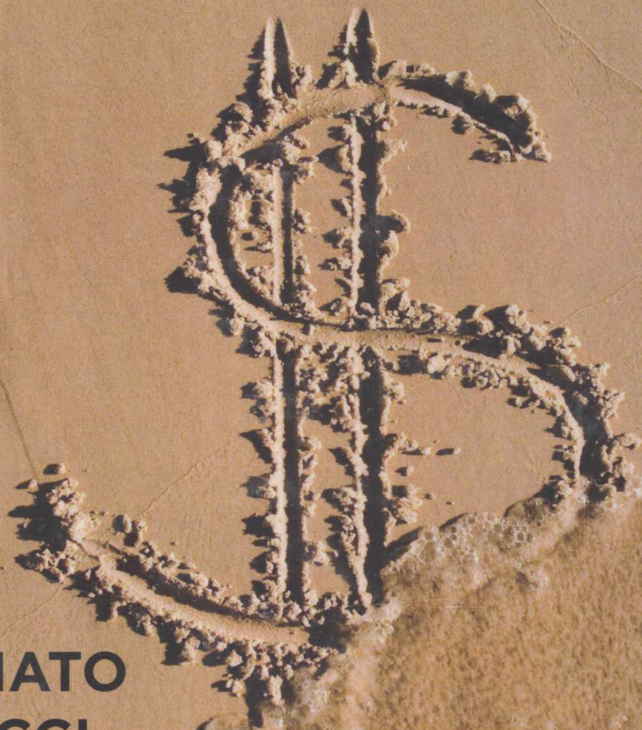
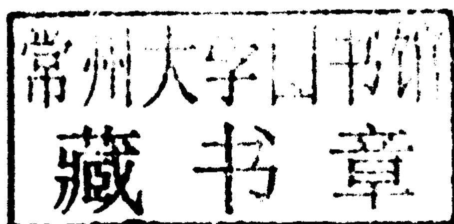


MASSIMO AMATO
LUCA FANTACCI

THE END OF FINANCE

The End of Finance

Massimo Amato and
Luca Fantacci



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Introduction

Far more than a temporary setback in an economic system with no practicable alternatives, the financial crisis that broke out in 2007 is also the crisis of a way of understanding and engaging in finance. The innovations that appeared in previous decades to promise indefinite economic growth by increasing the financial leverage and liquidity of the markets have suddenly become factors of fragility, recession and contagion.

If we take the trouble to examine it, history shows that this reversal is not only a recurrent event, but also a *permanent possibility* of the financial markets as they have built up throughout the modern era. It can, however, also show us something more. The crisis can be seen as heralding the end, not of finance, but of *one* form of it, finance based on financial *markets*, and hence the end of the idea of money *as commodity*.

On this view, the crisis is not only an event to be described or a problem to be solved, but also – and far more deeply – an *opportunity* for raising the question of reforming the system of finance and credit forcefully and for reopening discussion of the principles and ends to be taken as our starting points and goals if a truly healthy relationship between economy and finance is to prove thinkable and practicable.

The crisis affecting all of the world's financial markets during the last year, with results that are still largely unpredictable today, is accompanied by an equally disturbing loss of bearings at the theoretical level. Paraphrasing Marx, we could say that the 'practical panic' gripping the system's public and private actors for some time now has been accompanied by 'theoretical bewilderment' of a no less serious and widespread nature. Perhaps the most alarming aspect of the crisis is in fact the general and disconcerting incapacity to explain it,

or indeed even to understand what form its explanation could take. This incapacity is shared by economists, bankers, politicians and journalists, the most honest of whom have acknowledged it explicitly. As the economist Axel Leijonhufvud writes: 'There are two aspects of the wreckage from the current crisis that have not attracted much attention so far. One is the wreck of what was until a year ago the widely accepted central banking doctrine. The other is the damage to the macroeconomic theory that underpinned that doctrine.'[1]

For the most part, however, we are still left with vague assertions, which are very sketchy in their *pars destruens* and, above all, completely devoid of a *pars construens*.

In any case, the crisis has been accentuated by the difficulty, which is practical no less than theoretical, of understanding its nature. There are at least two reasons for this, the first being an almost total lack of clarity as regards the relationship that must be possible between creditors and debtors. The most recent financial innovations, for instance the securitized subprime mortgages, initially fostered *indiscriminate confidence* in debtors – who should by definition have been denied access to credit within the framework of traditional fiduciary relations – from creditors who were disposed to grant it because they were freed from the attendant risk precisely by the possibility of shifting it immediately onto a liquid market. A simple reversal of expectations was thus capable of generating, in creditors, a *general lack of confidence* towards debtors. When it is not clear where confidence is to be placed, there is rudderless oscillation between two extremes. During some periods, those with money to invest are willing to lend it to anyone at all, regardless of risk, as happened over the last ten years on a global scale. During others, they will lend only to governments regarded as reliable, or at very high interest rates, or indeed not at all, preferring to hold the cash. The 'crisis of confidence' is a crisis of the deep structures of confidence and tends to be accompanied by an indiscriminate contraction of credit, which in turn depresses investments and the economic system's prospects of growth, with obvious repercussions on expectations and confidence. In the *cyclone* of this vicious circle, a financial crisis therefore becomes real due to a structural lack of clarity about the relationship that should obtain between creditors and debtors; to be more precise and concrete, between those who must lend money and those who must spend the money lent, that is, in the final analysis, between finance and what is commonly known as 'the real economy.'

The second reason why the lack of understanding worsens the crisis is the fact that, as a result of the policymakers' incapacity to

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grasp its nature, the measures taken to find a way out of this crisis may instead simply pave the way for the next. By relying almost exclusively on unprecedented injections of liquidity, the central banks and governments have revealed their failure to understand that *liquidity is not simply an amount of money*, regardless of whether it is generated by the market, as happened during the boom, or made available by monetary authorities, as in the present crunch. What robs every intervention of its power and clarity is the failure to take into account a concept so simple that it is overlooked – first of all in economic theory. This concept can be expressed as follows: *money is not money if its circulation cannot be ensured.*

If this is how things stand, the basic problem is not the lack of money, but the possibility that all the money potentially available today is neither spent nor lent, but simply kept out of circulation, and in this sense accumulated. This is why we claim that the last resort measures adopted are to be seen, first and foremost, as paving the way for a probable crisis – a new and bigger one – rather than judged in terms of their immediate effectiveness. The monetary expansion with which the Fed, under Alan Greenspan, engineered a way out of the crisis of the new economy has in any case been recognized, albeit only retrospectively, as a fundamental contribution to the indiscriminate optimism from which the present crisis was to stem. This precedent is hardly encouraging.

If the present theoretical bewilderment is on such a scale, it might be thought that history could provide some clues, or even lessons. Our incapacity to decipher the crisis on the basis of current practical and theoretical knowledge has indeed prompted many to turn to the past. Since the beginning of the crisis, the need has been felt to find a precedent every time the economic indicators have registered a drop. This crisis thus started to be described as the worst in recent years, following the bubble of the new economy or the Wall Street crash of 1987. As the situation plummeted still further, the spectre of 1929 and the ensuing decade of depression was inevitably raised. We may in fact have something to learn from the comparison of this crisis with its most probable precedents, *but only if we ask the right questions*. The customary exercises of collective memory tend instead to assign history the task of comforting us, which is too easy and too demanding at the same time. The established retrospective readings suggest that, if we have already experienced crises, then we have also survived them. And we therefore feel authorized to conclude that all crises come to an end sooner or later. *But no one bothers to ask how and at what cost.*

If we are instead determined to respond adequately to this task of comparing, we must ask about the nature of finance. What does finance mean? What is the proper function of the financial system? What forms of the relationship between debtors and creditors are consistent with this function? How are the instruments developed by financial innovation, and the very principle of a self-styled 'democratization of finance', to be judged with respect to this function? What does it mean to say that finance must be 'at the service' of the real economy? What relationship must obtain between finance and trade? What is the role of international capital movements?

These simple questions run up against a widespread and more or less conscious tendency to avoid them. This is why we decided to make all the necessary preparations in order to pose them with all the necessary rigour.

The first part of the book is therefore devoted to a *phenomenology of finance*, through which we endeavour to show in what sense the structural characteristic of finance, in accordance with the latter's original meaning, is connected with a loan agreed upon *with a view to payment*, with a relationship between creditor and debtor constituted *with a view to a set term of maturity*, with the opening of an account *with a view to its closure* – in short, with a beginning *with a view to an end*.

Despite its apparent ambiguity, the title of this book is designed to make a precise point: the end *as purpose* [*il fine*] and the end as conclusion [*la fine*] coincide in the case of finance. It is not a question of imposing 'sound' ends on finance, but rather of recognizing that the purpose of finance as a set of economic operations regarding loans coincides with the end of such operations, which must be able to conclude with the agreed payment. In this sense, finance is designed to foster economic relations, or what Jacques Rueff aptly called 'the meeting of all debtors and all creditors'.[2]

This meeting is precisely what the financial system as we know it tends to make increasingly impossible and, above all, to prevent from taking place in accordance with due and agreed forms. The meeting does not take place in periods of crisis due to the manifest impossibility to pay debts – that is, due to the insolvency of debtors, whose bankruptcy makes their creditors insolvent too, with the risk of spreading the contagion. But it does not take place in periods of growth either, because the moment of payment can then be constantly delayed. Growth itself and the optimistic expectations it arouses have the effect of generating an expansion of credit, and hence of loans, with no regard to the effective possibility of payment, in a constant raising of the stakes.

'Delaying payments or reimbursements and causing such delays to overlap perpetually with one another: this was in short the great secret of the modern capitalist system, which could perhaps be most precisely defined as a system that would perish if all the accounts were settled at the same time.' This definition formulated by Marc Bloch, to which we will return in due course,[3] casts a piercing light on the modern history of the global financial system up to the current denouement, by suggesting that, at the root of the dangerous oscillation between euphoria and crisis, there lies a radical incapacity to perform the *exquisitely financial* function of settling accounts.

It is possible and useful to examine history on the basis of this insight. The second part of the book puts forward a thesis that makes Bloch's definition still more radical: the modern financial system not only prevents the closing of accounts, but also takes the shape of a system dispensing with any need for closure from the very outset, one in which it is possible for accounts not to be settled and for debts never to be paid. Striking evidence of this, to which we shall return at various points in the book, is the fact that our financial system rests on an *unredeemable debt* consisting of the banknotes of the central banks and, at the international level, of the dollars stockpiled in the currency reserves of the Middle and Far East.

This observation suggests another possible reading of the title, namely that the present crisis marks the end of a conception and practice of finance grounded in the systematic suppression of the end, understood as maturity and closure: here comes to its end a financial system that wants nothing to do with any end. We must therefore try to understand how it was possible for such a system to begin.

The objective pursued by the book in working its way back through the history of the western monetary and financial system is not to find comforting precedents, but to identify the key watersheds that have led up to the present situation step by step; to show that they were watersheds not through the pressure of the necessities of an evolutionary process with no alternatives, but precisely by virtue of decisions taken *and not taken* at the institutional level; and, finally, to show that the watersheds of this history are mostly connected with the overruling requirements of *war finance*.

On the one hand, therefore, the historical path winds back through the changes in the international monetary regime: from Nixon's cancellation, in 1971, of the convertibility between the dollar and gold – which in fact replaced the international currency, gold, with an unredeemable debt, the dollar – to the initial identification of gold as the international currency – which took place at the exchange fairs

of Bisenzone in order to make possible, on this basis, the emission of an unredeemable debt by the dominant military power of the time: the Spain of Philip II.

On the other hand, and in parallel with this process, our examination traces the course of financial innovation, in other words of a *securitization* that ends with ABS (Asset-Backed Securities) and CDOs (Collateralized Debt Obligations), but begins with the first forms of unredeemable paper securities: the notes issued by the Bank of England, the British government's consols, and the Spanish *asientos*.

On both sides, the history is not one of natural and progressive evolution; it is rather one of decisions taken with greater or lesser awareness, but never by chance.

Clear knowledge of the decisions behind us may help to improve our understanding of those before us and, above all, of what is at stake in this crisis and can no longer be ignored. The more strictly *political* third part of the book therefore asks how we can think of finding a way out of the crisis.

As readers will see, the focus of our considerations is on the thinkability of reform, and therefore on *reformability*, even before the individual provisions that can and must be adopted.

We will distinguish between expedient and reform in the light of the fundamental political question raised by the crisis – namely how to find a way out of the present financial system, which is based on disowning both its purpose and its conclusion, and into a financial system that may be in harmony with its truest functions. The question about reformability asks how we can inaugurate a form of finance turned upon the end/conclusion – the settlement of accounts – as its only properly economic end/purpose.

If it is to be established, such a form of finance must be thought out. Thinking finance today entails distinguishing things that are too often confused: money and credit, money and merchandise, the market economy and capitalism. And it is with respect to these distinctions that we shall put forward not only, and not so much, specific reforms but also, and rather, indications as regards what is to be reformed as well as the criteria and principles that any truly new system must be able to meet and take as its cornerstones.

Even though the need to get to grips with the financial system and its structural deficits is now commonly acknowledged, both the repeated slogans and the suggested remedies tend to remain on the surface of things. Calling for a 'new Bretton Woods' without saying what Bretton Woods represented in monetary and financial history,

or proclaiming the need for 'new rules' without asking what a rule for finance can and must be – more than anything else, these seem to be ways of concealing a basic difficulty, which concerns the apparently self-evident meaning of the term 'finance'. Everyone knows what finance is. Or at least so it seems. Nonetheless, perhaps for this very reason, nobody states clearly what it is, or what exactly in the system really needs reforming, or what exactly the rules should apply to.

This is why we set off from the simple question of what finance really is. The book's approach is therefore not evaluative. The point is not to pass judgement on the soundness or unsoundness of finance, but to ask what it is that makes a financial act economically important.

While Keynes's work has constituted an indispensable point of reference for us in this connection, it should be stressed that his theoretical and institutional project stretches far beyond its currently established interpretations. Our basic thesis is that all of Keynes's work as an economist and reformer is grounded on an idea of money differing radically from 'money as we know it' – to use an expression recurrent in the *General Theory* – in other words, as we shall see, from capitalist money. Well, the key feature of capitalist money is to be a commodity whose price – that is, interest – is determined on the money and financial markets. Therefore what distinguishes capitalism is, first of all, the fact of regarding money as merchandise.

It was against this idea of money and in favour of its radical reform that Keynes devoted all his intellectual energies throughout his entire life – and certainly not with a view to a revolutionary overturning of capitalism.

The age we are living in leads us to think that this is by no means a flaw. In fact we do not need a revolution, but something simpler and more subversive. The way out of this crisis is, first and foremost, by *thinking*; and what can make a concrete difference in the mode of thinking about finance is the ability to notice, above all, those differences that usually tend to be taken for mere variations.

The first of these radical differences masked as variations is between capitalism and the market economy. They are *not* the same thing. The market economy will always be understood in this book as the institutional place where markets are *constructed* for the *sole* purpose of making possible the exchange of economic goods and services – and where effort and inventive creativity can therefore be rewarded, labour can be recognized and recompensed in accordance with its dignity, and responsibilities can and must be assumed. Conversely, we shall endeavour to show that, in spite of any form

of economicism, capitalism is the *aneconomic* non-place where even what is not a commodity can be traded, and it is therefore possible to reap without having sown and to suffer without being guilty.

In capitalism financial crises are inevitable; in the market economy they are inadmissible. Being truly in favour of the market means starting to depart from capitalism. Departing from capitalism does not, however, mean abolishing finance. What comes to an end in this crisis is the idea of finance grounded in the representation of money and credit as commodities. We have attempted to draw all the conclusions deriving from the end of this representation, with a view to establishing a radically different institutional and theoretical perspective. The basic insight taken as our starting point is that the existence and sound functioning of a credit system capable of supporting real economic activity not only do not depend on, but are also hampered by, the idea of money as merchandise.

This insight also underpins the possibility of imagining an alternative financial system, in which money and credit are not traded and the relations between debtors and creditors are constructed so as to come to an end in payment and to give way to the production and circulation of goods; in short, a form of finance that can truly operate at the service of the market economy, or perhaps of the economy *tout court* – given that a system that can allow itself not to distinguish between what is a commodity and what is not is, quite simply, not an economy but a dangerous surrogate for one.

To conclude, a note about method and an invitation to readers. The fundamental nature of the questions addressed makes it impossible for this book to provide an exhaustive picture of the reforms that any adequate response to the crisis today would require. It has, however, enabled its authors to submit to the judgment of its readers a unifying perspective, both as regards studies already embarked upon by other scholars and with respect to further works intended to address the functioning of the financial system from a critical standpoint. In this sense, our work seeks to provide a seminal contribution, which not only can, but in a certain sense must, be followed up by more detailed studies.

A final note: all the translations of original sources are ours, unless otherwise specified, and all the quotations from works originally written in English are reproduced in their original form.

Massimo Amato and Luca Fantacci

Milan, 6 June 2009

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PART I

Phenomenology

1

Do we know what the financial markets are?

The growth of a *doxa* or general opinion increasingly favourable to financial markets and to their unrestricted liberalization appeared to have encountered no obstacles for years, if not indeed for decades. The objections had died down and the number of conversions increased, also and above all on the left. While subtle distinctions were certainly possible as regards allegiance to the new paradigm of financial globalization, that is all they were. The new order reigned triumphant, and any doubt or opposition could easily be branded as failure to keep up with the times.

In any case, the primary virtue of an ideology is to make things awkward not only for its adversaries, who may be numerous but remain captive to a counter-ideology, but also for the few dissidents. Rather than proponents of critical views, these are made to appear as no more than the advocates of a vanquished and outmoded ideology, who should be left to 'gnash their teeth' in silence. If an ideology is to aspire to 'hegemony', it is first of all essential that everything should be presented in the light of ideological juxtaposition. So it was that the collapse of an ideology so opposed to 'the market' as to feel no obligation even to think about it paved the way for a *doxa* so favourable to 'the market' as to feel no obligation to define it. It is within this self-referential dimension that the financial markets were able to find justification in ideological far sooner than in practical terms.

The outbreak of the crisis *momentarily* interrupted this self-referentiality. The ability to say something concrete about finance and its economic meaning suddenly became crucial. Was there any advantage taken of this opportunity to think? Has the crisis helped us to know a little bit more today about what finance is? Can we now claim a better understanding of that particular configuration of

finance known as the *financial markets*? In other words, can we, today, base our judgements in this field on more solid knowledge? Nearly two years after the crisis broke out, the answer is no. Why was the opportunity missed? A short chronological history of the predominant attitudes towards the financial crisis can help to find the answer.

The most widespread tendency at first was simply to deny that it was legitimate to talk about a crisis. It was, people said, a 'temporary setback' or a 'technical adjustment' on the part of the markets. 'Come on, let's not get worked up over nothing.' This was the response. There were indeed explicit warnings not to say *too much* about the possibility of a crisis in order to avoid lowering the expectations of financial agents.

In time, this approach gave way under the weight of evidence, but not to the point of complete surrender. The crisis was interpreted as a cyclical phenomenon that was bound to pass, and, above all, as nothing so serious as to call for any rethinking of the ruling model. The crisis was the price to be paid for prosperity, a sort of wildly astronomical telephone bill that *someone* had to pay every so often. But, since there was no certainty that *everyone* would have to pay, the survivors could still hope to start operating again in the best of all possible worlds.

Then came the Black October of 2008. The apologists maintained a sometimes deafening silence, and 'posthumous prophets' made their appearance. It suddenly transpired that everyone had already known that the system was untenable. This is not to say that no authoritative figures had spoken out before the fat was in the fire, to warn against the danger of financial trends that seemed to justify all the trust put in them solely by their apparent capacity for indefinite self-perpetuation.[1] The sudden glut of sages did, however, appear strange, to say the least.

This is, of course, nothing to be too surprised about in a disproportionately media-dominated society like ours, where the moulding of public opinion is no longer even connected with mechanisms of production, but rather with the constant and mobile management of widespread uncertainty – which stems in turn from a growing incapacity to master information that now affects all and sundry, from the simple 'man in the street' to the most sophisticated analyst or policymaker. In this society of pure information and widespread expectations, where what is 'true' tends to be what is regarded as such, there is a real risk of people reinventing their past in a way that becomes all the more dangerous the less it is recognized.

Thus it is that an article of faith can become an object of ridicule

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