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Greed, Risk-Taking, and Bubble Economies: The Failure to Learn

In economic and financial terms, last week was one of the most turbulent since the 2008 financial collapse that pitched us more deeply and permanently into the recession that was already underway, turning it into the Great Recession. Last week the stock market surged up and down by hundreds of points a day, panic over the European debt crisis rose and fell, and news on the performance of the American economy alternated between very bleak and somewhat hopeful, given our now limited expectations.

Some of this turbulence is tied to the high stakes gambling that still dominates Wall Street and financial markets around the world. Computer-based programs that buy and sell millions of shares of stock in seconds whenever the computer programs sense a trend up or down lead already somewhat volatile markets to swing wildly.

Much of the European debt crisis is also tied to this sort of speculative behavior. Huge amounts of money are being bet that various countries' government debt will go into default, and those bets make it more and more likely that that will happen, triggering another financial meltdown. Regulators in much of Europe finally temporarily outlawed this type destructive speculative gambling that was undermining efforts to stabilize Europe's financial system.

All of this is a sign that the very speculative forces that led to the financial collapse back in 2008 are back in the saddle and making fortunes on their high-stakes gambling that often indirectly impoverishes the rest of us as it chokes off spending and real economic activity. Our and the world's economies are still being disrupted by greed run amok in the search for super profits.

It could be argued that there is nothing new here. That is how financial markets have always operated with the resulting bubbles and bursts. If we look back over the last 500 years since worldwide trade began, one can see large numbers of such booms followed by busts in spices, sugar, tobacco, slaves, "new" land, furs, metals, energy resources, etc. Instead of talking about recessions and depressions, the earlier language described periodic "financial panics." The Great Depression eighty years ago was the last such big and long-lasting bust.

As the decades passed without a recurrence of such deep economic collapse, one might say we grew complacent. Bankers, investment analysts, and economists talked confidently about having put in place regulations and institutions that prevented such deep and long lasting declines from ever happening again. And there was some evidence of that. Since the early 1980s we had almost 30 years of more or less steady expansion in the national economy. Recessions in the early 1990s and early 2000s were so mild that much of the Western states did not really experience them. The expansion during the Reagan years set a record in terms of the length of that expansion. Then the expansion during the Clinton years broke that record.

What was impressive about those expansions was not that there were no financial shenanigans or crises, but how successfully we were able to digest them and returned to a growth path. We had the corruption of the Savings and Loan institutions which were looted by greedy hucksters and collapsed in insolvency. We had waves of hostile takeovers funded by junk bonds that raided healthy companies' assets. We had the high tech stock bubble built around high valued companies that had never produced a thing or earned a dollar of profit. We had the Latin American and Asian debt crises. We had the collapse of Enron and other huge, high-rolling, speculative companies. But somehow the economy took these financial stumbles and massive losses, tied to greed, phony accounting, and wishful thinking, in stride and continued on.

That may have given us a false sense of the reliability of our regulatory institutions and the actual safety of high-stakes financial speculation. We relaxed the regulations put in place following the Great Depression and also allowed a whole set of "shadow" financial businesses to develop completely outside of any regulatory structure.

Driving all of this, as with the previous financial bubbles, was the search for super profits. Where once investors may have been satisfied with a three to four percent return over inflation, returns that actually matched the rising productivity of the economy, investors were now told that that was chicken feed and that companies with such "low returns" were failing and there assets had to be taken over and used "more productively."

Most of the time the higher returns were generated by borrowing more and more money, leveraging a relatively smaller and smaller equity investment in more and more risky undertakings. The returns on the equity part of the investment were spectacular, the risk associated with the high debt and uncertain returns were ignored or hidden, and grand houses of cards were constructed.

The outcome of this last financial bubble was the same as the dozens of previous bubbles. In each of those bubbles, as one commentator has put it, participants kept chanting the mantra: "**<u>This</u>** time will be different. This bubble can grow forever." It was convenient and temporarily convincing group-think that ended in collapse, economic waste, and social pain.

Although looking back the collapse into our Great Recession is not surprising, what is disturbing is that the very greed and speculative behavior that got us deeply into the Great Recession has reemerged and continues to threaten our financial and economic stability. Apparently we have not suffered sufficient pain to emphatically say "enough is enough" and rein in those financial speculators who grow rich while continuing to gamble our future away.