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The Economic Problem

Man talks of a battle with nature, forgetting that if he won the battle, he would find himself on the losing side.

E. F. Schumacher, *Small is Beautiful*, 1973

Industrial humanity is behaving like King Midas. He turned his daughter into gold before he realised the limitations of his own conception of wealth.

Paul Ekins, *Wealth Beyond Measure*, 1992

What can Walt Disney teach you about financial crises? When the sub-prime mortgage crisis took hold in the spring of 2007, with the big financial players desperately beginning the search for exactly what lay in those structured debt investments they had believed were assets, the front line investigators were employed by a company in Connecticut, outside New York City, called Clayton Holdings. Clayton specialized in checking out risky mortgage loans for the big Wall Street firms, before or after they had been bundled up into the notorious structured investment vehicles (SIVs) that they were buying. It was at this point, checking one mortgage portfolio, that they found one that had been signed by the borrower simply as ‘M. Mouse’.

This was a symbolic moment. If Mickey Mouse can take out a mortgage, then the system is revealed to be without any of the checks and balances that are supposed to safeguard us all. Especially in the UK, people still believe that the great institutions that underpin our lives, known as banks, are dedicated to careful scrutiny and prudent lending: in practice, these institutions – like so many others – have been hollowed out, removing those checks, as well as those bank managers who might once have scrutinized Mr Mouse’s mortgage application and rejected it earlier.

It was a serious crisis, but it wasn’t exactly unprecedented. The Wall Street crash followed the great radio stocks boom. The 1987 crash followed the junk bond boom.

The dot.com ‘bust’ followed the dot.com boom. Now the 2008 crash has followed the property and credit boom. Although it always comes as a surprise to the people the novelist Tom Wolfe dubbed the ‘masters of the universe’, financial panic follows financial over-excitement, as surely as night follows day.¹ A handful of sacrificial lambs are blamed and sometimes even gaoled; regulations are tightened and loosened again. But the fundamental problem that the financial markets are the epicentre of a massive system, the main purpose of which is to make its key players unimaginably rich, is never properly addressed. Nor are the other structural problems of the economic system, which forgives the powerful their mistakes, and which cushions them against the hard times, and provides them with enough money to achieve their dreams, but exhausts the rest of us and punishes and corrodes the lives of the poorer two thirds of the world. ‘The economic problem’, as John Maynard Keynes put it, has not been solved, and there sometimes seems to be little prospect of solving it – even when its institutions suffer the kind of catastrophic collapse they suffered in 2008.²

The crucial fact is that the collapse of the financial markets is only a small part of the problem. It is simply the visible part of an iceberg that represents those crises the world faces which are driven by economic assumptions that no longer work. This latest unravelling – and there have been more than 40 currency crises since the Second World War – is the beginning of the end of the flawed dream that a handful of us could consume our way to economic nirvana. The planet can’t take it; the human psyche can’t take it; but economics seems to insist that we do it anyway. That looks increasingly like an impossible contradiction. Is there a way out?

This book suggests that there is: a ‘new economics’ approach, or to be more accurate, a bundle of approaches, that values real, rather than illusory wealth, and puts people and planet first. The good news is that there have been symptoms now for decades of the seeds of this new economics, which sets out to organize the muscles of the world differently. It is there in the emergence of local and ethical food, the rise of people’s demand for authenticity, in the rise of ethical business, ethical investment, fair trade and the massive growth in ‘downshifting’, in everyone from architects to economists learning from nature, of people deliberately earning less to have a better life. This new economics is based on a different framework: it recognizes a different yardstick of success. It is aware of the gap between money growth and real wealth. Its basic tenets are accepted in communities and in business alike, but have barely filtered into the ivory towers of government and their orthodox economic thinking.

The idea is not new. Books on the new economics have been written already, even if they did not use that term. But what was urgently needed was a book, written as much for non-economists as for the experts and specialists, which could set out the tradition, parameters, practicalities and claims of this new economics, and set these out in terms that policy makers can understand and use. We have tried to do that here by looking at the way the world works through the lens of the new economics, and

finding there some bizarre questions that seem to fly in the face of orthodoxy. Why do we work longer hours than some medieval peasants? Why are the best mechanics in the world Cuban? Why do we export as many chocolate waffles out of the UK as we import? Each one of these serves as an introduction to a different aspect of the new economics, whether it is the critique of the idea of wealth that lies at the heart of new economics, or whether it is the implications of that critique for money, trade, work or resources.

Those bizarre questions overlap, but they broadly cover the basic issues of the new economics, with a chapter of the book devoted to each – measuring wealth, money, markets, work, resources, trade, community and debt.

The sheer diversity of the immediate crisis – in credit, climate and energy – is also, paradoxically, an opportunity. Its sheer seriousness compels some response. The crunch is a combination of a credit-fuelled financial crisis, accelerating climate change and volatile energy prices underpinned by the encroaching peak in oil production. These three overlapping events threaten to develop into a perfect storm, the like of which has not been seen since the dustbowls, bankruptcies and unemployment of the Great Depression and quite possibly never before.

These immediate crunches are underlain by three fundamental crises: ecological, human and spiritual. These are not usually understood as economic problems, but that is exactly what they are: a by-product of faulty measurement and misleading values pedalled by an ill-directed economic system. These central crises are as follows:

The ecological crisis

The rising temperature of the biosphere is being caused by human economic activity, burning fossil fuels to drive the growth economy. As a result, the year 2005 was the hottest year ever. Carbon dioxide is at its highest level in the atmosphere for the last 2 million years, predominantly driven by industrial and human use of fossil fuels: the destruction of our natural capital for economic reasons, leading to climatic upheaval, more extremes of weather including increasingly severe droughts and floods, species loss and a real threat to the viability of the human food chain. If all the ice in the world melted, the sea would rise by up to 70 metres (m). But even a single metre will displace tens of millions of people in a country like Bangladesh, slightly more will be catastrophic for many parts of the world, flooding major cities and large parts of certain countries. Estimates also suggest that in the foreseeable future we are going to lose a quarter of our mammalian species, 12 per cent of our bird species and something like a third of our amphibians. The future for polar bears is bleak.

Then there is the inappropriately named ‘positive feedback’, when these changes cause knock-on domino effects. As the ice melts, there are less reflective surfaces, so less heat is reflected back. As more carbon dissolves in the sea, its ability to absorb carbon goes down, besides becoming more acidic and destroying coral reefs. As the sea warms, other greenhouse gases trapped in the sea bed stand to be released. As the tundra melts, it gives off methane and carbon dioxide. As the Amazon rainforest is destroyed, there is more drought, more fires, more destruction, less carbon absorbed and more released. These and many effects are described in the last report of the Intergovernmental Panel on Climate Change.³

The human crisis

This is the crisis of distribution. Despite two centuries of economic expansion and unprecedented growth in recent decades, around 1 billion people are going to bed chronically malnourished every night and 30,000 children are dying every day of preventable diseases. Behind those statistics lie individual stories of human tragedy all over the world. Worse, the inequality between those people and the wealthy has actually been increasing. In the late 19th century, the ratio of the richest 20 per cent in the world to the poorest was somewhere between 3:1 and 10:1. By 1960, the ratio between the richest and the poorest had grown to 30:1. By 1997, that had grown to 75:1.⁴ These are accelerating figures: now the richest 1 per cent of the world earn as much as the poorest 57 per cent of the world combined. At the same time, the poorest 5 per cent of the world actually *lost* a quarter of their real income.

The spiritual crisis

Yet even those who are among the winners under the current system are largely failing to benefit. Although gross domestic product (GDP) in the UK has doubled over the last 30 years, most measures of well-being have remained steady or dipped down. Similar studies are showing even some decline in well-being in most developed countries. The winners in the system are suffering from rising debt, rising stress, rising depression and mental ill health.

At the same time, the social glue that holds our lives together, and makes the economy possible, is also unravelling: families, neighbourhoods and relationships are fracturing under the pressure of high mortgages, benefit regulations and the kind of monoculture that drives out local enterprise, institutions and community life from many areas in the name of efficiency, centralization and corporate success.

When 12 million people in Europe are involved in some way in downshifting – earning less money for greater well-being – then you know the mainstream, which demands we should constantly accelerate our earning and spending, has a problem.⁵ Downshifting is incoherent in conventional economic terms, where people are assumed to maximize their income at all times. It is also evidence that

high growth economics does not necessarily produce greater well-being even for those who benefit financially.

Major change tends to emerge with the aid of economic catastrophe, though that is a depressing conclusion. Even so, it would have been hard to imagine, when the property boom was still at its height in the spring of 2007, that, within 18 months, governments would have been dusting off economic ideas that had been rejected for a generation or more, and would be desperate for new ones. The crash was predictable; the scale and speed of collapse was less so.

The immediate cause of the great unravelling was the so-called 'sub-prime' market, which was in itself nothing new. It was one aspect of the market that lent money to poorer people, at higher risk of default, in return for higher rates of interest. It had previously been a whole industry carved out between door-to-door loan sharks, shunned by the mainstream lenders. The big banks had been criticized on both sides of the Atlantic for failing the third of the population they considered unworthy for credit. But instead of expanding their own operations to cover them, they invested in 'sub-prime' companies to mop up the marginally bankable instead, and foremost among these was HSBC.

So it was hardly surprising that it was HSBC that revealed, in February 2007, that they were setting aside extra funds to cover bad debts in their American sub-prime lending portfolios. On the same day, one of the biggest sub-prime lenders in the USA, New Century in California, experienced a catastrophic loss of confidence after revealing a quarterly loss. Its senior executives were away in Ireland planning future projects: another metaphor for the faults of the system as a whole.

What had happened was that the investment banks believed they had discovered a way for mortgage lenders to lend money to poorer people at high rates of interest, but at negligible risk. What they did was to bundle the loans they had made together with a range of other loans from other markets, with varying degrees of risk, and sell them as safe investments. Then they could lend money from the sale to more investors and so on.

The disastrous model used by so many lenders meant bundling up their mortgages and selling them on, then using the proceeds to lend more. It meant that banks and other investors would buy the SIVs, getting the full value of the repayments over the years. The SIVs were then taken apart and reassembled into parcels called collateralized debt obligations (CDOs) and sold to hedge funds, which sold them on all over the world. Because these CDOs included debts from a range of different markets, they were believed to be insulated against risk: the mortgages might cause problems, but the other loans would offset the risk. That is how the credit ratings agencies Moody's and Standard & Poor saw it, giving them AAA ratings.

The trouble was that, once the truth about the sub-prime loans – M. Mouse and all the rest – became clear, this very safety aspect of the CDOs became their undoing. They could all rely on safe loans being in the package, but it also meant they could also rely on unsafe sub-prime loans being in there as well, and, as the default rate began to rise, that rendered them of doubtful and uncertain value.

By July 2007, Standard & Poor was threatening to cut its ratings on \$12 billion of sub-prime debt. A month later, the European Central Bank was pumping €95 billion into the money markets, as the flow of interbank lending, which banks need to deal with day-to-day withdrawals while their deposits are out on loan, all but dried up. A month after that, reports that Northern Rock was looking for emergency financial support from the Bank of England led to the first run on a British bank for over a century, with the alien sight of savers queuing for hours in the rain outside branches.

Since then, as we know, the crisis accelerated until most of the investment banks on Wall Street had disappeared, and – spurred by the bankruptcy of Lehman Brothers – most of the banks in Europe and North America were forced to accept state bail outs and partial state control, or went cap in hand to the sovereign wealth funds in the Middle East, to avoid bankruptcy. The economic assumptions of the past generation lay in ruins, the advice provided by the best financial minds had been disastrous, and occasionally fraudulent, and the architecture that runs the world's economies was broken beyond repair.

The epicentre of the disaster on the ground was by then the city of Cleveland, Ohio, where one in ten homes was repossessed and vacant, nearly every street blighted by boarded up properties and street gangs.⁶ With one in five US mortgages now sub-prime, many of them facing major hikes in the repayment rate after two or three years, more than 2 million foreclosure proceedings began in the USA in 2007 alone, many of them against people sold mortgages where the terms and interest rates were misrepresented to them, which is what happens when products are believed to be risk free by those selling them. Especially when those selling them are often paid on a commission basis, and are normally rewarded for the number of sales they achieve.

These sales were complicated by the bizarre packaging and repackaging of the actual mortgages into SIVs, and many families have been rescued by the fact that the final owner of their mortgage has, not surprisingly, mislaid the relevant paperwork, without which they are powerless to foreclose. The less fortunate mortgage payers found that huge unexplained fees had been added once they asked for help to delay payments, putting them even further in debt.

By October 2008 – financial crashes usually take place in October for some reason – the real question was whether not the financial system could survive. One estimate puts the total value of credit default swaps in the system, most of which include risky sub-prime loans, at as much as \$45 trillion: twice the total value of the

US stock market and three times the GDP of the US.⁷ The veteran investor Warren Buffett has already described derivatives, and other investment vehicles used by hedge funds and others, as ‘financial weapons of mass destruction’, and he may well be proved right.⁸ Certainly the events of the autumn of 2008 implied that something more serious was happening, as a series of major names – HBOS, Lehman Brothers, Merrill Lynch and all the others – were wiped off the map, driven out of business as much by the hedge funds as by any other mistakes they might have made. Governments have run up huge deficits propping up a banking system that may or may not be able to deliver any kind of recovery, except for itself.

The collapse of the New York and London economic model in 2008 may turn out to be as significant as the collapse of the Soviet model in 1989. If the financial system survives the crisis – and it usually does survive, despite the upheaval – it may briefly focus the minds of policy makers worldwide on the problems that lie behind these activities. As we write, the minds of most policy makers are obsessed with how to return to what they might call ‘business as usual’, but the sheer intractability of that – and the inevitability of another bust not far off when they do – might allow them to consider how self-destructive the system is and to ask themselves what kind of alternatives there are.

When, in February 2009, the bankers who were at the helm of the big UK banks gave evidence to the House of Commons select committee, they were unanimous that ‘nobody’ at the time had pointed out the risks. This was nonsense, of course, and evidence of the ivory tower where the masters of the universe have their dwelling. But if they had peered out of the window of that tower, and if the politicians do now, they might be forced to ask themselves why the system requires huge indebtedness, from rich to poor, just to chug on. Nearly all the money in circulation was created in the form of bank loans: under the current system we need these loans in order to have the money to exchange goods and services. And since most of that money began as mortgages, we need them – in this sense at least – in order to survive.

There is also the peculiar irrelevance to real life of this bizarre dance in Wall Street and the City of London, justified by their occasional ability to raise loans for productive expansion, but actually leaching vast fees and bonuses from the income of savers, pensioners, insurance payers and taxpayers. And behind that, there is a more fundamental problem: this global financial system, underpinning all our lives yet increasingly disconnected from real life, accelerates \$3 trillion through the system every day, nearly 90 per cent of which is speculation, mostly speculation in the foreign exchange markets.⁹ We find ourselves colluding in that system through our savings, pensions and credit card debts, but it has nothing to do with the job that the financial system is supposed to do – to facilitate the exchange of goods and services, to make capital available for people so that they can create productive businesses in the future.

The money system is no longer designed for this basic work of economics. Perhaps it never was, but its power is now huge. And, those who manage the world continue to accept the enrichment of those who run the system, under the misapprehension that some of those rewards will filter down to the rest of us.

We are living through a period when the politics of money has shifted. Fewer of the electorate are prepared to accept that enrichment of others, especially when the banks have so mismanaged the world. Fewer of us are prepared to be taxed more to prop up a failing financial system. The political shock of the collapse has led more people to look increasingly closely at money and where it comes from. Many of them are surprised to find that what they had assumed was no longer true. No, money hasn't been based on gold since at least 1931. No, money is not produced at the Royal Mint (no more than 3 per cent anyway). We have comforted ourselves with these cosy myths for generations. In fact, of course, the pound is worth what it is because of millions of transactions by foreign exchange dealers around the world. Most of the money in circulation is created by the private banking system as interest-bearing debt, and has to be paid back, plus a bit. We owe more than there is money to pay it off, but we keep the dance going by pulling off the trick year after year of growing the economy a little bit more – at least until the music stops.

These revelations, and the fury at the cost of bailing out the system again, may be enough, in themselves, to justify a mainstream search for a new kind of economics. The new economics is certainly a reaction against the narrow form of globalization that has gripped the planet, a combination of global deregulation of capital, a moral vacuum at the heart of the economic system, and a process whereby the powers and resources of nation states are handed over to monopolistic global corporations. This has been described as the 'neoliberal' agenda, though there is nothing very new and certainly nothing liberal about it, and its failures are increasingly obvious. But it is not just a reaction against globalization. In practice, the 'new economics', which has been emerging over the past three decades, has been as much a reaction against the results of the previous consensus, which drew on aspects of Keynes – the inflation, centralization and narrow measurements of success – as it has been against modern corporate globalization. It has a more fundamental critique at its heart, about the distance between money and real wealth.

'It may work fine in practice,' goes a joke the French make at their own expense, 'the trouble is, it doesn't work in theory.' Anyone who has sat through debates in Brussels or conferences in Paris will know all about the French love of theory, in contrast to the nuts and bolts obsessions of Anglo-Saxons about whether things will actually

work. So it is strange that Paris became the birthplace of an unusual revolt against the pre-eminence of theory over practice, of economic abstractions over reality and of statistics over real life. What is more, the rebellion by economics students had an impact that has echoed through the French establishment. A top-level inquiry recommended sweeping changes in the way economics was taught in French universities, backed by their education minister. It was one of the most successful coups by a branch of the new economics anywhere.

Calling themselves ‘post-autistic economics’ – ‘autistic’ is intended to imply an inward-looking, disengaged preoccupation with numbers – the movement spread quickly, but more quietly, to other universities in Britain and America. The movement’s leaders at the Sorbonne – Gilles Raveaud, Olivier Vaury and Ioana Marinescu – may not have had much of an impact on thinking outside academia, beyond causing mild consternation among econometricians. But their efforts may mark something more important: a growing disenchantment with the whole cult of measurement, statistics, targets and indicators, which has become such a feature of modern life, not just in the UK government, but around the world; and with the drift of mainstream economics away from the human reality it attempts to describe. As long ago as 1985, an article in *Atlantic Monthly* by Robert Kuttner suggested that universities were churning out economics students who were ‘brilliant at esoteric mathematics yet innocent of actual economic life’.¹⁰ The post-autistic campaigners were determined to do something about it.

Their campaign began with a web petition in June 2000 (www.paecon.net), protesting against the dogmatic teaching of neoclassical economics, to the exclusion of other points of view, and the ‘uncontrolled use’ of mathematics as ‘an end in itself’. Within two weeks, the petition had 150 signatures, many from France’s most prestigious universities, and *Le Monde* had launched a public debate. The call was taken up by students across France and, by the autumn, education minister Jack Lang had announced that he took the criticisms seriously, appointing the respected economist Jean-Paul Fitoussi to head a commission of inquiry.

He reported in 2001, backing many of the ‘post-autistic’ points. By then, there had also been a vitriolic exchange of articles by French and American economists, a counter-petition launched by the Massachusetts Institute of Technology, and a peculiar post-autistic petition by Cambridge PhD students in the UK – unusual in that the Cambridge signatories were too scared for their future careers to put their real names to it. There is certainly growing concern about the narrowing of economics: Cambridge economics professor Ha-Joon Chang has complained that economic history has been dropped from the curriculum.

But while post-autistic economics sprung from the economics profession, ‘new economics’ emerged from outside it. Both represent a critique of conventional economics – the ideas that underpin the rules by which the world is run – that is

primarily critical of the way that money measures the world. Both are sceptical of the claims that economics is a scientific and accurate representation of the real world. Together, and with other strands and critiques, they are reacting against economic assumptions that work so badly for most people and the planet, assumptions that may no longer be shared by most economists, certainly not all of them, but that have long since been adopted by those who advise policy makers. ‘Practical men, who believe themselves to be quite exempt from any intellectual influences, are usually the slaves of some defunct economist,’ said John Maynard Keynes.¹¹ Unfortunately for us, the current batch of practical men now rule the world. And the brand of economics they use is open to the following criticisms:

It ignores the planet

Conventional economics largely disregards environmental issues, and fails to take account of the damage done to the planet and to people. It ignores those side effects of economic success, the loss of rainforest, the pollution, the crime, dislocation and depression, all of which come under the heading of what economists call ‘externalities’.

It measures the wrong thing

Money measures value badly, and – to be more specific – measures of economic growth measure success badly as a result. The GDP is the money value of all the goods and services produced and exchanged in the nation in a year: it is the cornerstone of conventional economic success. Yet it is actually a means and not an end. Forgetting this skews the economic system, encouraging bad things that increase GDP and discouraging good things that don’t.

It misunderstands real life

Conventional economics assumes that markets work. It assumes that people have money or assets and can operate in the marketplace. It assumes we are isolated, rational individuals with all the information we need to make free choices, and that the uneven distribution of power is not a problem. It assumes that the price is an accurate reflection of such markets. In fact, of course, those perfect conditions never exist: many people have no power or assets to operate economically, and are anyway overwhelmed by the power of others.

It encourages vulnerability

Speak to poor cotton farmers in the majority of the world, and you realize that they are dependent, not so much on their own efforts, but on what happens to the world price of cotton, and on the \$4 billion of subsidies being paid to other cotton farmers, mostly in Louisiana and Texas, which allows the United States to dump cotton at

virtually no price onto the world market and devastate other producers.¹² What ought to be a level playing field – and is assumed to be in conventional economics – is often an unclimbable cliff, dominated by a handful of corporate monopolists, subsidised by tax paid by poor people in rich countries.

It colludes with short-termism

Most democratic systems are highly short term, based on a short electoral cycle, which encourages politicians to trade long-term change for short-term illusions of success. Financial bonuses in the private sector also fuel a short-term cycle, trapping their employees on the business equivalent of a hamster wheel, having to produce ever greater quarterly earnings.

It overvalues owners

Ownership by individuals of their home and enough land to make them independent is some guarantee of independence. But perpetual ownership by investors of companies excludes and devalues the work and imagination of other people involved in their success, and – since ownership extends way beyond most investment horizons – means an inefficient overpayment to investors.

It remains blind to values

The pursuit of pure markets by conventional economics blinds economists to those aspects that are beyond price – the ethics behind a product or the pursuit of well-being by earning less, rather than more. There is an increasing minority of people who want to reflect their values in the way they shop, invest and work.

It encourages consumption for its own sake

Because of the design of money, which has to be paid back plus interest, and the requirement for constant growth, the economic system has to move faster and faster just to keep still, generating new desires and unsatisfiable wants, leading to depression, disaffection and environmental degradation.

It encourages and relies on debt and indenture

Most of the money that circulates around the world was created in the form of debt that must eventually be paid off by somebody, plus interest. This represents a huge demand, not just on the indebted populations of the Earth, but on the planet's ability to produce enough to meet this constantly increasing demand.

Taken together, these criticisms reveal not just an economic system that is partially blind, but one that has no moral compass and is destructive of the environmental conditions on which civilization depends. It is an economics that assumes there is no

morality but supply and demand. Economics may have begun as a branch of moral philosophy, but it ignores the moral aspects of humanity, and other human aspects, as inconvenient for its theories. The result is a narrow economic system, which fails to reflect the real world, and is hurtling towards human and environmental limits. By putting economics back into its proper psychological and biological context, the new economics tries to return to those moral roots.

None of these are criticisms of markets in themselves. On the contrary, markets with clear social and environmental parameters can be effective ways for human beings to interact and get what they need. Amartya Sen, the Nobel prize-winning economist, said that ‘to be generically against markets is like being generically against conversation’.¹³ Markets are part of life, but they are not the same everywhere. They can be vibrant and bustling at street level in towns and villages, binding communities together. And, on a larger scale, they can be faceless, bland and destructive, the economic equivalent of aerial bombing, in which the pilot never gets to see the damage they cause on the ground. Their problem is the imbalance of power between those taking part, the measuring system they use, and the ecological context in which they have to provide feedback.

Behind them is a more fundamental problem about the claims to pre-eminence of conventional economics. Despite its flawed representation of the world, economics claims pride of place in policy discussions. Even media debates about the benefits of supermarkets or new airports end with this conundrum: the economy makes everything else possible, so it comes first.

This has led to a perverse upending of nature. The economy is supposed to serve the needs of people and planet, but the reverse is increasingly true. The privileges given to the private and financial sectors are justified by the way their success is supposed to serve the interests of society. People’s worth is increasingly judged by the value they create in the economy contributing to GDP growth, a process that seems to have been internalized so that people often see material possessions as the main source of self-worth. Yet beyond a relatively low level of satisfying needs, we are no happier.

Thanks to the deregulation of capital controls, the state itself is also increasingly subordinate to the needs of business and finance, and openly so. This is partly a logical consequence of the focus on income and profit growth: the business and financial sector are seen as the means through which this can be delivered, and so their needs are given priority. Also, the state’s tax revenue is, directly or indirectly, connected to the activities of these sectors, making their views influential.

The combination of all this means that the purpose of social, health or education spending, for example, is not to make people healthy and well for their own sake, but to increase their productivity. In the same way, education is not seen as a good thing in itself, but is valuable because it equips people with the skills needed for business to

compete in a globalizing world. In fact, everything becomes important and defined according to the ways in which it can increase this narrow profitability, primarily for corporations. Policy regards people simply as passive consumers of goods or services, which are ‘delivered’ to them by service providers. Energy consumption is profitable under this narrow interpretation of economics, but energy conservation is more problematic, so we consume. Health care consumption is profitable in the short term for providers, preventative health is not, so we become consumers of health ‘solutions’.

The pre-eminent profit motive also makes companies grow to increase their profits and grow yet more. This is facilitated by financial institutions, which have themselves grown to an enormous scale, but which also profit from arranging mergers and acquisitions in the business world. In the public sector, cost considerations, and the desire to centralize control, fosters a culture where bigger is better, and narrow economic efficiency considerations preclude holistic approaches and local participation in the delivery of public services. Even voluntary sector organizations, charities and social enterprises find that narrow short-term efficiencies of scale allow them to undercut smaller competitors when tendering for contracts, enabling them to grow yet more and drive out smaller organizations.

The result is a centralized sclerosis where giant corporations, public and private, dominate the details of people’s lives, alienated from the people they serve and – measured by narrow short-term profits – are increasingly ‘efficient’. But in their failure to engage the imagination and efforts of the vast majority of people on the planet, and their failure to deal with the holistic needs and skills of those they serve, they are massively inefficient.

At the heart of all this is the problem of money, its design, what it does and how it is allowed to behave, and the fundamental and ruinous disconnection between the idea of money and wealth. Conventional economics measures money, and assumes that it is real and valuable in itself; worse, that everything can be reduced to it, and so misunderstands the way the world is. That critique is both ancient, as old as money itself, and newly urgent, because it goes some way to explain why the economic system is working so badly for most of us.

But there is a more important implication than that. Conventional economics justified itself on the grounds that it was necessary to drag people out of poverty. ‘We have to pretend for a while that foul is useful and fair is not,’ wrote Keynes, warning that economics still needed to use people’s competitive instincts more than their collaborative ones.¹⁴ But it is increasingly clear that the reverse is true: like a casino the economic system that dominates our lives does not improve people’s lives, except for the tiny minority that it makes massively wealthy. It creates poverty every day, encouraged by faulty measurement and rigged institutions that favour the very rich. We can leave that economic system in place and battle to ameliorate its effects, or we

can build a new economics that does what the economic system claims to do. How to do so is the question that the new economics struggles with.

You can see the real economic effects of casinos if you climb 250m up into the Rocky Mountains in Colorado, where the air begins to thin, to the former Gold Rush town of Black Hawk. ‘Population: 350’, it used to say at the foot of the hill, but the legalization of gambling in Colorado in 1991 changed that overnight, and changed everything else too. Go there now and you find yourself directed by men in dark glasses at the tiny crossroads in the town centre, and almost every building from the Silver Hawk Saloon to the end of the town is now devoted to gambling – Doc Holliday’s Casino, Bonanza Casino, Crook’s Palace, Bronco Billy’s.

You can go there virtually as well, at www.blackhawkcolorado.com, to see what gambling does to a local economy. ‘We might point out that if you visit Black Hawk, leave your children at home,’ says the website. ‘Black Hawk is not a friendly place to people under the age of 21.’ Almost every economic activity apart from gambling has been driven out. Thanks to the legalization of gambling, nothing else is viable in Black Hawk. Which is why the manager of Central City, which has all but merged with Black Hawk, now says anyone thinking of opening their community to gambling ‘needs to have their head examined’.

So when other governments around the world, notably the British, began to consider super-casinos as a source of steady income for local government, this was based on a fallacy, itself based on a fundamental misunderstanding about money. Because all money is emphatically not the same. There is money that comes into the town, shakes a couple of hands, and disappears again outside the area into the pockets of investors and multinationals. There is also money that stays put, and recirculates among productive local enterprises, building local wealth.

But there is another kind of money as well: the kind that drives out everything else because it is so profitable and so corrosive. Gambling is one of those activities that replaces productive business and people by shady figures in dark glasses. For some reason, policy makers and old-fashioned economists find it bizarrely difficult to distinguish between these – perhaps because highly centralized nations listen only to their Treasuries, and they get the money either way. But this is another example of the short-term thinking that led those same Treasuries into the economic disaster of 2008 and its consequences, and that may lead to some broader thinking as a result.

What Black Hawk reveals is a more fundamental problem with the way money behaves through what Keynes called the ‘activities of a casino’. Those activities are so immensely profitable to those who run the casinos that other businesses become uneconomic. Speculating with money has so many rewards, which is why so many

previously productive corporations have hived off their production and remain empty shells run by their financial service departments, shifting what assets they still possess between shady tax havens to avoid national taxes. Porsche, the car maker, for example, made far more from speculative financial deals than from selling cars. So is it really a car maker that dabbles in finance, or a hedge fund that happens to sell a few cars?

The problem is that money used to measure value – real, human value – does it very badly: that is the starting point of the new economics. Money measures some aspects very well, such as short-term financial risk and returns, but it is also partially blind to the assets represented by people and planet. An economic system based on the idea that money measures value effectively is likely to devalue those assets, to forget them and ultimately to preside over their destruction – and therefore ultimately its own destruction.

The outlines of the new economics, and how it emerged, are the subject of the next chapter. But, fundamentally it is a new definition of wealth. It is everything that follows from the central discovery that money and wealth are not the same, that money is a means to an end – and not the only means required either. By unshackling itself from this ancient mistake, the new economics subsumes the old idea of an economic science into broader ideas of the way the world works. It resumes its proper place as a subset of biology or psychology in the way it explains the planet and the way people behave. It becomes the study of how human beings, and the places they live, can reach their full potential – using the far broader assets that they have at their disposal, which are not always reducible to money. The new economics is the rejection of money as the totemic centre of a pseudoscience. The next chapter describes how it came about.

Other books to read

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Notes

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