be linked to the decrease in the entrepreneurial risks. Two factors that may be identified with the reduction in entrepreneurial risks are: One, the separation of ownership and control, and two, the improvements in information systems.

The effect of the separation of ownership and control, is the uncoupling of the economic risk from the entrepreneurial function. With the economic risks being absorbed by the two categories of capitalist³⁸, the only risk that the professional entrepreneur has to bear is his reputation, and the

³⁷The reference is to the availability of a wider base of business knowledge and the emphasis on the development of analytical and problem solving intellect in business education.

³⁸According to Schumpeter (1959, pp.137) the entrepreneur is never the risk bearer, rather it is the one who gives credit who suffers the major loss if the undertaking fails. Although any property possessed by the entrepreneur may be liable, but the actual risk falls on the capitalist because he becomes the possessor of goods from a failed venture. The possibility of being able to reap the required returns either by selling off the machinery/assets or by utilizing them in the production process are rather slim. The same goes for the share holders who suffer an even greater risk than the creditors.

opportunity cost of his share in the firm's profits³⁹, hence the logic for the intensification of the spirit of entrepreneurialism, and the increased momentum of the development process.

The second factor relates to the improvements in information systems which has reduced the complexity of the entrepreneurial function, and altered the significance of the three qualities that Schumpeter (1959, pp.84-86) regards as the sine qua non for entrepreneurs: one, his intuition; two, his psyche; and three, his perseverance. Although the significance of entrepreneur's intuition cannot be questioned, the entrepreneurial risk has decreased because of the improvements in information systems. This includes improvements in the quality and the quantity of the market research, risk hedging techniques, and most importantly, the improvements in our computational ability in terms of the ability of the entrepreneur to generate and evaluate diverse risk and return scenarios related to a new venture. The second feature, the significance of the entrepreneur's psyche to assume the risk of doing something new than what is familiar and tested by experience can be connected to the magnitude of risks being assumed by the entrepreneur. With most of the down-side risks being absorbed by the capitalists (the separation of ownership and control), the entrepreneurial psyche for assuming the risk of doing something new is stimulated. The emergence of the producer services or consulting firms⁴⁰ as the suppliers of expertise beyond that which is generally available in any single business, is another factor that has reduced the entrepreneurial risk and speeded up the development process. An excellent example is the mega mergers in the financial services industry. The producer services (consulting firms) are involved not only in consummating the merger deals, but also in implementing the restructuring and reorganization of the new (merged) firm. By providing such services, these producer services/consulting firms not only develop expertise in managing mergers but also become the driving force behind further mergers and consolidation of the industry that happen as a consequence of the entrepreneurial initiative of the market leader. As regards the significance of the third feature: perseverance (i.e. the ability of the entrepreneurs to face up and conquer the reaction of the social environment against one who wishes to do something new), not

³⁹If the entrepreneur owns shares, then the loss he sustains on the shares relates to his capitalist function.

⁴⁰The importance of producer services/consulting firms is on account of the fact that they supply skills, expertise and experience in areas which are not generally available with the corporation's internal staff. They reap the advantages of specialization and scale economics. These services, by virtue of their contact with diverse clientele achieve a unique experience. Also, by virtue of contact with diverse clientele, they survey the competition, monitor markets, and scrutinize economic environment. These producer services (lawyers, bankers, accountants, etc..) are therefore able to link customers to communities of businesses with common problems. They inform clients of the market situation of competitors and counsel them with the options for handling specific problems. They provide technical advice as well as social advice. Producer services by enlarging the scale and the scope of strategic alternatives help in the intensification of competition (Nelson, 1995, pp.47).

only have the societal attitudes become more tolerant to changes, the economic power of the corporate has also increased substantially. Globalization has allowed them channels for bypassing the legal or political impediments of nation-states, and the power of the advertising media has provided them with a powerful weapon for conquering consumer resistance. These are some aspects related to the reduction in entrepreneurial risks, which can be connected to the speed-up of the development process.

5.3. The Pace of Innovation:

Although the concept of an inventor is different from that of an entrepreneur, there is a connection between the two. Inventor creates new products, while the entrepreneur commercializes them⁴¹, thus ‘innovation fuels entrepreneurialism’. The increase in the pace of innovation experienced in recent years can be explained in the context of applicability of the reciprocal of this statement too: ‘entrepreneurialism fuels innovation’. Lyotard (1984, pp.44) explains the circumstances leading to the entry of entrepreneurial forces into the arena of research. Traditional knowledge was based on revelation, scientific knowledge which replaced traditional knowledge was based on the presentation of truth, but finding or developing the truth requires laboratory and other equipment which also requires monetary input. Thus an equation between wealth, efficiency and truth was established. At the end of the eighteenth century, with the first industrial revolution, the reciprocal of this equation was also discovered: **no technology without wealth, but no wealth without technology**. Hence the rationale for the entry of the entrepreneurial forces into the arena of research. They directly funded their own private research departments for developing new innovations and improving their performativity. At the same time they also funded university departments and independent research groups on the theory that research must be financed at loss for a certain length of time in order to increase the probability of it yielding a decisive, and therefore a highly profitable innovation. The intensification in global competition has made innovation not simply a market entry strategy, but a market survival strategy. Hence the incentive for increasing the allocation of funds towards research and innovation for stimulating the process of development.

5.4 The Pace of Implementation of the Entrepreneurial Initiative:

There are two facets of this variable: one, relates to the flexibility of the organizational form, i.e., ease of restructuring the organizational form/structure for implementing the entrepreneurial strategy.

⁴¹As long as inventions are not commercialized, they are economically irrelevant. Herein lies the importance of the entrepreneur.

Two, the flexibility of the production system to adapt to the need for implementing and commercializing new innovations. We begin with the first facet, the flexibility of the organizational form. The proliferation of organizational forms has allowed the evaluation of what organizational structure would best fit the market environment and the implementation of the business strategy. The improvements in information systems and the availability of producer services/consulting firms as the purveyors of expertise and a potential external resource of the business, are the key to the increased flexibility of the business to restructure its organizational form for the implementation of the entrepreneurial initiative.

The second facet relates to the speed-up of the entrepreneurial initiative in terms of the flexibility of the production system for meeting the challenge of the speed-up of the innovation process. Unlike the previous section which dealt with the speed-up of the pace of innovation and its affect on the development process, the theme under consideration here is the speed-up and hence the decrease in time and cost of commercialization of innovation. Inventors create new products, while the entrepreneurs commercialize it. Until an innovation has been commercialized as an economic product (or process), it has no economic value. A major facet of the change can be linked to the change in production strategy from Fordism to post-Fordism⁴². Unlike Fordism which implies vertical integration and the ability to deliver standardized goods cheaply and on a mass scale, post-Fordism implies vertical disintegration through a system of sub-contracting and outsourcing so as to be able to deliver a variety of goods cheaply⁴³. This strategy not only allows product

⁴²Kumar (1995, Chapter three, pp.36-65).

⁴³The emergence of the change is linked to the emergence of what is described as 'third Italy' in the 1970s and 1980s as a dynamic area of small firms and workshops. The emergence of third Italy itself is linked to the power struggle between the organized labour and the management of large plants in the north of Italy (also referred to as First Italy) during the late 1960s that led to massive strikes and labour disturbances. These strikes and disturbances led to government legislation which gave workers of large plants the security of employment and allowed unions to establish factory councils with considerable powers. The emergence of third Italy was the reaction of the employers of large plants for overcoming the problem of organized labour by decentralizing production and resorting to sub contracting on a large scale (Ref: Kumar, 1995, pp.37-43).

David Harvey (1992, pp. 141-72), however, links the origin of the change to the strategy applied by the entrepreneurial forces for circumventing the over accumulation crisis of 1960s. The aim was to reduce the possibility of the repeat of any such crisis formation in the future. The strategy was to develop a flexible system of production. The entrepreneurs, therefore, targeted the rigidities in the system which constrained their ability to change and recreate their corporate empires. The end result was a transformation of their production strategy from Fordism to (what Harvey refers to as) 'Flexible Accumulation'. Flexible accumulation is aimed at bypassing the problems related to the rigidities of Fordism. The underpinning of flexible accumulation is minimization of fixed cost and lean systems of production. The aim is, flexibility of production to cater for the changing market conditions and economies of scope. The objective is flexibility with respect to labour processes, labour markets, products, patterns of consumptions, etc., which is achieved through organizational shifts towards

differentiation, but also substantially reduces the time and cost of converting new ideas into new products. Such an organizational form allows rapid deployment of new organizational forms and new technologies in production, hence the increase in the pace of implementation of entrepreneurial initiative.

The increased flexibility of the organizational form and the production process may be described as a 'catalyst' in the development process. It has allowed the speed-up of the process of implementation of the entrepreneurial initiative, and hence the speed-up of the development process itself. The shift from Fordism to post-Fordism or flexible accumulation is important not only for the change in production strategy from economies of scale to economies of scope, but also in generating sophistication in the process of subcontracting and outsourcing, which has been a major factor in facilitating the arbitrage of the production cost differential between nation-states, and in engendering the process of globalization which is a very important facet of entrepreneurialism.

5.5. The pace of Change in Market Equilibrium Following the Entrepreneurial Initiative:

As already discussed, it is not the entrepreneur's initiative, rather the consequence of his initiative that leads to economic development, and as a consequence a change in market equilibrium. I have referred to the transformation from Fordism to post-Fordism as the catalyst of change in our ontological conditions being experienced by us, because it has not only encouraged the entrepreneurs to innovate, but has also aided the competitors/followers of entrepreneurs in their endeavour. The consequence has been the compression of time interval between the entrepreneurial initiative and the change in market equilibrium. The reduction in time frame for the entrepreneur to retain his competitive advantage implies that continuous entrepreneurial initiative is required for maintaining competitive advantage in the marketplace.

We started this section by outlining the following equation as a hypothesis for providing a possible explanatory logic for the speed-up of the momentum of the development process.

$$D = f(n*i*I*E/r)$$

Where D is the development process.
 n is the number of entrepreneurs active in the marketplace.
 r is the entrepreneurial risk.
 i is the pace of innovation.
 I is the pace of implementation of entrepreneurial initiative.
 E is the pace of change in market equilibrium following the entrepreneurial initiative.

The aim of this section was to explain the effect of the transformation of each of the above noted variables in influencing the development process, and the power of transformation and change that is representative of the above equation. The aim was to connect this power of transformation and change to the crisis of confidence facing the modernist philosophical thought - a crisis that is also apparent in the financial services industry.

6. Conclusion:

The hypothesis under investigation in this chapter was:

The tensions reflecting the regulatory crisis in the financial services industry may be a subset of, or a part of a much wider area of tensions/crises facing the conceptual foundations of the regulatory philosophy: the modernist philosophical thought.

The regulatory framework for the control of the safety and soundness of the financial markets is based on Weber's bureaucratic rationality which rationalizes the need for the institutionalization of a meta-framework based on rules and regulations for the ordering and control of the operations of the financial services industry as a whole. The tensions in the financial services industry are a reflection of the problematic nature of this proposition. A deconstructive analysis of Weber's discourse on bureaucracy and Marx and Engels' discourse (Manifesto of the Communist Party) in light of Schumpeter's analysis draws attention towards the difference in the creative destruction and destructive creation of the modernist philosophers and that pursued by the entrepreneurs. The modernist philosophers (this includes regulators, political agents, etc. inspired by the modernist philosophy) aim to creatively destroy the contemporary system and destructively create and impose a new meta-framework based on reason which they assume to be timeless and eternal. The entrepreneurs, on the other hand, are a permanently revolutionary force. For them there is no such presumption of eternity linked to their destructive creation. Market is composed of not one, but a number of entrepreneurs, and the competitive market mechanism implies that entrepreneurs are continuously involved in the process of creative destruction and destructive creation in order to achieve commercial advantage over their competitors. It is this endeavour of the entrepreneurs to achieve commercial advantage that disturbs the basic assumptions of the meta-framework of the philosophers, regulators, political scientists, bureaucrats, etc.. The implication is, any framework that does not incorporate the contribution of the entrepreneur, effectively ignores the process of development. Such a framework can be effective only for a temporary period, the duration of which can be linked to one aspect: the momentum of the development process. This was also the message

of the previous section: it is the speed-up of the momentum of the development process which provides the explanatory logic for the present crisis in modernity and the tensions in the financial services industry.

In the context of the financial services industry, the question arises: what is the answer to the problem of safety and soundness in an industry that is continuously in the process of transformation and change? To answer the question, one needs to take a second look at the ideals behind the launch of the project of modernity (discussed in the previous chapter):

Past is a different country, history changes human nature, modern are different from the ancients. One could no longer look to the past for illumination and instructions. Moderns therefore live in a new world, and are thrown back entirely for new ways of thinking and acting; a complete new start on the basis of completely new principles - a break from the past; the dawn of an era of unending human progress on earth⁴⁴;

The implication being, that modernity as a concept was open ended, and implied continuous creation of new things, a revolution of new ideas and institutions. Yet there was a problem, in its formative phase, the prophets of modernity were convinced that there was a meaning to modernity. The French revolution which was the principle vehicle of the new consciousness became the basis for the aims of modernity: the achievement of freedom under the guidance of reason⁴⁵. The aim of the modernist philosophers and social scientists therefore became the rational organization of everyday social life using the accumulation of knowledge generated by many individuals working freely and creatively for the pursuit of human emancipation and the enrichment of their life. The basis of this endeavour was two fold: one, the scientific domination of nature promised freedom from scarcity, want, and the arbitrariness of natural calamity; two, the development of rational forms of social organization and rational modes of thought, promised liberation from the irrationalities of myth, religion, superstition, the dark side of our own human natures, and the release from the arbitrary use of (monarchical or religious) power. The conviction was, that only through such a project could the universal, eternal, and the immutable qualities of all humanity be revealed. It was during this period that the process of hypothetico-deductive reasoning formulated by Rene Descartes developed into the principal rhetoric of the modern social scientists. The modernist social scientist and philosophers applied Descartes' hypothetico-deductive argumentation not only to understand the evolution of society, but also to develop universal frameworks for developing a better society. They laid the foundation of modernity with its emphasis on certainty, optimism, and a rationally constructed social

⁴⁴Kumar (1995, pp.80).

⁴⁵Kumar (1995, pp.81).

order. It is this proposition that has continued to dominate our economic and social policy formulation (implicitly, if not explicitly) up to the present time. And it is this proposition, that has become problematical in the context of the time-space compression and the speed-up of the momentum of the development process generated by the entrepreneurial forces. We are again at the junction of a major transition. The situation is analogous to the conditions at the launch of the modernist project.

Past is a different country, history changes human nature, modern are different from the ancients. One could no longer look to the past for illumination and instructions. Moderns therefore live in a new world, and are thrown back entirely for new ways of thinking and acting⁴⁶.

We are again in transition, but not from the medieval to the modern, but from the modern to the postmodern epoch. But the question arises: What is postmodernism? Jean-Francois Lyotard (1984b) who is regarded as one of the leading prophets of the postmodern epoch provides a possible answer:

"What, then, is the postmodern? ... It is undoubtedly a part of the modern. ... A work can become modern only if it is first postmodern. Postmodernism thus understood is not modernism at its end but in the nascent state, and this state is constant⁴⁷."

In other words, postmodernism implies a permanently revolutionary state. Modernity, by rationalizing totalizing universal theories applicable across time and space, allowed itself to be bureaucratized and ossified, and hence lost its dynamic edge. Postmodernism is therefore modernity without its totalizing and universalizing preconceptions. The concept of postmodernism as a continuously dynamic philosophical thought, suggest a possible compatibility with Schumpeter's theory of economic development, and an avenue for examination for understanding the problems of the rapidly changing ontological conditions. This is also the message of the second part of the hypothesis:

- one: the tensions reflecting the regulatory crisis in the financial services industry may be a subset of, or a part of a much wider area of tensions/crises facing the conceptual foundations of the regulatory philosophy: the modernist philosophical thought.**
- two, the alternate philosophical thought which is generally described as postmodernism, may provide us with inspiration and ideas for the formulation of a regulatory strategy and regulatory framework that may facilitate the achievement of regulatory objectives while facilitating the amelioration of the tensions inherent in the financial services industry.**

⁴⁶Kumar (1995, pp.80).

⁴⁷Lyotard (1984b, pp.79)

CHAPTER SIX

AN EXPLORATION INTO THE CONCEPT OF POSTMODERN PHILOSOPHY

1. Introduction:

The idea of the present as 'postmodern' is now firmly on the agenda for debate. Diverse and at times conflicting references to postmodernism and postmodernity are to be found in a growing number of disciplinary fields and across an increasingly broad range of discursive formations. But this should not occasion 'panic'. And it does not necessitate an unqualified endorsement of the polymorphous perversities associated with some manifestation of the 'postmodern'. Rather, the critical implication is that complex transformation, questions, and problems deemed to be constitutive of the present are not adequately articulated in the prevailing forms of social theory, indeed cannot be so. That is the kernel of the 'postmodern' challenge to which a response is required.

Smart (1990, pp.28)

The above quote from Smart basically reasserts the rationale behind the second part of the hypothesis which is the area of investigation in this chapter.

one: the tensions reflecting the regulatory crisis in the financial services industry may be a subset of, or a part of a much wider area of tensions/crises facing the conceptual foundations of the regulatory philosophy: the modernist philosophical thought.

two, the alternate philosophical thought which is generally described as postmodernism, may provide us with inspiration and ideas for the formulation of a regulatory strategy and regulatory framework that may facilitate the achievement of regulatory objectives while facilitating the amelioration of the tensions inherent in the financial services industry.

The previous two chapters were aimed at investigating into the first part of the hypothesis that suggested the possibility of a connection between the tensions in the financial services industry and the tensions and the crises of confidence facing its philosophical foundations: the modernist philosophical thought. This chapter investigates into the second part of the thesis which involves an examination into the philosophical discourse that is challenging the logic and validity of the modernist philosophical discourse: the postmodern philosophical thought. The aim is to investigate into the postmodern philosophical thought as a source of inspiration and ideas that may assist us in

understanding the tensions in the financial services industry. However, before one can examine the concept of postmodernism, and the ideas generated within the realm of the postmodern philosophical thought, it is necessary to unravel the confusion surrounding the label of 'postmodernism'. This is necessary because there is no precise definition of postmodernism, and the term 'postmodernism' has been used in the media as a label for a number of phenomena, some of which makes sense, and some do not. Unravelling this confusion is therefore necessary in order to have a clear sense of what one is supposed to explore. This is the theme of section two of the chapter (section one being the introduction). The exploration of the concept of postmodernism is the area of investigation of section three which also forms the main body of the chapter. The approach adopted for examining the postmodern phenomenon is to classify postmodernism into three distinct but interrelated concepts: one, postmodernism as an epoch; two, postmodernism as a reaction to or a departure from modernity; and three, postmodernism as a signifier of the problematical features or the limits of modernity. First the concept of postmodernism as an epoch. Under this concept the term 'post' implies beyond, or after - a move to a new state of things - postmodernism as an indicator of a period of major historical transition of our society - the end of the modernist epoch and the beginning of a new epoch: the postmodern epoch. Within the concept of postmodernism as an epoch, three sub-themes that underlie the concept have been examined. These are one, postmodernism as a reflection of the changes in the social, cultural, and political conditions and practices; two, a shift in the way capitalism is working; three, a departure in our way of thinking about what could/should be done about the social conditions in the new epoch. It is the dynamic interaction between these three themes, that forms the basis of our experience of postmodernism as an epoch. The final subsection within the theme of postmodernism as an epoch relates to the implications for the financial services industry. The second approach that has been applied to examine the postmodernism, involves the use of the term 'post' as a contrast concept that implies: postmodernism as a reaction to or a departure from modernism (or modernity) which has been described as "positivistic, technocentric, and rationalistic", and "the belief in linear progress, absolute truths and rational planning of ideal social orders, and the standardization of knowledge and production". Postmodernism is, therefore, a reaction to or a departure from such mode of thinking. To understand and appreciate the concept of postmodernism as a 'reaction to, or departure from modernism' and its potential in encouraging a reconceptualization of the way we imagine, think, plan, and rationalize, it is necessary to examine: one, the source of inspiration and the underpinnings of power of the concept of postmodernism as a reaction to or a departure from modernism; and two, the counter-concepts that characterize the concept of postmodernism as a reaction to or a departure from the modernist philosophical thought. These are the two sub-themes that form the area of investigation of this section. The first sub-theme

involves an examination of: one, Foucault's genealogical analysis of knowledge; and two, Derrida's deconstructive analysis of knowledge. Both these philosophers and their philosophical enterprise can be described as the source of inspiration and the underpinning of the power of the concept of postmodernism as a reaction to or departure from modernism. The second sub-theme associated with the concept of postmodernism as a reaction to or a departure from the modernist philosophical thought, involves an examination of the counter-concepts that characterize the concept. The investigation covers eight key areas that form the basis of our ontological assumptions. These are: one, the problematic of disciplinary research; two, the concept of representation; three, relationship between the author, the text, and the reader; four, the concept of subject; five, the concept of truth; six, the concept of theory; seven, the concept of history; and eight, the concept of space. The final section of the exploration under the theme of postmodernism as a reaction to or departure from modernism relates to the implications for the financial services industry, which involves the application of ideas generated through the counter-concepts characterizing the concept of postmodernism and its underlying themes, to examine the tensions in the financial services industry. Postmodernism as a signifier of the problematical features or the limits of modernity is the third approach of investigation into the concept of postmodernism. This approach characterizes postmodernism as a concept that goes beyond modernity in the sense that it points to the limits of modernity. Here the term 'post' implies a reflection on modernism, i.e. 'modernity becoming conscious of itself'. This approach incorporates the works of philosophers and academics who find the project of modernity to be deeply problematical, whose endeavour is to lay out the problematical facets of modernity, while at the same time also making an effort to explore and understand the social and political codes and practices like tradition, ethnicity, etc., which were ignored and rejected by modernity (whose aim was to homogenize the social in line with the meta-discourses of the philosophers and social theorists). This approach (i.e. postmodernism as a signifier of the problematical features or the limits of modernity) is important because it allows us to examine the texts of the French philosophers like Foucault, Lyotard, and Derrida, whose philosophical works brought to light the problematical features of the modernist philosophical thought, and as a consequence stimulated the development of the postmodern philosophical discourse. This theme or this approach which involves the conceptualization of postmodernism as a signifier of the problematical features or the limits of modernity, therefore forms the stepping stone towards the next chapter which continues with the investigation into the second part of the hypothesis (which was also the inspiration for this chapter).

2. The Confusion Surrounding the Concept of Postmodernism:

Postmodernism has been described as one of the greatest intellectual challenges to established knowledge of the twentieth century¹. But the irony is that it is not possible to impose or arrive, by a definitional fiat, a universal concept of postmodernism. This is because the concept of postmodernism in itself rules out such a simplistic agreement. The term/label 'postmodern' or 'postmodernism' has, therefore, been described as fashionable, yet, irritatingly elusive to define². The commitment of postmodernism to open textuality implies that it is not possible to adopt a rigid definition of postmodernism - it precludes any possibility of formal foreclosure of its meaning³. Any attempt to devise a theory of postmodern society or postmodernity, or to delineate the role of postmodernism within the social order itself would essentially be a flawed effort to totalize or systemize. In effect it amounts to the development of a grand narratives that would be ripe for deconstruction⁴. That is why pluralism, indeterminacy, incredulity towards meta-narratives, agnosticism, deconstruction, innovation, and change are at the heart of the concept of postmodernism.

While the lack of specific definition and open-endedness, in itself is a part of postmodernism's appeal, at the same time however, this also makes 'postmodernism' a problematical concept to explain. One of the reasons for the difficulty could be the range of artistic, intellectual, and academic disciplines⁵ in which the term has been used, and more importantly, the differences in the ideas and the concepts that the term is considered to be representative of, in different disciplines. This is the reason why the concept of postmodernism has been described as being made up of distinct and overlapping features that cannot be aggregated or integrated⁶. This is also the reason why postmodernism has been described as "outrageously eclectic in its sources" and "synthetic and even syncretic in its expressions"⁷. It is this diversity in the usage of the term 'postmodernism',

¹Wisdom, J. O., (1987), "Challengeability in Modern Science", Blackmore Press, Dorset. (Cited in Rosena, 1992, pp.5).

²Featherstone (1991, pp.1).

³Turner (1990, pp.5).

⁴Featherstone (1991, pp.9).

⁵Featherstone (1991, pp.2) provides a listing of some of the fields where the term postmodernism has been employed. This includes the disciplines of music, art, fiction, film, drama, photography, architecture, literary theory and criticism, philosophy, anthropology, geography, and sociology. For details of some of the important works in these areas refer to Featerstone's text.

⁶Kumar (1995, pp.183).

⁷Kumar (1995, pp.103).

that creates an aura of confusion that surrounds the concept. The task is further complicated by the use of the term 'postmodern' by the media and popular press as a label and as a slogan for a wide variety of cultural and artistic phenomena some of which may appear to make sense, while some may not. This is the reason why the concept of postmodernism has been subjected to ridicule as hopelessly ambitious and empty. This is the reason why any reference to the term 'postmodern', immediately exposes one to the risk of being accused of jumping on a bandwagon or perpetuating a rather meaningless intellectual fad⁸. This is the reason why it is imperative that the aura of confusion surrounding the concept of postmodernism is cleared before a critical examination of the concept itself is undertaken.

To unravel the confusion surrounding the concept connected to the label of postmodernism, we need to examine its emergence. There is a certain degree of difference in the account of the emergence of the concept of postmodernism given by different authors. At the same time however, this difference is not a reflection of the difference in opinion regarding the concept of postmodernism, rather, it is a reflection of the orientation of the author.

Harvey (1992, pp.38) ties the genesis of postmodernism with the various counter-cultural and anti-modernist movements which sprang to life during the 1960s. Harvey describes these movements as: "Antagonistic to the oppressive qualities of the scientifically grounded technical-bureaucratic rationality as purveyed through monolithic corporate, state, and other forms of institutionalized power (including the bureaucratized political parties and trade unions), the counter-cultures explored the realms of individualized self-realization through a distinctive 'new left' politics, through the embrace of anti-authoritarian gestures, iconoclastic habits (in music, dress, language, and lifestyle), and the critique of everyday life". These movements which were centred in the universities, art institutes, and on the cultural fringes of big-city life spilled over into the streets resulting in the global turbulence of 1968⁹. The movement of 1968 though judged to be a failure on its own terms, was the cultural and political harbinger of the subsequent turn to postmodernism. It was somewhere between 1968 and 1972, that postmodernism emerged as a full blown, though still incoherent movement. According to Harvey (1992, pp.38) there was a certain irony in the movement against modernity and the development of postmodernism. It was the universal pretension of modernity combined with the liberal capitalism and imperialism (which it supported), which provided the material foundations for a cosmopolitan, transnational, and hence global movement of resistance to the hegemony of high modernist culture.

⁸Featherstone (1991, pp.1).

⁹The cities in the forefront of this movement were Chicago, Paris, Prague, Mexico City, Madrid, Tokyo, and Berlin.

Featherstone's (1991, pp.7-8) account of the genesis of postmodernism begins with Federico de Onis, who used the term 'postmodernism' in the 1930s to indicate a minor reaction to modernism. According to Featherstone, it was not, however, until the 1960s that the term became a ubiquitous label used by young artists, writers, and critics¹⁰ in New York to refer to a movement beyond the 'exhausted' high modernism, which was rejected because of its institutionalization in the museums and the academy. It gained wider usage in architecture, the visual and performing art, and music in the 1970s and 1980s. From this artistic postmodernism, the movement expanded into the wider arena of postmodernity as it drew in philosophers and social theorists who applied the term in the academic and intellectual fields as a concept to lay out the problematical facets of modernity, and/or to describe the emergence of a new epoch in which the tools and the concepts developed during the project of modernity have become problematical.

According to Cahoon (1996, pp.3-4) the term 'postmodernism' understood as distinguishing the contemporary scene from the modern, seems to have been first used in 1917 by the German philosopher Rudolf Pannwitz to describe the 'nihilism' of the twentieth century Western culture. The term then reappeared intermittently in other fields, most prominently in literary criticism referring to the reaction to aesthetic modernism. In philosophy it came in the 1980s to refer primarily to French post-structuralist philosophy, and secondarily to a general reaction against modern rationalism, utopianism, and what came to be called 'foundationalism'¹¹. In social science (also in the 1980s), the term was adopted to indicate a new approach to methodology. It also became linked to the concept of post-industrialism to indicate a shift in the character to the advanced Western economies. It was, however, in the 1990s, that the term 'postmodernism' became a ubiquitous label. It was brought into popular usage by the media as a label for everything from rock videos to the demographics of Los Angeles to reflect the cultural style and mood of the 1990s.

The three different accounts of the emergence of postmodernism, not only provide us with a view of the confusion surrounding the concept of postmodernism, but also provide us with an idea for unravelling the confusion, and begin our endeavour towards understanding the concept of postmodernism. One of the reasons for the differences in the accounts of the emergence of postmodernism relates to the differences in the orientations of the authors. David Harvey is a

¹⁰Prominent among them were the names of Rauschenberg, Cage, Burroughs, Barthelme, Fielder, Hassan, and Sontag (Featherstone, 1991, pp.7).

¹¹The attempt to establish foundations of knowledge and judgement, an attempt that has been the sole preoccupation of philosophy since René Descartes.

geographer and appears to be influenced by the idea of 'moment'¹². Harvey (1991, pp.429) explains the concept of 'moment' expounded by Lefebvre as: "fleeting but decisive sensations (of delight, surrender, disgust, surprise, horror, or outrage) which were somehow revelatory of the totality of possibilities contained in daily existence. Such movements were ephemeral and would pass instantaneously into oblivion, but during their passage all manner of possibilities - often decisive and sometimes revolutionary - stood to be both uncovered and achieved. 'Moments' were conceived of as points of rupture, of radical recognition of possibilities and intense euphoria. The idea was put to work to understand sublime moments of revolutionary fervour, such as the day the Paris Commune was declared. It was also to shape the consciousness of many students in the uprising of 1968". Harvey's concept of postmodernism is connected to the 'moment' when the idea of postmodernism became a social reality, and the events of 1968 constituted for many people the 'moment' when the idea of postmodernism became a social reality. The events of May 1968 as a 'moment' has also been acknowledged by Michel Foucault (1980a, pp.57) who describes it as a milestone or a moment when European revolutionary movements shed off the dogma of the 'Marx Effect'. The reference is to the equation: 'Marxism = Revolutionary Process'. Thus, opening up their intellect to new revolutionary thinking: the postmodern thinking. The concept of postmodernism is also echoed not only in the driving force behind the global turbulence of 1968 (antagonism to scientifically grounded techno-bureaucratic rationality, anti-authoritarianism, iconoclastic habits, etc.), but also in the character of the events themselves (cosmopolitan, transnational, and hence a global movement). Both these aspects are very important ingredients of the concept of postmodernism.

Cahoone is a professor of philosophy, he therefore stresses on the philosophical realm of postmodernism where it is linked to the French poststructuralist philosophy. His (1996. pp.1) view of postmodernism is that of an overlapping family of ideas, opinions, philosophical works, etc., some of which (labelled as postmodern) are very important works that raise deep questions, point to new developments, and generate new knowledge that deserve to be studied and investigated. Under this approach the accent would be on an examination of some of the ideas and works of the philosophers and social scientists which have become the source of inspiration in the development of the postmodern philosophical thought.

Featherstone is a sociologist, his realm therefore encompasses the social and the cultural aspect of the postmodern phenomenon. Featherstone's account is important because he draws our attention to the problematical realm of the postmodern phenomenon: the emergence of the label of

¹²The concept of moment was introduced by Henri Lefebvre in 1959 in "La Somme et la reste" which was an autobiographical, autocritical, and evaluative summary of much of his own life work in the context of the times.

postmodernism in the aesthetic realm¹³ which is not only the reason for the prominence of the label 'postmodernism', but also for the aura of confusion surrounding the concept of postmodernism. Featherstone examines the 'postmodern' phenomenon as a contrast concept by applying a framework of pairing between the modern and its postmodern equivalent (for example modernity with postmodernity, modernization with postmodernization, and modernism with postmodernism). Featherstone's framework of pairing is important because it brings to prominence the problematical nature of the pairing framework itself, which is an important part of the confusion surrounding the concept of postmodernism. Three arguments can be presented in this regard. One, the pairing of 'postmodernism' as a counter-concept against 'modernism' is problematical. The reason being that modernism¹⁴ in itself was a late nineteenth century aesthetic movement which developed as a

¹³The reference is to application of the concept of postmodernism in the area of art and literature, including poetry, drama, painting, music, etc..

¹⁴The concept of 'modernism' has been elucidated in a fair degree of detail by Kumar (1995, pp.85-100). Kumar explains the concept of 'modernism' as an end of the nineteenth century aesthetic movement that developed as a reaction to the foundational rationality and the techno-economic order of 'modernity'. He describes 'modernism' as a late nineteenth century cultural movement that caused a split in the soul of modernity, between modernity as a social and political project with its emphasis on science, reason, progress, and industrialism, and modernity as an aesthetic project that rejected the values of the former in favour of sentiment, intuition, and free play of imagination. The latter (i.e. modernity as an aesthetic project) is referred to as 'modernism'.

To understand the concept and the significance of modernism, it is necessary to examine its antecedents. The reference is to the late eighteenth century to the mid nineteenth century aesthetic movement referred to as 'Western Romanticism' which was a precursor to the development of modernism. According to Kumar (1995, pp.86) while Romanticism shared modernity's utopian sentiments of progress and revolution, at the same time however, it also challenged the foundational rationality of modernity. Romanticism challenged the leading principles of the enlightenment: reason was opposed by imagination, artifice by natural, objectivity by subjectivity, calculation by spontaneity, the mundane by the visionary, etc.. If modernity meant a sharp break from the past and an orientation towards the future, the Romanticism was inclined to seek inspiration from the past to criticize the uncreative present.

While modernism reflects some of the characteristics of Romanticism, and may even be seen as late Romanticism, but at the same time however, it may be regarded as qualitatively different from Romanticism in the sense that it went further than Romanticism in its assault on modernity. According to Kumar (1995, pp.98) modernism was no simple rejection of modernity. It was rather a reaction, a critical response to it. Modernism also involved a cultural avantgardism, with its hostility towards all received forms of art, and more generally towards the authority and legitimacy of the received cultural models of art and literature. They created new forms and styles of art and literature which broke the rules and conventions governing (contemporary) art and literature. The most extreme or radical of these were the Dadaism and Surrealism. Of these, Dadaism is of special importance. Kumar (1995, pp.97) describes Dadaism as an exuberant and outrageous assault on all the official ideas and institutions that had conspired to produce the disenchanted mood of the time (1916-20). The rage was directed not at politics but at art, the sacred cow of the establishment. The aim was to de-sacrilize art, to question its purpose and the very possibility of its existence in these modern times. The desire was to mock and shock the establishment through the use of the techniques of irony, absurdity,

reaction to the foundational rationality and the techno-economic order of modernity. But the concept of modernism is itself ambiguous¹⁵ because in some spheres (for example, architecture), modernism as a cultural movement affirmed rather than denied the principles of modernity. One of the problems with the concept of postmodernism in arts¹⁶ is that it appropriates rather than repudiates many of the

scandal, and subversion for presenting their ideas.

Unlike Romanticism, modernism had its affect beyond arts and literature. It also touched the philosophical, psychological, political, and social realms where rationalism, positivism and utilitarianism came under attack. In this respect Kumar (1995, pp.96) specifically names Freud and Bergson whose attack on reason, the central tenant of modernity, was profound. And most importantly, it was during this movement, that Nietzsche, largely ignored until this time, was reborn and acclaimed as the prophet of modernism. Kumar (1995, pp.97) describes the central influence of Nietzsche as the common factor that suggests a degree of continuity, and perhaps even identity between modernism and postmodernism.

¹⁵According to Kumar (1995, pp.98), modernism as a cultural movement both affirmed modernity, and denied it, it continued its principles, as well as challenged it to its very core. This is echoed in Cubism in art, which was both a critique of modernity, as well as a fascinating exploration of the modern and scientific ways of seeing. Modernism in some of its aspects as in Futurism and Constructivism, showed a fascination and almost an obsession with the modern. Their emphasis being that the modern society was not modern enough, i.e., tradition and nostalgia were still a drag chain. This facet is very prominent in the Modern Movement in architecture that stressed on the need for planning buildings and cities on scientific and universal principles: 'form should reflect function'. In this context, a project of special significance was the Bauhaus, founded by Gropius (1883-1969) in 1919, aiming at a new functional interpretation of applied art. Modernism in architecture implies modern buildings with their characteristic features of the 'International Style': geometric, rectangular, and streamlined. Modernism in architecture is important because it was primarily in architecture that claims for postmodernism were first seriously made. Postmodernism in architecture, can therefore, be understood to some extent, as a reaction against the kind of modernism represented in modernist architecture.

Modernism, according to Kumar (pp.99-100), like Romanticism, has a split soul. But the split was deeper and more neurotic, and also reflected a fin-de-siecle mood: a sense of crisis and a conviction of an end that would be the prelude to a new beginnings. Modernism had its own kind of confidence: a feeling of exhilaration in the midst of cultural despair. Its fascination for the new put it on the side of progress, and so connected it with one of the central ideas of modernity, but at the same time, this obsession with novelty eventually broke this connection. Change came to be viewed as desirable for its own sake rather than as the means for the realization of greater freedom or a more complete self-expression.

¹⁶Featherstone (1991, pp.7-8) summarizes some of the central features associated with postmodernism in arts as: the effacement of boundary between art and everyday life; the collapse of the hierarchical distinction between high and mass/popular culture; a stylistic promiscuity favouring eclecticism and the mixing of codes; parody, pastiche, irony, playfulness and the celebration of the surface 'depthlessness' of culture; the decline of the originality/genius of the artistic producer; and the assumption that art can only be by repetition.

features of modernism¹⁷, especially those that were developed as a reaction to modernity. In other words, the ‘post’ of postmodernism when paired with ‘modernism’ does not necessarily represent a contrast or a counter-concept. The second argument relates to the problematical feature of Featherstone’s pairing framework itself. This is explained by Kumar (1995, pp.101) who points out that, while it may be possible to differentiate between ‘modernism’ and ‘modernity’ as two separate concepts, it is not possible to do the same with ‘postmodernism’ and ‘postmodernity’, because both the terms are used interchangeably. The reason being (according to Kumar, 1995, pp.103), that the impulse to the postmodern theory originally came from the cultural sphere. This is reason why the label ‘postmodernism’ is more prevalent than ‘postmodernity’. From here it was picked up by thinkers and critics in other spheres including mass media, leading to an ever widening circle of social life being pronounced postmodern. In the process, elements from other theories first elaborated elsewhere were also incorporated into the postmodern realm¹⁸. This brings us to the third argument related to the modern-postmodern framework. Unlike modernism which encourages differentiation and specialization of disciplinary knowledge, postmodernism encourages the breakdown or the de-differentiation of the dividing line between the different realms of the society: political, economic, social, and cultural. The confusion primarily emanates from our efforts to analyze postmodernism in the context of the modernist framework.

Having unravelled some of the aura of confusion surrounding the concept of postmodernism, we can now begin our search for the concept of postmodernism itself. This is the aim of the next section.

3. The Concept of Postmodernism:

We begin by repeating the remark by Turner (1990, pp.5) noted at the beginning of section two of this chapter, that the commitment of postmodernism to open textuality implies that it is not possible to adopt a rigid definition of postmodernism - it precludes any possibility of formal foreclosure of

¹⁷Featherstone (1991, pp.7) summarizes the basic features of modernism as: an aesthetic self-consciousness and reflexiveness; a rejection of narrative structure in favour of simultaneity and montage; an exploration of the paradoxical, ambiguous and uncertain open-ended nature of reality; and a rejection of the notion of an integrated personality in favour of an emphasis upon the de-structured, de-humanized subject.

¹⁸Examples are, Daniel Bell’s (1974) post-industrial theory to highlight the role of knowledge in the postmodern era, and post-Fordism to stress on the change in the operational principles of capitalism from centralization of production to achieve economies of scale, to decentralization of production to achieve economies of scope.

its meaning. The question arises, how do we formulate a 'definition' of the concept of postmodernism when the concept of postmodernism itself would not allow such a possibility? The postmodernist answer to such a question would be to investigate into the concept of 'definition' itself.

The Encyclopedia of Language and Linguistics defines the term 'definition' as "the explicit attribution of a meaning to a word"¹⁹. At the same time however (also noted under the meaning of the term 'definition'), there is an ancient philosophical tradition which extends the notion of 'definition' to the description of the characteristics (often characteristics that are considered essential) of the phenomenon which corresponds to the term. In other words the term 'definition' does not refer to a word, but directly to the object. Here we have the answer to our question. The way out of the predicament created by the impossibility of arriving at a rigid definition of the concept of postmodernism, is to examine the characteristics of the postmodern phenomenon. This is the approach adopted by Rosenau (1992) to explain the concept of postmodernism. But the problem with this approach is the wide disparity in the characteristics that are considered to be and hence presented as being representative of postmodernism. Rosenau's strategy for surmounting the problem is to segregate the postmodernists into two categories on the basis of their orientations: the 'sceptical postmodernists'²⁰ and the 'affirmative postmodernists'²¹, and then to unravel the concept of postmodernism by outlining the characteristics that are representative of the two classes of the postmodernists. While this approach helps in introducing us to the body of opinions and ideas that characterize the two classes of postmodernists, it also creates a problem. The problem with this approach is that it gives the impression of postmodernism as having some sort of ideological underpinnings which is reflected in the characterization of the two classes of postmodernists. Nothing could be further than this, because if postmodernism takes the shape of an ideology, it would imply the application of a formal closure of its meaning, which would invalidate the concept of postmodernism itself. It is therefore necessary to apply more than one approach to examine the

¹⁹Belvedere, (1994, pp.843), "Definition in Legal Language", in R.E.Asher, and J.M.Y. Simpson, "The Encyclopedia of Language and Linguistics", Vol 2, pp. 843-850, Pergamon Press, Oxford, 1994.

²⁰The 'sceptical postmodernists' represent the negative and the gloomy side of postmodernism. They argue that the postmodern age is one of fragmentation, disintegration, meaninglessness and the absence of moral parameters and societal chaos. Inspired by Heidegger and Nietzsche, it speaks of the demise of the subject, the end of the author, the impossibility of the truth, and the abrogation of the order of representation. They believe that there is no truth. All that is there, is the play of words and meanings.

²¹The 'affirmative postmodernists' agree with the views of the sceptics regarding modernity, but are however more optimistic and more hopeful in terms of the postmodern age. These postmodernists seek philosophical and ontological practice that is non dogmatic, tentative, and non-ideological.

concept of postmodernism. The best strategy for examining the postmodern phenomenon would be to apply a collage²² of approaches to bring together the various opinions, ideas, and concepts that characterize the postmodernism phenomenon, and then try to extend these ideas to understand the tensions in the financial services industry.

The approach being adopted here to examine the postmodern phenomenon is to classify postmodernism into three distinct but interrelated concepts. These are:

1. Postmodernism as an Epoch.
2. Postmodernism as a Reaction to, or Departure from Modernity.
3. Postmodernism as a Signifier of the Problematical Features or the Limits of Modernity.

3.1. Postmodernism as an Epoch:

Under this approach, the term 'post' would imply beyond, or after - a move to a new state of things: a new 'epoch'. Postmodernism as an indicator of a period of major historical transition of our society. The end of the modernist epoch and the beginning of a new epoch: the postmodern epoch. Here a millennial feeling is also apparent. There is a sense of ending, and there is also an expectation of a new beginning. According to Caldwell (1975)²³, although there have been a number of transitional periods, but some have been more significant than the others because of the occurrence of a series of events and the culmination of a series of trends which have had a profound effect not only on the human condition but also on the human viewpoint and thinking. The transition from medieval to modern times was one such phase involving a change in our thinking and our condition. The present period (transition from modern to postmodern) was the next major phase of transition in our condition and our thinking²⁴. The term 'post', therefore, signifies the transitional present. It implies that there is more of an agreement of the close of the present era rather than the future state.

When the term postmodernism is used as an epoch, the aim is to identify features of the world which support the hypothesis that the society is moving towards a new postmodern era. This is also the basis of a number of concepts with the 'post' prefix which are used to explain the features of this postmodern epoch. This includes post-Fordism, post-industrialism, post-capitalism, etc.. The

²²Collage, though pioneered by the modernist, is a technique that postmodernists have used as a technique of representation. Collage involves the juxtaposition of diverse and seemingly incongruous elements from which the consumer of the text can pick and choose to suit his need.

²³Caldwell uses the term post-modernism instead of postmodernism. The hyphen has been dropped here to maintain consistency.

²⁴Caldwell (1975, pp.568).

term 'post' implying the progression to a new state of thing, and the implication that systems have changed radically, old theories and old mechanisms have become problematical for catering to the challenges of the present era, a review and reevaluation of the problems is therefore necessary.

To understand the concept of postmodernism as an epoch, it is necessary to examine three themes that underlie the concept. These are: **one**, postmodernism as a reflection of the changes in the social, cultural, and political conditions and practices; **two**, a shift in the way capitalism is working; **three**, a departure in our way of thinking about what could/should be done about the social conditions in the new epoch. This being a part of a cultural movement that is reconceptualizing our experience. It is the dynamic interaction between these three themes that forms the basis of our experience of postmodernism as an epoch. To appreciate the concept we need to undertake a more detailed examination of each of the three features and the interrelationship between them.

3.1.1. Postmodernism as a Reflector of the Changes in the Social, Economic, and Political Practices in the Society:

We begin with the first theme that underlie the concept of postmodernism as a epoch. The reference is to postmodernism as a reflector of the changes in the social, economic, and political practices in the society. Since it is a reflector of the different facets of those practices, it appears in different guises, hence the eclectic character of postmodernism²⁵. Rosenau (1992, pp.9) describes the situation as societal upheavals, cultural transformation, political change, deep philosophical debate over core values, and disciplinary crisis. The important thing is to understand what is happening and not necessarily to agree on a concept to capture it. Postmodernity as an epoch may therefore be viewed as a concept that alerts us to the key questions concerning contemporary social, economic, and political changes. While there may, as yet be no agreed meaning of the term postmodernism, the concept itself is important because it directs our attention to the changes taking place in our contemporary culture. Postmodernism should be seen as a concept that invites participation in a debate over the nature and direction of the new epoch²⁶.

A vital element of this change in our political, economic, and social practices relates to what is described as globalization and/or time and space compression. An examination of this element is necessary for understanding the postmodern condition. Because of the vital importance of this element of change, it has been examined in sufficient detail in Part IV of the thesis. Here, for the necessity of examining and understanding the concept of postmodernism, a brief discussion on the

²⁵Harvey (1992, pp.113).

²⁶Lyon (1994, pp.84).

phenomenon of time and space compression has been undertaken. We begin with the concept of temporal compression. Temporal compression implies the speed-up of our ontological reality. It implies acceleration in turnover times of production, exchange, and consumption. It also implies speed-up of the pace of information processing, decision making, knowledge generation, innovation, and change. Harvey (1992, Ch.17, pp.284-307) explains the consequences of temporal compression as the increase in the volatility and ephemerality. Whether it relates to fashions, products, production techniques, labour processes, idea and ideologies, values and established practices, all have been affected by the temporal compression²⁷. Compared to life in a less rapidly changing society, more situations flow through the channel of experience of a person during a given interval of time. This implies profound changes in human psychology. This transience creates a 'temporariness in the structure of both public and personal value systems'. Volatility and ephemerality makes it hard to maintain any sense of continuity. Past experiences get compressed into an overwhelming present, and the vision of the future is limited only to the extent to which it can be discounted into the present. Volatility also makes it difficult to engage in long term planning. Short-termism and learning to play with volatility therefore becomes the key strategy of success, as well as survival. The implication being, one has to be either, highly adaptable in responding to the changes in market shifts, or be involved in masterminding the volatility through the process of entrepreneurialism.

Having examined the concept and the implications of temporal compression, we can now examine of the concept and implications of spatial compression on the postmodern landscape. Reduction in the time and cost of communication is one of the most important forces behind the reduction in the friction of distance²⁸, and actuation of the process of spatial compression, leading to a phenomenon referred to as globalization. The implications of globalization on the ontological conditions are numerous, some of the more important ones are: one, the creation of systemic interdependencies between nation-states; two, the increased power of the corporate sector achieved through the linkage of their operations across the globe into an integrated global strategy; three, an implication of one and two is that political, economic and cultural life is now strongly influenced by developments at global level. This implies a reduction in the autonomy of the nation-states to take decisions at the national level independent of the state of affairs at the global level. As a consequence, the institutions and the practices at the national level are correspondingly weakened; four, a direct consequence of globalization and the reduction in the power base of nation-state and

²⁷The emphasis here being on the more general society wide effects.

²⁸Reduction in friction of distance implies reduction in the social distance, as well as the spatial distance when measured in unit of time and unit of cost, instead of the unit of length.

the improvement of societal transparency in the cultural and social realm, is the reduction in the significance of the ideologically imposed national culture and national identity, while at the same time a renewed importance of socially bound local culture and local identity at ethnic level. The renewed importance of ethnic identity combined with the increased flow of information about the other nationalities and ethnic groups who inhabit our global village, which is a consequence of the globalization of the media services implies a recognition and a better understanding of the other nationalities, ethnic and minority groups, their rights, their identity, differences, and the rights of the others. Postmodern landscape is therefore a plural landscape in which cosmopolitanism, cultural hybridization, multiculturalism, and multi-ethnicism are encouraged, while enlightenment's universalism and ethnocentrism are discouraged²⁹. The existence and availability of different styles and images from all around the world at one place implies that the natural way of life in the contemporary world involves a pot pouri or a heterogeneity of styles, images, cultures, etc.. This is the reason why the postmodern ontological landscape is unprecedented in human history - at least in the degree of its pluralism. This is the reason why postmodern culture has been described as being a culture based on eclecticism. This also the reason why collage and eclecticism have come to dominate the representation of the postmodern culture.

3.1.2. Postmodernism as an Epochal Shift in the Operations of Capitalism: The Inauguration of a New Stage in Capitalism:

Now we come to the second theme underlying the concept of postmodernism as an epochal shift in our ontological conditions. The reference is to the notion that postmodernism represents an epochal shift in the operations of capitalism, i.e., the inauguration of a new stage in capitalism (Harvey, 1992, pp.112; Lyon, 1994, pp.6). The suggestion being the link between the change in the operations of capitalism and its effect in terms of bringing about an epochal shift in the culture of the society. This theme incorporates Hal Foster's (1985) representation of 'postmodernism of reaction' where the emphasis is on replicating, reproducing, and reinforcing the logic of consumer capitalism³⁰. This is

²⁹This is reflected in Kumar's observation (1995, pp.121-122, and pp.193-194), that postmodernism reacts against enlightenment's universalism, and at the same time encourages enlightenment's cosmopolitanism.

³⁰The 'postmodernism of reaction' is closer to the concept of postmodern covered by the media and the popular press where the emphasis is on consumerism and avantgardism. Here the emphasis is on postmodernism as the cultural logic of consumer culture or the multinational capitalism. Here the argument is that postmodern cultural forms replicate, reproduce, and ultimately serve to reinforce the logic of consumer capitalism. Here the emphasis is on aiming to understand and to celebrate the contemporary consumer culture rather than to control it via a grand narrative. Hal Foster (1985, pp.xi-xii) and Barry Smart (1990, pp.24-25).

why postmodernism has also been referred to as the ‘ideological reflex of the latest phase of capitalism’s inventiveness’ (Kumar, 1995, pp.192). In this new phase of capitalism two issues are crucial, one, the prominence of new information processing and communication technologies and their application by the capitalist forces to achieve time and space compression, and the global expansion and extension of their corporate image: a phenomenon referred to as globalization; two, consumerism which represents a change in the corporate strategy of the capitalist sector from production to consumption³¹. Although philosophers and social scientists may not acknowledge, it has been the speed-up of the process of entrepreneurialism (a process that was examined in detail in the previous chapter), that has been a major force behind the compression of time and space, and the consequent changes in the social, economic, and political practices in the society.

3.1.3. Postmodernism as a Departure in Our Way of Thinking About What Could/Should be Done About the Ontological Conditions in the New Epoch:

Now we come to the third and final theme that underlies the concept of postmodernism as a epoch. Postmodernism represents a departure in our way of thinking about what could/should be done about the ontological conditions in the new epoch. This theme can also be viewed as the consequence of the first two themes where the emphasis is on the changes in our ontological conditions. The overtone of the discussion being, the realization and the acknowledgement that systems have changed radically. They have thrown up new forces and new configurations. We indeed are in a new epoch, old categories cannot simply be slapped on to the new forms (Kumar, 1995, pp.121). Postmodernism, therefore, represents a departure in our way of thinking about what could/should be done about the ontological conditions in the new epoch. The significance of this change in our thinking becomes conspicuous when we connect this with the observation by Harvey (1992, pp.115) that the change in the way we imagine, think, plan, and rationalize is bound to have material consequences.

³¹Lyon (1994, pp.56) explains the concept of consumerism as a change in focus of corporate strategy from production to consumption, and a consequent change in focus from the production of goods to the production of needs and wants. The implication is, a change in consumer culture where everything is commodified and the process is reinforced by constant television advertisement. Television becomes the key to the production of needs and wants, and the mobilization of desire and fantasy. Explaining the concept of consumerism, Harvey (1992, pp.287-288) argues that Marx’s analysis of commodity production is outdated because capitalism is now predominantly concerned with the production of signs, images, and sign systems, rather than commodities. This systems of production and marketing of images exhibits some special features which are quite different from those of manufacturing of commodities. Firstly, the consumer turnover time of images may be very short indeed. Secondly, they can be mass marketed instantaneously over space, thus they can help to relieve the pressure of overaccumulation by accelerating turnover time as well as overcoming spatial barriers. In such a scenario, ephemerality and instantaneous communicability over space becomes the virtues to be explored and appropriated by the capitalist forces.

3.1.4. Implications for the Financial Services Industry:

Having examined the concept of postmodernism as an epoch, we can now extend the concept postmodernism as an epoch and its underlying themes to examine the tensions in the financial services industry. In the financial services industry, we do see evidence of all the three themes underlying the concept of postmodernism as an epoch. The first two themes are clearly evident. We do see changes in the organizational and the operational configuration of the financial services industry, which does reflect an epochal shift in its operations. Financial institutions and the financial markets have moved out of the framework of nation-states, and have, or are in the process of becoming transnational entities competing in a global playing field. The phenomena of temporal and spatial compression are also apparent in the industry, which is evidenced by the increased systemic interdependencies between nation-states, and a reduction in the capacity and ability of action of the nation-states controlled by regulatory sector, whose existence and operational framework are still based on the modernist philosophical thought and its rationale of controlling and ordering the organization and the operations of the financial services industry by means of a regulatory framework based on minimum regulatory standards. The tensions in the financial services industry are evidence of the problematical nature of such a philosophy in meeting the challenges of the present epoch. This brings us to the third theme of the concept of postmodernism as an epoch: postmodernism represents a departure in our way of thinking about what could/should be done about the ontological conditions. This is where postmodernism can assist us in ameliorating some of the problems. This is also the aim of this chapter.

The concept of postmodernism as an epoch and postmodernism as a departure in our way of thinking about what could be done to manage the transition to the new epoch, is the theme of the essay by Caldwell (1975) in which he refers to postmodernism as an indicator of a period of major historical transition of our society. The significance of transitional periods, according to Caldwell, is associated with the occurrence of a series of events and the culmination of a series of trends which have a profound effect, not only on the human conditions, but also on the human viewpoint and thinking. The current phase of transition (the postmodern condition) is significant on account of three important consideration: one, intellectual transformations, i.e., changes in concepts, images, and values; two, the growing interdependency of people and nations; the third element which is also the main theme of Caldwell's essay relates to the tremendous growth in the amount of information organized and distilled into knowledge and the means of its dissemination. This is the single most important element of the present phase of transition (the postmodern condition). The importance of this facet of the present transition is based on the premise that the accelerating growth of information would by its own sheer magnitude, diversity, and utility, effect the state of knowledge itself and its

use. It would also lead to a change in the attitude and beliefs, or the view points and thinking of the individual members of the public, as well as the public and private sector institutions and agencies.

To a large extent, all organizations whether private or public, are information processing agencies. The aim of the private sector agencies is to extract information from the various sources, and use it to develop strategies for producing and selling goods and services that can help them in achieving competitive advantage in the marketplace. The success or otherwise of governmental agencies in the postmodern period relates to their ability to process and use the information about the changing market environment to bring about adaptive changes in the attitudes and the operational framework of their agencies in order to make them compatible with the market environment and the needs and expectations of the public.

Caldwell's essay is about the tensions created due to differential change in the attitudes and beliefs of the public, and the adaptive changes in the governmental agencies. His analysis is important because it not only draws attention to the logic for the problems/tensions, but also provides direction flags that can be applied for their resolution. According to Caldwell, the most crucial problem facing a society during transitory periods relates to the differential rate of change between the attitude and beliefs of the general public and private sector agencies (or the governed), and the adaptive changes in the attitudes and the operational framework of the public agencies. This includes the legal framework, and the organizational theories that form the basis of their operational frameworks and their actions. The changes in the attitudes and beliefs of the general public and private sector agencies may be expected to occur more rapidly than the adaptive changes in the governmental agencies, because the latter are based on old beliefs and concepts which continue to be reflected in their behaviours. The operational framework of the public agencies is still based on Weberian system of bureaucratic control. The problem with bureaucratic control is that: one, it is backward and not forward looking - the framework is developed on the basis of past experience; two, it involves the application of a formal closure to decision making which completely stultifies the creativity and the enterprise of the managers and the decision makers. The reason private sector do not suffer from such a malady is because the coercive laws of competition do not allow the private sector institutions to survive unless it keeps abreast of the change. The only exception would be a situation where monopoly or oligopoly is maintained with the implicit support of the governmental agencies, as was the case in financial services industry prior to the launch of the process of deregulation. Here, as a matter of interest it would be worth mentioning that the birth of bureaucracy itself was a response to the crisis of control created by the speed-up of material processing systems during the industrial revolution. The pioneering response to this crisis of control was the development of Weberian bureaucracy in business as well as public agencies (Kumar, 1995, pp.18). Later on,

however, the development of computer as an information process tool, and the development of management accounting as a tool for quantifying labour and other business operational costs allowed the management of private sector business organizations to supplant bureaucracy with information based decision making. The same, however, is not true for the public sector agencies. It is an irony that the system of management and control (bureaucracy) which was developed as a pioneering response to the problem of information overload generated by the industrial revolution, has become a problematical proposition, a drag chain, in response to the information overload and changes in our ontological conditions generated by the post-industrial revolution.

In the context of the central theme of Caldwell's essay³², when the ideas of significant portion of the governed (banks and securities firms) are no longer consistent with the assumptions upon which the thinking and the operational framework of the governmental agencies (regulators) are grounded, a variety of tensions develop. Caldwell (1975, pp.569) identifies four levels of tensions: one, between the governmental agencies (the regulator) and their critics (the public and the regulated); two, between different governmental agencies (inter-agency conflict: between those agencies committed to new orientations and those that serve traditional purposes); three, within the same agency (intra-agency conflict: between traditionally and transitionally oriented within the agency); and finally within the mind of the individual manager (in terms of the need for undertaking a reevaluation and revision of his and his agency's mission, or holding on to the tried and tested traditions). According to Caldwell, while some degree of tension is necessary for organizational health, and creative conflict has its beneficial effect, however, excessive tensions³³ could be damaging not only to the effectiveness of the public agency, but also to the survival of the public

³²The differential rate of change between the attitude and beliefs of the general public and private sector agencies (or the governed), and the adaptive changes in the attitudes and the operational framework of the public agencies.

³³These multiple levels of tensions are an indicator of the complexity of the task facing the public agencies in managing this transitory period. This can create problems for the personal of the governmental agencies. The self image of an agency's personal may differ dramatically from their image as perceived by those who no longer share their assumptions. The self image of dedication to mission and public service objectives may appear from outside the agency to be routine bound and self serving. Bureaucrats may be perceived as self perpetuating agents of obsolete programs and archaic institutional arrangements. When the stress between the agency and the citizens reaches a point of alienation, the legitimacy of the institution itself becomes questionable and its credibility impaired with the informed critics. If the communication media is strong and influenced by the critics, the effects of these tensions will be over a much wider sector of public opinion than those immediately opposing the agency programs. A crucial ramification of these tensions, is that the people committed to institutional mission and mandates find themselves increasingly on the defensive. Their resistance is reinforced by loyalty to institutions and tradition, plus the peer group consensus. This defence becomes a bureaucratic paranoia.

agency itself. If the stress between the agency and the citizens reaches a point of alienation, the legitimacy of institution becomes questionable and its credibility impaired with the informed critics.

The characteristics required for the management of public affairs during a transitory period are foresight, initiative, flexibility, and sensitivity. But possibly the greatest need and resource, of the public official in this era of transition is 'knowledge'. In the context of the present transition (from the modern to the postmodern era), the particular kind of knowledge that is necessary for the public agencies is not the quantifiable technically oriented knowledge or the knowledge of procedural know-how (which forms the major knowledge base of public agencies). Such knowledge, although a necessary attribute, increasingly becomes an insufficient attribute of effectiveness. This is partly on account of the increase in the pace of knowledge growth, especially in the area of technical knowledge, which implies increase in the speed of obsolescence of technical knowledge, and as a consequence, an increase in the ignorance of the public officials *vis-a-vis* the market participants. This (ignorance) is a very important aspect of the problem facing the public agencies during the present period of transition from the modern to the postmodern epoch. Ignorance, according to Caldwell (1975, pp.571), relates to the attitude of indifference or rejection towards things that could and should be known.

- Ignorance expands with the growth of knowledge. This is because the more we know, the more we become aware of the things that we could know, and need to know, but do not know because of either deficiencies in the content of information or in the organization of information presently available.
- Ignorance also increases with the expansion of knowledge because it becomes impossible for the human being to absorb all the rapidly increasing information that becomes available.

Paradoxically we are all 'innocent sinners', but the 'culpable sinners' are those who refuse to be guided by the available evidence.

The particular kind of knowledge that is necessary for the public agencies in this transitional era relates to the knowledge of trends, interactions, and synergistic effects. The task of public agencies during transitional time relate to reassessing priorities, redefining goals, and of devising the means towards the creation of a material and intellectual environment in which all other social institutions can play their respective roles in the transition³⁴. This requires intellectual development and the broadening of the knowledge base of the public officials. In other words it requires intellectual broadening and reorientation of knowledge base of the agency personnel, especially the

³⁴Today more than ever before, the problems of society in transition requires the public official to become a kind of cultural midwife. His role includes the function of policy analyst, interpreter, and in the most fundamental sense: a prophet.

decision makers on a continuous basis to prevent institutional obsolescence. Unfortunately, however, public agencies still seem to be oriented towards quantifiable, technically oriented training, thus they risk neglecting the 'essential' through their preoccupation with the 'practical', which is unfortunate because the tasks requiring technical knowledge (technical tasks) can be out-sourced to the private sector for whom the competitive market mechanism would insure against the obsolescence of their knowledge.

The 'affirmative action' most needed in the public service today is a determined effort to discover or develop administrators able to conceptualize policy alternatives and their implications, and to think operationally in systems terms. This is not the role of 'administrative technicians' or the conventional 'generalist', rather it requires insights, foresight, and the ability to focus. It requires the ability to obtain and apply knowledge more effectively. However to be effective, and this is very important, the knowledge should be socially shared. It should be possessed simultaneously by individuals and society in the aggregate. Here Caldwell is referring to the information/knowledge base of the public agencies. The reference is to the information asymmetry that the bureaucracy maintains under the guise of 'official secrets³⁵'.

In the context of the financial services industry, what is needed is intellectual broadening of the knowledge base of the regulators. This would imply that the regulators need not be concerned about the obsolescence of their technical knowledge because of the explosion of financial innovation (not only in the area of product development but also in the area of risk management and control). Technical analysis of risk inherent in the operations of the financial institutions can be passed on to the private sector agencies (for example audit firms, credit rating agencies, etc.). The key tasks required of the regulators during this transitory period involves the reassessment of priorities and the redefinition of goals. It requires administrators who are able to conceptualize policy alternatives and their implications, and think operationally in systems terms. And most importantly, it requires administrators who have the intellectual honesty and self confidence required for sharing their knowledge with the public. The emphasis here is on transparency, the emphasis here is on sharing of information with the markets to improve the market mechanism. In a high technology society, the most knowledgeable administrators would be helpless without informed collaborators. The key to success is effective organization and wide sharing of knowledge in order to enable the public agency to more readily achieve the public goals with reduced probability of error, yet also enabling an informed public to challenge administrative action where the use of public authority appears to be improper or unwise.

³⁵This aspect has already been discussed in Chapter Five during the discussion on Weber's 'Theory of Bureaucracy'.

3.2. Postmodernism as a Reaction to, or Departure From Modernism:

"No one exactly agrees as to what is meant by the term, except, perhaps, that 'postmodernism' represents some kind of reaction to, or departure from 'modernism'."

Harvey (1992, pp.7)

Under this approach the 'post' of postmodernism is characterized as a contrast concept that implies a reaction to or a departure from modernism³⁶ which has been defined as "positivistic, technocentric, and rationalistic", and "the belief in linear progress, absolute truths, the rational planning of ideal social orders, and the standardization of knowledge and production."³⁷ Postmodernism is, therefore, a reaction to or a departure from this mode of thinking. It is in this context that Harvey defines postmodernism as "a mode of thought that is anti-authoritarian and iconoclastic, that insists on the authenticity of other voices, that celebrates difference, decentralization, and democratization of taste, as well as the power of imagination over materiality, has to have a radical cutting edge even when indiscriminately used."³⁸ The concept of postmodernism as a reaction to and a departure from modernism is even more conspicuous in the following quote by Eagleton³⁹:

"Post-modernism signals the death of such 'metanarratives' whose secretly terroristic function was to ground and legitimate the illusion of a 'universal' human history. We are now in the process of wakening from the nightmare of modernity, with its manipulative reason and fetish of the totality, into the laid back pluralism of the post-modern, that heterogeneous range of lifestyles and language games which has renounced the nostalgic urge to totalize and legitimate itself. ... Science and philosophy must jettison their grandiose and metaphysical claims and view themselves more modestly as just another set of narratives."

³⁶It may be noted that the term 'modernism' being used here does not refer to the end of the nineteenth century aesthetic movement that developed as a reaction to modernity. Rather it is being used here synonymously with (high) modernity. The term modernism instead of modernity is being used as a contrast concept against postmodernism.

³⁷Harvey (1992, pp.7).

³⁸Harvey (1992, pp.353).

³⁹Eagleton, T. (1987), "Awakening From Modernity", Time Literary Supplement, 20 February 1987. (Cited in Harvey, 1992, pp.9).

Postmodernism as a reaction to, or departure from modernism is also the basis of the characterization of postmodernism and postmodernists by Rosenau (1992) who describes postmodernism⁴⁰ in humanities and social sciences, as being more than another novel academic paradigm. She describes postmodernism as a radically new and different cultural movement that is leading to a broad-gauged reconceptualization of the way we experience and explain the world around us. In its most extreme formulation postmodernism is revolutionary - it goes to the core of social science and dismisses it. In its more moderate form, postmodernism encourages substantive redefinition and innovation⁴¹. Postmodernist thinking challenges the underlying assumptions of mainstream social science and its research products. It questions the epistemological assumptions, methodological conventions, knowledge claims, all versions of truth, and policy recommendations⁴². The postmodern goal according to Rosenau (1992, pp.6), is not to formulate an alternative set of assumptions but to register the impossibility of establishing any such underpinning for knowledge, to "delegitimate all master codes". Postmodernists therefore call for a reexamination of all that modernity had delegitimated, for example, the tradition, the sacred, the irrational, etc.. Postmodern social scientists, therefore, support a refocusing of what has been taken for granted, what has been neglected, regions of resistance, the forgotten, the insignificant, the borderline, the subjugated, the rejected, the marginal, the peripheral, the excluded, the silenced, the disqualified, the differed, etc., all that modern age never cared to understand⁴³.

The key problem or the crucial weaknesses with modernism, according to the postmodernists, relates to the meta-languages, the meta-theories, and the metanarratives, which tended to gloss over important differences and failed to pay attention to the important disjunctions and details⁴⁴. In this respect postmodernism has been very important in terms of acknowledging 'the multiple forms of otherness' as they emerge from the differences from subjectivity, gender and sexuality, race and class, temporal and spacial geographic locations, and dislocations⁴⁵. The idea that all groups have a

⁴⁰Rosenau (1992) uses the word post-modernism instead of postmodernism (i.e., with hyphen rather than without it), the hyphen has been dropped for matter of consistency, even during the discussion of her analysis.

⁴¹Rosenau (1992, pp.4).

⁴²Rosenau (1992, pp.3).

⁴³Rosenau (1992, pp.8).

⁴⁴Harvey (1992, pp.113).

⁴⁵This aspect of postmodernism, has however, caused fears amongst the traditional neo-conservatives especially with respect to the accommodations of the postmodernism theory regarding

right to speak for themselves, in their own voice, and have that voice accepted as authentic and legitimate is essential for the pluralistic stance of postmodernism⁴⁶. The importance of postmodernism emerges from the opening it gives to understanding the difference between different subgroups, as well as the liberatory potential that it offers for a whole host of new social movement. ‘Pluralism’ is, therefore, one of the most important features of postmodernism, which itself may be characterized as a reaction to, or departure from the universalization and standardization of modernism.

The pluralism acknowledged in postmodern philosophy is not only pluralism across space, but across time as well. Putting it another way, it not only acknowledges that individuals and social groups may differ across space, but also that the same individuals and social groups may also differ across time⁴⁷. Hence the rationale for postmodernism’s opposition to the imposition of meta-discourses and meta-frameworks not only across space, but also across time. This can be explained in the context of the postmodernist concept of the ‘text’. In postmodernism, the concept of text is very broad. It is not simply the work of an author. The whole world of human thought and action is covered within the realm of ‘text’. According to the postmodern view, our texts and those of others are never settled. They are always in the process of development. The text we produce intersects with the text produced by others which we experience (either through talking, reading, seeing, etc.), which influences our texts in ways we cannot easily unravel. Our human mind is therefore, always reviewing and redefining our text in the context of our experience and our knowledge. Postmodernism acknowledges the dynamic nature of our text, and therefore, instead of aiming to order and control our text via a meta-discourse, postmodernism encourages us to unravel the text by trying to raise questions and making an effort to explore and understand the text.

Postmodernism can thus be viewed as a departure from modernism with regard to the perception of the problems of the present era, and the appropriate strategy required for meeting the challenge of the rapidly changing ontological conditions: whether it is appropriate to control the ontological conditions via a meta-plan, or it is more appropriate to examine and understand the change and allow flexibility for meeting the challenge of the change? This question points to the ‘becoming’ and ‘being’ conflict which is characteristic of modern and postmodern dialectic. Modernism is based on the rationale of ‘becoming’ which rationalizes the ordering and control of the ontological conditions as per the meta-framework developed by the policy makers. It ignores the

individualism, commercialism, and entrepreneurialism (postmodernism of reaction).

⁴⁶Harvey (1992, pp.48).

⁴⁷Kumar (1995, pp.107).

differences between beings and standardizes them as a homogeneous lot that can be, and also needs to be, ordered and controlled through a meta-framework that can be applied across time and space. Postmodernism on the other hand, implies an effort to understand the 'being' and respect the difference, the emphasis is on pluralism - the coexistence of different spaces. The only way that pluralism can be achieved without conflict is through improvement of the transparency of the society so that different subgroups understand and hence accept the rights of the others. Most conflicts and problems are after all, on account of ignorance which is connected to blind faith - whether it relates to traditional discourse or scientific discourse, blind faith in a discourse echoes ignorance. This is the basis of postmodernism's aversion for the global/universal meta-theories rationalized by the modernist philosophical thought as the basis for the development frameworks for ordering and control of the ontological conditions. Flexibility, pluralism, eclecticism, and transparency are therefore, not only the key characteristics of postmodernism, but also the key parameters of the postmodern strategy for meeting the challenge of the rapidly changing ontological conditions.

To understand and appreciate the concept of postmodernism as a reaction to or departure from modernism, and to appreciate its potential in encouraging a change in the way we imagine, think, plan, and rationalize, hence in the process of knowledge generation, it is necessary to examine: one, the source of inspiration and the underpinning of power of the concept of postmodernism, as a reaction to, or departure from modernism, the power that allows it to challenge the power of the meta-discourses of the modernist philosophical thought; and two, the counter-concepts that characterize the concept of postmodernism as a reaction to, or departure from the modernist philosophical thought. These are the two themes that will be examined in the remainder of this section.

3.2.1. The Source of Inspiration and the Underpinnings of the Power of the Concept:

To understand the source of inspiration of the concept of postmodernism as a reaction to or departure from modernism, and its underpinnings of power - the power that allows it to challenge the power of the truths and the meta-discourses that are constitutive of the modernist philosophical thought, it is necessary to examine: one, Foucault's genealogical analysis of knowledge; and two, Derrida's deconstructive analysis of knowledge. Both these philosophers and their philosophical enterprise can be described as the source of inspiration and the underpinnings of the power of the concept of postmodernism as a reaction to, or departure from modernism. We begin with Foucault's 'genealogical analysis of knowledge'.

(A) Foucault's Genealogical Analysis of Knowledge: In order to understand Foucault's genealogical analysis of knowledge, and the power that is concomitant with his genealogical analysis, it is necessary to understand the central idea that forms the basis of his philosophical enterprise. The discussion to follow has therefore been divided into two sections: one, a brief outline of the central idea that forms the basis of Foucault's philosophical enterprise; and two, the concept, and the basis of power of his genealogical analysis of knowledge.

The Central Idea Behind the Philosophical Enterprise of Michel Foucault: Foucault has been described as "Nietzsche's legacy operating at a deep level in the work of a major twentieth century thinker."⁴⁸ Like Nietzsche, at the heart of Foucault's philosophy is also the relationship between truth and power. However, unlike Nietzsche (1968), whose philosophy involved a fierce critique of the Western Philosophy in the context of the connection between the 'truth' and the 'will to power' of the philosopher behind the truth, Foucault's philosophy does not involve a simple critique of the connection between truth and power. Foucault approached the problem differently. He actually undertook a historical analysis of the emergence of truth-games in the arena of human sciences, and its effects in terms of the creation of the reciprocal relationship of power between the subject and the object of knowledge. This is the basis of Foucault's critique of the connection between truth and power.

Foucault describes his philosophical enterprise as a 'rupture' in the philosophical landscape that was dominated by Sartre and Marxism⁴⁹ (Florence, 1995, pp.257)⁵⁰. His endeavour, his task, from the beginning was not that of founding philosophy on a new 'cogito', nor of systemizing things previously hidden from view. Rather, it was "to interrogate that enigmatic gesture, perhaps characteristic of Western societies, by which true discourses (including philosophy) are constituted with the power we know them to have"⁵¹. Foucault places his philosophy within the 'critical tradition' of Kant. He describes his philosophical enterprise as the "critical history of thought"⁵²,

⁴⁸Said (1995, pp.264).

⁴⁹Marxism was described by Sartre as the unsurpassable philosophy of our time.

⁵⁰This biographical sketch on Foucault was actually written by Foucault under the pseudonym of Maurice Florence.

⁵¹Florence, (1995, pp.257).

⁵²Florence, (1995, pp.257).

where 'thought'⁵³ is conceptualized as "that act which poses a subject and an object in all their various possible relations", and 'critical history of thought' as "an analysis of the conditions under which certain relations of subject to object are formed or modified, to the degree that the latter⁵⁴ are constitutive of a possible knowledge (savoir)".

Foucault's philosophical enterprise can also be viewed as the history of the emergence of 'truth games'⁵⁵. The concept of 'truth games' is born out of the mutual development and the reciprocal ties between 'subjectification'⁵⁶ and 'objectification'⁵⁷, and the consequent relationship of power between the subject and the object. It is the history of the emergence of the rules according to which discourses susceptible of being called true and false are articulated on a domain of things. Foucault therefore investigates into the conditions of the emergence of these rules or truth games, and their effects on the real. Here it is important to clarify that Foucault's philosophical enterprise does not relate to all 'truth games'. His research and his philosophical enterprise primarily involved investigating into those 'truth games' in which "the subject itself is presented as the object of possible knowledge (savoir)". His area of research is limited to human sciences only, where the subject as well as the object are human beings. His research question is: "What are the processes of subjectification and objectification that permit the subject, as a subject, to become the object of knowledge (connaissance)?"⁵⁸. All of Foucault's books⁵⁹ basically ask the same question:

⁵³Here it is necessary to differentiate Foucault's interpretation of the concept of 'thought' from its more conventional interpretation as an 'idea', in which case the critical history of 'thought' would imply a critical history of ideas, which would connote a historical analysis of the errors or the misunderstandings to which these ideas are linked and upon which what we think today might depend (Florence, 1995, pp.257).

⁵⁴The object of knowledge.

⁵⁵Florence (1995, pp.258).

⁵⁶The concept of '**subjectification**' implies the question of what the subject must be, what his condition must be, what status he must have, what position he must occupy in the real or in the imaginary, in order to become a legitimate subject of any given type of understanding.

⁵⁷The concept of '**objectification**' implies the determination of the conditions under which something can become an object for a possible knowledge (connaissance), the method for problematization of the object, the methods of analysis that can be applied, and the part of itself that is considered pertinent for objectification.

⁵⁸Florence (1995, pp.258).

⁵⁹The theme of '**The Order of Things**', involved the question of analyzing the formation of certain 'human sciences', studied with reference to the practice of empirical sciences and their specific discourse in the seventeenth and eighteenth century. In this work, Foucault examined the formation of 'human sciences' in terms of the appearance of the speaking, labouring, and living subject, and its

"What are the games of truth by which man proposes to think his own nature when he perceives himself to be mad, when he conceives of himself as a living, speaking, labouring being; when he judges and punishes himself as a criminal?" And finally: "What are the games of truth by which human beings come to see themselves as desiring individuals?"⁶⁰

At the heart of Foucault's philosophical enterprise are three key methodological choices that form the basis of his genealogical research (Florence, 1995, pp.259-260):

1. A systematic scepticism about all anthropological universals. This does not mean that one should reject them all from the start, but that every aspect of our knowledge that is presented to us as having universal validity, with respect to human nature or the categories one may apply to the subject, must be tested and analyzed⁶¹. The first methodological rule for this type of research is, therefore, as follows:
 - avoid as much as possible the universals of anthropology (and those of humanism that artificially creates and maintains the rights, privileges, and nature of human beings as the immediate and timeless truth of the subject), in order to investigate their historical constitution.
2. A reversal of the philosophical approach of ascending towards the 'constituting subject' who is asked to account for every possible object of knowledge in general. Instead, to study the '**concrete practices**' through which the subject is constituted within a field of knowledge. To refuse the philosophical recourse to a constituting subject does not mean that the subject did not exist, or to making it an abstraction in the pursuit of pure objectivity. The aim of this

insertion in domains, and in the form of an understanding accorded scientific status. In '**Madness and Civilization**', '**The Birth of the Clinic**', and '**Discipline and Punish**', Foucault attempted to analyze the constitution of the subject which enabled him to appear on the other side of the normative division and become an 'object' of knowledge - as a lunatic, an invalid, a delinquent - as a result of the practices such as psychiatry, clinical medicine, and criminal science. His final project on '**History of Sexuality**', constitutes a third layer that complimented the analysis of the relations between the 'subject' and 'truth'. It involved the study of the "constitution of the subject as an object of himself: the formation of procedures by which the subject is led to observe, to analyze, to decipher, and to recognize himself as a domain of possible knowledge.". It entailed, a history of 'subjectivity', i.e., the manner in which the subject comes to know himself in a game of truth, where he has a relationship with himself (Florence, 1995, pp.258-260).

⁶⁰Foucault, Michael, (1985), "**The Use of Pleasure**", translated by Robert Hurley, Pantheon, New York, pp.6-7, (Cited in Eribon, 1995, pp. 296).

⁶¹To refuse the universals of 'insanity', 'delinquency', or 'sexuality' does not mean that these notion mean nothing, or that they are chimeras invented in support of a dubious cause. What it does mean is to **question oneself about the conditions** which permit us, according to the rules of stating truth and falsehoods to recognize the subject as a person who is mentally ill, or which allow a subject to recognize the most essential part of himself in the modalities of his sexual desires.

refusal is to make visible "the processes specific to an experience where the subject and the object are 'formed and transformed' by each other, each in relation to the other and as a function of the other."⁶²

3. From the second methodological principle emerges the third methodological principle: to address 'practices' as the domain of analysis, i.e, to take up the study in terms of **what 'we do'**: what we do with the insane, the delinquents, the ill, etc.. Thus, in order to explain what was thought about it at the time, instead of trying to deduce from the representation we have of them, or from the knowledge we believe we have of them (for example, the institutions in which they were placed in or the treatments to which they were subjected); thus, instead of investigating what was the form of true mental illness, or the modalities of real delinquency in a particular period, in order to explain what was thought about it at the time. Michael Foucault approaches these issues in a very different manner:

- he begins by studying the ensemble of ways of doing things (which are more or less methodological, more or less thought-out, more or less finalized) through which the real was given shape by those who sought to think and manage,
- and who (the latter) simultaneously constituted themselves as subjects capable of knowing, analyzing, and eventually modifying the real.

These are the 'practices' understood simultaneously as a mode of acting and thinking which provide the key of intelligibility to the correlative constitution of the subject and the object.

According to Foucault (Florence, 1995, pp.260), the importance of the analysis of relations of power becomes apparent the moment we begin to study, through these practices, the different modes of objectification of the subject. The aim of analysis of power is not a question of interrogating power about its origin, its principles, or its legitimate limits, rather the aim is that of studying the processes and techniques that are taken in different institutional contexts to operate on the behaviours of individuals taken individually or as a group:

- to shape, to direct, to modify their manner of conducting themselves;

⁶²This can be understood in the context of the discourses of mental illness, delinquency, or of sexuality. These discourses do not tell us of what the subject is, except in the context of a very particular game of truth. This does not mean that these games are imposed from outside upon the subject, according to a necessary casualty, or according to structural determinations. What these discourses and these games of truth do is to open up a field of experience where the subject and the object are constituted only under certain simultaneous conditions. This methodological principle of studying the concrete practices, on the other hand, allows us to understand how the subject and the object are constantly modified in relationship to each other, thus, how they modify the field of experience itself.

- to impose ends on their inaction or to inscribe it with global strategies (which are multiple in their form and place of exercise, and equally various in the procedures and techniques that they set into place).

These power relations characterize the way in which men are 'governed' by each other, and their analysis illustrates how the insane, the sick, or the delinquent subject is objectified through certain forms of 'governing' lunatics, the sick, criminals, etc.. The significance of such an analysis of power relates to its value in helping us understand the determining role that various and particular forms of 'government' of individuals have played in the different modes of objectification of the subject⁶³.

Having examined the central idea behind Foucault's philosophical enterprise and the methodological approach that forms the basis of his genealogical analysis, we can now examine his genealogical analysis of knowledge which forms the inspiration, and the underpinning of power of the concept of postmodernism as a reaction to, or departure from modernism.

The Concept and the Power of Foucault's Genealogical Analysis of Knowledge: The power of Foucault's discourse stems from his genealogical analysis of knowledge (savoir). Foucault approached knowledge (savoir), especially anthropological universals with a certain degree of scepticism and hostility: "knowledge as a kind of transparent mental prison". This is the opinion of Said (1995, pp.263), according to whom Foucault's archaeologies were purposely intended not to resemble sociologies of knowledge. Instead Foucault aimed to sever its connection with memory (its metaphysical and anthropological model), and to construct a counter-memory. The basis of the power of Foucault's genealogies is two fold: one, the effort he put into his archaeologies of knowledge. It involved Foucault, the archaeologist, the erudite researcher, digging up documents, raiding archives, rereading and demystifying canonical texts. He studied the origin of knowledge (savoir) itself, its formation, its organization, its mode of change and stability. He was therefore fully cognizant of its massive material presence, its complexity, and its epistemological status, up to its minutest detail; two, the sheer genius of Foucault the genealogist to apply the information revealed through his archaeological research to create a knowledge of knowledge. It involved Foucault, the genealogist, standing away from knowledge, spinning out a whole systematic apparatus so as to do to knowledge what knowledge does to its material. Knowledge is therefore taken apart and rearranged with the aim of controlling knowledge, rather than allowing it to control him. This is the basis of power of

⁶³Foucault's research question, and his methodological choices provide an avenue for researching into the power relation between the regulator and the regulated, which is after all connected to the concept of truth game involving the mutual development and the reciprocal ties between subjectification and objectification, where the regulator assumes the role of the 'subject' and the regulated (the financial institution) becomes the 'object' of examination.

Foucault's genealogical analysis of knowledge - he does to knowledge what knowledge does to its material - he takes control of knowledge, rather than allowing knowledge to control him, hence the power of his genealogical analysis of knowledge.

The Concept of Genealogy: Foucault (1980c, pp.117) refers to genealogy⁶⁴ as a form of history which can account for the constitution of knowledge, discourses, domains of objects, etc., without having to make reference to a subject which is either transcendental in relation to the field of events or runs in its empty sameness throughout the course of history.

Foucault's genealogy is an example of postmodern method in which the past is revisited to investigate and understand the present. Genealogical analysis, unlike modern history does not interpret the past through the present perspective. Genealogy is, rather, the history of the present in the sense that it finds its points of departure in problems relevant to the current issue and finds its points of arrival and its usefulness in what it can bring to the analysis of the present. The difference between Foucault's genealogy and the traditional historical research is that genealogy eschews the latter's implicit metaphysical search for origin or the primordial truth. According to Foucault (1995, pp.366) we should avoid thinking of emergence as the final term of historical development. Emergence is the entry of forces, it is their eruption, and the leap from the wings to centre stage, each in their youthful strength. Foucault's genealogy, is not a pursuit of the origin of an idea, an attempt to capture the absolute essence of things, their metaphysical essence, or the primordial truth. Genealogy does not go back in time to restore an unbroken continuity, or to demonstrate that the past actively exists in the present. Foucault (1995, pp. 365) explains the concept of genealogy, that an examination of descent of a trait or a concept allows one to understand the myriad events through which - thanks to which, against which - they were formed. Genealogy follows the complex course of descent with the aim of identifying and outlining the "accidents, the minute deviations - or conversely, the complete reversals - the errors, the false appraisals, and the faulty calculations that

⁶⁴In order to understand and appreciate the concept of 'genealogy', it is necessary to understand the difference between 'archaeology' and 'genealogy'. 'Archaeology' is the method that Foucault applies for revealing the historical contents of the emergence and the evolution of the knowledge and the discourses and institutions connected to that knowledge that dominates our present. 'Genealogy' on the other hand would be the application or the tactics by which the information revealed through the archaeological research is brought into play to create a knowledge of knowledge (Foucault, 1980b, pp.85). Foucault's research, therefore, involves two acts: one, Foucault, the 'archaeologist', the erudite researcher, digging up documents, raiding archives, rereading and demystifying canonical texts; and two, Foucault the 'genealogist' applying the information/knowledge revealed through his archaeologies to create a knowledge of knowledge. Since the concept of 'archaeology' is necessary to consummate the concept of 'genealogy', Foucault therefore employs 'genealogy' as a holistic concept that presumes archaeology as its necessary component.

gave birth to those things that continue to exist and have value to us; it is to discover that truth or being do not lie at the root of what we know and what we are, but the exteriority of accidents. This is undoubtedly why every origin of morality from the moment it stops being pious - and *Herkunft*⁶⁵ can never be - has value as a critique. ... The search for descent is not the erecting of foundations: on the contrary, it disturbs what was previously considered immobile; it fragments what was thought unified; it shows the heterogeneity of what was imagined consistent with itself."⁶⁶

Genealogy necessitates the removal of every mask to ultimately disclose an original identity which may be different from its image of primordial truth. In this respect Foucault (1995, pp.363) explains "if the genealogist refuses to extend his fate in metaphysics, if he listens to history, he finds that there is 'something altogether different' behind things: not a timeless and essential secret, but the secret that they have no essence or that their essence was fabricated in a piecemeal fashion from alien forms." In this respect he gives the example of the history of 'reason', that there was no primordial truth behind its emergence, rather it was born out of chance. The devotion to truth and the precision of scientific methods arose from "the passion of the scholars, their reciprocal hatred, their fanatical and unending discussions, and their spirit of competition - the personal conflicts that slowly forged the weapons of reason". The genealogical analysis of modernity therefore concentrates on the basis of the genesis or the emergence of the principles of modernity, and how they were thereafter given a metaphysical or an ideological status, as a result of which they became a liability rather than an asset. It was the output of such research by Foucault and his fellow scholars labelled as postmodernists which put a question mark on the validity of the metanarratives that form the basis of the modernist philosophical thought. Having examined the concept of 'genealogy' we can now examine the strategic application of genealogical analysis to control the power of discourses that are elevated to the status of truth.

The Power of Genealogical Analysis: The power of Foucault's discourse is concomitant with his line of attack and the basic strategy of his genealogical analysis. Foucault's line of attack is specifically towards: global, totalitarian, universal theories that claim the status of science and command the power that is embodied in scientific discourses. His genealogical strategy is: 'insurrection of subjugated knowledge'⁶⁷. The outcome of his genealogical analysis is: a certain fragility has been discovered in the very bedrock of existence (i.e. increasing vulnerability of the

⁶⁵German equivalent of the term 'origin'.

⁶⁶Foucault, (1995, pp.365).

⁶⁷Foucault (1980b, pp.80).

instability has been the discovery of "something that perhaps was not initially foreseen, something that one might describe as precisely the inhibiting effect of global, totalitarian theories."⁶⁸ In other words it is not that these global theories have not provided nor continue to provide in a fairly consistent fashion useful tools for local research, the negative aspects of these global, totalitarian theories which has been discovered in light of the recent criticism has been "the attempt to think in terms of a totality has in fact proved a hindrance to research."⁶⁹ In other words, totalitarian theories become mental prison, and hence impede the process of knowledge generation.

To appreciate the significance of genealogy, it is necessary to understand the concept of 'insurrection of subjugated knowledge'. According to Foucault (1980b, pp.81-82), there are two categories of subjugated knowledge whose emergence forms the basis of the 'insurrection of subjugated knowledge': **one**, the **historical contents** that have been buried and disguised in 'functional coherence' or 'formal systemization'⁷⁰. This is because the historical contents allow us to rediscover the ruptured effects of conflicts and struggles that are masked by the functionalist or systemizing thought. **Two**, the knowledge that has been **disqualified** as being inadequate to their task. This is knowledge located low down in the hierarchy, beneath the required level of cognition and scientificity⁷¹. It is the force of the critical discourse created by the association of the two categories of subjugated knowledge that forms the basis of the fragility created in the universal and scientific theories.

The significance of Foucault's genealogical analysis relates to the theme of this knowledge: 'the historical knowledge of struggles', or the memory of hostile encounters which even up to this day have been confined to the margins of knowledge (Foucault, 1980b, pp.83). It is the output of such researches involving "the painstaking rediscovery of struggles together with the rude memory of their conflicts" which Foucault (1980b, pp.83) refers to as genealogy or rather genealogical

⁶⁸Foucault (1980b, pp.80).

⁶⁹Foucault (1980b, pp.81).

⁷⁰The reference to the subjugated knowledge here implies those blocks of historical knowledge which were present, but disguised within the body of functionalist and systemizing theory. It is this emergence of the historical contents of the emergence and the development of the asylum system or the prison system (rather than the semiology of the life of the asylum, or the sociology of the delinquency) that forms the basis of Foucault's criticism.

⁷¹Foucault refers to this knowledge as the 'popular knowledge'. This is local, regional, differential knowledge which is incapable of unanimity. And which owes its force only to the harshness with which it is opposed (by the legitimate/global knowledge). It is through the reappearance of these popular/disqualified knowledge that the criticism performs its work.

researches. And these genealogies would not have been possible or even attempted, had it not been for the tyranny of globalizing discourses and their hierarchy. Foucault (1980b, pp.83) defines the concept of 'genealogy' as "the union of erudite knowledge⁷² and local memories⁷³ which allows us to establish a historical knowledge of struggles and to make use of this knowledge tactically today."

What genealogy really does is to entertain the claims to local, discontinuous, disqualified, and illegitimate knowledge, as against the claims of a unitary body of theory which filters, hierarchies, and orders knowledge in the name of some true knowledge and some arbitrary idea of what constitutes a science and its objets. Genealogy, according to Foucault, can therefore be described as 'anti-sciences'. This does not imply that genealogy is an attempt to rationalize the right to ignorance or non-knowledge. Genealogy does not deny knowledge. This, according to Foucault (1980b, pp.84) is not the concern of genealogy. The concern of genealogy primarily relates, not to the contents, methods or concepts of science, but to "the effects of the centralizing powers which are linked to the institution and functioning of an organized scientific discourse within a society such as ours". In this respect, Foucault gives the example of Marxism, which is also referred to as 'scientific socialism', which is a consequence of attempts by political scientists to confer Marxism with the status of a scientific political system. According to Foucault (1980b, pp.84-85), the problem is not whether Marxism (or psychoanalysis) is science or not. The problem lies in the rationale or the determination to make a science out of Marxism (or psychoanalysis) or any other study/theory. The problem lies with the aspiration that is presumed to accompany a statement or knowledge deemed to be scientific. The problem lies in the very question: "is it science?", which connotes the aim of disqualifying knowledge that is not deemed to be scientific. When one tries to or aspires to establish a political discourse like Marxism as scientific, the aim is not to demonstrate that Marxism has a rational structure and that, therefore, its propositions are the outcome of verifiable procedures. The aim is primarily two fold: **one**, to isolate it from the discontinuous forms of knowledge that circulate about it (criticisms and other political discourses not considered to be scientific); **two**, to invest the Marxist discourses and those who uphold them with the effects of power which the West (since medieval times) has attributed to science and those engaged in scientific discourse.

The concern of genealogy or rather the struggle of genealogy is against the effects of the power of a discourse that is considered to be scientific. According to Foucault (1980b, pp.85), "in contrast to the various projects which aim to inscribe knowledge in the hierachial order of power

⁷²'Erudite knowledge' refers to the historical contents related to the emergence and development of knowledge and institutions (of science).

⁷³'Local knowledge' refers to the popular knowledge which is considered as disqualified knowledge by science and scientific institution.

associated with science, a genealogy should be seen as a kind of attempt to emancipate historical knowledge from that subjection, to render them, that is, capable of opposition and of struggle against the coercion of a theoretical, unitary, formal and scientific discourse". The aim and hence the power that genealogical discourses acquire, relates to their ability to neutralize the power and the effects intrinsic to the power of the scientific discourse that is connected to the hierarchicalization of knowledge and the subjugation of local disqualified knowledge, and the historical contents of its own emergence and evolution.

Genealogy, thus, by reactivating the subjugated knowledge allows us the power to reevaluate, revise, enrich and improve the scientific knowledge which is now made to appear without its metaphysical garb and without the power that is concomitant with it. It allows us to approach and view scientific knowledge and universal discourses from a different angle. It allows us to release ourselves and our intellect from the mental prison which knowledge based on universal and global discourses represent, and to take control of the knowledge rather than allowing knowledge to take control of our intellect.

(B) Derrida's Deconstructive Analysis of Knowledge: As in the case with Foucault, there is also a connection between Nietzsche and Derrida. Derrida's reading of Nietzsche⁷⁴ is that of the first philosopher to knowingly unwrite or deconstruct the history of metaphysics⁷⁵. According to Norris (1991, pp.77), for Nietzsche, as for Derrida, the project of absolute knowledge was deluded at source by how language creates and capriciously misleads the process of thought. Philosophy has based itself unwittingly on a series of buried metaphors.

⁷⁴According to Norris (1991, pp.56-57), the importance of Nietzsche lies in his critique of western philosophy and its presuppositions which has had an effect on the theory and practice of deconstruction. What Nietzsche provides is a style of philosophic writings which remains intensely sceptical of all claims to truth - its own included - and thus opens up the possibility of liberating thought from the age-old conceptual limits. Nietzsche argued that philosophers were self condemned dupes (cheats) of truth who preserved it simply by effacing the metaphors or figurative discourse which brought it into being. Only by suppressing its origin in metaphor, had philosophy from Plato to the present, maintained the sway of a tyrannizing reason which in effect denied any dealing with figurative language. Reason had crushed out the imaginative life out of philosophy. Truth he concludes is a mobile marching army of metaphors, metonymies, and anthropomorphisms. Truths are illusions of which one has forgotten that they are illusions. Thus for Nietzsche, this insight led to the conclusion that all philosophies, whatever their claim to logic or reason, rested on a shifting texture of figurative language, the signs of which were systematically repressed under the sovereign order of truth.

⁷⁵Norris (1992, pp.73).

- The fundamental ‘laws’ of Aristotelian logic are held to be expressions of our inability to think beyond them, rather than possessing an absolute validity.
- Logic is the product of a will to understand which selectively arranges the habits of thought so as to make some sense of immediate experience.
- Concepts are formed on the groundless supposition that our knowledge of objects in the world comes directly from our experience of what it is to perceive them.
- The link between empirical self-evidence and conceptual truths, is a product of metaphorical displacement, raising the contingent into the necessary by a constant (though unrecognized) leverage of tropes⁷⁶.

According to Norris (1991, pp.59), Derrida follows the Nietzschean lead in his break from the self-accrediting notion of scientific methods and their validity. He criticizes ‘Science’ as a discourse linked to the repressive ideology of reason, which in turn took rise from the Greek equation between truth and logic. The significance of Derrida’s philosophy is that Derrida refuses to grant the philosophers the privileged status (a status they have always claimed) as the sovereign dispenser of reason. Derrida confronts the ‘will to power’ of the philosophers by deconstructing their texts. He argues that philosophers have been able to impose their various systems of thought only by ignoring or suppressing the disruptive effects of language. Derrida therefore picks out these effects by skilfully unpicking the elements of metaphor and other figurative devices at work in the philosophical texts⁷⁷. Derrida’s deconstruction acts as a liberating force in the sense that it allows one to take cognizance of the rhetorical nature of the philosophical arguments. It allows one to interrogate the rhetoric of closure, and lay out the problems that have merely been repressed or displaced rather than resolved⁷⁸.

Deconstruction suspends all that we take for granted about language, experience, and the ‘normal’ possibilities of human communication⁷⁹. It is very much the antithesis of Saussure’s structuralist’s theory which aims to search for the invariant and universal structures which provide a legitimate framework or a kind of regulative matrix for guiding one’s perceptions and analysis⁸⁰.

⁷⁶‘Trope’ refers to the figurative use of a word. There are categories of tropes: metaphor, metonymy, synecdoche, and irony.

⁷⁷Norris (1991, pp.18-19).

⁷⁸Norris (1992, pp.21).

⁷⁹Norris (1992, pp.xi).

⁸⁰The structuralist argument is that knowledge of the world is inextricably shaped and conditioned by the language that serves to represent it. Meaning, according to Saussure, are bound up in a system

Theory is rationalized on the basis of the presumption of ‘a deep, universal kinship’ between the method and the systems of meanings that it proposes to analyze. Deconstruction, on the other hand, starts out by rigorously suspending the structuralist’s assumed correspondence between mind, meaning, and the concept of method which claims to unite them⁸¹. According to Derrida, by repressing the problems which his own theory of language all but brought to view, Saussure, transcended the expressed limitations of his theory. For Derrida, there is a fundamental blindness in Saussurian text, a failure to think through the problems engendered by its own mode of discourse: the idea of the language as a signifying system which exceeds all the bounds of individual ‘presence’ and speech⁸². Derrida’s strategy is to pick out such loaded metaphors and show that they work to support a whole powerful structure of presumptions. In a way Derrida’s deconstruction can be considered as a practical application of Barthes’s criticism of the structuralist perspective, that the dream of total intelligibility, like ‘structure’ in its metalinguistic sense, belongs to a stage of thinking that is self-blinded by its own conceptual metaphors⁸³. An excellent example of this is Derrida’s criticism of Marx’s ‘dialectical materialism’⁸⁴, which itself is based on certain structuralist ideas. According to Derrida the language of dialectical materialism is shot through with metaphors disguised as concepts, themes that carry along with them a whole unrecognized baggage of presuppositions⁸⁵. By picking out the loaded metaphors and the presupposition in Marxist text, Derrida allows us to understand and appreciate the rhetorical nature of Marxist Philosophy of ‘Dialectical Materialism’.

According to Derrida, deconstruction is not a question of rejecting the text or deny its historical significance, rather, it is a matter of driving it to its ultimate conclusions, and seeing where

of relationship and difference that effectively determines our habits of thought and perception. Interpretation is a quest for order and intelligibility among the manifold patterns of sense which the text holds out to fit a reader. The role of the structuralist philosophy is to explain how these powerful conventions come into play, and to draw a line between interpretation based on ingenuity, and that based on proper, legitimate or competent readerly response (Norris. 1991, pp.4-5).

⁸¹Norris (1992, pp.2-3).

⁸²Norris (1992, pp.27).

⁸³Norris (1991, pp.7).

⁸⁴The philosophy of Karl Marx. The view of history as a conflict between opposing forces: thesis and anti-thesis which can be resolved by a new force: synthesis. He viewed the present conditions as class struggle between capitalists whose aim is private profit and the proletariat who resists exploitation.

⁸⁵Norris (1991, pp.75).

these conclusions work to challenge its conventional conclusions⁸⁶. In this sense it would be wrong to classify deconstruction as post-structuralist (i.e., in the sense of trying to displace and invalidate the structuralist project), because after all, if it was not for the tensions between the 'practice' and 'promise' exemplified in the structuralist thought, Derrida would hardly have initiated the questions that animate his writings. Deconstruction is a constant and vigilant reminder of what structuralist must be if it is to avoid the traps laid out by its seductive concept of methods⁸⁷.

The following excerpt from Derrida's interview allows us to understand and appreciate the concept, and hence the contribution of Derrida's deconstruction to our intellectual heritage:

To deconstruct is a structuralist and anti-structuralist gesture at the same time: an edification, an artifact is taken apart in order to make the structure, the nerves, or as you say the skeleton appear, but also, simultaneously, the ruinous precariousness of a formal structure that explained nothing, since it is neither a centre, a principle, a force, nor even the law of events, in the most general sense of this word.

Deconstruction as such is reducible to neither a method nor an analysis (the reduction to simple elements); it goes beyond critical decision itself. That is why it is not negative even though it has often been interpreted as such despite all sorts of warnings.⁸⁸

From the above discussion, it is obvious that Derrida's philosophy is very different from that of Michel Foucault. He attacks the metanarratives internally with the aim of outlining the problematical nature of the metaphysical concepts embedded within the text. As Derrida (1997, pp.9) explains with respect to his readings of Plato, Aristotle, and others, that deconstruction is "an analysis which tries to find out how their thinking works or does not work, to find the tensions, the contradictions, the heterogeneity within their own corpus". Deconstruction is not some method or tool that you apply on something from outside. Deconstruction is something that happens, and happens inside. There is deconstruction at work in the work/text itself, Derrida's aim is only to open up the closures to make this apparent. Derrida applies the same tools of reason as that applied in the development of the concepts and theories, to overturn and outline their problematical nature, and hence the incredulity towards metanarratives. He opens up the closures of the metaphysical theories, and leaves them in suspended animation, thus calling into question the status of the metaphysical theories as statements of truth. Because he applies the same tools as those applied in the development of the metanarratives, his text is therefore considered to be very abstruse and takes a lot of effort to understand and

⁸⁶Norris (1992, pp.30).

⁸⁷Norris (1991, pp.54).

⁸⁸Derrida (1995a, pp.83).

appreciate, and has therefore been summarily dismissed by many, and criticized by others as being negative rather than positive in its contribution. His text has also been compared to computer virus that destroys intellectual output, and disciplines⁸⁹, which is rather unfortunate, because through his method of deconstruction Derrida makes a significant positive contribution to our knowledge. By laying out the problematical features of our knowledge which we assume as truth, he helps in opening the gateway for the generation of new knowledge. This is echoed in Derrida's answer to his critics: "I try to dismantle not institutions but some structures in given institutions which are too rigid or dogmatic or which work as an obstacle to future research".

What is called "deconstruction" is concerned with (theoretically) and takes part in (practically) a profound historical transformation (techno-scientific, political, socio-economic, demographic) which affects the canons, our relation to language and to translation, the frontiers between literature, literary theory, philosophy, the "hard" sciences, psychoanalysis and politics and so on. Deconstruction therefore finds itself at the heart of what you call "tensions". It is a question of assuming these tensions, of "living" them as much as of "understanding" them. Those who fear and wish to deny the inescapable necessity of these transformations try to see in deconstruction the agent responsible for these changes, when in my eye it is above all else a question of trying to understand them, of interpreting them, so as to respond to them in the most responsible fashion possible.⁹⁰

This is the contribution of Derrida to the concept of postmodernism as a reaction to or departure from modernism, and this is also the basis of the underpinnings of the power of the concept of postmodernism as a reaction to, or departure from modernism - power that allows it to challenge and react to the truths and meta-discourses of the modernist philosophical thought.

Having examined the philosophical enterprise of Michel Foucault and Jacques Derrida which forms not only the source of inspiration, but also the underpinning of the power of the concept of postmodernism as a reaction to, or departure from modernism, we can now examine some of the counter-concepts that characterize this concept.

3.2.2. Counter-Concepts that Characterize the Concept⁹¹:

⁸⁹Derrida (1995b, pp.406).

⁹⁰Derrida (1995b, pp.413).

⁹¹The concept of postmodernism as a reaction to, or departure from modernism.

As apparent from the title, this approach to the concept of postmodernism involves an examination of the counter-concepts that represent a reaction to, or departure from modernism (or modernity) which has been defined as rationalistic, technocentric, and positivist, and the belief in the existence of, and hence the rationale for the search for the truth, and the imposition of a meta-framework (the truth) for the ordering and control of the ontological conditions. Postmodernism represents a departure in our way of thinking of what could/should be done to face the problems of the present era. The source of inspiration, and the underpinnings of the power of this reaction against modernist philosophical thought was the subject of discussion of the previous section which involved an examination of the basis of the power that is concomitant with the philosophy of Foucault and Derrida. Here we examine some of the counter-concepts that characterize the concept of postmodernism as a reaction to, or departure from modernism. The investigation covers eight key areas of our ontological assumptions that form the basis of our thinking. Investigation into the counter-concepts is aimed as understanding how postmodernism represents a departure in our way of thinking regarding the best strategy for confronting the problems of the new epoch - the postmodern epoch. The key text that forms the basis of this section is Rosenau (1992): "Post-Modernism and the Social Sciences: Insights, Inroads, and Intrusions". The discussion to follow covers the following eight areas of our knowledge base:

- A. The Problematic of Disciplinary Research.
- B. The Concept of Representation.
- C. The Concept and the Relationship Between the Author, the Text and the Reader.
- D. The Concept of Subject.
- E. The Concept of Truth.
- F. The Concept of Theory.
- G. The Concept of History.
- H. The Concept of Space.

(A) The Problematic of Disciplinary Research: There are two facets of the problematic of disciplinary research that are questioned by the postmodernist: one, the politics of disciplinary research, and two, the rigid differentiation between disciplinary boundaries.

i. The Politics of Disciplinary Research: The politics of disciplinary research is the area of investigation in Foucault's (1972) "The Discourse on Language", in which he explains the concept of disciplines, that "disciplines are defined by groups of objects, methods, and their corpus of propositions considered to be true, the interplay of rules and definitions, of techniques and tools: all

these constitute a sort of anonymous system, freely available to whoever wishes, or whoever is able to make use of them, without there being any question of their meaning or their validity being derived from who ever happened to invent them.⁹² To put it in simple words, disciplines outlines the requirements for the construction of new statements. In order to belong to a discipline, a proposition is required to fit into a certain type of theoretical field. In other words a proposition is required to fulfil some onerous and complicated conditions before it can be admitted within a discipline; even before it can be pronounced true or false, it has to be ‘within the true’. One would only be ‘within the true’ if one obeyed the rules of some discursive ‘policy’ which would have to be ‘reactivated each time one spoke’⁹³. Putting it another way, disciplines constitute a system of control in the production of discourse, fixing its limits through the action of an identity taking the form of permanent reactivation of rules. Although there may be certain advantages of such disciplinary controls in terms of providing order and certainty in the research process and a basis for the career development of the researcher, which is manifested in the huge output of knowledge generated within the confines of different disciplinary groups, at the same time however, there are negative implications of such restrictive controls: it repulses a whole teratology⁹⁴ of learning⁹⁵. Disciplines and methodologies including those upon which social and economic research is based thus become discourses of power which classify, process, and position people. Foucault (1980c, pp.133) therefore identifies the key problem in producing the truth as not being the truth itself or the ideological contents linked to the truth, but rather the fundamental problem relates to the politics of truth (i.e. the political, economic, and the institutional regime for the production of truth). This is what the postmodern question is all about. By laying out the problematical features of disciplinary research, postmodernism allows the researcher the power and the confidence to react against, and as a consequence, go beyond the constricting requirements of disciplinary research in the production of knowledge.

ii. The Problem of Rigid Differentiation Between Disciplinary Boundaries: One of the most conspicuous feature of postmodernism is its eclecticism and the de-differentiation of the rigid

⁹²Foucault (1972, pp,222).

⁹³Foucault (1972, pp. 224).

⁹⁴The reference here is to the local narratives and other knowledge that are considered to be de-legitimated knowledge because they cannot confirm to the requirements of scientific discourses.

⁹⁵Foucault (1972, pp. 223).

disciplinary boundaries. According to Rosenau (1992, pp.6-7), postmodernists question and therefore call for a de-differentiation of the rigid disciplinary boundaries between:

- natural sciences, humanities, social sciences, art and literature,
- between culture and life, fiction and theory, image and reality in nearly every field of human endeavour.

Rosenau (1992, pp.13) therefore describes postmodernism as the merging of the elements (not all) from a number of different, often conflicting orientations, including structuralism, romanticism, phenomenology, nihilism, populism, existentialism, hermeneutics, Marxism, critical theory, and anarchism. Postmodernists agree with some elements of these philosophical ideologies, while at the same time they disagree with some other elements of the same ideologies especially those which form the logocentric elements⁹⁶ of these theories⁹⁷. One of the most conspicuous features of modernism has been the development of a number of distinct disciplines and areas of specialization. Postmodernism reacts against this predilection of modernity through the process of de-differentiation, postmodernism thus allows new knowledge generation through the process of cross fertilization or hybridization between different disciplines and specializations, and hence encourages a more holistic approach to knowledge generation.

(B) Representation: Postmodern critique of the modernist concept of 'representation'⁹⁸ is a very important facet of the concept of postmodernism as a reaction to or departure from modernism. Representation assumes that there is something out there that is true or valid that has to be

⁹⁶Logocentrism refers to propositions that claim legitimacy by reference to some a priori concept.

⁹⁷For example: they agree with Marxists criticism of modern science as being a myth and enlightenment heritage as being totalitarian and dominating, but at the same time they criticize the Marxist project of emancipation itself as being logocentric in terms of its emphasis on the societal totality at the expense of le-quotidien (analysis of local or daily life). Similarly they agree with the critical theory which urges a suspicion of instrumental reason, modern technology, and the role of the media in a modern consumer society, but at the same time they question critical theory's emphasis on extra-textual explanations of social phenomenon and their search for truth as 'naive'. Paralleling anarchism, postmodernists question authority and the arbitrary impositions of any singular, systemic, point of view. They tolerate different, even contradictory perspectives. From Romanticism, the postmodernist inherit a critical stand vis.a.vis the objective, all that is supposedly permanent, and the unity of time and place. In agreement to the Romanticists, postmodernists question the dominant aesthetic values, that there are no universal criteria of beauty, goodness, and truth. The postmodernists, much like the Romanticists feel they live in a twilight world of transition between an unsatisfactory present and an unworkable past, a world in which the conventional social maps are no longer effective, but at a point of time when new ones have yet to be constructed (Rosenau, 1992, pp.13-14).

⁹⁸The following examination of postmodern view vis.a.vis 'representation' is based on Rosenau (1992, Chapter 6, pp.92-108).

communicated via ‘representation’. Representation also assumes a clear distinction between presence and absence. Representation is the practice of taking one thing for another. It assumes the identity of a concept with some undefinable unspoken presence. For example the representation of citizens through the elected members of parliament secures the presence of the people in their absence. Similarly theory tries to represent reality in a narrative form. Representation assumes the ability to reproduce and duplicate external reality⁹⁹. Representation also assumes the referential status of words, images, meanings, and symbols. It assumes that each constitutes a fixed system of meaning and that everybody understands them in more or less the same way. Representation is epistemologically objectionable to the postmodernists because it assumes the ability to reproduce and duplicate external reality. For the postmodernists representation is problematical because the assumptions on which it is based are themselves problematical. The key goal of deconstruction is to lay out the deficiencies in the representational claims of the modernists and their theories. This is also the contribution of Derrida. By laying out the deficiencies in the representational claims of the modernist philosophers and social scientists, Derrida releases us from the mental prison based on the a priori truths of representation.

(C) Relationship Between the Author, the Text and the Reader: The reorientation in the power and the relationship between the author, the text, and the reader¹⁰⁰ is one of the more distinctive features of the concept of postmodernism as a reaction to or departure from modernism. The author loses his control on the text, which takes on a life of its own, independent of the author. Instead of the author, the reader takes on the centre stage and assumes an unprecedented autonomy in extracting meaning from the text. This is the reason that postmodern text is referred to as ‘writely’ rather than ‘readerly’ text, implying that the reader rewrites the text in the process of interpreting the text. The basis of this rationale is discussed below:

Author: A modernist author is defined more broadly than just a writer. He is assumed to have privileged access to truth, reason, and scientific knowledge. He is looked upon as a legislator having the attributes of a specialist, a manager, a professional, an intellectual, or an educator. He is considered as an agent who creates a situation or is responsible for a larger play of events and a

⁹⁹The subject as researcher seeks to represent the object of inquiry. Representation assumes that an individual’s information processing procedures can in fact represent external reality. It assumes objectivity, where as an external object of nature is conveyed to the subject through the agency of ‘sense’. The implication being that representation depends upon the accuracy and correctness of the subject’s judgement, which implies subjectivity.

¹⁰⁰The following examination of postmodern view vis.a.vis the relationship between the author, the text, and the reader is based on Rosenau (1992, Chapter 2, pp.25-41).

specific social outcome. The postmodernists, especially the sceptical¹⁰¹ ones consider the concept of modern author to be analogous to that of hegemony¹⁰² in international relations, and therefore, try to correct the situation by sharing the power of the author with those being studied (the object), and at the time leaving everything to a more active reader.

Text: In postmodernism, the concept of text is very broad. It is not simply the work of an author. The whole world of human thought and action is covered within the realm of 'text'. Everything is a text including a life experience, a war, a revolution, a political rally and election, a personal relationship, a vacation, etc.. Postmodernists argue that every text is related to every other text. This phenomenon is known as intertextuality. In other words effects radiate out from a text and have an impact on all other text. Postmodernism therefore stresses on the importance of the reader in the process of reading and interpreting the text. Postmodern text, is therefore a plural text, i.e., more than one interpretation of the text is possible. The reader takes control of the text, hence the term 'writely text' - it is rewritten by the reader during his/her reading/encounter of/with the text. This is because it involves an intertextual encounter between the text of the reader¹⁰³ and the text being examined. The result of the encounter will be the reinterpretation of the text by the reader in the context of his/her own ontological assumptions, which may be different from that of the author. This intertextual encounter may (or may not) create a change in the reader's ontological assumptions, and as a consequence, may (or may not) create a change in the orientation and thinking of the reader. That is why postmodernists argue that in examining a text, we should not focus exclusively on what the text says, but also on what it fails to say and what it suggests by innuendo. This is the opposite of the modernist concept of text which assumes a passive reader, and hence is referred to as 'readerly text'.

¹⁰¹Rosenau classifies postmodernists into two classes: the sceptical postmodernists and the affirmative postmodernists. The definition of the two classes of postmodernists have been outlined in footnotes 20 and 21, on page.149.

¹⁰²Hegemony is "an ensemble of normalized knowledge practices, identified with a particular state and domestic society ... that is regarded as a practical paradigm of sovereign political subjectivity and construct". Its functions are to set the standards, designate by opposition what is abnormal, fashion the political agenda, establish 'ritual practices of enframing', without ever manifestly accomplishing any of these.

Ashley, Richard, (1989), **"Imposing International Purpose: Note on a Problematic of Governance"**, in Ernst-Otto Czempiel and James N. Rosenau (eds.), "Global Changes and Theoretical Challenges: Approaches to World Politics for the 1990s", Lexington Books, Massachusetts (Cited in Rosenau, 1992, pp.30).

¹⁰³The text of the reader consists of his/her experience and knowledge base which also forms the basis of his/her ontological assumptions.

Reader: Reader is the third element of the author-text-reader triad. Unlike modern text which implies a passive posture for the reader who is required to reconstruct the authors ideas, attitudes, and aims, in order to construct the meaning of the text (as intended by the author), the postmodern reader, on the other hand, is an active reader who assumes control of the text and reinterprets it (the text) in the act of reading. However, a possible qualification for the postmodern way of thinking is that the readers do not have absolute freedom in their readings - they are guided by professional communities. In other words the reader re-creates the text but within the context of what he has learned from an interpretative community.

By reacting against the hegemony of the author, and in the process reorienting the power and the relationship between the author, the text, and the reader, postmodernism encourages a much wider intellectual development. The broadening of the concept of text, and the transformation of the reader from passive to active, can also be interpreted as a realization of the increased level of literacy, especially in the West, and hence the confidence in the quality of intellect of the society to take its own decisions rather than having them imposed by others. It is also a reflection of the increased pace of the change of ontological conditions and the crisis of confidence in the author as the dispenser of 'truth'. This facet comes to prominence in the postmodernism critique and its reaction to the modernist concept of 'subject'.

(D) Subject: The difference between the modernist and the postmodernist concept of 'subject'¹⁰⁴ is a very important facet of postmodernism's reaction to modernism. Modernist concept of the 'subject' is similar to that of the modernist author. Postmodernists consider it as an invention of modernity, a child of the enlightenment process and rationalism. As modern science replaced revelation as the source of knowledge, the 'rational individual' was implanted to take the place of 'God'. Postmodernists criticize the modernist assumption of subject as being at the centre as sovereign - as an individual possessing the power of intuition to apprehend both internal and external reality¹⁰⁵. They criticize the subject for seizing power, for attributing meaning, and for dominating and oppressing. They question the value of a unified coherent subject such as human being, as a concrete reference point¹⁰⁶. They also criticize the modernist concept of the subject because it forms

¹⁰⁴The following examination of postmodern view vis.a.vis the 'subject' is based on Rosenau (1992, Chapter 3, pp.42-61).

¹⁰⁵Rosenau (1992, pp.46-47).

¹⁰⁶Rosenau (1992, pp.42-43).

the basis of the subject-object dichotomy¹⁰⁷. This subject-object dichotomy also implies a relation of power between the subject and object with the subject as the active entity taking decisions on behalf of the objects. Such arbitrary appropriation of power for the subject (the hierarchical relation of power between the subject and the object) is rationalized on the assumption of the subject as the 'rational individual'¹⁰⁸. Postmodernists consider the status of the 'subject' problematical, not only because the assumption of the subject being rational and having the intuition and the intellect to take the best decision on behalf of the others is questionable, but also because the subject can be a source of deliberate misinformation and manipulation¹⁰⁹.

The postmodernists, especially the sceptical ones, therefore react against the hegemony of the 'modern subject' by replacing him/her with the 'postmodern individual' who is conceptualized as an active human being constituting his/her own social reality, pursuing a personal quest for meaning but making no truth claims. The postmodern individual emphasizes choice, free expression, individual participation, private autonomy, and personnel liberation, without any need for universalistic claims and ideological consistency. S/he is non judgemental rather than dogmatic, and relinquishes the need to base attitudes or actions on reason or to lay claims on truth. The postmodern individual calls for an end to certitude, reasoned argument, modern rationality, objective modern science, law grounded on jurisprudence and art subject to evaluation on the basis of standard criteria¹¹⁰. Unlike their more sceptical counterparts, the affirmative postmodernists take a more lenient view of the subject. Instead of destruction, they call for a repositioning of the subject as a de-centred subject unrecognizable by the modernist, empiricist, and positivist - a subject who is focused not on the great men of history, but rather on the daily life at the margins. A subject who struggles for autonomy and seeks to construct a new identity by appealing to life, personal freedom and creativity¹¹¹. The postmodernist rejection of the modernist concept of subject, and his/her replacement by the postmodern individual or the repositioning of the subject by a de-centred subject,

¹⁰⁷In the context of social science research, this implies that the subject as the observer becoming the centre of power, while those being studied being relegated to the status of an object or a thing (Rosenau, 1992, pp.49-50).

¹⁰⁸A person who respects rational rules, the general will, the social conventions, and fix standards that seem fair (Rosenau, 1992, pp.43-44).

¹⁰⁹This is very much apparent in the field of politics where ideology and symbolism becomes a tool for manipulating the masses (the objects).

¹¹⁰Rosenau (1992, pp.53-56).

¹¹¹Rosenau (1992, pp.57-60).

is not only a realization of the reality of our present ontological conditions, but also a reflection of the pluralistic attitude of the postmodern philosophical thought.

(E) Truth: The concept of ‘truth’¹¹² is another important facet of postmodernism’s reaction to modernism. There are two aspects of the modern concept of ‘truth’ that are worth discussing: one, the accuracy and hence the legitimacy of truth; and two, the connection between truth and power. The basis for producing knowledge in the modernist philosophical thought is ‘truth claim’, and the assumption that truth is essential¹¹³. Almost all postmodernists reject ‘truth’ even as a goal or ideal because it is the very epitome of modernity. They reject universal truths and dismiss the idea that truth is out there waiting to be discovered. Truth makes reference to order, rules and values, and depends on logic, rationality, and reason, all of which are attributes questioned by the postmodernists. Postmodernists question the value of truth, because they think that it is impossible to evaluate the adequacy of ‘knowledge claims’ with certainty. All criteria for distinguishing between truth and falsehood requires the choice between categories. It is based on a hierarchy of values, that designates some as good and others as bad, which itself is arbitrary, and hence the arbitrariness of truth. The rejection of truth is also in line with the postmodernist views on representation. Representation assumes the possibility of a true image being reproduced and represented. This according to the postmodernists is impossible, truth to the extent that it tries to represent reality is therefore fraudulent. This is also in line with the postmodernists view of language as an artificial sign system. Meaning can therefore never be communicated completely through the agency of language. What actually is communicated about events is determined, not by the character of the events themselves, but by the linguistic figures or forms. Language has a will to power of its own. It generates meaning which is quite independent of the human agency of will.

Some postmodernists, especially the sceptical ones, are very antagonistic to the concept of truth¹¹⁴ because of the relationship between truth and power. The implication being the possibility of truth claims being products of power games manipulated into position by those whose interest they serve. The sceptic postmodernists therefore consider truth claims as a form of terrorism. Truth by its very existence is said to silence those who disagree. Truth claims serves to justify the powerful, and to make the weak feel at fault, and inadequate. This is echoed in Nietzsche and Foucault’s

¹¹²The following examination of postmodern view vis.a.vis the concept of ‘truth’ is based on Rosenau (1992, Chapter 5, pp.77-91).

¹¹³Rosenau (1992, pp.77).

¹¹⁴They consider it as some distorted form of rhetoric or propaganda.

exposition regarding the connection between truth and power. According to Nietzsche (1968, No. 481, pp.267), truths or facts are only interpretations, it is necessary to posit an interpreter behind the interpretation. The world is not knowable, it is interpretable. The drive behind interpretation is the 'will to power' - to compel all others to accept one's perspective as the norm and hence the truth. Foucault approaches the connection between truth and power somewhat differently. According to Foucault (1980b, pp.93), "in a society such as ours, but basically in any society, there are manifold relations of power which permeate, characterize and constitute the social body, and these relations of power cannot themselves be established, consolidated nor implemented without the production, accumulation, circulation and functioning of a discourse. There can be no possible exercise of power without a certain economy of discourses of truth which operates through and on the basis of this association. We are subjected to the production of truth through power and we cannot exercise power except through the production of truth." The emphasis is on the circular relationship between power and truth. We are therefore, either required to submit to the power of truth, or command power by producing the discourse of truth. Hence, the rationale for postmodernist antagonism for the modernist concept of truth.

The postmodernist antagonism for the modernist concept of truth, can also be connected to the modernist rationalization of the subject-object relationship. Truth implies an author, rejecting of truth implies a rejection of the author or the subject's right to impose his/her interpretation as the truth. It is also the connection between truth and theory, that forms the basis of postmodernist reaction to, and rejection of the modernist concept of theory. This is also the area of investigation of the next section.

(F) Theory: The concept of postmodernism as a reaction to or departure from modernism, is also apparent in the difference between the modernist and the postmodernist concept of 'theory'¹¹⁵. Postmodernists reject theories that are presented in the form of grand narratives that claim the status of being 'scientific' and 'objective'. They reject them as being logocentric, linear, and totalizing, that serve to legitimise modernity, and assume justice, truth, and hegemony. They reject them because modern theory by specifying a single interpretation interferes with, or resists the basic concept of postmodernism which emphasises on multiple interpretations. They reject them because they consider theory building as being analogous to truth seeking, which is characteristic of a totalizing and logocentric project. They reject them because modern theory assumes an epistemological reality whereas no such reality exists. They reject them because modern theory is assumed to operate in

¹¹⁵The following examination of postmodern view vis.a.vis the concept of 'theory' is also based on Rosenau (1992, Chapter 5, pp.77-91).

every context, which is dubious in an ever changing postmodern world. They reject them because modern theory, although claiming to be scientific, may actually be ideological and rhetorical, and may be used as an authoritarian weapon to provide legitimacy to monopoly of power. Last but not the least, postmodernists reject modern theory because it fails to fulfil the very goal that it sets for itself - it does not provide direction for practice or action, rather it may either be an ad-hoc justification, or a generalization of previous practice.

Sceptical postmodernists therefore substitute the modernist concept of theory with the postmodern idea of 'invitation to discussion'¹¹⁶. This is perhaps the reason why, there is no theory of the 'postmodern' in the modern sense of the word. The position of the affirmative postmodernists is slightly different. While they reject the intellectual hegemony implicated in grand theory, deny the truth claims of theory, and annul its privileged status, they do allow for decentred theory that is anti-positivist anecdotal empiricism that savours detail, and reserves a special place for what is unique in each and every life. The postmodern view of theory is reflected in Foucault's (1980d, pp.145) observation regarding the 'role of theory' in political power. According to Foucault, the 'role of theory' today, is not to formulate the global systematic theory which holds everything in place, but to analyze the specificity of mechanisms of power, to locate the connections and extensions, and to build little by little a strategic knowledge¹¹⁷.

In defence of the modernist concept of theory, and in reaction to the postmodern view of theory and truth, Rosenau (1992, pp.89-91) argues, that a world without a theory would mean the transformation of the entire intellectual climate of social sciences. It would mean an absolute equality of all discourses and an end to foundational claims. One possible outcome of the absence of the universal theory would be theory overload - it is not a question of no theory, but one of too many theories that are altogether equal. Postmodernism by erasing the difference between truth and error (or between theory and nonsense), opens the door to nihilism - since there is no truth, there is no error either. Postmodernists however argue, that the absence of any possibility of truth claims does not lead to nihilism, rather it makes totalitarianism impossible. The reason being that totalitarianism depends on its own version of truth. Postmodernism mediates against totalitarianism by abandoning truth claims and affirming gentler practices of listening, questioning, and speaking, hence the rationale for replacing theory with 'invitation to discussion'.

¹¹⁶Rosenau (1992, pp.81-82).

¹¹⁷In this respect Foucault observes that one of the reason that the traditional parties have been able to reestablish their hegemony over the 'left' and over the diverse forms of struggles which had not originally been under their control, is that only a profoundly inadequate logic was available to these (left wing) struggles for the analysis of their unfolding and their effects.

Another argument in favour of modern social science theory presented by Rosenau (1992, pp.90) is that modern social science seeks to produce objective theory that can be challenged on the basis of data, i.e. theory is data dependent and data has priority over theory in the sense that if data shows that the theory is wrong, then the theory must be abandoned. Data and evidence are the basis for arbitrating between two competing theories. But a counter argument against Rosenau's argument could be that the choice of the data itself is arbitrary, or may be based on some other theory with its own limitations, which itself indicate the problematical basis of the modernist theory. Furthermore, until a theory is proved wrong by another theory, the old theory is given the status of truth. This implies that the modernist theories are actually transitory truths that are dependent upon the accuracy and legitimacy of their ontological assumptions. This is also an indicator of the theory blindness of the modernist philosophical thought. Hence, the questionability of universal theories generalized across time and space, especially in social sciences where the society is continuously in the process of evolution and change. Hence, the rationale for the crisis facing the modernist philosophical thought. Postmodernism by releasing one from the straitjacket or the mental prisons of modern theory, allows the opening up of one's intellect to the realization of new ideas and new possibilities.

(G) History: The concept of 'history'¹¹⁸ is another important facet of the concept of postmodernism as a reaction to, or departure from modernism. One aspect of this facet has already been discussed in the context of Foucault's genealogy. Here it would be worth while to mention, that for the postmodernists, especially the sceptical ones, history is a humble discipline, dependent on the present, without any integrity of its own. The contemporary period is the time frame that counts most. "We live in the present as text, in a fragmented 'series of perpetual presents', where the future is only an 'anticipated presence', and the past a 'former presence'. History is only important to the extent that its traces have an impact on the contemporary, and even then, those traces are complex and intertextual. It is sufficient to let the present interrogate the past¹¹⁹. The speed-up of change of our ontological conditions in the new postmodern epoch has reduced the influence of the past to provide direction for the present and the future¹²⁰. Hence, the rationale for the reduction in the importance of history for the postmodernists.

¹¹⁸The following examination of postmodern view vis.a.vis 'history' is based on Rosenau (1992, Chapter 4, pp.62-76).

¹¹⁹Rosenau (1992, pp.64).

¹²⁰This aspect will be discussed in more detail in Chapter Eight which is on the phenomenon of 'temporal compression'.

(H) Space: The concept of postmodernism as a reaction to, or departure from modernism, is also apparent in the difference between the modernist and the postmodernist concept of 'space'¹²¹. Conventional geography which is based on the modernist philosophical thought, limits the concept of space to physical space, which implies that concrete objects located in objective geographical space can be charted out in terms of latitude and longitude. It assumes that once located, things stay put or if they move, they do so in a predictable pattern. The sceptical postmodernists concept of hyper space makes no such assumption. It takes into consideration the effects of electronic reality. It assumes that space has been annihilated and spatial barriers have disappeared - everything is in geographical flux, constantly and unpredictably shifting in space, as a result it is not possible for the individual human body to locate itself, to organize its immediate surroundings, and to talk cognitively, map its position in a mappable external world. This is in line with Marshal McLuhan's¹²² assertion that during the mechanical age we used mechanical technology to extend the reach of our physical bodies. Now during the electronic age we have used the electronic and telecom technology to extend our nervous system across the globe. The affirmative postmodernists, while rejecting the modernist concept of space and geography, rethink the concept of space in political terms rather than geographical. This forms the basis of their preference for local space, the space for community, the space of regional resistance, etc.. This is also the basis of the pluralist stance of the postmodernists - their emphasis on the respect of others space, and their insistence on the preservation of their own place. Both these postmodern concepts of space fit into Henri Lefebvre's (1991) concept of 'social space' - a concept that will be discussed in detail in the Chapter Nine which is on the problematic of spatial compression.

3.2.3. Implications for the Financial Services Industry:

Although an examination of the counter-concepts related to the eight key areas of our ontological assumptions, that characterize the concept of postmodernism as reaction to, departure from modernism, may appear as an over reaction and ideological, this is not necessarily true. This becomes apparent if we change our approach and view of postmodernism, as a complimentary rather than an alternative to the modernist philosophical thought. With this change in approach, the

¹²¹The following examination of postmodern view vis.a.vis the concept of 'space' is also based on Rosenau (1992, Chapter 4, pp.62-76).

¹²²McLuhan, and Powers (1989).

characterization of the counter-concepts discussed above, appear to be quite logical¹²³. The rationale for questioning the politics of disciplinary research is aimed at affording the researcher the power to question the a priori concepts and the basic assumptions related to one's research discipline. In the context of the financial services industry, this is of crucial importance because the regulatory framework itself is based on a number of theories and models developed within a realm of a particular disciplinary area, and are the products of the disciplinary rules and other systems of controls which are a part of the politics of the disciplinary research. This is important because, although the regulators act as the agents for the public, their intervention in the market mechanism may have negative repercussions on the public welfare. It is therefore necessary that the students of regulatory economics should recognize not only the benefits, but also the costs of regulatory intervention. The first step in this direction would be to question the a priori concepts and the basic assumptions related to the politics of regulatory economics¹²⁴. Within the realm of the problematic of disciplinary research, the tendency of the postmodernists towards de-differentiation of rigid disciplinary boundaries basically implies a conscious effort towards achieving intellectual broadening, which according to Caldwell (1975) is the most crucial attribute necessary for the public officials for meeting the challenges of the rapidly changing ontological conditions in the postmodern epoch. In the context of the financial services industry, one major weakness that plagues not only the regulators, but also the leading academics within the realm of regulatory theory is the disciplinary separation between the realms of economics, accounting and law. This weakness is very conspicuous in Goodhart et. al. (1998, pp.51-52) where the authors refuse to investigate into the role and the obligations of the external auditors in the scrutiny of the internal control mechanisms¹²⁵.

¹²³If we approach these counter-concepts as alternatives to the modernist concepts, these counter-concepts appear to become equivalent to reactional counter-moves. Reactional counter-moves, according to Lyotard (1984a), are not considered to be good moves because they are no more than programmed effects of the opponent's strategy; they play into the opponent's hand, and thus have no effect on the balance of power. Agnostic counter-moves, on the other hand, are unexpected counter-moves that disorient the system and affects the balance of power in the system. Examining these counter-concepts as complimentary rather than alternatives to the modernist concepts transforms postmodernism (as a reaction to, or departure from modernism) into an agnostic counter-move that affects the balance of power and disorients the system (defined by the modernist philosophical thought), and the counter-concepts start to appear rather quite logical.

The concepts of 'agnostic' and 'reactional' counter-moves are a part of the framework of 'language games' to be discussed in Chapter Seven in the context of the investigation into Lyotard's philosophy.

¹²⁴This aspect (to some extent) has been investigated in the two papers (McKenzie and Khalidi, 1994 and 1996) which form Chapters Two and Three of the thesis.

¹²⁵"these important questions are a major issue in accounting (and law), but not questions on which economics per se, can help much".

In the context of the financial services industry, the postmodern critique of 'representation' implies that the quantitative accounting data supplied by the financial institutions (the regulated) to the regulators should not be accepted at face value. Bettie et. al. (1995) cite a number of examples of banks which were considered as adequately capitalized, but failed because of inadequate provision for bad debts (infected assets were not shown as infected).

The postmodernist counter-concepts regarding the relationship between the author, the text, and the reader is also applicable for examining the regulatory framework in the financial services industry. The following two illustrative examples allow us an insight into the difference between the modernist and the postmodernist thinking vis.a.vis the problems in the financial services industry. Case one, would be the financial institutions (the regulated) as the authors of their accounting information (the text), and the regulators as the readers. Case two would be the regulators assuming the status of the modernist author (authors of the regulatory codes and the regulatory frameworks), and the financial institutions (the regulated) and the general public (including the depositors) as the readers. In both the cases, the modernist framework would imply all the power being appropriated in the hands of the author, with the readers being reduced to the status of passive participants. The postmodern counter-concepts, on the other hand empower the reader to take on an active role - to take control of the text. The reduction in the power of the author is reflected in the gradual change in the regulatory framework, where we see in case one, the gradual increase in the importance in the supervisory tool of bank examination where the regulator as the reader takes on a more active role - rather than accepting the accounting information provided by the financial institution (the text) on face value, the regulator as a postmodern reader takes control of the text. S/he rewrites the text (accounting information) in the context of the bank examination. In case two, where the financial institutions (the regulated) and the general public are the readers, and the regulator is the author, there is evidence of the concept of subsidiarity being applied with part of the regulatory responsibilities being passed on to the markets themselves (discussed in Chapter Three).

The postmodern concept of text is also relevant for understanding the tensions in the financial services industry. The postmodern concept of text allows us to visualize even a phenomenon like the financial services industry as a text for examination. The prudential regulations in the financial services industry can also be conceptualized as a text. The same applies to the tax regulations in the financial services industry. In fact the prudential regulations and the tax regulations can be combined into a single text (government regulations) to evaluate the disjunctions and the consequent tensions between the two sub-texts. Unlike prudential regulations which are aimed at safety and soundness of the financial institution, and hence the system, the tax regulations are aimed at maximization of government tax revenues. The disjunction between the two is very conspicuous

in the regulations related to the provision for bad debts. While the former encourages liberal provision for bad debts, the latter acts as a braking force. Bettie et. al. (1995) give quite a few examples where the tax codes discourage the provisioning for bad debts. Some of the problems related to the decrease in shock absorption capacity of the banks and the banking system as a whole can be connected to the negative implications of the tax regulations (Japan is perhaps the most conspicuous example).

The postmodern critique of the modern truth is another very important concept this is applicable to the financial services industry. In the context of the financial services industry, postmodern critique of the modern truth implies, that we should not accept the regulatory codes and their quantitative standards as statements of truth. Postmodernism encourages us to draw attention towards the problematical aspects of the regulatory codes and frameworks, thereby encouraging improvements in the regulatory codes and framework. Postmodernism also cautions us not to accept quantitative data on face value. The very rationale of auditing is to check the authenticity and the credibility of the accounting information¹²⁶. The incidence of audit failure, and the existence of expectation gap between the users of financial statements and the auditors, implies that even audited accounts can not be relied upon as statements of truth. It draws attention towards a very significant market failure where regulatory intervention may be justified¹²⁷. Unfortunately, not much attention has been given to this problem by the regulators in the financial services industry. The reason for this neglect, perhaps, lies in the disciplinary segregation between the realm of economics, law, and accounting discussed earlier.

The postmodern critique of theory is also in line with its critique of truth. We should not accept theories as statements of truth, but as direction flags. The overall message or the import of the concept of postmodernism as a reaction to or departure from modernism, for us the readers is to become active rather than passive readers, to approach text, especially theories rationalized as statements of truth and universal formulae with caution and a bit of scepticism. Similarly the message for us as the writers of the text is to view our own texts as direction flags rather than statements of truth. This is also what the thesis aims at - to act as a direction flag, rather than as a statement of truth.

¹²⁶For a discussion on the philosophy of audit, refer to Lee (1994), and Flint (1988).

¹²⁷The reference here is to the case of banking industry only. Systemic risk, and spill-over of externalities are problems peculiar to the banking industry that justify regulatory interventions.

3.3. Postmodernism as a Signifier of the Problematical Features or the Limits of Modernity:

Under this approach, the 'post' of postmodernism implies 'beyond'. It characterizes postmodernism as a concept that goes beyond modernity in the sense that it points to the limits of modernity. An extremist view under this approach would be to draw parallel between the 'post' of postmodernism with the 'post' of postmortem - postmodernism as the dissection performed on the dead body of modernity (Kumar, 1995, pp.67). A more appropriate view would imply, postmodernism as modernity viewed from the rear-view mirror. Here the term 'post' implies a reflection on modernism, i.e. 'modernity becoming conscious of itself'. This view (according to Kumar, 1995, pp.140-141) denies postmodernism as a new epoch or a new era, but accepts that we are in a new situation, a situation in which for the first time we are able to look back and analyze modernity. Since, knowledge and understanding comes post factum, postmodernity is therefore modernity recollected. We are now more aware of the limits of modernity, its over-ambitious and sometimes tyrannical enterprise. Postmodernity is therefore modernity emancipated from its fake consciousness. Intellectuals now realize that you cannot lay out rules and standards with reference to some universal truth. Postmodernity therefore implies a renunciation of the idea of constructing a perfect rational society governed by experts. It implies that intellectuals and experts should come down from their moral high ground of legislators, and accept a more modest role as interpreters and brokers of culture and knowledge, to help communities understand each other, while at the same time restoring to individuals their right to moral choice and reality, thereby allowing them (individuals, as well as, the society) to realize their full potential. The application of postmodernism to the social sciences does not seek to "improve and perfect" the social sciences, rather it attempts to undermine their foundational claims by making their underlying assumptions explicit. Postmodernism in social sciences, is therefore, in part, a response to the perceived inadequacies of scientific social science, which was based on the positivist, empiricist, and rational-logical model of modern science¹²⁸.

Modernity, as conceptualized in the late nineteenth century, was visualized as a perennial or timeless order, a once-and-for-all achievement, a meta-discourse that stands the test of time requiring only minor variations on the main theme. Postmodern theories point to the discontinuities in the history of modernity. They also point to the realities like ethnic differences, local identities, etc., which were ignored by the modernist philosophers in their endeavour to achieve standardised citizens of geographically bounded nation-states. The difference between modernity and postmodernity, according to Kumar (1995, 178-79), is that modernity emphasizes on the persistence of the past characteristics and hence the relevance of the past analysis of modernity. Postmodernists do not deny the continuity of some characteristics of the past, but draw attention to the fact that we are now in

¹²⁸Rosenau (1992, pp.9-10).

a position to take stock of the whole experience of modernity in ways that was not possible before. Hegel and Marx may have had acute insights to offer, but unlike them, we are now (with hindsight of experience) in a position to read through the problematical facets of their theories. Postmodernity, is therefore, modernity becoming conscious of its principles and practices. It involves drawing attention to the problematical nature of metaphysical presuppositions of the modernist philosophical thought, and hence the problematical nature of the modernist philosophical thought itself. It draws attention to the fact that the pursuit of unshakable foundations for analytical truth constitutes a fruitless project, because the metaphysical foundations that lie at the heart of Western philosophy are themselves problematical¹²⁹. It draws home the conclusion that the goals and values that have been central to the West European Civilization can no longer be considered universal, and that the associated universal project of modernity is unfinished because its completion is inconceivable and its value questionable¹³⁰. The overtone being, that the grand narratives of modernist philosophy have been rendered inoperative, and have therefore lost their credibility. This crisis in the very concept of modernity, which was expressed politically as 'the quest for rationalized world', according to Lyon (1994, pp.6), invited a lot of intellectual analysis - whether it was a catastrophe or an opportunity. This led to the development of the terminology 'postmodernity' to describe the emerging situation. In this respect postmodernity refers to the exhaustion of modernity.

The concept of postmodernism as a signifier of the problematical features or the limits of modernity also fits in with Hal Foster's (1985) categorization of 'postmodernists of resistance'¹³¹, which mainly consists of philosophers and academics who find the project of modernity to be deeply problematical, whose endeavour is to lay out the problematical facets of modernity, while at the same time also making an effort to explore and understand the social and political codes and practices like tradition, ethnicity, etc., which were ignored and rejected by modernity (whose aim was to homogenize the social in line with the meta-discourses of the philosophers and social theorists). Here the aim is to signify that the limits of modernity has been reached; that the grand old narratives of modernist social theories and philosophy have been rendered inoperative, and hence have lost their credibility; that the pursuit for unshakable foundations for analytical truth constitutes a fruitless

¹²⁹Smart (1990, pp.23).

¹³⁰Smart (1990, pp.27).

¹³¹Hal Foster classifies postmodernism into two categories: 'postmodernism of resistance' and 'postmodernism of reaction'. The former consists of those who seek to deconstruct modernism and resist the status quo, while the latter consists of those who repudiate modernism but celebrate the status quo, i.e., the consumer culture. The common element in both the categories is their disaffection or disillusion with modernism/modernity. Reference: Hal Foster (1985, pp.xi-xii) and Barry Smart (1990, pp.24-25).

project - one that will remain incomplete because the metaphysical presuppositions that are at the heart of the Western philosophy themselves are problematical. The grand hopes associated with the global and totalizing forms of social theories and the politics of revolutions have therefore lost their credibility.

This approach (i.e. postmodernism as a signifier of the problematical features or the limits of modernity) is significant because it allows us to examine the texts of the French philosophers like Foucault, Lyotard, and Derrida, whose philosophical works brought to light the problematical features of the modernist philosophical thought, and as a consequence stimulated the development of the postmodern philosophical thought. In view of the importance of the works of these three philosophers in generating knowledge that may provide us with useful insights into the problems of the present era - insights that may assist us in understanding and ameliorating the tensions in the financial services industry, it would therefore be appropriate to devote at least one full chapter for examining some of the ideas and insights generated by these philosophers. This is the aim of the next chapter which continues with the investigation into the second part of the hypothesis which was also the inspiration for this chapter.

4. Conclusions:

The aim of this chapter was to investigate into the concept and the ideas generated within the realm of postmodern philosophical thought, as a source of inspiration and ideas that may assist us in understanding and ameliorating the tensions in the financial services industry. A problem that was faced in this investigation was the confusion surrounding the label of postmodernism. The term 'postmodernism' has been used in the media as a label for a number of (sometimes even conflicting) phenomena. This is because that there was no precise definition of postmodernism. Unravelling this confusion was therefore necessary in order to have a clear sense of what one is expected to explore. The approach adopted for examining the postmodern phenomenon was to picture it as a collage incorporating three distinct but interrelated concepts or themes: one, postmodernism as an epoch; two, postmodernism as a reaction to, or departure from modernity; and three, postmodernism as a signifier of the problematical features or the limits of modernity.

The first theme, postmodernism as an epoch, implied postmodernism as an indicator of a period of major historical transition of our society - a move to a new state of things, a new 'epoch'. The end of the modernist epoch and the beginning of a new epoch: the postmodern epoch. In the context of the tensions in the financial services industry, the central idea that emerged from the

concept of postmodernism as an epoch, was that the most crucial problem facing a society during transitory periods is the differential rate of change between the attitude and beliefs of the general public and private sector agencies (the regulated), and the adaptive changes in the attitudes and the operational framework of the public agencies (the regulators). It is this disjunction that is at the source of the problems facing a society during a transitional epoch. The key to the problem is the need for a reorientation in the knowledge base of the personnel managing the public agencies (the regulators). The particular kind of knowledge that is necessary, is the knowledge of trends, interactions, and synergistic effects. The task of the managers of the public agencies during transitional periods are: reassessment of priorities, redefinition of goals, and the creation of material and intellectual environment in which all other social institutions can play their respective roles in the transition. This requires intellectual development and the broadening of the knowledge base of the public officials. This requires administrators who have the intellectual honesty and the self confidence that is necessary for sharing their information and their knowledge with the public. In the context of the financial services industry, the emphasis here is, not only on the intellectual broadening of the regulators so as to be able to reassess priorities and redefine goals, but also on the need for sharing of information with the markets to improve the market's self regulatory mechanism. The emphasis here is on transparency, after all as Caldwell (1975) observes: in a high technology society the most knowledgeable administrators would be helpless without informed collaborators. The implication being, the need to maximise the efficiency of the market's self regulatory mechanism to compliment the statutory regulatory framework.

The second theme of investigation into the concept of postmodernism, involved the use of the term 'post' as a contrast concept that implies: postmodernism as a reaction to or a departure from modernism (or modernity), which has been described as "positivistic, technocentric, and rationalistic", and "the belief in linear progress, absolute truths, the rational planning of ideal social orders, and the standardization of knowledge and production¹³²". In this respect postmodernism can be described as a broad-gauged cultural and intellectual movement that is re-conceptualizing the way we experience and understand the world around us. It involves a reexamination of the a priori concepts, and the meta-discourses which modernity had legitimated, as well as 'multiple forms of otherness' that modernity had de-legitimated. Postmodernism involves pluralism, not only across space, but also across time. Unlike modernity which is the philosophy of 'becoming'¹³³, postmodernism is the philosophy of 'being' which implies pluralism. The emphasis is on societal transparency to allow one

¹³²Harvey (1992, pp.9).

¹³³The emphasis is on the need to order and control the ontological conditions for overcoming the problems of the present as well as the future.

to explore and understand the others in the society around us. The investigation into the concept of postmodernism as a reaction to, or departure from modernism involved an examination of the counter-concepts presented within this theme. In order to understand and appreciate the power and the potential of these counter-concepts in encouraging a reconceptualization of the way we imagine, think, plan, and rationalize, it was necessary not only to examine some of the counter-concepts that characterize the concept of postmodernism as a reaction to modernism, but also to examine the source of inspiration and the underpinnings of power of this mode of thinking. The examination of Foucault's genealogical analysis of knowledge, and Derrida's deconstructive analysis of knowledge was undertaken for this purpose. The basis of power of Foucault and Derrida's philosophy relates to their ability to take control of knowledge rather than allowing knowledge to control them. It was their ability to interrogate and to locate the problematical facets of the concepts introduced within the realm of the modernist philosophical thought, that not only formed the basis of the power of their own discourse, but also provided the inspiration for the development of counter-concepts that have the power to rebel against and challenge our conventional (modernist) concepts. The counter-concepts examined within the realm of the concept of postmodernism as a reaction to or departure from modernism covered eight areas/elements of our ontological assumptions namely: the problematic of disciplinary research; the concept of representation; the concept and the relationship between the author, the text, and the reader; the concept of subject; the concept of truth; the concept of theory; the concept of history; and the concept of space. These counter-concepts which emerge from the problematical nature of the modernist concepts, provide us with a different perspective for examining and understanding the problems of the present era. The overall message or the inference drawn from the investigation into the counter-concepts presented within the realm of postmodernism as a reaction to or departure from modernism, for us the readers, is to become active rather than a passive readers, to approach the text, especially statements of truths and universal formulae with caution and a bit of scepticism. Similarly the message for us as the writers of the text is to view our text as direction flags rather than statements of truth. This is also the aim of this thesis. In the context of the financial services industry, this message would imply an awakening from the self blinded belief in the capacity and the potency of regulatory tools and the regulatory framework in achieving its regulatory objectives. This would imply a reduced emphasis on regulatory tools like the capital adequacy regulations and an increased emphasis on supervisory tools like bank examination, and a renewed thrust towards the maximization of the efficiency and the potency of the market's own self regulatory mechanism.

The final theme that was applied to examine the concept of postmodernism was: the concept of postmodernism as a signifier of the problematical features or the limits of modernity. This

approach characterizes postmodernism as a concept that goes beyond modernity in the sense that it points to the limits of modernity. Here the term 'post' implies a reflection on modernity (or modernism), i.e. 'modernity becoming conscious of itself'. This theme incorporates the works of philosophers and academics who consider the project of modernity to be deeply problematical, whose endeavour is to lay out the problematical facets of modernity, while at the same time also making an effort to explore and understand the social and political codes and practices which were ignored and rejected by modernity. This theme is of especial significance because it allows us to examine the texts of philosophers like Foucault, Lyotard, and Derrida, whose philosophical works brought to light the problematical features of the modernist philosophical thought, and as a consequence stimulated the development of new knowledge - the postmodern philosophical thought. This theme therefore forms a stepping stone to the next chapter which continues with the investigation into the second part of the hypothesis in the context of the philosophical works of the three above named philosophers.

CHAPTER SEVEN

AN EXPLORATION INTO THE PHILOSOPHY OF POSTMODERN PHILOSOPHERS: JEAN-FRANCOIS LYOTARD; MICHEL FOUCAULT; AND JACQUES DERRIDA

1. INTRODUCTION:

This chapter continues with the investigation into part II of the hypothesis. The story line of this chapter involves an exploration into the philosophy of three of the most important philosophers of the postmodern philosophical thought (especially in the context of the hypothesis under investigation): **Jean-Francois Lyotard** whose philosophical work ‘The Postmodern Condition: A Report on Knowledge’ is considered to be a pioneering work for having introduced the concept of postmodernism within the realm of philosophy and social science. His work is important because it involves an examination of ‘knowledge’ itself, including its forms, and its problematical features. His work introduces us to the framework of ‘language game’ as a tool for examining and understanding and examining the social bond, but also for understanding the problems of the present era. **Michel Foucault’s** philosophical enterprise has already been introduced in the context of the discussion on the concept of postmodernism as a reaction to or a departure from modernism. Here the area of his philosophical enterprise which comes under investigation, relates to his works on the problematic of ‘power’. It involves an examination of the different forms of power (power that is connected to the truth of law, power that is connected to repression, power that is connected to knowledge, power that is connected to our bodies and their use etc..) and their implications in the context of the tensions in the financial services industry. **Jacques Derrida** is the third philosopher whose philosophy has been explored. Derrida’s philosophy of deconstruction was discussed in the introduction to explain the logic for the use of the term ‘deconstruction’ in the title of the thesis. It was again discussed in Chapter Six in the context of the discussion on the concept of postmodernism as a reaction to, or departure from modernism. Here two areas of his philosophy have been explored: one, the concept of deconstruction in the broad sense - the sense that forms the basis of the title of the thesis; and two, the concept of deconstruction in the narrow sense - the method or the strategy that he applies to deconstruct the text (of other philosophers and social scientists), and its implications in the context of the tensions in the financial services industry.

The significance of the works of postmodern philosophers relates to their seminal effect on knowledge. The reference here is not only to the effect of their thinking in opening up of the problematical facets of various disciplines for reexamination, but also in the context of their metaphorical effect on knowledge. The reference here is to Gareth Morgan’s (1985, pp.12)

characterization of 'metaphor' as a way of thinking and a way of seeing that pervades how we understand the world generally. According to Morgan, new insights often arise when one reads the same situation from new angles, and that a wide and varied reading can create a wide and varied range of actions. This is also the significance of postmodern philosophy in general, and the works of the philosophers to be examined in this chapter in particular. They allow us to read the same situation from different angles, thus allowing us to create a wide and varied range of actions. This is also the logic for Part II of the hypothesis:

one: the tensions reflecting the regulatory crisis in the financial services industry may be a subset of, or a part of a much wider area of tensions/crises facing the conceptual foundations of the regulatory philosophy: the modernist philosophical thought.

two, the alternate philosophical thought which is generally described as postmodernism, may provide us with inspiration and ideas for the formulation of a regulatory strategy and regulatory framework that may facilitate the achievement of regulatory objectives while facilitating the amelioration of the tensions inherent in the financial services industry.

Part two of the hypothesis outlines the rationale for examining the philosophy of Lyotard, Foucault, and Derrida. The aim is to apply their ideas to examine the tensions in the financial services industry in the hope of developing new insights that may help us to understand and appreciate the problems of the present era. It is after all our understanding of the problem, our reading of the situation, which forms the basis of our search for answers.

2. Jean-Francois Lyotard:

Jean-Francois Lyotard's book 'The Postmodern Condition: A Report on Knowledge'¹ is considered to be a seminal work for having laid the foundations of the concept of 'postmodernism' in philosophy and social science². His definition of 'postmodern' as "incredulity towards

¹Lyotard, Jean-Francois (1984), "The Postmodern Condition: A Report on Knowledge", Manchester University Press, Manchester.

The original French edition of Lyotard's book "La Condition postmoderne: rapport sur le savoir", appeared in 1979 but the English translation was not available until 1984.

²The object of his study is 'the condition of knowledge in the most highly developed societies'. He employs the term 'postmodern' to describe this condition. The basis of the choice of the word 'postmodern', according to Lyotard (1984a, pp.xxiii), is connected to the use of the word on the American continent among sociologists and critics, to designate the state of our culture following the transformations which, since the nineteenth century, have altered the game rules for science, literature,

metanarratives³", according to Kumar (1995, pp.133), is regarded as one of the best-known and most generally accepted attribute of postmodern theory that not only unifies the highly diffuse and dispersed series of postmodern propositions, but in the process also points to the source or the thrust of the postmodern theory: it is not in the announcement of something new, in a positive sense, but in the rejection of the old, the past of modernity. Kumar's observation, although important, does not do full justice to Lyotard's contribution to our knowledge-base. Lyotard's contribution is much more than a simple signifier of the problematical features or the limits of modernism, he also provides a positive thrust towards knowledge generation. This is apparent from his answer to the question: "What is postmodernism":

"It is undoubtedly a part of the modern. ... A work can become modern only if it is first postmodern. Postmodernism thus understood is not modernism at its end but in the nascent state, and this state is constant⁴."

The concept of postmodernism as modernism "in the nascent stage, and this stage is constant", implies a permanently revolutionary disposition towards knowledge and art. It implies that the postmodern philosopher is analogous to the Schumpeterian entrepreneur, but in the intellectual and not the economic realm. He creates a discontinuity in Kuhn's paradigm leading to a paradigm shift in our knowledge.

"A postmodern artist or a writer is in the position of a philosopher: the text he writes, the work he produces are not in principle governed by preestablished rules, and they cannot be judged according to a determining judgement, by applying familiar categories to the text or to the work. Those rules and categories are what the work of art itself is looking for. The artist and the writer, then are working without rules in order to formulate the rules of what

and the arts. Lyotard own study places these transformations in the context of the crisis of narratives.

The working hypothesis of Lyotard's (1984a, pp.3) study is that the status of knowledge is altered as societies enter what is known as postindustrial age and cultures enter what is known as the postmodern age. This transition has been under way since at least the end of 1950s, which for Europe marks the completion of reconstruction. The pace is faster or slower depending upon the country, and within countries it varies according to the sector of activity. The general situation is one of temporal disjunctions which makes the development of an all encompassing (or complete) overview difficult. Lyotard therefore describes, or rather acknowledges, his study as being partially conjunctural. Furthermore, in order to keep his study manageable, he narrows down the context (or the object) of his study to one feature, around which his investigation revolves: 'the pragmatics of scientific discourse'.

³Lyotard (1984a, pp.xxiv).

⁴Lyotard (1984b, pp.79).

will have been done. ... Post modern would have to be understood according to the paradox of the future (*post*) anterior (*modo*)."⁵

To explain his idea, he gives the examples of Cezanne, Picasso and Braque, and Duchamp-Villon⁶, all of whom presented the unrepresentable in the presentation itself. The style of art they developed was not governed by the preestablished rules, and therefore could not be judged according to the determining judgement. The works they produced broke the preestablished rules that defined art, and in the beginning was therefore refused acknowledgement as art by the connoisseurs of art. These artists worked without rules to lay the foundations of a new style of art, and their works became the basis for the new rules developed by the connoisseurs of art for defining and judging of new works within this realm of art.

"The postmodern would be that which, in the modern, puts forward the unrepresentable in presentation itself; that which denies itself the solace of good forms, the consensus of a taste which would make it possible to share collectively the nostalgia for the unattainable; that which searches for new presentations, not in order to enjoy them but in order to impart a stronger sense of the unrepresentable"⁷

Modernity, by rationalizing totalizing universal theories applicable across time and space, allowed itself to be bureaucratized and ossified, and hence lost its dynamic edge. Postmodernism is therefore, modernity without its totalizing and universalizing preconceptions. The concept of postmodernism as a continuously dynamic philosophical thought suggest a possible compatibility with Schumpeter's theory of economic development, and an avenue for finding an answer to the disjunction between the regulators and the regulated.

Lyotard's work under consideration is a 'report on knowledge', in which he introduces us to a host of concepts that broaden our knowledge base, thereby improving our ability to understand

⁵Lyotard (1984b, pp.81).

⁶French post-impressionist painter Paul Cezanne (1839-1906) challenged and broke the rules of painting defined by the works of the impressionist painters (who themselves had broken the rules of art defined by the Salon, and established a new form of art which was described as the impressionist style of painting). But Cezanne's work itself pioneered a new style of painting: the post-impressionist style, and the implicit rules that he followed in his paintings became the explicit rules (established standards) for governing the post-impressionist style of painting. The standards and the rules established by Cezanne's art were latter-on broken by the cubist painters Pablo Picasso (1881-1973) and Georges Braque (1882-1963), who created a new style of art with its own new set of rules. These new set of rules set by the paintings of Picasso and Braque were (later-on) broken by Raymond Duchamp-Villon (1876-1918) who extended cubism from two dimension (painting) to three dimension (sculpture).

⁷Lyotard (1984b, pp.81)

and appreciate the world and the problems of the world around us. It is after all our perception of the problem, that forms the basis of the strategies that we develop for meeting the challenges created by the problem. In his seminal work, 'The Postmodern Condition: A Report on Knowledge', Lyotard introduces us to the concept of 'knowledge', the concept of 'narrative', the concept of 'metanarrative', the concept of 'science', and the concept and the process of 'legitimation' of scientific truths. He also introduces us to the reasons for the present crisis in the legitimation of scientific truths, he also introduces us to the crucial difference between natural and social science, and the problems created when the principles and methods of natural science are applied to social science. He draws our attention to the flawed nature of the modernist concept of 'society' visualized as a functional whole, and then introduces us to a new concept/tool for visualizing the society: society as a language game⁸, a concept which can be useful as a tool for analyzing and understanding the problems of the present era.

Since the rationale for the examining of Lyotard's philosophical work is primarily for understanding the tensions in the financial services industry, the discussion to follow will cover only some aspects of his discourse. The discussion to follow has been divided into four sub-sections: one, the incredulity towards metanarratives; two, the concept of society as a language games; three, problematical nature of the theories of social science; four the concept of paralogy as a source of inspiration for the future.

2.1. Incredulity Towards Metanarratives:

Lyotard uses the term '**modern**' to designate any science that legitimates⁹ itself with reference to a 'metadiscourse' making an explicit appeal to some grand-narrative¹⁰. It is the crisis and hence the

⁸Society as a fabric formed by the intersection of at least two and reality an indeterminate number of language games, obeying different rules. It is this conceptualization of social bond as a language game that also forms the basis of his postmodern alternative for legitimation of science: the legitimation by paralogy.

⁹Science, according to Lyotard (1984a, pp.xxiii), does not restrict itself to stating useful regularities and seeking of truth, it is obliged to legitimate the rules of its own game. This discourse of legitimation is a part of philosophy.

¹⁰The 'grand-narratives' or the 'metanarratives', referred to by Lyotard, are the great historico-philosophical schemes of progress and perfectibility, developed during the modern age, to form the basis for the construction of knowledge. Examples of metanarratives include, 'the dialectics of spirit', 'the hermeneutics of meaning', 'the emancipation of humanity', etc. (Lyotard, 1984a, pp.xxiii).

obsolescence of the metanarrative apparatus of legitimization¹¹ that forms the basis of the term 'postmodern' which Lyotard (1984a, pp.xxiv) defines as "incredulity towards metanarratives"¹². The crisis of scientific knowledge, according to Lyotard (1984a, pp.39), is not born of a chance proliferation of sciences, rather it is an effect of the progress of technology and the expansion of capitalism. It reflects an internal erosion of the legitimacy principle of knowledge. The logic for the crisis in modernity and hence the obsolescence of the metanarrative apparatus of legitimization is connected to the development of the principle of performativity¹³ - a principle that is also described as 'context control' or the principle of technology. The operational framework of the principle of 'context control', as explained Lyotard (1984a, pp. 47) is as follows:

- 'Reality' is what provides the evidence used as proof in scientific argumentation,
- 'Reality' is also what provides juridical, ethical, and political prescriptions and promises with results.
- This implies that one can master all these games by mastering 'reality'.
- Since technology can assist us in mastering 'reality', therefore, by reinforcing technology, one can reinforce 'reality', and hence one's chances of being just and right.
- The reciprocal of this is also logical: technology is reinforced all the more effectively if one has the access to scientific knowledge and decision making authority.

This points to the possible connection between technology and power. By controlling technology, one can control reality, and hence power. The implication being, that the goal of today's financial backers of research is only power. Scientists, technicians, and instruments are purchased, not to find truth, but to augment power. This is the basis of the incredulity towards the metanarrative apparatus of legitimization.

The logic for the incredulity towards the metanarrative apparatus of legitimization can be visualized from another angle. According to Lyotard (1984a, pp.43), there are two different kinds of progress in knowledge: one, a new move or a new argument within the established rules; two, the

¹¹Metanarrative apparatus of legitimization implies the legitimization of knowledge on the basis of a metanarrative. For example, a statement with truth-value that has to be legitimated through the application of the rule of consensus between sender and addressee of the statement, will be deemed acceptable (legitimated) if it is cast in terms of a possible unanimity between rational minds (this is the Enlightenment narrative, in which the hero of knowledge works towards a ethico-political end - universal peace (Lyotard, 1984a, pp.xxiii-xxiv).

¹²This incredulity is connected to the progress of science, and the obsolescence of the metanarrative apparatus of legitimization which is connected to the crisis in metaphysical philosophy and the university institution which in the past relied on it.

¹³The basis of the 'principle of performativity', lies in the attainment of the best input/output equation.

invention of new rules, in other words a change to a new game. Technology can be classified in the second category, because here it is not the presentation of proof but the principle of performativity that is the goal¹⁴. The principle of performativity that forms the basis of incredulity towards metanarratives can be connected to the concept of entrepreneurialism¹⁵, a concept that was the topic of investigation in Chapter Five.

The principle of performativity also provides an explanation for the tensions in the financial services industry. Unlike the financial institutions (the regulated) whose operational framework is based on the principle of performativity, the operational framework of the regulators (and hence, the regulatory framework in the financial services industry) is still based on the metanarrative apparatus of legitimization. The reason being, that the philosophical foundation of the regulatory framework is based on the modernist philosophical thought. Furthermore, unlike the regulated (financial institutions), the regulators have a monopoly over regulatory supply within the periphery of the nation-state. This is one facet of the problem facing the regulatory framework in the financial services industry, where Lyotard's philosophical work facilitates our understanding of the problem.

2.2. Society as a Language Game:

According to Lyotard (1984a, pp.15) the question of social bond itself is a language game: the game of inquiry - it immediately positions the person who asks (the sender), as well as the addressee, and the referent asked about¹⁶. The language game, therefore directly links and creates the social bond

¹⁴Lyotard (1984a, pp. 46) explains the implication of the principle of performativity on the language game of science: the production of proof which is an important part of the argumentation process designed to win agreement from the addressee of scientific messages, has fallen under the control of another language game in which the goal is not 'truth', but 'performativity' (i.e., the best possible input/output equation). The implication is that the idealist and humanist narratives are abandoned to justify the new goal: the goal of today's financial backers of research is only power. Scientists, technicians, and instruments are purchased not to find truth, but to augment power.

¹⁵According to Lyotard (1984a, pp.37), the grand narrative has lost its credibility regardless of what mode of unification it uses, regardless of whether it is a speculative narrative or a narrative of emancipation. The decline of the narrative can be seen as an effect of the blossoming, or the development of the techniques and technologies since the second world war. It can be seen as a shift in emphasis from the ends of action, to its means. It can also be seen as the effect of the redeployment of advanced liberal capitalism after its retreat during the protection of Keynesianism during the period 1930-60. A renewal that has eliminated the communist alternative and valorized the individual enjoyment of goods and services.

¹⁶Even before a child is born, by virtue of the name given to him, the human child is already positioned as a 'referent' in the story recounted by those around him, in relation to which he will inevitably chart his course (Lyotard, 1984a, pp.15).

that forms the basis of a society. Lyotard's concept of 'language games' is a powerful methodological approach for understanding not only the nature of the social bond that forms the basis of a society, but also for understanding the changes in ontological conditions that leads to a change in the society. The concept of language games has two elements: one, the language which is connected to the theory of communications, and two, theory of games. It is the combination of the two that forms the basis of the explanatory power of the theory of language games. We begin by looking at each aspect separately.

'Language' Game: The matter under examination here relates to the first half of the concept of language games, i.e., connection between language and our social bond. According to Lyotard (1984a, pp.40) our social bond is linguistic. It is not woven by a single thread, rather, it is a fabric formed by the intersection of at least two, and in reality an indeterminate number of language games, obeying different rules¹⁷. The 'atomization' of the social into a flexible network of language games also allows us to understand the increasing complexity of the present social scene brought about by the time and space compression. The complexity of the present social scene relates to the increased mobility of the players of the language game, and is not a consequence of the breaking up of the grand narratives - a consequence which some authors describe as the dissolution of the social bond and the disintegration of the social aggregates into a mass of individual atoms thrown into a Brownian motion. Lyotard describes such suggestions as absurd because no self is an island; each exists as a fabric of relations that is now more complex and mobile than ever before. Each person is located at 'nodal points' of specific communication circuits, however tiny they may be. One is always located at a post through which various kind of messages pass¹⁸. This is the first element of the theory of language games.

Language 'Game': Here the matter under examination relates to the second half of the concept of language games: the theory of games. Conceptualizing problems purely in terms of communication theory overlooks two key characteristics of the language games (Lyotard, 1984a, pp. 16-17): **One**, that messages have quite different 'forms' and 'effects' depending upon whether they are for example denotative, prescriptive, evaluative, performative, etc.. It is clear, that what is important is not simply the fact that they communicate information, the type of statement is also important

¹⁷In this respect he quotes Wittgenstein "our language can be seen as an ancient city: a maze of little streets and squares, of old and new houses, and of houses with additions from various periods; and this surrounded by a multitude of new burroughs with straight regular streets and uniform houses".

¹⁸Lyotard (1984a, pp.15).

because it effects the reaction or the countermove of the addressee. Each language partner undergoes a displacement when a ‘move’ pertaining to him/her is made¹⁹. This displacement implies an alternation that not only affects him/her in his/her capacity as an addressee and referent, but also as sender. The reference is to the possible countermove by the addressee to the message received. This is the **second** aspect of the theory of games. Two scenarios are possible in this countermove. It may be merely reactional, in which case the countermove has no effect on the balance of power²⁰. The other possibility is an unexpected countermove, that disorients the system. This is what Lyotard calls the ‘agnostic’ aspect of the society.

To understand our social relations, it is therefore necessary not only to picture society in terms of ‘theory of communications’, but also in terms of the ‘theory of games’ which accepts ‘agnostics’ as a founding principle²¹. The concept of ‘agnostic aspect of the society’ is important because it brings to the fore the rationale behind the change in our ontological conditions. It also allows us to understand how change is possible even in institutions afflicted with bureaucratic paralysis. The reason for the bureaucratic paralysis that afflict institutions, according to Lyotard (1984a, pp. 17), is because unlike ordinary conversation²², institutions require supplementary constraints for statements to be declared admissible within its bonds. These constraints function to filter the discursive²³ potential, implying their negative effects in terms of interrupting their possible connections in the communication network. These constraints also privilege certain classes of statements (sometimes only one) whose predominance characterizes the discourse in the particular

¹⁹According to Lyotard (1984a, pp. 16), atoms are not only placed at the crossroads of pragmatic relationships, but they are also displaced by the messages that traverse them.

²⁰Reactional countermoves are not considered as good moves because they are no more than programmed effects in the opponent’s strategy; they play into the opponent’s (sender) hand and thus have no effect on the balance of power.

²¹In this context, the essential element of newness is not only innovation, but also any (other) unexpected move. Hence, the importance of the agnostic aspect of the society for the language games.

²²In ordinary conversation, the interlocutors are not strictly bound by rules. A great deal of flexibility is allowed. Applying the metaphor of ‘war’, Lyotard explains conversation of words in which statements are the ammunition: questions, requests, assertions, narratives are launched into battle. The war is not without rules, but the rules allow and encourage the greatest possible flexibility of utterance.

²³In philosophy, the term ‘discursive’ refers to knowledge attained by reason or argument rather than intuition.

institutions²⁴. The implication being, that there are certain things that should be said, and there are ways of saying them. Bureaucratization is the outer limit of this tendency. Despite bureaucratic paralysis, change in institutions is possible because the limits the institution impose on potential language moves, are never established once and for all, even if they have been formally defined. Rather, the limits are themselves the stakes and the provisional result of language strategies within and outside the institution²⁵. Putting it another way, it can be said that the boundaries of institutions only stabilize when they cease to be stakes in the game.

The concept of ‘language games’ presented by Lyotard, provides an explanatory logic for the materialization of the gradual change in the regulatory framework in the financial services industry. The reference is to the regulatory dialectic between the regulators and the regulated that leads to a change in the regulations. This also includes a more proactive approach presently being adopted by the regulated entities (financial institution) by drawing attention to the sophistication of their internal risk management models vis.a.vis. the crudeness of the official regulations. The development of the pre-commitment approach to capital adequacy regulations in the financial services industry is an excellent example. It began with the Basle Committee’s proposal to incorporate capital requirements for market risks into the Basle Accord. The countermove by J.P.Morgan to this initiative by the Basle Committee, was to put its own internal control ‘Value at Risk’ (VAR) model for the management of market risks: ‘RiskMetrics’ into the public domain. It was a move that echoed the ‘agnostic’ aspect of the society, a move aimed at disorienting the system. This move influenced and induced the other major banks to follow the J.P.Morgan lead, and to reveal their own internal risk management models too. The aim was to exhibit the sophistication of their VAR model approaches as a strategy to rationalize the much lower capital requirements calculated and justified by their VAR approaches vis.a.vis the much higher capital requirements calculated via the crude approaches being proposed by the Basle Committee. After necessary deliberations on the merits or otherwise of the VAR approaches, the Basle Committee for Banking Supervision decided to allow the proprietary VAR internal control approaches of the banks to be incorporated into the capital adequacy regulations of the G10 countries. They gave the national regulators the onus for accepting

²⁴For example, ‘orders’ in the army, ‘prayer’ in church, ‘teaching’ in the schools, ‘narrations’ in families, ‘questions’ in philosophy, ‘performativity’ in business, etc..

²⁵Lyotard (1984a, pp.17) provides a few examples:

- If the question is: Does the university has a place for language experiments? The answer can be yes, if the university opens creative workshops.
- Can you tell stories in a cabinet meeting? The answer, once again can be yes, if the cabinet works with prospective scenarios.
- Can you advocate a cause in the barracks? The answers once again can be yes, if the old institutions are displaced.

or rejecting the internal control models of the individual banks. This put the national regulators in a difficult position. There was not one, but a number of VAR approaches in use by the banks, and assessing the adequacy or otherwise of each was not an easy task. Furthermore, a model that performs adequately in back-testing (use of historical data to test the limits of the model) is not a guarantee that it will perform adequately to cover the risks of the future. The pre-commitment approach was the response of the national regulators (US Federal Reserve) to pass the onus on to the regulated entities (bank's) themselves. The pre-commitment approach is basically an incentive contract between the regulators and the regulated. The regulated (financial institutions) apply their own VAR models to calculate their capital requirements for market risks. These calculations form the basis of their ex-ante pre-commitment to the regulators. As long as the ex-post value of the change in the value of the portfolio due to market risk, is within the bonds of this pre-commitment, there is no problem. Otherwise they risk being penalized by the regulators²⁶.

The pre-commitment approach is also an indicator of a major shift in the regulatory framework. It reflects a move from a prescriptive approach to a performative approach towards regulation. This brings us to another facet of the concept of language game that can help us in understanding the tensions in the financial services industry. The reference here is to the effect of terror on the language game. According to Lyotard (1984a, pp. 46), any force that works by means of the threat of eliminating the opposing player, rather than making a better move than him²⁷, is a force based on terror. Such force destroys the language game, and is therefore outside the realm of language games. In the context of the financial services industry, the basis of the regulatory framework is prescriptive utterances: prescribing the minimum standards. The basis of implementation of these prescriptive utterances is terror: "adapt your aspirations to our ends or else". One of the reasons for the tensions in the financial services industry is the reduction in the power of the regulators to terrorize the financial institutions (regulated entities) to comply with their prescriptive utterances outlined in the form of formal statement of regulations. The reduction in the ability of the regulators to terrorize the regulated by applying the threat of sanctions or to remove them from the language game, is not only linked to the globalization of the financial institutions, but also to the ever increasing size and hence the concentration of the industry by the big players that brings into play the 'too big to fail' doctrine. The reduction in the ability of the regulators to terrorize the regulated entities implies the need for a rethink of the approach towards regulations. The

²⁶Goodhart et. al. (1998, pp.83-86).

²⁷The reference is to the means of achieving the desired effect or efficiency derived from threat: "say or do this or you'll never speak again", then we are in the realm of terror, and the social bond is destroyed.

concept of language game provides a framework for evaluating alternative approaches towards regulation. One possible approach could be a shift in the regulatory strategy from prescriptive to evaluative utterances about the referent, and the inclusion of the market participants including the general public amongst the addressees, thus implies greater transparency and an improvement of the market's own self regulatory mechanism. This is the approach that forms the basis for the existence of the credit rating agencies. Although evaluative utterance is also the basis of CAMELS - the supervisory tool of the Federal Reserve Board, there is however a problem. The problem is that, unlike the rating agencies which have the markets and the general public included amongst the addressees, the regulators prefer to keep their qualitative evaluative utterances highly confidential, only allowing its own staff and those of the referent to be included amongst the addressees. The reason, or the basis on which the exclusion of the general public (the market participants and the depositors) from the list of addressees of the supervisory rating is rationalized is the possibility of bank runs. This reasoning is problematical on two counts: one, bank runs of the type experienced in USA during the 1930s have not been a major problem since the institutionalization of the safety net of deposit insurance; two, the very reason for bank runs is the contrary effect of confidentiality on the market's self-regulatory mechanism. This is because the markets are not aware of the gradual decline in the supervisory rating. It is only at the stage of full blown crisis that the public comes to know of the true picture. The reaction of the markets and the depositors in such a scenario is only natural. The real reason for confidentiality is also two fold: one, tradition: confidentiality has always been over emphasized in the banking industry. The matter has never been seriously reevaluated taking into consideration the costs and the benefits of increase in transparency in the context of the present ontological conditions. The concept of confidentiality is a convenient hiding place that can be invoked to rationalize all shortcomings and failing. In the book on financial regulations by Goodhart et. al. (1998) the concept of confidentiality has been invoked a number of times to rationalize and cover the failings of the central bank (pp. 41, 54, 55, 61, 67, 69, 211). The second reason for the confidentiality of supervisory reports is the supervisor/regulator's lack of confidence in their own ability to undertake qualitative evaluations. For example, in Goodhart et. al. (1998, pp.211) the authors, while accepting the positive/beneficial effect of increased transparency, still manage to find an excuse to rationalize a case against it: "the question of the desirable extent of transparency in the supervisory process is difficult. For example, the publication of the supervisor's own risk rating of the financial intermediaries which they supervise will increase the disciplinary effect, but may also add to risks of runs and of legal challenge (by those rated lowly)". This exclusion of the markets and the general public from the addressees of the regulator's evaluative statements reduces the effectiveness of the market self-regulatory mechanism.

Improvement of transparency is imperative in an environment where the principle of performativity is the basis of the market mechanism. This is also the rationale behind Lyotard's recommendations for computerization of the society: "**give the public free access to the memory and data banks**"²⁸ There are two arguments behind this proposal: **one**, change in function of the state: (government as the image of the society). According to Lyotard (1984a, pp.14) the economic redeployment in the current phase of capitalism, aided by the shift in technologies and techniques goes hand in hand with a change in function of the state as the image of society. The function of regulation and therefore of reproduction are being and will be further withdrawn from the administrators and be intrusted to the machines. The reference to machines by Lyotard does not imply some type of cybernetic control of society. The reference is to the use of machines for data and information storage which could be accessible to the decision makers. The decision makers who count in today's society, Lyotard (1984a, pp.14) are not the traditional political class²⁹, but a composite layer consisting of corporate leaders, high-level administrators, and the heads of major professional, labour, political, religious organization, etc.. Accessibility to information by these groups is therefore imperative for the smooth operation of the society in the postmodern era. **Two**, the effect of quantity and quality of information on the performativity, and hence the efficiency of the economy. According to Lyotard (1984a, pp. 51), it is not the accessibility to data banks that is important, what is important is the capacity to actualize the relevant data for solving problems, and to organize the data into an efficient strategy. Developing this idea further, Lyotard (1984a, pp. 51-52) points out, that as long as it is not a game of perfect information, the advantage will be with those having the knowledge and the accessibility to information. But in a game of perfect information, the advantage in terms of better performativity will be with those who can arrange the data in new ways. In the context of the concept of 'language game', this would constitute a new move. This new arrangement is usually achieved by connecting together a series of data that were previously held to be independent. This capacity to articulate what used to be separate can be called imagination. It is possible to conceive the world of postmodern knowledge as being governed by a game of perfect information in the sense that there are no scientific secrets and the data is accessible to all. In such a game, what the extra performativity depends upon is 'imagination'³⁰, which allows one either to make a new move or change the rules of the game. This is the crux of the argument

²⁸Lyotard (1984a, pp.67).

²⁹According to Lyotard (1984a, pp.14), what is new in all this is that the old poles of attraction represented by nation-states, parties, professions, institutions, and historical traditions are loosing their appeal.

³⁰Speed is considered to be a property of imagination.

for the improvement in transparency of the markets. By changing their regulatory strategy and regulatory framework from prescriptive to evaluative statements (for example, a multi-faceted rating system like CAMELS), and including the general public and the markets amongst the addressees, the regulators can help in improving the quality of the language game played by the market forces - a game played on the basis of principle of performativity.

2.3. Problematical Nature of the Theories of Social Sciences:

The regulatory framework in the financial services industry is based on the pragmatics of science, and suffers with the same problems that theories of social science suffer. This becomes apparent when we examine the pragmatics of scientific knowledge. **Science**, according to Lyotard (1984a, pp.18), is a subset of 'learning³¹'. It is also composed of denotative statements, but imposes two supplementary conditions on their acceptability:

1. The objects to which they refer must be available for repeated access, i.e. they must be accessible in explicit conditions of observation.
2. It must be possible to decide whether or not a given statement pertains to the language judged relevant by the experts.

Scientific knowledge is a subset of narrative knowledge, because it is also required to confirm to a certain disciplinary criteria. Lyotard (1984a, pp.23-24) explains the pragmatics of scientific knowledge in the context of the research game, that a new proposition when presented carries within it a set of tensions, all of which affect each of the pragmatic posts it brings into play: the sender, the addressee, and the referent. These tensions are classes of prescriptions which regulate the admissibility of the statement as 'scientific'. The first condition relates to the sender, he³² should speak the truth about the referent. This implies that the sender should be able to provide proof of what he says, and should also be able to refute any opposing or contradictory statement about the same referent. The second condition relates to the addressee, it should be possible to give (or refuse) his assent to the statement of the sender. This implies that the addressee is also a potential sender, because when he formulates his agreement or disagreement, he will also be subject to the double rules of the sender (provide proof, and refute contradictions). He is therefore supposed to have potentially the same qualities as the sender. He is his equal. The third condition relates to the referent, i.e., object of the statement. Here the rule of adequation becomes problematical. The reason:

³¹'Learning' is a set of statements, which to the exclusion of all other statements, denote or describe objects and may be declared true or false.

³²Lyotard does not use gender neutral language.

"what I say is true because I can provide the proof, but what proof is that my proof is true?" The scientific solution to the problem is based on two rules:

- **Rule one** is that, it is not that I can prove something because reality is the way I say it is.
- **Rule two** is that, as long as I can produce proof it is permissible to think that reality is the way I say it is.

The second rule is metaphysical; the same referent cannot supply a plurality of contradiction or even inconsistent proofs. Or stated differently: God is not deceptive³³. These two rules underlie what nineteenth century science calls verification and the twentieth century science calls falsification. They allow a horizon of consensus to be brought to the debate between the sender and the addressee. The basis of the consensus is the assumption that not every consensus is sign of truth, rather it is presumed that the truth of a statement necessarily draws a consensus.

This is also the basis of the objective underpinnings of the regulatory framework. Regulations like solvency ratio (capital adequacy requirements) that set the limits for minimum capital requirements as being 8 percent of total weighted assets are also based on the rules of adequation discussed above. The solvency of the bank or the adequacy of the regulatory capital is rationalized on the basis of the balance sheet position of the bank prepared by their accountant. The two of the rules of adequation comes into play: rule one is, that it is not that I can prove something because reality is the way I say it is; rule two is, that as long as I can produce proof (the balance sheet accounting value of capital) it is permissible to think that reality is the way I say it is. This argument, however, becomes problematical when we examine the difference between natural and social science. It is not God but the accountant who produces the balance sheet, and there are a number of ways of manipulating the accounts, legally as well as illegally³⁴.

The contradictory relationship between 'natural' and 'social' science becomes conspicuous when we examine the problematic of the legitimization process in science. According to Lyotard (1984, pp. 57), the relations between the scientist's statement and what the 'nature' says appear to be organized as a game without perfect information. The implication being, that the nature of

³³In natural science, nature is the referent which is controlled by God, and God is not deceptive.

³⁴Refer to Smith (1996), and Griffiths (1992) and (1995) for discussion on the legitimate techniques for manipulation of accounts. There are also illegitimate techniques for manipulating of accounts which are classified as fraud. Although one would expect the auditor, to be responsible for fraud detection, the accepted doctrine in the audit profession is that it is the management, and not the auditors who are responsible for fraud detection (Grey and Manson, 1989, pp.418). This view, however, is problematical in the context of the philosophy of audit (refer to Lee (1994), and Flint (1988), for a discussion in the philosophy of audit). It has also been challenged by St. Pierre (1983) on the basis of legal case histories where courts have put the blame for losses on account of the inability of the auditors to detect fraud. The regulators, however, appear to be oblivious of this reality.

statement produced by nature would be unpredictable. All that can be calculated is the probability that the statement will say one thing rather than the other. The problem is therefore, not to learn who the opponent is, but to identify the game it plays. This framework allows us to understand the difference between natural and social sciences. Lyotard explains the difference between natural and social science by linking it to the game played by God. If God plays the dice, then sufficient statistical regularities can be established. If, however, God plays Bridge, then the level of primary chance played by science could no longer be imputed to the indifference of the dice between which face it is up, rather it would be attributed to the cunningness of the player, or in other words, it would be left to a choice which itself would be left up to a chance between a number of possible pure strategies. The implication being, that nature is an indifferent and not a deceptive opponent, the same, however, is not true for human beings. This is the basis of the distinction between natural and human sciences. In natural sciences, nature is the referent, which is mute, but as predictable as a dice thrown a great number of times. In human sciences, on the other hand, the referent (man) is a participant in the game, one that speaks and develops strategies to counter that of the scientist. Here the kind of chance with which the scientist is confronted, is not object based or indifferent but behavioral or strategic - in other words, 'agnostic'. Thus, the metaphysical argument that forms the basis of scientific knowledge becomes problematical when the same principles are applied to social science. This also the crux of the problem with the presumed objectivity and scientific character of the quantitative ratio based regulatory framework in the financial services industry. This is why the supervisory tools like bank examination are imperative for the realization of the regulatory objectives.

This is not the only drawback in the rationale for the application of scientific approach to social science problems. Another problematical aspect relates to the visualization of the nation-state as a 'system'. This approach (nation-state as a closed system) is quite common in the socio-economic theories that form the basis of government policies. The basis of systems approach (nation-state as a closed system) lies in thermodynamics. It is based on the assumption that a system's performance can be predicted (and hence, ordered and controlled as per the principle of performativity), if all the variables are known. In social sciences the idea becomes problematical because, one, the referent is human whose behaviour cannot always be predicted; two, the complication increases with the increase in the size of the system. When nation-state is defined as the system, the application of the principle of performativity becomes very complicated. Not only is the system very large (number of variables), each variable (human being) that forms a part of the system, is in itself very complex indeed. Thus, a complete definition of the initial state of the system incorporating all the independent variables and their relationship within the system is more or less impossible. The phenomenon of globalization which has made the geographical frontiers of nation-states porous and hence rendered

the system open rather than closed, has added to the complexity of the problem. This reflects the problem with determinism which works within the framework of the unreachable, but conceivable, limit of the total knowledge of the system. To surmount the problem, a set of assumptions are introduced (by the system theorists). These assumptions are aimed at reducing the complexity of the system by reducing the number of variables and their relationship within the system. This reductionism that underlie the socio-economic theories employed by the economists, brings into focus the problematical nature of the governmental policies for the ordering and control of socio-economic system defined by the geographical boundaries of the nation-state. This argument leads to the conclusion that the idea (or ideology) of perfect control over a system, which is supposed to improve its performance is inconsistent with respect to the law of contradiction: it in fact lowers the performance level it claims to raise. This inconsistency explains the weakness of the state and socio-economic bureaucracy: they stifle the system or subsystems they control and suffocate themselves in the process (negative feedback)³⁵. This is an explanation for the problematical nature of the regulatory framework based on systems thinking, and aimed at perfect control of the system.

2.4. The Concept of Paralogy as a Source of Inspiration for the Future:

According to Lyotard (1984a, pp. 60-61), we no longer have recourse to the grand-narratives (for example, dialectic of spirits, or emancipation of humanity) as the basis for the validation of postmodern scientific discourse. Furthermore, the principle of consensus as a criterion for validation also appears to be inadequate. The assumption that the goal of language game is consensus is also not valid because consensus is only a particular state of the language game, not its end. Its end on the contrary is 'paralogy' or the search for dissent³⁶. Paralogy refers to the search for dissent, or in

³⁵An implication that can be drawn from the concept of negative feedback, is that there is no need to invoke any form of legitimization outside the system to invoke revolution against the central control of the bureaucracy (for example, the freedom of human agents inciting them to rise up against excessive authority), because the bureaucracy itself stifles and in the process suffocates itself (Lyotard, 1984a, pp.55-56).

³⁶The principle of consensus, according to Lyotard (1984a, pp.60), has two formulations: **one**, consensus is a component of the system, which manipulates it in order to maintain and improve its performance. It is the object of administrative procedures, and its only validity is as an instrument for use towards achieving the real goal, which is also what legitimates the system: 'power'. **Two**, consensus is an agreement between men defined as knowing intellects with free wills, and is obtained through dialogue. This is the form elaborated by Habermas. His conception is, however, based on the validity of the 'narrative of emancipation'. Lyotard considers it to be neither possible nor prudent to follow Habermas's lead in orienting our treatment of the problem of legitimization in the direction of a search for universal consensus through a dialogue of argumentation. In this respect, Lyotard (1984a, pp.64-66) provides three arguments one, social pragmatics do not have the simplicity of scientific

other words, the search for the unknown which in the context of the present status of knowledge may be portrayed as false knowledge. Paralogy also includes those practices that exploit the destabilization of the language games of truth in order to point to how little we really know and how much what we really do know is pure linguistic convention of an arbitrary nature³⁷.

According to Lyotard (1984a, pp. 61), consensus is a horizon that is never reached. Research that takes place under the aegis of paradigm (in Kuhn's sense) tends to stabilize; it is like the exploitation of a technological, economic, or artistic 'idea'. What is important is the fact that someone always comes around to disturb the order of reason. It is therefore necessary to recognize the existence of the power that dissents with the norm, and destabilizes its capacity for explanation, leading to the emergence of new norms for understanding³⁸. Hence, the significance of paralogy or dissent for understanding and appreciating our changing ontological landscape.

The case against 'consensus' can also be presented in the context of the pragmatics of science. According to Lyotard (1984a, pp. 64), the pragmatics of science itself provides the anti-

pragmatics. "It is a monster formed by the interweaving of various networks of heteromorphic classes of utterances (denotative, prescriptive, performative, technical, evaluative, etc.)." There is therefore, no reason to think that it would be possible to determine metaprescriptive common to all these language games, or that a revisable consensus like the one in force at a given moment in the scientific community could embrace the totality of metaprescriptions regulating the totality of statements circulating in the social collectivity. As a matter of fact, the contemporary decline in the 'narratives of legitimization' whether they are traditional or modern (for example, the emancipation of humanity, the realization of the idea, etc.), is tied to the abandonment of this belief. It is the void or vacuum created by the decline in the narratives of legitimization which the ideology of the 'system' with its pretensions (aspirations) to totality, tries to compensate, and which it expresses in the cynicism of its criterion of performance. Two, Habermas assumes that it is possible for all speakers to come to agreement on which rules or meta prescriptions are universally valid for language games. This assumption is problematical, because not only are the language games heteromorphous, they are also subject to heterogeneous set of pragmatic rules. Three, the assumption that the goal of dialogue is consensus, is problematical. The reason being, consensus is only a particular state of discussion, and not its end. Its end on the contrary is 'paralogy' or the search for dissent. These three arguments destroy the belief that still underlies Habermas's research, namely that humanity as a collective (universal) subject seeking its common 'emancipation' through the regularization of the 'moves' permitted in all language games, and that the legitimacy of any statement resides in its contribution to that emancipation. Lyotard therefore concludes that 'consensus' has thus become outmoded and suspect in value, as the goal of the language game.

³⁷In other words paralogy also points to the inadequacy of our existing knowledge which is basically of arbitrary and linguistic in nature. Derrida's philosophy of 'Deconstruction' is therefore also included within the concept of paralogy. By drawing attention to the problematical facets of our present knowledge, paralogical critiques induce and encourage us to create new knowledge. In this respect, the aim of the whole thesis can also be described as a paralogical exercise.

³⁸Or if one prefers, in a proposal to establish new rules circumscribing a new field of research for the language of science.

model of a stable system. "A statement is deemed worth retaining the moment it marks a difference from what is already known, and after an argument and proof in favour of it has been found. Science is a model of an 'open system', in which a statement becomes relevant if it 'generates ideas', that is, if it generates other statements and other game rules. Science possesses no general metalanguage in which all other languages can be transcribed and evaluated. This is what prevents its identification with the system and, all things considered with terror". Lyotard, therefore, concludes, that the division or the separation between the decision makers and the executors that exists in the scientific community today, is a fact of the socio-economic system and not that of the pragmatics of science itself. It is in fact, one of the major obstacles for the imaginative development of language.

Postmodern science, according to Lyotard (1984a, pp.60), by concerning itself with the undecidable, the limits of precise control, conflicts characterized by incomplete information, 'fracta', catastrophes, and pragmatic paradoxes, is theorizing its own evolution as discontinuous, catastrophic, non-rectifiable, and paradoxical. It is changing the meaning of the word 'knowledge'. It is producing not the 'known' but the 'unknown', and as a consequence also explaining the process of change in our ontological conditions. It is a discourse of legitimation that has nothing to do with maximized performance, rather it has its basis on difference understood as 'paralogy'. The significance of paralogy is reflected in its contribution to the pragmatics of science. According to Lyotard (1984a, pp.65), the pragmatics of science are centred on denotative utterances, which are the foundations on which it builds institutions of learning³⁹, but its postmodern development brings a decisive 'fact' to the fore: even discussions on denotative statements need to have rules. But, rules are not 'denotative' but 'prescriptive' utterances, rather the term 'metaprescriptive' utterances would be more appropriate because they prescribe what the moves of the language games must be, in order to be admissible. The function of the differential or imaginative or paralogical activity of the current pragmatics of science is to point out these metaprescriptive (science's presuppositions) and to petition the players to accept different ones. This will help in generating new ideas, or in other words new statements⁴⁰.

The question arises, whether it is possible to have a form of legitimation based solely on paralogy. The **first step** in this direction, according to Lyotard (1984a, pp.66), would be a recognition of the heteromorphous nature of language games. This implies a renunciation of terror that is implied in the assumption of language games being isomorphic and the rationale to make them so. The **second step** is the principle that any consensus on the 'rules' defining a game, and the 'moves' playable within it, must be local, i.e., it should be agreed on by its present players and

³⁹For example, institutes, centres, universities, etc..

⁴⁰It is necessarily to differentiate paralogy from innovation, because (frequently, but not necessarily) one is transformed into another.

subject to eventual cancelation (restricted not only across space, but also across time). This orientation allows a multiplicity of finite meta-arguments (i.e., argumentation that concerns metaprescriptives) to coexist. This orientation corresponds with the course of social evolution that is taking place, in which temporary contracts are supplanting the permanent institutions. This is because temporary contracts allow greater flexibility, lower costs, and most importantly, the sustenance of the creative turmoil that forms the motivation behind innovation and change. In the context of the financial services industry, the message for the regulators would be: one, to renounce the terror that is concomitant with the meta-prescriptive approach that forms the basis of the present regulatory framework; two, to acknowledge their rules (prescriptive statements) as being temporary contracts. This would allow the sustenance of the creative turmoil that forms the basis of paralogy, that is necessary for the regulations to meet the challenges of time and space compression. Perhaps the best option for achieving the regulatory objectives would be to move from a framework of 'prescriptive utterances' (laying down the rules) to a framework of 'evaluative utterances' (for example, a multi-faceted rating system like the CAMELS), with emphasis on maximization of the transparency to allow the market's self regulatory mechanism to achieve its full potency. Alternatively, if the regulators deem such a strategy to be too risky (the assumption being that the markets are too fickle to sustain prudence in purely self-regulatory environment), then a combination of prescriptive (that accepts and acknowledges the principle of paralogy as its end) and evaluative approach would be a suitable strategy for meeting the challenges of time and space compression.

Lyotard ends his discussion on the idea of paralogy as the inspiration for meeting the challenges of the future, with a point of caution, that his argument and his idea is not a 'pure' proposal for an alternative system, because any attempt at formulating and imposing an alternative would end up resembling the system it is supposed to replace. The proposal would then become a metanarrative, which would control and constrain the potential of the system.

"We should be happy that the tendency towards the temporary contract is ambiguous: it is not totally subordinated to the goal of the system, yet the system tolerates it. This bears witness to 'another goal within the system': knowledge of language games as such and the decision to assume responsibility for their rules and effects. Their most significant effect is precisely what validates the adoption of rules - the quest for paralogy⁴¹."

⁴¹Lyotard (1984, pp.66).

3. Michel Foucault

.. modernity is broadly about the massive social and cultural changes which took place from the middle of the sixteenth century, and is consequently and necessarily bound up with the analysis of industrial capitalist society as a revolutionary break with the tradition and a social stability founded on a relatively stagnant agrarian civilization. Modernity was about conquest - the imperial regulation of land, the discipline of the soul, and the creation of truth. In order to understand the contemporary critique of modernism, it is essential therefore to grasp the impact of Foucault on contemporary social theory, since it was Foucault who, through a number of brilliant studies of discourses (of psychology, penology, sexuality, and so forth) challenged the rationalist pretensions of modern systems of power."

Turner (1990, pp.4)

"Postmodernism has encouraged the view that the various fields and specialisms in the sciences are primarily strategies or conventions by which 'reality' is divided up, partly as a consequence of the intense struggle over truth by social groups in the quest for power. This view also partly explains the centrality of Nietzsche's will-to-power thesis within contemporary epistemology; the quest for truth is always the establishment of power."

Turner (1990, pp.5)

The first excerpt from Turner suggests the need to examine Foucault's in order to understand the postmodern critique of modernity. The second excerpt introduces us to the centrality of Nietzsche's will-to-power thesis in the postmodern debate. The connection between the two philosophers has already been covered in the discussion on the concept of postmodernism as a reaction to, or departure from modernism. Here we concentrate on Foucault's contribution with regard to his critique of the connection between power and truth, which he describes as "the rules of power and the powers of true discourses"⁴². The significance of Foucault's philosophical enterprise is that unlike Nietzsche, he did not simply criticize and expose the connection between truth and power, he actually made it the problematic of his investigation. He investigated into and revealed the different forms of power - power that is concomitant with the truth of law; power that is connected to repression; power that is connected to knowledge; and power that is connected to our bodies and their use, etc.. The aim of this section is to examine the various forms/concepts of power presented by Foucault, and the dialectical relationship between some of them. The aim is to apply Foucault's ideas for examining the tensions in the financial services industry, tensions that are connected to the

⁴²Foucault (1980b, pp.94).

dialectic of power between the regulator and the regulated. The discussion to follow has been divided into three sub-sections. The first sub-section is on the circular relationship between power and truth; the second sub-section investigates into the underpinnings that form the basis of Foucault's conceptualization of power; and the final sub-section (three) involves an examination of the various concepts of power that emerge from his investigation into the problematic of power, and the dialectical relationship between the two most important forms of power: the 'sovereign power' and the 'disciplinary power', and their connection with the tensions in the financial services industry.

3.1. The Circular Relationship Between Power and Truth:

According to Foucault (1980b, pp.93), in every society, there are manifold relations of power that permeate, characterize, and constitute the social body, and these relations of power cannot themselves be established, consolidated, or implemented without the production, accumulation, circulation, and functioning of a discourse of truth. Foucault thus, draws our attention to the connection between 'power' and the 'discourse of truth'. The connection is two fold: one, the power that is concomitant of the discourses given the status of truth. As Foucault (1980b, pp.94) observes, we are "subjected to truth in the sense in which it is truth that makes the laws, that produces the true discourse which, at least partially, decides, transmits and extends itself upon the effects of power. In the end, we are judged, condemned, classified, determined in our undertakings, destined to a certain mode of living or dying, as a function of the true discourses which are the bearers of the specific effects of power". Two, a consequence of this position of preeminence accorded to discourses of truth, is the 'production' of truth or discourses of truth as a 'means' for acquiring 'power'. In other words power (or rather, the pursuit of power) encourages us to produce truth, or as Foucault (1980b, pp.93) observes, "Power never ceases its interrogation, its inquisition, its registration of truth: it institutionalizes, professionalises, and rewards its pursuit." Thus, by connecting truth with power, Foucault not only revealed the circular relationship between power and truth, but also the consequences of this relationship. One can either accept to be governed by the discourses of truth, or acquire power by producing discourses of truth. Or as Foucault puts it "we are constrained or condemned to confess or to discover the truth".

The circular relationship between power and truth is also discernable in the financial services industry where the regulator holds the reign of power as the sovereign dispenser of truth. This status of the regulator has recently come under attack. The reference is to the initiative by J.P.Morgan with RiskMetrics that led to the decision by the Basle Committee of Banking Supervision to allow the proprietary VAR (Value at Risk) approaches of the banks to be incorporated into the capital

adequacy regulations of the G10 countries. Now J.P.Morgan repeated the same strategy with CreditMetrics. It is only a matter of time before it is also allowed to be incorporated within the regulatory framework⁴³. Foucault's discourse on the circular relationship between power and truth allows us to understand the significance of J.P.Morgan's strategy. In effect, what J.P.Morgan did with RiskMetrics and CreditMetrics was to acquire power by producing the 'truth', while at the same time challenging the status of the regulator as the sovereign producer and dispenser of truth.

3.2. The Underpinnings:

The underpinnings of Foucault's concepts of power lies in the methodological approach that he applies in his investigation into the concept of power. The three key methodological principles that form the basis of his research have already been discussed in Chapter Six in the context of Foucault's genealogical analysis of knowledge as the source of inspiration and the underpinning of power of the concept of postmodernism as a reaction to, or departure from modernism. These are: One, a systematic scepticism about all anthropological universals (and those of humanism that artificially creates and maintains the rights, privileges, and nature of human beings as the immediate and timeless truth of the subject), in order to investigate their historical constitution; two, a reversal of the philosophical approach of ascending towards the 'constituting subject' who is asked to account for every possible object of knowledge in general. Instead, to study the '**concrete practices**' through which the subject is constituted within a field of knowledge (i.e., the process of subjectification); and three, to address 'practices' as the domain of analysis, i.e. to examine the ensemble of ways of doing things through which the real is given shape.

To understand the underpinnings that form the basis of Foucault's concept(s) of power we need to connect these methodological principles to the theoretical concept of power. Perhaps the most common concept of power that we know is the concept of sovereign (royal) power. The reason, according to Foucault (1980b, pp.94), being that the juridical edifice of the Western world was constructed on the concept of sovereign power. The essential role of the theory of right, from medieval times onwards, was therefore, to fix the legitimacy of power of the sovereign. This is the main problem around which the theory of right and sovereignty is organized. When we talk about rights, we imply:

- The legitimate rights of sovereignty.

⁴³This is the opinion of Richard S. Dale (1997, pp.1) .

The technical documentation of RiskMetrics and CreditMetrics are available at J.P.Morgan's web-site (www.jpmorgan.com).

- And the legal obligation to obey it.

The reason theory of sovereignty has continued to exist (after the dissolution of monarchy), not only as an ideology of right, but also as the organising principle of the legal codes which Europe acquired in the 19th century beginning with the Napoleonic code, is because it guarantees to everyone, by virtue of the sovereignty of the state, the exercise of their proper sovereign rights. In other words the juridical systems in terms of its codification as well as its theorization, have enabled sovereignty to be democratized through the constitution of a public right in terms of a collective sovereignty⁴⁴. The concept of parliamentary democracy based on theory of sovereignty is what Hobbes project in 'Leviathan' is all about. Leviathan is a fabricated man, an amalgamation of certain number of separate individualities, who find themselves reunited by the complex of elements that go to compose the state; but at the heart of the state, there exists something which also constitutes it, and this is 'sovereignty' which Hobbes describes as the 'sprit' of Leviathan. This is also the key problem which all jurists try to explore: the idea of "the distillation of a single will - or rather, the constitution of a unitary, singular body animated by the sprit of sovereignty - from the particular wills of a multiplicity of individuals"⁴⁵. Foucault however finds this approach/pursuit of the jurists problematical. The reason being, it ignores the nature, the form, the operational apparatus and elements, and the effects of the application of power. According to Foucault, we should direct our researches, not towards the juridical edifice of sovereignty, or the state apparatus and the ideologies which accompanies them, but towards the nature of power, the domination and the material operators of power, towards forms of subjection, and inflections and utilizations of their localized systems, and toward their strategic apparatuses. Putting it another way Foucault's message is, that we must eschew the model of 'Leviathan' in the study of power, we must escape from the limited field of juridical sovereignty and state institutions, and instead base our analysis of power on the study of the techniques and tactics of domination⁴⁶, i.e., the emphasis should be on the application of power.

Foucault (1980b, pp.95), explains the general aim of his project on the 'problematic of power' as "to reverse the mode of analysis followed by the entire discourse of 'right' from the time of middle ages", by giving due weight to the fact of 'domination' and "to expose both its latent nature and its brutality". His aim was: one, to reveal 'right' as an instrument of domination; and two, to show the extent to which, and the forms in which 'right' transmits and puts into motion relations that are not relations of sovereignty, but those of domination. By 'right', Foucault implies, not

⁴⁴Foucault (1980b, pp.105)

⁴⁵Foucault (1980b, pp.97)

⁴⁶Foucault (1980b, pp.102).

simply the laws, but the whole complex of apparatuses, institutions, and regulations responsible for their application. And by 'domination', Foucault implies, not the domination of the king in his central position, but that of his subjects in their mutual relations; not the solid or global form of domination that one person exercises over the other, or one group over another, but the manifold forms of dominations that can be exercised within a society. In other words, it is not the domination implied in the uniform edifice of sovereignty, but the multiple forms of subjugation that have a place and function within the social organism that is the subject of Foucault's research⁴⁷. Putting it another way 'rights' should not be viewed in terms of a legitimacy to be established, but in terms of the methods of subjugation that it instigates. Foucault (1980b, pp.96) therefore describes the system of rights and the domain of law as, "the permanent agents of these relations of domination, these polymorphous techniques of subjugation. The problem for Foucault was therefore, to study the theme of rights while avoiding the central question of the theme: the question of the legitimacy of sovereignty, and the obedience of the individual subjects. The strategy that Foucault applies to surmount the problem, involves substitution of the problem of 'sovereignty and obedience' with 'domination and subjugation'. It involves the examination of the practices rather than the theoretical edifice of the problematic of right⁴⁸.

⁴⁷Foucault (1980b, pp.96).

⁴⁸To push forward his line of analysis Foucault applies his five methodological precautions (1980b, pp.96-102). These methodological precautions are important because they explain the basis of Foucault's discourse of power. Each of these is briefly discussed below:

One, instead of examining and analyzing power in terms of the regulated and legitimate forms of power in their central locations, the general mechanisms through which they operate, and the continual effects of these, our analysis should be concerned with power at its extremities, in its ultimate destination (i.e., in its more regional and local forms and institutions). Instead of trying to discover where and how the right of punishment is founded on sovereignty, and how it is presented in the theory of monarchical right, or the democratic right, we should focus on the way punishment and the power of punishment are effectively embodied in a certain number of local institutions which are actually involved in the exercise of punishment. In other words we should try to relocate our analysis of power at the extreme points where it is exercised, where it is always less legal in character.

Two, instead of examining the power at the level of conscious intension or decision, we should examine power at the point where its intension, if it has one, is completely invested in its real and effective practices. In other words the need is to study power in its external visage, at the point where it is in direct and immediate relationship with its object, its target, its field of application. It is here where it installs itself and produces its real effects. In other words rather than asking why certain people want to dominate, what do they seek, what is their overall strategy, we should instead ask how things work at the level of ongoing subjugation. Instead of examining how the sovereign appears to us in its lofty isolation, we should try to analyze and examine the subjects in terms of how they are constituted through a multiplicity of organisms, forces, energies, materials, desires, thoughts, etc.. We should try to grasp subjection in its material instance as a constitution of subjects. This would be the exact opposite of Hobbes project in 'Leviathan'. According to Foucault (1980b, pp.98), rather than worrying about the problem of the central spirit, we must attempt to study the large number of bodies

In the context of the tensions in the financial services industry, Foucault's message is very clear. Instead of emphasizing on the legal framework of regulations and the language of regulations, our emphasis should be on the principles and the problems of regulatory enforcement⁴⁹: the concept

which are constituted as peripheral subjects as a result of the effects of power.

Three, instead of examining power as phenomenon of one's individual consolidated and homogeneous domination over the other, or that of one group or class over others, or in terms of the difference between those who exclusively possess and retain it and those who do not have it and submit to it, power should be analyzed as something which circulates, or functions in the form of a chain. It is never localized here or there, never in anybody's hand, never appropriated as a commodity or a piece of wealth, rather power is employed and exercised through a net like organization. Not only do the individuals circulate between its threads, they are always in the position of simultaneously undergoing and exercising this power. They are not only its consenting target, but they are always also the elements of its articulation.

Four, The statement that 'power establishes a network through which it freely circulates', does not imply that we should undertake a descending analysis of power beginning/startling from its centre and aimed at the discovery of the extent to which it permeates into the base, of the degree to which it reproduces down to and including the most molecular elements of our society. Instead, we should conduct an 'ascending' analysis of power starting from its infinitesimal mechanisms each of which have their own history, their own trajectory, their own techniques and tactics, and then see how these mechanisms of power have been and continue to be invested, colonized, utilized, involuted, transformed, displaced, extended, etc. by ever more general mechanisms and by forms of global domination. What needs to be investigated is a historical analysis of the functioning of the mechanisms of power beginning from the lowest level. What needs to be investigated is how these mechanisms of power, at a precise moment, after undergoing certain number of transformation, became economically advantageous and politically useful, and as a consequence, all of a sudden, came to be colonized and maintained by global mechanisms and the entire state system. Such an analysis would indicate that it was the micro-mechanisms of power (the apparatuses of surveillance, the medicalization of sexuality, madness, delinquency, etc,) which from a certain moment of time, and for reasons which need to be studied, came to reveal their political usefulness and to lend themselves to economic profit, and therefore appeared to be of interest to the bourgeoisie, and hence was colonized by the global mechanisms of the state.

Five, what has taken place cannot be said to be ideological. It involves the production of effective instruments for the formation and accumulation of knowledge. It includes methods of observations, techniques of registration, procedures of investigation and research, and apparatus of control. The implication is, that the power which is exercised through these subtle mechanism, can only evolve, organize, and put into circulation a knowledge, or rather apparatuses of knowledge, which are not ideological constructs.

⁴⁹One consequence of the inadequate attention paid to the enforcement of the regulations is: theory failure. Theory failure is a concept that is different from the concepts of market failure and regulatory failure. It relates to the disjunction between the aims of the regulations and its enforcement. This is the area of investigation of Diver (1980) who applies a framework involving both, a top-down, as well as, bottom-up perspectives on regulatory enforcement. The import of the article is that the success or indeed the wisdom of regulatory interventions into the market depends upon the capacity of the policy makers as well as managers to harness those organization forces to their social vision. For this, it is necessary to synthesize both the perspectives (from the top looking down, and from the bottom looking up) into organizational strategies.

of supervision - where the intentions laid out in the language of the regulations are put into practice⁵⁰. The most important facet of the supervisory process is the bank examination in which the supervisor/regulator visits the banks to undertake a qualitative as well as a quantitative examination of the bank's operations, its financial position, the quality of its internal control procedures for control of risks, the quality of bank management, the soundness of the bank, future prospects, etc.. It is the process through which the supervisors/regulators not only scrutinize regulatory compliance by the bank, but also try to remove the information asymmetry between them and the bank management - beyond that which can be identified in the accounting data. Perhaps the best known and the most powerful of all supervisory tools is the US Federal Reserve Board's CAMELS Rating system⁵¹ which forms the basis of their supervisory actions. In the context of regulatory enforcement, strangely enough, the example of US Federal Reserve is an exception rather than a rule. It is only lately (in the last couple of years) that the banking regulatory community has finally realized the importance of regulatory enforcement or supervision for the safety and soundness of the banking system. The publication of the twenty five core principles on banking supervision released by the Basle Committee on Banking Supervision (1997), and Bank of England's (1997) risk based approach to banking supervision: RATE (CAMEL and COM), are examples of a positive change in the regulatory/supervisory philosophy.

3.3. Forms of Power:

This section involves a discussion on the various forms of power identified by Michel Foucault. The discussion to follow has been divided into seven sub-sections, of which the first six cover the six different forms of power identified by Foucault: one, the concept of Sovereign Power; two, the Marxist concept of Power; three, the concept of Power as Repression; four, the concept of Power as War, a War Continued by Other Means; five, the War - Repression, or Domination - Repression concept of Power; and six, Disciplinary Power. Of these, the first (sovereign power) and the final (disciplinary power) forms of power are relevant for examining and understanding the dialectic of power between the regulators and the regulated (financial institutions) in the financial services industry. The final sub-section (seven), therefore, involves an examination of the dialectical relationship between sovereign power and disciplinary power, and its implications for the financial services industry.

⁵⁰This is an area where academic output is, unfortunately, relatively scarce.

⁵¹In January 1997 the CAMEL system was revised to add a sixth component to the rating - sensitivity to market risk. CAMEL has now, therefore, become CAMELS.

3.3.1. Sovereign Power

The concept of sovereign power is important because it forms the basis of the regulatory framework in the financial services industry, and the problems and the limitations with sovereign power are also discernable in the regulatory framework.

The Concept: According to Foucault (1980b, pp.93), in every society the relationship between power, right, and truth is organized in a highly specific fashion. The basis of the organization of this relationship is the discourse of truth. The essential function of the discourse of truth is to lay down the law (or the rules of right) which provides the formal delimitation of power (i.e., fix the limits to the rights of power). The theory (or the discourse of truth) that forms the basis of sovereign power is the classical juridical theory of power, which defines power as a right⁵²:

- which one is able to possess like a commodity
- and which as a consequence can either wholly or partially be transferred through a legal act or through a contract.

Power according to this concept is therefore the concrete power which every individual holds, and whose partial or total cession/transfer enables political power or sovereignty to be established. The theoretical construction is based on the idea that the constitution of political power obeys the model of a legal transaction involving a contractual type of exchange⁵³. This implies that the theory of sovereignty can also be presented in the form of a contract - oppression schema: power as an original right that is given up in the establishment of sovereignty, and the contract as the basis of political power provides its points of articulation. The power so constituted risks becoming oppression whenever it over-extends itself (i.e., it goes beyond the terms of the contract). Sovereign power is therefore a contract power with oppression as its limit. This implies that as long as the power is within limits, it is legal. It becomes illegal and hence oppression if and when it transgresses these limits. Thus, under the contract-oppression schema, which is based on the juridical theory of power, the pertinent opposition is between legitimate and illegitimate⁵⁴.

To understand the concept of sovereign power, it is also necessary to understand the concept of 'law' which is also the principal mode of representation of sovereign power⁵⁵. 'Law', according

⁵²Foucault (1980b, pp.88).

⁵³Hence the analogy between: 'power and commodity', and 'power and wealth' that runs through all these theories. Thus we have a political power whose formal model is discoverable in the process of exchange - the economic circulation of commodities.

⁵⁴Foucault (1980b, pp.91-92).

⁵⁵Foucault (1980d, pp.140-141).

to Foucault (1980d, pp.141), is neither the truth of power nor its alibi, it is an instrument of power which outlines the limits of our rights (the rights of the sovereign, as well as the subjects), i.e. the difference between legality and illegality. This concept of law as an instrument of power which outlines the limits of our rights has positive as well as negative connotations. On the positive side, law as an instrument of power, by outlining the difference between legality and illegality underwrites a schema of power which is homogeneous for every level and domain. On the other (negative) side, the concept of law as an instrument of power that outlines the limits of our rights, induces a negative image of power (for example: refusal, limitation, obstruction, censorship). It induces an image of power as that which says 'no'. It also allows the fundamental operation of power to be thought of as that of the act of speech: enunciation of law, discourse of prohibition. The manifestation of power takes on the pure form of "thou shall not". And the challenging of power can be conceived to appear only as a transgression. Such a notion results in the reduction of power to that of a relationship between master and his slave. The master being one who pronounces law and speaks the truth, or the master who censures and forbids⁵⁶. It is this negative connotation of power represented as law, that gives the penal system the image of an apparatus of prohibition and repression of one class over another, or as an alibi for the lawless violence of the ruling class. This connotation, according to Foucault, however, is not necessarily true. The actual basis for the existence of the penal system is that of a mode of political and economic management which exploits the difference between legality and illegality⁵⁷.

The Emergence and the Development of Sovereign Power: The basis of power, as well as, the basis of legal thought in the Western societies since the medieval times, has been the traditional theory of sovereignty (which is rationalized on the basis of the classical juridical theory of power), which enables the foundation of absolute power in the body of the monarch as the sovereign. The 'right' in the West is the 'King's right', the mechanism of power and the legal system in the West have therefore been developed in response to the demands of Royal power and to serve it as its instrument⁵⁸. It was, however, around the 12th century that the juridical edifice of the Western world in the form of theory of sovereignty was constructed through the resurrection of the Roman Law⁵⁹. In other words, it was the resurrection of Roman law that played the technical and constitutive role

⁵⁶Foucault (1980c, pp.139).

⁵⁷Foucault (1980d, pp.140-141).

⁵⁸Foucault (1980b, pp.94).

⁵⁹which had collapsed with the fall of the Roman Empire

not only in the establishment of the authoritarian, administrative, and absolute power of the monarchy, but also as an instrument for the construction of large scale administrative monarchies. In the later centuries, the theory of sovereignty became a weapon - an instrument of political and theoretical struggle either to limit, or else to reinforce royal power⁶⁰. When it was used in positive light, it was used to justify the nature of the juridical armoury that invested royal power, to reveal the monarch as the effective embodiment of sovereignty, to demonstrate that his absolute power was appropriate for his fundamental right. When it was used in negative terms, it was used to justify the need to impose limits upon this sovereign power, the need for submitting the sovereign and his sovereign power to certain rules of rights, within whose confines it has to be exercised in order for it to be legitimate. The essential role of the theory of sovereignty, from medieval times onwards, was therefore, to fix the legitimacy of power of the sovereign. Or as Foucault (1980b, pp.95) observes, "when it comes to the general organization of the legal system in the West, it is essentially with the King, his rights, his power and its eventual limitations, that one is dealing." Whether the jurists were the King's henchmen or his adversaries, it was the royal power that they spoke about when they spoke of the grandiose edifices of legal thought and knowledge.

In the eighteenth century, with the birth of parliamentary democracy, the same theory of sovereignty was reactivated through the doctrine of Roman law (whose essentials we find in the writings of Rousseau and his contemporaries), but now with a difference. Now it was concerned with the construction of an alternative model of parliamentary democracy as against its use in administrative, authoritarian, and absolutist monarchies. The reason theory of sovereignty has continued to exist (after the dissolution of monarchy), not only as an ideology of right, but also as the organising principle of the legal codes which Europe acquired in the 19th century beginning with the Napoleonic code, is because it guarantees to everyone, by virtue of the sovereignty of the state, the exercise of their proper sovereign rights. In other words the juridical systems in terms of its codification as well as its theorization, have enabled sovereignty to be democratized through the constitution of a public right in terms of a collective sovereignty⁶¹.

3.3.2. Marxist Concept of Power:

The Marxist concept of power, according to Foucault (1980b, pp.88-89), is based on the economic functionality of power. Power is conceived primarily in terms of the role it plays in the maintenance

⁶⁰From the 16th century onwards (including the times of wars of religion), the theory of sovereignty was used as the basis of political struggle by the catholic monarchists as well as protestant anti-monarchist; by the aristocrat as well as the parliamentarians (Foucault, 1980, pp.103).

⁶¹Foucault (1980b, pp.105).

simultaneously of: the relations of production, and the relations of class domination, which the development of specific forms of forces of production has rendered possible.

3.3.3. Power as Repression:

Foucault (1980b, pp.90) develops this concept of power by extending, as well as, negating the Juridical concept of power. He lays out a proposition, that power is neither given or exchanged, nor recovered, but is rather 'exercised'. It only exists in action. If power is exercised, then the question arises, what sort of exercise does it involve. One possible answer is: power is essentially that which represses. Power represses nature, instincts, class, individuals, etc.. This concept is important because it directs our attention to the question or the underpinnings that formed the basis of Foucault's investigation of power. If power is an organ of repression, should'nt the analysis of power begin with an examination of the mechanisms of repression?

3.3.4. Power is War, A War Continued by Other Means:

Foucault (1980b, pp.90) develops this concept of power from the Marxist concept of power. He lays out a proposition, that power is not primarily linked to or required for the maintenance and reproduction of economic relations, but is above all a 'relation of force'. And if power is the way in which the relations of force are deployed and given concrete expression, then instead of analyzing it as a transferable contract or its functionality in terms of the maintenance of relations of production, should'nt we analyze it primarily in terms of struggle, conflict, and war. This question and this proposition forms the basis of the concept of power as: 'power is war, a war continued by other means'. This is primarily a reversal of Clausewitz's assertion that 'war is politics continued by other means'. This reversal of Clausewitz's assertion implies that during the reign of peace the role of the political power would be to perpetually re-inscribe this relation (disequilibrium relation of power between forces) through a form of unspoken warfare⁶². It also implies that the political struggles, the conflicts waged over power, with power, for power, the alterations in the relations of forces, the favouring of certain tendencies, the reinforcements, etc., that come about within the 'civil peace' should not be interpreted as anything but the continuation of war. They should be understood as episodes, factions, and displacements in the same war. Even when one writes the history of peace and its institutions, it is always the history of war that one is writing⁶³. This form/concept of power

⁶²This is apparent in the social institutions, in economic inequalities, and even in our bodies.

⁶³There is also a third implication. According to Foucault, the end result can only be the outcome of war, i.e., of a contest of strength, to be decided by recourse to arms. Only a final battle of this kind would put an end, once and for all, to the exercise of power as continual war. The political battle

can serve as a powerful tool for analyzing the politics of interest groups. It may also be applicable (to some extant) for understanding the competition/struggle between market forces that forms the basis of the market mechanism. It may also be applicable for understanding the regulator-regulated dialectic which is the cause of the tensions in the financial services industry.

3.3.5. The War-Repression or Domination-Repression Concept of Power:

This concept of power emerges from the combination of the concept of power as repression⁶⁴ and the concept of power as war, a war continued by other means⁶⁵. The connection between the two concepts is 'repression' - repression could be viewed as the political consequence of war⁶⁶. Under this approach, 'repression' does not occupy the place that 'oppression' occupies in relation to the contract in the classical theory of political right, which is seen as the abuse of sovereignty in the juridical order. 'Repression' is not the abuse, but is on the contrary, the mere effect and continuation of a relation of domination. According to this view, repression is none other than the realization, within the continual warfare of this pseudo-peace, of a perpetual relationship of force. Here the pertinent opposition is not between legitimate and illegitimate as in the case with juridical concept of power, but between struggle and submission⁶⁷. This form of power may be applicable for analyzing dictatorships or non-pluralist democracies in multi-ethnic nation-states. In the context of the markets, it may be applicable to monopolies or oligopolies maintained with the implicit

would cease with this final battle. This interpretation by Foucault is, however, problematical, because what is described as the final battle, would in effect be perceived as a final battle by the victor. It would lead to the creation of a new disequilibrium which can only be sustained through continual war. It would only be a final battle if it subsequently leads to the dismantling of the disequilibrium. The only way out of this problem of disequilibrium lies in the concepts of 'pluralism' and 'empathy'.

⁶⁴Foucault refers to this as Reich's hypothesis. Wilhelm Reich (1897-1957) was a psychoanalyst who broke from the Freudian school, developing a theory in which neuroses (mental disorder producing hysteria, anxiety, depression, obsessive behaviour) resulted from repressed, undissipated feelings or sexual energy. He expounded on the necessity for regular orgasms for the mental health of both men and woman. During the sexual revolution of the 1960s, he became something of a cult figure in USA.

⁶⁵The basis of this relationship of power lies in war (the hostile engagement of forces). Foucault refers to this as Nietzsche's hypothesis. Nietzsche is revered for his 'Will to Power' hypothesis, according to which the quest for truth is always for the establishment of power. 'Facts' are only 'interpretations'. The derive behind interpretations is the 'will to power' - to compel all others to accept his perspective as norm and hence truth (Nietzsche, 1968, No.481, pp.267).

⁶⁶Foucault (1980, pp.91).

⁶⁷Foucault (1980b, pp.91-92).

imprimatur of the political forces (the market regulators). It may also be applicable to the situation where the political forces (regulators) reign supreme, and the market forces are very weak.

3.3.6. Disciplinary Power:

The concept of disciplinary power is a relatively new phenomenon⁶⁸. It is connected with the emergence of the bourgeois society. According to Foucault (1980b, pp.103-104), as long as a feudal type of society survived, the mode in which power was exercised could be defined in its essentials, in terms of the sovereign-subject relationship. In other words, the relationship of sovereignty, whether interpreted in a wider or a narrower sense, encompassed the totality of the social body⁶⁹. This changed in the 17-18th century with the emergence of the bourgeois society and the invention of a new form of power: the disciplinary power. Foucault (1980b, pp.105) describes disciplinary power as one of the great inventions of the bourgeois society, and a fundamental instrument in the constitution of industrial capitalism and the society that developed with it. Disciplinary power is a form of power that differs radically from sovereign power, it is a power which lies outside the form of sovereignty, and cannot be described in terms of the theory of sovereignty. Disciplinary power, according to Foucault (1980b, pp.104), entails a completely new mechanism of power based on highly specific procedural techniques, completely novel instruments, and quite different apparatuses. It is a mechanism of power which allows the codification of continuous surveillance. It is a mechanism of power which allows for the calculation of power in terms of the minimum expenditure for the maximum return, i.e. the principle of performativity. It is a mechanism of power which is dependent upon bodies and their operations, rather than upon the earth and its products. It is a mechanism of power which permits time and labour, rather than wealth and commodities to be

⁶⁸It is a new phenomenon in the sense of its invention and/or emergence which is connected to the emergence of the bourgeois society. It is also a new phenomenon in the sense of the concept of 'disciplinary power' becoming a part of our knowledge base. Foucault was the first person to uncover the existence of this power which forms a very important facet of our present ontological conditions. The basis of the discovery of this form of power was the realization by Foucault (1980b, pp.92) that none of the above mentioned concepts of power were adequate for explaining the power formation that is connected to the emergence of the history of penal right, psychiatric power, control of infantile sexuality, etc.. The mechanisms that were brought into operation in these power formations were something much more than repression. The notion of repression, although a very important facet of the concept of power, is wholly inadequate for the analysis of the mechanisms and effects of power that is so pervasively used to characterize the present era. This was the basis of Foucault's search for a new concept of power - the search that led to the development of the concept of 'disciplinary power'.

⁶⁹The problems to which the theory of sovereignty was addressed were in effect confined to the general mechanisms of power, to the way in which its forms of existence at the higher level of society influenced its exercise at the lowest levels.

extracted from bodies. It is a mechanism of power which is constantly exercised by means of surveillance, rather than in a discontinuous manner by means of a system of levies or obligations distributed over time. It is a mechanism of power which is dependent upon a tightly knit grid of material coercions, rather than the physical existence of a sovereign. It is a mechanism of power which introduces a genuinely new economy of power, a form of power that is ultimately dependent upon the principle that "one must be able simultaneously both to increase the subjected forces and to improve the force and efficacy of that which subjects them⁷⁰".

Disciplinary power is connected to knowledge (savoir) itself. Since disciplines operate not only as the receptacles of knowledge, but also as the machinery of knowledge production, therefore the power of the disciplines, and hence the force of the disciplinary power can be connected to the expanse and the efficacy of knowledge (savoir) itself. Also, because disciplines differ according to their domains of knowledge, disciplinary power, may therefore, also take a variety of forms. According to Foucault (1980b, pp.106), disciplines have their own discourse - they engender apparatuses of knowledge (savoir) and a multiplicity of new domains of understanding. Disciplines are the bearers of a discourse, this discourse, however, is not a discourse of right, it has nothing in common with that of law, rule, or sovereign will. Disciplines may involve discourses that speaks of 'rules', but these rules are not juridical rules derived from sovereignty, rather they are natural rules or norms. The codes that they come to define are not that of law, but that of normalization. Their reference (and hence the basis of their power) is to a theoretical horizon which has nothing in common with the edifice of right, rather they are based on human sciences which constitutes their domain, and clinical knowledge which is their jurisprudence⁷¹.

In the context of the tensions in the financial services industry the concept of disciplinary power is very important. Three reasons can be cited: one, the connection between disciplinary power and knowledge (savoir) - the speed-up in the momentum of knowledge generation adds to the efficacy and the potency of the disciplinary power; two, the connection between disciplinary power and entrepreneurialism - the application of the mechanisms of disciplinary power to achieve commercial advantage in the marketplace; and finally, the incompatibility between disciplinary power

⁷⁰Foucault (1980b, pp.104).

⁷¹Foucault's research was based on mental patients, prison systems, sexual attitudes, etc.. This is the basis for the reference to 'clinical knowledge' as the 'jurisprudence' of disciplinary power. His ideas regarding the concept of disciplinary power are, however, applicable to other fields of knowledge too. An excellent example is the paper by Ezzamel (1991) which is based on the domain of accounting and the disciplinary power that is concomitant with the knowledge of accounting. The paper comprises of a case study demonstrating the disciplinary power of accounting knowledge in resisting, as well as, influencing an organizational change.

and sovereign power. It is the dialectical relationship between disciplinary power and sovereign power which lies at the heart of the tensions in the financial services industry. This is the area of investigation of the next section.

3.3.7. Dialectical Relationship Between Sovereign and Disciplinary Power:

According to Foucault (1980b, pp.106), the emergence of disciplinary power is important because it marked a major paradigm shift in the character of the society that developed from the nineteenth century onwards up to this day, a society that is characterized by:

- On one hand by a legislation, a discourse, an organization based on public right, whose principle of articulation is the social body and the delegated status of each citizen.
- On the other hand, by a closely linked grid of disciplinary coercions, whose purpose is, in fact, to assure the cohesion of this same social body.

Although the theory of right is a necessary companion of this grid (of disciplinary coercions), it cannot in any event provide the terms of its endorsement. These two limits (right of sovereignty and mechanisms of discipline) which define the arena in which power is exercised, are so heterogeneous that they cannot possibly be reduced into each other. Disciplinary power is in every aspect the antithesis of the mechanism of power transcribed by the theory of sovereignty. The key difference between the sovereign power and this new kind of power (disciplinary power), is that sovereign power is more closer to the power that is exercised over the earth and its products (**bio-power**) than that over human bodies and their operations. The theory of sovereignty refers to the displacement and appropriation on part of power, of goods and wealth, but not of time and labour. It allows discontinuous obligations distributed over times to be given legal expressions, but it does not allow the codification of continuous surveillance. It enables power to be founded in the physical existence of the sovereign, but not in continuous and permanent systems of surveillance. The theory of sovereignty, according to Foucault (1980b, pp.105), permits the foundation of an absolute power in the absolute expenditure of power. It does not allow for a calculation of power in terms of the minimum expenditure for the maximum return, i.e., the principle of performativity. The powers of a modern society are, therefore exercised through, on the basis of, and by virtue of, this very heterogeneity between a public right of sovereignty and a polymorphous disciplinary mechanism.

Foucault's conceptualization of sovereign power and disciplinary power, and the dialectical relationship between the two allows us to analyze and understand the tensions in the financial services industry. The power of the regulators and their regulatory code is dependent upon, and as a matter of fact is a part of the sovereign power of the nation-state. The power of the financial institutions (the regulated) on the other hand is connected to disciplinary power. The strengths and

the weaknesses (or limitations) of each of these forms of power is also apparent in the strengths and the weaknesses (or limitations) of the regulators and the regulated. The regulator-regulated dialectic in the financial services industry is actually a reflection of the encounter between sovereign power and disciplinary power. The strength of the regulators is connected to the strength/efficacy/potency of the sovereign power of nation-state within the global community of nations, and is limited to the geographical periphery of its frontiers. The strength of the financial institutions (the regulated) on the other hand is connected to their disciplinary power which is connected to knowledge and their competitive position in the marketplace. The consequence of globalization for the regulators has been the reduction in the strength/efficacy/potency of sovereign power of the regulators to order and control the financial institutions (the regulated). The consequence of globalization for the financial institutions on the other hand has been an increase in their size, power, and their ability to arbitrage between the nation-states. The disciplinary power of the financial institutions (the regulated) has also been augmented by the speed-up of the process of innovation and entrepreneurialism, both of which are connected to the increase in pace of knowledge generation.

Foucault explains the consequence of the increasing force of the disciplinary power, and the consequence of the encounter between disciplinary power and sovereign power, that at some point of time, the mechanisms of disciplinary power become politically and economically useful, and are therefore incorporated within the global mechanism of law and maintained by the entire state system. In this respect Foucault observes: "these techniques and these discourses to which the disciplines gives rise, invade the area of right so that the procedures of normalization come to be ever more constantly engaged in the colonization of those of law⁷²". This is Foucault's explanation for the global functioning of the 'society of normalization'. In the context of the financial services industry, the accounting codes that are a part of the regulatory framework, are actually codes of normalization that, at some point of time, were incorporated within the legal codes. Regulations like capital adequacy ratio are therefore actually based on the mechanisms of discipline (for example, accounting ratios) which have been incorporated within the legal codes. This also explains the gradual change in the regulatory framework and the structure of regulations that we are experiencing in financial services industry.

The incorporation of rules of normalization into legal codes leads to a number of problems, problems that are apparent in the regulator-regulated dialectic and the tensions in the financial services industry. Four of them are worth discussing: one, such rules of normalization (disciplinary codes) are based on knowledge and need to be updated regularly with the developments in knowledge. The problem with such rules of normalization that are transformed into legal codes, is

⁷²Foucault (1980b, pp.107).

the risk of becoming frozen in time and becoming outdated and incompatible in the context of the present knowledge base, and the present state of market development. This problem is quite evident in the financial services industry, and is a major cause of tensions between the regulators and the regulated; two, the rules of normalization that are a part of disciplinary power are required to be exercised continuously. The problem with sovereign power is that it is analogous to bio-power, and therefore involves the levy of discontinuous obligations over time; three, the problem with legal codes is that they lay out the limits between legality and illegality. This allows the regulated entities to prospect for loopholes within the law, and use the loopholes in the text of the law to bypass the context of the law, while remaining within the text of the law. Putting it another way, as long as you are within the limits defined by the law, you have the right to bypass the spirit or the (objective) of the law. This is a very important facet of the problem of regulatory dialectic; and four, the problem with law is that it has a negative feel to it. It is analogous to power that says no. Conversion of rules of normalization into legal codes lead to the loss of the positive aspect of power - power that creates knowledge, power that creates desire. As a consequence, these rules of normalization, after their conversion into legal codes, appear to have a negative feel to them. They appear to be repressive, and therefore provoke resistance. The tensions in the financial services industry are an evidence of this problem.

The question is, what is the answer to this problem? One possible answer to the problem that is already a part of the regulatory arsenal lies in supervision. The most important of the supervisory tools is the bank examination, which is a part of the remit of supervisory activity which the regulator/supervisor applies to bridge the gap between sovereign and disciplinary power, and the inadequacies that are a part of their regulatory framework. But, examination, in itself is a mechanism of disciplinary power. To understand and appreciate the power and the potency of the examination system as a disciplinary tool, one needs to understand and appreciate its three key attributes: **one**, '**hierarchical observation**', examination system in its modern institutional form makes possible the control of the individuals examined through a system of micro-penalty (good and bad marks). This apparatus of 'uninterrupted examinations' places individuals examined in a whole field of surveillance. In this respect examination is an exercise in hierarchical observation⁷³; **two**, '**normalizing judgement**', the system of examination also generates an archive in the form of written performances and review records which allow one to generate case-histories of each individuals examined and also to classify them into categories, and eventually into 'populations' with

⁷³Hoskin (1995, pp.5).

norms. In this respect examinations can be described as an exercise in normalizing judgement⁷⁴; and three, ‘mathamaticized model of reality’, the principle of assigning quantitative marks to a given quality implies that it is possible to weigh-up and compare the individuals examined across space, and to some extant also across time⁷⁵.

All these attributes are also inherent in the system of bank examinations carried out by the regulators/supervisors. But examination in itself is a form of disciplinary power, and to have its effect, it has to be combined with another very powerful disciplinary mechanism. The reference is to Foucault’s interpretation of the ‘principle of panopticon’. The ‘principle of the panopticon’⁷⁶ involves the reversal of the ‘principle of the dungeon’. It allows daylight and the overseer’s gaze to capture the inmate rather than the darkness of the dungeon which affords, after all, a sort of protection. The principle of the panopticon involves the construction of two buildings.

1. A perimeter building in the form of a ring.
2. A tower placed in the centre of the perimeter building having large windows opening on to the inner face of the ring (parameter building).

The outer building or the parameter building is divided into cells, each of which traverses the whole thickness of the building. These cells have two windows. One opening on the inside facing the window of the central tower, and the other (the outer one) allowing daylight to pass through the whole cell. All that is needed for the purpose of overseeing, is to put an overseer in the tower, and place in each of the cells of the parameter building the person to be overseen (for example the lunatic, the patient, the convict, the worker, etc.). The back lighting (from the outer windows)

⁷⁴Hoskin (1995, pp.5).

⁷⁵Discussing the history of examination system, Hoskin (1995, pp.12) describes the **allocation of quantitative marks to individual questions as the most momentous step in the development of the educational system** - a step that revolutionized education and transformed the society over a relatively short period of time. This happened in about 1792. This step which Hoskin describes as the ‘mathamaticized model of reality’ was a major breakthrough which made the science of the individual feasible.

⁷⁶‘Panopticon’ refers to the doctrine of English philosopher Jeremy Bentham who in 1787 conceived the idea of the ‘panopticon’ or the inspection house as a model for any type of institution intended to exert control over the actions of human beings. The idea was applied in the design of prisons and some hospitals. Bentham himself envisioned to apply the idea to schools, orphanages, etc.. It may be noted that Bentham’s invention was a machine for dispensing ‘Newtonian justice’ - the fruit of enlightenment’s morality - a new and positive form of relationship between the society and those of its members subjected to new and total forms of moral correction. Foucault views the panopticon as an architecture, or a machine, or an idea that induces in the inmate, a state of conscious and permanent visibility that assumes the automatic functioning of power. The concept of panopticon thus represents yet another form of power - power linked to transparency (Stewart, 1995).

enables one to pick out from the central tower what the people within these cells of the parameter building are doing⁷⁷.

Foucault views the panopticon as an architecture, or a machine, or an idea that induces in the inmate, a state of conscious and permanent visibility that assumes the automatic functioning of power. The concept of panopticon thus represents yet another form of power - power linked to transparency. Foucault (1980e, pp.152) therefore connects the concept of panopticon with Rousseau's dream behind the French revolution. According to Foucault, Rousseau's dream that motivated many of the revolutionaries was the dream of a transparent society. A society that is visible and legible to each of its parts, the dream that there should no longer exist any zones of darkness, for example, zones established by the privileges of royal power or the prerogatives of some corporations, or zones of disorder. It was the dream that each individual, whatever position he occupied might be able to see the whole of society, that men's hearts should communicate, their visions be unobstructed by obstacles, and the opinion of all reign over each.

According to Foucault (1980e, pp.152) Bentham's vision is the same as that of Rousseau, as well as, its opposite. Bentham looks at the problem of visibility only in terms of a visibility organized entirely around a dominating overseeing gaze. He looks at it as a project of universal visibility which exists to serve a rigorous, meticulous power. According to Foucault, it is Bentham's obsession and his technical idea behind the exercise of 'all-seeing' power that can be grafted on to the great Rousseauist theme of transparency. There is a phrase in panopticon "each comrade becomes an observer", Rousseau (according to Foucault) would have reversed the phrase to "each observer should become a comrade". In the context of the financial services industry, the present regulatory framework is based on Bentham's vision of panopticon, that the markets should be subjected to the domineering gaze of the regulator/supervisor. The present global framework of cooperation and collaboration between the regulators (especially in the context of sharing of information which was the basis of Basle Concordat) also appears to be a manifestation of Bentham's vision that 'each comrade becomes an observer'. There is a need to transform the regulatory framework, which is (presently) based on Bentham's obsession and his technical idea, into Rousseau's dream (each observer becomes a comrade) which is also the basis of the market's own self regulatory mechanism.

To understand the principle behind market's self regulatory mechanism, it is necessary to understand the principle behind the French revolution and its link with Bentham's panopticon. In this respect, Foucault (1980e, pp.153) observes: "The new aspect of the problem of justice, for the revolution, was not so much to punish the wrong doers, as to prevent even the possibility of wrong doing, by immersing people into a field of total visibility where the opinion, observation, and

⁷⁷Foucault (1980e, pp.146).

discourse of others would restrain them from harmful acts. This idea is constantly present in the texts of the revolution." The principle of the revolution was to remove areas of darkness that were negative to the principle of transparency and visibility which the revolution aimed to establish. The aim was to set up a mode of operation through which power could be exercised by virtue of the mere fact of things being known and people seen in a sort of immediate, collective, and anonymous gaze - a form of power which would refuse to tolerate areas of darkness. Bentham's project provides a formula applicable to many domains - the formula of 'power through transparency', or 'subjection by illumination'. The cost-benefits of the system are also obvious: "There is no need for arms, physical violence, material constraints - just a gaze. An inspecting gaze, a gaze which each individual under its weight will end by interiorizing to the point that he is his own overseer, each individual thus exercising this surveillance over, and against, himself. A superb formula: power exercised continuously and for what turns out to be a minimal cost⁷⁸". This is the rationale for the improvement of the market's transparency. In the context of the financial services industry, prudential governance will be self generating when the banks/securities firms know that the supervisory reports of their bank examination are open to the gaze of the others in the marketplace.

4. Jacques Derrida:

Derrida's deconstruction⁷⁹ has already been introduced earlier in the discussion on the concept of postmodernism as 'a reaction to, or departure from modernism'. There the emphasis was on the concept, and the basis of power of deconstruction as a philosophical thought providing the source of inspiration and the underpinning of power for the concept of postmodernism⁸⁰. Here the aim is

⁷⁸Foucault (1980e, pp.155).

⁷⁹My first encounter with Derrida's philosophical text was 'Writing and Difference', reading which was a very difficult exercise. The reason being, to understand and appreciate Derrida's works, it is necessary to undertake an in-depth prior reading, as well as, a concurrent parallel reading of the text being deconstructed along with the reading of Derrida's deconstructive analysis of that text. My own understanding of Derrida's philosophy of deconstruction is primarily based on the books and papers written by other authors on the concept of deconstruction, rather than Derrida's own philosophical works. The key texts that have facilitated my understanding and appreciation of Derrida's philosophy and his methods are Norris (1991), Caputo (1997), and Linstead (1993), besides Derrida (1997), and Derrida (1995) which consists of interviews and conversions with Derrida on the various aspects of his philosophy. No reference has been made to Derrida's philosophical texts because they mainly involve the exercise of deconstruction on various texts.

⁸⁰As a 'reaction to, or departure from modernism'.

two fold: one, to introduce the concept of deconstruction as a philosophical thought and as an idea in the broad sense, in the sense that forms the basis of the title of this thesis; and two, the concept of deconstruction in the narrow sense, in the sense of the actual strategy applied by Derrida for deconstructing the texts of other philosophers.

4.1. Deconstruction as a Philosophical Thought:

Caputo (1997, pp.54-55) describes the aim of deconstruction as a philosophical thought as: to achieve new enlightenment by questioning the axioms and certainty of the old enlightenment, for it may be that what the (old) enlightenment seeks cannot be found on the basis (foundations) that the (old) enlightenment lays⁸¹. The effect of this new enlightenment would be not to jettison reason but to redefine and redescribe it, for example, by steering clear of the simple opposition of reason and faith and seeing the extent to which reason is deeply saturated by faith; not to jettison emancipation, but to continue to seek it in places that were overlooked by the old enlightenment. Deconstruction implies the continuation of the struggle for emancipation, but by other means. It involves taking a second look at the things that the old enlightenment devalued. Deconstruction is not a demolition or destruction, but a way of releasing and responding, of listening and opening up, of being responsible not only to the dominant voice of the great masters, but also to the other voices that speak more gently, and more discreetly⁸². Deconstruction, according to Derrida (1997, pp.6), is made up of not the mixture but the tensions between memory, fidelity, the preservation of something given to us, and at the same time, heterogeneity, and something absolutely new, and a break. As a philosophy of institutions, deconstruction is, while suspicious of institutional power, aimed at making institutions livable, open-ended, porous, and structured round programs that do not try to program everything. The aim of deconstruction is to open up the institution to its own future⁸³. If reason and philosophy are about the right to ask questions about all that which we hold sacred, then in deconstruction it is reason and philosophy itself that comes into question.

Deconstruction is not aimed at creating tensions. It is not aimed at instigating transformation and change, although it does indirectly take part in the process of change, by laying out the problematical facets of the institutional structures undergoing transformation and change, and the forces at play in the change. Deconstruction as a philosophical thought, is aimed at understanding

⁸¹Deconstruction is therefore not anti-enlightenment.

⁸²Caputo (1997, pp.57).

⁸³Caputo (1997, pp.50).

the tensions that emanate from the transformations and change, so as to be able to respond to the challenges of the change with utmost responsibility. Whenever anything haloed and sacred comes into question in deconstruction, be it religion or law, science or democracy, knowledge or philosophy, it is in response to the tensions that already exist within the structure of these realms of knowledge. There is already a process of auto-deconstruction under way within these realm of knowledge. Derrida's deconstruction is aimed at making this process of auto-deconstruction explicit, deconstruction is therefore, not about destroying or creating tensions in the text. Deconstruction, according to Derrida (1995b, pp.413), "finds itself at the heart of what you call 'tensions'. It is a question of assuming these tensions, of 'living' them as much as of 'understanding' them. ... Those who fear and wish to deny the inescapable necessity of these transformations try to see in deconstruction the agent responsible for these changes, when in my eye it is above all else a question of trying to understand them, of interpreting them, so as to respond to them in the most responsible fashion possible." This is also the basic rationale of the thesis: to understand and to interpret the tensions so as to be able to respond to them in the most responsible fashion possible. In postmodernism the concept of text is very broad. It covers not only the work of an author, but the whole realm of human thought and action can be included within the concept of text. In the context of the title of the thesis, the whole regulatory framework in the financial services industry can be conceptualized as a text. It can be further extended to incorporate the whole of the financial services industry (including the regulators, the regulated, the markets, and the market participants, and their activities), in which the regulator-regulated dialectic itself may be viewed as a deconstructive process at work in the text, the tensions being only an indicator of this process. The basis for the choice of the hypothesis that forms the driving force behind the philosophical analysis of the tensions in the financial services industry, is to examine and understand the auto-deconstructive process that is under way in the financial services industry, to open up the closures in the regulatory institutions (and their regulatory framework), and to generate ideas that may help in opening up the regulatory institutions to their future.

Having examined the concept of deconstruction in the broad sense (as a philosophical thought) and its connection to the thesis, we can now begin our examination of the concept of deconstruction in the narrow sense - the strategy applied by Derrida to deconstruct the texts of other philosophers.

4.2. Derrida's Deconstruction Strategy:

Deconstruction is not a method, Derrida himself refuses to call it a method. One reason why Derrida refuses to describe deconstruction as a method, is because once it is defined or labelled as a method, a certain closure is applied to the concept, which acts as a braking force against its further evolution and development. Derrida is also sceptical about referring to deconstruction as a concept with a hierarchical structure, because once a term is fixed within a given explanatory system, it loses its radical insights⁸⁴. There is another and more important reason for not labelling or describing deconstruction as a method or a precise concept. It relates to the aim of deconstruction - the message that Derrida wants to convey through his deconstruction exercise. The aim is to examine the philosophical texts given the status of truth and to ask the question: "How is this truth effect achieved?"⁸⁵ The aim is to open up the closures in the text to expose the precariousness of the discourses that were revered as truths. If truth is the solidification of metaphors, then Derrida's deconstruction strategy can be described as the process of melting those truths in order to return them to their fluid state as a 'metaphors' to reveal their metaphoric origin. Deconstruction in the narrow sense, may therefore be conceptualized as the strategy or the critical process that Derrida employs vis.a.vis various philosophical texts, to melt them and return them to their fluid state as 'metaphors'.

The following is an account of the strategy or the critical process applied by Derrida to deconstruct the text of other philosophers⁸⁶. The discussion to follow has been divided into two sections: one, an examination of the elements of Derrida's deconstruction strategy; two, an examination of the two movements that are central to Derrida's deconstruction strategy.

4.2.1. Elements of Derrida's Deconstruction Strategy:

In this section we examine the two key elements that form the basis of the Derrida's deconstruction strategy. These are:

- (i) The concept of 'supplementarity'.
- (ii) The concept of 'metaphysics of presence', represented by the term 'differance'.

(i) The Concept of 'Supplementarity': The basis of Derrida's concept of 'supplementarity' lies in the recognition (and as a consequence the understanding and appreciation) of the relationship of power or oppositional logic of identity between the terms (or the words) used in any text.

⁸⁴Norris (1991, pp.32).

⁸⁵Hassard and Parker (1993, pp.xii).

⁸⁶This account is based on the description of the deconstruction process outlined by Linstead (1993).

- Although the positively valued term requires an understanding of its binary opposite (the negatively valued term) for achieving its meaning, the latter is suppressed. Examples of binary opposition are, white-black, good-bad, good-evil, hero-villain, God-Satan, profit-loss, asset-liabilities, regulator-regulated, etc..
- Although the binary opposites interpenetrate each other, they are treated as though they exist in hierarchy, a dualism, a relationship of power in which one term at any moment is dominant over the other.
- Central to Derrida's concept of 'supplementarity' is the recognition that the relationship between the two terms (the binary opposites) is not a partitioning of the unlikes, rather it is a joining⁸⁷ - a mutually supportive pivotal point around which the meaning of the word turns. The other word (the binary opposite or the dual) is needed to complete the meaning of the first term.
- Thus, it is not oppositional, but rather a relationship of supplementarity that exists between the two terms. Derrida, therefore, reconceptualizes the oppositional 'either/or' relationship with a 'both/and' relationship of supplementarity.

Supplementarity is, therefore, a subversive quality in which a term is necessarily inhabited by its opposite, and hence possesses the potential for its own corruption. Derrida, therefore, emphasizes the need to recognize the problematic nature of the positive term by placing it 'under erasure' - crossing it, but allowing it to remain legible, thus undermining the fixed appearance of the term, while at the same time acknowledging its necessity as a heuristic however inadequate. Where modernity pursues the opposition of terms, actively placing one over and against the other, thus rationalizing the marginalization of the trace of the dual (i.e. the binary opposite) in order to achieve a definite closure of meaning, postmodernity resist the closure of meanings, examining the 'other' term as well, and actively exploring the relationship of supplementarity between the two terms.

(ii) The Concept of 'Metaphysics of Presence' Represented by the Term 'Difference':

'Difference' is a term coined by Derrida by combining the terms 'deference' and 'difference' to explain the concept of 'metaphysics of presence' - a concept developed as a response to the problem of reflexivity.

- The concept 'metaphysics of presence' implies that no writing, utterance, and text can guarantee its own truth, and must necessarily resort to a meta-level of reference to derive its authority.

⁸⁷Each term is supported by the other to achieve its meaning.

- Any sign, thus ‘defers’ (yields) to another level of meaning, and simultaneously ‘defers’ (postpones) its presence. For example ‘writing’ denotes the absence of ‘speech’, and ‘word’ denotes the absence of the ‘object’ it is supposed to represent.
- Taking the example of the relationship between the ‘word’ and the ‘object’ it is supposed to represent, we know that the ‘word’ denotes the absence of the ‘object’ it is supposed to represent. In other words, the object ‘defers’ (i.e., yields to and postpones its presence) to the ‘word’ that represents it. At the same time, the ‘word’ also ‘differs’ from the object it is supposed to represent. Thus, the ‘word’ takes a life of its own which is not controlled by any referential link. Thus, the world we know is the world as represented, reality being undecidable.

The concept of ‘metaphysics of presence’ represented by the term ‘differance’ involving a combination of ‘deferring’ and ‘differing’, thus implies the continual never-fixed movement, a play of spacing within the text which keeps the meaning of the text in flux, and hence dynamic⁸⁸.

This forms a part of the process that Derrida calls deconstruction which is founded on an understanding of the concepts of ‘supplementarity’ and ‘metaphysics of presence’ represented by the term ‘differance’. Linstead (1993, pp.57), therefore, describes deconstruction as the process which Derrida applies as a way of:

- revealing the contradictions, and hence tensions inherent in the text,
- a means of exposing their logocentrism⁸⁹,
- their reliance on the metaphysics of presence,

⁸⁸This is also the basis of the concept of ‘metaphor’. Metaphor (for example, machine rationality, life as a journey, etc.) ‘defers’ (yields) to another level of meaning, and ‘defers’ (postpones) its own presence. At the same time its literal meaning also ‘differs’ from the object that the metaphor is supposed to represent. Thus the metaphor takes a life of its own. That is why Gareth Morgan (1996, pp.239) describes metaphor as a distinctly postmodern concept - a concept that has an inherent tendency to deconstruct itself, and the knowledge it generates. Morgan (1996, pp.234) describes metaphor as being truly postmodern, because the dialectical tensions between truth and falsehood implied in any metaphor demands a self-critical form of imagination and understanding. The inherent falsity of metaphor encourages a healthy scepticism of the way we view knowledge, and open our social constructions of reality to a kind of continuous deconstruction and reconstruction. The understanding of the role and the functioning of the metaphor in the creation of knowledge, obliges us to be aware of the blind spots and the biases that the use of metaphor creates. At the same time its inherent falsity and limitations act as catalysts for the further development of knowledge. This is because, no metaphor can ever bring closure, its inherent falsity and limitations define the frontiers for the generation of new debate and insights.

⁸⁹Logocentrism refers to a proposition that claims legitimacy by reference to some externally universal truthful propositions (i.e., a priori concepts).

- and of revealing their inescapable qualities of ‘differance’ and ‘supplementarity’ despite repressive textual strategies.

Derrida, therefore, while attempting to open up the closures of the texts he studies (by entering into them and using their own terms against them), attempts to avoid setting up a meta-level of critical terms that can become incorporated into the logocentrism he critiques⁹⁰. Two movements of deconstruction are therefore central to Derrida’s critique: ‘overturning’ and ‘metaphorization’. This is the area of examination of the next section.

4.2.2. Movements in Derrida’s Deconstruction strategy:

Two movements are central to Derrida’s deconstruction strategy: one, ‘overturning’; and two, ‘metaphorization’.

(i) Overturning: This is the first movement in Derrida’s deconstruction strategy in which he focuses on the binary opposition of terms existing in hierarchy in which one is suppressed. Unfortunately most deconstruction exercises involve only this first movement - the overturning of the binary hierarchy. This is where Derrida’s deconstruction differs from that of the others. His deconstruction exercise involves a second movement too: ‘metaphorization’.

(ii) Metaphorization: Metaphorization entails the recognition that the positively valued term, at any moment is defined only by contrast to the negatively valued term, and that they interpenetrate and inhabit each other. In Derrida’s writings, this emerges as a ceaseless movement between terms - giving his work an elusive quality which is an essential feature of his project. By keeping the hierarchy in process of flux, he introduces an element of undecidability into the structure and meaning of the text. This is an essential feature of Derrida’s text. Metaphorization is necessary to keep the process in motion, and to resist its degradation and the ossification into structure.

According to Linstead (1993, pp.55), Derrida’s deconstruction aims to point to the ways in which philosophy has rested its claims on reason, method, structure, and other concepts without acknowledging their metaphorical nature because of the risk to its own project in attempting to think beyond logocentrism. Derrida always attempts to expose this by working from within. He attempts to provoke this structure of concepts, by demonstrating the paradoxes of ‘differance’ and ‘supplementarity’ which affect it, thus bringing it down gently under its own weight. He applies the

⁹⁰This is because, although deconstruction seeks to avoid the mystifications of other texts, it itself is trapped within the pragmatics of language and is bound to share some of the blind-spots and traps which it exposes in other writings. There is, therefore, no solid independent ground on which the deconstructionist can stand, and the method of deconstruction can be applied to its text as well.

same tools used by the text (on which he works) to subvert its expressed function, and thus illustrates its problematical nature.

What is the significance of Derrida's philosophy for the financial services industry? In the context of the concept of deconstruction in the broad sense (i.e., as a philosophical thought), the whole thesis itself is an attempt to find an answer to the question. In the narrow sense (i.e., as a strategy or a method), Derrida's deconstruction strategy cautions us to recognize and realize the problematical concept of 'representation'. It points to the problems with the language in conveying its meaning. Accounting which is the language of finance, is after all a language⁹¹, and suffers from the same problems as those faced by any other language in conveying its meaning. The concepts of 'supplementarity' and 'differance' applies to the 'accounting' language as well. The bottom line accounting figures like the values of capital, asset, liability are all part of a whole framework which itself is based on certain assumptions and certain mechanical rules which differ across different regulatory regimes. While the Basle Committee on Banking Supervision has harmonized the capital adequacy regulations, it has ignored the difference in the accounting framework across different regulatory regimes, especially in the context of the framework for the provisions for loan loss, Bettie et. al. (1995) provide a number of examples in this respect. The implication being, the notion of Basle's Capital Adequacy Regulation as being the global standard of minimum safety buffer is problematical.

Some of the problematical aspects of the accounting and auditing framework have already been discussed earlier, and will therefore not be repeated here. Derrida's strategy of deconstruction cautions us that the concept of 'supplementarity' and 'differance'⁹² apply to the accounting figures as well. It cautions us not to accept bottom line accounting figures like capital, assets, liabilities, profits, and losses as statements of truth. They should be placed under erasure - crossing them, but allowing them to be legible, thus undermining their truth value. It cautions us not to accept accounting figures on face value as a statements of truth. Accounts should be viewed as discourses of truth that need to be deconstructed⁹³.

⁹¹The same analogy can be applied to mathematics as a language of quantitative science.

⁹²which is representative of the concept of 'metaphysics of presence'.

⁹³The very rationale of auditing is the verification and validation of the accounting information. This is also the aim of deconstruction. The incidence of audit failure, and the existence of expectation gap between the users of financial statements and the auditors, implies that even audited accounts cannot be relied upon as statements of truth. It draws attention towards a very significant market failure where regulatory intervention may be justified. Unfortunately, not much attention has been given to this problem by the regulators in the financial services industry.

5. Conclusion:

As in the case with Chapter Six, the driving force behind this chapter was also Part II of the hypothesis:

One: the tensions reflecting the regulatory crisis in the financial services industry may be a subset of, or a part of a much wider area of tensions/crises facing the conceptual foundations of the regulatory philosophy: the modernist philosophical thought.

Two, the alternate philosophical thought which is generally described as postmodernism, may provide us with inspiration and ideas for the formulation of a regulatory strategy and regulatory framework that may facilitate the achievement of regulatory objectives while facilitating the amelioration of the tensions inherent in the financial services industry.

The aim was to examine of the philosophy of the three great philosophers of the postmodern philosophical thought, Jean-Francois Lyotard, Michel Foucault, and Jacques Derrida, in order to draw inspiration and ideas from their philosophy. The aim was to apply the insights generated from their philosophy for understanding and perhaps (to some extent) resolving some of the tensions in the financial services industry. It is after all the way we perceive the problem, that forms the basis of the strategies that we develop for meeting the challenges created by the problem. In this respect, examining Lyotard's philosophical work 'The Postmodern Condition: A Report on Knowledge', was important because Lyotard's work is a 'report on knowledge', in which he introduced us to a host of concepts that help in broadening our knowledge base, and improving our ability to understand and appreciate the world and the problems of the world around us. Five important facets of Lyotard's philosophical work discussed in this chapter are worth repeating:

- One, the idea of postmodernism as modernism at a nascent stage and this stage is constant, implying a permanently revolutionary mode of philosophical thought which reflects the suitability of postmodernism as a philosophical thought for meeting the challenges of the rapidly changing ontological conditions being fuelled by the Schumpeterian entrepreneur.
- Two, the concept of postmodernism as incredulity towards metanarratives, a development that is connected to the development of the principle of performativity. This is important in the context of the financial services industry, because the principle of performativity has become the basic criterion for the operations of the market forces (the regulated). The same, however, is not true of the regulators whose operational framework is still based on the metanarrative apparatus of legitimization⁹⁴, hence the rationale for the tensions in the financial services industry.

⁹⁴The reason being, that the philosophical foundation of the regulatory framework is based on the modernist philosophical thought.

- Three, the notion of society as a ‘language game’, an idea, a tool for analysis, that has been developed by combining the concept of ‘language’ as the basis of social bond, and the concept of ‘game theory’ to explain the actions of the players or the participants in the language game. The concept of ‘language games’ allows us to understand the different forms of statements (for example: denotative, prescriptive, evaluative, performative, etc.), and their effects on the language game. It also allows us to understand the ‘agnostic’ aspect of the society which forms the basis for the materialization of change in a society. In the context of the financial services industry, the regulatory dialectic, and the gradual change in the regulatory framework and regulatory philosophy we are experiencing, can be connected to the agnostic countermoves of the financial institutions (the regulated). The best example of the agnostic aspect of the society is J.P.Morgan’s initiative with their Value at Risk framework ‘RiskMetrics’ which led to the development of the pre-commitment approach toward regulation - a change from ‘prescriptive’ approach to a ‘performative’ approach towards regulation. The concept of ‘language games’ also allows us to understand the contrary effect of ‘prescriptive’ approach to regulation, and the possible beneficial effect of a change in regulatory strategy from ‘prescriptive’ to ‘evaluative’ approach to regulation, on the quality of the language game played by the market forces⁹⁵ - a game played on the basis of principle of performativity.
- Four, the problematic nature of the theories of social science which is based on a blind application of methods of natural science to social problems, and the notion of nation-state as a system (a notion that finds its basis in the laws of thermodynamics) which encourages the development of a meta-framework for the ordering and control of the system.
- Five, the idea of paralogy and not consensus as a source of inspiration for the future. This is because paralogy lays stress on dissent or the search for the unknown rather than the known, thereby encouraging us to think differently, think creatively for meeting the challenges of the rapidly changing ontological conditions. This is also the message of the thesis for the regulators.

Foucault’s work on power is connected to our thesis because the regulator-regulated dialectic is, after all, a dialectic of power. Three aspects of Foucault’s work on the dialectic of power were examined:

⁹⁵The quality of the language game, and as a consequence, the efficacy of the market’s own self regulatory mechanism would only improve if the markets and the general public are included amongst the addressees of the supervisory evaluation reports.

- One, the circular relationship between truth and power, which implies that we either accept the power of truth and comply with the requirements outlined in the discourses of truth, or acquire power by producing discourses of truth. In the context of the regulator-regulated dialectic in the financial services industry, the initiative of J. P. Morgan with reference to RiskMetrics (and now with CreditMetrics) which led to the development of the pre-commitment approach towards regulation was an initiative to acquire power through the production of discourse of truth and challenge the status of the regulator as the sovereign dispenser of truth.
- Two, the underpinnings of Foucault's philosophy which is based on an examination of the actual practices in the application of law, rather than the juridical edifice of law. In the context of the regulation in the financial services industry, this implies the need for shift in emphasis from the legal framework of regulation and the language of regulations to principles and problems of regulatory enforcement: the concept of supervision. In other words, the emphasis should be on 'supervision', where the intensions laid out in the language of the regulations are put into practice. It is only lately (in the last couple of years) that the banking regulatory community has finally realized the importance of regulatory enforcement or supervision for the safety and soundness of the banking system. The publication of the twenty five core principles on banking supervision by the Basle Committee on Banking Supervision (1997) represents a positive change in the regulatory/supervisory philosophy.
- The third aspect of Foucault's philosophy examined involved an investigation into the various forms of power and the dialectical relationship between sovereign and disciplinary power. The power of the regulators is based on the sovereign power of the nation-state, and is connected to law as the instrument of power. The power of the regulated (financial institutions) on the other hand is based on disciplinary power, and is connected to knowledge and the apparatuses of knowledge as the instrument of power. The implication being, that the dialectical relationship between regulators and the regulated is actually a manifestation of the dialectical relationship between sovereign and disciplinary power. This is important because examination of the dialectic of power between the sovereign and the disciplinary forms of power allows us to understand the dialectic of power between the regulators and the regulated. This is also important because one of the problems with the regulatory framework in the financial services industry is that it is based on codes of normalization (which are a part of disciplinary power) which at certain point of time in our history were

converted into legal codes. This is important, because the conversion of rules of normalization into legal codes, leads to a number of problems. Four of them are important:

- One, such rules of normalization (disciplinary codes) are based on knowledge and need to be updated regularly.
- Two, the rules of normalization that are a part of disciplinary power are required to be exercised continuously.
- Three, the problem with legal codes is that they lay out the limits between legality and illegality, thus allowing the regulated entities to prospect for loopholes within the law, and use the loopholes in the text of the law to bypass the context of the law, without bypassing the text of the law.
- Four, conversion of rules of normalization into legal codes lead to the loss of the positive aspect of power - power that creates knowledge, power that creates desire.

A possible answer to these problems that is already a part of the regulatory arsenal lies in supervision. The most important of the supervisory tools which the regulator/supervisor applies to bridge the gap between sovereign and disciplinary power, is the bank examination. But examination in itself is a form of disciplinary power, and to achieve the desired supervisory objectives, it needs to be combined with another form of disciplinary power: Foucault's interpretation of the principle of 'panopticon': power through transparency, which implies the need for the regulators to share the results of their bank examination with the markets and the general public in order to maximise the disciplinary potential of the market's own self regulatory mechanism.

Derrida was the third philosopher whose philosophy was explored. Two approaches were applied to examine his philosophy: one, the concept of deconstruction in the broad sense, i.e., as a philosophical thought (in the sense that forms the basis of the title of this thesis); and two, the concept of deconstruction in the narrow sense, in the sense of the actual strategy applied by Derrida for deconstructing the texts of other philosophers.

- First, the aim of deconstruction in the broad sense. The aim of deconstruction as a philosophical thought is to achieve new enlightenment by questioning the axioms and certainty of the old enlightenment, for it may be that what the (old) enlightenment seeks cannot be found on the basis (foundations) that the (old) enlightenment lays. As a philosophy of institutions, deconstruction is, while suspicious of institutional power, aimed at making institutions livable, open-ended, porous, and structured around programs that do not try to program everything. The aim of deconstruction is to open up institutions to their own future.

Deconstruction is not aimed at creating tensions. Deconstruction as a philosophical thought, is aimed at understanding the tensions that emanate from the transformations and change. There is already a process of auto-deconstruction under way, Derrida's deconstruction is aimed at making this process of auto-deconstruction explicit. In the context of the financial services industry, the regulator-regulated dialectic itself may be viewed as a deconstructive process at work in the text, the tensions being only an indicator of this process. The basis for the choice of the hypothesis that forms the driving force behind the philosophical analysis of the tensions in the financial services industry, is to examine and understand the auto-deconstructive process that is already under way in the financial services industry. The aim is to generate insights and ideas that may help to open up the closures in the regulatory institutions and their regulatory framework, thus opening up the regulatory institutions to their future.

- The second approach applied to examine Derrida's philosophy of deconstruction was the concept of deconstruction in the narrow sense, i.e., deconstruction as the strategy that Derrida applies to deconstruct the text of other philosophers, where the aim is to examine the philosophical texts given the status of truth and to ask the question: "How is this truth effect achieved?" Derrida's aim is to open up the closures in the text to expose the precariousness of the discourses that were revered as truths. If truth is the solidification of metaphors, then Derrida's deconstruction strategy can be described as the process of melting those truths in order to return them to their fluid state as 'metaphors' (i.e., to reveal their metaphoric origin). In the context of the tensions in the financial services industry, Derrida's deconstruction strategy cautions us to recognize and realize the problematical concept of 'representation'. It points to the problems with the language in conveying meaning. Accounting which is the language of finance, is after all a language, and suffers from the same problems as those faced by any other language in conveying its meaning. It is based on a framework grounded on certain assumptions and certain mechanical rules which differ across different regulatory regimes. The difference in the accounting framework across different regulatory regimes, especially in the context of the framework for the provisions for loan loss implies that the notion of Basle's Capital Adequacy Regulation as being the global standard of minimum safety buffer is problematical. Furthermore Derrida's strategy of deconstruction cautions us that the concept of 'supplementarity' and 'differance' apply to the accounting figures as well. It cautions us not to accept bottom line accounting figures like capital, assets, liabilities, profits, and losses as statements of truth. They should be placed under erasure - crossing them, but allowing them to be legible, thus undermining their

truth value. It cautions us not to accept accounting figures on face value as a statements of truth. Accounts should be viewed as discourses of truth that need to be deconstructed.

PART

IV

**THE PROBLEMATIC OF
TIME AND SPACE COMPRESSION**

The Rationale:

When I first investigated into the concept of globalization about four or five years ago, literature on globalization was relatively scarce, especially in the area of economics and finance where the term ‘globalization’ was used primarily as a label for analyzing the trends in international trade, foreign currency transactions, primary and secondary cross border trading in bonds and equity securities, cross border portfolio investments, etc., and drawing conclusions regarding the consequences of these trends. Not much effort was made towards theorizing the concept of globalization (in the literature on finance and economics). At the same time, however, there was an emerging literature especially in the disciplines of politics, sociology, and geography where an effort was made towards theorizing about the concept and implications of globalization. Since then, the literature on globalization has (literally speaking) exploded, and the label of ‘globalization’ has become a ubiquitous label, but the situation in finance and economics in terms of theorizing the concept of globalization has remained more or less the same. Most of the literature in finance and economics on globalization still deals with the trends and possible consequences of the trends, which can be pigeonholed into a few categories. The area of business studies, sociology, politics, and geography, however, has seen the emergence of some excellent literature which allows us to understand and appreciate some facets of our rapidly changing ontological conditions (some of the significant examples being, globalization as a form of institutionalisation of the two fold process involving the universalization of particularism and the particularisation of universalism¹, globalization as hybridization², etc.). However, in spite of the explosion of literature on globalization, I have found the concept of globalization in itself, to be incomplete in terms of understanding and appreciating the dynamics of change that we are experiencing. It over-emphasizes the spatial dimension and under-emphasizes the temporal dimension. I consider the term ‘time-space compression’ as a more appropriate label for investigating into and understanding the change that we are experiencing.

My preference for ‘time-space compression’ over ‘globalization’ as a label for investigating into the dynamics of change that we are experiencing is on two counts: one, it allows us a greater latitude for examining our ontological reality. It allows us to examine our ontological conditions in

¹Robertson (1991) discusses globalization in terms of the thematization of four elements of human conditions. Two of these are particularistic elements: individuals and societies; and two are universalistic elements: the system of societies and the human kind (the species aspect). The late twentieth century globalization involves the institutionalization of both the universalization of particularism (individuals, and societies), and the particularisation of universalism (the system of societies and the humankind).

²The view of globalization as a process of hybridization that gives rise to global melange (Pieterse, 1994).

the context of 'space-time' as a single dimension, it also allows us the latitude to segregate the spatial, and the temporal dimension of our ontological reality for independent examination in separate chapters; two, it also allows us the latitude to investigate beyond the standard (commonsense) concepts of mechanical time and physical space, and undertake a philosophical analysis of the concepts of time and space in an effort to understand appreciate the concept and implications of 'time-space compression'. This is crucial because the way we represent time and space in theory affects the way we interpret and act with regard to the problems facing us. This is an important aspect of the disjunction between the entrepreneur led financial institutions, and the bureaucrat led regulatory agencies, and a cause of the tensions in the financial services industry.

Although in the contemporary era, the notion of 'time' and 'space' as being anything other than 'mechanical time' and 'physical space' would be perceived as unusual, and perhaps even irrational and absurd, a peek into history, however, reveals that until the launch of the enlightenment project an accepted ambiguity was allowed with regard to the these concepts of time and space. Aristotelian traditions held the view that time and space were among the categories which facilitated the naming and classifying of the evidence of our senses³. Time and space were conceptualized either as:

- Res-cogitan or mental (internal) objects, i.e., simple empirical tools for the ordering of sense data.
- Res-extensa or physical (external) objects, i.e., generalities in some way superior to the evidence supplied by the body's sensory organs.

The status of time and space therefore remained inconclusive and hence ambiguous. It was during the enlightenment era and the influence of Descartes philosophy and his Cartesian logic, that brought an end to the accepted ambiguity in the concepts of time and space. Consequently, with the advent of Cartesian logic, time and space entered the realm of absolute. The concept of time was also formalized as an external, absolute, and measurable quantity: the mechanical clock time or the Newtonian time⁴. Similarly the concept of space was formalized as Euclidian space⁵ - space as an absolute physical entity, an 'object' as opposed to 'subject', 'res extensa' as opposed to 'res cogitan',

³Lefebvre (1991, pp.1).

⁴The time which was a variable in Newton's laws of motion. In Newtonian physics, spatial separation and temporal durations between events are absolute dimensions independent of the observer's rate of motion (unlike Einstein's Theory of Relativity where they become relative to the observer's state of motion).

⁵Euclid was a geometrician, his emphasis was therefore on the geometric and the geographical facets of space.

or 'external object' as opposed to 'mental object'. Time and space, thus became universal, absolute, and external attributes - attributes that could only be evaluated objectively, and subjectivity was banished from the realm of our imagination with regard to the evaluation of problems interfacing the dimensions of time and space.

The concepts of mechanical time and physical space, whose foundations were laid during the enlightenment era were not considered as being problematical because they seemed to cater adequately for understanding and resolving our problems interfacing the dimensions of time and space, and gradually entered the realm of our commonsense. The problems of the late twentieth century, however, caution us against blind acceptance of the concepts that have entered the realm of our commonsense. They implore us to reevaluate these concepts in light of the problems associated with our present ontological conditions: the problem of time-space compression. The exclusion of 'res-cogitan' or our subjective judgment from our concepts of time and space, creates a false sense of objectivity, not only in our search for questions for the evaluation of problems interfacing time and space, but also in our search for answers for the resolution of the problems. This is perhaps the reason why the socioeconomic problems interfacing time and space are conceptualized as external, absolute and measurable problems requiring external, absolute, and measurable solutions. The socio-economic problems of the late twentieth century facing the policy makers of nation-states caution against the blind acceptance of this mode of thinking.

The tensions in the financial services industry are an indicator of the problematic nature of the modernist concepts of time and space, or of any framework based on these concepts. It is also an indicator of the inadequacy of these concepts in terms of assisting us in understanding the rapidly changing ontological conditions of the late twentieth century - a phenomenon known as 'time-space compression'. The existence of these tensions also provides a motivation for undertaking a philosophical re-investigation into the concepts of time and space, in an effort towards understanding the problems connected to the time-space compression of the present era, and the search for answers for their resolution.

The rationale for this part of the thesis is two fold: one, an examination of the phenomenon of time-space compression, and its ramifications especially in the context of the tensions in the financial services industry. In order to investigate into the temporal, as well as, the spatial aspects of the phenomenon of time-space compression, the concept has been segregated into two phenomena: the phenomenon of temporal compression; and the phenomenon of spatial compression; and two, the problematic nature of our conventional concepts of time and space which hinder, rather than help us in understanding the problems of the time and space compression, let alone facilitate us in developing a policy or a strategy for overcoming them. Hence, the need for broadening our

knowledge base through an investigation into some alternate concepts of time and space in an effort towards understand the phenomenon of time-space compression, and its ramifications for the financial services industry. The rationale for this part of the thesis, as was the case with part III, is to provide a different approach, a different perspective for examining and understanding the problem of time-space compression, and not necessarily that of providing an answer for the resolution of the problem. After all, it is our understanding of the problem that forms the basis of our search for answers. In order to give equal importance to the temporal, as well as, the spatial aspects of the problematic of time-space compression, this part of the thesis has been divided into two chapters:

- Chapter Eight: Problematic of Temporal Compression, and the Tensions in the Financial Services Industry.
- Chapter Nine: Problematic of Spatial Compression, and the Tensions in the Financial Services Industry.

CHAPTER EIGHT

THE PROBLEMATIC OF TEMPORAL COMPRESSION, AND THE TENSIONS IN THE FINANCIAL SERVICES INDUSTRY

1. Introduction:

According to Schlesinger (1977), when a society changes slowly, its presuppositions go for generations and without examination. The present is not much different from the past, the presumptions appear so obvious, that people do not know what they are assuming, because no other way of putting things had ever occurred to them. In a static or a slowly changing society the existing stock of wisdom which is based on the experiences of older generations provides sufficient guidance for the existing generations: the concept of linear time. The shift from a slowly changing to swiftly changing society alters a number of things. The present becomes radically different from the past. The traditional institutions and their roles come under severe and incomprehensible strain. Acceleration brings to the surface a whole range of issues that static societies never had to confront or articulate. It calls into question the presumptions that have become a part of our conceptual foundations, which we take for granted as *a priori* truths. It implores us to reexamine our presumptions and to broaden our knowledge base in an effort to understand and appreciate the contemporary state of our existence.

In line with Schlesinger's analysis, this chapter aims to examine the tensions in the financial services industry in the context of the problematic of temporal compression. The area of investigation of this chapter has been sub-divided into two main themes. The first theme relates to the problematic of temporal compression and its ramifications for the regulators in the financial services industry. Two approaches have been applied to examine this theme: one, temporal compression at a point of time; and two, the concept and the consequences of temporal compression over a period of time. The former approach examines the consequences or the implications of the speed-up or the intensification of our economic processes for the policy makers of nation-states in general and the regulators in the financial services industry in particular. The latter approach examines the rationale for the speed-up of the change in our ontological conditions. Both the approaches draw attention to the problematical nature of our mechanical concept of clock time to assist us in understanding the consequences of this change, hence the need for a reexamination of our concept of time, which is the second theme explored in this chapter. Theme two of this chapter therefore digs deeper into the problematic of temporal compression by re-evaluating the temporal compression in the context of some alternative concepts of time in an effort to understand and explain the tensions in the financial services industry.

Within this theme, two alternate concepts of time have been examined: one, the dialectical concept of time which combines the clock time, the social time, and the biological time. The other concept examined relates to the concept of temporal awareness and social time, and the tensions created when two groups with different temporal awareness and social time confront each other. This is an explanation for the tensions in the financial services industry connected to the regulator-regulated dialectic.

2. Temporal Compression:

2.1. The Concept:

Time compression basically refers to the speed-up of the temporal phenomenon. This includes the speed-up of the process of knowledge generation, speed-up of the process of decision making, speed-up of the process of implementation of decisions, speed-up of the process of reaping of the fruits of decisions (i.e. compression in the time horizon of the usefulness of the decisions), speed-up of the process of obsolescence of the fruits of the decisions (hence the rationale for short term time horizon), etc.. Temporal compression also includes the speed-up of the process of innovation, speed-up of the process of implementation of innovation, speed-up of the process of production, speed-up of the process of consumption, speed-up of the process of change in the pattern of production, speed-up of the process of change in the pattern of consumption, etc.. All these facets of temporal compression are also connected with the phenomenon of entrepreneurialism, which has already been discussed in detail in Chapter Five. They are also connected with the improvements in management information systems which not only speeds up, but also improves the decision making process. They are also connected to the improvements in the communication technology which speeds up the transmission of information across space, thereby allowing a greater and a quicker dispersion of the effects of temporal compression across space, and also contributing to the compression of space. Combining all these facets together, temporal compression can be conceptualized as the speed up of, as well as speed up of the change of, our ontological conditions.

2.2. The Ramifications:

In order to understand the effect of temporal compression on our ontological conditions, and its ramifications for the policy makers of nation-states (represented by the regulators in the financial services industry), two approaches have been applied to examine the phenomenon of temporal

compression. One, temporal compression at a point of time; two, temporal compression over a period of time.

2.2.1. Temporal Compression at a Point of Time:

The facet of temporal compression under consideration here relates to the speed-up, and hence intensification of economic process, and its ensuing implications for the policy makers of nation-states¹. A major consequence of temporal compression is the increase in volatility and ephemerality associated with a multitude of facets of our daily reality. Whether it is a question of interest rates, money supply, product life cycle, production techniques, labour processes, fashions, ideas and ideologies, values and established practices, etc., volatility, ephemerality, innovation, and change are the most conspicuous features of the present era. Volatility and ephemerality makes it difficult to maintain any sense of continuity. Past experiences get compressed into some overwhelming present, and the vision of the future is limited only to the extent to which it can be discounted into the present. The situation can be described as 'a crisis of explanatory logic', and 'the triumph of effect over cause, of instantaneity over time²'. The challenge of accelerating turnover time and the rapid write-off of traditionally acquired values means that it is impossible to say anything of solidity and permanence in the midst of the present ephemeral and fragmented world. The situation has been

¹Harvey (1990, pp.229) associates this facet of temporal compression with the turnover time of capital. The basis of his hypothesis is, that faster the capital is launched into circulation and recuperated, greater the profit, and also greater the temporal compression. There is, therefore, an omnipresent incentive for the capitalist (entrepreneur) to maximise his profits, and return on equity by reducing the turnover time of his capital, thus leading to an increase in the temporal compression. The strategy that the capitalist (entrepreneur) applies for achieving temporal compression involves the removal of the rigidity and the barriers in the production and the consumption process. The rigidity and barriers that affect the turnover of capital includes a number of factors, for example, rigidity of production and labour skills, fixed capital that is required to be amortized, marketing frictions, consumption lags, bottlenecks to money circulation, etc.. Technical and organizational innovations that can overcome or reduce such rigidity and barriers includes automation of production process, acceleration of physical processes (for example, fermentation, genetic engineering, etc.), sub-contracting, planned obsolescence in consumption, the mobilization of advertising to accelerate change in consumer tastes, improvement in the credit access to consumers to aid consumption, etc..

In a competitive marketplace, this is not the behaviour of one capitalist, rather the whole market is involved in the same behaviour. The competition for reducing the turnover time of capital implies an intensification of the market competition and the ensuing decrease in profit margins. Hence the need for increasing the turnover of capital by speed-up of production through innovations in production process and an equivalent speed-up in the consumption side through innovations in marketing management. The decrease in profit margin further fuels the speed up of turnover time of capital, thereby further intensifying the market competition.

²Harvey (1992, pp. 291).

described as the ‘schizophrenic dimension of our postmodern living³’. The volatility and ephemerality of the contemporary era makes it extremely difficult to engage in long term planning. At the same time learning to play with the volatility in an appropriate manner becomes the key to survival. The overtone is one, one has either to be highly adaptable to respond to the changes in market shifts, or be involved in masterminding the volatility. The first strategy of adapting to the market shifts means a shift from long term planning to short-termism⁴ and/or the application of hedging as the key business strategy. The second strategy which involves mastering or intervening actively in the production of volatility entails the entrepreneurialism which incorporates constant innovation and proactivation of change.

Another ramification of the temporal compression and the intensification of the market competition, is the reduction of profit margin, which also implies an increase in the probability of business failure. In the financial services industry, the increase in market competition implies an increase in the probability of bank/securities firm failure and hence an increase in the probability and magnitude of systemic risk facing the economic system.

The ramification of temporal compression in the financial services industry can also be examined from another angle: the impact of temporal compression on the decision making process. The temporal compression and the ensuing intensification of the market mechanism impacts the decision making process in three ways: one, the reduction in the time available for making crucial decision; two, the reduction in the time available for implementation of decisions, in order to maximise market share and profits; thirdly and most importantly, the reduction in the time available for initiating corrective action when faced with a crisis situation. The effect of temporal compression on the decision making process is, therefore, the increase in the probability of strategic errors.

In the context of the financial services industry, especially the securities industry, a possible ramification of temporal compression is the increase in likelihood of ‘heard behaviour’ amongst the market participants. Heard behaviour implies a strategic shift in the behaviour of majority of the

³The reference to ‘schizophrenia’ here, is based on Lacan’s description of schizophrenia as a linguistic disorder, as a breakdown in the signifying chain of meaning that creates a simple sentence. When the signifying chain snaps, then ‘we have schizophrenia in the form of a rubble of distinct and unrelated signifiers’. In schizophrenia it becomes difficult to achieve temporal unification of the past and the future with the present. This is also the basis of the ‘crisis in explanatory logic’, and the ‘triumph of effect of cause’ (Harvey, 1992, pp.53).

⁴The emphasis on short-termism has its negative side effect on the managerial performance. The tension of the job, and the frenzied life style of the financial operators whose addiction to work long hours, and the rush of power leads to stress related mental disorders like yuppie flu, schizophrenia, etc..

market participants from information traders⁵ to liquidity traders⁶. The availability of less time for analyzing the economic situation and the market trend, implies that once the market leader takes a decision there is a greater probability that others will follow suit (on the belief in the rationality of the market leader) rather than their own analysis of the economic conditions and the market potential. The effect of temporal compression on inducing a heard behaviour also implies the possibility of a worst case scenario involving the spiralling of a minor tremor into a full blown crisis in a very short time, i.e the speed-up, or the temporal compression of the process of evolution of crisis. The affect of temporal compression is more severe in the case of a downward, than an upward market turn. While the upward trend is gradual, the downward trend is drastic. Everyone in the market may have a sense that the market is overvalued, but may continue riding the bubble (or following the heard) until the first major plunge occurs, then the heard behaviour takes control but in a more drastic way: a phenomenon referred to as market crash. Such a possibility is greater in an opaque market, where either the information is scarce or the quality of information is suspect. In such markets, the behaviour of the market participants signal information. The possibility of heard behaviour is greater in such markets. The recent crisis in the South East Asian financial markets is a case to the point.

The effect of temporal compression in the financial services industry is reflected by: one, the increase in the value of the turnover of the financial markets; and two, the increase in the speed of price adjustment to new information. These two facets also point to the effect of temporal compression on the crisis potential in the financial markets. The effect of temporal compression in terms of the magnitude and the speed of crisis formation⁷ is very much evidenced in the recent crisis South East Asia. The earlier stock markets crashes in 1987 and 1989 and the currency crisis of Mexico are other examples of this facet of the temporal compression.

For the regulators in the financial services industry the ramifications of temporal compression at a point of time, are two fold: one, the effect of temporal compression on market turnover, which implies an increasing size (monetary value) of the systemic risk facing the market participants, which has the potential of developing into a major crisis; two, the effect of temporal compression on the speed of market adjustment/reaction which may perpetuate a market crisis, i.e. the reduction in time available for planning a corrective action or initiating a rescue plan to control the crisis. The

⁵Information traders are those traders who make their buy and sell decisions on the basis of information about the performance and/or the future prospects of a security.

⁶Liquidity traders are those traders who make their buy and sell decisions on the basis of market movements, on the assumption that the market movements are based on information trading.

⁷The reference is to the market's reaction to change in information, or change in perception about the market conditions.

implication for regulators and policy makers of the nation-states, is the need to evaluate their regulatory framework in the context of the capacity and capability their preventive (or prudential) and protective (or safety net) regulations to cater for the challenges of temporal compression. The key to the prevention of future crisis is a rethink of the preventive mechanism not only in the context of the consequences of the market crash following the bursting of the speculative bubble, but also in term of controlling the rise of the speculative bubbles and the herd effect that follows the upward rise of the bubble. A framework⁸ based on mathematical formulae and fixed quantitative standards like capital adequacy regulations are not necessarily the answer to such problems. The reason being, that the value of a firm's capital moves up and down with the speculative bubble⁹, and is also suspect to window dressing and creative accounting¹⁰. Furthermore quantitative standards like capital adequacy regulations also give a false sense of security to the regulator as well as the regulated as long as the these standards are being satisfied.

The only answer to the problem of temporal compression lies in the improvement in the quality and quantity of information supplied to the market. This includes information about the market (for example, economic indicators), as well as, the market players (firm specific information). After all it is in opaque markets (where the quality and quantity of information is suspect) where the possibility of systemic risk is maximum.

2.2.2. Temporal Compression Over a Period of Time:

Now we come to the second facet of the temporal compression which relates to the speed-up of change in ontological conditions over a period of time. This facet of temporal compression allows

⁸The preventive mechanism of the existing regulatory framework does not take into consideration the problems of time compression. It works by imposing standards that aim to delimit the possibility of financial institution's failure, and if it does happen then the capital should be adequate to buffer a liquidation or a rescue action. However the reality of temporal compression has made this a problematic proposition. The overtone is, the need for the strengthening of the preventive regulations to cater for the present realities of temporal compression.

⁹Since capital is the difference between the value of assets and liabilities, during the rise of the bubble, as the value of the assets (marked to the market) rise, it also inflates the value of the capital. The same is true in the deflation of the value of the assets that follows the market crash.

¹⁰In the case of banks, where the major portion of the assets consists of loans, creative accounting techniques can be used to cover-up bad debts, and thus 'window dress' the capital of the firm. The implication being, that it is very easy for the creative accountants to 'window dress' the balance sheet in order to satisfy the statutory regulatory requirements.

us an insight into the rationale for temporal compression at a point of time¹¹. This facet of temporal compression is associated with the acceleration in the process of knowledge generation, and the entrepreneurial initiative in applying the knowledge to affect a change in the ontological conditions in an attempt to achieve competitive advantage in the marketplace. It covers the acceleration in the process of innovation, and more importantly, the acceleration in the process of implementation of innovations which leads to an alteration in the pattern of production and consumption, and hence a change in the ontological conditions. In the context of the financial services industry, this facet of the temporal compression is evidenced by the speed of innovations being introduced by the financial institutions and more importantly the speed of their absorption by the market place which is echoed in the speed of change in the profile of the market place. This facet of temporal compression is also evidenced from the speed of change in the profile of the financial institutions themselves, who appear to be in a process of continuously recreating themselves. Whether it is through mergers and acquisitions, or through vertical and horizontal restructuring, they appear to be in a process of constant reexamination of their strengths and weaknesses vis.a.vis their competitors, and restructuring themselves to achieve competitive advantage in a marketplace which appears to be becoming more and more ephemeral. A matter of great salience in the compression of time which we are experiencing, relates to the fact that the temporal compression related to the speed-up in the pace of change is not limited to the production side (financial institution) only, the consumption side (the user/customer profile as well as portfolio) is also undergoing a temporal compression - a change that is also being proactivated by the entrepreneurial forces within the financial institutions¹². The strategy of proactivation of change has become a very important part of the strategy of the corporates (the financial institutions). The strategy of pro-activation is at the heart of the process of temporal compression. It is not only applied vis.a.vis the consumers, but also to other areas of their social interface. This also includes government agents whose assistance can facilitate their aims. The implication for the regulators and the policy makers of nation-states is that they are faced with a situation where a change in the market environment and market risk profile is constantly being proactivated by the entrepreneurial forces of the financial institutions, and the pace of this change

¹¹This was the theme of the previous section, which involved an investigation into the implications of temporal compression.

¹²Here the domain knowledge generation relates to marketing research, and the domain of innovation incorporates various aspects of marketing management including advertising, cold calls, direct selling, sales promotion, etc. where the aim is not only to tap active demand by providing the product information, but also through the conversion of latent demand into active sale. Marketing is also at the back of proactivation of latent demand through the strategy of forced obsolescence, which is at the back of the changing pattern of products, production, and consumption. Hence the temporal compression in the speed-up of the change in ontological conditions.

is increasing. The effect of time compression in terms of the speed-up of the change of ontological conditions also implies increase of the discontinuity in the temporal flow which interrupts the linear flow of history and creates problems in the application of frameworks/models based on linear thinking. Temporal compression, therefore, speeds up the obsolescence of the models and standards based on historical data.

The question is, does the present regulatory framework take into consideration this facet of time compression? Can a static regulatory framework developed at a point of time, based upon the market profile and historical data up to that point of time, and incorporating knowledge evolved up to that point of time, even imagine about catering for the challenges of a market which is constantly in the process of evolution? If the answer to this question is not an emphatic 'yes', then the question arises why do the regulators hold on to a static regulatory framework based upon mechanical logic. The answer lies in the philosophical foundations of the regulatory agencies - the modernist philosophical thought and its belief in the linear flow of time as an a priori truth¹³. Hence the rationale for the employment of quantitative parameters of safety net in the regulatory framework for monitoring the safety and soundness of financial institutions. But the constantly changing ontological conditions (this includes the profile of risks, the profile of market participants, the profile of financial markets, etc..) which is reflected in the qualitative change in the marketplace implies that the basic concept or the a priori truth regarding the structure and the operations of the markets do not hold. Hence, the rationale for the tensions apparent in the financial markets. Hence, the inadequacy of any framework which does not take into consideration the discontinuity in terms of the qualitative change consistently brought about by the market forces. Hence, the questionability of the modernist philosophical thought¹⁴ and its concepts of mechanical and linear time to provide us with an understanding of the phenomenon of the temporal compression, and/or to provide us the direction flag for meetings the challenges of the rapidly changing ontological conditions. Having examined the concept of temporal compression and its ramifications for the regulations in the financial services industry, it is necessary to go beyond the concept of mechanical or clock time, to search for alternate concepts of time in order to understand the problems emerging from our rapidly changing ontological conditions. This is the aim of the next section.

¹³They conceptualize the operations of the financial markets to be encapsulated within a particular framework or structure.

¹⁴The modernist philosophical thought is based on the idea of the existence of a natural logical order of things. It makes no allowance for the discontinuity and change. Hence, the importance of Kuhn's thesis.

3. A Reevaluation of the Concept of Time:

"What is time? if nobody asks me, I know, but if I want to explain it to some one, then I do not know."

St. Augustine¹⁵

The aim of this section is to reevaluate the concept of time in an effort to generate new insights for understanding the tensions in the financial services industry, the tensions associated with the phenomenon of temporal compression. This section has been divided into two subsection: one, the need for a reevaluation of the concept of time; and two, an examination of some alternate concepts of time - concepts that can facilitate our understanding and appreciation of the phenomenon, and the consequences of temporal compression.

3.1. The Need for a Reevaluation of the Concept of Time:

Before one can reexamine the need for a reevaluation of time, it is necessary to understand the basis of the modernist concept of public or the objective time, a concept that has entered the realm of our commonsense. Lucas (1973, pp.15) explains the two principles that form the basis of the modernist concept of public or the objective time: one, each person is conscious of an amount of time passing, but does not naturally agree with others on how much time has passed; two, we, however, do normally and naturally, agree about the order in which temporal events occur. An external and objective concept of public time can therefore be developed by selecting any suitable measurable process to overcome the problem of the internal and subjective time (principle one). Ancient Romans used twelfth part of day light as the measure. This used to vary from season to season, therefore after the invention of the chronometer (clock), it was later replaced by the mechanical clock time . This became the modernist concept of time, time that was linear (single dimension) and measurable, time that was external and objective. By reducing time to such a narrow concept, the modernist philosophers externalized our temporal consciousness (principle one) and impaired our ability to comprehend qualitative change, and the problems associated with the change. The limitations of the modernist concept of external, absolute, and objective time, the Newtonian clock time, and the significance of the limitation becomes apparent when we examine some of the alternate definitions of time outlined in Lucas (1973, pp.3-4):

- Time as a universal experience, a moving image of eternity.
- Time as a measure of change with respect to earlier and later.

¹⁵St. Augustine, "Confessions", Book XI, Ch.XIV, pp.xvii, cited in Lucas (1973, pp.3).

- Time as an extension of the mind, or time as consciousness.
- Time as the passage from possibility to actuality, or aspiration to achievement.
- Time as the order of events.
- Time as the form of becoming, or possibility of change.
- Time as the clock time or chronological time.
- Time as the independent variable in the laws of mechanics.
- Time as the fourth dimension, and therefore unreal and only imaginary.

From the above definitions, it is apparent that time is not only the concomitant of consciousness, but is also the process of actualization, and the dimension of change. Time is connected with persons, both as sentient beings, and as agents of change (Lucas, 1973, pp.3). The problem with the modernist concept of time is that it uncouples and ignores the things that change, the space in which they change, and the agents that bring in the change, from the concept of time which in actuality is the dimension of change. Newtonian concept of 'absolute, true, and mathematical time' assesses time from the implied single vantage point of a stationary ideal observer which is realistically unobtainable¹⁶. The observer and the keeper of the objective time for Newton was 'God', hence the rationale for separating subject and his/her subjectivity from the concept of time, hence the rationale for using spatial and numerical concepts to quantify time and its duration, hence the rationale for belief in linearity of time, hence the rationale for the paternalistic attitude inherent in the discourses of the modernist philosophers, and the discourses and framework based on modernist philosophies, hence the need for a reevaluation of the concept of time. The next section therefore examines some alternate concepts of time in an effort to understand the problems associated with the phenomenon of temporal compression.

3.2. Alternate Concepts of Time:

In this section, two concepts of time are examined: one, the concept of dialectic time, and two, the concept of social time. Both these concepts are important because both the concepts incorporate the subjective and the internal facets of time, and both deal with the phenomenon of temporal compression, and the consequences emerging from it.

3.2.1. Dialectical Concept of Time:

The problem with the modernist notion of linear and mechanical time, is that it ignores the subjective dimension of time, and as a consequence undervalues the importance of the connection between time

¹⁶Riegel (1977).

and change. It uncouples the agent of change, and his/her experience of change, from the concept of time, which after all, is the dimension of change, thus handicapping (rather than helping) our ability to understand and appreciate the process of change. To overcome the problem of the separation of the objective and subjective dimensions of time, Riegel (1977) introduces the concept of 'dialectical time' which encompasses person's subjective time, the mechanical clock time, social time, and biological time within one conceptual framework. Regal describes 'dialectical time' as an inter-phenomenon produced by the interplay of multiple ongoing events. It combines both the relational¹⁷ and the absolute¹⁸ concepts of time. It is both intrinsically and extrinsically determined. Experience of time thus involves the interaction of at least two event sequences, for example the phenomenon observed and the measurement taken. The importance of dialectical logic is that it is a mode of thinking that can facilitate our capacity to comprehend change, development, and history. Regal's concept also allows us to understand and appreciate the vital importance of the link between time and space. According to Regal, what objects are in space, events are in time. Events involve objects, and objects change. The connection is so intimate that only through conceptual separation of space from time has it become possible to regard objects as independent from events. He gives the example of a person's life history. In reviewing a person's life history, we often tend to focus only on the changing person. We do not focus on the fact that the society is also changing in many ways that has a direct bearing on the person's behaviour. Putting it another way, through their activities individuals also change the society and the historical conditions, which in turn change the individual. The concept of dialectical time also points to the risks of using historical analysis for predicting the future: the old models may not describe what is happening because the very foundation on which the old models were based has changed.

The concept of dialectical time allows us to understand the regulator-regulated dialectic in the financial services industry. The financial institutions through their actions not only affect a change in the ontological conditions in the industry, but are also affected by the changes in the ontological conditions brought about by other forces in the industry¹⁹. The same applies to the actions and the consequences of the actions of the regulators. Not only are the regulatory actions,

¹⁷Relational time is intrinsically defined either in the experience of the observer or by the overt order of the events. Relational time arises from serial interactions between events. The temporal structures of individual experiences and cultural documentations arise from variations of event sequences.

¹⁸Absolute time is extrinsically defined and regarded as constitutive of nature and is physically prior to events.

¹⁹This is also the basic argument of George Soros (1998) in "**The Crisis of Global Capitalism**".

a reaction to or a consequence of the changes in the ontological conditions brought about by other forces in the industry, but the regulatory actions also have an affect on the ontological conditions in the industry. The concept of dialectical time implies that the regulated entities will react to the regulatory actions through a change in behaviour. This reaction may not necessarily be uniform and immediate, because there are entrepreneurial forces amongst the regulated entities who may initiate innovations to take advantage of the changes in the regulatory framework, which may lead to further changes in the behaviour in the regulated entities. These changes in the behaviour of the regulated entities which are a consequence of the regulatory action, may be positive, or negative, or a combination of the two. The concept of dialectical time implies that a follow-up regulatory action may be necessary for correcting the negative consequences of the original regulatory action. The concept of dialectical time implies that the regulatory dialectic between the regulator and the regulated would, and should continue. This, however, is contrary to the basic premise of the modernist philosophical thought and the concept of linear time which implies that history can be analyzed to reveal a model that can be applied across time and space. The existence of such a premise implies that regulatory reaction to the consequences of their original action will be slow. Regulatory reaction will be delayed until major deficiencies in the regulatory framework become clearly apparent, or some catastrophic event happens which makes a major reevaluation and the revision of the regulatory framework unavoidable.

3.2.2. Concept of Temporal Awareness and Social Time:

Riegel's (1977) concept of dialectical time by synthesising the agent of change and the experience of change into the concept of time allows us an insight into the dialectical relationship between the regulator and the regulated, and the problem created when one side of the dialectic is not able to match the dynamism of the other side. Riegel's concept of dialectical time also allows us an insight into another important facet of the temporal phenomenon: the concept of temporal awareness or temporal consciousness. The concept of temporal awareness or temporal consciousness is important because it allows us an insight into an important facet of the problematical relationship between the regulators and the regulated. The reference is to the problems created when two segments of the society having different temporal consciousness interface each other. To understand the concept of 'temporal awareness', one needs to understand Jean Piaget's theory of cognitive development, according to which even the most basic features of perceptions and thought are the result of constructive activities of the child in interaction with sensory data and experience²⁰. The implication being, knowledge and understandings are mental constructions that gradually emerge from the child's

²⁰Cited in Wessman and Gorman, (1977, pp.14-15).

repeated encounter with the world. Thus, children's ideas regarding time (temporal awareness) are neither innate nor simply learned, but rather are intellectual constructions that emerge and undergo successive transformations through experience and actions. This implies that every person will have slightly different temporal awareness depending upon his or her experience and actions. This idea can be extended to social groups and their collective consciousness. Collective consciousness refers to the collective ideas and the shared values of social configurations which form the basis of their collective behaviour and attitudes²¹. This is another level of social reality which inspires both the collective conduct and the resistance that it encounters. Institutions can also be categorized as social configurations or social groups because they also embody a collective consciousness that is referred to as corporate culture. The concept of collective consciousness and temporal awareness imply that different institutions and social groups have different temporal awareness, and hence different collective consciousness towards change. It also implies that when two institutions/social groups with dissimilar temporal awareness interact there will be a possibility of tensions. This inference can be extended to explain the tensions between the regulators and the regulated in the financial services industry. After all, the regulators and the regulated are two different social groups with different temporal awareness and different collective consciousness towards change. To understand and appreciate the problems created when two social groups with different temporal awareness, and hence different collective consciousness towards change, interface each other, we need to examine the framework of social time presented by Georges Gurvitch (1964) in his book "The Spectrum of Social Time".

Georges Gurvitch (1964) introduces the concept of 'social time' to explain the effect of differences in 'collective consciousness' of social groups on their temporal awareness. He develops a temporal framework which he refers to as the 'spectrum of social time' to explain the range of perceptions and attitudes of social groups with regard to change (time is, after all, the dimension of change). Gurvitch divides the global society into partial elements, each of which moves in its characteristic social time. These partial elements include the social classes, specific groups, micro social elements, etc., each of which tends to move in its own time. In the context of the financial services industry, the regulators and the regulated can be regarded as two separate partial elements that move in their own characteristic time. Similarly each of these partial elements, for example, regulators, can be further sub-classified into separate partial elements on the basis of their functionalities and nationalities, and their spectrum of social time. The difference between partial

²¹Collective attitudes refer to the attitudes of social configuration which encircle a collective mentality of emotional preferences and dislikes, of predispositions to act and react, of tendencies by groups and their members to assume specific social roles, of frameworks where social symbols are manifested and where the collective values are exempted or repudiated (Gurvitch, 1964).

elements is reflected in terms of their social roles, attitudes, values, etc., which vary in their duration, in their rhythm, in their degree to which they are dominated by the past or projected into the future, etc.. The key import of Gurvitch's proposition is that social life of each of the partial elements or social group takes place in divergent and often contradictory manifestations of social time which becomes apparent when different social groups with different awareness (social time) confront each other directly. This is also a possible explanation for the tensions in the financial services industry. The aim of this section is to investigate into this proposition. The discussion to follow has been subdivided into two sub-sections:

- (A) Gurvitch's Framework of Social Time.
- (B) Application of Gurvitch's Framework of Social Time to Examine the Tensions in the Financial Services Industry.

(A) Gurvitch's Framework of Social Time: Gurvitch outlines eight distinct classes of social time which can be used as frames of reference for classifying the collective consciousness of different social groups. Before discussing each of the eight categories of social time outlined by Gurvitch, it is necessary to clarify that: one, it is not necessary that the collective consciousness of a social group will fit exactly into one class of social time. Rather, in most of the cases, the collective consciousness of social groups will show characteristics of more than one social time in varying degrees of dominance which can be arranged hierarchically; two, a social group does not remain permanently fixed in a particular social time. It is influenced by the changes in the ontological conditions. It is also influenced by the dialectic interaction that takes place when two social groups with different social times interface each other, i.e. dialectic interaction between different social groups with different social time engender a gradual change in the temporal consciousness of the groups. The eight classes of social time outlined by Gurvitch are briefly discussed below:

i. Enduring time (time of slowed down long duration) The past is dominant and projected into the present and the future. The present and the future thereby risks annihilation. Examples include kinships and locality groupings where traditions are considered sacrosanct. Bureaucracies also show characteristics of enduring time. Their present and perhaps future operations are based on fixed rules and regulations which were developed in the past. Social groups and organizations where enduring time dominates are very susceptible to the acceleration of time.

ii. Deceptive time It is a time of long and slowed down duration, dissevered by abrupt crisis and unforeseen forces interrupted by a flood of discontinuity. In this 'surprise time' a rupture between the

past and the present occurs thereby reinforcing discontinuity. Examples include, charismatic-theocratic structures which were meant to be ever lasting, yet were confronted with revolution that destroyed their social structures, e.g. ancient China, and Egypt. The period spanning the ten years of the decade of 1980s which culminated in the breakdown of the centrally planned socialist economies and their conversion to the market driven economies, can also be classified as deceptive time. The rise and the sustenance of stock market bubble until its eventual crash also exhibits characteristics of deceptive time.

iii. Erratic time This is time of uncertainty par excellence where contingency is accentuated. During erratic time, the present appears to prevail over the past and the future, and discontinuity appears to be conspicuous. In the context of social roles and of collective attitudes, the regulated social roles collide with repressed, aspired, fluctuating and unexpected social roles. This is the time of global societies in transition. The present era which is described by many academics as the transition and transformation from industrial to post-industrial society, where the domination of modernist philosophical thought is increasingly being challenged by scholars labelled as postmodernist, also shows the characteristics of erratic time.

iv. Cyclical time (a dance on one spot). The past, present, and future are mutually projected into each other with an accentuation of continuity and a weakening of contingency. This class of social time is predominant in archaic societies where the mythological, religious, and magical beliefs play an important part. It is also predominant in peasant communities where seasonal cycles are a prominent part of their culture. Although Gurvitch considers this to be a relatively unimportant category which is dominant only in archaic societies and peasant communities, cyclical time is quite prominent even in the technologically advanced social groups. The concepts of economic cycles in macro-economic theory, product life cycles in marketing management, are few of the prominent examples of modern day theories involving the concept of cyclical time.

v. Retarded time This is a delayed time whose unfolding is awaited so long that, although the future is actualized in the present, it is not efficient. In other words the future becomes the present so late that it is out-modeled as soon as it is crystallized. The groupings that move in retarded time are closed groupings or those to which admission is difficult, for example, nobles, landed gentry (feudal society), certain corporations whose members are selected (e.g. stock exchanges before the deregulation of market entry controls), licensed professions such as academic faculties and more broadly the public service professions (bureaucracy). The attitude and operational conduct of

regulatory agencies in terms of their new regulatory initiatives also exhibits characteristics of retarded time.

vi. Alternating time This is time alternating between delay and advance. Here delay refers to past and advance refers to future. Alternating time represents the state where the society is in a state of predicament whether to hold on to the tried and tested values of the past, or to change and leap into the unknown future because change and innovation may be necessary for survival. The victory of one over the other can only end with a bitter struggle and the issue is always precarious. This is often the time of communities where their tendency to immobility is shed. Alternating time reflects the state of predicament when an organization is faced with a major decision regarding change. The time period of predicament faced by the governments prior to the inauguration of the deregulation process in the financial services industry can be classified as alternating time. The predicament facing the regulators of the present era regarding the problems related to the regulation of the financial services industry also shows characteristics of alternating time.

vii. Time in advance of itself (or time pushing forward) This is the time in which the future becomes the present, or a period in which a qualitative change is undertaken. This is a time where discontinuity, contingency, and the qualitative change triumph together over their opposites. This is perhaps the most appropriate reflection of the temporal consciousness of the Schumpeterian entrepreneur who aims to introduce discontinuity in the circular flow and hence change the future. This is, therefore, the social time of competitive capitalism. The temporal awareness of the speculators can also be classified within this class of social time because the operational framework of the speculators, after all, involve the anticipation of the future.

viii Explosive time This is the time in which the present and the past are dissolved into an transcended future. In this time discontinuity, the contingency, and the qualitative change are maximized and their opposites reduced to a minimum. This is the time of acts of collective creation which always intervenes in social reality and becomes apparent and dominant during revolutions. The explosive time, when it is effective, endangers the global and partial structures in existence. Examples of social formulations include revolutions and radical transformations of global structure. The state of the financial services industry in which a major strategic change in the structure of the industry itself is in process, may be regarded as a personification of explosive time.

(B) Application of Gurvitch's Framework of Social Time to Examine the Tensions in the Financial Services Industry:

Gurvitch's framework of social time is important because it facilitates our understanding and appreciation of the differences between social groups (and institutions) in terms of their attitudes towards change and hence their process of thinking, the basis of their reasoning, their operational philosophy, and their framework of operations. It brings into focus the spectrum of social time or the temporal consciousness which envelopes societies and institutions, and influences their operations at the conscious, as well as, the unconscious level. It also helps us to understand the tensions that may emerge when two social groups (or organizations, or institutions) having different social times, and hence different temporal consciousness, interface each other.

Having examined each of the eight categories of social time, we now apply Gurvitch's framework of social time to analyze: one, the social time that is representative of the environment of the financial services industry, and two, the social times that are representative of the temporal consciousness of the regulators and the regulated, and the consequences of the disjunction in the social time (or the temporal consciousness) between the two, that forms the basis of the tensions in the financial services industry.

Social Time in the Financial Services Industry: The ontological conditions in the financial services industry as a whole appear to exhibit the characteristics of more than one form of social time. They echo the characteristics of explosive time, as well as erratic time and deceptive time. We begin with '**Explosive time**'. Gurvitch defines explosive time as the time in which the present and the past are dissolved into an transcendent future. This is apparent in the financial services industry where a revolutionary change appears to be in progress. We are seeing the emergence of a new global structure. The big players are merging to form even bigger players. They are expanding geographically to encompass the whole globe, cross functional merges between banks, insurance companies, and securities firms is taking place. Financial innovation is still on, and new financial products continue to be developed and introduced into the marketplace. Thus, we see the present and the past being dissolved into a transcendent future.

The characteristics of '**erratic time**' are also apparent in the financial services industry. Discontinuity appears to be conspicuous. The present appear to prevail over the past and the future. This is apparent in the new crisis that are materializing for which we did not have a historical precedence. The Asian currency crisis, the Russian currency crisis, the (earlier) European Currency Crisis , etc. are reflective of the uncertainty facing the regulators in terms of formulating their regulatory strategy for controlling and maintaining the stability of the international financial system.

'Deceptive time' is the third category of social time (from Gurvitch's framework) whose characteristics are apparent in the financial services industry. The rise of a bubble economy or a bubble market echoes some of the characteristics of deceptive time. Until the crisis happened, the Far Eastern economies were locked in deceptive time. And since the start of the crisis, the erratic time has become predominant. The continual rise of the European and the American stock markets also manifests some characteristics of deceptive time. The rising market capitalization and the increasing price earning ratios raise a number of questions: Is the market correctly valued? Is a crisis expected in the new future? When will it happen, nobody knows, but everyone is aware of its possibility, but would not like to think about it. An awareness of being encapsulated in deceptive time is conspicuous.

Having examined the temporal consciousness that echo the environment of the financial services industry, we now examine the temporal consciousness of the two key participants in the market: the regulator and the regulated whose operational strategies, and whose activities form the basis of the social times and the ontological conditions in the industry.

Social Time of the Regulators and the Regulated (Financial Institutions): Having examined the social times that echo the ontological conditions of the industry as a whole, we now examine the temporal consciousness of the two key forces striving to control the environment in the industry: one, the financial institutions whose operational strategies are geared towards their aim of improving their market share and their profitability; two, the financial services regulators whose regulatory framework is geared towards their aim of maintaining the systemic stability of the marketplace.

We begin with an examination of the temporal consciousness of the financial institutions who are the representative of the entrepreneurial forces aiming to bring about a qualitative change and a discontinuity in the circular flow. In an industry characterized by explosive time, innovation, proactivation of change, and speculation about the future have become the basis of the operational framework of the financial institutions who aspire to proactivate a qualitative change not only in their own operations, but also in the structure and operations of the industry as a whole. In the context of the spectrum of social time, the financial institutions aspire to live in '**time in advance of itself**'. Time in advance of itself reflects the temporal consciousness of the speculation activities of the financial institutions, because it involves speculation about the future in the present based on the presently available information set. Time in advance of itself is also apparent in the entrepreneurial initiative by the financial institutions to proactivate a change in the regulatory framework. An example is the initiative of J.P.Morgan to reveal its Value at Risk (VAR) system of internal control

(RiskMetrics), which led to a qualitative change in the regulatory framework in the financial services industry.

Compared to regulated entities, the regulators, however, appear to be living in a completely different frame of social time. Their strategy and their operational framework appear to be dominated by the past. Although they accept a qualitative change in the industry, they appear to be living in an '**enduring time**'. They still appear to cling to the preconceptions of linear time and the regulatory framework developed decades ago. An element of '**alternating time**' is also apparent in the operations of the regulators. It is not that they are completely without any initiative. The Basle Committee of Banking Supervision is an exception to the rule. It has continuously been involved in reevaluating and revising the regulatory tools and the regulatory framework in the financial services industry in an effort to improve the global environment of regulations in the financial services industry. However, despite their initiatives, regulators in general (this includes the Basle Committee) still fight to hold on to the tried and tested past represented by quantitative regulations rather than attempting to initiate a qualitative change in the regulatory framework. Other than enduring, and alternating time, an element of **retarded time** is also apparent in the operations of the regulatory agencies. The reference is to the time take in the assessment of relative pros and cons of the new initiatives, that when at last a decision is taken regarding a change, the decision is delayed to such as extant that it is no more efficient.

An examination of the social times of the regulators and the regulated shows a considerable disjunctions in the temporal consciousness of the two entities. The tensions in the financial services industry are only a symptom of this disjunction. In an industry characterized by '**explosive time**', where the major players (financial institutions) aspire to live in '**time in advance of itself**' or '**time pushing forward**', it is necessary that the disjunction in temporal consciousness between the regulators and the regulated be removed if the regulatory objective of maintenance of market quality and sustenance of systemic stability are to be achieved. One possibility would be to partially delegatee some aspects of the regulatory functions to the private sector firms with quasi regulatory function like rating agencies, and audit firms. Another possibility would be to undertake their supervisory function as a collaborative effort with such market players. In either case, it is the amelioration of the disjunction between the temporal consciousness of the regulators and the regulated that should be a regulatory objective if the tensions in the financial services industry are to be reduced.

4. Conclusion:

The investigation into the problematic of temporal compression brought into focus a number of problems. Investigation into the phenomenon of temporal compression at a point of time brought into focus the implications of the speed-up or the intensification of our economic processes. This includes increase in volatility and ephemerality, reduction in profit margins, reduction in time for decision making, increased risk of business failure, reduction in time for undertaking correcting action to control problems, etc.. In the context of the financial services industry, the consequences include the increase in volatility, increase in market turnover, the increase in systemic risk, increase in the speed of market adjustment, all of which point to the increase in the level of difficulty facing regulators. Simple quantitative regulations based on rule-of-the-thumb cannot achieve the regulatory objectives unless combined with market transparency (which is dependent on the quality and quantity of information about the markets) as a regulatory objective. This is because the possibility of crisis is greater in an opaque marketplace. The implication being, that the maintenance of the quality and the transparency of the market should be at the top of the regulatory objectives.

The examination of the concept of temporal compression over a period of time brought to focus the rationale for the temporal compression at a point of time. This facet of temporal compression is associated with the acceleration in the process of knowledge generation, and the entrepreneurial initiative in applying the knowledge to affect a change in the ontological conditions in an attempt to achieve competitive advantage in the marketplace. In the context of the financial services industry, this facet of the temporal compression is evidenced by the speed of innovations being introduced by the financial institutions and more importantly the speed of their absorption by the market place which is echoed in the speed of change in the profile of the market place. This facet of temporal compression is also evidenced from the speed of change in the profile of the financial institutions themselves, who appear to be in a process of continuously recreating themselves. The consequence is the increase in the discontinuity of the temporal flow which interrupts the linear flow of history and creates problems in the application of frameworks/models based on linear thinking. Temporal compression speeds up the obsolescence of the models and standards based on historical data. This brings into focus the problematical nature of the regulatory framework in the financial services industry, and its connection with the mechanical concept of clock time and concept of linear flow of history which encourages over-emphasis on quantitative parameters and under-emphasis on qualitative parameters. This was the rationale for undertaking a reevaluation of the concept of time.

Although time is the dimension of change, the mechanical concept of clock time by severing the subjective component of time from the objective component of time, creates problems in our ability to understand the dynamics of the change that we are experiencing. This was the basis of the

investigation into the alternate concepts of time: the concepts of dialectical time and the concept of temporal awareness or social time. The rationale for examining the alternate concepts of time was to provide direction flags for understanding the phenomenon of temporal compression and its consequence. The dialectical concept of time, by combining the subjective and objective facets of time into a holistic concept allowed us an insight into the dynamism of change that the concept of time represent, and the problems that arise when a static framework is imposed on the society or any societal group. Gurvitch's framework of social time, brought to the fore the disjunctions in the temporal awareness of the regulator and the regulated, and thus provided a direction flag for a possible avenue of action by the regulators. The aim of this chapter was to expand our knowledge base, to provide new insights for understanding the dynamics of change that we are experiencing (the concept of temporal compression). It is after all our understanding of the problem that forms the basis of the strategy that we develop to confront and resolve the problem.

CHAPTER NINE

THE PROBLEMATIC OF SPATIAL COMPRESSION, AND THE TENSIONS IN THE FINANCIAL SERVICES INDUSTRY

1. Introduction:

The aim of this chapter is to examine the tensions in the financial services industry in the context of the problematic of spatial compression. The area of investigation of this chapter has been divided into two main themes. The first theme relates to the problematic of spatial compression and its ramifications for the regulators in the financial services industry. The discussion on this theme begins with an examination of the concept and the consequences of globalization, and then moves on to a more specific investigation into the concept and consequences of spatial compression. Although the concept of globalization and spatial compression imply the same meaning, and can be used synonymously, but here they have been discussed separately, because of the difference in the approach adopted to examine them. While the discussion on globalization involves an examination of the concept and the consequences of globalization, the emphasis of the discussion on spatial compression, on the other hand, is towards explaining the concept of spatial compression which forms the basis of globalization. The second major theme covered in this chapter relates to the inadequacy of the Cartesian concept of 'physical space' in terms of allowing us to take cognizance of the dynamics of the change, and the consequences of the change that we are experiencing (spatial compression). This is one of the fundamental reasons for the tensions in the financial services industry. Hence that rationale for a reinvestigation into the concept of space. This is also the basis for examining Henri Lefebvre's concept of 'social space'. Lefebvre combines the space occupied by the sensory phenomenon, with the mental space, and most importantly, the space of social practice, to develop a single holistic concept of space, the concept of 'social space'. The significance of social space as a concept relates to its utility as a tool not only for analyzing and understanding the change we are experiencing - the phenomenon of 'globalization', but also for understanding and appreciating the consequences of this change. The concept not only allows us to take a holistic view of the space at a point of time, but also allows us to understand the process of change of (social) space across time. These two facets of the concept of social space have been examined in detail in two separate sections. First, the process of change in space across time: a phenomenon which Lefebvre refers to as 'production of space'. The second facet of Lefebvre's concept of social space relates to the 'organization of space' (which we had earlier referred to as space at a point of time). Lefebvre's concept of space is very different from our pre-existing concept of space as a physical thing. Social

space is visualized as encompassing a number of networks with material underpinnings whose primary purpose is to facilitate communication/relationship between the subjects. The significance of this concept relates to its utility as a tool for examining and understanding the organization of space. It has therefore been used to examine the organization of: one, the space of capitalism; two, the space of markets; three, the space of a market participants (financial institution); four, the space of political forces (the regulators); and five, the spatial disjunction between the regulators and the regulated. The final section is the conclusion which involves a sum up of the consequences of the problem of spatial compression in the financial services industry in the context of the above analysis.

2. The Concept of Globalization:

McGrew, (1992, pp.318) refers to globalization as the recognition "that there are dynamic processes at work constructing and weaving networks of interaction and interconnectedness across the states and societies which make up the world community". It is this recognition that allows us to understand and appreciate the phenomenon of 'globalization' as the process of creation of linkages and interconnections, which according to Held and McGrew (1993, pp.262), "transcends the states and societies which make up the modern world system". The phenomenon of globalization therefore involves the breaking down of national barriers and the development of transnational spaces and entities. The emphasis here is on 'transnationalism' - the development of transnational spaces and transnational entities. The word 'transnationalism' means transcending or extending beyond nation. The focus of transnational entities is therefore global rather than the national markets. Not being rooted in one country they have the potential to escape any regulations. Transnational corporations are non governmental bodies (mainly business corporation) operating across national boundaries, sometimes on a global scale, which seek as far as possible to disregard these boundaries, which (as a consequence of their operations) serve to establish links between national societies. A distinguishing feature of transnational relations is that although, they operate within the societal domain, in effect they operate beyond direct state control. A distinguishing feature of the transnational corporations is their role in terms of the force that is harnessing the technology to link their activities on a world wide basis as per an integrated global strategy thereby creating linkages between the national economies. Transnational corporations are therefore a key element behind the progressive global economic integration.

Besides transnational corporations another key element related to the concept of globalization is technology which has not only removed or reduced the constraints of time and space which

are/were the main impediments against interaction between entities separated by national boundaries, rather it has allowed the fusion of time and space (i.e., ability to undertake real time operations at a number of locations across the globe irrespective of one's location in space). Globalization has therefore been referred to as the "reordering of time and space¹". The reference is to the phenomenon known as 'time-space compression'. The developments in communication technology have cut through the spatial barrier across nations allowing on-line real time communication and control, irrespective of one's location on the globe. Similarly developments in computer technology have cut through the barriers in the space of imagination (the ability to process data and transform it into useful information). The barriers of physical and social distance measured in time are collapsing. Globalization can therefore be described as annihilation of space through time. Information can be transferred instantaneously, and events can be experienced instantaneously irrespective of distance. The overtone is: distance measured in time is collapsing. The globe has been opened up for economic exploitation. A technological universalism is also removing the spatial distinctiveness and identity of places. Globalization can therefore be conceptualized as the crystallization of the entire world as single place, or the processes by which the world becomes a single place². While technology facilitates on-line real-time cross border transactions, it is the force of capitalism personified by the transnational corporations that have harnessed the facilities provided by technology and are converting the world into a global market place. That is why Held and McGrew (1993, pp.263) have given equal weight to transnationalism and technology as the force behind globalization. They observe: "Technology and capitalism has 'shrunk the globe', removing distance and social time as the dominant constraints upon social interaction and relations". A key outcome of the globalization process is the alteration of the nature, scope, and capacity of the sovereign states in terms of their regulatory ability which is being challenged and reduced (in some spheres) by the market forces. As a result nation states are losing their autonomy in terms of their ability to take economic decisions independent of the global economy³. This aspect can be recapitulated in the following observation by Smelser⁴:

¹ Held and McGrew (1993, pp. 263).

² Robertson (1987).

³ Sometimes the words **autonomy** and **sovereignty** are confused. **Autonomy** refers to the ability of the state to independently direct its economic policy. **Sovereignty** refers to the purely legal control of a state over its definite territory. Thus it is quite possible for a state to lose its autonomy while still maintaining its sovereignty.

⁴ Quoted in McGrew (1992, pp. 315).

"One of the hallmarks of human history in the late twentieth century is the increasing internationalization of the world: in production, trade, finance, technology, threats to security, communications, research, education, and culture. One of the major consequence of this is that the mutual penetration of economic, political and social forces among the nations of the world is increasingly salient; and it may be that the governments of nation-states are progressively losing degrees of direct control over the global forces that affect them."

The consequence of the emergence of a highly interconnected global system is that many of the traditional functions of a nation state cannot be fulfilled effectively without some sort of international cooperation and coordination. This aspect is incorporated in the definition of globalization within the modern day concept, that it involves "a global system of production and exchange which is beyond the control of any single nation-state (even of the most powerful); extensive networks of transnational interaction and communication which transcend national societies and evade most forms of national regulation; the power and activities of a vast array of international regimes and organisations, many of which reduce the scope of action of even leading states⁵". The consequence of globalization is therefore the mutual penetration of economic, political and social forces among the nations of the world and the progressive loss of direct government control over these global forces. As a result new issues are thrust on to the global agenda requiring global management or at least global regulations wherever global externalities are involved. Whether it is the question of pollution control, whether it is the question of depletion of ozone layer, whether it is the question of prudential control of the financial services industry, wherever transborder externalities are involved, national solutions are to no avail. For transborder matters global arrangements are a necessity.

The existing framework of regulations within the financial services industry was developed during the period when the banking and securities markets of nation-states were isolated from each other. In today's global economy where the markets are in competition with each other and the banking and securities firms have become or are in the process of becoming transnational conglomerates, the regulators who are still constrained by the geographic boundaries of the nation-states are losing their autonomy for action, and as a consequence, their ability to control the risks within their jurisdictions. This points to the need for a fundamental rethink of the regulatory strategy in line with the changed circumstances if the regulatory objectives are to be achieved.

⁵Held, and McGrew (1993, pp. 283).

3. Spatial Compression:

3.1. The Concept:

The concept of 'spatial compression' or 'shrinkage of the globe' can be explained by interfacing of the Cartesian concept of physical space with the sociological concept of distance. Putting it simply, 'spatial compression' implies the reduction in sociological distance between world spaces. In the context of the social interface, the Euclidian parameter of distance (measured in miles or kilometres) is not the most appropriate measure of the separation between spaces, there are other more appropriate parameters available. This includes the distance measured in time, distance measured in cost of communication, distance measured in terms of cost of market entry, distance measured in terms of transaction cost, distance measured in terms of quantification of cost of regulatory barriers, etc.. A multitude of developments in communications and information technology⁶ unleashed by one set of entrepreneurs, harnessed by another set of entrepreneurs in transforming these technological developments into monetary profits, combined with the deregulation of government induced impediments (regulatory barriers) has facilitated the reduction in the distance between world spaces when measured in the context of our sociological interface. The consequence of this has been a revolutionary change in our attitude towards physical distance as a spatial barrier, and hence a revolutionary change in our experience of space. This is what the concept of 'spatial compression' or 'shrinkage of the globe' is all about, it reflects a revolutionary change in our attitude towards physical distance as a spatial barrier, and hence a revolutionary change in our experience of space.

3.2. The Framework of Spatial Compression:

Harvey (1992, pp.219-222) provides a simple conceptual framework that can be used to understand the transformation in our experience of space. The framework involves the interaction of four

⁶The change in attitude towards distance can be explained in the context of a multitude of developments in the area of science and technology combined with the entrepreneurial initiatives in harnessing and transforming these technological developments into monetary profits. Examples include, the development of jet technology and the reduction in cost of air travel brought about by competition within the airline industry; development of technologies in freight transportation industry (e.g. containerization) that has helped in streamlining and simplifying the logistics, thereby speeding up the process of freight handling, reducing the cost, and bringing about a revolutionary change in international trade; development of satellites and fibre optic cables communication system that has rendered the unit cost and time of communication invariant with respect to distance; the development of instant real time communication systems that has made greater centralization of management control compatible with greater decentralization in the areas of production and marketing; the dematerialisation of money and money related instruments (equities, bonds, etc..) into electronic form that has made the financial services industry oblivious to the constraints of spatial separation; the development of global media and entertainment industry that has reduced the cultural impediments in communication; etc.. It is the combined effect of all these factors that has contributed towards the 'annihilation of space through time' - phenomenon referred as 'compression of space' or 'shrinkage of the globe'.

elements: distanciation or friction of distance, appropriation of space, domination of space, and production of space. Each of these briefly explained below:

- i. **Distanciation or the Friction of Distance.** Distance is both a barrier as well as a defence against human interaction. It imposes transaction costs with regard to accessibility, whether it is a question of flow of goods, flow of money, flow of people, flow of labour, flow of power, flow of information, etc.. Distanciation is the measure of the degree to which the friction of space has to be overcome to accommodate social interaction. It incorporates not simply the physical distance but also the social and the psychological measure of distance. The important factor under consideration is the degree to which the friction of space has to be overcome to accommodate social interaction.
- ii. **The Appropriation of Space.** The concept under consideration here relates to the use of space, including land, built environment, social networks, etc.. It refers to the ways in which the space is occupied and used by objects, activities, individuals, classes, and other social groupings. It also encompasses systematized and institutionalized appropriations which include the production of territorially bounded forms of social solidarity.
- iii. **The Domination of Space.** The reference here is to the application of legal and/or extra legal means to achieve domination and control of space. This reflects how the individuals or powerful groups dominate the organization and production of space to achieve control over either the friction of distance or over the manner in which space is appropriated by themselves and others.
- iv. **The Production of Space.** The concept under consideration here relates to the developments that help the reduction of friction of space, the appropriation of space, and the domination of space. It includes the development of new systems of land use, transport and communications, physical infrastructure, territorial organization of social infrastructure, etc., and the knowledge base related to these.

These four dimensions are not independent of each other. There is a dialectical relationship between them. It is the dialectical relationship between these dimensions that is the key to understanding our shifting experience of space over time. For example the friction of distance directly affects the appropriation as well as the domination of space. The production of space helps to reduce the friction of distance, thereby altering the conditions of appropriation and domination. Use of legal or extra legal means to control the friction of distance or distanciation (this includes regulatory barriers) directly affects the appropriation and hence the domination of space. Similarly, persistent appropriation of space by a particular group amounts to a defacto domination of that space.

Harvey's framework allows us to understand the basis of spatial compression or the shrinkage of the globe. A multitude of developments in the communication and information technology, which could be characterized under the concept of 'production of space' helped in the reduction of friction, thereby allowing the entrepreneurial forces to appropriate the world spaces in their effort to achieve comparative advantages, and gain extra profits. In the financial services industry, the dematerialization of money and money related instruments and the electronic revolution facilitated the reduction of friction of space, thereby allowing the financial institutions to appropriate and later-on dominate the global space. Also in the financial services industry, a major cause of friction of space were the regulatory barriers, especially the market entry barriers imposed by the authorities (this includes the statutory, as well as, the self regulating authorities) who dominated the market through legal or extra legal means. The deregulation of these barriers combined with the advances in the electronic technology (in terms of increase in the capacity and reduction in the cost of communications and information processing technology) helped in bringing about a major reduction in the friction of distance thereby making the appropriation of global spaces by the financial institution possible. Financial institutions were, therefore, able to expand beyond the periphery of the space of nation-states and become global players. With time, and with greater appropriation of global space, their domination over the global spaces also increased - a process that is still on. In the context of the present situation, while the financial institutions are becoming global players appropriating and dominating global markets, the expanse of appropriation and domination by the regulatory agencies is strictly circumscribed within the geographical frontiers of the nation-state.

The principle of sovereignty implies that one nation-state is not allowed to appropriate the space of another nation-state without its consent. The experience of the misappropriation and domination of space during the pre-world war-II era by the colonial powers/nation-states implies that a friction of distance in term of psychological distance between the governmental agencies exists which is a barrier in the resolution of problems where international space is concerned⁷. The private

⁷To comprehend the full significance of spatial compression and its implications for the Financial services industry, we need to go back in history and examine the transformation of space during the period from the Renaissance era up to the second World War, and its contrast with the spatial order of the post World War II era. The spatial transformation during the Renaissance era can be explained in terms of the evolution of maritime knowledge, and more importantly, the commercialization of maritime industry which created a spirit of entrepreneurialism amongst the explorers, the traders, and the colonialist empires to appropriate, and then dominate the world spaces. Consequently during the Renaissance era, and up to the end of World War II, the public sector (the colonist nation-states) as well as the private sector corporations worked in tandem to reduce the friction of distance in order to achieve their aspiration of appropriating and dominating the global spaces. The incentives that drove the private sector also drove the governments of nation-states. The incentive was: the 'will to power'

sector corporations, however, do not face the problem of such psychological barrier in getting the approval of the host nation for operating in their space. The private sector corporations therefore continue to appropriate the space of more than one nation-state without encroaching upon the sovereignty of the individual nation-states. Thus, a clear spatial disjunction between the nation-states and the private sector corporations exists.

Initially, the implications of the disjunction were intelligible because of the friction of distance between world spaces. The private sector corporations neither had the information system to allow management at global level, nor the communication infrastructure to operate in a globally integrated mode. The private sector corporation therefore primarily operated in a decentralized mode with a weak centre and strong autonomous national units which were separately regulated by the national regulators, and were referred to as multi-national enterprises. The scenario started to change in the nineteen eighties. Unlike the Renaissance era, this time it was not simply the development in communication technology, but rather, the combination of the communication and the computer technology that changed the scenario of the global space. The power of computers in terms of converting raw data into useful information and the speed of transmission of information across the world spaces made decentralization compatible with greater centralization. It has allowed the fusion of time and space. In other words, the combination of computer and communication technology not only allowed the multinational companies a holistic picture of their world wide operations, but also allowed them to integrate and actively manage their world wide operations within a holistic framework based upon a global strategy. The consequence was the transformation of the private sector corporations from the multinational form into the transnational form of management.

In the financial services industry, where the financial instruments were already or in the process of dematerialization, the deregulation⁸ of market entry and other government induced barriers, combined with the powers of the computer and the computation technology allowed the creation of a market environment where global competition between financial institutions became possible. A consequence of the potential presented from holistic management at global level has been the desire by financial institutions to outgrow their national identity and acquire a global or a

and the 'will to profit'. The result was a competition between the nation-states to appropriate and dominate the world spaces. The result of this competition was death, destruction, and war between the empire builders. World War II marked a water-shed in the conduct of inter-national politics by the nation-states. The aim was to control the consequences of nation-states extending their space beyond their geographical periphery. A new political order was set up in which sovereignty and hence the autonomy of the nation-states was circumscribed within the periphery of their geographical frontiers.

⁸This includes the dismantling and/or the reduction in the market entry and other regulatory barriers imposed by the regulatory authorities to competition from outside the national borders.

transnational identity. Thus, in the course of a few years the regulators were faced with a completely new environment. The regulatory framework, which was built to cater for spatially segregated and closed national systems, now appeared to be porous. The result: tensions between the regulator and the regulated in the financial services industry. At the heart of these tensions are a number of disjunctions. Here we discuss only those related to the spatial dimension.

One, unlike the regulators, the financial institutions (the regulated) are not locked within the geographical frontiers of a single country. The implication: disjunction between the holistically managed transnational financial institutions and the nationally managed regulatory systems. The disjunction in terms of the difference in the spatial reach of the regulators and the regulated implies, that unlike the management of the transnational financial institutions (the regulated entities), the regulators do not get a holistic picture of their risks. The separation of functional regulators within the same country adds to the problem⁹. This implies the possibility of creation of blind spots or areas of regulatory laxity that can become the potential source of contagion. The existence of the possibility of regulatory blind spots combined with the relative opaqueness of the financial position of a financial institution, implies that in time of stress the counterparties and the other market players may over react leading to the possibility of crisis formation, and perhaps failure of a financial institution.

The **second** disjunction relates to the desire of the financial institutions to outgrow their spatial identity. Unlike the strict national identity of the regulators, the regulated (financial institutions) are not constrained by a single spatial identity. Regulatory requirements may require them to garb themselves with a particular national identity, but with time, and with more and more cross-border mergers and acquisitions, the concept of national identity will diffuse and the financial institutions will acquire a global identity. Such a scenario may create potential problems in cases where a global financial institution is faced with a crisis situation which requires protective (safety net) intervention (i.e., application of public funds to undertake a rescue operation).

The **third** disjunction relates to the link between the concept of space and its influence on the operational framework of the regulators and the regulated. This is by far the most important disjunction because it forms the basis of the first two disjunctions discussed above. Unlike the

⁹The reference is to the functional separation between the banking and the securities regulators which is becoming a complication in view of the tendency towards universalization of the banking industry (i.e., development of universal banks). The incentive for universalization of the banking industry is fuelled by the incentive to reduce functional barriers between the banking and securities business, and to achieve economies of scope. The circumscription of the regulatory scope through the separation of regulatory authority between the two functional regulators is yet another element of disjunction between the private sector financial institutions and the public sector regulatory authorities. This is yet another facet of the tensions in the financial services industry.

regulators whose operational framework are constrained by the geographical restrictions imposed by the Cartesian concept of physical space, the operational framework of the financial institutions (the regulated) appear to be oblivious to these constraints. This is a very crucial disjunction that needs to be investigated further. The need is to unravel this disjunction by investigating beyond the concept of physical space. The need is therefore to undertake a reevaluation of the concept of space in order to broaden our knowledge base, and to draw insights that may help us in reforming and revising the regulatory framework, with the aim of reducing the disjunction between the regulators and the regulated. This is the area of investigation of the next section.

4. Need for a Reevaluation of the Concept of Space:

We began our discussion on the rationale for part IV of the thesis by referring to the accepted ambiguity that existed in the concept of space during the pre-enlightenment era. The ambiguity related to the question: whether space was a mental construct that was internal to the subject, or was it an objective reality that was external to the subject (the concept of physical space). It was Descartes and his Cartesian logic, that separated the subject and his/her subjectivity from the concept of space. Thus, space became an objective reality: the concept of physical space (which, because of its geometrical connotations is also referred to as Euclidian space). The problems of the present era, especially those related to the spatial dimension, hint at the possibility that the Cartesian logic of space as an objective reality independent of the subject, may be incomplete, and hence problematical. If this proposition is valid, then a necessary overtone of the proposition is, that the Cartesian concept of space, by ignoring some of the vital facets of our spatial comprehension, it handicaps our imagination and our ability to undertake a holistic analysis of the problems of the present era. This proposition forms the basis of this section which aims to search for an alternate concept of space, a concept that has the capacity to facilitate our understanding the problems of the present era, especially the problems associated with the tensions in the financial services industry. This is the basis for examining Henri Lefebvre's (1991) discourse on the production of space which is the area of investigation of the next section. Lefebvre reevaluates the various concepts of space, and then synthesizes them into a unitary theory of space: the theory of social space. The next section therefore undertakes an analysis of Lefebvre's concept of space and the application of his concept of space to understand the tensions in the financial services industry connected to the phenomenon of spatial compression - a phenomenon that is also labelled as 'globalization'

5. The Concept of Social Space:

"Space does not eliminate the other materials or resources that play a part in the socio-political arena, be they the raw materials or the most finished of products, be they business or culture. Rather, it brings them all together and then in a sense substitutes itself for each factor separately by enveloping it. The outcome is a vast movement in terms of which space can no longer be looked as an 'essence' as an object distant from the point of view of (or as compared with) the 'subjects', as answering to a logic of its own. Nor can it be treated as a result or a resultant, as an empirically verifiable effect of the past, a history or a society. Is a space a medium? A milieu? An intermediary? It is doubtless all of these, but its role is less and less neutral, and more and more active, both as instrument and as goal, as means and as end. Confining it to so narrow a category as that of 'medium' is consequently woefully inadequate¹⁰."

From the above excerpt, it is clear that Lefebvre considers the Cartesian concept of space (space as a medium) as woefully incomplete and hence inadequate for understanding the problems of the present era. Lefebvre also rejects the concept of mental space (also referred as the epistemological space or philosopher's space) as problematical and incomplete. The reason being, that philosophers have a predilection towards creating abstract objects, and most importantly, analogous to the Cartesian space, it also ignores the collective element¹¹. Lefebvre combines the space occupied by

¹⁰Lefebvre (1991, pp.410-411).

¹¹According to Lefebvre (1991, pp.1-7), while the scientific attitude towards space is structurally linked to the spatial sphere, the epistemological concept is also guilty of eliminating the collective subject. In this respect he criticizes some philosophers like Noam Chomsky (linguistics), Derrida (grammatology), Roland Barthes (semiology) as being guilty of promoting sophistry whereby the philosophico-epistemological notion of space is fetishized and the mental realm comes to envelop the social and the physical ones. Such concepts reflects a powerful ideological tendency. The problem with this approach is that it is unconsciously expressing the ideas of a dominant class. What is happening, is that a particular theoretical practice is producing a mental space, which then becomes the locus of the axis or pivot or reference point. This mental space then apparently becomes the reference point for the theoretical practice. Thus a circular relationship exists which is separated from the social practice. This creates an abyss between the mental space and the physical and the social space. Philosophico-epistemological thinking has therefore failed to furnish a basis for science - the science of space. They may supply inventories of what exists in space or may even generate a discourse on space but cannot ever give rise to a 'knowledge of space'.

the sensory phenomenon¹², with the mental space¹³, and most importantly, the space of social practice, to develop a single holistic concept of space, the concept of 'social space'¹⁴.

"(Social) space is not a thing among other things, nor a product among other products: rather, it subsumes things produced, and encompasses their relationships in their coexistence and simultaneity - their (relative) order and/or (relative) disorder. It is the outcome of sequence and set of operations, and thus cannot be reduced to the rank of a simple object. At the same time there is nothing imagined, unreal or 'ideal' about it as compared, for example, with science, representations, ideals or dreams. Itself the outcome of past actions, social space is what permits fresh actions to occur, while suggesting others and prohibiting yet others. Among these actions, some serve production, others consumption (i.e. the enjoyment of the fruits of production). Social space implies a great diversity of knowledge¹⁵".

The term 'social' implies the primal importance that Lefebvre attaches to the subject and his/her subjectivity¹⁶: "the whole of the (social) space proceeds from the body¹⁷". Metaphorically speaking, unlike the modernist concept of space which can be described as the 'stage' or the 'theatre' for the staging of the human drama, Lefebvre's concept of space includes, not simply the stage or

¹²The nature, the cosmos, the concept referred to as physical space.

¹³This is the space of the philosophers and the mathematicians and includes their logical and formal abstractions.

¹⁴This is reflected in Lefebvre's preliminary hypotheses (1991, pp.27):
"Social space will be revealed in its particularity to the extent that it ceases to be indistinguishable from mental space (as defined by the philosophers and mathematicians) on one hand, and physical space (as defined by the practico-sensory activity and the perception of 'nature') on the other. What I shall be seeking to demonstrate is that such a social space is constituted neither by a collection of things or an aggregate of (sensory) data, nor by a void packed like a parcel with various contents, and that it is irreducible to a 'form' imposed upon phenomenon, upon things, upon physical materiality. If I am successful, the social character of space, here posited as preliminary hypothesis, will be confirmed as we go along".

¹⁵Lefebvre (1991, pp.73).

¹⁶This includes his/her knowledge, his/her imagination, his/her ontological assumptions, his/her relations with other subjects, his/her actions as a part of a group, etc., all of which have an affect on his/her interpretation of the problems, and consequently his/her relationship with the other subjects, and his/her actions.

¹⁷The genesis of a far-away order can be accounted for only on the basis of the order that is closest to us - namely the order of the body (Lefebvre, 1991, pp.405).

the theatre for staging of the drama (physical space), but also the actors, their intellect¹⁸ and the products of their intellect, their relationship with the other actors, and their act (both individual and collective). Thus, Lefebvre provides a holistic concept of space - the space of a society, of social life - a space which they may enjoy, and modify to serve their needs.

The significance of social space as concept relates to its utility as a tool for analyzing and understanding the society and its problems¹⁹. It not only allows us to take a holistic view of the space at a point of time, but also allows us to understand the process of change of (social) space across time. Lefebvre explains the concept of space at point of time in terms of the concept of 'network': space as a network having material underpinnings whose only purpose is to facilitate communication/relationships between the subjects. He explains the process of change of space across time in terms of the concept: 'Production of Space'. Since the space at a point of time is an output of the process of change across time, it would therefore be more appropriate to investigate into the concept of 'production of space', before examining the concept of space at a point of time. The discussion to follow has therefore been divided into two sections: one, the process of change in space across time: the concept of 'production of space'; and two, space at a point of time: the organization of space - space as a network of relationships.

5.1. The Process of Change in Space Across Time: The Concept of 'Production of Space':

The concept of 'production of space' connects the concept of space with time, thus allowing us to understand the process of change of (social) space across time. The connection between time and space implies that every social space is the outcome of a process²⁰ and, therefore, has a history. It implies that time and events leave traces on space that can influence our future actions. It also implies that space is not static, it is forever in the process of evolution and change. And most importantly, it draws attention to the dynamism and creative capacity embedded within the concept of social space, which is the product of the actions and relationships of the subjects, and the process of actual materialization of change in space. "Social space *per se* is at once *work* and *product* - a

¹⁸Covering the realm of mental space incorporating their knowledge, their ideas, and their imagination.

¹⁹Lefebvre (1991, pp.34) observes: "From the point of view of knowing (connaissance), social space works (along with its concept) as a tool for the analysis of society".

²⁰Lefebvre (1991, pp.110).

materialization of social being²¹". The concept of production of space involves an investigation into the question: why and how the space changes, and what are the consequences of the change? The concept of 'production of space' is, therefore, the key to understanding of the process of change in the space of the financial services industry, and the consequences emanating from the change for the regulators and the regulated.

To understand Lefebvre's concept of 'production of space', we first need to understand Lefebvre's concept of 'production' which has been borrowed from Marx's philosophy, and is representative of the process of materialization of change in space. According to Lefebvre, one of the important contributions of Marx to philosophy, was that instead of examining things taken 'in themselves', in isolation from one another, he undertook a critical analyses of the productive activity itself (social labour; the relations and mode of production)²². He worked his way back from the results of productive activity (the products) to the productive activity itself, and concluded that any reality presenting itself in space can be expounded and explained in terms of its genesis in time. The import of this conclusion (which emerged in Marx's thinking only in an ill defined form) was, that any activity developed over (historical) time engenders (produces) a space, and can only attain practical 'reality' or concrete existence within that space²³. The contribution of Lefebvre to our philosophy of space is that, unlike Marx, who analyzed production and the productive activity in the narrow sense (material products produced by labour), Lefebvre analyzes production and the productive activity in the broad sense²⁴. Unlike Marx, he analyzes not simply things in space, but

²¹Lefebvre (1991, pp.101-102).

There is a difference between the concepts of 'work' and 'product'. According to Lefebvre (1991, pp.70), whereas a 'work' has something irreplaceable and unique about it (for example, a work of art), a 'product' on the other hand can be reproduced exactly, and is in fact, the result of repetitive acts and gestures. Both these concepts are different from natural 'creation'. Nature 'creates' and does not produce. It supplies only use value, i.e., it provides the resources for 'creative' and 'productive' activity on part of the social humanity.

²²Lefebvre (1991, pp.89).

²³Lefebvre (1991, pp.115).

²⁴According to Lefebvre (1991, pp.68) in the discourse of Marx and Engels there is some ambiguity in the concept of 'production'. It has two senses: one a very broad, and other restrictive and precise. In the **broad sense**, humans as social beings are said to produce their own life, their consciousness, and their own world. Thus, production in the broad sense of the term encompasses a multiplicity of works and a great diversity of forms. Human being have produced juridical, political, religious and artistic and philosophical forms. Even nature itself, as apprehended in social life by the sense organs, has been modified and therefore in a sense produced. Unfortunately, neither Marx nor Engels leave the concept of production in an indeterminate state of this kind. They narrow it down to the level of 'product' as things in space, with the result that the concept loses its broad sense. The narrowing down of the concept brings it closer to the everyday, and hence banal sense - the sense that

the space itself with a view to uncover the social relationships embedded in it, and the process that leads to the production of space. Hence the basis of his proposition: "**(social) space is a (social) product**²⁵".

A number of inferences can be derived from the above proposition²⁶. **One**, if space is a product, our knowledge must be expected to reproduce and expound the process of production²⁷; **two**, if space is produced, if there is a productive process, then we are dealing with history. The forces of production (this includes, nature; labour and organization of labour²⁸; technology and knowledge; superstructures consisting of the state and its agencies, business corporations or capitalist forces, etc.) and the relations of production play a part in the production of space²⁹; **three**, since the forces of production and the relations of production involve the human element which is creative and dynamic, we are therefore dealing with dynamic space. The notion of dynamic space implies that it is possible to explain the process of materialization of change in space and the production of a new space in the context of a dialectical framework involving the forces of production and the relations of production; **four**, the notion of dialectical relationship between the forces of production and their relations of production, implies that the net effect of any (major) change in the forces of production and/or their relationships of production (whether they relate to change in the knowledge base, change in technology, change in market environment, change in regulatory environment, change in ideology

it has for the economists. As a consequence, the concept of 'production' as in the case of the concept of 'labour' loose their attributes of creativity, inventiveness, and imagination.

²⁵Lefebvre (1991, pp.26).

²⁶This proposition should, however, not be accepted in its literal sense, because space, or rather social space, is much more complex and polyvalence in character. Space is never produced like a product in the economic sense, nor is it produced (constructed) like a superstructure, because it is at once a precondition as well as a product of social superstructure. It is a means of production as well as the result of production, and cannot be separated from the forces of production including technology and knowledge, or from the social division of labour which shapes it, or from the state and the superstructures of the society that try to organize and control it. The state and its constituent institutions try to organize the space according to their specific requirements, they, therefore, also become a part of the forces of production. Space is also a network of social and economic relationships. It is the dialectical relationship between the forces of production and their relations of production that combine to produce space, and leave their mark on history.

²⁷Lefebvre (1991, pp.36-37).

²⁸The term labour is used in its broad sense and not the narrow Marxist sense of a proletarian.

²⁹"If space is produced, if there is a productive process, then we are dealing with history; ... the forces of production (nature; labour and the organization of labour; technology and knowledge) and naturally, the relations of production play a part ... - in the production of space". Lefebvre (1991, pp.46).

(for example socialism), etc.), it will lead to a change in the edifice of the existing space. If it is a major change in the forces of production or the relations of production, the consequence would be the production of a new space very different from the earlier one. The production of a new space that followed the dissolution of the feudal societies and the rise of merchant capitalism is an example of the production of a new space³⁰. The same logic is applicable to the production of urban space that followed the industrial revolution. This implies that the space of the contemporary era can be explained in the context of the same logic. The reference is to Daniel Bell's (1974) thesis³¹ of the emergence of post-industrial society in which the economic sectors would see a shift in dominance from the goods producing sector to the service sector, and in which knowledge rather than machines would be the key resource for the generation of wealth. Knowledge, in Bell's view, had altered the course of capitalism and changed its essential characteristics, and hence has contributed to the production of a new space - the space of post-industrial capitalism. Although Bell's thesis is a very important direction flag for understanding the force behind the production of the contemporary space, his thesis is a bit problematical because of the overemphasis on theoretical knowledge not only for directing of innovation, but also as the basis of government policies for social control³².

³⁰According to Lefebvre's (1991, pp.46), "each mode of production has its own particular space, the shift from one mode of production to another must entail the production of a new space". In this respect Lefebvre gives the example of creation of a new space in Tuscany and Venus. In Tuscany, from around the thirteenth century, the Tuscan urban oligarchy of the merchants and the burgher began transforming the lordly domains by establishing a metayage system which resulted in the production of a new space that was neither rural nor urban, but the result of a newly engendered spatial relationship between the two. The result was an increase in surplus and an increase in wealth.

³¹Daniel Bell (1974) was one of the first person to hint the emergence of a new kind of society with knowledge as an essential ingredient. He gave currency to the notion of 'post industrialism' which entailed the replacement of the factory worker image of industrialism by the new professional and technical 'elite' of the service sector. Knowledge, in Bell's view, had altered the course of capitalism and changed its essential characteristics. Just as agrarian societies based on the land had given way to industrial societies based on manufacturing, industrial societies would give way to 'information society' based on telecommunication and computers.

³²Bell's philosophical foundations were founded on high modernism. This is conspicuous in the third element of his theoretical framework: 'axial principle', which he describes as the centrality of theoretical knowledge for the purpose of social control, and the directing of innovation and change. Bell thesis of the post-industrial society is based round the following five elements (1974, pp.14):

1. **Economic sector:** The change from a goods producing to a service economy;
2. **Occupational distribution:** The preeminence of the professional and technical class.
3. **Axial principle:** The centrality of theoretical knowledge as the source of innovation and policy formulation for the society.
4. **Future orientation:** The control of technology and the technological assessment.
5. **Decision making:** The creation of a new intellectual technology.

A more recent and a less problematic critique of the contemporary space has been provided by Nelson (1995). Nelson explains the changing horizon of our contemporary space in the context of a qualitative change in the concept of capitalism itself - a change he refers to as: post-industrial capitalism. According to Nelson in recent years corporations have acquired new resources, qualitatively different from those available in the past. These resources are organizational and knowledge-based and are tantamount to a revolution in the inventory of tactics and strategies available to corporations. He explains the difference between industrial and post-industrial capitalism in terms of three developments that form the kernel of the new era in capitalism: one, an expanded domain of managerial activity; two, a wider base of knowledge for understanding markets and corporations; and three, a more flexible organization capable of translating managerial and professional discretion into competitive advantage. The last of these facets is very important to our discussion on the 'production of space'. It alludes to the managerial prerogative to transform and alter the organizational structure of the business corporation to fit the organizational strategy and the demands of the market environment. The improved information systems of the business organizations of the present era allow the management a holistic snapshot of the business's internal and (to quite an extent) external environment, and also allows them the flexibility to restructure and recreate themselves³³. The implication being, that the space of business organizations in the present era of 'post-industrial capitalism' is very much flexible in scale and scope. Another facet of post-industrial capitalism relates to the globalization of space - a phenomenon also referred to as 'compression of space'. Global space, according to Lefebvre (1991, pp. 125), was a void waiting to be filled. As soon as the technology for producing global space was developed, and the regulatory barriers impeding the process of globalization were removed, the void was filled. Globalization implies not only spatial expansion in the scale of corporate operations, but also the integration of information from the expanded domain of operations into a holistic global corporate strategy. The implication being, that the space of post-industrial capitalism is not only flexible, but also globally integrated in which the local, national, and regional parts are linked together by the business corporations via a holistic global strategy. A crucial ramification of the holistically integrated operations of business corporations of today, is the increase in systemic inter-dependencies between nation-states.

The thesis of production of space is important not only for understanding the process of reorganization of space, and the production of new space. It is also very important to understand the

³³This includes corporate restructuring, mergers and acquisition, strategic alliances, etc.. Other than improvement in information systems that allow management with a holistic view of the business's internal and external environment, and the improved business knowledge of managers of today, a key factor that has made the process of corporate restructuring less difficult is the emergence of specialized consultancy services that actually facilitate this transformation.

space of the present era. It was the technological change initiated by the industrial revolution that lead to the production of a new space that was very different from the previous space. The same logic explains the change we are presently experiencing. Technological and managerial developments not only permit intervention at every level of space (local, regional, national, and worldwide), but also allows management the discretion to restructure and reorganize the space of their business corporations to fit their strategy. As a result, space as a whole (in geographical, as well as historical context) is modified. Not only has the expanse of the space increased, the space itself has become more dynamic. This is the space of the post-industrial era.

In the context of the regulator-regulated dialectic and the tensions in the financial services industry, Lefebvre's thesis of production of space is important on two counts: one, the concept of 'production' implies that it is possible to examine and understand the process of change of space across time. This proposition can be applied to analyze the space of the regulator, as well as the regulated entities (financial institutions). There is a stark contrast in the way the regulators and the regulated entities reorganize their space to take advantage of the opportunities engendered from the change in market conditions (this includes the process of deregulation and the technological innovations in the computer and the communications technology). Although there have been a few initiatives on part of the regulators to meet the challenges of the changing ontological conditions in the financial services industry being precipitated by the financial institutions, they do not commensurate with the dynamics of the space of the financial institutions of the post-industrial era³⁴. The second inference drawn from Lefebvre's thesis of 'production of space' that can be applied to understand the tensions in the financial services industry, relates to the organization of space. The size especially of the major players (in terms of their expanse) is of global proportions. Furthermore, the space of financial institutions is dynamic in scale (size) and scope (functional areas). If the regulators are to achieve their objectives of monitoring the safety and soundness of these institutions, not only should the mental realm (functional expertise) of the regulators commensurate with the operations of the regulated³⁵, but the spatial reach of the regulators should also commensurate with the expanse of the regulated. Furthermore the mental realm and the spatial reach (both of which are incorporated within Lefebvre's concept of social space) of the regulators

³⁴The reference here is to the development of inter-nation institutions, for example, the Basle Committee of Banking Supervisors, and the International Organization of Securities Commissions (IOSCO).

³⁵The reference is to the technical competence of the regulators in terms of their ability to examine the safety and soundness, and robustness against risks of the regulated institutions holistically.

should also be flexible and dynamic to account for the process of the change in the space of the financial institutions (the regulated) of the post-industrial era.

The flexibility of the scale and scope of the business organizations of the post-industrial era of capitalism, and their globally integrated operations implies that any regulatory framework that is not flexible and does not commensurate with the scale and scope of the activities or the structure of the business organization, and does not undertake a holistic evaluation of their risks will not be able to achieve its objectives. Having examined the concept of 'production' or the process of change in space across time, we now examine the concept of space at a point of time, where the area of investigation relates to the organization of space.

5.2. Space at a Point of Time: The Organization of Space - Space as a Network or Relationships:

"The initial basis or the foundation of social space is nature - natural or physical space. Upon this basis are superimposed - in ways that transform, supplant or even threaten to destroy it - successive stratified and tangled networks which, though always material in form, nevertheless have an existence beyond their materiality: paths, roads, railways, telephone links, and so on. ... Each such material underpinning has a form, a function, a structure - properties that are necessary but not sufficient to define it. Indeed, each one institutes its own particular space and has no meaning or aim apart from that space. Each network or sequence of links - and thus each space - serve exchange and use in specific ways. Each is *produced* - and serves a purpose; and each wears out or is consumed, sometimes unproductively, sometimes productively³⁶".

Lefebvre's concept of space is very different from our pre-existing concept of space as a physical thing. He goes beyond the concept of simple physical space. He incorporates the users of the space, and the rationale for the actual use of the space by them, into the concept of social space, thus, allowing us to visualize space and the organization of space in a completely new light. Consequently, the concept of social space implores us to look at physical features like paths, roads, railways, telecom system, etc., beyond their materiality to incorporate the users and their use (or the objective for their use). The concept of social space, therefore, allows us to look at these physical features as part of the organization of space developed by the human beings with the aim of networking human communication. Social space can, therefore, be visualized as encompassing a number of networks with material underpinnings whose primary purpose is to facilitate communication/relationship

³⁶Lefebvre (1991, pp.402-403).

between the subjects. These networks may include geographical features like roads, railways, air routes, sea routes, etc. that serve communication based on physical movements of subjects (human beings) and their material goods. These networks may also include electronic channels of communication like telephones, intranets, internet, electronic exchanges, television, radio, etc., that serve communication based on information transfer between the subjects. Each of these spaces are incorporated into the concept of social space, because the basis of their existence is to serve human interaction, and to foster human relationship.

The concept of space as network interfacing human interaction, that are produced by them to serve exchange, implies that we are faced, not by one, but a multiplicity of social spaces, which we generically refer to as social space. But this multiplicity is different from the multiplicity that arises from segmenting and cross sectioning of space ad infinitum as is the case with physical space. Here, the networks superimpose, and/or interpenetrate themselves over one another³⁷. The development of new networks do not lead to the eradication of the earlier ones from their social context, as the earlier ones were also superimposed over one another over the years. Similarly, the world wide network does not abolish the local (although it does affect it). The phenomenon can be understood in the context of the markets: local, regional, national, and international markets; Each market over the years has consolidated and has achieved concrete form by means of a network: for example, a network of buying and selling points as in the case of markets for commodities, financial markets incorporating a network of banks and securities exchanges, etc.. The real change that has revolutionized the space of the present era, and has made it very different from the space of the earlier societies relates to the evolution and the development of the electronic channels of communications. The development and the proliferation of the electronic channels of communication implies that physical attributes like distance and geographical frontiers of nation-states are no more spatial constraints against interaction. It is possible to intervene and generate space at every level of space: local, regional, national, worldwide. The local market and the local market participants need not remain local any more, it is possible to connect them into a world wide market network via the electronic channels of communication.

".. the *places* of social space are very different from those of natural space in that they are not simply juxtaposed: they may be intercalated, combined, superimposed - they may even sometimes collide. Consequently the local ... does not disappear, for it is never absorbed by the regional, national, or even worldwide level. ... national spaces embraces the regions; and the world spaces does not merely subsume national spaces, but even ... precipitates the formation of new national spaces through the remarkable process of fission. All these spaces,

³⁷Lefebvre (1991, pp.86).

meanwhile, are traversed by myriad currents. The hypercomplexity of social spaces should by now be apparent. ... The principle of interpenetration and superimposition of social spaces has one very helpful result, for it means that each fragment of space subjected to analysis masks not just one social relationship but a host of them that analysis can potentially disclose³⁸".

The above excerpt from Lefebvre's 'production of space' explains the organization of (social) space. Unlike concept of physical space which induces us to visualize space as a 'thing' bounded by physical boundaries that can only be organized by segregation and fragmentation, Lefebvre's concept of social space - space organized as a network of social relationships induces us to visualize space as a 'phenomenon' that can be examined in order to understand the actual organization of space. This is also the significance of the concept of social space - its utility as a tool for examining and understanding the organization of space. The concept can be applied at a macro level, as well as, at a micro level. It can be applied to analyze space of an abstract phenomenon like the space of capitalism, as well as a real phenomenon like the space of the marketplace. The concept can also be applied understand and analyze the organization of space of a market participant (for example a financial institution), as well as that of the political forces (this includes governmental agencies like financial services regulatory agencies) that try to control the operations of the markets and the market participants. The discussion to follow examines, one, the space of capitalism; two, the space of the markets; three, the space of the market forces (financial institutions); four the space of the governmental agencies (regulators); and five, the spatial disjunction between the regulators and the regulated. We begin with the space of capitalism.

5.2.1. Space of Capitalism:

"Capitalism and neocapitalism has produced abstract space, which includes the 'world of commodities', its 'logic' and its world wide strategies, as well as the power of money and that of the political state. This space has been founded on the vast networks of banks, business centres and major productive entities, as also on motorways airports and information lattices. Within this space the town - once the forcing-house of accumulation, fountainhead of wealth and centre of historical space - has disintegrated³⁹".

The above excerpt from Lefebvre draws attention to two important facets of the space of capitalism: one, the concept of capitalism as an ensemble of the spaces, or as a superstructure composed of a

³⁸Lefebvre (1991, pp.88).

³⁹Lefebvre (1991, pp.53).

number of interlinked sub-structures or networks which includes the space of financial markets, the space of commodity markets, the space of the labour markets, the space of the local as well as the transnational corporations which operate in these markets (this includes space of financial institutions), the space of nation-states and the space of the governmental agencies that are representatives of the nation-state) like the national regulators who try to control the space of the capitalism within their geographical boundaries, etc.; two, the consequence of spatial compression, and the development of electronic markets, which have reduced the importance of geographical spaces (or physical markets) like towns as the centre/hub of capitalism.

5.2.2. The Markets:

Lefebvre's (1991, pp.101) describes the form of social space as 'encounter', 'assembly', and 'simultaneity'. Unlike natural space in which things are juxtaposed, social space by contrast implies actual or potential assembly, at or around a single point. Unlike natural space, where the emphasis is on things in space, the emphasis of social space is on the relationships which implies 'encounter' between things in space (here the word 'things' has been used in the broad sense which includes human subjects as well as organizations and institutions involving human subjects). The form of 'encounter' under consideration here is 'dialectical encounter' which implies 'simultaneity' in the relationship between the subjects. All these three forms of social space are discernable in the organization of space of the markets. The principle of the markets involves the accumulation of counterparties at or around a point, rather than the simple juxtaposition of things in space. It also implies centrality, or to be more appropriately, dialectical centrality, i.e., two way rather than a one way interaction between the centre and the periphery. This is echoed in the space of the markets located at the urban centres. This is also echoed in the space of markets for securities, commodities, etc. which require accumulation of counterparty orders at or around a point. The advent of electronic communication has allowed the accumulation of counterparty orders without the need for the bodily accumulation of the representatives of the counterparties at a place of assembly. This explains the transformation of securities markets from floor based trading which required the assembly of the representatives of the counterparties at, or around a point, to electronic trading in which the orders of the counterparties accumulate/assemble at or around a point which happens to be a central computer based trading system, irrespective of the location of the traders, through a telecom network.

5.2.3. The Market Forces (Financial Institutions) :

The concept of social space also allows us to analyze and understand the organization of space of a globally integrated financial institution. Its space is represented by a global network interfacing and

integrating the various sub-entities of the group represented by a number of sub-networks interfacing the markets at regional, national, and even local levels. Thus, the space of a global financial institution may be visualized as a hierarchy of geographical networks with a global network at the top linking the regional networks, which in turn may link the national networks represented by subsidiaries, affiliates, branches etc. A similar sort of arrangement may also prevail in the context of the different functional areas.

The real change that came in the last couple of decades that has created problems for the national regulators relates to the deregulation of market entry barriers, combined with the improvements in the information systems and communication technology which has significantly improved and eased the information exchange across the globe. It has allowed the national and regional networks to be integrated within the global network, and has made holistic operations at global level possible. From the concept of 'production of space', we know that these networks are not static. The financial institutions are continually involved in reevaluating and revising them to take advantage of the regulatory and the technological changes, as well as the changes in the competitive environment of the markets. In the context of the financial services industry, where the dematerialization of money and money related instruments (securities and their derivatives) implies that the world of finance has become oblivious of the constraints of physical space, the visualization of the space of the financial institutions as a network of relationships allows us to draw three inferences that directly affect the operational framework of the regulators of the nation-states: one, that the nation-states are not water tight entities, their geographical frontiers are porous as far as information exchange is concerned. Two, that the national markets are not separate. They are connected via the networks of the financial institutions which are active participants of more than one market. Three, the functional markets (for example, banking, securities trading, insurance, etc.) are also not distinctly separate. They are also connected via the networks of the financial institutions who are participants in more than one functional markets. All these three inferences have important ramifications on the operational framework of the governmental agencies like the regulators whose operational effectiveness is constrained by its sovereign reach.

5.2.4. The Political Forces (The Regulators):

Unlike the markets and the market forces, whose operational framework is a manifestation of Lefebvre's concept of social space - space organized as a network for communication, the operational framework of the governmental institutions like the regulatory agencies is encumbered by the concept of physical space and is based on the organizational principle of physical space which is segregation and fragmentation. This is because nation-states are themselves artificial entities defined by their

geographical frontiers⁴⁰. The regulatory agencies set up with the aim of monitoring and controlling the operations of the markets and the market forces within the confines of the physical space of the nation-state. Hence the geographical frontiers of the nation-state therefore marks the limits of their authority. This is the reason why unlike the globally integrated space of the financial institutions (the regulated entities), the regulatory space is segregated and fragmented into a number of national regulatory spaces. The problem is exacerbated by the functional segregation, and hence fragmentation of the regulatory space within the same nation-state⁴¹. An example is the functional separation between the banking and the securities markets regulators within the same nation-state. Functional separation, by segregating authority among different regulators fragments the regulatory space, thus creating the possibility of leaving parts of financial institutions completely unregulated, and hence certain risks completely opaque from the eyes of the regulators and the other market players. Thus, unlike the market players (the regulated), whose space organized as a network, not only crosses national boundaries but also crosses functional boundaries, the space of the governmental agencies (the regulators) are not only segregated across national boundaries but also across functional boundaries. The implication being the creation of a major problem, not only on account of the functional separation of power which reduces the operational effectiveness of the functional regulators, but also leads to the creation of a major problems of information asymmetry, which cannot be bridged unless the asymmetry in organization of space between the regulators and the regulated (financial institutions) is eliminated⁴².

The question is, why do governmental agencies ignore the organizational framework of the market forces, and instead attempt to organize space by segmenting and fragmenting it. Lefebvre provides the following answer:

"The *ideologically* dominant tendency divides space up into parts and parcels ... It bases its image of the forces occupying space on the idea that space is a passive receptacle. Thus, instead of uncovering the social relationships (including class relationships) that are latent in spaces, instead of concentrating our attention on the production of space and social relationships inherent in it - relationships which introduce specific contradictions into

⁴⁰The emergence of the concept of 'nation-state' was discussed in Chapter Four.

⁴¹The basis of the functional segregation can also be connected to the influence of the organizational principles of physical space: segregation and fragmentation.

⁴²In USA, in the banking industry, the institution of consolidated supervision of banking groups by the Federal Supervisor is aimed at overcoming the problem of fragmented supervision and information asymmetry. There is, however, no such consolidated supervisory requirement for the securities firms in the US Securities and Exchange Commission (SEC) regulations.

production, ... we fall into the trap of treating space as space 'in itself', ... We come to think of spatiality, and so to fetishize space in a way reminiscent of the old fetishism of commodities, where the trap lay in exchange, and the error was to consider 'things' in isolation, as 'things in themselves'"⁴³.

Lefebvre (1991, pp.89) draws attentions towards the blind ideological tendencies which forms the basis of decision making in governmental organizations. This precisely is the problems with governments and public agencies. Instead of analyzing space with a view of uncovering the social relationships embedded in it, the dominant tendency is of counting and/or listing the things, the various objects, that the space contains. The dominant tendency is of organizing space by dividing space and things in space into fragments, and then visualizing each of these fragments as separate parts, and acceding the control over each of these truncated fragments to various agencies, thus setting up mental barriers.

Another explanation for the tendency of government and governmental agencies to organize space by dividing it on the basis of geographical territory may be found in history. In the dark ages of the pre-industrial societies⁴⁴ where the monarchs were the sovereign, control of land (physical space) was the basis of power. The physical frontiers of the land also marked the frontiers of the control and authority of the sovereign. The principle of control within the geographical frontiers of the physical space was coercive power - laying out the law, or the difference between legal and illegal. The principle of sovereignty implied that the sovereign had the absolute power to make any laws, and also the absolute authority to take any action related to his subjects (constituted by people living within the periphery of the physical space of his kingdom). Although we have moved from the pre-industrial to the post-industrial era, and sovereignty has be democratized, the principle of sovereignty has remained unchanged. It is still connected to the physical space. The only difference is that the absolute power of the monarch has been replaced by the absolute power of the parliament. This is very much apparent in the organization principle of the regulatory authority when viewed from a global level. It involves segmentation and fragmentation of authority in line with the geographical periphery that marks the sovereignty of each nation-state. Although we have moved from the pre-industrial to the post-industrial era, the organizational principle and the concept of power employed by the political authorities involving governmental agencies has remained the same.

⁴³Lefebvre (1991, pp.89-90).

⁴⁴These societies were dependent upon the control of labour power and the extraction of primary resources from nature. In these societies, the priests, the warriors, and the feudal were the controlling powers under the ultimate authority of monarch who was also the sovereign power.

5.2.5. The Spatial Disjunction Between the Regulators and the Regulated:

As was the case with the concept of social time, the concept of social space allows us to understand the disjunction in the organization of space existing between the regulators (who are representatives of the governmental agencies) and the regulated (the financial institutions who are representatives of the market forces). Unlike the market forces (financial institutions) whose space is organized as a network that extends beyond the geographical frontiers of the nation-states, the spatial reach of the regulatory authorities is restricted within the geographical limits of the national frontiers. As long as the communication and the information technologies were not adequately developed, as long as the segregation and fragmentation of markets was sustained through regulatory barriers (including strict market entry controls), the spatial disjunctions between the governmental agencies (the regulators) and the market forces (the regulated) were not very conspicuous. The deregulation of these controls, combined with the developments in the communication and information technology has made the spatial disjunctions between the regulators and the regulated conspicuous, and made the regulatory framework problematical with regard to the regulatory objectives.

At the root of this disjunction lies the concept of space which forms the basis of the organization of space. Unlike the political forces including the regulators who conceptualize space as physical space, the private sector financial institutions conceptualize space as a social space. Unlike the organizational principle of the regulators which is based on the principle of fragmentation and segregation, which controls, restricts, and limits communication, the organizational principle of the regulated entities (financial institutions) which is based on the principle of network, instigates and stimulates communication. Thus, unlike the former which organizes by segmenting the space, the latter is involved in integrating space by developing networks interlinking different social spaces. Hence the basis of the organization of their space as a network of branches, subsidiaries, affiliates, etc.. Thus, a clear disjunction in the principle of spatial organization is evident. This disjunction in the concept and hence the organization of space is at the heart of the regulator-regulated dialectic and the tensions in the financial services industry.

The disjunction in the concept of space and the subsequent disjunction in the principle of organization of space between the regulators and the regulated is at the root of a number of problems. One, the concept of physical space implies that each nation-state is an independent sovereign entity circumscribed by impervious geographical borders and therefore segregated from the other nation-states. The concept of social space, however, cautions us that nation-states are connected to each other through the networks of transnational corporations (TNCs). The concept of transnationalism in the context of the financial services industry implies that each bank and securities firm has its own network, and hence its own space, which is not circumscribed by the geographical

borders of nation-states. They may have a nation-state level network represented by branch or subsidiary or affiliate level operations, but that does not reflect the whole picture of their operations. The reason being that this national level network is also connected with the regional and the global level network of the parent. Furthermore, each institution in itself may be composed of a number of internal networks that are representative of different functional activities. It may also be a member of a number of external networks like stock exchange, derivative exchanges, etc.. In a world where the national level sub-networks of the financial institution are increasingly being integrated with the global network of the parent, transfer of contagion and systemic risk have become a cross border reality. Visualization of national market as a sovereign entity bounded by the geographical frontiers of the nation-state that can be controlled by the governmental agencies, hinders rather than help us in taking cognizance of the problems of the present era.

Two, the regulatory framework of the regulatory agencies by limiting its spatial expanse to the area circumscribed within the geographical frontiers of their nation-states tends to focus only on the space represented by the national level network of the financial institution, and ignores the rest. National regulators, therefore, get a partial view of the risks related to the operations of the financial institutions (the regulated). This problem is more serious in the securities industry where the absence of any regulatory provisions for consolidated supervision, combined with the geographical and functional segregation, implies that each regulator gets a partial (and therefore incomplete) picture of the financial position and hence the risk profile of the securities firm. This implies that the regulators do not have a picture of the global risk profile of the financial institution, nor do they have the authority to control the potential risks that emerge from outside their geographical frontiers.

The problem with the policy makers and the regulators of the nation-states is not that they do not realize the existence of these disjunctions between them and the private sector financial institutions. The problem is not that they have not taken any initiative to overcome the problem of spatial disjunction. The problem lies in the strategy applied for overcoming the problem. In the context of the European Union, the problem of spatial disjunction has partially been surmounted through the institution of the home country regulation/supervision allowed under the Investment Services Directive (1993), and the Second Banking Coordination Directive (1989). This is an incomplete solution on two counts: one, the expanse of the European Union Directives is only applicable within the geographical frontiers of the European Union; and two, home country supervision brings to the fore a new problem: the problem connected to the differences in supervisory competencies among the national regulators. While the differences in the regulatory standards have been surmounted through the directives on harmonization of minimum regulatory standards, the differences in supervisory competencies regarding the enforcement of regulations, on

the other hand, have been completely neglected. The strategy completely neglects the potential problems that can be created on account of the differences in supervisory competencies between the regulators of nation-states⁴⁵.

The strategy of harmonization being undertaken under the umbrella of multilateral forums like Basle Committee on Banking Supervision and International Organization of Securities Commissions (IOSCO) to overcome the problem of spatial disjunctions is also problematical. The aim of harmonization is to remove the friction between regulatory authorities in the context of the differences in their regulatory framework. It does not involve a re-examination of the suitability of the present regulatory framework based on minimum quantitative standards for meeting the challenges of time and space compression. The implication being, that if the regulatory framework itself is problematical, then the harmonization strategy also becomes problematical. The harmonization strategy also brings into focus a number of other problems. It brings into focus the problem of universalism versus particularism. The differences in perception of the policy makers of different nation-states towards risk, and the differences in their regulatory and supervisory competence combined with the interest group politics played by the home-base financial institutions brings into focus the dialectical interaction between universalism and particularism. The dialectical relationship between universalism and particularism also brings into focus the problematical aspects of the process of universalization. For instance, there is a possibility that what is presented and promoted as a universal framework may actually be an ethnocentrically conceived product of the nation-state actually presenting and promoting the framework. After all the Basle Accord was also the joint product of a bilateral cooperation of the US and UK banking regulators which was later-on presented through the multilateral forum of Basle Committee as a universal product. Furthermore the process of harmonization which involves the negotiations between the regulatory authorities of different nation-states is itself a problematic process in which the final product is generally a watered down version that satisfies all rather than the best solution. The European Union Directives on Deposit Guarantee (1994)⁴⁶ and the Capital Adequacy Directive (1993)⁴⁷ are examples of this predicament.

The harmonization strategy reflects a total belief in the present regulatory framework and regulatory tools like capital adequacy to cater for problems like failure of banks and securities firms and the transfer of contagion that may develop into systemic risk. It does not involve the

⁴⁵Refer to Diver (1980) on the problems of regulatory enforcement.

⁴⁶Discussed in Chapter Two (McKenzie and Khalidi, 1994).

⁴⁷See Dimson and Marsh (1993), and Khalidi (1996).

development of a new framework to meet the problems of the rapidly changing ontological conditions. It is simply a strategy to: one, reduce the friction between the regulatory authorities in the context of differences in regulatory standards; Two, surmount the problem of regulatory arbitrage that can be created by the differences in regulatory costs endured by the regulated entities (banks and securities firms); and three, eliminate the areas of regulatory laxity that have the potential of becoming the source of cross border contagion and/or systemic risk. The harmonization strategy is therefore aimed at overcoming (a few of) the consequences of the spatial disjunctions between the regulators and the regulated rather than the disjunctions or the causes of the disjunctions themselves. This is the crux of the problem facing the regulators in the financial services industry which Lefebvre's concept of social space brings to our realization.

6. Conclusions:

The objective of the chapter was to examine the tensions in the financial services industry in the context of the problematic of spatial compression. The aim was not only to investigate into the problematic of spatial compression, but also into the problematic of space itself. In line with this aim, the chapter was divided into two main themes: the first one was on the problematic of spatial compression and its ramifications for the regulators in the financial services industry, while the second theme was on the problematic of time itself, and its ramifications for the regulators in the financial services industry. The first theme was further divided into two sub-themes: one, the concept and consequences of globalization, and two, the concept and consequences of spatial compression. While the discussion on globalization involved an examination of the concept and the consequences of globalization, the emphasis of the discussion on spatial compression, on the other hand, was towards examining the concept of spatial compression which forms the basis of globalization. The investigation into concept of globalization brought to the fore some of the interesting facets of the globalization phenomenon, for example, globalization as the process of creation of linkages and interconnections, which transcends the states and societies which make up the modern world system; globalization as the reduction in the barriers of social and physical distance; globalization as the annihilation of space through time, and as a consequence the fusion of time and space; globalization as a technological universalism that is also removing the spatial distinctiveness and identity of places crystallization of the entire world as single place, etc.. The key force behind globalization are the transnational corporations, and a key outcome of the globalization process is the alteration of the nature, scope, and capacity of the sovereign states in terms of their regulatory ability which is being

challenged and reduced (in some spheres) by the market forces. The consequence of the emergence of a highly interconnected global system is that many of the traditional functions of a nation state cannot be fulfilled effectively without some sort of international cooperation and coordination. As a result new issues are thrust on to the global agenda requiring global management or at least global regulations wherever global externalities are involved. Whether it is the question of pollution control, whether it is the question of depletion of ozone layer, whether it is the question of prudential control of the financial services industry, wherever transborder externalities are involved, national solutions are to no avail. For transborder matters global arrangements are a necessity. The existing framework of regulations within the financial services industry was developed during the period when the banking and securities markets of nation-states were isolated from each other. In today's global economy where the markets are in competition with each other and the banking and securities firms have become or are in the process of becoming transnational conglomerates, the regulators who are still constrained by the geographic boundaries of the nation-states are losing their autonomy for action, and as a consequence, their ability to control the risks within their jurisdictions. The implication being the need for a fundamental rethink of the regulatory strategy in line with the changed circumstances if the regulatory objectives are to be achieved. This was also the conclusion of the second sub-theme on the problematic of spatial compression⁴⁸, but with a difference. It also provided direction flag for further investigation - the connection between the concept of space and its influence on the operational framework of the regulators and the regulated. This was also the basis of the second theme of investigation of the chapter - the need for a reexamination of the concept of space itself. This was also the basis of examining Henri Lefebvre's concept of social space - a concept that not only allows us to take a holistic view of the space 'at a point of time', but also allows us to understand the process of change of (social) 'space across time'. These two facets of the concept of social space were therefore examined in detail. The process of change in space across time has been explained by Lefebvre as 'production of space'. The concept of production of space implies that space is not static, it is in the process of evolution and change. It also points to the dynamism and creative capacity embedded within the concept of social space. The concept of 'production of space' is, therefore, the key to understanding of the process of change in space of the financial services industry, and the consequences emanating from the change for the regulators. Lefebvre's thesis of production of space is important because it draws attention to, one, the flexibility and dynamism inherent in the space of the financial institutions (regulated entities); and two, the fact that any regulatory framework that is not flexible and does not commensurate with the scale and

⁴⁸where the emphasis was on investigating into the concept (and consequence) of spatial compression which forms the basis of globalization.

scope of the activities or the structure of the business organization of the regulated (financial institutions), and does not undertake a holistic evaluation of their risks will not be able to achieve its objectives. The second facet of Lefebvre's concept of social space relates to the concept of space at a point of time where the emphasis is on the 'organization of space'. Lefebvre's concept of space is very different from our pre-existing concept of space as a physical thing. He incorporates the users of the space and the rationale for the actual use of the space into the concept of social space, thus, allowing us to visualize space and the organization of space in a completely new light. Social space is visualized as encompassing a number of networks with material underpinnings whose primary purpose is to facilitate communication/relationship between the subjects. These networks not only include geographical features like roads, railways, air routes, sea routes, etc. that serve communication based on physical movements of subjects (human beings) and their material goods, but also electronic channels of communication like telephones, intranets, internet, electronic exchanges, television, radio, etc., that serve communication based on information transfer between the subjects. Lefebvre's concept of social space, organized as a network of social relationships induces us to visualize space as a 'phenomenon' that can be examined and studied with the view of discovering and exposing the actual organization of space. The significance of this concept relates to its utility as a tool for examining and understanding the organization of space was demonstrated by visualizing the space of capitalism, the space of the marketplace, the space of a market participant (for example a financial institution), and the space of the political forces (this includes governmental agencies like financial services regulatory agencies) that try to control the operations of the markets and the market participants. The concept was also applied to examine the disjunction and the implications of the disjunctions in the organization of space of the regulators and the regulated. Unlike the financial institutions whose space is organized as a hierarchy of geographical and functional networks spanning a number of markets, the organization of the space of the regulators is encumbered by the limitations of physical space (whose principle of organization is segregation and fragmentation). When we combine this disjunction with the earlier discussed disjunction related to the production of space (unlike the regulators whose space is static, the financial institutions are actively involved in managing their space to take advantage of the market opportunities), the logic for the tensions in the financial services industry become apparent. These disjunctions are direction flags that needs to be targeted by the regulators as a source of tensions in the financial services industry.

PART

V

CONCLUSIONS

CHAPTER TEN

CONCLUSION

What is called 'deconstruction' is concerned with (theoretically) and takes part in (practically) a profound historical transformation (techno-scientific, political, socio-economic, demographic) which affects the cannon, our relation to language and to translation, the frontiers between literature, literary theory, philosophy, the 'hard' sciences, psychoanalysis and politics and so on. Deconstruction therefore finds itself at the heart of what you call 'tensions'. It is a question of assuming these tensions, of 'living' them as much as of 'understanding' them. Those who fear and wish to deny the inescapable necessity of these transformations try to see in deconstruction the agent responsible for these changes, when in my eye it is above all else a question of trying to understand them, of interpreting them, so as to respond to them in the most responsible fashion possible."

Derrida (1995b, pp.413)

The above citation from Derrida regarding the relationship between deconstruction and tensions in the realm of literary theory bears some resemblance to deconstruction and tensions in the financial services industry. In line with Derrida's explanation this thesis may be regarded as an effort towards understanding and interpreting these tensions. It is after all our understanding of the problem that forms the basis of our actions.

The origin of the thesis lies in the two papers incorporated in Part II of the thesis, both of which can be described as a critique of the regulatory framework in the sense that they provide direction flags to the multiple level of tensions in the financial services industry. Chapter two examined the tensions in the context of the EU Directive on Deposit Insurance, which included: one, tension between the safety net provided by the deposit insurance and the problem of moral hazard, a problem that rationalizes the principle of depositors co-insurance. The problem with this solution is that not only is it contrary to the goals of the Deposit Guarantee Directive of a safe and sound financial system, but also the depositors are not provided adequate information for monitoring; two, the tension between the Deposit Guarantee Directive and the other financial market directives, especially the Bank Solvency Directive, a tension which is connected to the difference between book value and market value of bank capital, the difficulty in differentiating between solvency and liquidity problems, differences in the objectives of central banking and banking supervision, and the problems connected with the timing of the bank closure or wind-up; three, the tensions between the

objectives of the deposit guarantee directive and the 'principle of subsidiarity'¹. This includes the tension between the host and the home country minimum standards, tension between the deposit insurance and the lender of last resort functions, tension between the difference in treatment for foreign branches and subsidiaries, tension between the de-jure and de-facto deposit guarantee with respect to the 'too big to fail' principle, tension between the private and public deposit guarantee schemes, etc..

Chapter three took the critique a step further. It involved an examination of the tensions on a much broader level: tension between the power of regulatory authorities as embodied in mathematical formulae contained in regulations and the power of financial institutions that is exerted through the markets; tension between the constructive and destructive nature of financial innovation and the inability of regulators to keep pace with change; tension between universal norms contained in regulations and transient and uncertain market relations; tension between competition and safety within financial markets; tension between a desire for uniformity by regulators and a desire for difference by financial institutions; tension between transparency and opaqueness in the flow of financial information; tension between the regulators constrained by the boundaries of the nation state and the industry which now has no territorial constraints; tension between the regulators who are extra-market and the industry which is free to innovate within market structures; tension that inappropriate regulation may engender financial fragility. Chapter three was a direction flag to the multiple level of tensions in the financial services industry emerging as a consequence of the tensions between the changes in the structure of the industry being brought about by the creativity of the market forces, and the problematical nature of the control engineering framework of the regulators which is based on linear progress, rational choice, and a desire for unchanging social order - a framework which is inconsistent with the challenges of the dynamic market environment of the present era which is being controlled by the entrepreneur driven financial institutions. Since the regulators are not a part of the process, they cannot keep pace with it, and hence cannot control it. The gradual changes in the regulatory philosophy emerging in the financial services industry is perhaps a realization of the problem. The conclusion of chapter three which was also the conclusion of part II of the thesis was: is it possible to have financial calm and order in a dynamic and competitive environment driven by the entrepreneurial forces? The only answer that one can suggest to such a question is, if the operations of financial markets are going through a paradigm shift, the researchers should also be prepared for a paradigm shift in the way they seek to understand these

¹The smaller units right to act is operative to the extent and only to the extent that it alone can act better than a large unit in achieving the aims being pursued.

markets. At minimum they should be prepared to raise questions and to raise direction flags that may help us in understanding the tensions in the financial services industry.

This conclusion of part II was also the objective of part III and IV of the thesis. The aim of part III and IV (both of which were written concurrently) was not that of formulating policy objectives, or of proposing an alternate system. The aim was only to investigate into the problem, but from a different angle so as to be able to provide a different perspective on the tensions in the financial services industry. This was the rationale for examining the problems related to the regulatory framework in the financial services industry at the level of its philosophical foundations: the modernist philosophical thought. Investigation at the level of philosophical foundations allows a lot of latitude or freedom for research, which is apparent in the discussion on the modern and the postmodern philosophical thought in part III of the thesis. A similar analogy is applicable to part IV of the thesis which involved not only an investigation into the phenomenon and problems of time and space compression, but also an analysis of the problems with our conventional concepts of time and space. It also involved an examination of some alternate concepts of time and space in an effort to understand some of the problems of the present era interfacing the dimensions of time and space.

The driving force behind the discussion in part III was the hypothesis that:

- one: the tensions reflecting the regulatory crisis in the financial services industry may be a subset of, or a part of a much wider area of tensions/crises facing the conceptual foundations of the regulatory philosophy: the modernist philosophical thought.**
- two, the alternate philosophical thought which is generally described as postmodernism, may provide us with inspiration and ideas for the formulation of a regulatory strategy and regulatory framework that may facilitate the achievement of regulatory objectives while facilitating the amelioration of the tensions inherent in the financial services industry.**

Investigation into the history of the modernist philosophical thought, allowed us an insights into the origin of a number of problems of the present era. It also allowed us an insight into the problematical concept of nation-state and the framework of inter-national and intra-national society developed during the last quarter of the nineteenth century and the first quarter of twentieth century. It also allowed us an insight into the problems created when a rigid framework or a static meta discourse is imposed across time and space. The different phases of the crises and the regeneration of the modernist philosophical thought are an evidence of this problem. The present crisis is different from the earlier ones, because it is not simply a crisis connected to the change in the ontological conditions, rather, it is a crisis connected to the speed of change in our ontological conditions which implies a major reduction in the time span for the survival of a meta discourse. It was this conclusion that formed the basis of the storyline of chapter five which involved an attack

on the central dilemma of the modernist philosophical thought: the philosophy of 'becoming'. Examination of Max Weber's 'Theory of Bureaucracy', and Marx and Engels' 'Manifesto of the Communist Party' in the context of Schumpeter's 'Theory of Economic Development' allowed us an insight not only into the central flaw with the static or rigid framework of the modernist theories, but also brought to the foreground the force behind the change which creates a discontinuity in the circular flow and as a consequence affects the assumptions that form the basis of the economic and social theories of the modernist philosophers and social scientists. Schumpeter's 'Theory of Economic Development' is also important because it allows us to understand and appreciate the concept of market mechanism. It allows us to extend the basic idea of the theory (by incorporating the changes in the business world) to explain the speed-up of the momentum of the development process, and the compression in the time frame for the survival of the modernist meta theories. Hence the crisis of confidence in the modernist philosophical thought and the theories and frameworks based upon it.

Schumpeter's 'Theory of Economic Development' is also important because it bears comparison with Jean-Francois Lyotard's (1984b) definition of postmodernism as 'not modernism at its end but in the nascent state, and this state is constant', which implies a permanently revolutionary state. Hence, the rationale for part II of the hypothesis that suggests the need for examining the postmodern philosophical discourse as a source of inspiration and ideas. But investigating into the concept of postmodernism is not without its hazards. The reason being that the label of postmodernism has been associated with a variety of phenomena some of which makes sense, while some do not. It was therefore necessary to unravel the confusion surrounding the concept of postmodernism in order to be in a position to examine the postmodern philosophical thought as a source of ideas and inspiration (or direction flags) for understanding the problems of the present era, in general, and the tensions in the financial services industry, in particular. The unravelling of this confusion is itself a contribution of the thesis because it not only clears the way for a positive investigation into the concept of postmodernism, but also provides a sense of direction for examining the concept of postmodernism itself. This was the rationale for applying more than one approach for examining the concept of postmodernism. Since the aim of examining postmodernism (as per part II of the hypothesis) was that of providing a source of ideas and inspiration (or direction flags) for understanding the problems of the present era, three distinct but inter-related approaches were applied to examine to concept of postmodernism and its implications for the financial services industry. These were: one, postmodernism as an epoch; two, postmodernism as a reaction to or a departure from modernity; and three, postmodernism as a signifier of the problematical features or the limits of modernity. Under the first approach

(postmodernism as an epoch), postmodernism is visualized as a period of major historical transition of our society from the modern to the postmodernism epoch - the term 'post' signifying the transitional present. This approach was examined in the context of three sub-themes: one, postmodernism as a concept that alerts us to the changes in the social, cultural, and political conditions and practices in the society; two, postmodernism as a concept that signifies an epochal shift in the operations of capitalism: the inauguration of a new stage in capitalism - the stage of post-industrial capitalism; and three, postmodernism as a concept that signifies a realization and acknowledgement that systems have changed radically which have thrown up new forces and new configurations, and that old categories cannot be slapped on to the new forms - a reevaluation and reassessment of the problems is therefore necessary. Postmodernism therefore signifies a departure in our way of thinking about what could/should be done about the problems connected to the ontological conditions of the new epoch. Each of these three sub-themes examined in the context of the concept of postmodernism as an epoch serves as a direction flag for examining the tension in the financial services industry. Of these, the third theme incorporating Caldwell's (1975) essay is of special significance. The essence of his argument is that the most crucial problem facing a society during transitional periods is the differential rate of change between the attitude and beliefs of the general public and private sector agencies (or the governed), and the adaptive changes in the attitudes and the operational framework of the public agencies. It is this disjunction that is the source of the problems. The key to the resolution of the problem is the realization of the change, and the need for an adaptive change in our attitude towards the change. For this, a reorientation of the knowledge base of the personnel of governmental agencies is necessary. The characteristics required for the management of public affairs during a transitory period are foresight, initiative, flexibility, and sensitivity. This requires intellectual development and the broadening of the knowledge base of the public officials. The type of knowledge required by the public officials (for example the regulators in the financial services industry) is the knowledge of trends, interactions, and synergistic effects, and not the quantifiable technically oriented knowledge, or the knowledge of procedural know-how, which forms the major knowledge base of the public agencies. Unfortunately, however, public agencies still seem to be oriented towards quantifiable technically oriented training, thus they risk neglecting the 'essential' through their preoccupation with the 'practical', which is unfortunate, because the tasks requiring technical knowledge (technical tasks) can be out-sourced to the private sector for whom the competitive mechanism of the market forces would insure against obsolescence of knowledge. The task of public agencies (regulators) during transitional periods necessitates the reassessment of priorities, redefining of goals, and devising the means towards the creation of material and intellectual environment to stimulate all social agencies to play their needful role in this

transition. However to be effective, and this is very important, the knowledge should be socially shared. For the regulators in the financial services industry, the emphasis here is on transparency, the emphasis here is on sharing of information with the markets to improve the market mechanism, because in a high technology society, the most knowledgeable administrators would be helpless without informed collaborators. It requires administrators (regulators) who have the intellectual honesty and self confidence that is required for sharing the knowledge with the public. The key to success is effective organization and wide sharing of knowledge in order to enable to the public agency to more readily achieve the public goals with reduced probability of error, yet also enabling an informed public to challenge administrative action where the use of public authority appears to be improper or unwise. This is also the advice for the regulators in the financial services industry.

The second approach for examining the concept of postmodernism basically involved an examination of the counter concepts presented within the realm of postmodernism, counter concepts which could be described as a reaction to or a departure from modernism which has been defined as "positivistic, technocentric, and rationalistic", and "the belief in linear progress, absolute truths, the rational planning of ideal social orders, and the standardization of knowledge and production²." To understand and appreciate the power and the potential of these counter concepts in encouraging a reconceptualization of the way we imagine, think, plan, and rationalize, it was necessary not only to examine some of the counter concepts that characterize the concept of postmodernism as a reaction to modernism, but also to examine the source of inspiration and the underpinnings of power of this mode of thinking. The examination of Foucault's genealogical analysis of knowledge, and Derrida's deconstructive analysis of knowledge was undertaken for this purpose. The basis of power of Foucault and Derrida's philosophy relates to their ability to take control of knowledge rather than allowing knowledge to control them. It was their ability to interrogate and to locate the problematical facets of the concepts introduced within the realm of the modernist philosophical thought, that not only formed the basis of the power of their own discourse, but also provided the inspiration for the development of counter-concepts that have the power to rebel against and challenge our conventional (modernist) concepts. The counter concepts examined within the realm of the concept of postmodernism as a reaction to or departure from modernism covered eight areas/elements of our ontological assumptions namely: the problematic of disciplinary research; the concept of representation; the concept and the relationship between the author, the text, and the reader; the concept of subject; the concept of truth; the concept of theory; the concept of history; and the concept of space. These counter-concepts which emerge from the problematical nature of the modernist concepts, provide us with a different perspective for examining and understanding the

²Harvey (1992, pp.9).

problems of the present era. They caution us to approach the concepts of representation, theory, and truth with a bit of scepticism. By widening the concept of text, they encourage us to expand the horizon of our analysis. By reducing the power of the author they caution us as writers to view our text as direction flags, and not as statements of truth. This is also the message for the readers who are transformed from passive to an active reader. This is also the message for the regulators and the regulated.

The final approach, postmodernism as a signifier of the problematical features or the limits of modernity characterizes postmodernism as a concept that goes beyond modernity in the sense that it points to the limits of modernity. This approach incorporates the works of philosophers and academics who find the project of modernity to be deeply problematical. They point to the discontinuities in the history of modernity, and the problematical facets of the once-and-for-all or timeless meta-discourses developed by the modernist philosophers and social theorists in their quest for a rationalized world. Their endeavour is to lay out the problematical facets of modernity, while at the same time also making an effort to explore and understand the social and political codes and practices like tradition, ethnicity, etc., which were ignored or rejected by modernist philosophers (whose aim was to homogenize the social in line with the meta-discourses of the philosophers and social theorists, and to develop standardized citizens of geographically bounded nation-states). They draw attention to the problematical nature of the metaphysical presuppositions that underlie the modernist philosophical discourses, and hence the problematical nature of the modernist philosophical thought itself. Postmodernity under this approach, is therefore, modernity becoming conscious of its problematical principles and practices. This approach also provided the stepping stone for an exploration into some facets of the philosophy of Jean-Francois Lyotard, Michel Foucault, and Jacques Derrida, as a source of inspiration and ideas for understanding the tensions in the financial services industry.

Lyotard's essay 'The Postmodern Condition: A Report on Knowledge' was important because it introduced us to a number of ideas that provide us with new insights for understanding the tensions in the financial services industry. An example is Lyotard's conceptual framework of language game as a tool for understanding the gradual change in the regulatory framework and regulatory philosophy that we are experiencing. The framework of language games also provides an explanatory logic for the regulatory dialectic in the financial services industry which is a reflection of the agnostic countermoves of the financial institutions (the regulated). Agnostic countermoves by the financial institutions (the regulated) were also the driving force behind the emergence of the pre-commitment approach which is a very important change in the regulatory framework, because it involves a paradigm shift in the regulatory approach - a change from prescriptive

approach to regulation to a performative approach to regulation. The concept of language game also allows us to understand the contrary effect of terror on the language game. The system of regulation in the financial services industry which is based on prescriptive approach to regulation is based on terror as the basis of its application. Terror destroys the language game. The effect of globalization has been the reduction in the ability of the regulators to terrorize the regulated entities. The tensions in the financial services industry are a reflection of this phenomenon. In the context of the concept of the language game, one possible strategy would be a change from prescriptive to evaluative approach to regulation, which would imply increased importance of qualitative supervision. But to achieve the desired effect, it is essential that the results of the supervisory evaluation be shared with the market participants, because improvement in the quality of transparency of the markets can not only improve the performativity of the market players, but also the efficacy of the market's own self regulatory mechanism. Another important facet of Lyotard's work relates to the problematical nature of the theories of social science. Lyotard allows us an insight into the limitations of theories of natural science when applied to problems connected to social science, an insight that allows us to understand the problems with the presumed objectivity and scientificity of the quantitative ratio based regulatory framework in the financial services industry. The final aspect of Lyotard's essay that was examined relates to paralogy and not consensus as a source of inspiration for the future. Paralogy emphasizes on dissention and search for the unknown rather than the known, thereby encouraging us to think differently, and think creatively. It encourages the sustenance of creative turmoil that is necessary for meeting the challenges of the rapidly changing ontological conditions. However, to achieve this, two things are important: one, renunciation of terror that underlie prescriptive utterances; and two, any consensus on the rules defining a game must be temporary (i.e., agreed by the present players and subject to their eventual cancellation). This is also the message for the regulators.

Foucault's philosophical enterprise that was examined relates to the problematic of power, after all the tensions in the financial services industry are a consequence of the dialectics of power between the regulators and the regulated. Three policy implications emerging from the examination of Foucault's discourse on power are important: one, the circular relationship between power and truth: "we are constrained or condemned to confess or to discover truth". The pursuit of power encourages us to produce truth. In the context of the financial services industry, the regulatory initiative of J.P.Morgan with respect to RiskMetrics can be described as 'the pursuit of power through the production of truth'. It was an act that challenged the status of the regulator as the sovereign producer and dispenser of truth, and brought about a revolutionary change in the nature of the regulatory framework. The reference is to the development of the pre-commitment approach

to regulations which was a change from the prescriptive approach to regulations to performative approach to regulations. Now J.P.Morgan has produced yet another discourse on truth: CreditMetrics. It is only a matter of time before it also becomes a part of the regulatory framework in the financial services industry. Two, we should direct our researches not towards the juridical edifice of sovereignty or the state apparatus and the ideologies that accompany them (i.e., instead of examining and analyzing power in terms of the regulated and legitimate forms of power in their central locations and their general mechanism of operations), our analysis should be concerned with power at its extremities, at its ultimate destination, at the point where it is in direct and immediate relationship with its object, its target, its field of application, at the point where its intention is transformed into effective practices. It is here where it (power) installs itself and produces its real effects. The implication being the need for a change in focus from the 'problematic of regulations' to the 'problematic of supervision' where the emphasis is on regulatory enforcement. This is the key area of weakness in the regulatory conundrum which has only recently become the focus of regulatory scrutiny. The reference is to the publication of '25 Core Principles on Banking Supervision' released by the Basle Committee on Banking Supervision. Three, the disjunction in the form of power employed by the regulators and the regulated. Unlike the regulators whose source of power is the sovereign power - a form of power that is dependent upon and affected by the limitations of the sovereign power of the nation-state (which has been affected by the phenomenon of globalization), the power of the regulated (financial institutions) is based on disciplinary power - a form of power that is dependent upon knowledge. The increased pace of knowledge generation provides an explanation for the increasing power of the financial institutions. This is not the only problem. The source of the problem is the regulatory framework itself which finds its basis in the codes of normalization which are a part of disciplinary power. Applying these disciplinary codes through the instrument of law (which is a tool for the implementation of sovereign power) leads to a number of problems. Four of them are worth discussing here: one, such rules of normalization (disciplinary codes) are based on knowledge and need to be updated regularly with the developments in knowledge. The problem with such rules of normalization that are transformed into legal codes is the risk of becoming frozen in time and becoming outdated and incompatible in the context of the present state of knowledge, and the present state of market development. This problem is quite evident in the financial services industry, and is a major cause of tensions. Two, the rules of normalization that are a part of disciplinary power are required to be exercised continuously. The problem with sovereign power is that it is analogous to bio power and therefore involves the levy of discontinuous obligations over time; three, the problem with legal codes is that they lay out the limits between legality and illegality. This allows the regulated entities to prospect for loopholes

within the law, and use of loopholes in the text to bypass the context of the law while adhering to the text of the law. Putting it another way, as long as you are within the limits defined by the law, you have the right to bypass the spirit of the law. This is a very important facet of the problem of regulatory dialectic. Four, the problem with law is that it has a negative feel to it. It is analogous to power that says no. Conversion of rules of normalization into legal codes leads to the loss of the positive aspect of power - power that creates knowledge, power that creates desire. As a consequence they appear to be repressive, and therefore instigate resistance. The tensions in the financial services industry are an evidence of this problem. One avenue for bridging these problems is the supervisory tool of bank examination, which itself is a form of disciplinary power. But to have the desired effect it needs to be combined with another form of disciplinary power: Foucault's interpretation of the principle of 'panopticon: power through transparency', which implies the need for the regulators to share the result of their bank examination with the markets to improve the market's own self regulatory mechanism.

Jacques Derrida was the third philosopher whose philosophy was explored. Two approaches were applied to examine his philosophy of deconstruction: one, the concept of deconstruction in the broad sense, i.e., the concept of deconstruction as a philosophical thought aimed at achieving new enlightenment by questioning the axioms of old enlightenment, where the emphasis is on opening up the text to reveal the tensions in the text in an effort to understand them. This was also aim of the thesis. The second approach applied for examining Derrida's philosophy of deconstruction relates to the concept of deconstruction in the narrow sense, i.e., deconstruction as the strategy that Derrida applies to deconstruct the text of other philosophers, to reveal the tensions in their text, where the aim is to reveal the precariousness of the texts that were revered as discourses of truth (or *a priori* truths). Derrida's deconstruction strategy draws attention to the problems with the language in conveying its meaning. In the context of the tensions in the financial services industry, the mechanics of Derrida's deconstruction strategy involving the application of the concepts of 'supplementarity' and 'differance', allows us to realize that accounting, after all, is a language (the language of finance) and suffers as in the case with any other language in conveying meaning. It cautions us to realize that bottom line figure like capital do not necessarily tell the truth. It cautions us to realize that the notion of Basle Accord as the harmonized global standard of the capital adequacy regulations is problematical - problems remain in the differences across nation-states in the accounting framework, differences in the tax code (which have counter-prudential effects), and the differences in the requirements for the provisions for bad debts, etc.. The message for the regulators and the users of financial statements is that accounting is also a language, we should not blindly believe in the bottom line figures like the value of the capital as statements of truth. They

should be placed under erasure - crossing them, but allowing them to be legible thus undermining their truth value, and implying the need to deconstruct the accounting information presented in the financial statements in order to reveal the tensions underlying those statements.

Part IV of the thesis was based on the problematic of time and space compression. In order to give equal importance to the dimensions of time and space, each of these two dimensions were examined separately in different chapters. The aim was not only to examine the concept and the ramifications of time and space compression for the financial services industry, but also to investigate into the problem from a different angle, in order to broaden our knowledge base, to generate a different perspective that may help us to understand and appreciate the problems of the present era. This was the reason for examining the concept of time and space compression as two separate concepts. This was also the reason for applying two approaches for examining the phenomenon of time and space compression: 'at a point of time' and 'over a period of time'. This was also the reason for reexamining the concepts of time and space, and going beyond our conventional concepts of time and space in the search for answers to the problems of the present era.

The chapter on the problematic of temporal compression involves the application of two approaches for examining the problematic of temporal compression and its ramifications for the regulators in the financial services industry: temporal compression 'at a point of time' and 'over a period of time'. When the consideration was on temporal compression 'at a point of time', the emphasis was on the implications of the speed-up or the intensification of our economic processes for the policy makers of nation-states in general and the regulators in the financial services industry in particular. This includes increase in volatility, and ephemerality, reduction in profit margins, reduction in time for decision making, increased risk of business failure, reduction in time for undertaking correcting action to control problems, etc.. When the consideration was on temporal compression 'over a period of time', the emphasis was on the basis or the logic for temporal compression 'at a point of time', - a phenomenon that can be connected to the speed-up of the change in our ontological conditions over a period of time which included the speed-up of the processes of knowledge generation, innovation, and entrepreneurialism, and hence an increase in the momentum of the development process and the increase in the discontinuity in the temporal flow. This approach was important because it brought to our realization the inadequacy of our mechanical concept of clock time. Although time is the dimension of change, the mechanical concept of clock time, by severing the subjective component of time from the objective component of time, creates problems in our ability to understand the dynamics of the change, the consequences of this change, that we are experiencing. Hence the rationale for a reevaluation of our concept of time,

including the search for alternate concepts of time. Two concepts were examined in this respect: one, the concept of dialectical time which combines the clock time, the social time, and the biological time into one holistic concept of time. This concept, by combining the subjective and objective facets of time into a holistic concept, allows us to understand the dynamism of change that the concept of time represents. Not only are we (our thinking) changing with the changes in our ontological conditions, but we through our actions are also changing the ontological conditions. This is very true in the context of the actions of the regulators and the regulated in the financial services industry. The concept of dialectical time also allows us to realize the problems that arise when a static framework is imposed on a societal group, as is the case with the regulatory framework in the financial services industry. The other concept examined was the concept of temporal awareness or social time. It involves an examination of Gurvitch's (1964) framework of social time to examine the social time of the financial services industry as a whole, and the social times that are representative of the regulators and the regulated. Gurvitch's framework of social time, brought to the fore the disjunctions in the temporal awareness of the regulator and the regulated, and thus provided a direction flag for a possible avenue of action by the regulators. The overtone being the need to address this issue of disjunction in temporal awareness if the tensions in the financial services industry are to be controlled.

The aim of the chapter on spatial compression was two fold: one, to understand and appreciate the concept of globalization and/or spatial compression and its consequences; and two, to draw attention to the inadequacy of the Cartesian concept of physical space in terms of allowing us to take cognizance of the dynamics of the change and the consequences of the change we are experiencing (spatial compression), and to understand the basis of the tensions in the financial services industry. Henri Lefebvre's concept of 'social space' was examined as a possible answer (as a conceptual tool) to the problem. Lefebvre combines the space occupied by the sensory phenomenon, with the mental space, and most importantly, the space of social practice, to develop a single holistic concept of space, the concept of 'social space'. The significance of Lefebvre's concept of social space as concept relates to its utility as a tool not only for analyzing and understanding the change we are experiencing (the phenomenon of globalization), but also for understanding and appreciating the consequences of the globalization, and was therefore examined in detail. The concept not only allows us to take a holistic view of the space 'at a point of time', but also allows us to understand the process of change of (social) 'space across time'. These two facets of the concept of social space were therefore examined in detail. The process of change in space across time has been explained by Lefebvre as 'production of space'. The concept of production of space implies that space is not static, it is in the process of evolution and change. It

also points to the dynamism and creative capacity embedded within the concept of social space. The concept of 'production of space' is, therefore, the key to understanding of the process of change in space of the financial services industry, and the consequences emanating from the change for the regulators. Lefebvre's thesis of production of space is important because it draws attention to, one, the flexibility and dynamism inherent in the space of the financial institutions (regulated entities); and two, the fact that any regulatory framework that is not flexible and does not commensurate with the scale and scope of the activities or the structure of the business organization of the regulated (financial institutions), and does not undertake a holistic evaluation of their risks will not be able to achieve its objectives. The second facet of Lefebvre's concept of social space relates to the concept of space at a point of time where the emphasis is on the 'organization of space'. Lefebvre's concept of space is very different from our pre-existing concept of space as a physical thing. He incorporates the users of the space and the rationale for the actual use of the space into the concept of social space, thus, allowing us to visualize space and the organization of space in a completely new light. Social space is visualized as encompassing a number of networks with material underpinnings whose primary purpose is to facilitate communication/relationship between the subjects. These networks not only include geographical features like roads, railways, air routes, sea routes, etc. that serve communication based on physical movements of subjects (human beings) and their material goods, but also electronic channels of communication like telephones, intranets, internet, electronic exchanges, television, radio, etc., that serve communication based on information transfer between the subjects. Lefebvre's concept of social space, organized as a network of social relationships induces us to visualize space as a 'phenomenon' that can be examined and studied with the view of discovering and exposing the actual organization of space. The significance of this concept relates to its utility as a tool for examining and understanding the organization of space was demonstrated by visualizing the space of capitalism, the space of the marketplace, the space of a market participant (for example a financial institution), and the space of the political forces (this includes governmental agencies like financial services regulatory agencies) that try to control the operations of the markets and the market participants. The concept was also applied to examine the disjunction and the implications of the disjunctions in the organization of space of the regulators and the regulated. Unlike the financial institutions whose space is organized as a hierarchy of geographical and functional networks spanning a number of markets, the organization of the space of the regulators is encumbered by the limitations of physical space (whose principle of organization is segregation and fragmentation). When we combine this disjunction with the earlier discussed disjunction related to the production of space (unlike the regulators whose space is static, the financial institutions are actively involved in managing their space to take advantage of the market

opportunities), the logic for the tensions in the financial services industry become apparent. These disjunctions are direction flags that needs to be targeted by the regulators as a source of tensions in the financial services industry.

The aim of the thesis as I had stated at the end of the introduction is metaphorical: The aim is not to solidify metaphors to achieve the semblance of truth, but to provide a different approach for visualizing the problems in the financial services industry, to serve as a direction flag for understanding the problems of the present era. It is aimed at intellectual broadening. The modernist philosophical thought not only forms the basis of the regulatory philosophy in the financial services industry, but also forms the foundations of most of the economic theories (e.g. monetary policy) and the institutions (for example International Monetary Fund, The World Bank, United Nations, etc.). These theories and institutions which were founded on the basis of modernist philosophical thought are facing the pressure of time and space compression, and the rapidly changing ontological conditions. The thesis may also be viewed as a preamble that can serve as a stepping stone for a deconstructive investigation into the problems facing these theories and institutions.

I end my thesis with the following citation from Gareth Morgan, and leave the rest to the imagination of the (active) reader:

"If there is one thing that I have learned about academic work it is that every piece is implicitly or explicitly biased and incomplete. Metaphor symbolizes this, because whenever we engage the world through metaphorical modes of experience we are always engaging the world in partial, biased ways."

Morgan (1996, pp.235-6)

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¹This bibliography covers only the literature cited in Part III and Part IV of the thesis. It does not cover the literature cited in Part II which consists of two publications both of which have their own independent list of references.

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