

The Double Movement Ten Years After the Fall of Lehman Brothers

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Abstract

Ten years after the collapse of Lehman Brothers and the sharpest moments of panic within the global - and particularly the United States banking system - a somewhat strange dynamic has appeared. While the principal agents behind the crisis have collapsed their own institutions, the markets that they dominate, and even provoked what has been called the third crisis of economic theory, their political power has not waned. This theme has been well addressed by some academics such as Mirowski (2013), while it has flummoxed others. In this paper, we will argue that Karl Polanyi's theory of the "double movement" offers a coherent framework that is able to account for the history of the last ten years. Polanyi argues that different groups and members of society seek protection from the market, and that this search for protection has been the driving force between historical change. Polanyi does not ignore class; rather, he argues that different social classes can protect themselves in more or less effective ways. We argue that during the last ten years, the interests of globalized financial capital have been able protect themselves with utmost effectiveness, while all other classes have been trampled, often not even recognizing how or why actions are taken against the general interest.

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Introduction

The first round of Quantitative Easing (QE) in response to the US financial panic of 2007-2009 was unleashed in 2008, officially as a measure to stimulate the economy. Ten years later, the idea that monetary policy becomes ineffective at the lower ranges of interest rates has gained acceptance amongst mainstream economists. Yet the tardy and incomplete recognition of the limits of monetary policy raises suspicion as to the real intentions behind programs of QE. Indeed, the "Keynesian" solution of fiscal stimulus in the face of macro crisis is a tried and true solution, as shown convincingly from the 1920's onward in both reality and theory. In addition, QE was indeed attempted in the 1930's. In *A Monetary History of the United States*, Milton Friedman quotes Federal Reserve (Fed) governor Harrison as telling his directors that banks "must have some funds with which to stay in business"(Friedman and Schwartz, 1963: 518).

The argument that QE is a policy tool to give banks "some funds" has also been argued by many in the current context. The consideration that monetary policy can aid banks but not the public in general finds strong support in Karl Polanyi's *The Great Transformation*, and his concept of the "double movement". Polanyi states that "Modern central banking, in effect, was essentially a device developed for the purpose of offering protection without which the market would have destroyed its own children" (Polanyi, 1944: 201). During the current crisis, central banks alone were insufficient, and private banks protected themselves through Treasury departments as well. The extra-market bank bailouts carried out through these two institutions maintained afloat the north Atlantic banking system, and the world's most dominant banks undeniably couldn't have survived without it.

However, as we argue here, various rounds of QE have also had other consequences of note. In this brief article, we focus on the stock market gains of the recent years from a broad viewpoint, analyzing the specific mechanisms of this growth, the political economy in which they are situated, and the theoretical

consequences of these public policy measures. These three issues will conform the three main sections of this article, bookended by the introduction and the conclusion.

The Political Economy of QE

As mentioned, QE can be seen as one arrow in the quiver of monetary policy options for bailing out banks. And while it certainly has served this function, it has also spread the bounty to the political constituency of financialization - the rentier class. Speaking to the unveiling of QE2, then Chairman of the Fed Ben Bernanke said that QE had helped to boost the stock market: "I do think that our policies have contributed to a stronger stock market, just as they did in March of 2009" (Isidore, 2011), referring to QE1. A key way in which QE policies were supposed to buoy the economy in general was through keeping interest rates low, which would prompt more lending and in general increase the money supply.

However, a policy of low rates would always hurt savers, a point later made by Stanley Fischer, former central banker of Israel, speaking in his capacity of Fed Vice Chairman in 2015: "Well, clearly there are different responses to negative rates. If you're a saver, they're very difficult to deal with and accept, although typically they go along with quite decent equity prices" (Smialek and Randow, 2016). While we would certainly wonder about the historical veracity of this claim, the quote nevertheless highlights the incentives put forth by the Fed: savers should move into the stock market in some sort of retail portfolio rebalancing. This channeling of savings into the stock market is certainly not new. The privatization of pensions has transformed "savers" into "investors" around the world over the last decades, and indeed, savers have never been a reward class under neoliberalism. Productive investment, employment, and savings have been consistently been overtaken by financial investment.

The Neoliberal political project does entail an order, and at the apex is Wall Street, a position clearly manifested by their impunity from market discipline under the "too big to fail" precedent. So while stock market investors are favored at the expense of savers, and institutional investors are favored over retail investors, at the corporate level executives and shareholders of Wall Street and related firms are

avored over all others. As returns on the bond market have crashed with interest rates in general, the last gift that the neoliberal project can offer is financial profit through the stock market. In an expanding market, the rising tide serendipitously floats small boats along with great ones.

The evolution of the specific mechanisms to float the market

When QE was first used in the US in the 1930's, Friedman reports that "Time and again, at meetings of the New York Bank's directors and of the Federal Open Market Committee, the desirability of achieving some run off was stressed and agreed to by almost everyone present. The System felt itself in a straitjacket from which it urgently wished to be freed" (Friedman and Schwartz, 1963: 519 - 520). During the various rounds of QE, the Fed did flirt with an escape from the straight jacket of asset purchases. The resulting "taper tantrum" saw a cooling off of the asset price growth in what could be seen both as the market dependence on central bank and treasury munificence and as a good way to keep the market rally at least somewhat in check.

Both during the Great Depression and today's Great Crisis, the real straight jacket facing central banks is that of asset price deflation on the one hand, and serving constituent banks on the other. In both episodes, once financial deals were found to be fraudulent, financial wealth was instantly destroyed on a scale that could not be compensated for by any market mechanism. As much as prominent analysts and policy makers wished for a new financial bubble (Krugman, 2013; Summers 2014), Wall Street had lost the credibility to be able to conjure up the type of market euphoria necessary to create a bubble that could reach the retail level. While five years after the crisis the stock market had made significant advances, interest rates were still falling. As official policy around the world went from zero interest rate policy to negative interest rate policy, the alarm sounded from policy makers revealed that the original express goal of QE - to lower rates - was false. Lower rates were simply a mechanism to aid banks, again opposed to the other side of the straightjacket: financial deflation.

Up until around the time of the Trump administration's arrival in 2016, the post-crisis Fed maintained the federal funds rate at .25%, for years, with its balance sheet in constant expansion, and consisting of mortgage backed securities and Treasury Bonds. However, the Fed has never dropped its interest rate into negative territory, nor did it ever official purchase equities or corporate bonds on a consistent basis. The European Central Bank (ECB) likewise has yet to officially purchase equities, but has done the other two. The central banks of Japan and Switzerland have both held their official interest rates at negative levels while purchasing equities.

As of the end of June 2018, the the Swiss National Bank (SNB) had slightly over 85 billion dollars (85 thousand million) invested equity holdings, with the top positions concentrated in Apple, Microsoft, Amazon, Johnson & Johnson, Facebook, and Exxon (Nasdaq, information online). For its part, at the end of the following month, the Bank of Japan was reported to have \$227 billion invested in the Tokyo Stock exchange, equaling 4% of the total market and converting the BoJ into "a top ten shareholder in 40% of Japan's listed companies" (Tomito, 2018).

Such large scale interventions in equity and bond markets by erstwhile non-market participants is certainly a historical novelty, and with this official assistance, the world's largest companies have also ridden the tide and have also engaged in large scale share buybacks. While this is far from a historical novelty, the size and scope of the buybacks is of note in this context. Indeed, Standard and Poor created various Buyback Indexes between 2012 and 2013 for retail speculators to be able to participate in the gains of the equity market expansion schemes already described. From 2013 to date, these indexes have seen significant gains over the traditional S&P 500. The use of bank loans for leveraged stock buybacks has underpinned the run of equity market gains since these dates, and has provided two forms in which Wall Street can gain from the trend. First, by lending to other companies to buy back their own stocks, Wall Street banks realize profits, while second, when Wall Street banks buy back their own shares - and this has accounted for a significant buy highly variable portion of all share buybacks during this period - they can transfer great amounts of wealth to their shareholders and executives.

The specific dynamics of the huge global equity market increase in the last five years can largely be attributed to the mentioned factors. We would not call this a market bubble, however, as the monetary expansion has been more driven by the injection of State money rather than private bank money, and as there appears to be little fraud involved in luring retail investors into the scheme. We rather feel that Polanyi's double movement can account best for the global stock market surge. Unlike in the Great Depression, when governments around the world carried out programs to protect the citizenry from the market's collapse, after the Great Crisis, official responses around the globe have centered on protecting markets and their most important participants, but not on protecting society at large. Such a response has created new and academically fascinating situations.

A "broken" market that floats

Along with the double movement, another key concept developed by Kari Polanyi is that of the three false commodities - land, labor and money - and the notion that these three things will be ruined if left alone to the market. With the assistance of Kari Polanyi, we can more easily expand these categories into humanity, nature, and financial markets. Surely the most evident way in which the market has been broken is shown in the financial panic of 2007-2009; however, the ongoing state support of markets has done even more to damage to both the normal functioning of the markets and its justifying ideology.

In the 1930's, authorities appeared to be caught between returning private markets to their correct functioning and combatting the rot of deflation. Friedman describes the "straight jacket": "the result was that the System drifted into a policy of holding a rigid portfolio of government securities. It did not want to buy and felt it could not sell" (Friedman and Schwartz, 1963: 519). Perhaps this was the lesson that Bernanke learned from Friedman when he told Friedman that "we won't do it again" (2002). This time the Fed would feel no such compunction in violating all of the principles of the free market in order to bail out Wall Street and protect its core constituencies. Yet with no Keynes to save capitalism from the bankers, even the

bankers are complaining, such as Goldman Sachs's Lloyd Blankfein (2018): "where central banks all around the world are buying all the risky assets which then therefore put a damper on volatility and the opportunities to perform, that's not a natural state" (CNBC, 2018).

In Kari Polanyi Levitt's *From the Great Financialization to the Great Transformation*, the author emphasized her father's maxim that "laissez faire" is planned. The idea of a self-regulating market has always been fictitious, although as highlighted by Blankfein's above comment, it is more evident today than in the past. Today's strange market configuration has had clear impacts on non-financial firms as well. Particularly in the case of the US, the difference between retained earnings and net investment has grown steadily since the beginning of the last decade, and the tendency has grown since 2007. Based on data from the Fed, Brender and Pisani note that since the end of the last century, non-financial companies have maintained net investment lower than retained earnings, with a part of the later used in the repurchase of shares. Based on corporate reports, they offer the example of several of the largest non-financial companies, such as Apple, Amazon, Alphabet, and Pfizer, as prime employers of large share buybacks (2018: 116-117).

With the liquidity provided by the Fed, the flow of profits feeds the buyback of shares and therefore the rise in stock markets, but this rise does not correspond to any significant investment processes. The Fed simply feeds new benefits based on the stock market capitalization of both financial and non-financial firms. As the market continues its destructive path, state institutions must continue to deepen their "market" rescue. Therefore the historically novel market developments are accompanied by even greater novelty outside of the market: while one part of the double movement is evident, the other is missing. From the 2007-2009 panic onward, central banks and treasuries have rescued the largest financial firms, and the financial rentier class has fairly successfully protected itself from the market's destruction. Yet there have been few victories for coherent national movements (much less international ones) to protect the common working people from the same market destruction.

As Polanyi-Levitt highlights: "Following the First World War, social conflicts arising from draconian financial requirements to conform to the rules of the gold standard" (Polanyi-Levitt: 100) were historically decisive. After trying to restore the gold standard in the 1920s, and the catastrophic result of the austerity of those years, societies sought to collectively protect themselves against the forces - often incorrectly perceived - that caused economic and social destruction. In the face of today's market disasters, governments and central banks have consistently placed the interest of the new *haute finance* ahead of all other considerations. As Kari Polanyi states, "the liberalization of trade and capital in the last quarter of the twentieth century has once again freed capital from regulation" (Polanyi-Levitt, 2018: 101). In effect, today's *haute finance* is haughtier than ever, as it has freed itself from both the regulation of the market and that of society at large.

Conclusion

Karl Polanyi argues that roughly two centuries ago, *haute finance* rose to such prominence that it was able to successfully administer the hundred years peace. Shortly after this ended, the "golden thread" snapped and the Second World War occurred. Today, *haute finance* is arguably more dominant than ever. Karl Polanyi insists in *The Great Transformation* that the remarkable hundred years peace was only achieved because of the resistance of the common working people to the advances of the market. Today, *haute finance* has been able to remain politically dominant even while the markets under its control have broken down. Such a strange juncture in history raises many issues. Karl Polanyi convincingly argues that capitalism only became a dominant mode of production once the Speenhamland system's protection of the labor market was lifted and land, labor, and money were fully the ward of private markets. As credit and money are today so heavily supported by the State, the question of whether we can describe today's economy as fully capitalist necessarily comes to the fore. Whatever the conclusion, the direction that financial markets have taken - particularly after the 2007-2009 panic - taken together with the notable absence of the second part of the double movement, certainly indicates an important historical rupture.

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