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Article

A Fetish and Fiction of Finance: Unraveling the Subprime Crisis

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Abstract

As the moderately strengthened financial regulation of Basel III comes into effect over the next seven years, this article sets out a cautionary reminder as to why regulation needs to move beyond a focus on the mitigation and distribution of risk. To do so, the article unravels the much-misunderstood experiences of eight Norwegian municipalities whose investments plummeted as the subprime crisis unfolded: investments that had no immediate ties to subprime mortgage lending or mortgage-backed securities. Focusing on the processes, practices, and instruments of financialization, the article puts forward two new analytical concepts—“the fetishization of the knowledge of risk” and “fictitious distance”—to help explain how the crisis spread so quickly and extensively that it threatened not only the municipalities’ investments but also the functioning of global finance as a whole. In so doing, it becomes clear that financialization has set a far more risky form of capitalism that is manifest through

concrete economic geographies, from towns and cities in the United States to "distant" Norwegian municipalities. In the highly interconnected entanglement of geographies and finance that make up the global financial system, the fetishes and fictions of finance cannot be ignored.

Keywords:

financialization securitization risk subprime crisis fictions of finance financial regulation

Notes

1 Our thanks to Francis Longstaff for his feedback on the magnification of losses across connected structured instruments. See also IMF (2008, Box 2.2) for a useful analysis.

2 Haugesund was a plaintiff only in the court case against DEPFA Bank, not in the case against Citigroup.

3 TOBs carry a "put option" that allows the lender to ask for his or her capital back at par value at any reset date. The floating rate certificate is the borrower's promise to repay both the interest and capital to the lender. This option effectively protects the lender from value fluctuations of the bond, and risk is, therefore, carried by the borrower.