

# Chapter 13

## Cybernetic Approach for the Stock Market: An Empirical Study of Bangladesh

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### ABSTRACT

*The old idea of segmented macroeconomics of the financial sector competing with the real economy is replaced by a new model. This model formalizes the new architecture for the macro economy, and its relationship to the stock market. In this model relating to a reconstructed state of the economy and the emergent structure of the financial architecture, money and spending are treated as complementary elements of growth and development. The overarching structure in the end is the Money, Finance, Spending and Real Economy (MFSRE) with its extensively complementary inter-variables relationship in a general system and cybernetic form of interrelationships. The stock market, exemplified by the empirical case study of Bangladesh's state of the economy and the Dhaka Stock Exchange, bring out the true example of the macroeconomic analysis. The new financial architecture with its stabilization, sustainability and growth and wellbeing as basic-needs regime of development is contrasted with old macroeconomic belief and policies based on outmoded macroeconomic beliefs and futures.*

### INTRODUCTION

Stock market turnover rates, yields, yield rates, and stability are indicators of the health of the economy for those countries that depend upon such a financial institution. But it is not such an important support system for an economy that does not have stock market, and does not need one. Instead they depend upon real asset pricing mechanism for measuring the economic and social standards. The stock market is then not an essential institution to act as a barometer of economic change. But these two opposite views tell a much larger story about the economic processes and their social effects. Meera (2004, p. 59) puts the emptiness of the casino barometer of a stock market and its underlying financial system in value formation in the following words: "Financial institutions create money out of nothing but lend it out of interest.

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This characteristic of fiat money called seigniorage is at the root of financial crisis, monetary instability, and unjustness. The fractional reserve requirement also makes possible the creation of additional money through multiple deposit creation. All this has brought about huge volumes of liquidity in the global monetary system, which is responsible for the huge asset price bubbles faced in many countries.”

To investigate into these opposite views regarding the financial system with or without stock market we note what lies behind stock market in the organization of asset valuation to protect the wealth of savers and to contribute to and reinforce the relationship that money and finance has with the real economy. Furthermore, stock market stability also requires inflation targeting and a participatory form of development model for the protection and wellbeing of the marginal savers. The ethical principle here linked with the economic objective is derived from Rawls’ Difference Principle (1971) as an example. On the point of national wellbeing Rawls wrote (op cit, p. 14-15):“... inequalities of wealth and authority are just only if they result in compensating benefit for everyone, and in particular for the least advantaged members of society.” The moral theme underlying the Difference Principle is equally applicable to the purpose of financial stability and social and economic measurement of wealth. The question then stands whether stock markets can deliver such a concept of wellbeing. Likewise, we need to ask whether there is an alternative economic and socially productive activity that establishes the total wellbeing criterion for the nation.

And on this objective issue the structural changes linked with stock market and alternative financial institutions also invoke the nature of participatory role between central bank and commercial bank on the matter of money, finance and real economy complementary relationships. On this issue Mishkin (2007a, p. 55) presents his view:

*First, it (central bank) should advocate a change in its mandate to put price stability as the overriding, long-run goal of monetary policy. Second, it should advocate that the price stability goal should be made explicit.... Third, the Fed should produce an ‘Inflation Report’ ... that clearly explains its strategy for monetary policy and how well it has been doing in achieving its announced inflation goal.*

Furthermore, the issues of monetary relations involving central bank and commercial banks, and inflation targeting to stabilize prices also invoke the study of asset pricing mechanism for the common good on the wellbeing side. On this asset-pricing issue for inflation targeting Mishkin (2007b, p. 59) emphasizes the use of monetary policy for the stabilization of stock market fluctuations. He points out the importance of regulating the monetary policy effect on inflation targeting so that stock market effects on investment as a major form of spending (fiscal side) remains well maintained. Besides this there is need to maintain the transmission effect of stock market changes on household liquidity and household wealth.

Firstly, a combination of the above-mentioned socio-economic problems faced by the prevalent monetary, financial, and real economy relations is summarized in analyzing the causes of stock market turmoil. Next, the formalization of a new financial architecture with participatory linkages requires development and application of a revolutionary new form of model that is epistemologically premised on unity of knowledge. From the formalism of the new financial architecture comes out the problems of economy and society discussed above. These comprise firstly, the nature of functional relations between money, finance and real economy that leads to price stabilization, economic growth, monetary and fiscal expansion with appropriate financial instruments.

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