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ORGANIZATIONS

# MARKETS *on* TRIAL

The Economic Sociology of  
the US Financial Crisis

Michael Lounsbury • Paul M. Hirsch

RESEARCH IN THE SOCIOLOGY OF ORGANIZATIONS  
VOLUME 30

# MARKETS ON TRIAL: THE ECONOMIC SOCIOLOGY OF THE U.S. FINANCIAL CRISIS

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# INTRODUCTION





# MARKETS ON TRIAL: TOWARD A POLICY-ORIENTED ECONOMIC SOCIOLOGY

Michael Lounsbury and Paul M. Hirsch

Market failures often have devastating societal effects, and the more dramatic and widespread they are, the more ideologies and policies underlying them require critical scrutiny (Polanyi, 1944). Similar to the 1929 stock market crash and Great Depression, events in the early 21st century have created heightened uncertainty and ambiguity, as well as efforts to reevaluate received wisdom. Over the past three decades, neoclassical models of the Chicago and Austrian Schools of free market economics infused and guided U.S. government policy and enforcement, leading to severe cut backs in regulation of the banking and investment industries. Although these ideas and practices also spread around the world, the United States provided the beacon. Wall Street became the *wild west* with repeated market bubbles and collapses, culminating in the so-called *Great Recession*, ushered in by the subprime meltdown in 2008 and concomitant global financial collapse. During the aftermath of the most recent debacle, Federal Reserve Chairman Alan Greenspan admitted, “Those of us who have looked to the self-interest of lending institutions to protect shareholders’ equity, myself included, are in a state of shocked disbelief” (*New York Times*, October 24, 2008). After the housing bubble burst in 2008, Greenspan acknowledged a “flaw in the model that

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I perceived is the critical functioning structure that defines how the world works” (*PBS News Hour*, October 23, 2008).

Such remarkable confessions should give pause to those continuing to promulgate the neoliberal agenda. For social scientists, the *Great Recession* has invited and opened up the possibility for a wider array of conceptualizations and approaches to financial markets. And given that free market approaches rooted in neoclassical microeconomics have garnered increased scrutiny in recent years, the current global calamity provides even greater impetus for the flowering of alternative perspectives on the economy from both within and outside of the economics discipline. The development of paradigmatic variants from within economics has included the expansion of institutional economics (North, 1990; Williamson, 2000), the embrace of richer approaches to the psychology of individuals via behavioral economics (e.g., Akerlof & Shiller, 2009), as well as the revitalization of macroeconomics, which includes a revival of (albeit modified) Keynesianism (e.g., Hayes, 2008). In contradistinction to these *heretical* movements from within, this volume focuses attention on the contributions of a powerful, ascendant paradigm that has emerged outside of the economics discipline – economic sociology. Our aims are to demonstrate the fruitfulness of economic sociology as a lens to explore the financial crisis and address key architectural and policy issues regarding the financial system, as well as advocate for the development of a more policy-oriented economic sociology.

Economic sociology is an international field that is diverse and rapidly growing. It differs from free market and other variants of economic theory in several fundamental ways (e.g., Block, 1990). A key difference is that most economic models rely on an assumption of human rationality that is very narrowly conceived. Economic sociologists challenge this by highlighting how rationality is socially constructed and culturally contingent (e.g., Fligstein, 1990; Dobbin, 1994; Hamilton & Biggart, 1988). In addition, instead of employing a taken-for-granted understanding of markets as sites for calculating economic actors, economic sociologists have questioned universalistic notions of markets and their inherent efficiency, taking a more critical and empirically grounded approach to assessment of their broader architecture and dynamics (see especially Fligstein, 2001).

Economic sociologists point to the importance of taking better account of such critical factors as power, national context, the state, regulators, culture, and social networks. Economists tend to ignore how economic action is fundamentally interpenetrated with such wider concerns (Swedberg, 1994; Granovetter, 1985). Although the intellectual roots of economic sociology