

Exploring the Connections in the Political Economy of the Global Financial Crisis¹

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1. Using the ‘Connections’ Website

The Connections in Political Economy (CPE) website at www.politicaleconomy.org.uk is based on the idea of the 'concept map', providing a visual depiction of the links that might be followed from one topic of research and area of literature to another. It consists of a set of hyperlinked pages assigned to particular topics and issues. Each page contains annotated 'reading lists' and links to a variety of sources of information of varying degrees of depth of analysis. These range from seminal texts to contemporary media comment and debate. The 'Connections' project is necessarily an ongoing venture.

We begin by providing a brief explanation of the motivation for this project.

We then move on to the main purpose of the paper which is to explore the connections that can be made within the political economy literature which are relevant to the Global Financial Crisis.

Students in the 21st century are accustomed to using a wide and growing range of Internet directories, portals and open content encyclopedia. This has brought with it enormous benefits but also important challenges. Students must learn how to judge the reliability and the appropriateness of the various sources they come across. The popularity of sites such as Wikipedia, as a quick source of information for assignments is testimony to the power of hyperlink Internet pages as an aid accessing information. Such sites however, lack guidance with regard to both the appropriate academic level of suggested references and to a structure of the relationships between different topics. Such structures will normally be established within the context of an academic program. Moreover, problems have been identified with the use of such sites with respect to "the denial that there is any controversy and the systematic manipulation to suppress any mention of it"² But controversy and debate is an essential feature of the issues of political economy.

¹ A version of this paper was presented at the First International Conference in Political Economy of the International Initiative for Promoting Political Economy (IIPPE), 'Beyond the Crisis' September 10-12 2010, Rethymno, Crete.

² See 'The Power of the Wikipedia Editor'
<http://www.libraryplanet.com/2008/04/17/the-power-of-the-wikipedia-editor/>

Students of political economy will often explore the writings of major contributors to different theoretical perspectives in order to put these in the context of real-world issues of social concern. Most of the important issues which have an economic or political economy content can be shown to be interrelated. The ongoing development of our understanding of such issues often requires us to make connections between different topics of analysis and bodies of literature. An ability to make such connections is the result of experience gained over time from exposure to a wide range of literature, and in teaching, presenting and discussing such ideas with colleagues and students. Novice students have yet to develop this way of thinking about making such connections.

Nevertheless, the discovery that everything seems to 'fit together' will often be found to be an exciting and liberating experience which acts as an important motivator for future study.

The 'Connections' website can be likened to a roadmap which identifies the existence of places to visit, how they are connected and what interesting things can be found there. But, to extend the analogy, it is not a travel guide. Seasoned travelers and developers (i.e. researchers) have little need for travel guides to help them get around what for them is familiar territory, but nevertheless will still find value in referring to a map which reminds them of places that they might otherwise have forgotten.

Section 2 represents a suggested introductory tour guide to the main "places" that are relevant to an understanding of the issues involved in the Global Crisis. It is suggested that new 'visitors' spend a short time in each place in order to get a feel for the breadth of issues involved, before returning to explore each place in depth.

2. Connections in the Political Economy of the Global Financial Crisis

The onset of major economic change and reversal of economic prosperity on the scale experienced by the global economy in the years following the US sub-prime crisis of 2007/8 has inevitably produced a significant thirst for knowledge, not just by students of economics but by the wider public whose livelihoods have been damaged or threatened. But how is this thirst to be satisfied?

We argue that enlightenment is unlikely to be gained from the writings of those mainstream economists whose vision of the economic world could never have entertained the slightest possibility of this crisis, and who are now unable to provide a convincing theoretical basis for policies that they have advocated in the aftermath of the

crisis. Furthermore it is clear that the battle of ideas has become more and more ideological³. In the wake of the crisis the media debate has become quickly dominated by representatives of finance whose earlier lack of understanding should have excluded them from having anything sensible to say, and who clearly have a vested interest in helping to shift the blame and the costs of the crisis.

The crisis has had enormous distributional implications, including the increased need felt by particular groups to defend their relative positions and to attach blame to other parties. The believed certainties, optimism and apparent cooperation of the so-called 'Great Moderation' leading up to the crisis, at least within the developed world, have now been replaced by widespread realisation of the fundamental uncertainties of the market, together with a need to attach blame. Such rivalries can be seen between groups within national economies, between nations (e.g. within Europe) and between groups of nations.

The issues raised by the crisis are wide and varied. Some are related to particular institutional developments that have only recent historical specificity, such as the fallout from the US sub-prime crisis, its implications via collateralisation and the various details of the bank bailouts. Other analyses have focused on developments which have a longer timeframe. These include the growth of financialisation since the 1980s, the instabilities arising from the particular role of the US dollar, and the related emergence of global imbalances since the turn of the century. Alongside these developments, significant ideological changes have taken place within mainstream academic economics over the last 30 years, which have been seen to provide an underpinning for unrealistic claims about market efficiency. The influence of market fundamentalism, and the exclusion of heterodox ideas and the history of economic thought from academic curricula, have been acknowledged to have contributed to the crisis.

The crisis has indicated the relevance of fundamental concepts which transcend the details of the current historical events. These include the roles played by rent extraction, political patronage and capture, mercantilism, and the fundamental uncertainties associated with 'free', unregulated markets, to name just a few. Such 'timeless' concepts have their origins in other periods of economic and social upheaval and in the writings of the 'worldly philosophers' of earlier times.

³ A useful elaboration can be found here: <http://www.marxists.org/glossary/terms/i/d.htm#ideology>

"Ideology is a system of concepts and views which serves to make sense of the world while obscuring the social interests that are expressed therein, and by its completeness and relative internal consistency tends to form a closed system and maintain itself in the face of contradictory or inconsistent experience".

....."The word is used with a wide variety of connotations" including "false ideas which help to legitimate a dominant political power".

The promotion of political economy as a network of connected issues and topics of research, rather than simply an umbrella title for a variety of disparate, unrelated ideas, necessarily requires us to begin by clarifying what exactly is meant by political economy. What are the characteristics of political economy that make connections possible? The next section is based on the discussion at the following CPE page:

<http://www.politicaleconomy.org.uk/whatispoliticaleconomy.htm>

2.1 What is Political Economy?

Political economy can be defined in different ways. Our preferred definition, which is presented on the above CPE web page, is as follows:

We will define political economy as economic and social analysis which takes seriously the reality of power and vested interests in determining economic outcomes.

Economic analysis is held to be a crucial component of political economy since it is necessary to apply tools of economics in order to explore the alternative economic implications arising from the expression of economic power whose objective may be distributional advantage.

Power is assumed to be held at the level of groupings or broad categories of economic agents and their representative institutions, rather than at the level of individuals.

Those categories may be defined in various ways by exploring the shared interests in, and rivalry over, their command over economic resources and monetary institutions.

A common categorisation (but by no means the only one), is in terms of class interests. Rivalry has been explored between landlords and capitalist (as in the analysis of the English classical economists), or between workers and capitalists (as in the analysis of Marx and subsequent writers), or between industrial capitalists and financial capitalists (as in the analysis of Keynes and Post Keynesians, and also of Marx).

The role of government and governmental institutions has also been an important subject for analysis in political economy. Within a domestic economy, enormous economic power is held by the state by virtue of its ability to levy taxes and create laws. But how it uses the power has been the subject of much debate throughout the history of political economy. On whose behalf does the government use its economic power? These are the legitimate questions of political economy.

Mainstream economics views the government in relation to the something called '*the private sector*', where the latter has been likened to a 'unified happy family'.⁴ Within mainstream macro economics there is a division between Keynesians and New Classicals concerning the motivations for government policy. On the one hand, the Keynesian approach has been to adopt the assumption of the benevolent policymaker who always attempts to act in the national interest. On the other hand, New Classical economists have adopted an antigovernment approach which sees the government as having its own agenda which invariably causes it to act *against* the national interest. (e.g. Due to the desire of politicians to be reelected in government)

However this version of political economy is unsatisfactory, given the divisions of interests that exist between groups within the 'private sector'. It is by assumption biased against any notion that a particular group *within* 'the private sector' may act against the interests of others in that sector. Moreover it is not much use in helping us understand the political economy of the Global Financial Crisis. For it not only prevents us from attributing any responsibility for the crisis to the expressions of the autonomous interests of finance, it also denies the possibility that government policy might be designed in the interests of that group. We therefore take the view that the private sector should not be assumed to be one big happy family.⁵

Finally we may also point out the existence of some other the ways in which mainstream economics differs from political economy, in terms of the former's narrow focus on individualistic behaviour (and therefore its neglect of rivalry between group interests); its insistence on abstract, formalistic, a-historical and deductive reasoning; and the exclusion of any role for the study of the history of ideas. In contrast, political economy and the CPE website places great importance on historical developments and the ways that the 'worldly philosophers'⁶ of the past have made sense of economic change.

We may now move on to explore just some of the many examples of what constitutes the political economy approach to the current crisis, by selecting the following page from the CPE menu, shown in figure 1.

⁴ This discussion is based on an excellent exposition of 'The Political Economy of Economic Policy Making' provided by Thomas I. Palley in "Plenty of Nothing, The Downsizing of the American Dream and the case for Structural Keynesianism", Princeton University Press, 1998, pp116-119

⁵ Palley points out that, unlike the mainstream Keynesian approach, 'structural Keynesianism' "recognizes that the domain of economic policy making is a 'contested terrain'" op. cit., page 119

⁶ The novice student is advised to peruse Heilbroner, Robert L. (2000) *The Worldly Philosophers: The Lives, Times and Ideas of Great Economic Thinkers*, for an excellent introduction.

2.2 “The 2007/8 Securitised Debt Crisis and Its Macroeconomic Consequences”

<http://www.politiceconomy.org.uk/subprimecrisis.htm>

Our first port of call is necessary in order to remind ourselves of the scale and unpredicted nature of the crisis which initiated the wider global crisis. This page is typical of the website's contents in providing both a map of connections to other pages (see fig 2) together with an annotated directory of links to a wide variety of sources of information and contemporary commentary covering the actual events of the crisis.

It is important to recall that the ongoing global macroeconomic crisis was instigated by the activities of private financial capitalism. The enormity and suddenness of the crisis in the financial world remains a matter of public record given the justifiable attention that it received in the world media. But it can so easily become yesterday's news. The conventional wisdom of that time that this was a crisis of private capitalism, caused by private finance, and that this was never in dispute in the mainstream media. The spotlight of every news bulletin and many newspaper headlines was on the disastrous 'mistakes' of the so-called 'masters of the universe'.

On the complacency of policy makers prior to the crash, the connections page provides access to the statement by Ben Bernanke in 2005 that he did *"not think that the national housing boom is a bubble that is about to burst"* and that the increase in US house prices *"largely reflect strong economic fundamentals, such as a strong growth in jobs, incomes and the number of new households."*⁷ Similarly, as late as May 2007 and as Chairman of the US Federal Reserve, Bernanke was still arguing that *"the expansion of subprime mortgage lending has made home ownership possible for households that in the past might not have qualified for a mortgage and has thereby contributed to the rise in the home ownership rate since the mid-1990s.... Not only the new homeowners but also their communities have benefited from these trends."*⁸

For the purpose of contrast, CPE provides access to a valuable record and timeline of dissenting voices, compiled by the Real World Economics Review.⁹ Specific examples of heterodox comment are included, such as this one from Hudson in 2006¹⁰:

⁷ There's No Housing Bubble to Go Bust: Fed Nominee Has Said 'Cooling' Won't Hurt

By Nell Henderson, Washington Post Staff Writer October 27, 2005;

<http://www.washingtonpost.com/wp-dyn/content/article/2005/10/26/AR2005102602255.html>

⁸ Ben Bernanke, The Subprime Mortgage Market

Speech at Federal Reserve Bank of Chicago's 43rd Annual Conference on Bank Structure and Competition, Chicago, Illinois May 17, 2007

<http://www.federalreserve.gov/newsevents/speech/bernanke20070517a.htm>

⁹ See 'Foresight and Fait Accompli: Two Timelines for the Global Financial Collapse'.

Real World Economics Review

<http://rwer.wordpress.com/foresight-and-fait-accompl-i-two-timelines-for-the-global-financial-collapse/>

¹⁰ Michael Hudson, The New Road to Serfdom. An illustrated guide to the coming real estate collapse
Harpers Magazine, May 2006

"Most members of the rentier class are very rich. One might like to join a class..... if you have the wherewithal to fill out a mortgage application, then you need never work again. What could be more inviting..? That's the pitch, anyway. The reality is that, although home ownership may be a wise choice for many people, this particular real estate bubble has been carefully engineered to lure homebuyers into circumstances detrimental to their own best interests. The bait is easy money. The trap is a modern equivalent to peonage, a lifetime spent working to pay off debt on an asset of rapidly dwindling value..."

Turning next to the details of the crisis itself, there is much in the public record to choose from. A useful collection can be found at PBS Frontline Inside the Meltdown, *"How the economy went so bad, so fast and what Bernanke and Paulson didn't see, couldn't stop and weren't able to fix"*¹¹ This contains much material from the public record, including a timeline of the dramatic events which runs from June 2007 through to October 2008, together with examples of the statements of alarm of the US political elite.

For an overview of the crisis and its consequences, Fullbrook's online 'book', *'Crash. Why it happened and what to do about it'*¹² is an excellent and accessible collection of articles by important contributors to the literature. We also recommend other material which explains the role of the banks and particular financial innovations in the crisis. Karl Beitel's article is helpful to those wishing to place these developments in a systemic, political economy context. As well as providing a lucid exposition of the central features of the financial innovations which characterised the fragility of the financial system he emphasises that the crisis was *"not the result of bad policy decisions or well intended but ultimately misguided public interventions..... On the contrary, the tendency excessively to expand financial claims is inherent in a system where credit creation, fuelled by financial innovation, has become progressively decoupled from real accumulation -- i.e., tangible capital investments. Episodic crises are endemic in such a system of decoupled financial speculation. What has happened before will happen again, potentially on an even greater scale."*¹³

Blackburn provides a description of the events of those years which also puts the crisis in the context of a longer historical time period: *"The credit crunch came as the climax of a long period of gravity-defying global imbalances and asset bubbles..... In what follows I interpret the credit crunch as a crisis of financialisation. When properly embedded in structures of social control, finance can help to allocate capital, facilitate*

<http://michael-hudson.com/wp-content/uploads/2010/03/RoadToSerfdom.pdf>

¹¹ PBS Frontline: 'Inside the Meltdown' <http://www.pbs.org/wgbh/pages/frontline/meltdown/>

¹² Edward Fullbrook (Ed), Crash. 'Why it happened and what to do about it' <http://www.paecon.net/CRASH-1.pdf>

¹³ Karl Beitel 'Understanding the Subprime Debacle', Monthly Review, May 08. <http://monthlyreview.org/080512beitel.php>

*investment and smooth demand. But if it is unaccountable and unregulated it becomes sovereign in the reallocation process, and can grab the lion's share of the gains it makes possible, including anticipated gains before they have been realised".*¹⁴

Another dramatic feature of the crisis of 2008 was the political fallout, particularly in the USA, concerning the need to rescue the banks in order to avoid a complete collapse of the economy. There is plenty of material on record on this aspect of the crisis which can be accessed at the CPE page, "The 2008 Debt Crisis and the Wall Street Bailout".

The question was hotly debated whether Wall Street was being rescued to support 'Main Street', or to support the profits of Wall Street at the expense of Main Street. There was much evidence of belief in the latter proposition.

Michael Hudson struck a chord in September 2008 when he argued that "*Saturday's \$700 billion junk mortgage bailout is the largest and worst giveaway since a corrupt Congress gave land grants to the railroad barons a century and a half ago. If it goes through, it will shape the coming century by giving finance unprecedented power over debtors – homebuyers, industry, state and local government, and the federal government as well.....*"¹⁵

As the crisis gained pace through its effects on real activity, and spread throughout the global economy, its wider social and political effects were clearly of concern to mainstream media. For example, in March 2009 the Financial Times observed that:

*"Economics is convulsing European politics. Governments have fallen in Iceland and Latvia; strikes or protests have erupted in Greece, Ireland, France, Germany, Britain, Lithuania, Ukraine and Bulgaria. Financial turmoil has shaken even the continent's furthest-flung outposts: the French Caribbean island of Guadeloupe has been ravaged by violent strikes, while Russia flew riot police into ice-bound Vladivostok to quell street protests. This spasm of unrest was hardly expected when the crisis broke in the summer of 2007: many Europeans believed they would be spared the worst effects of a disaster forged in the suburbs of the US. Since then, as the crisis has spread, initially sanguine forecasts have given way to ever more gloomy predictions....."*¹⁶

¹⁴ Robin Blackburn, The Subprime Mortgage Crisis, New Left Review 50 March–April 2008.
<http://www.newleftreview.org/?view=2715>

¹⁵ Michael Hudson, The Paulson-Bernanke Bank Bailout: Will the Cure be Worse than the Disease? Counterpunch, Sept. 22, 2008, <http://michael-hudson.com/articles/debt/080922CureWorse.html>

¹⁶ John Thornhill Agitation as middle-class Europe struggles to cope
Financial Times March 11 2009,
<http://www.ft.com/cms/s/0/3a090842-0e84-11de-b099-0000779fd2ac.html>

A further feature of the evolution of the crisis, as more information became available, was the questionable legality of the banks' behaviour and the recognition that the problems had been by design rather than by accident. Various examples of comment are provided on the CPE page. For example, we have this extract from James Galbraith,

"..... the financial industry was largely overrun by ... the art of originating mortgages that were plainly fraudulent. lenders certainly knew that the borrowers would not be in a position to continue to service those mortgages past, at most, three or four years—mortgages that were in fact designed to have that result..... there is no nonfraudulent reason for a lender to knowingly accept an inflated appraisal on a house. No known explanation of that can be construed as innocent. I think it's fair to say that if this sounds to you like a criminal enterprise, that's because that's exactly what it was..... " ¹⁷

We may point out that by 2010 it had also become clear to the US authorities that there were grounds for prosecution, as reported in the Guardian:

"According to the SEC, Goldman cheated customers in a 2007 deal concerning a mortgage-backed security known as a "synthetic CDO" called Abacus. The bank is accused of failing to tell investors that a US hedge fund, Paulson & Co, was going "short" by betting that the security would decline in value. Paulson is alleged to have been allowed to stuff Abacus with mortgages doomed to default..." ¹⁸

Soon after, Morgan Stanley was reported to be *"a target for a criminal investigation into controversial tactics adopted by firms to bet on a slump in home loans at the beginning of the global financial crisis. Prosecutors are said to looking at packages of mortgage-backed securities issued in 2006.....Morgan Stanley was involved in designing the two synthetic collateralised debt obligations (CDOs) sold to investors. The bank's trading desk is said to have sometimes taken "short" positions on them, betting they would fall in value."* ¹⁹

At the same time the Wall Street banks and the major ratings agencies came under suspicion for *"an allegedly 'cosy' relationship"* which raised the possibility that they *"cheated in the hunt for valuable triple-A grades"* ²⁰

¹⁷ James K. Galbraith THE GREAT CRISIS AND THE AMERICAN RESPONSE?
Levy Economics Institute, Public Policy Brief 112, June 2010
http://www.levyinstitute.org/pubs/ppb_112.pdf

¹⁸ Goldman Sachs faces criminal investigation, Guardian, 30 April 2010,
<http://www.guardian.co.uk/business/2010/apr/30/goldman-sachs-criminal-investigation>

¹⁹ Morgan Stanley may be next target of US prosecutors, Guardian, Wednesday 12 May 2010
<http://www.guardian.co.uk/business/2010/may/12/morgan-stanley-inquiry-claim>

²⁰ Guardian, Wednesday 13 May 2010
<http://www.guardian.co.uk/business/2010/may/13/wall-street-banks-investigated-mortgages-ratings>

We may then draw attention to various observations that have been made about the burden of consequences of such behaviour.

For example, Hossein-Zadeh observes that "*Never before has so much debt been imposed on so many people by so few financial operatives—operatives who work from Wall Street, the largest casino in history, and a handful of its junior counterparts around the world, especially Europe.....*

After transferring trillions of dollars of bad debt or toxic assets from the books of financial speculators to those of governments, global financial moguls, their representatives in the State apparatus and corporate media are now blaming social spending (in effect, the people) as responsible for debt and deficit" ²¹

Philip Stephens reported in similar vein in the Financial Times in July 2010:

"It has been three years since the roof started to fall in. The markets (and the bankers) still rule.

.....hundreds of billions of dollars in toxic assets that once sat on the books of the banks have been piled on top of the deficits caused by the crash-induced recession. Families are paying the bankers' bills through rising taxes, shabbier public services and higher unemployment..... " ²²

We will now proceed to connect to another CPE page. Figure 2 shows the various connections that can be made. For this introductory tour it is appropriate to consider the role of mainstream economics by selecting the following page.

<http://www.politicaleconomy.org.uk/subprimecrisis-intellectualfailure.htm>

2.3 The Financial Crisis and 'Intellectual Failure'

Here we may recall that it was not just 'the bankers' who were the object of public criticism. There was widespread condemnation in the media of those who, it was felt, should have anticipated the crisis. This CPE webpage provides various examples.

Anatole Kaletsky, writing in The Times, pulled no punches with his assertion that: "*Academics - and their mad theories - are to blame for the financial crisis. They too deserve to be hauled into the dock"* ²³

²¹ Ismael Hossein-Zadeh, The Vicious Circle of Debt and Depression
<http://heterodoxnews.com/htnf/htn100/Ismael-debt-depression.pdf>

²² Philip Stephens, Three years on, the markets are masters again
Financial Times July 29th 2010

²³ Anatole Kaletsky, Economists are the forgotten guilty men, The Times, February 5, 2009
http://www.timesonline.co.uk/tol/comment/columnists/anatole_kaletsky/article5663091.ece
Also see, "Goodbye, homo economicus",

Readers of the Financial Times were also informed that "*Official models missed the crisis not because the conditions were so unusual, as we are often told. They missed it by design. It is impossible to warn against a debt deflation recession in a model world where debt does not exist.*" ²⁴

According to the Head of the UK's Financial Services Authority, "*the crisis had to be viewed in the light of a 'fundamental intellectual failure' around the world of regulators, politicians and economists.*"²⁵

But such "intellectual failure" had been well known to heterodox economists. In response to the above, it was important to set the record straight:

"In economics there has been intellectual failure, but by zealous and influential members of the neoclassical school of economics. Those economists have unfortunately dominated "the mainstream" and have dictated the terms of the conventional wisdom, to the exclusion of what therefore became labeled 'heterodox'" ²⁶

So it is important to acknowledge that, as Galbraith points out, "*there is a considerable, rich, promising body of economics, theory and evidence, entirely suited to the study of the real economy and its enormous problems. This work is significant in ways in which the entire corpus of mainstream economics simply is not.*" ²⁷

In the light of the ongoing ideological battle for ideas it is also important to raise the problem of vested interests. We include this extract from Hodgson who states the problem succinctly:

"Financial economists are less likely to speak out in favour of regulation when they have lucrative consultancy contracts with firms involved with derivatives, hedge funds and questionable financial innovations." ²⁸

real-world economics review, issue no. 50, 8 September 2009, pp. 151-156,

<http://www.paecon.net/PAERreview/issue50/Kaletsky50.pdf>

²⁴ Dirk Bezemer, Why some economists could see the crisis coming

Financial Times, Sept 7th 2009

<http://www.ft.com/cms/s/0/452dc484-9bdc-11de-b214-00144feabdc0.html>

²⁵ FSA head promises regulation revolution

Financial Times (Jennifer Hughes) February 26 2009

<http://www.ft.com/cms/s/0/e2789988-03a4-11de-b405-000077b07658.html>

²⁶ Robert Jones, Folly of excluding the hard-won wisdom of the past

Financial Times, Letters, March 5 2009

<http://www.ft.com/cms/s/0/28a5f70c-0927-11de-b8b0-0000779fd2ac.html>

²⁷ James K. Galbraith, Who Are These Economists, Anyway? THOUGHT & ACTION, FALL 2009

<http://www.nea.org/assets/docs/HE/TA09EconomistGalbraith.pdf>

See also, "The Financial Crisis and the Systemic Failure of Academic Economics"

by David Colander, et. al. Outcome of one week of discussions within the working group on 'Modeling of Financial Markets' at the 98th Dahlem Workshop, 2008.

http://www.debtdeflation.com/blogs/wp-content/uploads/papers/Dahlem_Report_EconCrisis021809.pdf

²⁸ Geoffrey M. Hodgson The great crash of 2008 and the reform of economics

Cambridge. Journal of Economics.2009; 33: 1205-1221

But the public understanding of the issues is distorted by a complete failure on the part of the media to investigate or even acknowledge that the problem of bias exists. As Mirowski observes:

"most conventional outlets for economic ideas have become willfully uninterested in the tangled conflicts of interest of the modern economics profession. Does anyone care that Martin Feldstein was on the board of AIG in the runup to its disastrous failure?Is anyone curious about the tangled history of the funding and organization of the Chicago School of economics? Does anyone care that Larry Summers worked for numerous hedge funds and investment firms before they had to be rescued by an administration that included...Larry Summers" ²⁹

Frequently, so-called 'independent economists' who are also employees of hedge funds or investment banks, are invited onto TV and radio to provide recommendations and comment on economic policy. We listen in vain for a qualification from presenters along the lines of 'they would say that, wouldn't they!'

We might also point out the importance of vigilance in questioning the origins of analysis of so-called 'independent' think tanks and 'institutes' whose macroeconomic analysis may have been 'outsourced' to the representatives of finance. ³⁰

Having established that there are significant reasons to challenge the status afforded to mainstream analysis and its policy recommendations, we are now in a position to provide substance to the alternative political economy approach to the crisis.

There is much information available which has been catalogued on a variety of 'topics' pages on the CPE site. For purposes of this brief review we will consider just three of the CPE pages which we suggest students might explore first. These are 'Financialisation', 'The Crisis and Marxian Economics' and 'The Crisis and Post Keynesian Economics'.

²⁹ Philip Mirowski, The Great Mortification: Economists' Responses to the Crisis of 2007--(and counting) The Hedgehog Review, Summer 2010

http://www.iasc-culture.org/publications_article_2010_Summer_mirowski.php

³⁰ See for example this extract from an influential report from the UK Institute for Fiscal Studies:

"This year's Green Budget has been produced in collaboration with David Miles and his colleagues at Morgan Stanley....Morgan Stanley argue that taxpayer losses from the Government's interventions in the financial system are most likely to be small, and there may even be a profit"..... "But there is clearly a danger investors will take fright at the state of the UK public finances, pushing up gilt yields.... "Given plausible projections for interest payments and social security spending, the Green budget estimates that Government will have to impose a real freeze on total spending by Whitehall departments".

Robert Chote, Carl Emmerson, David Miles and Jonathan Shaw, January 2009, More tax increases or spending cuts needed to pay for cost of credit crunch,

The IFS Green Budget: January 2009 <http://www.ifs.org.uk/publications/4417>

2.4 Financialisation

<http://www.politiceconomy.org.uk/financialisation.htm>

It is sometimes claimed by mainstream apologists that no one could have predicted the sub-prime crisis or its wider consequences and that it came as a complete surprise to everyone. Now while it is true that few could have predicted the precise timing and exact institutional details of the events of 2007/8, it is not true that all analysts were surprised.

Here we can identify a number of writers who have focused on the deeper structural changes that have taken place, both nationally and at the global level of economic relations. These have indicated a growing instability which it is claimed would inevitably result in crises. Indeed the 2007/8 crisis is just the latest of several financial crises which have a common theme.

We have already considered the importance that political economists attach to historical method (see 2.1). It can now be pointed out that for many researchers a full understanding of the Global Financial Crisis can only be gained by examining not just recent historical events, but more importantly a historical process that has taken place over several decades. This is a stance which is common to an increasing number of writers who refer to this process as 'Financialisation'.

The analysis covered by the term 'Financialisation' may be introduced by referring to the succinct definition provided by Epstein in the introduction to his 2005 collection³¹.

“the increasing role of financial motives, financial markets, financial actors and financial institutions in the operations of the domestic and international economies.”

Extracts from reviews of this book, contained on the CPE site, are also useful for gaining a feel for the scope of the literature.

For similar introductory purposes there are a number of excellent survey articles available online, which may be accessed from CPE. These include Thomas Palley's '*Financialization: What It Is and Why It Matters*'³² and Robert Guttman's '*Primer on Finance-Led Capitalism and Its Crisis*'³³.

³¹ Gerald A. Epstein (Editor)
Financialization and the World Economy
Edward Elgar Publishing Ltd; illustrated edition edition (26 Aug 2005)

³² Thomas I. Palley Financialization: What It Is and Why It Matters
The Levy Economics Institute Working Paper No. 525 December 2007

By way of example, we include the following extract from Palley:

‘Financialization is a process whereby financial markets, financial institutions, and financial elites gain greater influence over economic policy and economic outcomes. Financialization transforms the functioning of economic systems at both the macro and micro levels. Its principal impacts are to (1) elevate the significance of the financial sector relative to the real sector, (2) transfer income from the real sector to the financial sector, and (3) increase income inequality and contribute to wage stagnation. Additionally, there are reasons to believe that financialization may put the economy at risk of debt deflation and prolonged recession.....’

and these extracts from Guttman:

"This contribution to the debate on finance-led capitalism seeks to identify the principal structural changes in the nature of finance over the last couple of decades.."

and

“Ever since we responded to the worldwide stagflation crisis of the 1970s and early 1980s by deregulating banks and letting them reshape the workings of our economy, we have lived in a system dominated by finance”.

Continuing with the theme of putting analysis in a historical context, our next two CPE pages focus attention on contemporary analysis which has its origins in the work of influential thinkers from the past. An important characteristic of heterodox analysis which distinguishes it from the mainstream is the belief that fundamental ideas developed in earlier times have continuing relevance.

2.5 The Crisis and Marxian Economics

<http://www.politiceconomy.org.uk/subprimecrisis-marxian.htm>

Marxian political economy makes the inevitability of the crisis of capitalism central to its understanding of capitalism’s historical development. The relevance of this perspective to the current crisis can be understood with the aid of the links to a variety of recent books and articles. Links are provided to online bookshop purchasing details and to online synopses and reviews for the following books from

John Bellamy Foster and Fred Magdoff (2009) ³⁴ :

http://www.levy.org/pubs/wp_525.pdf

³³ Robert Guttman A Primer on Finance-Led Capitalism and Its Crisis

<http://regulation.revues.org/document5843.html>

³⁴ John Bellamy Foster and Fred Magdoff. The Great Financial Crisis: Causes and Consequences
Monthly Review Press U.S. Feb 2009

“an excellent example for the usefulness of studying Marx’s works and that of other Marxist political economists, e.g. the writings of Paul M. Sweezy and Harry Magdoff, in order to better grasp the dynamics and contradictions of the financial turmoil and its implications for social conflict”.

and

Leo Panitch, Sam Gindin and Gregory Albo (2010)³⁵ :

“With an unparalleled understanding of the inner workings of capitalism, the authors provocatively challenge the call by much of the Left for a return to a largely mythical Golden Age of economic regulation as a check on finance capital”

Illustrative extracts from online articles and discussions are also provided, such as this from an interview with Cyrus Bina who outlines the central features of a Marxist assessment of the crisis:

*“Such an assessment must inevitably include the dynamics of capital accumulation, necessity of the crisis, and the renewal and rejuvenation of the system with respect to redistribution of wealth and, especially, nature of class polarisation across the global economy”*³⁶

Other immediately accessible material includes collections of articles, such as those at the Workers Liberty Website³⁷, whilst direct access (with extracts) is also provided to contributions from Beitel³⁸, Beams³⁹, Harvey⁴⁰, Roberts⁴¹, Ure,⁴² Ismael Hossein-Zadeh⁴³ and Hudson⁴⁴.

³⁵ Leo Panitch, Sam Gindin and Gregory Albo
In and Out of Crisis, The Global Financial Meltdown and Left Alternatives
PM Press/Spectre May 2010

³⁶ Economic Crises, Marx’s Value Theory, and 21st Century Capitalism:
An Interview with Cyrus Bina, Radical Notes, 11th May 2010

<http://radicalnotes.com/content/view/133/39/>

³⁷ <http://www.workersliberty.org/marxists-crisis>

³⁸ Beitel, Karl. Understanding the Subprime Debacle. Monthly Review, May 2008.

<http://monthlyreview.org/080512beitel.php>

³⁹ Nick Beams. The World Economic Crisis: A Marxist Analysis
Lecture delivered in November and December 2008.

<http://www.wsws.org/media/nb-lecture-1208.pdf>

⁴⁰ Interview with David Harvey on the G20, the Financial Crisis and Neoliberalism
Democracy Now April 2nd 2009

http://www.democracynow.org/2009/4/2/marxist_geographer_david_harvey_on_the

⁴¹ Paul Craig Roberts. Dead Labor Marx and Lenin Reconsidered
Counterpunch October 7, 2009

<http://www.counterpunch.org/roberts10072009.html>

⁴² John Ure, Ageing capitalism from the Marxist perspective
Financial Times Letter to Editor, Dec 31 2009

<http://www.ft.com/cms/s/0/9f6519fa-f5ac-11de-90ab-00144feab49a.html>

⁴³ Ismael Hossein-Zadeh,

Holes in the Keynesian Arguments against Neoliberal Austerity Policy—It Is not “Bad” Policy, It Is Class Policy, July 22nd 2010
<http://heterodoxnews.com/htnf/htn102/%5BHossein-Zadeh%5DClass-Policy.pdf>

⁴⁴ Michael Hudson, From Marx to Goldman Sachs: The Fictions of Fictitious Capital, and the Financialization of Industry
Critique Journal of Socialist Theory, Volume 38, Issue 3 August 2010, pages 419 - 444

The CPE site contains several pages on topics related to Marx. (as shown in figure 1). From the current page, for example, the interested student might connect directly to a specific topic, 'Karl Marx: Money, Finance and Economic Crisis'. This provides links to seminal works by Marx as well identifying specific contemporary work on the financial aspects of Marx's writings.

Our final example of writers who have challenged mainstream analysis and policy are those of the Post Keynesian school of economics.

2.6 The Crisis and Post Keynesian Macroeconomics

We use the term 'Post Keynesian' to comprise those writers who derive their ideas from the fundamental insights of Keynes regarding the crucial role of uncertainty and the consequent importance of money and monetary institutions in understanding the vulnerability of a monetary economy to instability and crisis. This necessarily excludes those mainstream (so-called) 'Keynesians' who 'borrowed' their title and never grasped the meaning or significance of Keynes ideas, which "*now seem alien to a generation of economics professionals whose macroeconomics education has been systematically denied exposure to Keynes's fundamental insights concerning money and uncertainty*"⁴⁵. (More opportunities to explore these issues are available elsewhere on the CPE site.)

We may begin by pointing to the work of Paul Davidson. The CPE site provides access to several articles on the crisis which challenge the role of mainstream theory. Extracts are provided, such as the following:

*"What has caused this contagion to spill over and cause this tremendous increase in market failures? The answer is simple. This problem has developed as economists and market participants have forgotten Keynes's liquidity preference theory [hereafter LPT] and have, instead swallowed hook, line, and sinker the belief that the classical efficient market theory [hereafter EMT] is a useful model for understanding the operation of real world financial markets....."*⁴⁶

<http://michael-hudson.com/2010/07/from-marx-to-goldman-sachs-the-fictions-of-fictitious-capital1/>

⁴⁵ '.....Promoters of such ideas have been excluded to the "heterodox fringes" by the dominance of Chicago New Classicals and Harvard "New Keynesians", who have insisted on rational expectations models in which money is not a major source of movements in output, except where prices are sticky'.

Robert Jones, 'Ideas that will be alien to a generation of economists',
Financial Times, Letters December 31st 2008

⁴⁶ Paul Davidson, Securitization, Liquidity and Market Failure. Challenge Magazine May/June 2008

The Connections page also provides access to details and useful reviews of Davidson's recent book, 'The Keynes Solution'⁴⁷.

Particular importance has been attached to the writings of Hyman Minsky whose work in the 1980's on financial instability is now widely recognised to have had significant predictive relevance to understanding the genesis of the current crisis.

Much of Minsky's original work is available via the The Levy Economics Institute⁴⁸ and various links are included from the CPE page⁴⁹.

In the wake of the sub-prime crisis there have been a number of introductory articles about Minsky which have been published for a non-academic audience and which provide useful starting place for novice students. An example is available from the online investment advice newsletter, 'The Daily Reckoning'.⁵⁰

For applications of Minsky's analysis to the current crisis there are an increasing number of recommendations on the CPE page, including those by Fernandez et al⁵¹, Wray⁵², Kregel⁵³ and Galbraith⁵⁴

<http://econ.bus.utk.edu/faculty/davidson/securitizationprice%20talk10.pdf>

See also "Alternative Explanations Of The Operation Of A Capitalist Economy: Efficient Market Theory Vs. Keynes's Liquidity Theory" Real-World Economics Review, issue no. 50 2009

<http://www.paecon.net/PAERReview/issue50/Davidson50.pdf>

⁴⁷ Paul Davidson, The Keynes Solution, The Path to Global Prosperity, Palgrave Macmillan Sep 2009

"shows how the basic foundation of the Chicago School underlying Greenspan's policy decisions, as well as the likes of Friedman, Lucas, Scholes and Merton, led to errors that propelled America into the worst economic crisis since the Great Depression".

⁴⁸ The Levy Economics Institute of Bard College, <http://levy.org/>

⁴⁹ e.g. Hyman P. Minsky, The Financial Instability Hypothesis, Levy Economics Institute WP 74 May 1992

<http://www.levy.org/pubs/wp74.pdf>

⁵⁰ Simon Wilson "Hyman Minsky: Why Is The Economist Suddenly Popular?"

The Daily Reckoning Fri 13 Apr, 2007

<http://www.dailyreckoning.co.uk/economic-forecasts/hyman-minsky-why-is-the-economist-suddenly-popular.html>

⁵¹ Fernandez, Luisa, Kaboub, Fadhel & Todorova, Zdravka

On Democratizing Financial Turmoil:A Minskian Analysis of the Subprime Crisis.

Levy Economics Institute WP 548 Nov 2008

http://www.levy.org/pubs/wp_548.pdf

⁵² L. Randall Wray, Financial Markets Meltdown. What Can We Learn from Minsky?

Levy Economics Institute, Public Policy Brief April 2008 <http://www.levy.org/vdoc.aspx?docid=1049>

and

The Return of Big Government, Policy Advice for President Obama.

Levy Economics Institute. Public Policy Brief No. 99 March 2009 http://www.levy.org/pubs/ppb_99.pdf

⁵³ Jan Kregel

It's That "Vision" Thing: Why the Bailouts Aren't Working, and Why a New Financial System Is Needed

Levy Economics Institute. Public Policy Brief No. 100, April 2009

http://www.levy.org/pubs/ppb_100.pdf

⁵⁴ James K. Galbraith, A "People First" Strategy: Credit Cannot Flow When There Are No Creditworthy Borrowers or Profitable Projects, Levy Economics Institute, Strategic Analysis, April 2009

<http://www.levyinstitute.org/publications/?docid=1129>

This completes our brief tour of just some of the material available on the *Connections in Political Economy* website. We must point out that there are numerous other pages on the site and many of these are also relevant to the Global Financial Crisis, providing access to material on topics such as “The Debt Crisis and The Macro Policy Debate”, “21st Century Deficit Hysteria”, “21st Century Crisis in Europe”, “Corporate Power and Political Influence”, and “Dollar Hegemony”.

3 Concluding Comments

The global crisis, which began as a crisis for financial institutions and their immediate clients, was caused by the actions of a small, wealthy minority. This has subsequently had adverse effects on the welfare of the remaining majority, with sometimes devastating consequences for many innocent ‘bystanders’. It has inevitably created a thirst for understanding, not just among formal students of economics but also among the wider population.

At the same time, however, those with a vested interest in shifting the blame and therefore the cost of the crisis onto others, have made great strides in dominating the media and in influencing the public debate about policy

⁵⁵

The ‘Connections in Political Economy’ website is an attempt to raise awareness and understanding of political economy by providing access to the rich and diverse sources of analysis and comment that are available on a variety of issues. Those issues are represented in a series of interconnected maps which its hoped will help stimulate interest in the study of political economy at a wider and deeper level.

The present paper demonstrates the use of the website in the context of what is necessarily a brief guide to the political economy of the Global Financial Crisis. The examples which have been discussed for each ‘issue’ are by no means exhaustive. Also the issues covered on the site inevitably go beyond those which we have been able to cover in this introductory tour.

⁵⁵ Robert Jones, Vested interests ensure we won’t escape from this crisis
Financial Times, Letters, February 25 2010
<http://www.ft.com/cms/s/0/d6586ea2-21ae-11df-acf4-00144feab49a.html>

Figure 1 The opening menu page.

Phase 1 Development Funded by www.politiceconomy.org.uk About "Connections"
What is Political Economy?
Praise for this site

The Economics Network

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All pages

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Figure 2 A typical map of connections

Address <http://www.politiceconomy.org.uk/subprimecrisis.htm>

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Connections in Political Economy and Global Economic Issues

Explore the diverse analyses of national and global economic issues.

```

graph TD
    A["The 2008 Securitized Debt Crisis and its Macroeconomic Consequences"] --> B["21st Century Crisis in Europe"]
    A --> C["The 2008 Debt Crisis and Marxian Analysis"]
    A --> D["The 2008 Debt Crisis and the Macro Policy Debate"]
    A --> E["The IMF and the World Bank"]
    A --> F["Financialisation"]
    A --> G["The 2008 Debt Crisis and the Wall Street bailout"]
    A --> H["The 2008 Debt Crisis and Post Keynesian Economics"]
    A --> I["Financialisation: Economic Rent and the Rentier"]
    A --> J["References & Resources  
New Window  
Or Scroll Down this page"]
    
```

Also see specific Newspaper Comment and Correspondence on these these issues:-
[The Debate about the UK Fiscal Deficit](#)
[Global Imbalances](#)

Address <http://www.politiceconomy.org.uk/subprimecrisis-intellectualfailure.htm> Internet