THE INTELLECTUAL ORIGINS OF THE GLOBAL FINANCIAL CRISIS

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THE INTELLECTUAL ORIGINS OF **THE GLOBAL FINANCIAL CRISIS**

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Frontispiece: Gluttony, from *The Seven Deadly Sins*, engraved by Pieter van der Heyden (c. 1530–72) 1558 (etching and engraving) (b/w photo), Bruegel, Pieter the Elder (c. 1525–69) (after) / The Israel Museum, Jerusalem, Israel / Vera & Arturo Schwarz Collection of Dada and Surrealist Art / The Bridgeman Art Library International

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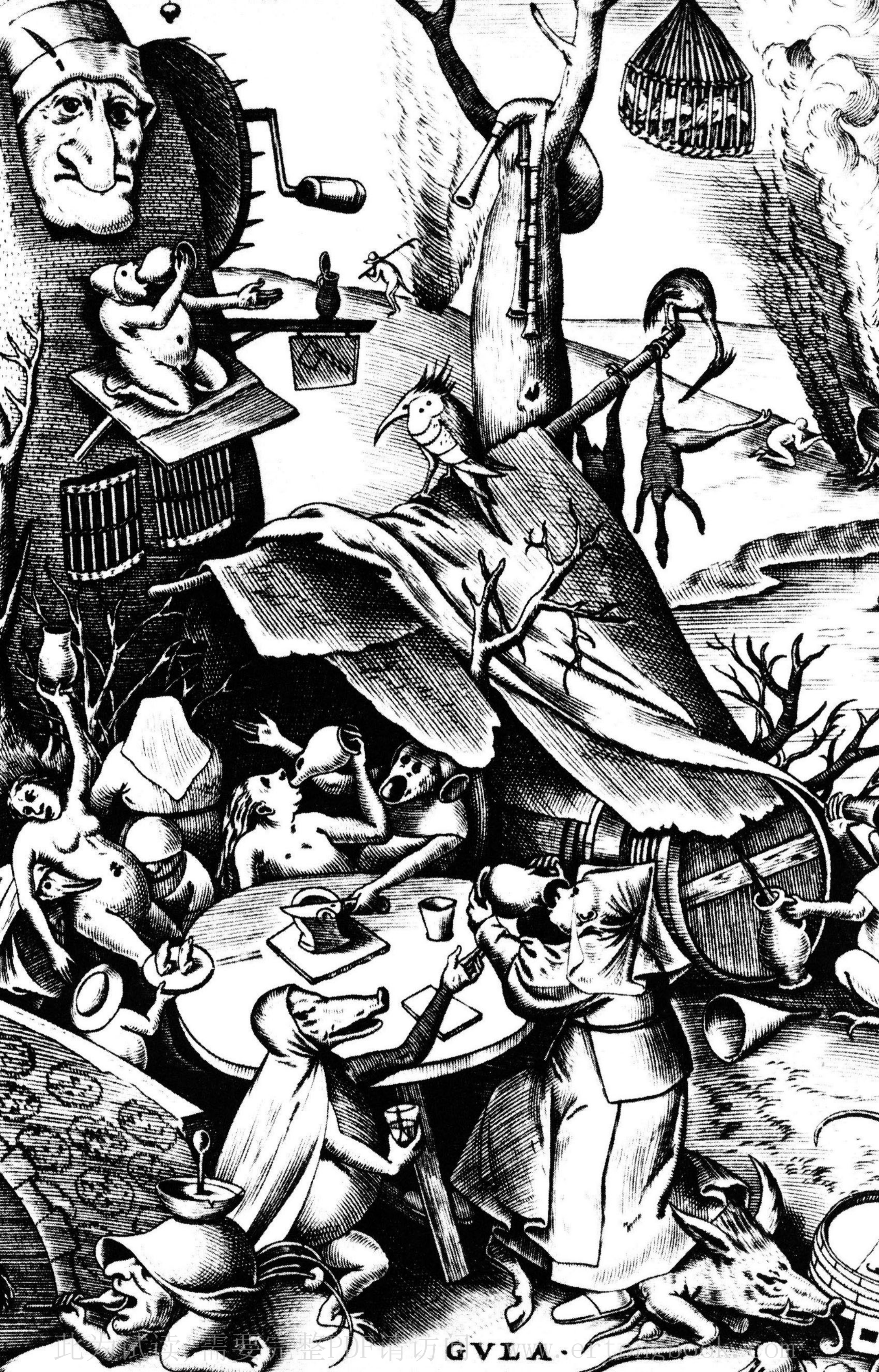
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Preface

As world markets crumbled in the fall of 2008, I was teaching a seminar on Hannah Arendt's book *The Origins of Totalitarianism*. The second main section of Arendt's exploration of twentieth-century totalitarianism is called "Imperialism." In it, Arendt shows how the imperialist insistence that political power expands infinitely is one of the root causes of totalitarian governance. Arendt describes imperialism as the importing of the economic principle of unlimited growth into the realm of politics. She argues, convincingly, that while growth may be an important principle of economics, politics demands limits. A state requires borders, and a citizenry depends on a sense of themselves as sharing a common sense of right and wrong. In short, politics requires judgment and limitation, both of which are overwhelmed by the economic and imperialist imperatives for infinite expansion.

Arendt's insight into the political implications of the subordination of political to economic thinking struck me as deeply relevant to the emerging financial crisis. Although the financial crisis has many economic, political, and psychological causes, it is, in important ways that Arendt makes visible, a result of a crisis in political judgment. In our globalized world, political limits fall prey to economic rationality. Tax havens and rent seeking allow global corporations to evade national regulation; nations are set into competition for business; a growing economy becomes the foundation of national security; and the free market—the absence of government—is seen as the epitome of good governance. In the frenzy for growth and the confidence in the invisible hand, governmental institutions around the world ceded their authority to regulate, set limits, and to govern. In Arendtian terms, the financial crisis emerged from our elevation of the economic rationality of infinite growth over the necessarily limited practice of political judgment.

Arendt's book made cogent the fact that the financial crisis shared with totalitarianism a rootedness in the elevation of economic over political modes of governance. The rise of economic thinking is central to

Arendt's lifelong concern with the retreat of political judgment in our times and our willingness to be ruled by technocratic and bureaucratic rationality instead of insisting on our collective freedom. Arendt, I realized, offered a profound and underappreciated way to think the depth and danger of the current financial crisis.

It was around this time that I was working to institutionalize the Hannah Arendt Center for Politics and Humanities at Bard College. I approached Alex Bazelow, a Bard graduate and friend of both Arendt and her husband, Heinrich Bluecher. Alex generously agreed to help support a conference exploring the intellectual origins of the financial crisis. I also approached Dimitri B. Papadimitriou, president of the Levy Economics Institute at Bard and Taun Toay, of the Levy Economics Institute; I asked them to commit the Levy Institute to cosponsor a conference that took a broad and Arendtian look to the origins of the financial crisis. They generously agreed. The ensuing conference, "The Burden of Our Times: The Intellectual Origins of the Global Financial Crisis," took place in October 2009 at Bard College.

As do all Hannah Arendt Center conferences, the "Burden of Our Times" conference brought together public intellectuals, artists, journalists, businesspeople, and academics from across the disciplines to address the relevance of Arendt's thinking to a contemporary political event. The effort is to spur thinking about politics in the spirit of Hannah Arendt and to encourage people to "think what we are doing."

The conference produced a unique blending of discourses, with humanities professors speaking about derivatives and tax havens and economists and business leaders thinking through the philosophical implications of thinkers such as Arendt, Max Weber, and Michel Foucault. Richard Bernstein, writing in the *International Herald Tribune* and the *New York Times*, advised the Financial Crisis Inquiry Commission, created by Congress to investigate the causes of the recent and ongoing financial crisis, to consider the Arendtian analysis presented at the Bard conference. There was a clear sense that doors had opened that should not simply be allowed to shut.

Taun Toay and I asked the participants to expand and polish their essays for publication. At the same time, we asked that they make an effort to preserve the style and form of the original oral presentations. The essays that follow are the result. They are as a whole shorter than typical academic essays, and they have fewer footnotes and scholarly trappings.

Instead, they present efforts to think with and, at times, against Arendt in her call for thinking what we do.

—Roger Berkowitz

This volume is a work of twenty-six contributors and two editors and would never have been finished without the assistance of many others. From the beginning, Bard's President, Leon Botstein, encouraged and supported our efforts. Funding for the conference, which also supported publication of this book, was generous and came from Wendy and Alex Bazelow, Mischa Frusztajer, Alice and Nathan Gantcher, Richard Gilder, Amy and Jeffrey Glass, James Grosfeld, Robert and Martha Lipp, Jack Nusbaum and Nora Ann Wallace, Marshall Rose, Barbara and Jon Roth, and Will Weinstein.

In planning the original conference, we were assisted greatly by Debra Pemstein and Mary Strieder. In addition, a number of Bard students—especially Alice Baker—assisted in preparing the manuscript for publication. Finally, we are deeply indebted to Helen Tartar, Thomas C. Lay, and Eric Newman at Fordham University Press, and the copy editor, Teresa Jesionowski. Fordham Press has been a strong supporter of the Hannah Arendt Center, and their engagement and professionalism are extraordinary.

—Roger Berkowitz and Taun N. Toay

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Contents

INTRODUCTION

The Burden of Our Times

:: ROGER BERKOWITZ

> *A crisis becomes a disaster only when we respond to it with preformed judgments, that is, with prejudices.* —HANNAH ARENDT, *BETWEEN PAST AND FUTURE*

An accomplished businessman, one deeply involved in the housing industry, wrote me when I solicited his views on the intellectual causes of the financial crisis. The cause of the crisis is really quite simple he said: Cheap money—the combination of low interest rates, lax regulation, financial innovation, and excess leverage—led to unprecedented speculation.

From an economic point of view, the cheap money hypothesis is unassailable. But in a volume on the *intellectual* origins of the financial crisis, we need to go further. For starters, we might ask: What is cheap money?

Cheap money means money that can be borrowed at little cost. When interest rates are low, those with money have no incentive to keep it in the bank. When low interest rates are combined with lax regulations, the chances of successful investments are increased, and incentives for risky speculation are increased. In an era of cheap money, saving is discouraged, and speculation is encouraged.

If cheap money is behind the bubble, what is behind cheap money? And when did the era of cheap money begin?

Some, like Charles Morris, say it began in the aftermath of 9/11 and the bursting of the technology bubble, when the Federal Reserve reduced the federal funds rate to 1 percent and kept it there until 2004, financing the bubble in housing prices that lasted until 2007.[1]

Others, like George Soros, say that it began with the free-market fundamentalism of the 1980s. Globalization, deregulation, and financial innovation led to an unprecedented increase in leverage and speculation. Credit market debt in the United States exceeded 350 percent of GDP in

2007. Limitless and unregulated credit creation helped create a "super-bubble" in asset prices.[2]

Still others argue that the epoch of cheap money began on August 15, 1971, the day that the United States abandoned the gold standard. As a fiat currency, the dollar is not backed by hard assets, and the potential supply of dollars is limited only by the imagination and demand of the citizenry. For William Fleckenstein, the loss of the gold standard in a democratic political system that rewards politicians for their largess cannot but lead to an ever-increasing supply of dollars. "In a social democracy with a fiat currency," he writes in his motto that was long emblazoned on his website, "all roads lead to easy money."[3]

Another chorus of experts—like Hunter Lewis in his essay in this collection—argues that the rise of easy money is rooted in *government* policies developed in response to the Great Depression in 1929. When governments flood markets with easy money in times of economic contraction, well-meaning intervention encourages a moral hazard, incentivizing speculators to employ ever-greater amounts of leverage with the expectation that they will profit in good times and be bailed out in bad times.

Yet still others would say that the era of cheap money is much older, that it began on May 5, 1716, the day that John Law founded "Law and Company," as the national bank of France. Law's radical innovation was that paper money—as opposed to silver and gold coin—could be printed, and thus the supply of money could exceed the amount of gold and silver on which its value was based.

What this little tour of the last three hundred years tells us is that if cheap money is the economic cause of the financial crisis—and my friend is right in at least a strict economic sense that it is—it is an answer that tells us very little.

John Stuart Mill, writing amid the great financial crisis of 1826, argued that cheap money will expand irrationally in times of speculative optimism, inaugurating a vicious cycle of boom and bust. Some booms are longer. Some busts are deeper. But the boom-bust cycle of cheap money is part of the speculative nature of capitalism itself. In his essay "Paper Currency and Commercial Distress," Mill argues that the factual unavoidability of economic crises generated by speculation was an adequate defense of cheap paper money against those who would use the crisis to criticize it. For Mill, cheap money and the speculative frenzies that cause cheap money are simply unavoidable parts of a capitalist economy.[4]

Mill is certainly not the only defender of cheap money who points to the inevitability of boom-bust cycles. On the contrary, most economists see booms and busts as simply part of the capitalist system, predictable and necessary crises that cannot be avoided. Thus, Joseph Schumpeter has written that business cycles "are not like tonsils, separable things that might be treated by themselves, but are, like the beat of the heart, of the essence of the organ that displays them."[5] And Arthur F. Burns, the great student of business cycles, wrote back in 1947: "For well over a century business cycles have run an unceasing round. They have persisted through vast economic and social changes; they have withstood countless experiments in industry . . . ; they have confounded forecasters without number, belied repeated prophecies of a 'new era of prosperity' and outlived repeated forebodings of 'chronic depression.'"[6] For Burns and Schumpeter, as for Mill, cheap money and the crises it engenders are part and parcel of capitalism. We have no choice, they suggest, but to accept the inevitability of crises.

The impulse to normalize the recent financial crisis by pointing to the realist inevitability of easy money, booms, and busts, harbors a danger. By familiarizing, analogizing, and making understandable the 2008 crisis in global finance, the easy money thesis also reconciles us to the crisis. It is all too easy for us today to simply shrug and say that crises are part of capitalism. To do so, to say that the crisis was caused by cheap money, is to say that there is nothing more to say. To explain the 2008 financial crisis as an inevitable by-product of capitalism is to forestall further inquiry, to overlook personal and corporate fraud, to refuse to judge individual and collective wrongs, and to abandon ourselves not simply to the vagaries of the market, but also to the misdeeds of miscreants. Above all, such an approach risks thoughtlessness.

When this crisis hit, I happened to be teaching Hannah Arendt's *The Origins of Totalitarianism*. Two of Arendt's insights struck me as having particular relevance to our present situation. First, Arendt confronted a similar phenomenon in which the crisis of totalitarianism was being normalized. The world has long known dictators. Hitler and Stalin, so it was said, were proof positive of the continuity of human frailty. Against this view, Hannah Arendt argued that it was mistaken to understand totalitarianism as simply the latest form of tyranny. Indeed, one should not understand totalitarianism, for to understand it is to normalize it and to desensitize ourselves to the fact of its extraordinary evil.

Against the effort to understand, Arendt counsels comprehension. By comprehension, she means, "the unpremeditated, attentive facing up to, and resisting of, reality—whatever it may be."[7] The factual reality of totalitarianism, as Arendt comprehended it, was that in our world today any and every evil is possible and can even be rationally justified by otherwise well-meaning people. What is needed, she argued, was that we face up to the fact that totalitarianism, genocide, and administrative massacres were now ever-present dangers in our times. Originally titled *The Burden of Our Time*, Arendt's book *The Origins of Totalitarianism* seeks not to explain totalitarianism but to face up to its singular actuality. Arendt's passion was, as she later wrote, "to think what we are doing."[8]

Crises offer particularly good opportunities to think what we are doing. A crisis "tears away façades and obliterates prejudices" and thus allows us "to explore and inquire into whatever has been laid bare of the essence of the matter."[9] When she discusses the crisis of education, Arendt affirms that the essence of education is natality—the fact that, born into a preexisting world, human beings must be educated both to fit into and also to remake that world. What we need to ask amid our contemporary crisis is: What is the essence of economics today that the crisis lays bare?

Surprisingly, since she is rarely cited as an authority on economic affairs, Arendt offers an original and thoughtful road map to think through the financial crisis, one that begins with the insight that the essence of economics is unlimited growth. In her telling, the seeds of the financial crisis are not in economics itself, but in the importation of economics into politics, or rather the dominance of infinite growth—an economic principle—in the realm of politics, where it does not belong.

Arendt develops her thesis about the dangerous subordination of politics to economics in *The Origins of Totalitarianism*. She argues that imperialism is the most important intellectual foundation of totalitarianism. At the root of imperialism is the transfer of the economic principle of unlimited growth to politics. Imperialism has its economic roots in the "realm of business speculation"—specifically the bursting of an investment bubble in the 1870s. As national entrepreneurs sought new markets, they enlisted state support for economic expansion. "Expansion as a permanent and supreme aim of politics is the central idea of imperialism."[10] The rise of imperialism, Arendt argues, means that politics becomes subservient to economics.

Arendt fears the confusion of economics and politics and especially the elevation of economics over politics. Since politics demands the imposition of limits and "stabilizing forces that stand in the way of constant transformation and expansion," she argues that imperialist expansion brought with it a grave and destabilizing threat to the political order. When politics under the sway of economic imperatives is forced to expand on the world stage, political leaders must offer ideologies that give meaning to an ever-larger, undefined, disconnected, and homeless mass, a population that replaces a citizenry. Under the economic imperatives of growth, politics becomes world politics.

It is an open question today whether politics can return to a political activity that sets moral, ethical, and economic limits on human action. The prevalence of economic and scientific thinking—thinking that by their natures evades limits—means that politics is caught up in discourses that make the central boundary-setting idea of politics immensely difficult, if not impossible. Those who, in the name of community, defend the purity of national boundaries confront the same inexorable economic laws that defeat advocates for local ownership against chain stores as well as those who defend some notion of biological humanity in the face of a seemingly inexorable advance of human implants, genetic modification, and prosthetic medicine. The economic and scientific spirit of our age supports the implacably modern maxim that whatever can be done, should be done. Thus political judgment limiting action—economic, global, or scientific—is increasingly an anachronism.

The confusion of economic and political thinking is rampant today. I refer not only to George W. Bush's claim to be a CEO president, the increasing appeal of businessmen as politicians, and President Barack Obama's pragmatism, but to the more general confusion today between prosperity and happiness. We now believe that if we achieve a certain—apparently ever-increasing—level of material prosperity, we will be happy. The welfare state is inseparably part of democratic capitalism, and politics—to a degree unimaginable in the recent past—now defines the common good as the commonwealth. Political legitimacy, as countries like China make clear, is guaranteed more by economic security than political liberty. As Michel Foucault observed nearly fifty years ago, economic prosperity "produces legitimacy for the state that is its guarantor."[11] Economics, not politics, is increasingly the foundation of modern politics.

Not only politics but also who we are—as a matter of personal identity—is defined by economic thinking. Amid productivity gains that offer riches that were unimaginable decades ago, let alone centuries ago, we continue to labor away—and not out of need. Freed from need, and yet deprived of a publicly meaningful religious, cultural, or civil life beyond economic concerns, modern economic citizens work to consume. *Homo sapiens* is replaced by *homo oeconomicus*. As economic beings, we treat ourselves as consumers. Every consumer is an entrepreneur, the CEO of his personal corporation that invests in the right schooling, training, and universities—all of which promise a certain return on the investment. Even health care, as President Obama reminds us, is justifiable primarily as a good investment in our future productivity. The economic foundation of our present worldview is so natural that we rarely today perceive its strangeness. When we hear human rights advocates proclaim that human rights is good for business or antiwar activists discourse on the economic costs of war, we forget that other cultures in other times did not reduce ethical and martial considerations to economic calculus.

Our philo-economism also obscures the fairly obvious fact that "a man does not 'by nature' wish to earn more and more money."[12] Take that statement by Max Weber seriously, and let it sink in. Throughout history, humans have wanted to live well, but they have generally sought to avoid work whenever possible; they have wanted to be rich, but they have sought wealth to attain power or to avoid work; when they have worked, they worked from need. Those who succeeded became aristocrats and paid others to work for them, so that they could pursue the more meaningful activities of politics, leisure, and pious devotion.

How did *homo oeconomicus* overcome man's natural hedonism? How did econocentrism overcome the religious prescriptions against acquisitiveness and the love of money? How did capitalism emerge as the natural and dominant way of assessing value in the world?

The most famous answer to this question was given by Max Weber in his book *The Protestant Ethic and the Spirit of Capitalism*. Put aside Weber's controversial historical thesis about the importance of Protestantism to capitalism—a thesis that Liah Greenfeld has brilliantly adopted and adapted in her book *The Spirit of Capitalism* and in her essay in this volume. At the heart of Weber's account is his claim that the rise of an unnatural and specifically capitalist ethic—to earn more and more money combined with the a strong work ethic that limits the spontaneous enjoyment of life outside of work—is rooted in the increasing rationalization of society, culture, and humanity itself. What capitalist rationality demands is that humans act according to the reason of profit and loss.