

Finance and debt in the global economy: a crisis for development



A talk given by Nick Dearden, Director of Global Justice Now, 5th March 2019 at the University of Chester. Event jointly arranged between International Development Studies at the University and Chester World Development Forum. The talk drew on Nick's article published in the magazine "Ninety-Nine" in October 2018, which is reproduced here in full.

#10YearsOn

Ten years have passed since the defining moment of the financial crash: on 15 September 2008, investment bank Lehman Brothers collapsed. The financial system froze and political elites stared into the abyss. Those who had believed the market to be infallible suddenly rediscovered the power of the state – to print money in unimaginable quantities, to take private corporations into public ownership, and to bail out those whose anti-social activities had created this mess.

Ten years on, what can we learn? Today, the financial markets are as powerful and as reckless as ever. They could inflict another crash on us tomorrow.

Indeed it was the failure of our leaders to control big finance, and instead push the bill for the crisis onto the rest of society through radical austerity, which has led to the political crisis we now face: Brexit, Trump and the fascists in the Italian government.

But big social change rarely happens overnight. The financial crisis has killed the idea that 'the market knows best'. There is no going back to the day before Lehman Brothers collapsed. And if we are to have any hope of regaining lost ground, we must learn the lessons of the financial crisis.

The coming debt crisis

Though extreme, the 2008 financial crisis is far from unusual. I was in Quito, Ecuador, on 15 September 2008. Appropriately enough, I was there to celebrate Ecuador's 'debt audit', a process through which Ecuador meticulously examined the debts it had accrued through previous financial crises.

The audit, sanctioned by Ecuador's radical president Correa, was a lesson in how the financial system works, and how an overly-powerful financial system benefits the very wealthy, and fuels inequality in society. Such a system is also prone to crisis, and when these crises come, the debts created by a tiny section of society are forced onto the rest of us, with the poorest bearing the greatest weight of all through austerity, privatisations, and massive debt repayments.

Ultimately Ecuador found that as long as finance is out of control, we can never be 'all in it together'.

Ecuador's government used the audit to wipe out billions of dollars worth of 'illegitimate debt', and it put in place new laws to control finance. Sadly, those lessons were not learnt by the vast majority of countries that plunged into recession and debt on 15 September 2008.

Financial power, crisis and inequality

The financial crisis was rooted in a global economy which had come to worship financial power. It's no surprise that those countries most committed to 'financialisation', like the US and UK, fell victim of the crisis first.

Financialisation refers to a process whereby finance becomes an end in itself, rather than helping businesses invest or helping governments build better countries. 'Investments' increasingly become short-term speculative bets, driving prices up or down simply to profit, achieving nothing productive along the way. New ways of speculating are constantly being invented (collateralised debt obligations, subprime mortgages, high frequency trading) to allow more money to be made, faster, and with hugely destabilising effects on the wider economy.

But this isn't just about bigger banks and hedge funds. Finance infects the rest of the economy with its 'make a quick buck' logic. The 'real' economy is increasingly forced to behave in the

same way in order to attract investment. So, for example, supermarkets, mobile phone companies, or car manufacturers increasingly profit from financial trading, from extending credit, from 'renting' airspace, rather than from producing real things.

Households are affected too, as more and more people live on credit, paying interest and rent directly into an already bloated financial sector. Even public institutions like universities start to think like hedge funds, as they are drained of public money and forced to compete for investment by, for instance, selling bonds on the market.

For global justice campaigners, three things stand out. First, such an economy is increasingly short-term in its thinking, making long-term development impossible. Whether it be workers, farm land, or ecosystems, finance will act as a giant extractor, exploiting anything for short-term gain.

Second, such a system is deeply crisis-prone. The post-war period of more regulated finance saw very few financial crises, compared to the explosion of crises as finance was deregulated from the late 1970s onwards. Needless to say, these crises are bad for development, especially when used to impose radical austerity and economic restructuring on society.

Finally, financial power is inseparable from inequality, the great scourge of our world today. That's because financial power benefits those who already have assets and wealth. Just look at the astronomical rise in property prices over the last 20 years. Then compare that with the stagnation of ordinary people's wages. The only thing that hides this inequality is the debt which has allowed so many to participate in the consumer economy. But when the debt dried up in 2008, everyone could clearly see what had happened to our society. We had become the 'haves' and the 'have nots'.

From 'third world' to first world debt crisis

It was a financial crisis in the late 1970s which triggered one of the most significant events in the last 50 years – though you'll be lucky to learn about it in schools or universities. The 'third world' debt crisis was sparked in 1979 when reckless banks, which had been happily boosting their profits by lending to developing world countries, including many unsavoury dictators, suddenly raised interest rates to stave off inflation.

Starting with Mexico in 1982, dozens of countries were brought to the verge of default. But rather than taking control of the well-known high street banks that had lent the money, and forcing investors to take the hit, western governments effectively bailed out the banks using public institutions like the International Monetary Fund (IMF) and World Bank.

The banks went free, profits intact, while the poorest people in the world paid the price for their reckless lending. From Latin America to Africa to Asia, the IMF imposed 'structural adjustment' policies on dozens of countries. Governments were told that if they imposed austerity, privatised public services and liberalised trade and investment, they could pay 'their' debt and their problems would be over.

This wasn't true. While the world of finance boomed as a result of these new policies, those struggling to make ends meet found their economies destroyed, their education and healthcare devastated, their communities hollowed out. More than 50 countries were pushed into the most extreme poverty. The voices of these countries, many of which were calling for radical economic reform at an international level, was undermined from that moment on. The richest countries used financial power to reimpose the old relationships of Empire.

And the crises continued, throughout the 90s, as financial deregulation, the beating heart of globalisation, was pushed by politicians. Countries including Thailand, Indonesia, Brazil and Russia were devastated by financial crises, as 'hot money' poured into economies, inflated asset bubbles, and then withdrew, collapsing economies and leaving millions of people jobless and impoverished.

The crisis this time

The 2008 financial crisis was bigger. It should have been a wake-up call. Now, financial deregulation wasn't just destabilising Thailand or Brazil or Russia, as they had in the 1990s, but the US and UK.

And for most of us, the crisis did indeed expose all the injustices of the 'market knows best' economy. We marched with the trade unions in the 'Put People First' protests. Oxfam told the world that the result of this financialised system was that the eight richest men in the world had more wealth than the bottom half of the world's population. The Occupy Movement took over public spaces throughout Europe and the US, while UK Uncut sat down in high street shops demanding they paid their taxes.

Even some politicians seemed to get it. "Financial markets cannot govern us!" proclaimed a group of European leaders "This crisis is a failure of poorly, or unregulated markets, and shows us, once more, that the financial market is not capable of self-regulation. It also reminds us of worrisome escalating income discrepancies in our societies." Surely, this was time for change?

So what happened? As banks started to fall, the system of toxic bets and debts unravelled. The US and British authorities saw complete collapse ahead. To save the banks, massive bail outs were organised. To stop the system seizing up, 'quantitative easing' pumped vast sums of money into the economy and interest rates fell to near zero.

These policies were not totally wrong in themselves. To some degree they helped forestall a deeper depression still. But they were nowhere near radical enough. They helped saved the system, not change it.

As money poured into the banking system, it was all too often used to shore up balance sheets and allow more unregulated flows of 'investment' around the world. The nationalisation of large swathes of banking wasn't used to force banks to adopt a different model – of long term investments aimed at definancialising the economy. With a few honourable exceptions, such as Iceland where popular protest brought down the government and forced politicians to use new money to reduce the debts of ordinary people, the banking sector carried on as normal.

In most of Europe, the picture was reminiscent of the 'third world' debt crisis. Time and again, the private debts of the banks was pushed onto the public sector – in Spain, Italy, Portugal, Ireland and even Britain. They were then 'paid' by the poorest in society, through eye-watering levels of austerity and privatisation.

Greece, the most severe case, was forced into one of the longest depressions in history. While cancer patients had to buy their own medicines, and the Red Cross warned of a humanitarian emergency, Greece's economy was sold off to the very banks and hedge funds that had created the financial crisis. Where democratic governments refused to follow the orders of the European Central Bank, they were replaced by unelected regimes to carry through the process.

The system was saved to stagger on a few more years, but at a terrible cost. The inequities of that system continued to grow. In the US, in the 5 years following Lehman's collapse, 95% of income gains accrued to the top 1%. The New York Times reported, very conservatively, that the average income of the richest 1% rose from \$871,100 in 2009 to \$968,000 by 2013. The remaining 99% saw their incomes fall – those at the bottom most sharply of all.

Meanwhile, investors flooded into African markets to achieve better returns than they could in the West. The 'African miracle' was proclaimed. Doubtless some of this investment was well used. But by and large it simply fuelled the crisis-prone financial economy. Today Africa faces a new debt crisis. In sub-Saharan Africa, Jubilee Debt Campaign has found that outstanding debt doubled between 2008 and 2016, to \$450 billion dollars.

Faced with growing inequality, serious poverty even in rich societies, a failure to hold those who created the crisis to account, and a lack of solutions from the centre left parties, anger grew. The breeding ground for xenophobia and the politics of hatred had been created, just as the financial crash of 1929 fed into fascism into Europe.

Without very substantial change, it will continue to grow. Our task has never been more urgent.

The world we want to see

How can we get out of this mess? If the problem is financial power, then surely the answer must be definancialisation. This entails, of course, serious financial regulation. But we're still heading in the wrong direction, and Trump is tearing up even Obama's tepid reforms, while finance in

Europe is begging for more freedom. We must make sure banks are forced to behave responsibly, to think long-term, and to shrink. The establishment of public banks and support for cooperatives and local banks, serving local community needs, is vital too.

We must reverse the trend of introducing financial markets into every aspect of life by building strong, democratic public services and public institutions. Short-term profit maximisation has no useful role to play in the provision of healthcare or education. But neither does it play a useful role in creating a sustainable energy system, in building good quality housing for all, developing new medicines, or even in developing the new technologies which will underline the economy of the future. We must look to new forms of ownership, even reinventing the 'commons' as a system of collective ownership and control over large swathes of our economy.

Globally, we must stop finance super exploiting everything in the world. Rather than telling southern governments 'you need more investment, let the market work its magic', we need to support them in regulating and taxing that investment, which is the only way to make investments genuinely useful for a country, and to support countries in building domestic economies rather than serving the demands of global capital. Rather than encouraging more unregulated capital flows, aid could be used to help the construction of public services, local economies, taxation and regulation.

None of this is utopian. Here in Britain we carried out a similar task after the second world war when we recognised that the financial markets had failed to produce the healthcare, the education and the housing which people in our country needed to live a dignified life. Poverty was slashed, inequality shrunk, crises were reduced. But we can't sit back and wait for the political establishment to come to its senses. There are many vested interests who oppose these policies, and large sections of the establishment would rather whip up racism and xenophobia than challenge those interests.

Only serious pressure from below can ensure real change happens. That's the long-term battle we're engaged in. All big change is pushed from below, none of it happens quickly. Even the best politicians in the world cannot deliver transformative policies without activists prepared to support but also push them.

And the change must be international. It's understandable that at this moment politics has become very domestically-focussed. But the big changes we need can't happen only at that level, they must be global. You can't make life better in Britain by trampling on the rights of those elsewhere.

Early in the crisis, it looked like Southern countries might finally get more say over the future of the global economy, something they've been denied since the last 1970s. The UN General Assembly elected the late Rev Miguel d'Escoto Brockmann, a left-wing Nicaraguan priest as their president, and he presided over a process which tried to lay out a different pathway for the global economy.

Ultimately d'Escoto's efforts were quashed by the power of the rich countries and institutions like the IMF, but his determination to push for a voice for the hundreds of millions of voiceless was heroic and his refusal to accept a world dominated by finance should inform our battle against injustice today. As he said: "The anti-values of greed, individualism and exclusion should be replaced by solidarity, common good and inclusion. The objective of our economic and social activity should not be the limitless, endless, mindless accumulation of wealth in a profit-centred economy but rather a people-centred economy that guarantees human needs, human rights, and human security, as well as conserves life on earth. These should be universal values that underpin our ethical and moral responsibility."

The financial crisis signalled the slow death of the financialised economy. It's up to us to build something better.