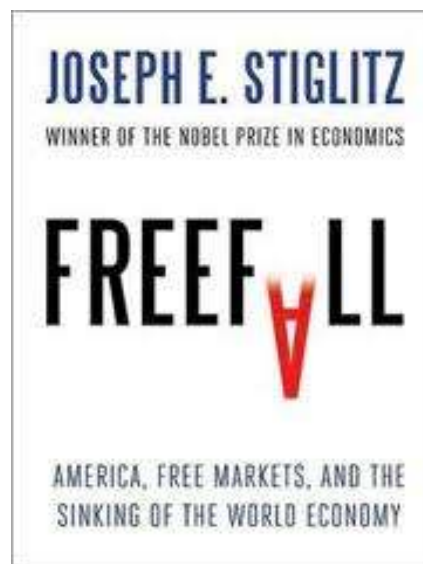


Stiglitz on capitalism in freefall

Reviewed by Bruce Duncan

Joseph E Stiglitz, *Freefall: America, Free Markets, and the Sinking of the World Economy* (New York: W W Norton & Co., 2010), pp. xxx + 361. It has extensive footnotes but no index.

Among the many analyses of the Global Financial Crisis, Joseph Stiglitz's *Freefall* is one of the most outstanding. It traces how the crisis occurred, despite urgent warnings from himself and others (including Nouriel Roubini, George Soros and Robert Shiller), and gives a stinging indictment of the ideology behind the free-market policies that impelled the economic catastrophe. "This book is about a battle of ideas, about the ideas that led to the failed policies that precipitated the crisis and about the lessons we take away from it" (p. xii). Like John Maynard Keynes, Stiglitz argues that markets do not work well on their own, and require astute regulation.



Stiglitz writes with great authority on these economic questions. Currently a professor of economics at Columbia University, he has been awarded the Nobel Prize in economics and was former senior vice president and chief economist at the World Bank during the crisis of 1997-98. Far from global financial systems working well in recent decades, he notes that by one account there have been 124 economic crises in developing countries from 1970 to 2007.

Stiglitz is particularly critical of the economics profession, "for it provided the special interests with arguments about efficient and self-regulating markets – even though advances in economics during the preceding two decades had shown the limited conditions under which that theory held true" (pp. xx-xxi). Warnings were ignored, since "too much money was being made by too many people" (p. 18). "Free market ideology turned out to be an excuse for new forms of exploitation". (p. 221). He laments that he saw "too many of our best students going into finance. They couldn't resist the megabucks." (p. 276).

"Many of us would not like to think that we conform to the view of man that underlies prevailing economic models, which is of a calculating, rational, self-service, and self-interested individual. There is no room for human empathy, public spiritedness, or altruism." (p. 249).

Stiglitz focuses his criticism on the disciples of Milton Friedman in the economics profession. "Economics had moved – more than economists would like to think – from being a scientific discipline into becoming free market capitalism's biggest cheerleader." (p. 238). Some former communist countries "replaced Karl Marx with Milton Friedman as their god. The new religion has not served them well." (p. 225).

“Economics, unintentionally, provided sustenance to this lack of moral responsibility. A naïve reading of Adam Smith might have suggested that he had relieved market participants from having to think about issues of morality. After all, if the pursuit of self-interest leads, as if by an invisible hand, to societal well-being, all that one has to do – all that one should do – is to be sure to follow one’s self-interest. And those in the financial sector seemingly did that. But, clearly, the pursuit of self-interest – greed – did not lead to social well-being...” (p. 281).

Given the multiple failures in the financial system, Stiglitz is insistent on the government playing a greater role in regulating and sustaining the economy: “the financial crisis showed that financial market do not automatically work well, and that markets are not self-correcting” (p. 185).

Stiglitz quoted Friedrich Hayek: “‘Probably nothing has done so much harm’ to the market advocates’ cause as the ‘wooden insistence... on certain rules of thumb, above all of the principle of laissez-faire capitalism’”. Hayek argued that government had a role to play in diverse areas, from work-hours regulation, monetary policy, and institutions to the follow of proper information.’ (p. 273).

The author is also caustic about the role of international institutions in handling the current crisis, particularly the IMF which “had pushed deregulatory policies, including capital and financial market liberalization, that contributed to the creation of the crisis and to its rapid spread around the world.” (214). He argued that the IMF had imposed “harsh conditionalities” on developing countries “that had actually made the downturns in the afflicted countries worse. These conditions were designed more to help Western creditors recoup more of their money than they otherwise would have been able to, than to help the afflicted country maintain its economic strength.” (p. 215).

Stiglitz continued that America seemed to take little responsibility for “having created the global mess in the first place.” (p. 216). The IMF and the World Bank “pushed market fundamentalism (neo-liberalism,” it was often called), a notion Americans idealized as “free and unfettered markets.” They pressed for financial-sector deregulation, privatization, and trade liberalization” (p. 220), while the advanced industrial countries facilitated “corruption by providing safe haven for corrupt officials and secret bank accounts for their money.” (p. 217).

Among his suggestions for rebuilding the global economy on sounder foundations, Stiglitz argues strongly for a new global reserve currency to replace the US dollar. This would mean that developing countries no longer had to maintain huge reserves of currency in the event of a crisis, and that these funds could be released to pay for urgently needed spending on services and infrastructure, thus increasing global demand, and helping eliminating the need for countries to strive for large trade surpluses. “Poor countries are lending to the United States hundreds of billions, indeed trillions, or dollars at a low (in 2009, near zero) interest rate... The value of the implicit foreign aid that the United States receives, in being able to borrow at a lower interest rate than it otherwise would be able to, exceeds by some calculations, the total value of the foreign aid that the country gives.” (p. 232).

Stiglitz insists on the fundamental issues in economic decision-making involve moral dimensions, which the neo-liberal ideology that had captured many economists fatally ignored. “[We] should take this moment as one of reckoning and reflection, of thinking about what kind of society we would like to have... We have gone far down an alternative path – creating a society in which materialism dominates moral commitment, in which the rapid growth that we have achieved is not sustainable environmentally or socially, in which we do not act together as a community to address our common needs, partly because rugged individualism and market fundamentalism have eroded any sense of community and have led to rampant exploitation of unwary and unprotected individuals and to an increasing social divide.” (p.275-76).

Few writers can address these complex issues with such competence, clarity and credibility as Stiglitz. If the world is to avoid repeating the financial crisis a few years down the track, then world leaders will need to pay close attention to the diagnosis in *Freefall*. ♦