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Introduction

Over the past decades, few things have been anticipated more anxiously or eagerly than the decline of American financial power. Although few doubt that the United States has benefited tremendously from the expansionary dynamics of financial markets, this advantage is often seen to have involved speculative gains bought at the expense of long-term sustainability – that is, a reckless mortgaging of the future. American finance is seen to be hugely inflated, not supported by economic fundamentals, and forever in danger of collapsing. And so, with each major crisis (the end of the Bretton Woods system in 1971, the stock market crash of 1987, the bursting of the Internet bubble at the turn of the century, and the "subprime" crisis that struck in 2007), a chorus of commentators rises to announce that the days of American hegemony in global finance are now really numbered. But American finance has repeatedly shown itself to be quite resilient. The fact that predictions of imminent decline or collapse have been made time and again over the past decades should lead us to approach such claims with a certain degree of caution. This book argues that there is considerable coherence to the construction of American financial power: Far from a house of cards, it is a proper edifice, built on foundations with their own distinctive points of strength and weakness. Even if the early twenty-first century turns out to have been the apogee of U.S. financial power, American financial actors have built up capacities that they will be able to wield for decades to come, and how the American state manages the dynamics of its financial system will remain a central question until well into the present century.

MARKET, STATE, AND POWER

The perceived threat to America's hegemonic position during the 1970s was one of the founding concerns of the field of international political economy (henceforth IPE). The approach that emerged took the Bretton Woods era from the end of World War II to the early 1970s as representing the high point of American power. In this perspective, whereas during the interwar period America's isolationist reluctance to shoulder the responsibilities of hegemony had been responsible for global economic breakdown (Kindleberger 1973), after World War II the United States committed itself to ensuring the stable reproduction of the international market economy by embedding it in regulatory institutions (Block 1977; Ruggie 1982; Gilpin 1987). The rise of economic globalization trends was seen to upset the parameters of this order of "embedded liberalism" and so to erode U.S. financial power.

Perceiving not only America's growing balance of payments deficits but also its consistent ability to attract capital to finance them, more recent IPE perspectives began to question strong claims about the decline of American power. They criticized the tendency in orthodox IPE to reduce political power to the policies of the official state and to pay insufficient attention to its socioeconomic sources. The notion of "structural power" was introduced to draw attention to the fact that control often operates in more indirect ways, that is, by influencing the institutional conditions under which actors make decisions. This concept provided the theoretical basis for a revised interpretation of the relationship between financial globalization and the American state: The reemergence of global finance, although responsible for the demise of the U.S.-dominated embedded liberal Bretton Woods institutions, also laid the basis for a more structural form of American power (Strange 1986, 1988; Gill and Law 1989; Walter 1993; Helleiner 1994; Arrighi 1994; Germain 1997; Seabrooke 2001).

However, in practice this notion of structural power has remained close to traditional notions of "the market," reflecting a persistent structuralism in IPE scholarship that has entailed a continued reliance on an external conception of the relationship between market and state. Financial expansion is consequently still depicted as a process whereby markets autonomize themselves from their institutional context and undermine political capacities: The analysis of American finance has remained centrally organized around the idea of a transition from embedded liberalism to the "disembedding" tendencies seen to be characteristic of the era of neoliberalism and globalization. The recent IPE literature has accordingly tended to develop its own thesis of American decline. Although it is recognized that the growth of financial markets has entailed considerable benefits for the United States, those are seen as primarily speculative in nature and not properly embedded in or supported by institutional structures; eventually, it is often argued, the American state will have to bow before the disciplinary imperatives of globalizing financial markets (e.g., Strange 1986, 1988; Germain 1997; Brenner 2002; Arrighi 2003). Thus, although the capacity of the American state is to some extent acknowledged, it is treated as a residual category, understood primarily in terms of the ability to defy or postpone the effects of growing economic constraints. This book is motivated by the belief that the very significant financial powers wielded by the American state deserve a less cavalier treatment, and it will argue that this requires breaking with an approach to political economy that is centrally preoccupied with the logics of state and market.

Even if one of modern-day IPE's central claims is that the distinction between politics and economics should not be mistaken for a material separation, the implications of this insight have not been pushed far enough to permit a full conceptualization of their institutional linkages (Watson 2005). This is particularly evident in the prominence of a particular appropriation of Polanyi's (1957) work, which frames capitalist development as driven by the interacting logics of market disembedding (i.e., the tendency of markets to escape from their institutional context) and reembedding (i.e., a countermovement whereby political forces seek to re-regulate the market). Such an approach conceptualizes the role of institutions primarily in terms of their ability to constrain markets and limit their reach; the expansionary logic of markets itself is seen not as constructed through the norms and rules provided by institutions but rather as driven by a presocial logic that is at odds with the regulatory effects of institutional structures (Krippner 2002; Beckert 2003; Gemici 2008; Jones 2008). This framework, premised on the idea that markets and institutions are governed by their own distinctive logics, is not sufficiently geared to the possibility that markets and their properties might, at their very core, be institutional constructions that can potentially function as vehicles of state power.

The approach adopted in this book conceptualizes market expansion as involving the creation of new social forms and linkages and so putting in place the foundations for new patterns of institutional control over the dynamics of human interaction. In recent years, several perspectives have emerged that emphasize the socially constructed nature of even the most basic and seemingly technical economic phenomena (Knorr-Cetina and Bruegger 2002; de Goede 2005; Mackenzie 2006; Aitken 2007; Langley 2008). This "social finance" literature is critical of IPE's tendency to attribute independent causal powers to markets and to give short shrift to the microlevel norms and practices that shape financial life. It views the structural aspects of power not merely as setting parameters for action but as operating through the very production of market actors' identities, capacities, and interests. This approach, however, has tended to generate its own kind of structuralism: Market processes are now seen to operate through effectively internalized financial norms. Political institutions are considered important nodal points of social relations but nonetheless viewed as being fully subject to a regime of market pressures. As a result, the portrayal of neoliberal financial expansion in the social finance literature is largely consistent with IPE's analysis of this process in terms of the disembedding of financial markets and their disciplinary effects.

It is important to approach the institutional construction of financial life as a more open process: Human agency is not exhausted or preempted by social forms and always retains an element of instrumentality in relation to them. This does not, however, imply a return to the assumption of the rational economic actor with a preexisting set of interests (Whitford 2002). Instead, the perspective advanced here emphasizes the pragmatic dimensions of the process of social constitution: Our engagement of institutional forms is motivated by the experience of problems and the aim to address those by improving our grip on the world, and it is through this process of interaction that we assemble an identity and constitute our selves as social actors (Berger and Luckmann 1966; Dunn 1997: 695; Beckert 2002: 252; Whitford 2002: 345). Through institutions, we build up skills and capacities that allow us to navigate social life (Berk and Galvan 2009: 544). Such socialization does not necessarily entail a rigidification of agency: The development of useful habits is in fact crucial to the development of problem-solving capacities, the bricolage-like process whereby subjects recombine existing structures to expand their range of options (Berger and Luckmann 1966: 53; Dalton 2004: 604–5; Berk and Galvan 2009: 555; Engelen et al. 2010). Institutions, then, often have enabling effects (Herrigel 2010), fostering rather than constraining people's strategic and creative capacities.

That is, of course, not to deny that institutions also have constraining effects. But what a perspective centered on the interaction of practices permits us to see is that the absence of strategic flexibility is not an effect of institutional forms in and of themselves but stems from the operation of social power differentials: The growing capacity for innovative, problem-solving agency and the contracting room for maneuver available to other actors represent obverse sides of the same process of social construction (Knafo 2010). Such inequalities are organized around, yet not fully reflected in, institutions, which never exhaust the complex dynamics of human interaction (Holzman 1996; Novak 2008: 764). This element of misrepresentation is crucial to the functioning of institutions because it diverts attention from patterns of control and so promotes legitimacy (Eagleton 1991). The mediation of social connections by institutions thus facilitates the operation of power on a more systematic, structural basis than would ever be possible if control were only ever exercised directly and visibly (Lukes 1974; Roy 1997: 13). Institutions leverage particular agencies, extending their reach over wider tracts of social life.

The leveraging of the agency of some over that of others expresses itself as a process whereby institutional configurations acquire a certain degree of coherence and identity, creating a discursive context where we can meaningfully talk about organizational forms (e.g., the Treasury) as possessing agency and capacities. This context sets the stage for subsequent interactions: Elite actors' privileged access to institutional mechanisms of control allows them to play a dominant role in shaping the development of social life (Savage and Williams 2008). As a consequence, inequality often has a cumulative character: Social constructions tend to become layered, with new ones built on top of existing ones, thus allowing power to sink more deeply into the basic modalities of social life and to take on more structural qualities. What this amounts to is a picture of society as a pyramidal constellation of institutional mechanisms, where interaction channeled through the forms of everyday life results in the creation of networks of structural power that form the basis for the construction and legitimation of higher-level institutions (Abrams 1977). It is through these processes that public authority is constructed: Statehood, as the public sanctioning of relations of control, can be found at all levels of social life. The official state, rather than being a substantive entity in and of itself with merely external connections to the social realm, sits at the pinnacle of this constellation (Bratsis 2006), deriving capacity and leverage from its linkages to social institutions. We need a conception of the "integral state" (Gramsci 1971), that is, an understanding of power that does not confine its view to the institutions of the formal state but examines its internal connections to processes situated at different levels of social life.

It bears emphasizing that this process of hegemonic socialization is only poorly captured through concepts such as "entrenchment" or "stabilization." The dynamics of human interaction do not slow down or become less complex: The layering of social constructions is not a result of gradual, default accretion but occurs through ongoing strategic adjustments. At no point does the pragmatic disposition give way to a lifeless submission to norms, and as actors exploit the leeway available to them, they generate new interdependencies that existing institutions do not afford much grip on (i.e., new contradictions and problems that put pressure on the integrative capacity of existing institutions). In such situations, elite actors can often avail themselves of considerable latitude pursuing reforms aimed at institutionalizing the new social effects in ways that are consistent with existing mechanisms of structural power. Thus, the construction of the integral state involves a dynamic process of continuous institutional adaptation and elaboration through which dominant actors build their capacities vis-à-vis subordinate actors.

In capitalist societies, the integral state expands dramatically. The modern polity, organized on principles of legal equality (Wood 1995), can tap into sources of legitimacy that were not available to more traditional forms of rule. It is precisely this projection of neutrality that permits power relations to become layered to an unprecedented extent and life in modern society to become shot through with institutional rules and norms (Mitchell 2005), resulting in the build-up of an elaborate, intricately interconnected constellation of control mechanisms. In this way, the modern state comes to have access to what Mann (1984: 189; 1993: 59) has called "infrastructural power," that is, a capacity to implement projects through a social sphere characterized by a high degree of connectivity. Compared to more traditional forms of rule, infrastructural power is indirect, diffuse, and crucially dependent on the kind of legitimacy that secures cooperation (Calhoun 1992). The capacity of the modern state can be highest when it is organically allied to social networks of control and leveraged by an infrastructure of lower-level institutions and norms (Mann 1993; Ansell 2000; Hobson 2000; Novak 2008; Bell and Hindmoor 2009; Konings 2010).

However, modern power is a contradictory affair: The proliferation of institutional forms in social life lays the foundations for, but does not automatically translate into, a higher degree of effective political capacity. Because structural power relations are constituted through the limits on more direct forms of authority and regulation, the immediate effect of their expansion is often precisely to complicate and jeopardize existing institutional capacities. The mediated nature and complexity of modern power means that its operation is often not transparent to its participants, making it difficult to wield even for those who are positioned favorably in its networks and derive a great deal of leverage from them. Dominant actors are likely to have considerable strategic leeway and room for experimentation, but they are not above the contradictions and confusions of power: They must still fumble around for the right switches and levers and learn how to manipulate them (i.e., work their way, through trial and error, toward the more subtle skills required for the navigation of indirect social relations).

This conceptual framework permits us a new vantage point from which to examine the dynamics of capitalist development. The systemic logic and expansionary qualities of capitalist markets arise through processes of institutional construction that establish the conditions for more far-reaching, structural forms of control over the dynamics of social interaction; but these complex patterns of new connections generate their own problems, which have to be maneuvered, negotiated, and managed. The tensions that characterize capitalist development, therefore, are not best seen in terms of the clash of an economic market logic with its institutional surroundings but should be viewed as contradictions internal to the processes whereby our practices become institutionalized and modalities of control are built. Whereas IPE has typically taken the financial instability of the modern era as evidence for the idea that capitalist markets tend to destroy institutional capacities for the coordination of socioeconomic life, this book interprets the tensions faced by the modern American state as inherent aspects of the processes through which financial power develops, reflective of the difficulties involved in navigating indirect modalities of power and managing increasingly complex and interwoven networks of social relations. Thus, the narrative laid out in this book traces how institutional innovations create mechanisms of control and so enhance the structural basis of political authority yet how, at the same time, the creation of such indirect power relations is responsible for new contradictions and challenges that need to be handled and negotiated and prompt further institutional reform and innovation.[1]

[1] The primary objective of this book is to elucidate the nature of modern financial power through an engagement with political economy themes; it does not aim to contribute to the rich literature on American political development. But because I will draw on this literature to place the analysis of finance in its historical and social context (and will do so without explicit consideration of the many important issues that it raises), it seems appropriate to briefly situate the approach adopted in this book with respect to the main conceptual perspectives employed in that field (for an overview, see Orren and Skowronek 2004). The modern study of American political development is dominated

THE DEVELOPMENT OF AMERICAN FINANCE: TOWARD A NEW INTERPRETATION

The rest of this chapter offers an outline of the interpretation of American financial development that this book presents, giving an overview of the central arguments concerning the sources of U.S. financial power and highlighting the respects in which the narrative differs from the conventional account. We begin this outline by drawing attention to a sense in which modern finance can be said to be "American" that is generally not sufficiently appreciated. The IPE literature typically locates the origins of modern-day financial markets in the breakdown of the Bretton Woods system in the early 1970s – and it views the dynamics that resulted as an amplified reemergence of the liberal financial structures that prevailed under British hegemony. This book advances a different perspective: It traces the origins of the financial practices and relations that have shaped financial life over the past decades back to the transformation of the American financial system from the late nineteenth century. The direct descendants of the distinctly American institutional forms that emerged in that context would profoundly shape the nature of present-day finance.

Chapters 2 and 3 are devoted to sketching the contours of the pre–Civil War financial landscape out of which those new institutions would arise. One key objective here is to question the usefulness of taking the notion of a liberal market economy as a conceptual starting point. This is

by perspectives that place a great deal of emphasis on the autonomy of the institutional structures of the state. This institutionalist turn, led by authors such as Skowronek (1982) and Skocpol (1979, 1985), was motivated by a concern that overly society-centered approaches – which include views of American history as governed by a consensual culture of classical Lockean liberalism (e.g., Boorstin 1953; Hartz 1955) as well as the New Left's rediscovery of social conflict (e.g., Countryman 1967; Domhoff 1967; Bernstein 1968; Weinstein 1968; Henretta 1974, 1979; Gutman 1976; Nash 1976; Clark 1990, 2002) – tend to give short shrift to the constitutive role of institutions and to assume that the institutional level is a somewhat passive manifestation of social life. The literature that has emerged from the institutionalist turn tends to analyze the process of state building in terms of the internally generated dynamics and expansion of bureaucratic structures and executive agencies (e.g., Finegold and Skocpol 1995; John 1997; Carpenter 2001). Although many authors seem to acknowledge that especially Skocpol's (1985) criticism of society-centered approaches might have bent the stick too far in the other direction and emphasize the mutual interaction between state and society (e.g., Bensel 1990, 2000; Orren 1991; Sanders 1999), even they tend to work with an overly narrow conception of political authority and state capacity, which are seen to derive primarily from the state's internal cohesion and organizational integration. In recent years, several authors (e.g., King and Lieberman 2007; Novak 2008) have argued for the need to look behind the state's formal framework and to conceptualize the constitution of its infrastructural capacities through its institutional linkages with social life.

important particularly because – contrary to the idea that the U.S. financial system should be comprehended as an instance of the Anglo-Saxon market-based model – the United States did not follow in the tracks of financial modernization laid down by Britain. The highly dynamic and liquid financial system that emerged during the late nineteenth century did not represent a variation on a general model of liberal finance but can only be understood as a complex and highly specific historical construction, driven by its own institutional logic. That construction emerged out of a pre–Civil War system that had greatly limited financial integration and the infrastructural mechanisms that elites and public authorities could deploy. Although many of the elements of British finance were transported to the New World, for various reasons early America did not reproduce the systemic dynamics of British finance. In particular, the absence of a nationwide market for well-secured short-term obligations made the American banking system consistently illiquid and crisis-prone. Political strife, in which agrarian interests played a key role, time and again thwarted attempts to construct a more integrated financial system.

During the last decades of the nineteenth century, this fragmented financial structure prompted the development of practices and strategies that set American finance on a qualitatively new path, giving rise to a system that was much more dynamic, expansionary, and integrative than the British system had ever been. Chapter 4, covering the postbellum era, traces the emerging contours of this new system of financial intermediation. Central to this account is the fact that, as banks' need for liquidity intensified, they responded by pioneering a distinctive form of "financial banking" (Youngman 1906: 435) based on the investment of funds in the stock market and associated speculative markets. American banks' ability to practice securitization *avant la lettre* had major consequences. The development of these new financial networks meant that financial elites were able to leverage their stock market dealings with the savings of ordinary Americans. In addition, banks' newfound access to liquidity meant that they were now in a much better position to create liquidity and extend credit for a variety of purposes.

The emergence of this much more expansionary institutional basis gave a highly significant twist to the role of finance in American society. Whereas throughout the nineteenth century the relationship between financial institutions and the American lower classes had been fraught with antagonism, the new framework was capable of integrating a wide variety of popular interests and ambitions. Consequently, the period saw the rapid proliferation of institutional connections between the realm of high finance and everyday life. Moreover, this dramatic financial growth did not occur through a retreat of the state but precisely through the expansion of public and civic authority. These observations point toward a portrayal of the late nineteenth and early twentieth centuries that differs in key respects from the conventional characterization of this period as the classic age of liberal high finance. Chapter 5 examines the contradiction-ridden expansion of these new networks of financial power. The foundation of the Federal Reserve system in 1913 was a response to recurrent crises brought on by the sudden evaporation of market liquidity. But as it left fully intact the web of techniques and connections that stood at the basis of America's distinctive pattern of financial expansion, the presence of a lender of last resort served to fuel rather than dampen the unstable growth of new forms of credit. The systemic risks entailed by America's trajectory of financial growth were recognized only when it was too late.

The Crash and the Great Depression affected not just the United States but also the world at large. IPE interpretations of the interwar period revolve around the idea that the forces of instability could have such dramatic global consequences because of America's irresponsible foreign policies. According to this perspective, after World War I the United States had replaced Britain as the world's preeminent financial power, yet its politics and policies remained mired in myopic unilateralism and failed to provide the international economy with stabilizing institutional foundations. Chapter 6 argues that this interpretation relies too much on a cyclical model of capitalist history, which sees hegemonic powers as successively taking responsibility for the reproduction of the international market economy. The United States' inability to stabilize the dynamics of its financial system was a significant factor in the making of the global economic depression of the 1930s, but this is not best understood in terms of America's failure to discern its true hegemonic interests. America's financial interest in the world was simply still relatively limited: The challenge to Britain's position in international finance resulted from the intergovernmental debts incurred by European countries during World War I and the dollar's growing role as a reserve currency, but an infrastructure of dollar-centered private credit relations linking American finance to the international economy in an organic way remained largely absent. When, decades later, a dense web of connections between American finance and the world economy developed, its operational mechanisms reflected not an abstract image of liberal world order but rather the specific institutional mechanisms that American finance had developed at home.