ROBERT KUTTNER. The crash that failed.

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Review of "Crashed: How a decade of financial crises changed the world" by Adam Tooze, Viking.

The historian G.M. Trevelyan said that the democratic revolutions of 1848, all of which were quickly crushed, represented "a turning point at which modern history failed to turn". The same can be said of the financial collapse of 2008. The crash demonstrated the emptiness of the claim that markets could regulate themselves. It should have led to the disgrace of neoliberalism—the belief that unregulated markets produce and distribute goods and services more efficiently than regulated ones. Instead, the old order reasserted itself, and with calamitous consequences. Gross economic imbalances of power and wealth persisted. We are still experiencing the reverberations.

In the United States, the bipartisan financial elite escaped largely unscathed. Barack Obama, whose campaign benefited from the timing of the collapse, hired the architects of the Clinton-era deregulation who had created the conditions that led to the crisis. Far from breaking up the big banks or removing their executives, Obama's team bailed them out. None of the leading bankers whose fraudulent products caused the economy to crash went to jail; criminal prosecution took a back seat to the stability of the system. Obama's tepid program provided just enough stimulus, via a modest public-spending program and cheap unlimited credit for bankers, for a slow recovery. But the economic security of most Americans dwindled, and the legitimacy of the system was called into question. One consequence has been the rise of the far right; another is Donald Trump.

In Europe the aftermath was worse. Fragmented into twenty-eight member states, the EU could not pursue even the minimal policies of Obama. Germany had already spent some E1.3 trillion on the economic integration of the former DDR and was in no mood to underwrite the recovery of the entire continent. Germany insisted that the struggling countries had to practice austerity in order to restore the confidence of private financial markets. In a deep recession, even orthodox economists at the International Monetary Fund soon recognized that austerity was a perverse recipe for economic recovery.

But the German demands dictated policy for the continent. In addition, the European Central Bank (ECB) had neither the formal powers nor the political consent of its national masters to become a lender-of-last-resort, as the Fed has been in the US since 1932. After the crash, the Fed kept interest rates down and made credit easily available to the financial industry, which prevented the collapse from becoming a general depression. The US government took on debt to pay for services without having to raise taxes (a policy known as fiscal stimulus), and it could extend credit to keep markets liquid. But Europe, because of Germany's worries that these policies would lead to inflation, had no way to extend credit to struggling nations or to raise money through the sale of bonds, which would have allowed the ECB to provide debt relief or to invest in public services.

The political result was the same on both sides of the Atlantic—declining prospects for ordinary people, animus toward elites, and the rise of ultra-nationalism. In the US, there is at least a left-wing opposition in waiting, with a coherent explanation for what went wrong and a progressive alternative to Trumpism. Progressives have been gaining influence in the Democratic Party, and it's possible that a neo-Rooseveltian left that supports financial regulation, public investment and redistribution will come to power in 2020.

Not so in Europe. Parties such as the German Social Democratic Party, the British Labour Party and the French Socialists disgraced themselves as co-sponsors of the neoliberal formula that brought down the economy. The European left today is weaker than at any time since World War II. There is just one EU member nation with a left-wing government and a working majority in the national parliament—Portugal—and it is a tricky three-party coalition. In Greece, the radical left-wing party Syriza ostensibly leads the governing coalition, but its sovereignty has been crushed by Athens's minders in Brussels; today Syriza's policies are indistinguishable from those of the center-right. In nation after nation, the main opposition to the party of Davos is neofascism.

There have been hundreds of illuminating books on the great financial collapse. *Crashed*, written to mark its tenth anniversary, will stand for a long time as the authoritative account. In his masterful narrative, the economic historian Adam Tooze achieves several things that no other single author has quite accomplished. Tooze has managed to explain a hugely complex global crisis in its multiple dimensions, and his book combines cogent analysis with a fascinating history of the political and economic particulars.

In Tooze's account, the survival of neoliberalism is one of several related ironies. Before the crash, economists had thought that the next crisis would be caused by America's budget deficit and its trade deficit, as well as the shakiness of its co-dependency with China, which both benefited from the trade deficit and bought Treasury bonds to offset it. But when the collapse came, it was "a financial crisis triggered by the humdrum market for American real estate".

The US housing bubble was pumped up by subprime mortgage derivatives that allowed lenders to sell off high-risk loans homeowners were unlikely to pay back. These were invented on Wall Street beginning in the 1980s, accepted by US regulators, and disseminated like financial toxins globally. And this raises a further irony. The crisis was thought by many Europeans to have shaken American financial hegemony and the dominant status of the US dollar. Tooze begins his tale at the annual convening of the UN General Assembly in New York on September 23, 2008, a week after the collapse of Lehman Brothers. "One after another, the speakers at the UN connected the crisis to the question of global governance and ultimately to America's position as the dominant world power," he writes. French president Nicolas Sarkozy poured scorn on the Americans: "It's a multipolar world now." Yet as Tooze explains, the collapse reinforced the financial supremacy of Washington and New York. "Far from withering away," he writes, "the Fed's response gave an entirely new dimension to the global dollar."

Distilled to its essence, the crisis was an implosion of bank balance sheets. Commercial and investment banks had gotten overleveraged—carrying too much debt—and were borrowing money in overnight markets to invest in exotic securities that were themselves

overleveraged. When the entire structure of borrowed money collapsed, the losses more than wiped out all the capital of the banking system—not just in the US but in Europe, because of the intimate interconnection (and contagion) of American and European banks. Had the authorities just stood by, Tooze writes, the collapse would have been far more severe than the Great Depression: “In the 1930s there was no moment of such massive synchronization, no moment in which so many of the world’s largest banks threatened to fail simultaneously.”

Fed Chairman Ben Bernanke, a scholar of the Great Depression, understood the stakes. While insisting to Congress that the emergency response was mainly to shore up US finance, Bernanke turned the Fed into the world’s central bank. “Through so-called liquidity swap lines, the Fed licensed a hand-picked group of core central banks to issue dollar credits on demand,” Tooze writes. In other words, the Fed simply created enough dollars, running well into the trillions, to prevent the global economy from collapsing for lack of credit. This response, he observes, “contradicted the conventional narrative of economic history since the 1970s,” which claimed that markets thrived when states refrained from regulating them. Bernanke instigated government action on an unimagined scale to prop up a private system that supposedly did not need the state. How to explain the contradiction? The state had been hijacked by private finance—both in the permissiveness that caused the crash and in the subsequent policies that contained it but did little to spoil the bankers’ party.

Tooze is especially good at explaining the many Fed inventions that pumped trillions of dollars into every obscure corner of the financial industry. He demystifies the impenetrably technical contrivances used by both private companies and central banks. Tooze computes the staggering sums, running into the tens of trillions of dollars. Using deposit guarantees, loans to banks, outright capital transfers, and purchases of nearly worthless securities, the Fed and the Treasury recapitalized the banking system. To camouflage what was at work, officials invented unlimited credit pipelines with disarmingly technical names.

The Term Auction Facility, for instance, provided banks with funds they could no longer get in the frozen market for commercial paper—unsecured, short-term corporate loans—eventually committing a total of $6.18 trillion. To restart that market, the Fed invented the Commercial Paper Funding Facility, which pumped $737 billion into it. The largest beneficiary was the Swiss bank UBS. Virtually unlimited capital also guaranteed funding for retail stockbrokers and much more. The blandly named policy of quantitative easing, which drove interest rates down to almost zero, was a euphemism for Fed purchases of immense quantities of private and government securities.

The crisis, Tooze writes, “was a devastating blow to the complacent belief in the great moderation, a shocking overturning of the prevailing laissez-faire ideology.” And yet the ideology prevailed. Homeowners, both those defrauded by subprime mortgages and millions of others whose houses were suddenly worth less than their debt, were the real victims of the collapse. But they got little help. In a reversal of New Deal priorities, most of the relief went to the biggest banks, while smaller banks and homeowners were allowed to go under. Obama’s $75 billion mortgage-restructuring programs, known as HAMP and HARP, were used to benefit bank balance sheets, not hard-pressed homeowners, as intended by Congress. Banks were permitted to invent complex

provisional loan “modifications” with opaque terms that favored lenders, rather than using their government subsidies to provide refinancing to reduce homeowner debts.

The Dodd–Frank Act, passed in 2010 and meant to limit abuses in the financial industry, was too weak to begin with, and its implementation was largely crippled by the industry’s influence, years before Donald Trump’s deregulatory crusade. Long before the recession was over, the budget hawks around Obama, who opposed government spending, succeeded in prematurely changing the administration’s priority from recovery to deficit reduction. So compromised was the administration that the financial commentator Rick Santelli, speaking from the Chicago Board of Trade in 2009, could depict the bailout program as a corrupt alliance between the liberal rich and the undeserving poor meant to defraud middle-class Americans, and then issue the first call for a new Tea Party.

How did a nominally center-left administration, elected during a financial crisis caused by right-wing economic ideology and policy, end up in this situation? Tooze reminds us of the Hamilton Project, a small unit at the Brookings Institution created in 2006 by Robert Rubin, former co-chairman of Goldman Sachs and Clinton’s treasury secretary, and his protégés. The project, which had substantial influence on Obama’s thinking, his program, and his appointees, promoted budgetary orthodoxy, no interference with Wall Street, and small-scale social investment initiatives such as retraining programs and support for small business. “When the economists linked to the Hamilton Project envisioned disaster,” Tooze writes, “they worried about excessive public debt, underperforming schools and a Chinese sell-off. What they did not put in question was the basic functioning of the American economy, its banks and financial markets.”

Turning to Europe, Tooze explores the fatal combination of Germany’s demands for austerity with the structural weakness of the ECB and the vulnerability of the euro. In Europe, because of bad policy, the implosion of private financial assets led to a crisis of sovereign debt. Before the collapse, cheap debt caused risky investments to flow into Southern Europe. Countries such as Greece and Italy had, before the introduction of the euro in 1999, been prone to inflation because of high deficits, and the governments, corporations, and citizens of those countries had been made to offset the risk of devaluation by paying higher interest rates to lenders. But in the 2000s there was no risk of devaluation; Portugal or Greece now enjoyed interest rates that were only slightly higher than Germany’s, and markets failed to take account of the risk of default, which was more serious than that of devaluation.

After the crisis began, misguided responses compounded the damage. In Ireland, a badly corrupted government took bank losses onto the state’s own balance sheet, suddenly putting Ireland in receivership to Brussels and Berlin, which provided capital in exchange for stringent conditions. In Greece, before the crash, the budget books had been altered by a center-right government (with help from Goldman Sachs, which created special securities that allowed Athens to disguise the increased public debt). In 2009 the newly elected social-democratic government of George Papandreou and his Pasok party dutifully reported the faked books and the real numbers to Brussels and the world. Greece’s budget deficit was not 3.7 percent, as the outgoing government had falsely claimed. It was more like 12 percent, or four times the permitted limit under EU rules.

Financial markets responded by speculating against Greek sovereign debt, requiring Greece to pay much higher interest. But instead of treating the Greek situation as a crisis to be contained and helping a genuinely reformist new government find its footing, Brussels and Berlin treated Greece as an object lesson in profligacy and an opportunity to insist on punitive terms for financial aid. This mainly served to bail out Greece's creditors and pushed the Greek economy deeper into depression. To qualify for the meager program of what Tooze terms "extend and pretend" from the EU, the ECB, and the IMF, the Greeks were made to pursue excruciating cuts in public services and pensions as well as auctions of public assets at fire-sale prices. At one point in the austerity bargaining with the Greek government, Tooze reports, the German finance minister, Wolfgang Schäuble, "suggested that perhaps it would be better for the Greeks not to hold elections." Schäuble knew how unpopular these policies were. His words suggested that he would sacrifice Greek democracy in order to get the Greek government to accept the austerity demands. This was a coerced version of the neoliberalism that had already been discredited by the collapse.

A central player in this tragedy was the European Central Bank. Tooze does a fine job of explaining the delicate dance between the bank's leaders and its real masters in Germany. Since Germany opposed continent-wide recovery spending, the bank could only pursue monetary policy. The model was the Fed. Yet while the Fed has a congressional "dual mandate" to target both price stability and high employment, the ECB's charter allowed for price stability only. In the Maastricht Treaty, which was signed in 1992 and created the euro, Germany's requirement for giving up its cherished deutsche mark was an agreement that the euro would be protected from inflation. The ECB inherited the Germans' fear of inflation. The treaty was made even more austere by the 2011 fiscal compact demanded by Merkel, which added more penalties to enforce the limits placed on debts and deficits. Thus Greece, a nation hit by severe recession and loss of private investor confidence, had no choice but to pursue austerity to reassure creditors.

A central bank with the prerogatives of the Federal Reserve might have prevented this outcome. But the ECB could not legally purchase the sovereign debt of member nations. The first two presidents of the ECB, the Dutchman Wim Duisenberg and Jean-Claude Trichet of France, took pains to be more German than the Germans. In 2011, however, Mario Draghi of Italy got the job. Draghi was far from a radical. He was trained at MIT and had spent three years as a managing director at Goldman Sachs. Draghi, a foe of inflation, had been viewed as the most "German" of the available candidates. But as the crisis deepened, he gradually expanded the boundaries of the ECB's remit, cutting interest rates and making two rounds of loans to European banks. In 2012, Tooze recounts, Draghi, speaking off the cuff in an urgent effort to reassure markets, declared that the ECB "is ready to do whatever it takes to preserve the euro."

Nobody was sure what that meant, not even Draghi. "As usual, the inflation hawks at the Bundesbank were aghast at the idea of ECB bond buying," Tooze tells us. "But for Merkel it was the better of two bad options." The ECB, with the consent of the Germans, came up with one of those bland-sounding names, Outright Monetary Transactions, for its direct purchases of government bonds. But the program, at the insistence of the Germans, was restricted to nations in compliance with Merkel's rigid fiscal terms, which limited national deficits and debts. In other words, the money could not go to the very nations where it was

needed most, since the hardest-hit countries had to borrow heavily to get themselves out of the recession. And so, despite Draghi, Europe continued to tread water rather than make progress toward recovery. The banks, however, survived.

Tooze excels at explaining the byzantine political bargaining that led to policy compromises that avoided outright depression but stifled the European economy. These were the consequences of shifting alliances among national leaders, with the French, Italians, and Spanish, who were less opposed to inflation, against the conservative Germans and Dutch, as well as complex infighting within the political leadership in individual nations. The infighting was compounded by the interests of different national and international politicians and institutions, above all the banks. Much of the pressure was on Merkel, whipsawed between her own fiscal conservatism, the hostility of the German electorate to bailing out the supposedly profligate southern nations, and her need to hold the EU together. At one excruciating all-night negotiation at which she felt ambushed by other national leaders, Tooze reports, Merkel broke down and declared, "*Ich will mich nicht selbst umbringen.*" (I do not want to kill myself.) Reading Tooze, you realize that it's a miracle that the EU and the euro survived at all—but they did so at terrible human cost.

Crashed does have some minor blemishes. One is its structure. Tooze generally proceeds chronologically. For the most part, this strategy works. However, because he picks up, drops, and then resumes several important subplots—such as the euro, the Fed, and China—the text occasionally loops back on itself, leading the reader to wonder, "Didn't I read this before?" Conversely, there are some aspects of the story that are omitted or glossed over. For example, the ideal of liberalized trade, and the use of trade treaties to promote deregulation or privatized regulation of finance, is a major element of the story of how neoliberal hegemony promoted the eventual collapse. But except for a passing reference, trade and globalized deregulation get little mention here.

Similarly, while Tooze writes extensively about the central bankers Ben Bernanke and Mario Draghi, he has almost nothing to say about Janet Yellen. Her nomination as Fed chair in 2013 to succeed Bernanke was an epochal event and an improbable defeat for the proponents of austerity, deregulation, and bank bailouts who influenced Obama's policymaking. Yellen, a left-liberal economist specializing in labor markets, was the only left-of-center Fed chair other then FDR's chairman Marriner Eccles. She also believed in tough regulation of banks. The extension of quantitative easing well beyond its intended end was substantially due to Yellen's concern about wages and employment, and not just price stability, since low interest rates can also help promote recovery.

The story of how Yellen got the job is also emblematic of deeper power struggles. Obama had all but promised the Fed chair to Larry Summers, who dearly wanted it. But the newly elected progressive senator Elizabeth Warren, who had tangled repeatedly with Summers in her previous position as chair of the Congressional Oversight Panel for the bank bailout program, organized fellow Senate Democrats to warn Obama that Summers would not be confirmed. Warren and the liberals also openly lobbied for Yellen. In Tooze's book, we first meet Yellen in passing on page 503, in a brief reference to the gradual phase-out of quantitative easing, with no explanation of how she got to the Fed or who she was, and not much on her subsequent work.

Another odd omission is the savings and loan scandal of the 1980s. Tooze writes only that many savings and loans went broke in that decade because, while they lent money at fixed rates, they had to pay rising interest rates on deposits from consumers. But far more important were their reckless speculative investments, which had nothing to do with mortgages, plus their excessive borrowing, allowed by the Garn–St. Germain Act of 1982, for which the savings and loan industry had lobbied. The folly was compounded by extensive corruption, for which hundreds of savings and loan executives were criminally prosecuted. The scandal prefigured the deeper corruption to come.

What, finally, are we to make of this saga? Tooze ends the book with a short chapter called "The Shape of Things to Come," mainly on the ascent of China, the one nation that avoided all the shibboleths of economic and political liberalism, though it also, of course, does not have a political democracy. But as Tooze reminds us, coalitions in the US that fought for government oversight of capitalism prevented the disasters of laissez-faire policies, making "The difference between the Treaty of Versailles and the Marshall Plan, or Herbert Hoover's and FDR's responses to the Great Depression." He aptly adds, "The political in 'political economy' demands to be taken seriously."

Robert Kuttner is cofounder and coeditor of The American Prospect, and a professor at Brandeis's Heller School.

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