Rush to develop stock markets has huge downside

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France had the first one back in the 12th century. In 1980, less than 60 existed worldwide. But since then, the number had doubled.

Stock markets, once a way to manage debt and create capital for companies, have seemingly become a status symbol for some nations, or are used as a means for countries to access international funds for development.

But Michael Lounsbury, in the University of Alberta's School of Business, argues that the global rush to develop modern financial institutions-including stock markets-has had a huge downside.

Lounsbury says that, in many cases, especially since the fall of the Soviet Union, there has been an inexorable push to create markets, where they, or even countries for that matter, did not previously exist. While the creation of these markets in many underdeveloped countries has not necessarily contributed to the global economic crisis, their creation and the accompanying development of other market institutions did likely contribute to the recent global financial crisis.

"In countries like the Czech Republic, for example, there was a strong need to not only create a stock-market apparatus but also to employ certain kinds of policies that mimicked U.S. economic policies, which often did not fit their societal context," said Lounsbury. "The result has been disastrous for some countries."

Lounsbury cites the example of the fall of the Soviet empire and the rush by American experts to try to "capitalize" Russia. He says American economists "parachuted" into Russia, armed with plans and policies dictated by institutions like the International Monetary Fund. Under their direction, former state-controlled industries were privatized and ownership spread around the state to citizens in the form of stocks.

"Most of these newly privatized companies were taken over by mafia-like organizations that ran things like oligarchs," said Lounsbury. "Russia did not have a foundation to become a U.S.-style market economy."

Lounsbury also decries the purely symbolic development of markets. He notes that these markets are created for the sake of appearance, in order for the governments of these countries to access funds from groups such as the IMF or the World Bank to support their social policies. Lounsbury notes that such approaches often do little to foster real economic growth and development.

"In many cases, these markets serve no important function in the societies or economies of these countries," said Lounsbury. "The vast majority of stock markets have little substantive trading activity or infrastructure to support the use of a stock market to propel economic growth and development."

Lounsbury, who favours socio-economic approaches to markets, notes that the latest financial crisis has enabled new conversations about approaches to markets that account for substantive social welfare concerns, and such a shift in policy is a positive step that would serve to address many inequalities found in society. While some may cringe at the idea of more government involvement in markets, he says that more government-instilled policies are necessary to build a stable economy and a stable, equitable and productive society, as well as to prevent financial crises from having such a massive impact on all segments of society.

"The economy should be conceptualized more as an appendage to the society that we want, not as a kind of unfettered dictator that unravels society," said Lounsbury. "If the financial crisis taught us anything, it's important to have rules and oversight; you can't just have a market take away all the rules and let it run amok."

Provided by University of Alberta