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M. Moschella and E. Tsingou (2013), "Conclusions: Too little, too slow?", in Great Expectations, Slow Transformations: Incremental change in post-crisis regulation, M. Moschella and E. Tsingou (eds), Colchester, ECPR Press. pp. 193-216. ISBN: 9781907301544.

The definitive version is available at:

La versione definitiva è disponibile alla URL:

http://press.ecpr.eu/book_details.asp?bookTitleID=83

Chapter 9

Conclusions: Too little, too slow?

Manuela Moschella and Eleni Tsingou

'If there is a reproach to be made, it is that regulatory progress has not been faster.'

> Andreas Dombret, Member of the Executive Board of the Deutsche Bundesbank, [Speech delivered at the Global Seminar *Financial regulation - bridging global differences*, Salzburg,] 16 August 2012.

1. Great expectations

As some time has now passed since the onset of the global financial crisis, it is far from controversial to claim that a crisis that originated in the small subprime mortgage market in the United States triggered the worst global downturn since the Great Depression. Echoing the early stages of the 1930s crisis, the world witnessed an unusually sharp drop in asset prices and output, followed by the failure and near-failure of prominent financial institutions, all of which culminated into by generalised financial distress (Eichengreen 2012). Analogies with the early stages of the Great Depression were largely drawn to justify unconventional monetary policy by central banks: in order to prevent a repeat of the 1930s cascade of financial failures, monetary authorities around the world acted decisively in pumping liquidity. Next to monetary policy, however, the other policy area where the Great Depression analogy has been largely evoked is that of financial regulation. Similarly to the 1930s, when a regulatory clampdown on banking activity was adopted to restore confidence in the US financial sector, the crisis that started in 2007 raised expectations of a profound overhaul of the financial system and its global interconnectedness, that is, the factors that were understood to be at the heart of the crisis. Public mobilisation against the banks, the pronouncements of key leaders and regulators, which did not shy away from comparing the post-crisis environment to the 'Bretton Woods moment' that materialised as a reaction to the 1930s, were all signs suggesting that a quick and substantial (re)regulation of the global financial sector was on the agenda and about to take place.

However, this book offers a sober assessment of the way in which policy-makers exploited the window of opportunity provided by the crisis. Rather than a decisive intervention to fix the problems exposed by the crisis, the post-crisis regulatory reform process has proceeded quite slowly and by way of marginal adjustments. If the conventional wisdom holds that turning points, such as an external shock, usually bring

major intellectual reassessment and policy changes, the cases in this book in fact show that the 'external shock' of the crisis has not led to such comprehensive overhaul. Rather than rapidly lurching forward on the heels of economic disruptions and popular discontent, the key feature of the regulatory reform has been its incremental, non-paradigmatic dynamics.

While incremental change is neither wrong nor bad in principle, it is nonetheless problematic for the post-crisis regulatory agenda. The problem derives from the fact that, as political scientists know quite well, the window of opportunity does not stay open for a long time – and when it shuts down, it is difficult to restore the conditions favouring the changes that had seemingly just been possible. This is exactly the risk that is materialising as the centre stage of the crisis moves from the financial sector to the sovereign debt market. As the overriding focus of policy makers is shifting to Europe's financial turmoil and the impact it could have on the rest of the world, it has not been uncommon to hear calls to water down or delay regulatory reform. An excessive regulatory pressure, so the argument goes, could put at risk the global economic recovery, exactly at a time when the euro crisis is already impairing the global growth prospects.

However, and in spite of the fact that the sovereign debt crisis in Europe is a major source of risk to global stability, it would be not only mistaken but also dangerous to slow further down the financial regulatory reform process. To start with, the same sovereign debt crisis, which is not least driven by systemic problems in some countries' banking systems, underscores the urgent need to make the financial system more resilient. Furthermore, the financial sector is still a major source of potential risk. For instance, many banks remain highly leveraged, including those that appear well capitalised (Bank for International Settlements 2012: 5) and the level of risk is growing also in the banks that were saved by public money (Brei and Gadanecz 2012). In short, the 'problems with banks' is far from having been solved (Rethel and Sinclair 2012). On top of that, there is also mounting evidence that innovative products are already being developed to circumvent some new regulations (IMF 2012). Last, but not least, the financial scandals of the last few years, from the fraud allegations on mortgage-backed securities to the mismanagement of the Libor setting-process, have not undermined but reinforced the case for speedier and more comprehensive regulation.

The chapters collected in this volume have investigated the causes that help explain why 'the regulatory progress has not been faster', to use the words Andreas Dombret, member of the Executive Board of the Deutsche Bundesbank, in the opening statement to this concluding chapter. Specifically, we addressed the question of why the regulatory reform process has been incremental although the conditions were in place for a more decisive and radical outcome. Indeed, as clarified in the Introduction to this volume, the crisis had opened up a window of opportunity for rapid and radical reforms by significantly changing the institutional context in which financial policy-making takes place: public mobilisation and the shift of the

financial debate from technical to political bodies such as the G20 Leaders were all factors that led us to expect the kind of punctuated change that is associated with quick and profound policy changes.

In unveiling the factors that prevented a punctuated-type of change from occurring, we set out to make both empirical and theoretical contributions. At the empirical level, our study maps and assesses the changes that have taken place in a number of crucial areas of financial governance including financial supervision (Baker), offshore financial centres and shadow banking (Rixen), accounting (Botzem), banking governance infrastructure (Carstensen) and banking and derivatives regulation (Quaglia, Pagliari and Young), the rules that apply to hedge funds and credit rating agencies in the EU internal market (Quaglia) and those that govern the mortgage-related markets and products (Kjar). While these case studies do not exhaust the regulatory reform agenda, they cover important or contentious reforms which highlight activity at various levels of governance, provide a contrast between pre and post-crisis debates, and allow investigating the role played by a wide range of actors, from those that operate in the private sector to those in the official community. Furthermore, they provide a comparison of the dynamics of change across governance levels and also, in several areas that are important to the workings of global finance while going beyond the usual banking/securities/insurance subsector analyses often employed when studying financial regulation (e.g. Singer 2007). By mapping what has changed in these sectors, we also provide a complementary analysis to those economic studies that have thus far investigated the progress that has been made in making markets and institutions more transparent, less complex, and less leveraged (e.g. IMF 2012).

Furthermore, the contributions collected in this book provide a theoretically informed analysis of the changes that have taken place thus far. In particular, we deliberately decided not to elaborate new concepts and theories. In contrast, we opted to build on the insights developed within the historical institutionalist literature, which has long focused on processes of incremental, path-dependent changes, and to exploit the opportunity for fruitful cross-fertilisation by expanding those insights and combining them with those developed in the IPE scholarship.

The resulting theoretical model suggested in this volume builds on recent versions of HI in that it incorporates the importance of normative underpinning and, above all, redresses the balance between agents and institutions by taking a more agent-centred perspective that emphasises the microfoundations of political actors' preferences (e.g. Fioretos 2011: 373-76; Mahoney and Thelen 2010). Attention to these microfoundations is crucial to the processes of change examined in this book: as the constraints and opportunities in the global financial institutional framework changed following the crisis, the calculations of political actors also adapted and evolved. The ways in which they evolved, however, and the way in which they were translated into operational practices, were both facilitated *and* constrained by previous developments in the multiple institutions that make up global financial governance. Temporality and

sequence, institutional density, positions of power across actors and within networks, as well as knowledge patterns were all factors that mediated the impact of the exogenous shock of the crisis by diverting the responses towards an incremental dynamic. In other words, echoing findings at the domestic level, where historically-grown institutions largely mediate globalisation forces explaining the lack of policy converge,[1] in this study, the historically-grown features of global financial governance mediated the impact of the crisis and explain the lack of profound overhaul in its aftermath.

Adopting this theoretical framework, as will be clarified below, all the chapters in this volume shed light on how incremental change is the result of the activity of change actors and/or veto players that operate within the constraints and possibilities defined by the institutional characteristics that global financial governance has acquired over time. They were crucial in tilting financial regulation towards an incremental dynamic of change because they shaped the micro-level incentives for change actors and veto players to change (or reproduce) existing financial rules and institutions. It is also important to note that, as suggested in the Introduction of the volume, change actors and veto players did not necessarily perform different roles in the post-crisis regulatory reform process – sponsoring change and opposing it respectively. The empirical evidence is far more mixed, showing that the same set of political actors can act as both change agents and veto players.

In what follows, we review the key findings that can be extrapolated from the empirical chapters assessing the extent to which they lend support to the theoretical propositions staked out in the Introduction. Subsequently, we move to speculate on the implications of the post-crisis reform process for global financial governance. In this section, we also engage with the observation according to which incrementalism is mainly instrumental and serves to preserve the status quo. Finally, we reflect on the other challenges for the regulatory reform agenda and suggest some themes for future research, especially in a comparative perspective.

2. Summary of the findings and their implications

What change?

One of the primary contributions of the chapters collected in this volume is that of identifying and mapping the dynamics and the type of change that have been adopted across a number of key financial sub-sectors.

[1] On the differences in national policy responses to external, common challenges see, among others, Berger and Dore (1996); Schmidt (2002); Soederberg et al. (2005).

While all cases show evidence of some change and reform, the scope, pace and expected outcome of such reform all point to the significance of incrementalism in understanding the process.

To start with, in spite of the evident policy failures exposed by the crisis, popular anger and political support for more wide-ranging reforms, the type of changes that have been adopted thus far are mainly concentrated at the level of policy instruments and settings. In the immediate aftermath of the onset of the crisis, as evidenced by the pronouncements of the G20, there was a general focus on big policy areas, covering all facets of financial activity. As reform proposals materialised, the agenda was either rendered more modest or the tasks enumerated and simplified. This is especially notable in Quaglia's analysis, as it provides a bird's eye view of the changing European regulatory landscape. Instead of comprehensive reform, we see changes in policy instruments and adjustments to the level of regulation and composition of the regulators. As such, Quaglia stresses that we need to see the full picture before we can determine that the overall reform, while incremental, can indeed amount to more than the sum of its parts. The empirical cases in this volume also show contrasting examples in the *potential* importance of changes in governance settings and infrastructure. Whereas Rixen, in his analysis of the changes in the regulation of offshore finance maintains that reform activity is merely symbolic with few meaningful consequences, Carstensen, in his discussion of cross-border resolution regimes shows that rationalising bank resolution infrastructure can potentially have wide-ranging consequences as can be seen in the discussions of a European banking union.

Changes at the level of policy goals have been quite rare, if not altogether absent. This is especially the case in the mortgage services industry as can be seen in Kjar's contribution, and that despite its central role as a crisis trigger. The main exception in the empirical analyses of this volume is the ideational change in the adoption of a macroprudential regulation agenda and discourse by regulators and supervisors: this change is the one are of reform with the closest resemblance to paradigmatic changes in Hall's terminology (1993). However, although Baker accounts for this development in terms of a shift in the policy paradigm, his assessment of the shift from micro to macroprudential regulation also shows how this development is closely linked to pre-existing knowledge among regulatory circle insiders; macroprudential ideas are driven by policy entrepreneurs that hold a privileged position in the relevant institutional setting and did so in the pre-crisis period. Finally, another important category of change that is possible to extrapolate from the empirical chapters is one that pertains to the procedures according to which rules are created. In this context, Quaglia shows that a pooling of sovereignty is taking place in the post-crisis regulatory framework at the European level, whereas Botzem provides examples of how changes in the composition of the International Accounting Standards Board (IASB) enabled that professional community to claim change was taking place even in the absence of more wholesale shifts in accounting governance.

While virtually all contributions shed light on the incremental changes that have taken place thus far, a comparative look at the chapters allows us to see some important differences. In particular, under the rubric of incremental changes, it is possible to distinguish between areas in which change has been characterised by cautiousness and timid advances from areas in which change has been symbolic at best, offering little scope for further reform or change in practices at a later date.[2]

The changes in offshore and shadow banking regulation, as well as those in accounting standards fit with this symbolic image quite well. In Rixen's chapter, for instance, policymakers (change agents) tried to square the circle between jurisdictional competition and financial interest capture on the one hand and public demands for stricter regulation on the other by resorting to incremental, but often ineffective and symbolic, reform measures. But policy makers are not alone in pursuing symbolic adjustments. Private sector actors also moved in this direction in order to manage or control the process of regulatory change. In line with one of the key findings of HI, actors that stood to lose from more rapid intervention intervened to 'manage change', control it. So, as Botzem shows, the IASB's reaction to the financial crisis can be interpreted as a strategic response combining the avoidance of confrontation, reframing criticism and carefully renewing organisational leadership.

Symbolic change can also be the result when different dynamics are at play. As Kjar shows in the case of the reform of mortgage services industry, the domestic setting can make veto players of the constituency of homeowners in the US and Denmark and render change insignificant and merely symbolic also. In Kjar's case, the existence of 'economic patriots' who are reluctant to see changes in their domestic housing systems is aligned with the preferences of the mortgage industry for modest change.

As this overview of the changes mapped in the book reveals, one of the dominant features of the post-crisis financial regulatory process is the gap between what could have been possible and what actually took place: on the whole, political actors settled around adjustments in existing policy settings and instruments. In some cases, political actors even masqueraded minor action under the rhetoric of change. As such, though the authors in this volume do not automatically subscribe to a historical institutionalist approach, their findings directly speak to that research tradition. In particular, the contributions unveil the many ways in which change materializes without disruption through different types of incremental dynamics (Streek and Thelen 2005).[3] So, what explains this big gap between possibility and action? What accounts for the emergence of different types of incremental change?

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[2] Symbolic change is akin to the 'hypocrisy' that many international bureacrucies display when they face external pressures for change that are not in line with dominant internal culture and preferences. For a detailed discussion of such hypocrisy, see in particular Weaver (2008).

[3] For an analysis of different incremental changes and the disctinction between change patterns that can be characterised as layering and those that can be characterised as conversion see in particular Mahoney and Thelen (2010) and Streeck and Thelen (2005). For an application of these concepts to the patterns of change at the

Not punctuated, nor paradigmatic: accounting for incremental change

In this volume, in order to explain the prevalence of incremental change, , we suggested investigating the interaction between evolving institutional frameworks and the microlevel, agent-driven processes that create incentives for changing (or reproducing) existing financial rules. The contributing authors followed this thread in their empirical analyses. In doing so, they brought to the surface how the institutional and normative features that global financial governance has acquired over time interacted with the agency of different political actors. This interaction gave rise to a type of change that was more constrained than the type of change which would have been plausible to expect from a passing look at the post-crisis environment. In what follows, we thus review and examine the institutional and normative features that channeled change into an incremental direction as well as the political actors that set in motion the process of change and shaped it along the way. While we focus on each dimension separately for analytical purposes, it is important to remember that they are flip sides of the same coin: the post-crisis incremental dynamics cannot be successfully explained by focusing on the one without the other.

In the first place, we find that specific institutional features pushed the reform process onto an incremental direction. The findings of the chapters lend support to the propositions set out in the Introduction in that the relevant institutional constraints to major, quick change can be traced back to different levels of analysis – intergovernmental, domestic and transnational level. The common denominator here is that the relevant institutional constraints were the result of long-term processes in global financial governance. The distribution of power among states, with no one state in an overly dominant institutional position, domestic vested interests and national economic structures, the density and complexity of the sites of authority in global financial governance and the embeddedness of specific policy ideas on how to govern financial markets were all factors that were the result of institutional legacies of long-term political battles and previous rounds of reforms. In other words, temporality is crucial to understanding why the specific institutional features took the shape they did when the financial crisis burst. These institutional features dampened the push for reform following the onset of the crisis.

At the intergovernmental level, the importance of these institutional factors are most clear when looking at the cleavages among the states involved in the negotiations on regulatory reform at the EU level or in terms of overhauling offshore and shadow banking governance arrangements . With no clear leaders or too diffuse state power, ambitious reform proposals were watered down. Indeed, regulatory change was possible to the extent to which it did not produce rules that significantly depart from those in place in the few, dominant financial markets. Quaglia's empirical case shows that pre-crisis 'market making' and

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international level, see Moschella and Vetterlein (forthcoming).

'market shaping' coalitions endured and were at the centre of post-crisis reform compromises and consensus (similar dynamics within the EU are also at play in the analysis of Carstensen this volume). On the other hand, Rixen provides an account where there was ultimately a lack of interest in clear action when it came to offshore and shadow banking regulation among the main state actors in financial governance which were unable to overcome issues of jurisdictional competition.

Domestic factors are also relevant in explaining the prevailing pattern of incremental change. Interest group lobbying and the structure of domestic economies have been of particular importance. Indeed, in line with our theoretical expectations, the political actors that stood to lose from the outcome of the regulatory process took action to preserve their interests and the investments made in existing regulatory designs. This is exactly the case of the financial industry. Pagliari and Young's chapter clearly shows how the domestic financial industry in the United States influenced the pattern of regulatory reform of derivatives. It also explains, however, that this influence was conditional on the industry's capacity to adjust its advocacy strategies in response to the changes in the regulatory environment triggered by the crisis. In particular, financial institutions aligned their interests and preferences to those of a wider range of corporate stakeholders, moving the focus away from calls to 'punish the financial sector' and emphasising the importance of not harming Corporate America instead.. It was exactly the mobilisation of corporate end-users of financial products, and in this case, especially derivatives, that helped the financial industry to slow down more ambitious reforms in this area. In this instance, therefore, we have a case of vested interests maintaining their privileged position and weakening regulatory reforms.

Domestic considerations were also a key determinant of the incremental pattern of change for a number of regulatory reforms debated at the international level, where the variety of domestic financial systems mattered. In particular, whether a system is more market-based or bank-based had an impact on the regulatory process affecting both preferences and coalitions at the international level. This is evident, for instance, in the division between the US and UK, on the one had, and continental EU countries in the negotiations on Basel III first, and the CRD IV later. Reflecting the organisation of their domestic markets, continental EU countries acted to defend the specific structure of national financial markets arguing that 'traditional' (continental) banks engaged in less risky trade finance/financial activities. They thus opposed the leverage ratio, asked for a modification of certain aspects of the liquidity rules and wanted a longer transition period (Quaglia in this volume, also Howarth and Quaglia 2013). Elsewhere, we observe seemingly different systems such as those of the US and Denmark exhibiting similar resilience in keeping their housing finance systems and the practices of mortgage providers in particular relatively unchanged (Kjar in this volume).

Among the domestic factors that pushed the regulatory reform process onto an incremental direction, capacity problems in domestic administration were also important as Baker's chapter reveals. In this case,

the translation of macroprudential concepts into operational practices has been slowed down by lack of data and the need for a period of experimentation and trials. Anticipating future implementation problems, regulators converged on more incremental measures while keeping a long-term macroprudential agenda alive.

Other factors that help explain the post-crisis incremental dynamics can be found at the transnational level and, in particular, in the specific institutional configuration that global financial governance has acquired over time. Echoing historical institutionalist insights on institutional density and complementarity as discussed in the Introduction to this volume, a number of case studies show that the institutional landscape, which consists of several club-like and expert-driven institutions (see also Tsingou 2012), creates positive feedback effects and increasing returns for the political actors that operate in such a fragmented landscape (Rixen this volume). Under these conditions, the incentives for radical change are limited at best and may be driven mostly by concerns for efficiency (Carstensen this volume). Indeed, actors that enjoy the positive returns from existing institutional designs are more inclined to adopt only those rules that are compatible with existing ones. The incremental dynamics in accounting regulation are a case in point. As Botzem's chapter shows, the IASB's institutional configuration, which values expertise and favours isolation from public pressures, was the most powerful obstacle to a profound post-crisis overhaul. Since the organisation is able to define what counts as expertise and exercise social closure, the only change that can materialise – and the one that actually materialised after the crisis – is a limited, and highly-controlled type of change. Indeed, this dynamic ensures that change does not call into the question the functioning and expert legitimacy of the institution..

Another key factor that can help account for the substantial continuity in global regulation can be traced back to the normative framework. Baker's analysis of the inclusion of macroprudential (MPR) ideas in the reform process shows that while the inclusion of these ideas as policy itself is new, we need to consider first, that these ideas were theorised and debated (albeit in small circles) prior to the crisis and that adoption is gradual and is happening in parallel with adjustments to existing microprudential principles. As such, MPR is 'new' thinking that does not, even in ideational terms, fully replace 'old' thinking. In a different case, Carstensen, examining the development of resolution regimes in the aftermath of the crisis, points to the contradictions between ideational consensus in principle but the difficulty of reconciling ideas of 'universality' and 'territoriality' in practice.

Although the institutional and normative characteristics summarised thus far are certainly key factors in explaining the incrementalism in the post-crisis reform process, the role of actors engaged in the reform process as change agents and veto players needs to be further investigated. That is to say, in order to explain change, we should also focus on 'the microlevel processes that create incentives for individuals to reproduce (or not) designs during and after [critical historical] junctures' (Fioretos 2011: 375-76). Also, we

should recognise the dynamic relationship between structures and agency without privileging one over the other. Botzem puts it well in this volume in his analysis of the IASB, noting that simply referring to the institutional characteristics of the IASB is not sufficient to explain how the organisation reacted to the crisis. A thorough explanation of change instead requires focusing on how powerful actors inside the IASB organised, mediated and actively managed change.

Building on the importance of combining an agent-centered approach with the more traditional insights of historical institutionalism, all chapters take as a starting a point the identification of the key actors that support/advocate (change actors) and oppose change (veto players) within the distinct constraints and opportunities provided by the institutional environment in which they operate. In this context, actors' motivations and, more importantly to the purposes of this study, actors' reform strategies are endogenous to the distinct institutional context.

The findings of the empirical chapters reveal that the key political actors that support or oppose change include both state and non-state actors, officials and private sector representatives. Furthermore, in line with our theoretical expectations, the identity of change agents and veto players cannot be anticipated ex ante because it is not fixed. The same actor can play the role of change agent and veto player according to the institutional context in which they operate. For instance, government actors sometimes acted as change agents for certain reforms and as veto players in others. This is particularly evident in the chapter on the post-crisis EU regulation (Quaglia this volume). Whereas the main political cleavage was between the Anglo-Saxon countries and the Continental EU countries in the case of banking regulation, with the former acting as change agents and the latter as veto players, these roles were less stable as the regulatory process moved to other financial sectors. Quaglia shows that instead, in the cases of the regulation of credit rating agencies and hedge funds in Europe, France and Germany were the main sponsors of the new rules, hence acting as agents of change, with the UK and some nordic countries such as Sweden and Finland performing veto player roles. The importance of differentiating between types of public actors and their potential roles in pushing or stalling reform also comes through in the empirical cases, most notably in Carstensen's analysis of post-crisis bank resolution regimes. Carstensen shows that while there has been much change agent activity from the European Commission on cross-border resolution thinking and policy, national authorities are more reluctant to push through ambitious implementation of these ideas (Carstensen this volume).

The private sector too has acted both as change agent and veto player according to the sector or issue area under regulation. In Carstensen's analysis, for instance, the private sector as represented by the Institute of International Finance is a clear change agent in promoting internationalisation of the regime. Elsewhere, however, the interests of the financial industry follow veto player characteristics. This is notable in the example of derivatives regulation in the US (Pagliari and Young this volume) and mortgage providers in the

US and Denmark (Kjar this volume) but also in the governance of accounting standards, where the IASB strategically defined rules for 'normal' times (Botzem this volume). As such, the findings from the empirical cases warn us to keep an open mind about who wants change and in whose interests it is to stall it and to recognise the issue-specific dynamics and different tactics and motivations at play.

In conclusion, our study, like most HI, places significant attention on historical contextualisation 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). At the same time, however, we stressed the importance of a careful examination of agency within the institutional constraints and opportunities that political actors face in their activity. Despite some expectations for bigger and speedier changes, the activity, motivations and strategies of change actors and veto players has been heavily informed by the deep-seated institutional characteristics that global financial governance has acquired over the past two decades, entrapping change into an incremental dynamic.

3. Incrementalism as a regime-preserving strategy? Unpredictability and complexity of the post-crisis politics of financial reforms

To summarise the main message of this book, which is supported by the solid empirical findings reviewed above, we can say that the onset of the crisis created the perceived conditions for quick, paradigmatic change in how global finance is governed. All the textbook factors for such change were indeed in place: from the large-scale implications of regulatory failures to the politicisation of previously technical issues and the changes in the policy-making context. In spite of this window of opportunity, however, global financial governance has been largely fixed at the margin via small, incremental changes in key regulatory areas. In short, the great expectations for change have been largely disappointed. The distinct institutional characteristics of global financial governance reduced the room of manoeuvre for the political actors pushing for change and even foreclose what they could think of in terms of regulatory reforms. The same institutional features that global financial governance has acquired over the past two decades played into the hands of veto players transforming them into de facto change agents that managed the pace and content of the regulatory reform process. Cautious advances and regulatory gaps have thus been the ultimate result – a situation that is miles away from a profound rethink and restructuring of how global finance is regulated.

Given the current state of affairs in financial regulation several years since the start of the crisis, we can raise the question of whether the incremental policy-making mode that we unveiled in this book adds up to

little more than a regime-preserving strategy. In other words, is it possible to conclude from our analysis that the process of change has altered something just to ensure that things stay as they were before the crisis? Is incrementalism just a cover for conservative forces, both among change agents and veto players, to maintain the status quo? And does that mean that the long-term consequences of this round of reform will be negligible for the future of global financial governance?

The most immediate – but inaccurate – reading of our findings suggests a positive answer to these questions. Indeed, as the findings have shown, more often than not the regulatory reform process has accommodated the requests of those political actors that wanted to preserve (and not change) the existing financial regime. By building a coalition with corporate end-users, the financial industry succeeded in containing the regulation of the derivatives market – and thus preserving their profitable activities in this market. Likewise, change agents within the IASB managed the regulatory reform process in a way that maintained the primacy of professional, private expertise in setting global accounting rules. The incrementalism of banking reforms, including those of the shadow banking sector, was strongly supported by those governments that wanted to preserve the competitive advantage of their domestic financial industry. A regime-preserving orientation can also be detected among the most outspoken change agents: for instance, while BIS and other prominent economists forcefully advocated the adoption of MPR, the debate has evolved in a way that preserves the centrality of unelected technocrats in shaping the rules for financial markets.

Although these findings clearly show that long-term trends, entrenched positions and crystallised power constellations in global financial governance severely constrained the politics of post-crisis reform, we argue that the incremental dynamics of change that have been analysed in this volume cannot easily be dismissed as nothing more than an example of regime-preservation. This argument rests on both empirical and theoretical observations.

At the empirical level, several findings indicate that the incremental dynamics that characterised the post-crisis regulatory reform are not solely a strategy for preserving the status quo but also a necessary strategy for altering the status quo and entrenching change. For instance, in case of macroprudential regulation, economists in key international regulatory agencies deliberately decided to embark on a slow-moving experimentation of the new regulatory ideas in order to collect the necessary evidence to both win the policy debate among technocrats and gather support from political leaders and the wider public. The same financial industry did not overly oppose some key regulatory proposals because of their incremental nature: that is to say, the opposition of the financial industry was less decisive than in the recent past also because the proposed reforms have postponed implementation phases allowing both for more time to adapt to the new rules and to organise a more sustained lobbying effort in more propitious policy-making contexts.

In short, change agents settled on a no-radical solution in order to win consensus or overcome institutional constraints. Veto players also accepted – albeit grudgingly – incremental reforms because they thought that their incremental nature would have pushed back the moment in which the effects of the reforms would have been felt. Anticipating time inconsistency problems, with policymakers reneging on their policy decisions or rethinking them as a result of lobbying pressures, incremental reforms became acceptable even to those actors who would have otherwise opposed them. While these incremental changes are a 'second-best option' from the perspective of those who wanted more radical transformations, their long-terms effects should not be underestimated as the following theoretical observations contend.

Indeed, at the theoretical level, the ambiguity of the new rules and the unintended consequences of the post-crisis round of reforms are likely to undermine the regime-preserving nature that incrementalism is often accused of. To start with, although the current round of reform can be read as attempt of producing stability in an unstable world by formalising risks and ambiguities (Best 2005 ; Blyth 2006), new rules still need to be reproduced in practice through agents that apply them to their specific – and changing – situations (Streeck and Thelen 2005). Wolfgang Streek (2011: 664) summarises the logic behind the processes of change that take place due to the 'imperfect reproduction of existing rules':

'the conditions under which social rules are supposed to apply are inevitably unique and varying in time, due to the fact that the world is more complex than the principles we have devised to make it predictable. This forces actors to apply rules creatively, actualizing and modifying them in the process'.

In short, there is an inherent ambiguity in the rules that guide behaviour. This suggests that the rules that have just been created will be in need of (re)interpretion, especially in highly evolving contexts as financial markets are. Their reproduction and practical application are thus not given but subject to interpretation by the relevant actors. Given the need for interpretation and reproduction, even the most 'incremental', managed changes adopted thus far provide actors with the room of manoeuvre to develop new interpretation about how a specific rule should work under changed circumstances or about how a specific aspect of the world economy should be (re)interpreted. As Mahoney and Thelen (2010: 11) put it, 'actors with divergent interests will contest the openings this ambiguity provides because matters of interpretation and implementation can have profound consequences for resource allocations and substantive outcomes.' This, in turn, can bring about a more profound type of change than the one that it is possible to envisage from today's perspective.

Next to the ambiguity inherent in the new financial rules, another consideration that speaks against the equation incrementalism = conservatism derives from the application of the notion of unintended consequences. Indeed, as HI scholarship has long demonstrated, change cannot be conceived as a dichotomous variable but it is better conceptualised as a continuous interaction between continuity and change (Thelen 1999). It is this blend of elements of continuity and change that allows for unexpected consequences to arise. That is to say, once some elements of change are brought into well-defined institutional designs, their consequences are not easy to anticipate. For instance, it is not uncommon that rapid and substantive policy shifts are triggered by the slow, cumulative effects of previous policy changes (Haydu 1998; Howlett 2009; Kay 2007).

This is exactly the case that may materialise in the area of global financial governance. Although the reforms that have been adopted thus far are based on small, slow adjustments to existing rules and institutions, these apparently insignificant changes can set the stage for bigger ones tomorrow. It is already possible to speculate on some developments that may bring about these big, unintended consequences.

For instance, the unintended effects of the rules adopted today may spring from the wrong incentive and negative spillover effects. Banking regulation can serve as a prime example here. Indeed, one of the immediate threats is that of regulatory arbitrage, as stricter rules imposed on banks via Basel III set incentives for activities and risks to be pushed from the core of the financial system outward to the nonbank financial sector, where the new rules do not apply. As already noted, then, there is mounting evidence that innovative products are already being developed to circumvent some new regulations (IMF 2012). In short, today's regulation may create the conditions for increased risks tomorrow. As these risks become clear – or lead to a new crisis – the case for more stringent regulation in today's overlooked markets will become a pressing concern.

A similar pattern towards more decisive regulation than it is currently the case may be triggered by the lack of regulation. That is to say, there are financial markets and products whose regulation has not yet been discussed or entered the radar screen of regulators and policy makers. This challenge is not new to scholars of financial regulation: financial regulation – as most other forms of regulation – is usually reactive, rearward-looking. Like the generals that keep on fighting the last war, after a crisis starts, policy makers and regulators have an incentive to regulate the areas that are perceived to be at the origin of the crisis. However, given the speed of financial innovation and the scope of financial interconnectedness, it is likely that today's reforms (and lack thereof) won't stand up to the test of the next crisis, triggering a new round of regulatory reform. Although the regulatory actions that have been adopted so far are largely incremental, they have nonetheless set in motion a dynamic of change that is largely unpredictable especially in light of the evolving conditions in financial markets. This situation does not ensure that political actors will totally control the outcome of the regulatory reform process.

This unpredictability is further discernible from the new alliances that have been built as a reaction to the crisis. In particular, the financial industry-corporate coalition is more unstable that the coalition made up solely of financial firms that dominated the reform process since the late 1990s. Although the two groups' interests converged around the need to mitigate the effects of too stringent regulation of derivative markets and products, the foundations upon which this alliance is based are shaky at best. The two groups represent constituencies with dramatically divergent preferences that reflect the different distributional implications of cross-border capital flows (Frieden 1991; Goodman and Pauly 1993). Furthermore, the presumed conservative character of current incremental reforms is also called into question by the growing divergences within the financial industry. Rather than being a monolithic group, the crisis has exposed severe fault lines among financial industries (Helleiner and Pagliari 2011: 184). As a result, and in spite of its incremental nature, the post-crisis regulatory reform process does not guarantee a 'lock-in' effect based on the reproduction of the status quo and its privileges.

Based on the above observations, it would be premature, we submit, to dismiss the result of the post-crisis regulatory reform out of hand. Under the dominant incremental dynamics highlighted in our case studies, there are important elements of novelty that may, in the long run, bring about a more profound overhaul of the way global finance is governed. This conclusion is not dictated by some sort of 'optimism' towards the reform process. It is based on a careful analysis of empirical findings and theoretical insights.

So, in our view, the main problem with the post-crisis regulatory reform lies not so much in the presumed conservatism associated with the incremental dynamics of change. More disturbing than the potential conservative effects of incrementalism are its complexity effects. That is to say, one of the major problems of the incremental dynamics of post-crisis regulatory reform lies in inducing the creation of complex regulatory systems. Rather than dismantling and replacing old rules with new ones, the incremental regulatory process has indeed proceeded by small adjustments, modifications, and rule expansions. However, as new rules have been layered on old ones (as in the case of banking regulation with the adoption of Basel III, see Baker in this volume) or existing supervisory tools have been redirected to new purposes (as with the emerging consensus on how to resolve distressed financial institutions, Carstensen in this volume), the resulting outcome has been a complicated regulatory web that puts extra work on regulatory authorities in adequately assessing risks in global financial markets while multiplying the possibilities for private actors to game the same rules.

Andrew Haldane, Executive Director of Financial Stability at the Bank of England, has powerfully summarised the potential negative effects of this layering-cum-complexity process by examining the new banking regulation embodied in the Basel III accord. In a paper presented at Jackson Hole in August 2012, titled The Dog and the Frisbee, Haldane (2012) explained that dogs do not need to understand the physics behind a frisbee's trajectory in order to catch it. Similarly, capital standards are better when they are higher

and blunter than when they are lower and more sophisticated. Complex maths, models and risk-weighting that underpin current banking regulation are easier for banks to game than simple rules. Furthermore, complex rules are of not help to regulators too. Haldane illustrates this point by comparing predictions about the chances of failure for a sample of 100 global banks in 2006, based on the simple ratios of assets/equity with the corresponding complex, Basel III-style risk-weighted one. The simple metric wins decisively over the more sophisticated risk-weighted system.

So the major risk stemming out from the incremental dynamics of the post-crisis financial regulatory reform is not so much the potential conservatism associated with the regime-preserving efforts of the reforms adopted thus far. But one of the most potentially damaging effects of the incremental patterns of reform is the complexity it has helped creating: given the inability to bring about a major overhaul of global financial regulation, change agents and veto players have created a regulatory system that reproduces and amplifies some of the mistakes of the recent past. In particular, this pattern of incremental reproduction has increased the complexity of the regulatory environment. This could help private sector actors to escape the rules that have just been created and put an excessive burden on public authorities who are in charge of supervising the new system.

4. The politics of global financial regulatory reforms: a prospective research agenda

Several years into regulatory negotiations and reforms, time has come to start reflecting on the main challenges that policy makers and regulators around the world will face as the result of the reforms that have been adopted thus far. In particular, it is possible to think of at least two main challenges – whose investigation will be of primary importance for scholars interested in the politics of financial regulatory reforms. These challenges pertain to the problem of implementation and to the relationship between advanced economies and emerging markets in the governance of the global financial system.

The first challenge is associated with the implementation of the measures whose origins and adoption have been traced here. By the time we started working on this book, the greatest challenge to the post-crisis reform process stemmed from coordination and cooperation problems among the actors involved in the negotiations – not only governments but also regulatory agencies and private sector actors. That is to say, the main problem was that of overcoming cognitive limitations, mutual distrust and conflicting interests that hinder the adoption of consensus solutions. Given this overriding concern and considering that much regulatory reforms have only recently been adopted or remain under examination, the chapters in this book have analysed the politics of the post-crisis regulatory reform by focusing solely on the stages of rules

formulation, negotiation, and decision. In other words, we opted not to cover in our analysis the other important stages of the regulatory process, namely rule implementation, monitoring, and diffusion. It is important to note, however, that issues related to implementation – such as the presence of necessary organisational capacity and networks to implement a specific regulatory reform – loom large during the process of regulatory formulation, negotiation, and decision. For instance, Baker's case study in this volume shows that the political actors involved in the development of the macroprudential regulatory framework (mainly economists from key domestic and international regulatory agencies) have been cautious in pushing through the new framework because of the need to test new ideas and develop appropriate organisational capacities in domestic agencies.

In short, thus far, we treated implementation problems as one of the independent variables that help explain the incremental pattern of the post-crisis regulatory reform. When political actors anticipated implementation problems, they settled on minor, slow-moving regulatory solutions. However, implementation problems can also be treated as the dependent variable to be studied. That is to say, a question can be raised of what factors and conditions favour (or hinder) the implementation of new regulations. And this is one of the most pressing issues that the international community is facing in the next stage of the post-crisis reform process. So, although the empirical chapters have bracketed this important issue, in these conclusions, we can start reflecting on what the major implementation problems are and what research areas they open up.

To start with, implementation problems are likely to differ according to whether implementation is required at the international or domestic level. At the international level, implementation will require either the development of new skills and bureaucratic practices by the regulatory agencies that will have to perform new tasks or the development of cooperative practices among international regulatory bodies. For instance, the implementation of the macroprudential framework requires regulatory bodies such as the BIS, the FSB and the IMF to develop common understandings of the measures that will make up the MPR policy toolkit. Furthermore, the implementation of the MPR ideas is closely related to the development of new methodologies and data to assess risks from a macro, systemic perspective. In other words, the shift to a systemic oversight approach requests a demanding organisational effort from the international bodies that will undertake it – i.e. it requires these bodies to develop resources to collect and pool information on a wide range of potential sources of financial risks. A systemic approach to financial surveillance also requires the development and operationalisation of new standards against which to assess domestic policies (on these issues see also Baker 2012; Moschella 2011). In order to ensure implementation of the agreed-upon measures, international regulators will also need new powers. The secretary general of the International Organisation of Securities Commission (IOSCO), David Wright, has already made this point explicit noting that, in order to be successful, the watchdog would need more deterrents at its disposal. In

his words, 'It's all very well setting up principles but we have to implement them globally. Our role at Iosco will increase. Imagine a world where there are 15-20 major financial markets with nobody at global level able to enforce [regulation].'

Implementation of some of the new reforms will also require the deepening of inter-institutional cooperation among several regulatory bodies. For instance, the transformation of the FSF into FSB has also been marked by an increased, formal role of the FSB in overseeing the activities of the other standard-setting bodies. In particular, the FSB has been delegated the power to 'undertake joint strategic reviews of and coordinate the policy development work of the international standard setting bodies to ensure their work is timely, coordinated, focused on priorities and addressing gaps' (FSB Charter, Article 2). For this new power to be effectively implemented, however, the FSB will need to interact more closely with the other standard-setting bodies in order to assess their progress. Similarly, the post-crisis 'data initiative', which has been adopted at the promptings of the G20 Leaders to fill in data gaps on key financial sector vulnerabilities relevant for financial stability analysis, is closely dependent on the collaboration of several international bodies. For instance, the Interagency Group on Economic and Financial Statistics (IAG), which was established at end-2008 to coordinate work on the improvement of economic and financial statistics among international agencies, include the Bank for International Settlements (BIS), the European Central Bank (ECB), Eurostat, the IMF, the OECD, the UN, and the World Bank. The collaboration of the FSB and the IMF is another prime example of the way in which inter-institutional coordination will impinge on implementation efforts. Indeed, both bodies have been mandated to carry out Early Warning Exercise (EWE) to detect vulnerabilities in the global financial system. The implementation of the newly-launched EWE will thus closely rely on how well the two bodies coordinate their surveillance activities.

The implementation of the regulatory reforms adopted thus far will also face domestic-level problems. The starting point here is that, much like other global regulation, the effectiveness of the rules governing global finance closely depends on domestic regulatory regimes (Mattli and Woods 2009: 3; on global regulation see also Büthe and Mattli 2011 and Djelic and Sahlin-Andersson 2006). This is particularly the case because much of global financial regulation is best characterised as soft law. As the empirical findings here collected have shown, the content of the post-crisis regulatory reforms has not deviated from this general reliance on soft law. As a result, the conditions present at the domestic level will be crucial for financial regulation to become binding. Hence, differences in domestic financial markets and regulatory structures, existing legislation and regulators' organisational capacities will certainly play a key role in the pace and content of the implementation efforts. The presence of different conditions across domestic regulatory settings poses the risk of uneven or partial implementation of the regulatory reforms adopted thus far. Fragmentation and potential regulatory arbitrage effects cannot be ruled out. As Quaglia notes in this volume, 'in the case of the new pieces of [EU] legislation, their effects will very much depends on how they are implemented in

the member states.' The variation in domestic conditions also poses the risk of delays in implementation. This is particularly the case in those jurisdictions where the domestic implementation process opens up several access points to the lobbying of the financial sector, with the United States being an apt case in point (cf. Singer 2007; see also Connaughton 2012). These observations thus point to the need for scholars interested in the politics of financial reform to monitor how the implementation of the important – although incremental – reforms will unfold in the next few months and years. Furthermore, this is exactly an area where cross-fertilisation between IPE and comparative political economy could prove the most promising. That is, in order to make sense of future implementation patterns, we need both an understanding of the distinctiveness of global financial rules but also of the varieties of national regulatory structures that 'mediate' the international rules.

Next to implementation problems, another serious challenge for the future of the post-crisis regulatory process stems from the rise to the prominence of emerging market countries in the international financial regulatory debate. Although the debate is far from settled on whether and when emerging markets will take over the advanced economies (c.f. Prasad and Ding 2011; Subramanian 2011), it is far from controversial that over the past two decades, per capita income in emerging and developing economies taken as a whole has grown almost three times as fast as in advanced economies (Derviş 2012). Emerging markets have therefore a key interest in ensuring that their economic achievements are not undermined by global financial instability, as has been the case since the start of the crisis. In spite of the decoupling hypothesis positing the resilience of the emerging markets in the face of the financial shocks in the advanced world, emerging markets have been put under severe pressure by the developments in the more advanced financial markets. In particular, while in the early stages of the crisis emerging markets had to cope with severe capital outflows caused by the process of global deleveraging, in the final quarters of 2009, the easing in monetary conditions in the advanced economies pushed capital flows in the opposite direction. Since then, in order to stem currency appreciation and asset bubbles, several emerging countries, such as Brazil, Chile and Peru, have heavily intervened in their currency markets reviving memories of currency wars (Financial Times, Trade war looming, warns Brazil, 10 January 2011). In other words, the financial stability and the economic well-being of emerging market countries has been put at risk by the 'spill-over' effects of the policies adopted in the advanced economies to manage the crisis since 2007.

A more assertive role for emerging market countries in the international financial regulatory reform agenda should therefore not be surprising. For instance, these countries are likely to be key players in the debate on the legitimation of the use capital controls (Gallagher, Griffith-Jones, and Ocampo 2011). This group of countries also has key interests in other items in the international regulatory agenda, from the measures to ensure the safety of banking systems to those to curb speculation on commodity and food prices.[4]

[4] For the role of the US in regulations over agricultural derivatives markets see Helleiner and Clapp (2011).

Emerging markets' potential growing assertiveness is also justified in light of the discredit brought on advanced economies' financial system as a result of the crisis. It is now abundantly clear that, although many factors contributed to the crisis, weak regulation played a primary role. Indeed, the countries where the global financial crisis originated had weaker regulation and supervisory practices (for example, less stringent definitions of capital, less stringent provisioning requirements, and greater reliance on banks' own risk assessment), as well as less scope for market incentives (for example, lower quality of financial information made publicly available, more generous deposit insurance coverage) (World Bank 2012, ch. 2).

In short, the crisis hit hardest the countries where regulation was weaker– and the weakest ones belong to the group of the advanced economies in contrast to what had happened in the 1990s. At that time, the post-crisis financial architecture exercise was dominated by the G7 countries and their leadership was amply justified in light of the financial weaknesses that the crisis exposed in the emerging markets (c.f. Baker 2006). Should we follow the same script today, emerging markets should play a more decisive role in the post-crisis financial regulatory reform process. This is especially the case for the BRICS whose financial support has been courted more or less explicitly by several advanced economies especially in Europe.

As such, one important future line of research lies in shedding light on the role of emerging markets in the international regulatory debate and its likely trajectory and implications. In this connection, it will be increasingly important to know more about the domestic political economies of these emerging players in global financial governance. In other words, while the literature on global financial governance and regulation has primarily focused on the political economic characteristics of the advanced economies in general and key jurisdictions in particular (such as the US and the European Union), future studies may no longer ignore political economic developments in the emerging market countries. Besides, we need to know more about the interest group politics, regulatory practices and ideas in these countries to make sense of their role in the global financial regulatory debate. This knowledge is all the more needed in light of the changes in the membership in several regulatory committees that have been decided on the heels of the crisis. Indeed, since 2008, the Basel Committee for Banking Supervision expanded from 13 member countries (all developed economies) to 27 (of which 10 are emerging economies). The Committee on the Global Financial System also expanded from 13 to 22 countries including Brazil, China, Hong Kong, India, Mexico, Singapore, and South Korea. The shift from the FSF to the FSB has also been accompanied by membership expansion from 11 countries to 24 countries, of which 10 are emerging economies in addition to Hong Kong, Singapore, and South Korea. In December 2010, the IMF has also adopted a significant realignment of its quota shares. Although the reform has not yet been approved by the required majority to enter into force, once enacted, it will result in the presence of the four largest emerging economies (Brazil, China, India, and Russia) among the Fund's ten largest shareholders.

This membership expansion brings with it a potential risk of heterogeneity of preferences among the actors that are involved in financial negotiations – a development that stands in stark contrast to the prevailing homogeneity that has characterised global financial governance over the past two decades (Helleiner and Pagliari 2011: 183). Future research will thus need to investigate whether such heterogeneity will become an asset to improve the rules that govern global finance or an obstacle to any decision.

Finally, another great puzzle for future research agendas in global financial governance relates to the role of the states and public authority vis-à-vis that of the markets (Germain 2010) and the resilience of pre-crisis economic ideas, and in particular, those associated with the 'neoliberal' orthodoxy. The failure to abandon the economic theoretical basis of financial governance, in spite of the events that have been unfolding since 2007, is indeed one the great puzzles of the post-crisis debate (cf. Crouch 2011). Our analysis and the empirical insights of this volume show a great deal of nuance on this issue, including on the importance of differentiating between form and policy content when discussing financial reforms. As such, future research may also focus on whether incrementalism and layering have altered neoliberal ideas-derived practices in financial governance. Finally, following the ultimate regulatory outcomes of the issues areas studied in this book (and others) will lead to clearer understandings on whether we can expect any further shifts in the make-up of the governors of finance, with technocratic expert networks coming to share governing space with new actors and with the post-crisis politicisation of finance leading to more ingrained practices of public scrutiny.

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