Financial Markets and Organization Theory
Submission for a “Professional Development Workshop” (PDW)

Primary sponsor: OMT
Other sponsors: CMS and SIM

Organizers: Daniel Beunza and Emilio Marti
Presenters: Mary Benner, Paula Jarzabkowski and Marc Schneiberg

Abstract
Organization theorists are well placed to make a distinct contribution to our understanding of financial markets because financial markets are made up of organizations—whether in the form of banks, stock exchanges, or hedge funds—and because financial markets affect organizations such as publicly traded companies. Specifically, organization theorists can illuminate (a) the social construction of market prices, (b) how financial markets influence corporate behavior, and (c) the priorities and struggles in financial regulation. The proposed PDW seeks to address these topics and establish an annual platform for organization theorists with an interest in financial markets. In the first hour, three leading organizational scholars will present their work on financial markets; in the second hour, the presenters and organizers will give feedback to junior scholars as part of a paper development workshop.
Analyzing financial markets from a management theory perspective

Since the 2008 financial crisis, organization theorists have become more interested in financial markets, as highlighted by the edited volume “Markets on Trial” (Lounsbury & Hirsch, 2010). Indeed, organization theorists can make a distinct contribution to our understanding of finance because financial markets are made up of organizations—from banks and stock exchanges to hedge funds—and because financial markets affect organizations such as publicly traded companies (Beunza & Millo, 2014; Davis, 2009; Marti & Scherer, 2016; Munir, 2011). Specifically, theories and methods from organization theory can help illuminate (a) the social construction of market prices, (b) how financial markets influence corporate behavior, and (c) the priorities and struggles in financial regulation, as we now explain.

a. The social construction of market prices

Financial economists tend to assume that liquidity and market prices emerges automatically wherever there is supply and demand for a security (Carruthers & Stinchcombe, 1999). By contrast, organization theorists see financial markets as socially constructed (Abolafia, 1996). In their view, liquidity will only emerge if market participants have a shared understanding of the securities that they are trading (Carruthers & Stinchcombe, 1999) and if market participants engage in sensemaking (Beunza & Millo, 2014). Likewise, while financial economists take market prices for granted (as the best existing estimate of value), organization theorists see market prices as resulting from shared imperfect valuation practices and routinized interactions (Beunza & Garud, 2007; Jarzabkowski, Bednarek, & Spee, 2015; Zuckerman, 2004).

Studying the social construction of financial markets is particularly important to understand when and why this construction process may fail. The unraveling of financial markets can have severe macroeconomic consequences, as the 2008 financial crisis has shown (Fligstein & Goldstein, 2010, 2015; Lounsbury & Hirsch, 2010). Studying financial innovations offers a promising way to understand why the social construction of markets may fail. For example, Beunza et al. (2011) explore high-frequency trading, which involves algorithms that trade in a fully automated way. These authors warn that, compared to human market participants, the secret
algorithms of high-frequency traders produce fewer social cues. In turbulent market conditions, market participants will have a worse sense of what other market participants are doing; high-frequency trading may thereby contribute to breakdown in sensemaking.

b. *How financial markets influence corporate behavior*

Organization theorists are also in an excellent position to study how financial markets influence corporate behavior. Increasing shareholder pressure (Davis, 2009) and the increased influence of securities analysts (Benner & Ranganathan, 2013) have forced corporations to align their business decisions with expectations from financial markets. As a consequence, CEOs with a finance background have become a widespread phenomenon (Fligstein, 1990), CFO are now part of the top management teams (Zorn, 2004), and corporation rely increasingly on financial activities to increase their profits, such as with car leasing (Lin & Tomaskovic-Devey, 2013).

Organization theorists can explore the strategies that shareholders use to exert the aforementioned pressures on corporations. Cobb (2015) has demonstrated that the presence of active and short-term shareholders made it more likely that US corporations switch to less employee-friendly pension plans. The emergence of socially responsible investing offers another promising area for future research. For example, researchers could explore the effect of divestment activities, such as the recent “carbon bubble” divestment campaign of environmental NGOs that targets fossil fuel companies (McKibben, 2012). This divestment campaign has gained followers among university endowments, churches and some pension funds, but it remains unclear whether more mainstream investors—such as mutual funds—will join it.

Organization theorists can also study how corporations deal with pressure from financial markets. Specifically, researchers can study how financial pressure influences the relative bargaining power of executive versus non-executive employees (Marti & Scherer, 2016; Shin, 2014). Goldstein (2012) has shown that shareholders depend on top management for cost-cutting that will increase shareholder value (at least in the short-term). Due to this dependence, increasing shareholder pressure will likely bolster the bargaining power of top management, while undermining the bargaining power of non-executive stakeholders (Goldstein, 2012).
c. Priorities and struggles in financial regulation

Organization theorists can furthermore analyze financial regulation. Current research on financial regulation comes mostly from economists (e.g., Admati & Hellwig, 2013; Cooley & Walter, 2010; French et al., 2010; Scholes, 2010). Organizational research can go beyond economic research, for example, by exploring the role of financial innovations in financial regulation. Funk and Hirschman (2014) find that ambiguous financial innovations allowed elite actors to undermine the Glass-Steagall regulation, thus undermining the separation of commercial and investment banking. Organization theorists can also explore the discursive dynamics of financial regulation. Riaz, Buchanan, and Bapuji (2011) find that bankers appeal to their expert authority and divert blame by blaming others. Tourish and Hargie (2012: 1045) find that when explaining the failure of their banks, bank executives use metaphors that “minimize learning from failure.”

Organization theorists can also explore alternative approaches to the current financial regulation. Schneiberg and Bartley criticize that current regulation represents “a remarkably narrow vision of what regulation is and does” (2010: 282). Based on the insight that regulation constitutes markets, Schneiberg and Bartley argue that financial regulation should go “beyond a discourse of ‘intervention’ to consider a far-reaching restructuring of financial markets” (2010: 301). Similarly, Marti and Scherer (2016) criticize current regulation as technocratic, and outline ways in which a more inclusive approach to financial innovation could involve different societal groups into the regulatory process. These authors propose “deliberative polls” (Fishkin, 2009), in which a random sample of citizens would discuss a controversial issue of financial regulation together with experts for some days.

Abstracts of the presentations

a. Mary Benner: Securities analysts’ challenges and the locus of novelty, innovation, and valuable strategies

Prior research has documented a variety of situations where analysts may be challenged. For example, Zuckerman (1999, 2000) documents that when firms’ strategies did not clearly fit within an industry category covered by analysts, or straddled the boundaries of analysts’ existing
categories, it was more difficult for firms to gain analyst coverage. Benner (2010) documented that analysts are also challenged and less effective as intermediaries when firms’ strategies are novel or unique, or when firms undergo radical technological changes that fundamentally change strategies and how firms are valued (see also Benner & Ranganathan, 2012; Litov, Moreton, & Zenger, 2012). Yet at the same time, strategy research highlights the importance of novelty, uniqueness and complexity for value creation (i.e. the most valuable strategies are likely to be novel, unique or complex) as those are the strategies that are most likely to be differentiated from competitors and difficult to imitate. Benner & Zenger (2015) describe these issues and note the potential for a ‘lemons’ discount for particular types of strategies, arising in part from the difficulties analysts face as market intermediaries when firms’ strategies and actions are costly to analyze. It may be that the discounts associated with strategies that are novel, unique, or complex and otherwise valuable – but costly for analysts to evaluate – make such potentially valuable strategies increasingly difficult for publicly traded firms to pursue. These discounts suggest that there will be pressures for difficult-to-evaluate strategies to migrate to private equity or to firms funded by sophisticated ‘growth’ investors with longer-term investment horizons, who have the ability to understand strategies and reduce information asymmetries.

b. Paula Jarzabkowski: A relational framework for examining the distributed functioning of global financial markets
This presentation theorizes how the global market for reinsurance, which trades in the cover for devastating economic losses, such as those arising from hurricanes, earthquakes, and terrorist attacks, functions. Such risks are highly unpredictable and uniquely tailored, making them difficult to model and price in standardized ways. Despite lack of a common pricing model or standardized electronic platform, trading of these risks is highly distributed across multiple organizations around the globe. For example, risks originating in companies in Japan or Thailand may be shared amongst different reinsurers in key financial centers around the world. When triggered by a disaster, these same risks may occasion losses to companies anywhere in the world, as insured global supply chains are disrupted. The market that has developed to trade these
risks is founded on a complex web of distributed knowledge-based practices and trading relationships (e.g. Knorr Cetina, 1999; MacKenzie, 2011). Yet organization theory has provided few theoretical resources for understanding the distributed, interdependent practices of such markets (see also Beunza & Stark, 2012). Existing theories tend to focus on field-level institutions that shape market practice (e.g. Abolafia & Kilduff, 1988), market embeddedness in networks of social relationships (e.g. Baker, 1984; Granovetter, 1985), or mediation via electronic trading platforms (e.g. Knorr Cetina & Bruegger, 2002). This presentation draws from a 3-year ethnographic study of the global reinsurance market, conducted with some 60 firms in 17 countries, to develop a relational theory of the interdependent inter-organizational practices within which distributed markets function. This theoretical framework allows organizations theorists to address new questions about financial markets including the potential systemic threats arising from globally distributed practices.

c. Marc Schneiberg: Organizational structure in American banking and its effects on local economies during the Great Recession

Organizational scholars interested in finance focus, with good reason, on the social structures of trading rooms, the transformation of giant, money center banks, and the shift from traditional to market-based banking grounded in securitization, derivatives transactions and the high volume production new financial instruments. Yet in their haste to identify new organizational tendencies, scholars have attended less, if at all, to the role that traditional, cooperative and community based bank organizations can play in buffering communities and local economies from crisis, potentially fostering resilience and renewal even in this neoliberal era. To address this neglect, I use new datasets on the ecologies of banking organizations in the US to document the continued importance of community banks and credit unions within local economies from 2007 through 2013. These are financial institutions that are grounded in “Jeffersonian” logics of community, relational banking, economic autonomy and local self-governance. They provide small businesses, consumers and communities in many places with access to banking enterprises that are geared toward the substantive interests of consumers and communities rather than the
one-sided pursuit of shareholder value. I then consider the effects of these alternatives on local economies and communities in the US during the Great Recession, presenting preliminary results from an ongoing study of banking structure effects on some specific outcomes: new establishment formations, the size and growth of the small business sector, income inequality, and the surge and recovery of unemployment from 2006 to 2013. Such ecologies of alternatives have served and might continue to serve as platforms for more decentralized, small stakeholder capitalisms of independent producers, prosperous working classes and vibrant communities.

Relevance for the sponsors

a. Relevance for main sponsor: OMT

We hope to have shown that by studying financial markets, organization theorists address “questions worth answering” (Davis, 2015: 314): from questions related to the stability of financial markets, to questions about how shareholders shape the priorities of corporations, and to question around increasing income inequality. We thus see the emerging field of organization theory research on financial markets primarily as “problem-driven work” (Davis & Marquis, 2005: 335) that addresses key societal issues. At the same time, the fact that organizational research on financial markets gets published in major journals—such as Academy of Management Review (Marti & Scherer, 2016), Administrative Science Quarterly (Funk & Hirschman, 2014), or Organization Science (Cobb, 2015)—suggests that this research is also theoretically relevant.

b. Relevance for other sponsors: CMS and SIM

There has also been a rising interest in financial markets in CMS. For example, De Cock and Nyberg (2014) and Erturk et al. (2010) have recently studied private equity firms; Glynos et al. (2012), Froud et al. (2010), and Riaz et al. (2016) explore the financial crisis; Veldman and Willmott (2015) explore the rise of a financialized approach to corporate governance. Our PDW gives these researchers a platform to meet and exchange ideas on how to foster critical organization theory research on financial markets. Within the SIM division, researchers have started to explore how corporate social responsibility (CSR) is possible in a financialized
economy. For example, Jones and Nisbet (2011) find that pressure from financial markets narrows down CSR to exercise that benefit consumers and investors, while employees and communities can hardly expect to benefit from CSR activities. Our PDW highlights the rising importance of financial markets as an understudied factor that influences CSR.

**Format of the PDW**

The PDW will have two parts. In the first, which will not require registration, three leading organization theory scholars will present their research on financial markets. In addition, the organizers will give a short overview on the emerging research field of organizational research on financial markets and offer some concluding remarks. In the second part, the PDW gives researchers who work on financial markets the opportunity to receive feedback on their work. To participate in the second part, researchers will have to submit a short paper (of up to 10 pages) to the organizers by July 15, 2016. We will select up to 10 short papers to create up to five roundtables with the presenters and organizers. The total duration of the PDW will be 120 minutes. The following table illustrates the schedule. After that, we present the abstract for each of the three presentations in their order of appearance.

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<thead>
<tr>
<th>Content</th>
<th>Time (minutes)</th>
<th>Presenter</th>
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<tbody>
<tr>
<td>Introduction: An overview over organizational research on financial markets</td>
<td>10’</td>
<td>Emilio Marti (Cass Business School, City University London)</td>
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<tr>
<td>Presentation 1: Securities analysts’ challenges and the locus of novelty, innovation, and valuable strategies</td>
<td>10’ presentation &amp; 5’ Q&amp;A</td>
<td>Mary Benner (Carlson School of Management, University of Minnesota)</td>
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<tr>
<td>Presentation 2: A relational framework for examining the distributed functioning of global financial markets</td>
<td>10’ presentation &amp; 5’ Q&amp;A</td>
<td>Paula Jarzabkowski (Cass Business School, City University London)</td>
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<tr>
<td>Presentation 3: Organizational structure in American banking and its effects on local economies during the Great Recession</td>
<td>10’ presentation &amp; 5’ Q&amp;A</td>
<td>Marc Schneiberg (Department of Sociology, Reed College)</td>
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<tr>
<td>Concluding remarks</td>
<td>10’</td>
<td>Daniel Beunza (Department of Management, London School of Economics)</td>
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<td>Break to clear the room for the registration-only second part (10 minutes)</td>
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<tr>
<td>Paper development roundtables with the presenters and organizers</td>
<td>45’</td>
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**Total length (including break): 120 minutes**
Short biographies

a. Organizers

Daniel Beunza is an Assistant Professor of Management at the London School of Economics (LSE). His research in sociology explores the ways in which social relations and technology shape financial value. Specifically, his research focuses on financial analysts, algorithmic trading, and shareholder engagement. His articles are part of an emerging literature known as the “social studies of finance” and have been published in journals such as *Industrial and Corporate Change, Organization Studies* and *Socio-Economic Review*. Daniel obtained his PhD from New York University and taught at Columbia Business School in New York City before joining LSE.

Emilio Marti is currently a visiting scholar at Cass Business School (City University London) on a scholarship from the Swiss National Science Foundation. His research interests include corporate social responsibility, financial innovations, financial regulation, performativity, and socially responsible investing. He won the “Best Dissertation Award” from the Society for Business Ethics for his dissertation, which he received from the University of Zurich in February 2015. One of his papers is forthcoming in the *Academy of Management Review* and another has been conditionally accepted in the *Journal of Management Studies*.

b. Presenters

Mary Benner is an associate professor in the Strategic Management and Entrepreneurship Department of the Carlson School of Management, University of Minnesota. Her research at the intersection of organization theory and strategic management explores how firms innovate and adapt to technological change. She has studied the effects of systematic process management practices such as ISO 9000 and Six Sigma on firms’ innovation and responses to new technologies, and is currently examining the influence of financial markets and securities analysts in how established firms adapt to technological change. Her research is published in leading academic journals and has won several awards. She is an Associate Editor at *Administrative Science Quarterly* and was previously a Senior Editor at *Organization Science*. 
Paula Jarzabkowski is a Professor of Strategic Management at Cass Business School, City University London. Her research focuses on strategy-as-practice in complex contexts, such as regulated firms, third sector organizations and financial services, particularly insurance and reinsurance. Her research in this regard has been foundational in the establishment of the field of strategy-as-practice. Her work has appeared in a number of leading journals including *Academy of Management Journal, Organization Science, Strategic Management Journal, Journal of Management Studies* and *Organization Studies*. Paula has just released a new book, entitled “Making a Market for Acts of God: The Practice of Risk-Trading in the Global Reinsurance Industry” based on her 3-year ethnographic study of the industry.

Marc Schneiberg is the John C. Pock Professor of Sociology at Reed College. He is an economic and organizational sociologist who researches the rise, contemporary fates, and economic consequences of organizational diversity and alternatives to giant, shareholder corporations in American capitalism. This work addresses both the evolution of cooperative and other alternative enterprise systems in the US, including electrical and agricultural cooperatives, insurance mutuals, community banks, and credit unions, and how the emergence of such enterprises can help upgrade markets, regulate corporations, and foster more decentralized and small stakeholder trajectories of capitalist development. Schneiberg also studies association, regulation and self-regulation in American manufacturing and finance. He is Editor of *Socio-Economic Review*, and Consulting Editor of *Sociological Science*. 
References


