Valuing financial assets out of markets: why it is crucial, why it is justified, how it could be made

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The financial crisis of 2007-2008 has revived old controversies on financial theory and financial markets. Since then, very little has changed, though, in what is taught and institutionally recognized in this area of knowledge. Financial regulation, its latest developments included, remains embedded in concepts deriving from mainstream financial theory. One reason for such an inertia is certainly the strength of institutional constraints. But there also conceptual reasons.

When asked why they didn't see "this" coming, mainstream financial theorists can rightly answer that the central prediction of efficiency theory is that no one can. Besides, that's not their job to see anything coming: their job, so the story goes, is to test assumptions against historical data.

Then, when faced with the fact such market swings as those seen in 2007-2008 illustrate the idea that market prices may not reflect fundamental value, they can also rightly answer that no one can tell what it is, and then ask who we are to dare and say what asset prices *should* be.

But then, these assets are priced; they have to be, one way or another. The crucial point is: which is the best one? Crucial, for if we can demonstrate that non-market settings would be better than markets at pricing financial assets, then we would have deprived the aforementioned theorists of any line of defense.

For this, we don't need to test assumptions against historical data. It would be pointless, for, if a fundamental value is not objective – and it is not – then no test of that kind can tell us if a market is good at reflecting it. We don't have figures to compare the prices with, so we can't test this[1]. Only logical reasoning, based on factual evidence, can help us. Part of this job has been already made by Kaldor (1939), but we will focus on explaining why

[1] To be honest, Shiller (1981) tried to do this, but one can always argue, as was the case, that his fundamental "benchmark" is not the good one.

the reasoning of Hayek (1945) intending to show why markets are better than any other solution to price anything doesn't apply to financial markets.

We will conclude by making a case for the creation of independent valuation institutions that would be in charge of pricing financial assets and maybe other goods used for speculative purposes. This would require a kind of "institutional engineering" whose features we can only suggest and delineate, hoping to trigger a discussion on this topic.

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