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Chapter 1

Introduction The financial crisis and the politics of reform: explaining incremental change

Manuela Moschella and Eleni Tsingou

1. The global financial crisis and global financial regulation: big expectations but small change

> 'One of the things most astonishing to posterity about our own times will be not how much we understood but how much we took for granted. We revel in every new excuse to label our times revolutionary; ours is the atomic/permissive/electronic/affluent/space age. Attention centers on the glittering pageant and dramatic incident, rather than on the elusive processes that evoke the incidents. Revolutions must be visible, palpable, and immediate, although it is the annual change of only one percent that can produce some of the greatest transformations. Paradoxically, a glib preoccupation with the 'revolutionary' has tended to reduce our sensitivity to change itself' (Heclo 1974: 1).

Since the onset of the global financial crisis, 'change' has been the catchword in the international regulatory debate. In an attempt to respond to the weaknesses in financial regulation and supervision exposed by the crisis,[1] important legislative changes have been adopted in the world's leading financial centers, notably the Dodd-Frank Act in the United States and European Union legislation mandating the creation of new pan-European regulatory and supervisory authorities. At the international level, the leaders of the Group of 20 (G20) endorsed major reform proposals, partly in conjunction with the revamped Financial Stability Board (FSB) in areas such as banking regulation, compensation practices, resolution regimes, the development of macroprudential frameworks and tools, and the workings of derivatives markets and their infrastructure.[2] Interestingly, the regulatory reform process has often been presented in terms of a revolutionary transformation. At the height of the crisis, several political leaders suggested

[1] The literature on the causes of the global financial crisis is already quite large and it is not the purpose of this volume to review it thoroughly. For an introduction to the causes of the crisis from an economics perspective see, among others, de Larosière 2009; IMF 2009; Carmassi, Gros and Micossi 2009; Gorton 2008; Obstfeld and Rogoff 2009; Truman 2009.

[2] At the time of writing, the latest report assessing the implementation of G20 recommendations for the strengthening of financial stability was issued in June 2012. Financial Stability Board, *FSB Report on the Overview of Progress in the Implementation of the G20 Recommendations for Strengthening Financial Stability,* available at http://www.financialstabilityboard.org/publications/r_120619a.pdf

comparisons between the current reformist moment and the Bretton Woods moment (Parker and Barber 2008; Porter, Winnett and Harnden 2009), when the creation of new rules and institutions 'revolutionized' international monetary cooperation. Much early emphasis from policy-makers and indeed scholars[3] focused on the potential for significant transformation in global financial regulation. Referring to Peter Hall's (1993) seminal study on the paradigmatic shift in UK economic policymaking, Mark Blyth (forthcoming) laments the absence of third-order change. Nevertheless, as the quotation from Heclo at the start of this section reminds us,[4] the disproportionate attention towards revolutionary change risks reducing our understanding of change itself.

This is important as the process of international financial regulatory reform as it has evolved, displays few of the revolutionary characteristics that had been touted. For instance, although progress has been made on microprudential banking regulation with the introduction of higher and counter-cyclical buffers into the Basel III accord of the Basel Committee on Banking Supervision (Basel Committee), Basel III has not altered the practice of allowing banks to measure their own risk when setting capital requirements (Haldane 2012) and there is still no agreement on what should exactly count as liquid assets to satisfy the proposed liquidity standards. Furthermore, a stinging issue throughout the crisis, that of 'too-big-to-fail' financial institutions, remains under-explored and instruments aimed at increasing the loss absorbency capacity of systematically important financial institutions (SIFIs) have yet to be incorporated into formal and binding rules. As for the development of macroprudential regulation, which aims to preserve the health and stability of the financial system as a whole, agreement on what policy tools fall into its scope is still in its infancy (Baker in this volume). In addition, the creation of an effective cross-border resolution scheme is still on the nominal 'to do' list, as is the regulation of the over-the-counter (OTC) derivatives market and the shadow banking system (Carstensen and Rixen in this volume). Finally, and despite the criticisms it has attracted, the International Accounting Standards Board (IASB) has displayed remarkable stability in the content of rules, governance structure, and decision-making (Botzem in this volume). In short, the process of international financial reform has fallen short of initial (and proclaimed) expectations of rapid and revolutionary transformation and has instead been characterised by small and incremental changes.

The incremental pattern of change in global financial regulation may also be considered puzzling in theoretical terms – primarily because the conditions for the kind of punctuations that are associated with very large and often very consequential policy shifts appeared to be in place.[5] Indeed, it is often recognised that an exogenous shock, such as the one offered by the global financial crisis, is likely to trigger a reaction that overcomes the institutional frictions that usually constrain policy change. Periods of 'normal' marginal

[3] See, for example, Posner 2009; Singer 2009.
[4] The quotation is linked to Heclo's study on the evolution of social policy in Britain and Sweden (1974).
[5] According to Baumgartner and Jones (1993) incremental policy making, while common and dominant most of the time, is only one of two models of policy making: periods of incremental adjustments are routinely punctuated by short-lived bouts of radical policy change.

adaptation are interrupted by more infrequent and atypical periods of 'non-linear' policy changes (Howlett and Migone 2011, 54). Such changes are more likely to occur when the exogenous shock interacts with heightened public and government attention and with the alteration of the policy subsystem that is involved in the decision-making (Baumgartner and Jones 1993, True et al.). These are precisely the conditions that characterised the post-crisis environment. Indeed, the crisis catalysed public and policy-makers' attention around financial regulatory issues (see also Helleiner, Pagliari and Zimmermann 2009). At the same time, the debate on the content of financial rules became increasingly politicised, as attested by the primary role accorded to the G20 political leaders in international financial negotiations – although experts retained a primary role in diagnosing the crisis and suggesting reform proposals. As such, the conditions for a punctuated-type of change were in principle in place; instead, incremental changes prevailed.

Why was the reform process incremental although the conditions for more rapid and abrupt transformations appeared to exist? And is there anything specific about financial policy that prevents punctuations from occurring, making this policy field different from those where the existence of punctuations is now well-established? [6]

This book answers these questions, investigating the empirical pattern of incremental change in the post-crisis financial regulatory debate. Based on examination of a variety of policy fields within the area of finance broadly defined, the findings of this collaborative project suggest that the specific institutional frictions that characterise global financial governance and the activity of change agents and veto players involved in the process of global regulatory change make financial regulation largely immune to the punctuation-like model of change. Whereas in the standard punctuated model, institutional frictions beget punctuations – they can slow down change but they lead to bigger policy changes than in cases where external inputs would have been introduced more gradually, the combination of institutional frictions with the distinct type of actors involved in the international regulatory process prevents policy punctuations from occurring.

Although we collectively demonstrate that the process of change in international financial rule-making and content, and of the institutions of finance, does not fit with the punctuated model of policy change, we nonetheless argue that the incremental changes here examined do not rule out bigger and deeper transformations. This means that, in finance, paradigmatic change is less likely the result of an exogenous shock than is the case in the area of budgeting (Baumgartner, Foucault, and Francois 2006; Breunig and

[6] The best studied example of the combination of incrementalism and occasional punctuations is governmental budgeting (Jones et al 2009). Indeed, the frequency distributions of public budget changes, both in one-country and cross-countries studies, rule out the standard incremental model lending support to leptokurtic distributions (Baumgartner, Foucault, and Francois 2006; Breunig and Koski 2006; John and Margetts 2003; Jones and Baumgartner 2005; Mortensen 2005; True et al. 2007).

Koski 2006; John and Margetts 2003; Jones and Baumgartner 2005; Mortensen 2005; True et al. 2007) or macroeconomics (Hall 1993). In finance, as will be discussed in the Conclusions of this book, paradigmatic change is instead associated with incremental, endogenously-driven dynamics. In this light, our findings support the body of scholarship that suggests that radical transformations are not solely the result of the orthodox homeostatic or exogenously-driven punctured equilibrium model of policy change (Cashore and Howlett 2007; Coleman et al. 1996; Howlett 2009; Thelen 2003; Mahoney and Thelen 2010). Radical transformation may also result from the cumulative effects of previous policy changes, thus underscoring the importance of 'process sequencing' (Haydu 1998; Howlett 2009; Kay 2007; Thelen 2003).

The editors and contributors of this volume have set themselves an ambitious goal, that of speaking to scholars interested in the dynamics of policy change at large. We find that the importance of investigating factors at all levels of governance (domestic, interstate and transnational) is of increasing relevance to understanding policy change, especially as the type of fragmented governance encountered in finance against a multitude of actors and vested interests, can arguably be observed in other policy processes. That said, the book is primarily aimed to enrich International Political Economy (IPE) scholarship. Indeed, one of the motivations of our research project was the dissatisfaction with the treatment of the process of change in the existing IPE literature on global financial regulation. Specifically, existing studies offer only partial insights into the question of incremental change and seldom address it directly. Scholars of international financial regulation have focused mostly on the causes of regulatory change rather than what pattern change actually follows. As a result, while important insights have been developed on the actors involved in the politics of reform of international financial rules and on the instruments and resources used in the reform process,[7] we have yet to get a comprehensive picture of why and how change is sometimes quick and other times slow to materialise, or why, how and when it entails a profound rethink of previous practices or amounts to little more than small adjustments in existing instruments.

This is not to say that existing scholarship is silent on the dynamics of policy change. To the contrary, several scholars have made a number of suggestions that are key to the puzzle explored in our study. For instance, in his work on global finance as a technical system, Porter (2003) has suggested that the regulation of global finance is predisposed towards incremental developmental trajectories because of the legacy of previous technical knowledge and patterns of collaboration. Focusing on governmental policy networks, Baker (2006) has suggested some of the factors that help account for the incremental pattern he detects in the G7 case, suggesting that incrementalism can be understood in light of the prevailing economic ideas and shared understandings, and the routines and procedures that mark G7 activity. In a

[7] For instance, as will be discussed at greater length below, important insights have been developed regarding the influence exerted on the process of international financial reform by actors such as governments (Drezner 2007), national regulatory authorities (Singer 2007), international organisations (Abdelal 2007), transgovernmental networks (Baker 2006) and transnational networks of public and/or private sector officials (Porter 2005; Tsingou 2008).

similar vein, Best (2004) has drawn attention to the incremental nature of the shift from Keynesianism to monetarism by bringing to the surface the legacy of once-dominant ideas even when new ideas gain currency in academic and public circles. As this brief overview of the arguments on incrementalism reveals, current scholarship acknowledges the need to explain different dynamics of change. But we suggest that some of the explanations advanced to account for the incremental dynamics of change have not been fully explored, nor systematically tested.

Building on these insights, the contributions to this volume share an interest in explaining the incremental pattern of change that has dominated the post-crisis reform agenda. Specifically, we argue that, in order to explain this pattern, we need to complement and expand the conventional focus on the actors involved in the process of regulatory change with a stronger emphasis on the institutional frictions that actors confront.[8] These factors, which are illustrated in the following sections, include: the concentration of financial power in a limited number of states, vested interests in dominant institutional positions, gaps in implementation capacity at the domestic level, as well as the fragmentation and club-like nature of global financial governance.

This book sets out to make three main contributions to the literature on policy change and global financial governance. First, our study helps determine that an incremental policy change model best fits with the policy area of international financial regulation. This has implications for the study of change in financial policy and related policy areas (e.g. signalling changes in public policy priorities relating to access to credit, financialisation or trade-offs between stability and competitiveness) but also opens up potential comparative research agendas across issue-areas.

Second, we explore the normative dimension associated with the incremental pattern of change. We thus engage with the question of whether incremental changes are simply a cover for status quo and conservative forces to prevail, a proposition supported by some of the contributions to this volume (in particular Botzem and Rixen). Indeed, since the publication of Lindblom's article on the politics of 'muddling through' (1959), which addressed the tenets of incrementalism as a mode of policy-making, incrementalism has been accused of being an inherently conservative picture of the policy process. In this book, however, we provide a more nuanced understanding of incrementalism suggesting that it cannot be always and automatically equated with conservatism. Rather, as some contributions in this volume show (most notably Baker), in the area of international financial regulation, incrementalism can be a useful political strategy to offset conservative forces and may foreshadow more fundamental policy changes.[9]

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[8] As explained in greater detail below, the emphasis on constraining factors and sequencing leads us to engage with the analytic concepts developed within historical institutionalism (HI).

[9] Lindblom himself rejected the accusation of conservatism. For a summary of the arguments used by Lindblom see, for instance, Rothmayr Allison and Saint-Martin 2011: 3.

Finally, this volume puts forward an important contribution to the study of global financial governance in the aftermath of the global financial crisis by providing a theoretically-informed examination of the phenomenon of regulatory change that is meant to achieve bridge-building between the study of change in international political economy and comparative political economy (Farrell and Newmann 2011; Fioretos 2011b). Indeed, our explanation of incremental change borrows extensively from the insights developed within the historical institutionalist (HI) tradition on the study of change in domestic settings (as developed, among others, by Pierson 2004; Thelen 1999, 2004; Steinmo, Thelen and Longstreth 1992; Streeck and Thelen 2005). In particular, we build on recent theoretical and empirical studies that have expanded HI's core institutionalist focus with a more clearly agent-centreed perspective that keeps in due consideration the dynamic relationship between actors and the constraints/opportunities of the environment in which they operate (Bell 2011a; Mahoney and Thelen 2010).

As explained in some detail in subsequent sections, historical institutionalism holds valuable substantive insights and analytical tools for theorizing how incremental change occurs in international finance and why the international financial system may be more suited to incremental than radical reforms. Although we stress the relevance of HI to our empirical puzzle, it is not the purpose of this book to provide a manifesto for the application of HI to the study of change in global financial governance. Our adoption of HI is more practical than theoretical. We believe that HI provides substantive insights and analytical tools to investigate patterns of institutional, incremental development at the domestic level that can be useful in analysing patterns of institutional development in the international financial system too. Hence, although contributors do not necessarily subscribe to the historical institutionalist label, they share a substantive focus on factors such as power, temporal processes, institutional constraints, and inefficiency – in short, the factors that constitute the core of the HI tradition.

Before proceeding, some clarifications are in order. Firstly, although our interest in incrementalism is accompanied by an emphasis on the constraints that influence the process of change, the role of agency in the reform process is in no way discounted and is a common feature in all chapters. As has long been noted, 'background factors don't do policies. Policymakers do' (Lundquist, 1980: xiii). Studying actors' preferences, motivations, strategies, and ideas is therefore of utmost importance to the puzzle addressed in this study. As such, the chapters in this book explore the constraints associated with two categories of actors: *change agents* and *veto players*. Combining the role of actors, which has been largely investigated in existing literature, with the constraints that actors face, we attempt to strike a balance between strategic action and institutional constraints.

Secondly, it is important to clarify what type of changes in international finance we analyse. Indeed, one of the most common problems in the study of change is that 'scholars are often insufficiently clear as to exactly what it is that they are studying' (Capano and Howlett 2009: 3-4). [10] That is, significant ambiguity exists on the type and level of change under investigation. In order to sort out this ambiguity, in this study, we reject the distinction according to which incremental change indicates adaptive and reproductive minor change whereas major change indicates disruption of continuity. Rather, we submit, incremental change can be as transformative as major changes (see also Streek and Thelen 2004). We thus define incrementalism in relation to Peter Hall's (1993; 279) definition of 'normal policymaking,' as a process that adjusts policy without challenging the overall terms of a given policy paradigm – at least in the short run. That is to say, incremental changes preserve some broad continuities with past regulatory policies.

For the purposes of this study, then, incremental changes can be found at different levels – from formal institutions to soft governance arrangements and norms (Abbott and Snidal 2000). In particular, some of the contributors to this study analyse formal institutions and rules (Quaglia in this volume) as well as looser forms of cooperation such as standards and international early warning systems (Carstensen in this volume). Other contributors focus on either the changes in decision-making practices in financial regulation (Botzem in this volume) or the changes in the prevailing norms that inform international financial regulation and supervision (Baker this volume). Further, a group of contributions analyses the changes in the distribution of resources (material and immaterial) among different actors and stakeholders participating in international financial policy-making (Pagliari and Young in this volume). Finally, some contributions analyse areas of finance where contentious political factors are most pronounced whether defined in interstate competitiveness terms or at the domestic level (Rixen and Kjar in this volume).

The remaining part of this Introductory chapter is organised as follows. In the next section, we analyse existing literature on the evolution of global financial regulation and how it addresses and/or explains the incremental pattern of change in the post-crisis regulatory reform process. In Section 3, we develop the analytical tools and concepts that are taken up in the volume's case studies. In particular, we delineate the set of factors shaping the pattern of incremental change in global financial governance. Section 4 explains the relevance of studying the evolution of global financial governance by using the analytical concepts and methods developed within historical institutionalism. Section 5 provides an overview of the book.

[10] In the public policy literature, the ambiguity that surrounds the study of change is known as the problem of the dependent variable (Capano 2009; Green-Pedersen 2004; Howlett and Cashore 2009).

2. What do we know thus far? The actors of global financial regulation

The question of who shapes international financial rules and how the process of rule-creation takes place has long interested IPE scholars. Since the pioneering works of Kapstein (1989, 1992) on the negotiations of the Basel accord, scholarship on international finance has produced important forays into the political and market pressures that shape international financial rules and harmonization (Simmons and Elkins 2004; Simmons 2001; Cerny 1994). In particular, scholars have assessed the role played by factors such as the structural power of the United States (Strange 1988), capital mobility (Andrews 1994), domestic societal interests (Singer 2007; Seabrooke 2006) and private sector lobbying (Underhill 1997; Gill 1990) among others. In a review of the literature post-financial crisis, Helleiner and Pagliari (2011) suggest three distinct explanations for the evolution of international financial regulation based on the policy arenas that drive the process of rule-creation and change: interstate, domestic, and transnational explanations. Interestingly, and in spite of the significant differences among them, the three explanations share an emphasis on the actors involved in the regulatory processes and the resources that they possess to influence it.

For instance, the studies that fall within the first explanation place emphasis on a specific category of actors: leading states or great powers. In this reading, market size and adjustment costs are the crucial resources these actors possess. As Drezner (2007: 28) explains, the logic that unpins interstate explanations is 'market size [which] alters the distribution of payoffs by reducing the rewards of regulatory coordination for large market states and increasing the rewards for small market states. This gives the great powers a bargaining advantage and alters the perception of other actors so as to reinforce the likelihood of regulatory coordination at a great power's status quo ante.' Furthermore, market size endows great powers with the option of economic coercion as a way of convincing other actors in the system to change their financial rules in line with those preferred by the great powers. As a result, changes in international financial rules and institutions are closely dependent on the national interests of leading states.

Interstate explanations have several weaknesses, including a limited ability to account for states' interests over time and a neglect of domestic societal interests (Büthe and Mattli 2011). For our purposes, it is worth noting that, although interstate explanations do not explicitly address the question of incremental change, they offers some insights in the post-crisis context. For instance, a common theme in the scholarship is that financial regulation will be significantly enhanced when leading states have a common interest in more stringent regulation. Otherwise, leading states act to narrow the scope of regulation (Wood 2005). But the logic that underpins interstate explanations does not help distinguish between the conditions under which the regulation of finance will be modified incrementally, suddenly or be maintained as is. Additionally, such explanations underplay the role of weaker actors in influencing international regulatory outcomes (Sharman 2006). Yet it has become important to take the role of such actors into account, especially in the aftermath of the global financial crisis. Following years of preaching to emerging market countries about

internationally recognized standards of financial conduct (Walter 2008), the crisis erupted in the so-called 'sophisticated' financial markets. The reform process has thus far enlarged membership of the financial governance infrastructure to include more emerging market countries and it is yet possible that some of these countries, such as China, will become more assertive in influencing the international regulatory debate.[11] Furthermore, one of the effects of the crisis has been that of rebalancing power in favour of emerging markets' financial institutions, many of which, by market capitalization, now figure among the top 20 world banks – with Chinese banks occupying the three top spots of the ranking in 2009.[12]

The second set of explanations of international financial regulation shift the emphasis to domestic-level actors – be they domestic regulators (Singer 2007) or financial institutions (Busch 2009; Mügge 2006). Domestic actors are deemed able to shape international regulatory outcomes because of the key political resources they possess. Within the domestic explanation of international regulatory outcomes, significant attention is also placed on the institutional specificities of national capitalisms (Hall and Soskice 2011). For instance, Hubert Zimmermann (2009) has explained the international regulatory preferences of Germany and the UK in 2008-09 as they relate to the specific characteristics of their national capitalisms – coordinated and liberal market respectively. Similarly Manuela Moschella (2011b) has explored how the EU international regulatory preferences in the immediate aftermath of the global financial crisis were significantly shaped by the apparent discrediting of the UK 'liberal' model of capitalism in favour of the Franco-German 'regulated' model (see also Quaglia forthcoming and, on pre-crisis coalitions, Quaglia 2010).

Although domestic explanations do not explicitly engage with the question of what causes incremental financial regulatory change, they also contain some important insights. For instance, in his study of domestic regulators, Singer has identified a trade-off between stability and competitiveness in determining more or less international regulatory cooperation across three areas of finance – banking, securities, and the insurance sector, suggesting a pattern of international regulatory change that is highly dependent on the preferences of the regulators in the leading financial centres. This approach shares many of the drawbacks of interstate explanations, while also failing to account for the bargaining and deliberative dynamics that take place at the international level. The same problem affects those explanations that put the emphasis on the characteristics of domestic capitalisms; they are strong in highlighting domestic preferences but do not provide a satisfactory explanation for the process of decision-making at the international level.

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[11] Note, however, that such expectations are relatively contained – see, for example, Walter (2009) on this issue. On the increasing dependence of developed countries from emerging markets' finance see also Helleiner and Pagliari 2011: 176.

[12] Financial Times, *Top 20 financial institutions by market capitalization, $bn, 1999-2009*. Available at http://www.ft.com/intl/cms/7a7a1484-17a3-11de-8c9d-0000779fd2ac.swf Accessed 13 July 2011.

This shortcoming is largely addressed by the third set of explanations identified by Helleiner and Pagliari (2011), transnational explanations that explicitly focus on the processes and dynamics that takes place in international regulatory fora. This strand of scholarship explains that the evolution of the international financial regulatory regime is heavily influenced by the activities of actors that operate across rather than through governments, whether transgovernmental networks that overcome the domestic/international divide (Baker 2006; Porter 2005) or transnational policy communities in which the divide is not solely domestic/international but also public/private (Tsingou 2009) and where specialist expert knowledge prevails (Botzem 2012).

We believe that scholars adopting transnational explanations most clearly address the issue of incremental change. Baker's (2006) and Porter's (2003) insights on incremental evolution in global financial governance as a consequence of technical authority and *esprit de corps* have already been referred to. Likewise, in her account of the influence of private actors after the crisis, Tsingou (2009) attributed the incremental pattern of regulatory reform, in spite of the worst financial upheaval since the 1930s depression, to the enduring power of transnational private interests as these are firmly engrained among the members of the policy community in charge of the rules of global finance and have the capacity to constrain the spectrum of policy ideas discussed and adopted. There are, nevertheless, two problems with this set of approaches when our focus shifts away from actors and towards understanding the nature of change. The first is that the suggestions on incremental change are spot insights rather than clearly developed hypotheses that inform a research agenda on the incremental pattern of change. The second is that transnational explanations have primarily focused on the actors involved in the international regulatory process but have paid insufficient attention to the institutional frictions and actor interaction that constrain the activities of the actors analysed.

In what follows, we aim to fill this gap by developing a theoretical framework able to account systematically for the incremental dynamics of change. We take into account the role of agency in the process of change by investigating change agents and veto players, but we also endeavour to put greater emphasis on the institutional frictions that, combined with the activity of transgovernmental networks and transnational communities, help explain incrementalism in the international financial regulatory process.

3. Explaining incremental change in the post-crisis financial regulatory reforms: redressing the balance between actors and institutions

The theoretical framework suggested here takes as a starting point an agent-centred constructivist-oriented approach. Since ideas exist in a competitive marketplace where alternative ideas are always available, actors frame and manipulate ideas to mobilize support (Blyth 2003). In other words, the process

of change requires actors sponsoring their ideas and aiming at persuading other agents (Widmaier, Blyth, and Seabrooke 2007; see also Chwieroth 2010). The importance of active policy entrepreneurs and the ideas they support is widely recognized in the literature on the creation of global regulation. As Mattli and Woods (2009: 17) put it, 'public and private entrepreneurs play key roles in mobilising opposition, and ideas may offer the necessary frames for pro-change interests and glue for coalitions'. The role of policy entrepreneurs acquires key importance in the policy area under investigation where the uncertainty associated with financial crises strengthens the importance of actors able to interpret them, diagnose their causes, and propose blueprints for their solutions (Blyth 2002, 2007; Baker forthcoming). In short, economic crises do not speak for themselves (Hay 1996) and their effects do not automatically lead to new policy and ideational consensus (Grabel 2003; Moschella 2010).

As previously discussed, for the purposes of this study, we identify two distinct categories of actors that help explain processes of change in global financial regulation: change agents and veto players. The identity of these actors, we submit, can be most diverse: in different times and different circumstances, governments, societal interests, or transnational technocrats can play the roles of change agents and veto players. Assigning roles is therefore a matter of empirical investigation and is not defined *ex ante* in our theoretical framework.

Whereas change agents lead the process of change by being explicit advocates of specific changes or hidden supporters, veto players, in principle, aim at maintaining the status quo in order to preserve their privileges and safeguard their interests. In the area of financial reform, several studies have shown how special interests are able to shape rules and institutions in narrow and effectively closed policy communities (Moran 1990; Underhill 1995; Coleman 1996). These actors may sustain the reproduction of existing institutions over time, vetoing or opposing change that affects them. Although veto players generally oppose change, it is also plausible to think of them as actors expressly promoting change. This happens when veto players realise that regulatory change is the only way to maintain their privileged position. For instance, in the context of financial policy, if actors do not adapt to shifting financial innovations and changing economic conditions, the risk of losing their privileged position is the highest. Hence, it is possible that 'the very industries that benefited from regulation in the past lobby for change' (Vogel 1996: 13). It is also important to note that, similarly to change agents, veto players can be more or less explicit in their strategies.

While we take as a starting point of our analysis the role of agents as in much of the IPE constructivist scholarship reviewed in the previous section, we complement the analysis on the role of the agents with a careful examination of the institutional constraints and opportunities that the actors face in their activity,

including actor interactions.[13] In doing so, we build from important, recent attempts that have drawn attention to agent-centred model of institutional change (Bell 2011a, forthcoming). That is to say, we acknowledge that agents are the ultimate propellant of change but also that institutional environments shape agents' ability and discretion. Hence, to explain change, 'we need to model agents both as partially constrained by their immediate institutional contexts and also as operating in institutional and structural settings that constantly evolve and potentially open up new opportunities for agents.' (Bell 2011a: 898).

In what follows, we therefore concentrate on the dynamic interaction between agents and institutions that help explain incrementalism in global financial regulatory reform processes. Since the existing literature, as discussed in the previous section, is extensive on the actors involved in international regulatory processes, the factors identified below focus on the institutional dimension of the process of change. Nevertheless, as the empirical chapters show, it is the combination between the specific agents involved in global finance and the distinct institutional frictions of global financial regulation that explain the prevalence of incrementalism over punctuations.[14]

The institutional frictions that are relevant to the process of global financial regulatory change are grouped into three blocs according to the strand of the global finance literature they mainly refer to (Table 1).[15] Note, however, that whereas some factors are specific to one of the three political arenas of global financial regulation – interstate, domestic and transnational –, other factors do not relate to a single arena only. For instance, although we discuss the institutional frictions associated with the presence of vested interests in the section dedicated to the domestic political arena, vested interests can be found at both the intergovernmental and transnational levels. Likewise, the discussion of ideas and routines as institutional frictions is conducted in the section on the transnational arena although these frictions are present in the intergovernmental and domestic arenas too. In short, the typology proposed below is an analytical tool that assists us in discussing a number of frictions that help account for incremental change in global financial regulation but should not be considered as a way to exclusively assign a specific friction to each of the three political arenas. Furthermore, the list is neither exhaustive nor exclusive. It is also worth noting that the factors identified below may pertain to one of the stages of the regulatory decision-making process

[13] Mahoney and Thelen (2010: 31) advance a similar point when they argue that 'the interactions between features of the political context and properties of the institutions themselves [are] critically important explaining institutional change' and how the type of change actors and the different strategies they adopt are likely to differ in specific institutional settings.

[14] There are studies that attempt to distinguish between the factors that influence the outcome of regulation – i.e. whether public interest or captured regulation prevails (see Mattli and Woods 2009 for instance). To our knowledge, however, no similar attempt has been made to systematically analyse and test the conditions that help explain the dynamics of regulation.

[15] Note, however, that we also move beyond the scholarship explicitly reviewed in the previous section.

(agenda-setting, negotiations, implementation and enforcement), whereas other factors are present in more than one of the stages. Finally, whereas some constraints are formal, others are more informal.

Table 1.1 Institutional frictions and potential paths to incremental change in global financial governance

	Institutional friction	**Potential Path to Incremental Change**
Interstate dimension	Concentration of financial power	*Change agents adopt limited reforms to escape veto*
Domestic dimension	Vested interests in dominant institutional position	*Veto players adapt to new challenges to maintain privileged position*
		Change actors change slowly to avoid overt opposition
	Gaps in implementation capacity	*Veto players lengthen policy implementation*
		Change actors build implementation capacity
Transnational dimension	Fragmented and club-like global financial governance	*Change agents seek support across several regulatory bodies*
		Veto players are insulated from public pressures
	Ideational inertia	*Change agents roadtest new ideas and build institutional support*

In what follows, we discuss each of the identified institutional frictions in turn. In examining their characteristics, we also suggest in what ways they are likely to be associated with incremental dynamics of change. That is to say, we provide some illustrations of how the presence of specific institutional friction may prevent the emergence of paradigmatic changes. It is important to note, however, that these suggestions are just illustrative and indicative. As the empirical case studies that follow indicate, and as we discuss in the conclusions, there are several pathways to incremental change and, above all, it is the interaction between change actors and veto players, on the one hand, and institutions, on the other, that shape the pattern of regulatory dynamics.

The interstate dimension and processes of incremental change

Although the role of experts and technocrats is crucial in the creation of global financial regulation, the role of governments should not be underestimated (see Rixen in this volume). On the one hand, many important decisions are taken through intergovernmental bargaining, where states attempt to attend to a specific national interest. On the other hand, the implementation of global financial regulation is closely dependent on domestic regulatory regimes, as will be explained at greater length below. Furthermore, since regulatory reform is about more than liberating markets, state actors are key factors in reforms

because they address two things that are more relevant to states than any other actors: 'finding new ways to raise government revenue and designing new mechanisms of policy implementation' (Vogel 1996: 19).

In the interstate arena, the main institutional friction that helps explain the prevalence of incrementalism in the process of global regulatory reform is the concentration of financial power – and associated veto power – in only a few states. For instance, those states with the largest markets occupy a privileged position in global negotiations because they may veto decisions that could damage their financial interests by using the threat of closing their markets or that of going-it-alone. As a result, change is often based on the lowest common denominator among state preferences to escape veto players and deadlock (also Quaglia in this volume). That is to say, for regulatory changes to be adopted, change agents should not support changes that significantly depart from the rules and practices in place in the dominant financial markets. In particular, the transformation of global financial rules would need not to impose significant costs for the most powerful states in the system. This limits the range of reformatory policy options, thus giving rise to incremental patterns of change.

The domestic dimension and processes of incremental change

Within the domestic policy-making arena, two main institutional obstacles to regulatory reform are the presence of vested interests and the lack of implementation capacity. The first is closely related to the concept of institutions adopted in this study: the institutions in global financial governance can be conceived as the legacies of political struggles. This means that certain actors are advantaged by existing institutions and have a vested interest in their survival. This is the case of the financial industry in our area of investigation – although the crisis has altered their influence too (Pagliari and Yound in this volume). Furthermore, once an institution is in place, actors make greater relation-specific investments, and this develops an interest in preserving current institutions (Pierson 2000a, 2000b, also Gourevitch 1999). For instance, as David Lake (1999: 46) has noted, since private actors 'have grown out of and adapted to the current [global] governance structure,' they 'have little interest in seeing it overturned or even significantly modified'. But domestic societal actors can also benefit from such arrangements; when the interests of powerful electoral blocks coincide with those of particular financial institutions, enacting reform and changing the status quo can lead to intense political struggles (Kjar in this volume).

Although the actors that benefit from existing institutions prefer the status quo, change is still possible. For instance, actors that benefit from existing institutions may adapt those institutions in order not to lose their comparative advantage. This is particularly the case in a rapidly-innovating sector like finance. Indeed, faced with changing economic conditions or with shifting financial innovations, veto players may realize that their advantage is better preserved by adapting existing rules and institutions rather than by maintaining the status quo. It is also conceivable that veto players would accept short-term sacrifices to

their interests in order to maintain long-term coalition success (Scharpf 2000: 782). It is within this space that changes may take place in an incremental fashion. Indeed, the logic is that the actors that have an interest in a specific institution will prefer an incremental adaptation in order to control the process of change. Following this thinking, we can interpret the limited but nevertheless substantive reforms at the European level as a process that addresses some criticisms while deflecting attempts at more radical transformation (see Quaglia in this volume).

Next to a process driven by the actors that benefit from existing institutions, the actors that are disadvantaged may also drive the process of change; as Thelen (1999) has noted, losers from an institutional arrangement do not disappear. They also adapt and work to transform this arrangement, including via the formation of coalitions with other actors (Pagliari and Young in this volume). This has important implications for the dynamics of policy change. Indeed, if change agents occupy a disadvantaged position in the regulatory status quo, they will enact change in slow and incremental steps in order to avoid overt opposition and political blockages by the actors that are privileged. The timing of change is also slowed down because agents need to mobilise and nurture political support against entrenched interests. This hypothesis fits with the well-established finding in domestic political systems that 'countries with many veto players will engage in only incremental policy changes' (Tsebelis 2000: 464).

The second institutional friction that shapes the pattern of global financial regulatory change relates to organisational and bureaucratic capacity. Indeed, reforms at the international level often depend for their implementation on domestic regulatory authorities and bureaucratic apparatuses. The capabilities and organisation of these regimes therefore provide incentives for and constraints on what governments can put into practice (Raustalia 1997). Furthermore, in the area of finance, the domestic level assumes a key role as many of the global rules of finance are flexible best practice standards rather than firm rules per se (Tsingou 2008); they are interpreted in regulatory terms and implemented within a domestic setting. The discretion accorded to domestic bureaucratic systems in implementing global financial regulation therefore magnifies the importance of the former and bears important implications for the patterns of policy change in at least two respects. First, veto players may oppose change at the implementation stage, lobbying domestic regulators for lengthening application of internationally-negotiated rules. Second, change agents need to develop the necessary institutional infrastructure before enacting their preferred policy changes (see Baker in this volume)

The transnational dimension and processes of incremental change

Finally, and with particular reference to the transnational dimension of global financial regulation, the institutional frictions that are more likely to shape the pattern of regulatory change in an incremental

fashion are the institutional framework and the ideational orientation of global financial governance.[16]The governance framework of global finance is of crucial importance to explain patterns of change. Two features are of particular relevance: the fragmented nature of the global regulatory regime and the club-like quality of cooperation. The governance of international finance is indeed distributed among multiple transnational public and private international institutions (Porter 2005) where no single regulatory body clearly dominates. These bodies include the international financial institutions, international groupings of regulators and supervisors such as the Basel Committee, IOSCO, and the International Association of Insurance Supervisors (IAIS).[17] The governance framework also includes private sector actors, some of them global representative groupings for banking and other financial industries, others more issue-driven and responsible for standard setting, such as the IASB. While some of these bodies have distinct competences, they also share responsibilities. This has a number of consequences for the dynamics of regulatory change. Firstly, the development of new policies requires consensus in more than one regulatory body. For instance, the task of developing regulatory standards for SIFIs is shared among the FSB and the Basel Committee (which will set additional capital requirements). Under this fragmented institutional framework, change is more likely to be incremental. As a result, change agents will need to mobilise support in several regulatory bodies while turf battles and overlapping competences offer veto players multiple opportunities for influence. A similar institutional patchwork can be observed in the ongoing discussions about resolution regimes (Carstensen in this volume).

Next to the fragmented nature of global financial governance, its club-like quality also affects patterns of regulatory change. Policy networks at the transnational level usually operate through informal and exclusive processes where expertise and socialization are critical resources for influencing regulatory outcomes. These features, we suggest, tilt the balance in favour of incrementalism at least for two reasons.

First, this peculiar structure shields the global regulatory debate and decision-making from public scrutiny and pressures (housing finance is a notable exception as shown by Kjar in this volume). The comparison with other policy fields may be of help to clarify this point. For instance, Hall's explanation of paradigmatic change in Britain's economic policymaking emphasizes the role played by actors outside the community of policy experts. In his view, paradigmatic change was ultimately possible because the contest over policy choice spilled beyond the boundaries of the Treasury.[18] Similar emphasis on the attention to an issue by actors that do not belong to the community of experts is also present in several studies that have analysed

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[16] Vogel (1996) adopts a similar distinction between regime organization and regime orientation, although he refers to domestic regulatory systems.

[17] The World Bank, for instance, assists member countries in the design and implementation of policies that strengthen the domestic financial system and helps countries in identifying risks in this system. The Basel Committee, IOSCO and IAIS, in turn, provide specialised knowledge by setting the standards in the field of banking supervision, securities and insurance supervision respectively.

[18] On this point, see also Blyth (forthcoming).

a variety of policy sectors - from nuclear policy (Baumgartner and Jones 1991) to civil rights, environment, energy, transportation and foreign trade policies to provide a few examples (see the contributions in Baumgartner et al. 2011). In contrast, in the policy field of global financial regulation, the kind of public attention, mobilisation and pressure that these studies identify is most difficult to achieve. As a result, change is 'managed' by a closed policy community that is likely to embark on small changes whose scope and consequences it can control (Botzem in this volume), and prefer long timeframes of implementation.

Second, the club-like nature of global finance is a likely source of incrementalism in that policy communities responsible for financial regulation tend to share common mindsets and normative orientations about the proper scope, goals, and instruments of financial regulation and are also affected by 'cognitive locks' regarding appropriate courses of action (Blyth 2002).[19] Since these ideas set the parameters of possible and appropriate behaviour, they also constitute a major obstacle to rapid and radical policy changes, especially given the rarity of the moments in which new ideas suddenly displace old ones, leading to abrupt changes in behaviour and policy. Most of the time, policy changes take place within the parameters set by existing ideational frameworks. The 'ideational inertia' is magnified in the presence of well-developed agencies and bureaucracies as is the case in financial regulation. Under these circumstances, 'any efforts to change have to first overcome the power of habitual perceptions, emotions, and practices' (Hopf 2010: 540).

Ideational factors therefore lead to incremental change because new ideas need to be developed and accepted within a policy community. Furthermore, to win the support of the 'experts', new ideas also need to be tested against empirical evidence and historical experience (Baker in this volume). This is especially the case in global finance where technical knowledge is a key component of its governance (Porter 2003). Indeed, the process of change in policy communities made up by experts relies heavily on the process of road-testing and experimenting with new ideas in the face of empirical anomalies before coming to abandon old ideas. Next to the steps necessary to test and develop new ideas, the process of change follows an incremental pattern also because policy entrepreneurs have to establish institutional support for ideas to translate into policy action (Widmaier, Blyth and Seabrooke 2007: 754). In global finance, this means that ideas have to gain an institutional presence in the regulatory bodies that drive the process of change. For instance, for the ascendance of the ideas on macroprudential regulation, a key factor has been their diffusion from the Bank for International Settlements to other professional ecologies (Baker forthcoming; Seabrooke and Tsingou 2009). In other words, the development and acceptance of new ideas take place through a drawn-out sequential process (Blyth 2002) where the stages of collapse and consolidation of ideas are required for an appropriate conceptualization of change (Legro 2000). Seen from this perspective, even the alleged Bretton Woods 'moment' was not the kind of rapid and radical change

[19] According to Vogel (1996: 20), these beliefs usually reflect 'actors' adherence to broad doctrine, such as economic liberalism; their predisposition toward certain functional tasks …; and their commitment to specific policy mechanisms'.

that is usually portrayed. Rather, it 'took place well over a decade after the momentous financial crises of the early 1930s. The delay was not just a product of the unique historical circumstances of the era. It took time for old ideas and practices to lose their legitimacy and for new ones to emerge as models for the future' (Helleiner 2010: 624).

In conclusion, in this section, we have identified a number of institutional frictions that, when combined with the activity of change agents and veto players, help explain the dynamics of change, in this case incrementalism. The institutional frictions identified are those typical of the area of international financial regulation and may help explain the prevalence of incrementalism over the alternative punctuated model.

By emphasizing institutional constraints and frictions, we take inspiration from most of the substantive and analytical features developed by historical institutionalism. While HI has been developed in the subfield of Comparative Politics to explain the evolution of domestic institutions, we submit that HI holds key value for the study of IPE in general and the study of the evolution of global finance in particular (see also Fioretos 2011a). In the following section, we explain how HI is relevant to our study and examine its potential contribution to research agendas relating to global finance, in line with similar efforts to apply HI to explanations of IO behavior (Moschella 2011a; Rixen, Viola and Zürn forthcoming), tax policies (Rixen 2011) and multilateral cooperation (Fioretos 2011b). We also identify the areas where we move beyond HI or redress it by mixing the insights developed in other theoretical traditions. In particular, we highlight the ways in which HI may usefully complement agent-centred approaches in the explanation of policy changes in global financial regulation.

4. Historical Institutionalism and Change in Global Financial Governance

What is the advantage of borrowing from historical institutionalism to explain the empirical puzzle of incremental change in global financial governance? There are at least three main reasons as to why HI is relevant to the puzzle addressed in this study: the focus of the research agenda, the approach to empirical problems, and the engagement with questions of efficiency and legitimacy that gets us to reflect on the normative dimension of global financial governance. All three factors helpfully complement agent-centred constructivist scholarship.

First, HI is relevant to our study because of its research agenda. Indeed, the core of HI's research agenda revolves around the question of institutional evolution over time (Pierson 2004; Pierson and Skocpol 2001; Thelen 2004; Sanders 2006). That is to say, 'the substantive profile of historical institutionalism is characterised by attention to large questions with an explicit temporal scope that concern the creation, reproduction, development, and structure of institutions over time' (Fioretos 2011b: 372). As such, the insights developed in HI can help explain the pattern of institutional evolution we observe in global finance.

The understanding of institutions in HI is also relevant to our study. In contrast to more rationalist understandings according to which institutions are exogenous coordination mechanisms that generate or sustain equilibria, HI conceives institutions as the legacies of political struggles that emerge from and are embedded in concrete temporal processes (Thelen 1999: 382).[20] That is, institutions emerge from particular historical conflicts and constellations (see also Steinmo 1993). In a more expanded version that borrows from sociological institutionalism, institutions are also viewed as a set of shared understandings that affect the way problems are perceived and solutions are sought (as in Katzenstein 1996).[21] From an HI perspective, then, institutions do more than channel policy and structure political conflict: they define preferences.

The conception of institutions that characterizes HI heavily informs our analysis. Indeed, the contributions to this volume focus on a variety of institutions – formal institutions and rules (Botzem; Quaglia; Rixen), regimes (Carstensen) and supervisory principles (Baker); and the policy practices and strategies of actors (Pagliari and Young; Kjar) – which are conceived as something more substantial than mere coordination mechanisms among the actors involved. From our perspective, the institutions that help govern global financial governance are the result of political struggles and temporal processes that crystallise interests as well as routines and habits. Furthermore, the institutions we study are not external to the actors that seek to change them (or oppose change). Rather, actors act within the institutions, their strategies and motives are shared by them, influencing the dynamics of change itself.

An additional practical contribution of HI to our study is its focus on the incremental pattern of change. HI has long been seen to have a bias towards explaining stability rather than change and for privileging structure over agency (see discussion in Crouch and Farell 2004; Katzneslon 2003) and indeed, HI's emphasis on path-dependency and mechanisms of reproduction (Pierson 2000a; Mahoney 2000) has led to powerful explanations of institutional stability and persistence.[22] At the risk of simplifying a much more nuanced debate, two mechanisms are usually identified in explaining institutional stability. The first mechanism is strictly connected to the distributional outcome of institutions. Since specific institutions benefit some groups more than others, those who are advantaged by the existing institution will struggle to preserve it. The second mechanism, which draws from the economic institutionalist literature (Arthur 1995; David 1985; North 1990), revolves around the notion of increasing returns (Pierson 2000a). Since in politics, the creation of new institutions requires overcoming the barriers to collective action and is generally characterised by high start-up costs, coordination effects, and adaptive expectations, the introduction of

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[20] For a discussion of each of the three strands in HI see Hall and Taylor (1996). Other useful reviews include Lichbach and Zuckerman (2002), Immergut (1998), and Kato (1996).

[21] In new institutionalism in sociology, institutions are conceived as 'shared cultural scripts', 'shared cognitions' and 'interpretive frames' of the way the world works (Meyer and Rowen 1991).

[22] In the fields of American Politics and Comparative Politics see, for example, Pierson (1994) Skocpol (1992), Collier and Collier (1991) and Hall and Soskice (2001); in International Relations, see Krasner (1988) and Spruyt (1994).

new institutions will be the most unlikely. In contrast, institutions that succeed in crossing these initial thresholds should be expected to have a good chance of persisting for very long periods of time (Pierson 2000b: 78).

By focusing on the mechanisms of reproduction, HI has long been criticized for not having been conducive to satisfactory explanations of institutional change.[23] However, HI is now a tradition that is able to explain change by having identified several mechanisms that undermine path-dependence processes (Pierson 2004; Thelen 1999, 2004) and by focusing more on the behaviour of political actors that help shape change (see Streeck and Thelen 2005; Mahoney and Thelen 2010). In particular, the causes of change have been found in the same mechanisms that ensure institutional reproduction so that path dependency contains both elements of continuity and structured change (Thelen 1999: 384). Institutional change is not conceived as a dichotomous variable but as a continuous interaction between continuity and change, which gives rise to an incremental pattern of change (Thelen 1999). Building on these insights, scholars working within the HI tradition have uncovered a variety of forms of incremental change that stand in opposition to exogenously-driven changes. These forms include, among others, layering, conversion, drift, and displacement (Streeck and Thelen 2005; Hacker 2004; Mahoney and Thelen 2010).[24] Although incremental, the processes of change identified by HI scholars are regarded as being able to bring about profound transformations (Thelen 2003; Mahoney and Thelen 2010).[25]

The second practical contribution of HI to our work regards its approach to theorizing change. In particular, we share with HI the methodological approach that begins with the analysis of empirical puzzles that emerge from observed events or comparisons (Thelen 1999: 373). Indeed, most HI studies begin with a question on an empirical puzzle – be it different levels of taxation (Steinmo 1993), or vocational training regimes and party systems across countries (Thelen 2004; Collier and Collier 1991). In a similar vein, we begin with empirical puzzles that emerge from observed events, in our case, the global financial crisis and the ensuing pattern of incremental change in the reform process. Our study, like most HI, places significant attention on historical contextualization and temporality, the notion that the timing and sequence of events shape political trajectories by conditioning the interests of and options available to actors in contemporary reform processes (Pierson 2000a, 2004). Temporality and sequence are also key in global financial regulatory processes.[26] Indeed, global financial governance arrangements are complex in terms of analytical purchase and implementation capacity. Thus, changing them requires the existence of a number

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[23] Bell (2011a) offers a comprehensive discussion of some of these criticisms but also shows why these matter for HI less than it sometimes appears by reminding us of the importance of agency in much HI scholarship.
[24] For a full discussion of these forms of incremental change see, for instance, Mahoney and Thelen 2010: Ch. 1.
[25] Other examples of small changes leading to change in policy goals include Coleman et al (1996) on agricultural policy change, Capano (2003) on the Italian administrative reform, Posner (2007) on financial integration in the EU, and Moschella (2011) on IMF surveillance.
[26] On global regulation as made up of several stages, see also Mattli and Wood 2009, and Abbott and Snidal 2009.

of preconditions. For instance, adopting a macroprudential approach to financial regulation and supervision requires well-developed analytical frameworks, expertise, and organisational infrastructure to analyse the financial system as a whole (Baker this volume; Moschella 2011a). Likewise, the design of capital controls is influenced by administrative capacities of different agencies, institutional and legal constraints, and other country-specific factors (Ostry et al. 2011). The existence of the required knowledge and administrative capacities cannot be assumed; rather, they are more likely to be built over time.

In addition to sequence and temporality, another crucial insight of HI, which fits well with our case, is the interaction and interdependencies among different institutional subsystems. Indeed, HI conceives of institutions not only in isolation but also as embedded in a wider institutional configuration whose pieces, which emerged at different points in time, 'do not necessarily fit together into a coherent, self-reinforcing, let alone functional, whole' (Thelen 1999: 382), but do clash with each other. For instance, Streeck (1997) has shown the ways in which industrial-relations institutions created problems and pressures for the stability of other institutions, especially vocational education and social welfare institutions.

This insight also applies to the area of global finance, where different sectors (banking, securities, insurance) are regulated differently at the global level. Variations affect (1) the actors involved, from the international financial institutions to international groupings of regulators and supervisors, (2) the degree of formal institutional cooperation, from formal treaties to voluntary standards, and (3) the degree of private sector authority as compared to the public sector (Cutler et al. 1999; Graz and Nölke 2008). The governance of global finance is therefore characterized by multiple, but closely-related regulatory regimes, similar to what Keohane and Victor (2011) call 'regime complexes'. As a result, as in the interdependencies among different institutional subsystems identified by HI scholars, change in one area of governance may have implications for another area. Furthermore, changes in the broader institutional configuration (for instance, in terms of new ideas about how to govern financial markets) may well have repercussions on the trajectory of change of single governance regimes.

Finally, HI contains important insights that can get us to critically reflect on questions of efficiency and legitimacy in global financial governance. Having expressly challenged the functionalist view of institutional development, according to which 'outcome X (an institution, policy, or organization, for instance) exists because it serves function Y' (Pierson 2000c: 476), one of the key insights of HI scholarship is that the process of adaptation of existing institutions is inefficient because actors work within constraints that are defined by the past. Stickiness, path dependency, and vested interests are the key factors here. A famous instance is that of the QWERTY keyboard, which David (1985) argued illustrated the ways in which a technology that gains an initial advantage over alternatives prevails over time despite the greater efficiency of alternative technologies. Thus, 'the outcome is that patterns of adaptation that would ensure greater collective efficiency often do not occur, that positions of privilege and divisions of labour regularly persist

though relative balances of power shift, and that institutions frequently outlive their original rationale' (Fioretos 2011b: 376).

These insights are particularly crucial for the process of change in global financial governance: as anticipated by HI, interest groups often see great benefits in reproducing existing arrangements rather than changing them; and global financial governance mechanisms may remain little altered despite a new balance of power that in principle can favour emerging markets. In short, HI alerts scholars interested in the politics of global financial regulation of the strength of the forces that oppose change and of the implications of such conservatism for the legitimacy of the global financial system.

In conclusion, HI holds valuable substantive insights and analytical tools to theorise change in global finance and explain why the financial system is more likely to evolve through incremental rather than radical reforms. This is not to suggest that the insights developed within the HI scholarship can be uncritically applied to the area of global financial regulation or that HI simply holds the key to the explanation of change in global financial regulation. More narrowly, what we want to suggest is that HI offers the missing element for explanations of change in IPE. Indeed, as previously discussed, the most important and recent studies of policy change in IPE have emphasised the role of actors and their interpretation of reality to account for institutional variance after moments of uncertainty, including wars and economic crises (Widmaier, Blyth and Seabrooke 2007). These studies certainly deserve credit, including for demonstrating the crucial importance of actors and their ideas in an academic field that has long been dominated by materialist explanations. Nevertheless, constructivist accounts of the process of change in the international economy have somehow neglected some of the key institutional factors that interact with agency to bring about change (also Bell 2011a). By focusing on this neglected dimension, which stands at the core of HI scholarship, we therefore aim at redressing the balance between agency and the institutions within which agents operate. This effort, we submit, helps us provide a thorough explanation of processes of change. Whereas the focus on actors' ideas may well answer the question of *why* change is initiated, the focus on institutional frictions allows us to focus on answering the question of *how* change takes place: whether punctuations or incrementalism prevails. In what follows, we provide a brief overview of how the book elaborates upon these issues and offer a short presentation of our empirical material.

5. Plan of the book

Incrementalism is a mode of policy change that is well-known and studied in the comparative politics and comparative public policy literature. In the IPE literature on the politics of financial regulation, however, incrementalism is known but under-researched. The book aims at filling this gap by testing and extending the application of insights primarily developed for explaining processes of change at the domestic level.

Although the study of IPE will certainly be enriched by the analytical toolkit developed in other academic subfields, it will, we submit, be a two-way process. That is to say, by identifying the specific conditions that make financial regulation incremental, our research project is also able to speak to the broad community of scholars interested in patterns of policy change, providing detailed cases that can open up opportunities for further cross-issue comparative research. The remainder of this chapter provides a preview of the contributions and outlines how the different cases shed light on why incremental change has prevailed in the reform process following the global financial crisis. The volume is organised in two parts: the first focuses more on the evolution and reform of the regulatory framework post-crisis while the second is explicit in its emphasis on the actors at the centre of these processes.

The first empirical case is provided by Andrew Baker, who focuses on the development of macroprudential ideas and how this significant ideational change has the potential to bring about more radical policy reform over time. Drawing on policy material and personal interviews pre- and post-crisis, Baker provides an analysis that highlights the dynamics of change across the transnational and domestic levels and explains how ideational coalitions can work to develop ideas into policy, building institutional support and know-how.

The attention then turns to the specifics of the reformed and reforming regulatory landscape. Lucia Quaglia surveys the state of play in financial services governance in the European Union and examines how regulation and legislation enacted following the crisis measure up to intentions and the pre-crisis status quo. In her analysis, Quaglia finds institutional innovation and policy impetus but also enduring resistance both by states and private financial actors. As such, across governance levels, she observes that a significant number of veto players have placed constraints on more comprehensive reform. At the same time, she reminds us that such incrementalism should not be seen as maintenance of the status quo per se, as European financial governance has a history of proceeding in small steps.

Moving on to the specifics of regulatory reform, Martin Carstensen offers an analysis of the nascent regime for bank resolution. By focusing on an area of regulatory concern that was expressly highlighted by the crisis, Carstensen follows the regulatory debate and traces the genealogy of reform ideas and the ideational struggles over how the principle of resolution regimes is to be translated into regulatory mechanics. Carstensen finds that although resolution as a principle is not fundamentally threatening pre-crisis global finance, resulting policy implementation can alter how financial crises are funded. As such, Carstensen offers a case where thinking through regulatory dynamics in a manner that seemingly represents little or only incremental change to the operation of finance can lead to significant changes for the governance of finance in the long-run.

The section closes with a contribution by Thomas Rixen who examines regulatory reform in relation to offshore financial centres and shadow banking. Rixen focuses on two interlinked cases which attracted a great deal of political attention in the aftermath of the crisis, though assessments as to their significance as factors in the crisis remained mixed. Overviewing reforms in these areas, and contrasting these reforms to original intentions, Rixen finds that change can be characterised as mostly symbolic. In explaining this outcome, Rixen points to enduring competitiveness interests of key states and in particular, their conception of jurisdictional competition. Aside from stressing the importance of the interstate dimension in explaining modest change, Rixen also provides a case where reform fails to keep pace with official pronouncements when those are actually detached from the issues perceived to be at the core of the reform process.

The volume proceeds with three chapters more explicitly focused on the actors at the centre of the reform. Firstly, Stefano Pagliari and Kevin Young examine how financial institutions, seeing their privileged position in the regulatory framework threatened, have adapted their strategies and formed new advocacy coalitions, thus acting as veto players to reform. By tying their interests and preferences to the needs of the non-financial private sector, financial institutions have thus blocked more radical change. Empirically, Pagliari and Young survey the US regulatory and legislative debates regarding derivatives and, by analysing responses by financial and corporate financial actors, show that adaptability and mobilisation can slow the pace and weaken the content of reform, accounting for incrementalism even in the face of public scrutiny and implementation capacity.

The next chapter by Sebastian Botzem shifts attention to the role of experts after the financial crisis, specifically analysing the enduring authority of the International Accounting Standards Board (IASB). Botzem provides an overview of the key controversies and changes in global accountancy and shows that the IASB chose to undertake institutional reform and modestly change its governance structure and rule-setting procedures, while exhibiting flexible crisis management in adjusting the content of rules (fair value accounting) in non-normal times. Botzem shows that veto players can follow particular tactics to block extensive change. By acting strategically during the crisis and through the presentation of pre-crisis institutional reform decisions as post-crisis governance overhaul, the IASB managed the pace and content of change and avoided a possible crisis of expertise credibility, maintaining control of the ideational agenda.

The final case moves the focus to the domestic level and housing finance. Examining the US and Danish systems pre-and post-crisis, Iver Kjar explains how actors can use their institutional position at the domestic level to oppose change. Specifically, Kjar takes an everyday IPE approach to highlight the importance of societal interests in lending legitimacy to existing and reforming governance frameworks. Kjar explains that the political power of homeowners as an electoral force has acted as a veto to radical change in housing finance in two seemingly very different financial systems and that, despite the central role of housing at the

onset of the financial crisis. When backed by such societal concerns, the financial institutions which have long benefited from these arrangements are able to maintain a privileged position and withstand calls for more substantial change.

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