Stiglitz on reforming the global economy

Reviewed by Bruce Duncan


Joseph Stiglitz has emerged as one of the foremost economists today and in this 2010 Report has detailed what needs to be done to reform the international architecture of economic institutions to advance better social outcomes, social equity and sustainability.

In 2008, the president of the UN General Assembly, Miguel D’Escoto Brockmann, asked Stiglitz to chair a Commission of Experts on the global economy, and particularly to advise the June 2010 UN Summit on how to address the problems arising from the global financial crisis, the threat from climate change and the challenge of world development. This book is the outcome of their deliberations.

Stiglitz visited Australia in 2010 and spoke in various capital cities (available on the net). He won the Nobel Prize for his analysis of how deficiencies in access to market information undermine the operation of supposedly free markets. Currently professor of economics at Colombia University, he has been senior vice-president and chief economist at the World Bank, and president of the council of economic advisors to President Clinton. His prodigious writings include *Globalization and its Discontents*, *The Three Trillion Dollar War*, *Making Globalization Work*, and *Freefall*, on the global financial crisis.

In his preface, Stiglitz reiterates his critique of neoclassical economics and the neoliberal philosophy that extolled free markets as automatically leading to optimal outcomes. “The crisis exposed deep flaws in notions of market fundamentalism, the theory that unfettered markets would lead to efficient and stable outcomes. So too the idea that markets could be self-regulating was shown to the oxymoron that it was.” Even the Financial Stability Forum was “guided by some of the same flawed economic models and philosophies, and not surprisingly failed to prevent” the global financial crisis. (p. ix).

Stiglitz highlights the moral culpability involved in the catastrophe that befell many developing countries as a result of the economic crisis: “the developing countries
were innocent victims of America’s mismanagement of its economy”. Moreover, the United States “had foisted on unwary developing countries liberalization policies without appropriate safeguards. These policies had exposed the developing countries to enormous risk; but the developing countries still did not have the resources to deal with the consequences.” (p. x).

“The blame should not rest just with the governments of the developed countries and the international financial institutions. More broadly, financial markets had been influential in encouraging the developing counties’ adoption of the Washington Consensus policies, which had served the developing countries so poorly, even as they served the banks so well.” (p. x-xi).

He wrote that there had been more than a hundred financial crises in the last thirty years, in contrast with the stability after World War II, and argued that better regulation is needed.

Stiglitz is particularly critical of the IMF “for its long-standing support for the deregulation and liberalization policies that were central to creating the crisis and its rapid spread.” Moreover, the IMF was dominated by western commercial interests and ideology which had imposed harsh economic policies to enforce repayment of debts. Its policy prescriptions conditional on financial aid insisted on “reductions in expenditures and tightening of interest rates, just the opposite of the Keynesian policies pursued by the advanced industrial countries in the crisis.” (p. xix.).

Stiglitz welcomed some recent reforms in the IMF that allow countercyclical policies, and even in some cases imposing capital controls. But he argues that further reforms are needed, with better representation of developing countries on the IMF, with more funds going to poorer countries and in grant form, not as loans. (p. xix).

Stiglitz also called for major reforms of international taxation loopholes, particularly in developed countries themselves with their bank secrecy provisions. The Commission recommended urgent attention to the problem in perverse incentives and bonuses by bank and finance officials: “the typical financial executive’s incentive scheme encourages short-sighted behaviour and excessive risk-taking. What had happened was predictable and predicted.” (p. xx).

Writing in January 2010, Stiglitz was alarmed that “In most countries, the financial sector has successfully beat back attempts at key regulatory and institutional reforms. The financial sector is more concentrated; the problems of moral hazard are worse. Global imbalances remain unabated.” (p. xxii).

In his foreword, Miguel d’Escoto Broctmann wrote that on 26 June 2010 the UN General Assembly adopted the statement, “World Financial and Economic Crisis and its Impact on Development”, in part reflecting the influence of the Report of the Expert Commission (p. xxv). He highlighted the “imperious economic perspective that has been implemented, often under duress, across the global during the last 35 years.” (p. xxvii).
Brockmann added that the Commission stressed that “the present crisis demonstrates failure at many levels – of theory and philosophy, of institutions, policies and practices, and, less overtly, of ethics and accountability”. He continued that “the system itself – its organization and principles, and its distorted and flawed institutional mechanisms – is the cause of many of these failures”. Moreover, “unlike the laws of physics, we have a political choice to determine when, where, and to what degree the so-called laws of economic behaviour should be allowed to hold sway.” (p. xxvii).

Brockmann noted “the almost complete absence of political accountability’ for responsibility in the crisis. “As the greatest economic philosophers – whose number surely includes Aquinas, Smith, Marx, and Keynes – have all recognized, homo oeconomicus, the acquisitive, emotionally cardboard, and socially atomistic construct of academic economics is a reductio ad absurdum. They did not merely assume that the ethical vocation of human beings should inform their economic decisions and institutions; they insisted on it…” (p. xxviii).

The Stiglitz Report highlights that questions of social equity and philosophy must be brought into the heart of economic policy. It recognises that “in most advanced industrial countries, median wages stagnated during the last quarter century, while income inequalities surged in favour of the upper quintiles of the income distribution.” (p. 23). It urged that the policies for recovery must reverse this “growing inequality of income and wealth” (p. 25).

The Report quotes the US Congressional Oversight Panel of the financial bailout package (the TARP) that “the regulatory failure that gave rise to the current crisis was one of philosophy more than structure.” (p. 61). The neoliberal economic philosophy was favoured by special interests which promoted such ideas (p. 64).

Far from the power of such special interests being broken, the Report warns of a danger that “existing power structures can seize hold of these moments of crisis and use them for their own benefit, reinforcing inequalities and inequities. There may be a greater concentration of economic and political power after the crisis than before.” (p. 198)

Nevertheless, the authors of the Report are cautiously optimistic that intelligent reforms can enhance the wellbeing of everyone, especially in the less-developed countries and among the poorest people. “They have been among the innocent victims of this crisis.” (p. 201). The reconstruction must also deal with “the climate crisis, the energy crisis, the growth in inequality in most countries around the world, the persistence or poverty in many places, and the deficiencies in governance and accountability, especially within international organizations.” (p. 195). ♦