



---

## Implications of Institutional Dispositions of Neoliberalism

Slobodan Lacic<sup>1</sup>, Mimo Draskovic<sup>2</sup>

<sup>1</sup> Associate Professor, Faculty of Economics, University of Montenegro, Podgorica, e-mail: [sasalacic@mail.com](mailto:sasalacic@mail.com)

<sup>2</sup> Assistant Professor, Maritime Faculty of Kotor, University of Montenegro, Kotor, e-mail: [rookie@t-com.me](mailto:rookie@t-com.me)

---

### ARTICLE INFO

Received May 27, 2015  
Received in revised form Oct. 27, 2015  
Accepted December 01, 2015  
Available online Dec. 03, 2015

**JEL classification:**  
E42; E52

**DOI:**  
10.14254/1800-5845.2015/11-2/7

**Keywords:**  
Neoliberalism,  
Banks,  
Interest rates,  
Monetary policy,  
Derivatives,  
High frequency trading

---

### ABSTRACT

This analysis starts with an assumption that vertical paradigm of neoliberalism positions the state regulation only as a formal center of power, and that non-state institutions (mainly banks) acquire de facto economic and political leverage over the state. Here is a definitive break with the liberal horizontal paradigm (order). State institutions coordinate the vertical system and mediate between the individual institutional pillars. Standard of price setting is determined by oligopolistic and monopolistic prices. In this document, we test the hypothesis in the case of dominating the instruments of the "market" institutions in relation to the regulatory instruments and inefficiently modeled financial markets over the entire financial system, i.e. privileged institutions over the state authority. Specifically, we prove the domination of the market interest rates over the official interest rates, modification of the protective and destructive corporate pattern "too big to fail", as well as aggressive manipulating the selective scope of derivative and high frequency trading.

---

## 1. APPROACHING THE ISSUE OF INTERVENTIONAL CONTROVERSY

The concept of unconditional government intervention that assumes rescuing private entrepreneurs, whereby the public bears the cost, is known as Keynesianism. The modern state has created institutions that enable improvements in production and distribution, but also the incentives to coincide the interests of society with the interests of entrepreneurs, who are the founders and take initiatives. Relative importance of corporations has dramatically increased in relation to the state because multinational investments grew several times faster than the economic growth. Corporate sector with the rule of oligopoly has enthroned as the dominant sector of the economy. The concentration has led: to the creation of monopolies and oligopolies, and eliminating the competition; and controlling the industry through vertical integration (Lacic, 2012, p. 288). Mentioned economic-political constellation is explicitly expedient to analyze in a monetary, banking and credit system of the most developed financial economies (US, UK, Japan).

Given that the Federal Reserves (Fed), formally dominant global financial institution, over the last decade have held short-term interest rates at record low levels, Wall Street got the impetus to create the risky loanable products (e.g., subprime or interest). Using cheap money (essentially for free) the Fed have favored the large banks (big players) in the Wall Street, which manipulated the markets and de facto controlled the central bank. By “bailing-out“ the banks, the Fed were supposed to put themselves in danger and exposed to the collapse, in the conditions of factual insolvency (on the market-to-market basis) and the enormous leverage (debt). During the recent financial crisis, the Fed “secretly“ conducted so far unprecedented intervention, worth more than an annual US GDP. The price of the arrangement is several times lower than the interbank borrowings. The implications of such operations are:

- interventions based on (artificially) low interest rates over a longer period have not been carried out in order to stimulate demand,
- interventions have a negative impact on the market volatility and the economy in general, and
- interventions create monetary framework with rapid decrease of the money multiplier (which is difficult to prevent) and reaching levels from 1929.

Restrictive or expansive direction of monetary policy, in the context of causes of world financial crises, has been the subject of numerous theoretical and empirical research (modeling) at the level of monetary macroeconomics and/or financial econometrics. Contrary to M. Friedman and Schwartz (1991) and others during the nineties, O. Blanchard (2003) has suggested that the Fed was not directly responsible for the contraction of nominal money supply (money multiplier decrease) during the period 1929-1933.

The real money stock was almost constant. The consequences included the ultimate decline of nominal interest rates and the high rate of deflation – a proportional decrease in the price level. Recall, the bank lending was dominant for the purpose of financing speculative activities, but interventions of the central bank managed merely to “temporarily stimulate the economy“. According to A. Schwartz, on the eve of the current crisis, monetary policy in the United States was expansive, while analysis, such as D. Henderson’s and J. Hummel’s (2008), show that A. Greenspan’s policy was “imperfect“, but with restrictive direction.

The development paradigm with particular criteria and values has existed in all historical periods of the society. Development has always had a contradictory character, because order and chaos have never existed in a pure form, but in different combination. The dominance level of order or chaos in society was determined by the extent of the crisis in general and in specific areas, and consequently by the rate of development (Draskovic, 2014, p. 5). But through the lens of phenomenology and ontology, there is nothing unusual, because the order of the above formulas is maintained by the same methodology by which it was created: paradoxes, promises, opportunistic behavior, interests of big capital, and power ambitions.

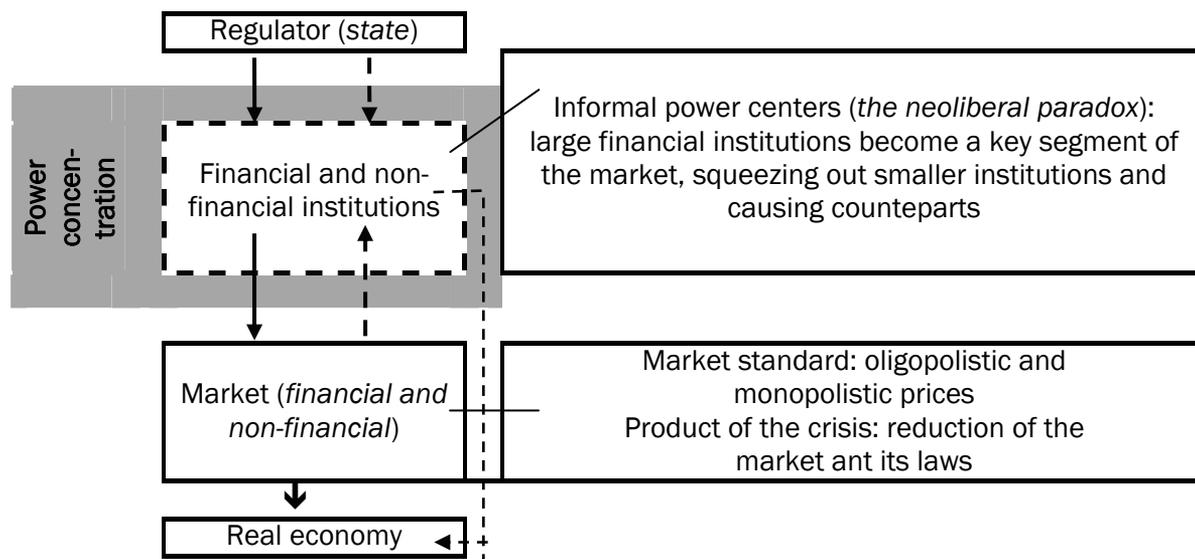
## 2. TRANSMISSION OF POWER AND CONTROL IN NEOLIBERAL HIERARCHY

A lot has been written about the causes of the global economic crisis, applying the various aspects: mythical, realistic, perspective, causal, consequential, structural, cyclical, programmed and other. Objective researchers should note the connection, as well as the specific synergy of global and local influence factors. There is one common denominator, and that is the lack of regulation at all levels, from the national and down, or generally deficit of institutional development, institutional competition and institutional discipline. In the era of knowledge, globalization, virtualization, decentralization and informatization, the only realistic and efficient connective tissue should be institutional subordination of economic entities at all levels. In other words, institutional pluralism should be a prerequisite for all other economic activities, measures, plans and results. Why is there institutional deficits at all levels, due to which the contemporary global economic crisis has provoked strong reaction of the state?

Krugman (2009, p. 38) writes about the blindness of the economics profession, which has not predicted very strong possibility of catastrophic failures in a market economy, because of the illusion of rational individuals and their interactions on the perfect markets. Many other economists have warned that the dominant neoliberal concept of economic policy and unwarranted enormous wealth are unsustainable, and that financial markets are very unstable (N. Chomsky, A. Kobjakov, M. Hazin, S. Rich, J. Stiglitz, J. Gray, G. Soros, M. Rabin, D. Harvey et al.). The limitations of human rationality and imperfections of the market have been ignored, as well as the possibility of quasi-institutional and opportunistic behaviors that are manifested through various forms of virtual and speculative business, greed, weakness of institutions, government and business ties, ideologized economic theory and its apologetics, deficit of the moral, legal, environmental and other social restrictions (Draskovic, 2009, p. 129).

One of the basic contradictions of neoliberal economic policy is that it has enabled paradoxical gap between the privileged power of the elite and limited institutional power of the state. Another contradiction has directly resulted from the first: an elitist urge for quick creation and increase of the wealth, dominance and total power have substituted institutional control. In such circumstances, institutional vacuum (created intentionally, due to the neoliberal conception of institutional redundancy), has reproduced the power of networking and informal groups (Draskovic, 2014). Contradictional context of neoliberal economic policy has its doctrinal terminology, monistic-institutional, anti-developmental, cognitive, strategic, interest, redistributive, ownership, civilizational, geopolitical and ideological sense, but also a number of crisis quasi-manifestations in practice. The mentioned economic policy, in global and local boundaries, has appeared as immoral, inhumane, brutal, chaotic, crisis and hegemonic system of the power, domination, violence, exploitation, and greed. All this have resulted in neoliberal monopolization.

Figure 1. Modification: from liberal to neoliberal paradigm



Legend: —> liberal paradigm; - - -> neoliberal paradigm

Source: Author's creation

Important for our presentation is the way that has led to a rearrangement of institutional recomposition of competence and actual decision making, which essentially meant the modification from liberal to neoliberal paradigm (Figure 1). The modern theory of corporatism does not

recognize historical rise of corporatism, from the initial dominant influence of the state, and then its gradual weakening, and finally the enthronement of corporation. It has constructed a model, through which the state and large corporations have formally imposed a comprehensive system of regulating the societal relations, a privileged relationship of individual corporations within the sector, and then the system of “agreement and arrangement“ between the countries – corporations, system for redistributing the profits among the selected participants, unlimited financial and logistical support of state institutions during hardships.

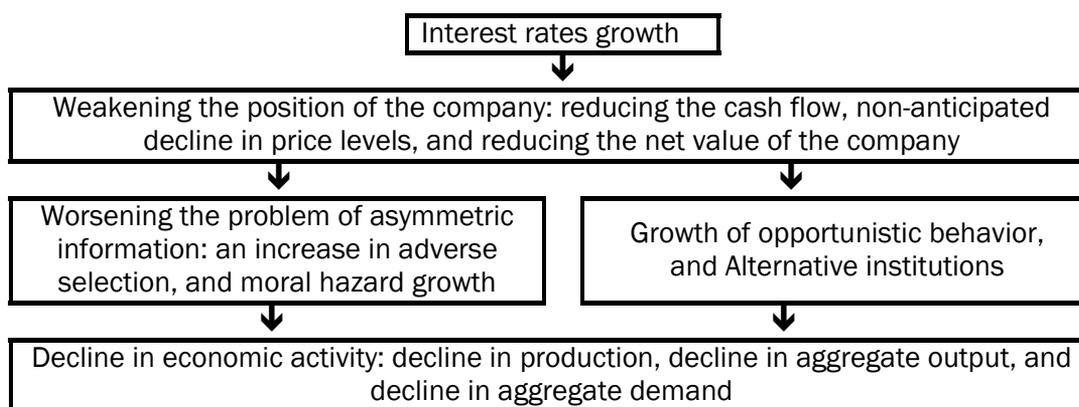
Introducing the theory of imperfect competition, in the thirties and forties, oligopoly and limited (imperfect) competition among several large sellers are increasingly seen as an important and significant limitation of the free play of market forces and mechanistic marginalism. Model (theory) of power in setting prices is increasingly represented in the literature, empirical research of monopolistic conditions in many economy sectors. We conclude that large corporations have definitely broke up with the old joint stock-capitalist relations. Real managers of large corporations are interested in a part of the social product, instead of the amount of paid dividends. Multinational corporations have become the new nation-states, while the old nation-states, being less powerful, began to follow the orders of the market (Lakic, 2012, p. 292).

The risk is multiplied by prevailing speculative and arbitrage strategies in relation to the hedging investment strategy. Aggressive strategies based on the prompt and/or net buying and selling are taken over by the gigantic financial conglomerates. Institution size, measured by assets or deposits, by total revenues and their comparison, by value added as a net income and, in particular, by off-balance items, becomes the basis of domination and thereby abuse, which usually does not lead to an adequate regulatory or regulative response. The dominance of the institutions over the state regulation is manifested in: dominance of price of instruments of dominant market institutions; change of legislation in favor of favored institutions, at the expense of state authority. Central banks as cartels of private banks (Fed case) take on the mechanism for implementing economic policy. Thus, the supreme monetary authority legally and factually takes over the powers of government (state), but is in the process of policy implementation stays in a subordinate position in relation to commercial, investment and universal banks and, indirectly, their extended entities such as hedge funds, SPV or SPE. These institutions are becoming informal center (concentration) of power. The interbank markets (wholesale markets) become the center of the world market in terms of inputs and consequences, determining not only the quantity but especially price indicators (interest rates, exchange rates) and speed of trading.

### **3. MANIPULATING THE INTEREST RATES: RELEVANCE OF THE MARKET INTEREST RATES**

Due to the financial crisis, the collapse of financial markets complicates the problem of asymmetric information and prevents the efficient allocation of resources in accordance to the most productive investment opportunities, resulting in a remarkable decline in economic activity. The theory of financial crisis on asymmetric information, in terms of cause and implications, has found a practical field for analysis in the current financial crisis. According to the theory, restrictive monetary policy has fueled the crisis through the following factors: the rise in interest rates, stock downs, non-anticipated decline in price levels, increasing uncertainty and banking panics. However, the fact is that the accumulated and deferred implications are tens of trillions of dollars of debt on the balance sheet of the banking system, whose growth is doubled compared to the rate of economic growth. For example, for every dollar of economic growth, the banking system creates US \$30 credit. Restrictive monetary policy in the context of an extreme case of increased problems effectuates the following mechanism (“extreme case of asymmetric information“) – Figure 2.

**Figure 2.** Effects of restrictive monetary policy in the context of crisis



Source: Author's creation

Due to the increased role of financial markets in the allocating the financial resources, central bank provides refinancing instruments. At least one of the tools (instruments) of the central bank is an official interest rate. In addition to managing the short-term money market rates, manipulation of official interest rates should contribute to designing the explicit intent of monetary policy and stabilizing the market expectations. This, further, should contribute to reducing the instability of interest rates. Due to disintermediation and financial innovations, there are changes in financial assets or increased volatility of monetary aggregates. This is another reason why central banks change the official interest rates, as a corrective measure, in order to make the stance of a monetary policy clear. The management of the central bank would be rather simplified if discount (base) rate was above the market or moved in accordance with them.

The use of interest rates in the evaluation (implementation) of monetary policy in crisis conditions is based on insufficiently clear and/or argumentative (correct) interpretation of the role of interest rates. By establishing control over the flow of money and credit, in order to prevent anarchic fluctuations in the economy, the central bank uses its official interest rate (discount rate) as a classical monetary policy instrument. Changes in this interest rates on central bank's loans have a significant effect on interest rates in the economy in general, although it reflects the movement of interest rates in the market. A larger number of market interest rates that exceed the discount rate have influenced the complexity of managing the discount window. The borrowings of depository institutions at the central bank have increased. Profitability has been achieved at the expense of the central bank: through lending at higher interest rates. The consequences of such financial system operations are:

- imposing a serious moral hazard to the overall economy,
- legalizing the mechanism through which the manipulative trading practices and prices in the so-called free market are being favored, and
- abusing the monetary system.

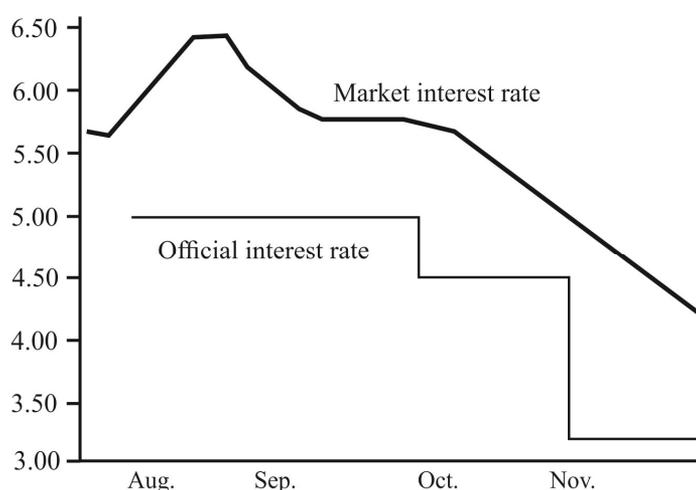
Generally, the accepted view is that the housing bubble, emerging financial crisis and the current economic difficulties are caused by expansionary monetary policy. Inadequate access to transmission is based on the following mechanism: in a recession, direction of monetary policy is expansive, low interest rates create a process of general increase of prices, which is a precondition of evolving the housing crisis in the financial crisis. Wrong interpretation of the effects of low interest rates on expansionary monetary policy implies inconsistency with the factual implementation of a restrictive monetary policy. Leaving aside the relation between supply and

demand, as a basic determinant of interest rates, i.e. the possibility of displacing the official interest rates in both directions, the interest rates on the interbank market have produced the adjustment of discount rate.

Simplicity of ongoing process of determination of interest rates, especially LIBOR, with totally routine process of factual calculations, results in indexing the extremely large scope of assets worldwide. The assessment of financial instruments, mainly consumer's, worth hundreds of trillions of dollars is applicable to mortgages, loans for credit cards and cars, for more currencies and loan maturities. However, banks that participate in determining LIBOR rates are not obliged to borrow at these rates. Due to the absence of data on lending in the interbank market, it is unclear whether the loans were granted at these rates. Exhaustion of interbank liquidity (supply) is explained by the inclusion of exceptional growth in credit risk, which resulted in an interest rates increase. The general opinion is that the market for commercial paper probably provided data on prices and quantity.

Since LIBOR itself is not sufficient as an indicator for the analysis, it is necessary to follow the spread with official (base) rate. The collapse of investment bank Lehman Brothers has influenced the level of LIBOR, and dramatic worsening of the crisis has led to the lowest level (3.54%) of three-month LIBOR after the bank collapse. Theoretically, it could be interpreted that a significant decline in interest rates of the central bank from 4.5 to 3% at the beginning of November 2008, has led to a further lowering of LIBOR. In conditions before the crisis, with official interest rate of eg. 3%, LIBOR should be higher by 10 or 20 basis points. However, the inconsistency of relations between the two rates at the beginning of the credit crisis (August 2007) was a trend (Lakic, 2010, pp. 38-39). Despite the decrease of an official rate, relatively high level of LIBOR resulted (mid October 2008) in a significant increase in variable interest rates on mortgage loans. A bank bailout should influence the formation of LIBOR at a lower level, but reference interest rate in the UK rose above 6%. Although the liquidity inject into the banking system in the amount of 40 billion pounds (October 2008) had a positive sign, the impact on interest rates had limited ("moderate") effect. Operating dominance of the market over the official interest rate can be thus obvious – Figure 3.

**Figure 3.** The inconsistency of the official and market interest rates (LIBOR, 12.11.2008)

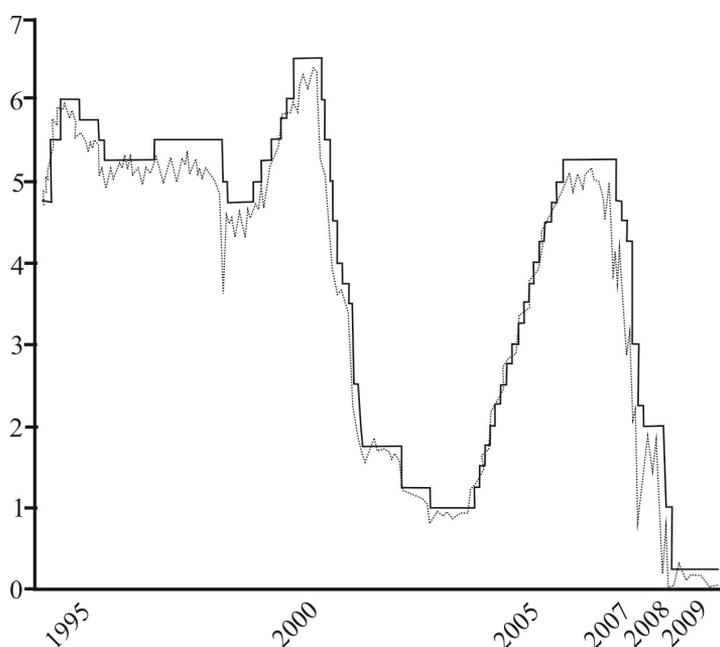


Source: Author's creation

Reducing the impact of interest rates of major central banks (i.e. the Fed) indicates that the control function of the Central Bank has no practical foundation. Namely, the central bank has a

partial possibility to move interest rates in both directions. Reduction of the discount rate, for example, can be interpreted as an indication of decision to increase the liquidity in the system. However, instead of deciding on the desired level of interest rates, the Federal Reserve had just followed the market. This reaction was evident after the fall of market rates in October 2000, followed by growth in June 2003, and finally fell again in February 2007. The Bank of Japan was also constantly adapting its target rate to maintain direction in line with developments (fall or rise) in the bond market. Practically, the drop of interest rates was not registered on bullish markets. This is a proof that direction of interest rates, rather than monetary authorities, has determined the changes in the market (speculators and/or manipulators) – Figure 4.

**Figure 4.** Dependence of the Central Bank's reaction on the market (1995-2009)



Source: Author's creation

Change of Treasury bills would cause immediate response of the target rate's for the Fed Funds. Figure 4 shows the relation between target rate of the Federal Reserve and the 90-day Treasury Bill Yield. The first two quantitative easing of the Federal Reserve represent the bail-outs through constant manipulation of the money supply. Large amounts of bought securities had the alleged aim to increase liquidity and prevent growth of interest rates. Liquidity management of the Federal Reserve in the form of QE 3, argued as "psychological uplift of the investors", at the bond market has initiated: (artificial) manipulating the interest rates; attractiveness of investing in debt instrument (bonds). The significant increase in banks' profitability is the result of two factors: fixing the short-term interest rates at nearly zero level by the central banks (Fed, ECB); long-term growth of the interest rates caused by inflation. Starting from the previous analysis the conclusion is unambiguous: creating inflation by the central bank is in the interest of speculative and manipulative operations of the Wall Street's institutions.

Selective credit control as a common form of monetary intervention in the leading financial systems have enabled de facto power to corporate banks, through the so-called agreement and arrangement with the Central Bank, to redirect funds of primary issue in accordance with "national interests". Selective mechanism of central-bank lending should be present in the economic systems where "market mechanism" is not sufficiently effective, so the issuing bank was supposed to substitute the imperfection of the money market. Preventing specific purpose lend-

ing left consequences for banks of small and medium size (non-corporate). In essence, linking of banking and industrial concerns derogates the influence of state agencies and at the same time creates a system of cross-ownership, usually under the dominant influence of the banks with the highest share of assets. This process is completed by implementing long-term practice of preventing the collapse of the banks that caused the crisis disorders, known as financial neo-liberal approach “too big to fail”.

F. Baring (1797), H. Thornton (1802) and W. Bagehot (1873) have seen the stabilizing role in the lender of last resort in crisis circumstances. The current crisis has caused collapse of several hundred small and medium-sized banks, and the government rescue has awarded the companies that basically failed at real market standards. US monetary system is an initiator and real brake of the the world financial system, even to the level of overall destruction. The Fed have approved 16.1 trillion of almost interest-free loans to the privileged (chosen) banks, and not only in the US. That is less than a third of 3.8% for interbank borrowings (20.10.2008) at one-month level. On the other hand, regardless of the increased capital, “*a pretty good capital base*” is low compared to current liabilities, i.e. debt. A leverage of the Central Bank has increased more than 3.3 times compared to the 2008 crisis. The debt of banks in the balance sheet is enormous. The debt and the banking system are growing faster than the US economy more than 15 times in comparison to the pre-crisis period. All of this is a consequence of vertical schemes (position manipulation) of neoliberalism.

#### 4. HIGH DERIVATIVE AND HIGH FREQUENT TRADING

Derivative and high frequent trading are crucial segments of the financial system in terms of the total value (hundred trillion or quadrillion dollars) and speed of trading (milli or nanoseconds). Initially designed in seventies to confront the risks of interest rates and currency, financial derivatives were then constructed for speculative operations, drastically surpassing the total assets of banks and, ultimately, shaped the extreme risky environment in the financial and, generally, the global economic system. Vertical paradigm of neoliberalism is supported by the exponential growth of a notional value of derivatives and, therefore, in the lack of adequate regulation, i.e. with regards to the market capitalization. Manipulation of derivative contracts derives from the observation that the price depends on, or is derived from the underlying assets, ie. the value is determined by fluctuations in an underlying asset.

Financial derivative has no underlying value and is not an investment into anything realistic: it is a legal and highly leveraged bet (without control) on the future value or performance of something else. Comparison with the world GDP and assets of corporate banks indicates to:

- fundamental (not formal) circumvent of the regulatory mechanism: protection or safety until a crisis occurs; regulation exacerbates the situation; implementation of regulation is not legally precise,
- size of derivative market, potentially destructive: hypothetical value of an institution is equivalent to the several GDPs of the largest economy and exceeds the overall world economy,
- absence of a mechanism for suppressing the bubble burst and spreading of derivative crisis: poor quality of derivative exposure; no access to the full information on prices and commissions; rapid breakdown which cannot be covered with money, and
- disproportionate amount of derivative risk: a small number of institutions in the concentrated industry involves almost the full amount of exposure.

Alternative institutions and alternative instruments are the pillars of neoliberal dogma, but they could also be a tool of overall destruction. Credit default swap (CDS) was created as an alternative instrument for the protection from default credit commitments, a product of significant confrontation to default risk of individual debtors, an arrangement which carries the risk of inability to collect a loan (in the form of bonds or loans). A holder of financial claim may transfer

credit risk to other transactor, who takes over the credit risk, the transfer price (premium) is paid by the buyer of protection against credit risk. When concluding the CDS arrangement, the protection seller (loan collateral) agrees to pay the receivable amount to the protection buyer, if he/she can not collect his/her receivables on loans or bonds of the company or state. CDS are similar to the instruments such as insurance policy or guarantees covering credit risks. CDS is sold by banks, hedge funds and insurance companies, charging a premium for providing insurance. When a customer experiences a default, the regulator is usually not present to make sure that the CDS seller has the money and is able to pay CDS insurance to the buyer.

Problems of arrangement are: aggregate undercapitalization of the CDS seller, because their allocated reserves are a small portion of the required percentage to be paid the agreed sum of the insurance; false sense of security to the bond buyers, which contributes to the outbreak of crisis (eg. Greek debt crisis). Namely, the CDS sellers have bought CDS in other insurance companies to protect them, as they considered, from merely possible bankruptcy of Greece. As buyers of CDS arrangements, countries come in a huge exposure and debt position at the slightest negative economic trend. From conditionally justified reasons of secrecy in concluding the CDS contracts, arises space for protectionist, corrupt and in cartel effects of global financial entities. The consequence is the so-called Crony capitalism, that finances and protects unofficially privileged companies and firms. The implications of institutional disposition of this instrument (arrangement) can be reflected in the following stages:

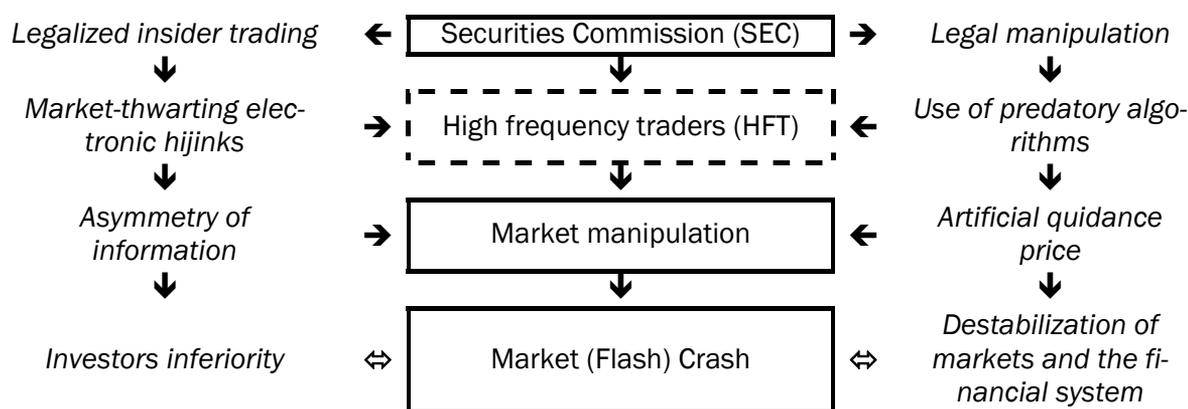
- *Manipulation pattern* was achieved by establishing rating package of CDS contract, not by individual CDS contracts. Quotations serve the banks to hide enormous subprime lending positions i.e. index serves the speculators who bet on the decline and crisis of subordinate mortgage market. Trade occurs mainly in the OTC markets, which moves away from transparency in trade;
- *Regulation bypassing*. The reform of the law on banks and financial institutions placed emphasis on regulation and clearing house, but the law did not specify the implementation thereof. In the beginning, consequences were delays and inefficiency, and also the effective lobbying the banks to prevent the implementation of the adopted legislation. Although through crisis, regulation and control of CDS trade was globally reduced to formal and superficial activity of regulators;
- *Instrument disposition*. Package of rating CDS contract is a set *CDS arrangements* that are directly related to the movement of market index. The outstanding absurd consisted of the following: growing the rating package of CDS contracts, growing and full value of the index of the stock exchange (specifically ABX.HE Stock Exchange). The aforementioned disposition suggests an aggressive strategy of neoliberalism, also observed in ETFs, and
- *Implementation problem* is identified in the following: The establishment of a small protective capacity of CDS, first by the sellers, later by customers, is an implementation problem. At the same time, holders do not want to activate the CDS. For effective implementation of the CDS arrangement the ideal conditions are the global economic crisis and recession. CDS are molded as suboptimal real decisions.

High frequency trading (HFT) is a business model “within the market” and complicated transaction through which the computers make tactical decisions in real-time to use the opportunities before others by dominating the market, starting from a fragmented and highly fluid trading in securities and derivatives, and complexity of predatory algorithms for the purpose of routing prices of instruments and making profit from artificial increase or reduction of prices. The theoretical basis of commercial algorithms is included in the Theory of market microstructure in modern interpretation (O'Hara, 2014; Aldridge, 2013; Christiansen, 2009; etc.). The theory does not emphasize the use of trading algorithms for speculative or, more precisely, manipulative operations in order to make more profit, while market risk is not so significant. The practice, however, does not suggest the reason for obtaining the best possible prices for an order (“algorithms for optimal execution”). Hence, high frequency trading is based on:

- manipulative scope of operation, when the market scam (legal manipulation) is the cause of systemic risk,
- practically legislated insider trading, based on predatory algorithmic trading strategies,
- weakening of transparent price discovery, by hidden trade liquidity,
- reduction of public liquidity, available to the conventional stock exchanges, and
- destabilization of the market and threat to the financial security of citizens, while “financial elite“ harvest wealth by socially useless techniques.

Empirical studies of determinants of high frequency trading are supporting previous findings. The prevailing opinion is that the primary causes of the (market) volatility are HFT and enormous trust in computer systems (*Market Strategies International* 2010; Kirilenko et al., 2014). Relatively recent research, such as F. Zhang (2010), suggest that HFT produces adverse effects on the capital market in the United States: increasing price volatility of stocks. Analysis show that high frequency traders do not contribute to the stabilization of prices during the unusually volatile period. It has been proved (Huh, 2014) that under conditions of asymmetric information, the creation of markets through HFT provides less liquidity actions. High frequency traders, according to the analysis (eg. Brogaard et al., 2013), due to the informativeness, had an advantage in price efficiency and imposed the costs of adverse selection to other investors. According to S. Ghilani (2012), Capital Wave Strategist, high frequency trade is not fair, nor consistent in preserving the free and regulated markets, i.e. it is illegal.

**Figure 5.** Example of regulator’s “incompetence“ consequence



Source: Author’s creation

However, the essence of the vertical model functioning, as a part of most commercial operations of investment banks, is the guiding price of instruments by dominating the market, with a guaranteed profit (common market manipulation), and in trading with insider capital flows, which are unprotected and sold to the high frequency traders with exclusive advantage (legal insider trading). By inserting quotas on the market, high frequency traders try to deceive or provoke reaction of other market participants in adapting their quotas. “System defects“ consist of implicit response from the authorities (legislators, lobbyists, regulators such as the SEC), giving to HFTs the “license to steal from others“, which allows pulling money from uninformed (inferior) investor – small or large (pension funds). The so-called quants – mathematicians and physicists and rogue algorithms, unwilling and unable to quantify the risk, cause moral hazard and erode the fundamentals (credibility and overheating) of the market.

## 5. CONCLUSION: IMPLICATIONS OF DISPOSITION PARADIGMS

Claims of prominent economists that the financial systems evolve at an accelerated pace towards a market-centrist, not a bank-centrist system (dominated by banks), are directed towards the creation of views on a lot more efficient system, and resource allocation, as well as lower volatility of the financial markets. In accordance with this view, market rules will curb all excessiveness, the state institutions will prevent fraud and abuse, and the public will be effectively informed. Quantitative models are supposed to hide the following facts: a) absolute market efficiency is impossible, b) perfect markets are a product of the economic theory structure, c) thesis on market rationality in determining the financial cost is indefensible, d) diversification can not prevent losses, and e) nonlinear development is characteristic of globally-linked markets in crisis.

This, actually, justifies the market fundamentalism, funded in a vertical constellation of financial corporatism, which is a consequence of vertical strategy of domination. Corporatism represents an economic superiority, deciding factor and instrument of uncontrolled operations of corporate entities in relation to state entities (regulators, agencies, commissions). Modern technological progress and economic trends in the international framework, based on protectionism for one side and discrimination for another, have resulted in a homogeneous concentration of power: *industrial – industrial corporations; financial – industrial and financial conglomerates*.

Nation-states have less power and follow the orders of the market, and large corporations completely dominate the political systems. Freedom of competition and advancement of individuals and small businesses usually is not permitted. In collectivist system, a liberal system of free enterprise is far from reality, with the rapid growth of economic inequalities and “elite” control of the national wealth.

Holders of monetary and liquidity management are the only official body that, at the height of the financial crisis, can quickly react by intervention mechanism. The current financial problems were “unusual” regulatory interventional operations and “unconventional” changes of monetary policy. Accordingly, the escalation of the financial crisis has had two repercussions in the monetary system: leading central banks cut their interest rates, which coincides with enormous increase in the price of housing; monetary policy has encouraged moral hazard, by crediting system, initiated by the mortgage loans of high risk profile. Traditional instruments of interest rates proved to be ineffective in the midst of the current crisis. First of all, there were reactions of central banks on long-term market changes that have already occurred. On the other hand, the mechanism by which speculators gain priority over other investors, is known as “telegraphing the market” by the monetary system managers.

Generally accepted claim that the central bank is a “suppressor of financial distress” has no real basis. It is evident that monetary authorities and government agencies are not able and/or do not tend to prevent a banking panic. Laws relating to the central bank formally empower the monetary authorities in the broader economic context, but financial flows are actually determined and directed by mega banks that exist outside the relevant scope of an adequate regulation and supervision.

Prudential regulation, lending in a last instance and deposit insurance are mechanisms that even exacerbate the consequences of economic downturns such as the recession, but also strengthen the financial supremacy of corporate banks. Financial derivatives are the one and high-frequency trading is the another fundamental market mechanism of institutional predatorship, allowing the neoliberal disposition of the “market” and “non-market” participants: oligopolistic and/or monopolistic treatment of prices and sustainable market manipulation, are creating a bubble as real distortionary input.

## REFERENCES

- Aldridge, I. (2013), "Market Microstructure and the Risks of High-Frequency Trading", *Working Paper*, Princeton Quant 2013 Conference, New York.
- Blanchard, O. (2003), *Macroeconomics*, Prentice Hall, London.
- Brogaard, J., Hendershott, T., Riordan, R. (2013), "High-Frequency Trading and Price Discovery", *European Central Bank Working Paper*, No. 1602, Frankfurt am Main.
- Christiansen, J. V. (2009), "Financial Market Microstructure and Trading Algorithms", *AEF Thesis*, Copenhagen Business School.
- Draskovic, M. (2009), "Globalna finansijska kriza i neoliberalna dogma", *Ekonomija/Economics*, Vol. 16, No. 1, 127-148.
- Draskovic, V. (2014), *Neoliberal Metaphor – Quasi-economic paradigm*, Elit-Rifin, Podgorica-Zagreb.
- Friedman, M., Schwartz, A. (1991), "Alternative Approaches to Analyzing Economic Data", *American Economic Review*, Vol. 81, No. 1, 39-49.
- Ghilani, S. (2012), "Wall Street Insight & Indicements", *Money Morning*, Different Articles, Oct.
- Henderson, D. R., Hummel, J. R. (2008), "Greenspan's Monetary Policy in Retrospect: Discretion or Rules", *Cato Journal Briefing Papers*, No. 109, 1-9.
- Huh, Y. (2014), "Machines vs. Machines: High Frequency Trading and Hard Information", Federal Reserve Board, *Staff Working Papers*, New York.
- Kirilenko, A., Kyle, R. S., Samadi, M., Tuzun, T. (2014), "The Flash Crash: The Impact of High Frequency Trading on an Electronic Market", *Social Science Research Network* (Electronic Publishing), New York.
- Krugman, P. (2009), "How Did Economists Get It So Wrong?", *The New York Times*, September 6, 36-43.
- Lakic, S. (2010), "Monetary Management And Control Under Uncertainty And Crisis", *Montenegrin Journal of Economics*, Vol. 6, No. 11, 35-48.
- Lakic, S. (2012), "Corporatism as a Totalitarianistic Foundation and Practicism", *Montenegrin Journal of Economics*, Vol. 8, No. 2, 275-294.
- O'Hara, M. (2014), "High Frequency Market Microstructure", *Johnson Graduate School of Management Working Paper*, New York.
- Stiglitz, J. E. (2014), "Tapping the Breaks: Are Less Active Markets Safer and Better for the Economy", Presented at the Federal Reserve Bank of Atlanta (April 15), Financial Markets Conference: *Tuning Financial Regulation for Stability and Efficiency*.
- Zhang, F. (2010), "The Effect of High-Frequency Trading on Stock Volatility and Price Discovery", *Working Paper*, Yale University, New Haven.