

RECENT BOOKS ON DEGLOBALISATION AND THE ECONOMIC CRISIS

The developments that led to the implosion of the financial system in the USA went largely unnoticed by the public and the regulators. Gradually however, the prehistory of the Great Recession is being written from different perspectives. One important contribution to this body of knowledge is *Fool's Gold. How Unrestrained Greed Corrupted a Dream, Shattered Global Markets and Unleashed a Catastrophe* (338 pp, Little Brown 2009), written by Gillian Tett of the *Financial Times*.

She emphasises that many of those responsible for inventing credit derivatives were not driven by

greed, but by the conviction that these innovations would create a better functioning financial system and thus benefit the general economy. This may be especially true of the small group of bankers at J.P. Morgan – Peter Hancock, Bill Winters, Bill Demchak – who are at the centre of Tett's narrative. They did not invent credit derivatives, but developed them further and prepared the ground for a dramatic increase in the use of derivatives. When we first encounter them in Tett's book in the year 1994, most of them are under the age of 30, and strong believers in the Efficient Market Hypothesis. One of the things they found so attractive with credit derivatives

was that these instruments were not restricted by regulations.

In 1999 the group wrote a very influential manual, *The J.P. Morgan Guide to Credit Derivatives*. In the book, the authors did not express their own doubts and reservations about credit derivatives, but they later avoided the excessive risk-taking to which many of their colleagues at other banks exposed themselves.

The most remarkable thing about this whole development was that it went unnoticed for so long, Tett says. And how could these financial instruments that were so poorly understood by those who used them become so widespread and influential?

The few who were sceptical had difficulties making themselves heard. They faced a powerful establishment which included Alan Greenspan, leading academic economists and the strong lobby of the financial sector, which repeatedly managed to block attempts at regulation.

What was the role of the Efficient Market Hypothesis in the crisis? It stated that the financial markets themselves would correct imbalances and set the right prices. If this is true, regulation is unnecessary and there is no reason to fear bubbles. Justin Fox, columnist at *Time*, has written the history of this idea in *The Myth of the Rational Market. A History of Risk, Reward, and Delusion on Wall Street* (382 pp, Harper, 2009). It is an instructive and entertaining account of the complex relation between academia and Wall Street.

The Efficient Market Hypothesis can be traced

back to the years immediately after the Second World War, but the crucial moment was the formation of the "Chicago School" of economics with Milton Friedman, Gene Fama and Michael Jensen as leading economists. Their influence on economics and policy was tremendous, but in fact many of the school's central tenets were challenged already in the 1970s. As Robert Shiller puts it, the leap from the fact that it is hard to predict stock prices to the assumption that those prices must therefore be right, is "one of the most remarkable errors in the history of economic thought".

At the end of the 1990s, this hypothesis was in deep trouble even in the eyes of its central advocates. Nevertheless it continued to have considerable impact, not least on policy-makers like Alan Greenspan. His belief in the rationality of markets made him consider it superfluous to regulate the shadow banking sector, and he failed to spot the bubble in the housing market, perhaps because the hypothesis said such things simply did not occur.

This ought to be a time for critical self-scrutiny by mainstream economists. An attempt at systematic revision is made by George A Akerlof and Robert J Shiller in *Animal Spirits. How Human Psychology Drives The Economy, And Why It Matters for Global Capitalism* (230 pp, Princeton University Press, 2009). The whole notion of *homo economicus*, the rational actor, who first gathers all available information and then makes a careful analysis of the different options before making a decision, is a theoretical construction with very little bearing on reality. People's decisions are often influenced by emotions and ideas without foundation, and they easily shift between

over-optimism and panic. Above all we are social beings, and therefore inclined to be cognitive conformists – we accept as truth what other people think is true.

This of course has a profound influence on all economic activity, but as Akerlof and Shiller point out, human psychology is not so easy to quantify and feed into mathematical models. If you want to integrate emotional aspects into economic theory, you must revise your methodology, which could change the scientific identity and status of the whole discipline of economics.

Animal Spirits may very well be an influential book, since it challenges mainstream economics from within and does so in such a polite way that it is unlikely to offend anyone. It may present a clever strategy to achieve change in the discipline of economics discipline, but fundamental questions are avoided. Akerlof and Shiller carefully dodge the question of whether mainstream economics to some extent was responsible for the crisis.

The Great Recession is also a crisis for the particular variant of capitalism that many mainstream economists have favoured. Until recently it seemed just a matter of time before the rest of the world would follow in the footsteps of the USA and the UK. Today the Anglo-Saxon model has lost most of its status and this coincides with a massive geopolitical shift. The USA is gradually falling from its unique hegemonic position and as a result of the crisis Asia seems to be growing faster than predicted as a result of the crisis. In *The Post-American World and the Rise of the Rest* (292 pp, 2009, Penguin) *Newsweek* editor Fareed Zakaria attempts to explore what this new world

order will look like from an American perspective. Not so bad despite everything, is his message to his fellow Americans. It is not America that is stagnating but the Rest that are advancing, largely due to their huge populations. The USA must accept that it cannot control the world, but even in a multipolar world, the country will maintain a special position, according to Zakaria. It has better relations with all the other great powers than they have with each other, and therefore the USA can become a kind of global hub.

Furthermore, the Rest will eventually “go America’s way”, since there is basically only one way to be modern. The world is becoming more open and democratic, Zakaria claims, and if other nations want to be innovative, they should adopt American individualism with its lack of respect for authority.

If there is basically only one way to be modern, then the growing dominance of Asia will not be a dramatic change for the West. The world will continue to integrate and be dominated by a global culture. According to this view, people in the West are more modern than they are western. If there are many ways to successfully modernise and be modern, we should on the contrary expect competition and rivalry between the various models of capitalism, and they will not all necessarily be democratic. Such a global diversity, according to the Italian political scientist Giovanni Grevi, will be the consequence of the USA’s declining power (see interview on page 8). Grevi is certainly not alone in thinking along such lines.

The central argument in Martin Jacques’ book *When China Rules the World. The Rise of the*

Middle Kingdom and the End of the Western World (550 pp, Allen Lane 2009) is that there are indeed many ways to be modern and that the willingness of the Rest to imitate the West is rapidly fading. The globalisation of capitalism will not lead to a political or cultural convergence. The economic success of the Rest boosts their confidence in their own traditions and world views.

China is a civilisation that pretends to be a nation, according to Jacques. Historically, the state has had a much more dominant position than states in the West. It has not been challenged by organised religion, landowning aristocracy, military establishment or an urban bourgeoisie. The primary role of the state has been to keep the vast empire together, and in fulfilling this task it has been able to draw on vast reservoirs of loyalty from the people. The fact that China is a civilisation-state has enabled it to integrate different systems within the empire. This tradition has been a prerequisite for the pragmatic experimentation that has characterised China’s development in recent decades. The regime has tested different sets of rules in the regions and then picked the rules most suited to a general reform. China will dominate Southeast Asia, says Jacques, and in so doing it can draw on its historical experience of centralised government and regional pluralism.

What kind of relations will the different poles in this multipolar world have? There is a risk of a grab for resources that may end in confrontations. One lesson some have drawn from the food crisis of 2006–2008 is that the global market is not to be trusted. To achieve secure food supplies you must have direct control over food-producing areas. For some time now it has been said that the

territorial war is obsolete, but that suddenly appears a premature conclusion.

The only solution to the food crisis is deglobalisation, says the Indonesian sociologist Walden Bello, who claims to have coined this term a decade ago. In *The Food Wars* (176 pp, Verso, 2009), he firmly rejects many of the prevalent explanations for the food crisis. It was not caused by the demand for biofuel, nor by China’s growing appetite for meat. The main reason for the crisis has been a combination of free trade and the “structural adjustment” that the International Monetary Fund and The World Bank have been implementing since the 1980s. In the developing countries, state subsidies for the agricultural sector were abolished. At the same time, local farmers were exposed to competition from heavily subsidised Western producers and subsequently forced out of business. Countries in Africa and Asia that had earlier been net exporters of food became importers.

The global crisis brings a golden opportunity to roll back this development and return to traditional, small-scale agriculture, says Bello. The once mighty Western powers that could dictate the terms are weakened and challenged for instance by China in Africa. The goal for all countries must be food self-sufficiency and deglobalisation. There is no need to conform to a general trend, according to Bello. One size does not fit all, each country needs to find its own way.

Does this advocacy of the “peasant’s way of life” seem irrelevant? If the crisis is prolonged and globalisation primarily associated with insecurity, this vision might become attractive for large groups, perhaps even in the West.