CRISES AND (THE ABSENCE OF) ETHICS: INSEPARABLE MAGDEBURG SPHERES?

Stephan V. Arthur *

Abstract

Ethics and trust can avoid crises, just as, as recent events have clearly proved, the reverse is true. The paper is simply constructed: Section 1 provides a historical analysis; Section 2 deals with today's situation, drawing similarities and differences and the possible outcomes thereby arising; the final section concludes. Historical data are difficult to come by for most countries, especially when they should also be comparable across time. In general, and for this reason, US data have been used: however, the situation in other countries was little different, as will be shown, so that the data may be considered to be representative.

Keywords: Business cycle, depression, banking industry, equity market, credit

** Formerly of the Bank for International Settlements*

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Introduction

In 1654, outside the town of Magdeburg, Germany, Otto von Guericke proved that the forces generated by creating a vacuum, in this case within two halves of an evacuated sphere, were sufficiently large to withstand the joint power of 16 horses. Metaphysically speaking, nothingness was stronger than something measurable. Ethics and trust can avoid crises, just as, as recent events have clearly proved, the reverse is true.

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1. A historical analysis

The following quotations are taken from the Bank for International Settlements (BIS) 2nd Annual Report of 1932:

- *"One of the objects of the Bank (the BIS) is to facilitate collaboration between Central Banks – collaboration not only in connection with the maintenance of monetary stability but also in connection with a better organization of credit in the respective markets and the facilitation of international capital transactions."*
- *"The year under review has been one of dramatic occurrences in the whole field of international finance, credit, monetary stability and capital movements, both public and private. The record of this year of unparalleled world-wide disturbance reflects itself in the progress, resources and activities of the Bank ..."*
- *"Events of this second fiscal year*[12] *have shown to what extent our monetary systems, both great and small, have become interdependent, and how internationalism in monetary matters is not merely a theory or a desirable evolution but an accomplished fact."*

12 1 April – 31 March is meant here, which also was, and is, the BIS financial year.

It is precisely this last quote which illustrates that globalisation – so much in use today – is not at all a new concept. Granted, the internationalism referred to in 1932 was perhaps not as encompassing as is now meant, but, even today, at least in the minds of most economists and politicians, large areas of the globe are still excluded, for example, much of Africa which remains, in global economic terms, a pinprick on the map.[13]

Much has been made recently of the parallels between the present financial crisis and that of 1929 which triggered the Great Depression. This is hardly surprising since, at least in the United States, the present recession is clearly the worst since that of 1929,[14, 15] which, in itself, was the worst – and longest – that the World experienced during the whole of the 20th Century. Perhaps too little has been made of the differences, and certainly there has been little mention of another recession period known as the Long Depression, which, again at least in the United States, was, according to the National Bureau of Economic Research (NBER), the longest identified period of contraction since 1855.

The NBER, which is the official body for such matters in the United States, does not define a recession in terms of two consecutive quarters of decline in real GDP (the common definition used by many economies). Rather, a recession is a *"significant decline in economic activity spread across the economy, lasting more than a few months, normally visible in real GDP, real income, employment, industrial production, and wholesale-retail sales."* Understandably, evaluating such data takes considerably longer: for example, the most recent decision of the Business Cycle Dating Committee of the NBER, which was to announce the present cycle's peak as being in December 2007, was on 1 December 2008. Such a time lag of 12 months is, for example, from an investment banker's viewpoint, of very limited use, but his reaction to a perceived situation may well actually help to trigger that situation to either occur or be exacerbated, something that has recurrently been observed in the equity markets, most recently since September 2008.

13 "When America sneezes, Europe catches a cold, Asia develops pneumonia and Africa's tuberculosis gets worse" is still a common adage in the English language.

14 All actual data and period references are as of 31 October 2009.

15 However, 3rd quarter GDP (positive) growth was surprisingly strong and gives an initial indication that the recession may be over. Indeed, if 4th quarter figures are similarly strong, 2009 growth will only minimally be the wrong side of zero. Nonetheless, the picture remains bleak in the major European economies.

Table 1. US business cycles

Period	Number of cycles	Average contraction (in months)	Average cycle length (in months)
1855 – 1886	6	29	64
1887 – 1917	9	18	41
1918 – 1944	6	18	54
1945 – 1972	6	10	56
1973 – 2007	5	11	84
1855 – 2007	**32**	**17**	**57**
Sources: NBER; author's calculations.			

Returning to the NBER's work on defining business cycles and drawing from their data, Table 1 groups the 32 identified business cycles over approximately 30-year sub-periods, which vary slightly in length depending on the end of a particular cycle. The table illustrates the following: contractions (i.e. from peak to trough) have, since the end of World War II, been relatively short and considerably shorter than the previous 100 years. In the last sub-period – and this includes the downturns caused by the oil shocks of 1973 and 1978/9 – the US economy was in contraction for only 13% of the time. In fact, since July 1990 until end-2007, it has been in recession for only 16 of these 234 months! Even over the whole 153 years, the US economy has been in expansion for 70% of the time.

The table hides several salient features: the last contraction started in March 2001, so, statistically speaking, the next was long overdue (a cycle lasts around 5 years on average). The three longest expansionary periods of at least 7 years have all occurred since the 1960s, two of which – totalling almost 18 years – have been since November 1982! The longest period of contraction – 65 months – started in October 1873 (the Long Depression), followed by the 43 months from August 1929 (the Great Depression).

What the table also does not show are the magnitudes of the cycles, i.e. the severity of the crisis and the extent of the recovery: generally speaking, the shorter the cycle, the less intense the crisis and the smaller the (need for) recovery.

As the majority view is that we face depression (rather than recession), this paper concentrates on the Long and Great Depressions. History teaches us that, although a single event can trigger others more momentous – for example, the assassination of Archduke Ferdinand in Sarajevo on 28 June 1914 – it is rarely that that event is, in itself, isolated, but a result of others, often disparate and in the distant past. Historian economists have this in mind when discussing cause and effect.

Consequently, the events leading to the Long Depression were equally diverse and had effects long after this particular depression had ended. Not all the details or causes can be given here, but the following are the most major.

Post-Civil War overexpansion. In America, with the end of the Civil War in 1865, the economy expanded rapidly. The railroad industry, the nation's second largest employer (after the farming industry), laid, in the seven years preceding the depression, 56,000 kms of track. As a result, the amount of capital required was enormous, but so was the degree of risk, with little foreseeable short-term return on investment.

Black Friday. On 24 September 1869, thousands of overleveraged speculators – a term not uncommon today – were ruined when gold premiums collapsed, itself caused by a bank trying to corner the gold market and being prevented from doing so by the US Administration flooding the market with government gold.

Treaty of Frankfurt. Apparently unrelated, in Europe the Treaty of Frankfurt was signed on 10 May 1871, ending the Franco-Prussian War. Apart from the loss of large tracts of land to the Germans, the French were obliged to pay war reparations which it completed ahead of schedule two years later. The terms of the treaty were to find their precise counterpart almost 50 years later at the end of World War I, an act which was arguably at least partly causal for the rise of the NSDAP. However, back to 1873: the German economy boomed as a result of this foreign "investment", but it too, like the United States, resulted in overexpansion.

Fourth Coinage Act. This Act, signed into law on 12 February 1873, demonetised silver and moved to a gold standard. Previously, silver officially backed most nations' currency, but, due to the Napoleonic Wars, the United Kingdom was the first to move to gold. By 1879, most other countries had followed suit, including the Latin Monetary Union.

A notable exception was China, which retained the silver standard: as a direct result, its economy suffered the least 60 years later, when adherence to the gold standard became a causal factor in the Great Depression. In 1873, the immediate effect was, naturally, to depress silver prices, but it also led to a contraction in the money supply. This in turn placed an impossible burden on the heavily-indebted farming industry and the cash-hungry railroad companies.

Vienna Stock Exchange crash. Back in Europe, the Vienna Stock Exchange crashed on 9

May 1873: as the Austro-Hungarian Empire was the fifth-largest economy in Europe, this was not an insignificant financial event.

Jay Cooke & Company fails. On 18 September 1873, this Philadelphian investment bank, which, like many other banks, had heavily invested in railroads, failed. This was the straw that broke the nation's back. The New York Stock Exchange closed for 10 days; many banks failed. At the peak of the depression, the unemployment rate rose to 14% in the United States, wage cuts led to social unrest and, in all, at least 15,000 businesses failed. In Germany, there was a move towards protectionism; there and in Austria, the Jews were blamed for the economic collapse – recall that this is 1873, not 1933!

Table 2 illustrates, as well as possible, due to the scarcity of reliable data, the effects on the US economy. On the face of it, conditions, if you had work, were not too bad: production and productivity rose, prices declined and money supply was contained (indeed, real money supply declined). However, these last two points should give cause for concern, and especially so since prices declined further for the next 20 years, bottoming out only in 1899; prices only returned to their 1873 level during World War I. The same phenomenon will be observed later.

Table 2. The Long Depression – core data

For 1873 – 1879	Measure	Value
Unemployment	Peak rate	14%
Real GDP per capita	Average growth	+2.0% p.a.
Consumer price inflation	Average	–3.0% p.a.
Money supply	Average growth	+2.6% p.a.

Several events leading to this episode in American history apply equally today and, more so, in 1929, when the collapse of the New York Stock Exchange on 29 October arguably – but certainly visibly – triggered the Great Depression. Rather than cite events leading to this depression, a consideration, in chronological order of publication, of the views of leading economists as to the root cause or causes may be useful. The list is not exhaustive but certainly contains the most influential opinions.

Inequality of wealth and income. Already in the 1920s, Catchings and Foster argued that consumers had insufficient income to purchase the goods which the economy produced, and unequal wealth distribution caused the depression. They argued that the economy would only recover if the government produced money to encourage consumer spending, at the same time reinflating prices and wages. In fact, the United States went, as during the Long Depression, through a period of strong deflation. Their opinions are interesting insofar as similar arguments are propagated today, not least because, in the 1930s, their ideas were instrumental in Roosevelt's New Deal.

Debt inflation. Irving Fisher, in the Depression's final year (1933), argued that the banks' exuberance to give credit at very favourable terms naturally led to over-indebtedness, fuelling speculation and asset bubbles. This all sounds familiar and, unsurprisingly, Fisher's views are shared by the present Chairman of the Federal Reserve, Ben Bernanke. To put matters into perspective, margin requirements were 10%; today's capital ratio as stipulated by the Basel Committee is 8% and Lehman Brothers' capital ratio, immediately prior to failing, was between 3 and 4%! Furthermore, Fisher postulated nine chain of events which are drawn into the later discussion on today's situation.

Classical Keynesian. Naturally, no list can be complete without the theory of John Maynard Keynes, unquestionably one of the foremost economists of the day. He argued in 1936 that if public savings increased, consumption would fall as would interest rates. Lower interest rates should, in theory, lead to increased investment and demand should remain constant. However, if businesses invest based on profit expectations, they would be disinclined to do so if consumption would decline further. This could then lead to a depression.

Classical monetarism. Should the reader find this argument weak, then perhaps more favour can be found with that of Milton Friedman and Anna Schwartz. In their view (published in 1963), the Depression was caused by the fall in the money supply: people saved more and consumed less. As a result, production fell, unemployment rose and prices could not react sufficiently quickly to stop a worsening spiral. In addition, they bluntly blame the Federal Reserve – established in 1913 – for failing to use policies and take corrective action.

Ben Bernanke was invited to speak on the occasion of Friedman's 90th birthday on 8 November 2002. His speech is recommended, since it gives a very succinct account of events from 1929 to 1933 from the Federal Reserve's perspective, linking them to the episodes identified by Friedman and Schwartz. He ends – and recall that he was not yet its Chairman – with the words, *"Let me end my talk by abusing slightly my status as an official representative of the Federal Reserve. I would like to say to Milton and Anna: Regarding the Great Depression. You're right, we did it. We're very sorry. But thanks to you, we*

won't do it again." It appears that he has taken his own promise to heart.

"Austrian school". In the same year, 1963, Hayek and Murray Rothbard, in reply to Friedman's hypotheses, argued that the Federal Reserve was indeed largely to blame, as it had expanded the money supply in the early 1920s and only tightened belatedly and, as it transpired, insufficiently, in 1928. Furthermore, the Federal Reserve effectively regulated the amount of credit that private banks could issue and the monetary expansion led to an unsustainable credit-driven boom.

The Gold Standard. Finally, in this "tour de table", a review of the Gold Standard is necessary. Due to the cost of World War I, many countries abandoned the gold standard, but returned to it at the pre-war price of $20 per fine ounce. In order to pay the war reparations demanded by France in gold, Germany was forced to endorse a credit-financed industrialisation process to stimulate exports. The United States also lent money to Germany to help in this process, and France paid off its debts with the United States and the United Kingdom using the money from the German reparations. This eventually disastrous vicious circle led to the drawing up of the Dawes plan, and the whole was overseen by the institution created for that purpose, the BIS. Hence the opening citations in this paper from the BIS 2nd Annual Report and where, later in the same report, it explains how most of the Bank's energies were devoted to addressing the resulting turmoil.

Table 3, in much the same way as Table 2, illustrates the effects of this depression on the US economy. Comparing with the earlier table, it can easily be seen that the effects of the Great Depression were much greater and, indeed, more in keeping with what one would expect: consumer confidence and spending declined, new money was neither needed nor forthcoming, all causing prices to fall; production was cut back, unemployment rose and GDP fell. This naturally led to the vicious spiral feared today, with unemployment peaking at rates not seen since in the United States. Unlike the Long Depression, measures taken in 1933 by the Administration – Roosevelt's New Deal – quickly restored confidence and the US economy was pretty much back on track by 1936. Given the political developments in Europe, this would prove to be, literally, life-saving.

Table 3. The Great Depression – core data

For 1929 – 1933	Measure	Value
Unemployment	Peak rate	24.9%
Real GDP per capita	Average growth	–8.1% p.a.
Consumer price inflation	Average	–6.7% p.a.
Money supply	Average growth	–7.0% p.a.

In the summer of 1932, Franklin Delano Roosevelt, in his acceptance speech as presidential candidate of the Democratic Party said, *"I pledge you, I pledge myself, to a new deal for the American people."* He won the election by a landslide. On Inauguration Day,[16] his speech contained the following excerpts:

- *"... the only thing we have to fear is fear itself – nameless, unreasoning, unjustified terror which paralyzes needed efforts to convert retreat into advance."*
- *"... there must be an end to a conduct in banking and in business which too often has given to a sacred trust the likeness of callous and selfish wrongdoing. Small wonder that confidence languishes, for it thrives only on honesty, on honor, on the sacredness of obligations, on faithful protection, on unselfish performance; without them it cannot live ..."*
- *"Faced by failure of credit they have proposed only the lending of more money. Stripped of the lure of profit by which to induce our people to follow their false leadership, they have resorted to exhortations, pleading tearfully for restored confidence. They know only the rules of a generation of self-seekers."*
- *"Finally, in our progress toward a resumption of work we require two safeguards against a return of the evils of the old order; there must be a strict supervision of all banking and credits and investments; there must be an end to speculation with other people's money, and there must be provision for an adequate but sound currency."*

Within two months, Congress had passed laws reforming the banking industry, and laws providing emergency relief, work relief and agricultural programmes. Two years later, a second wave of laws included trade union protection, programmes to aid tenant farmers and migrant workers and the setting up of Social Security programmes (this last point will be revisited).

16 Held until then on 4 March, a date Roosevelt himself later in the year changed to the present 20 January.

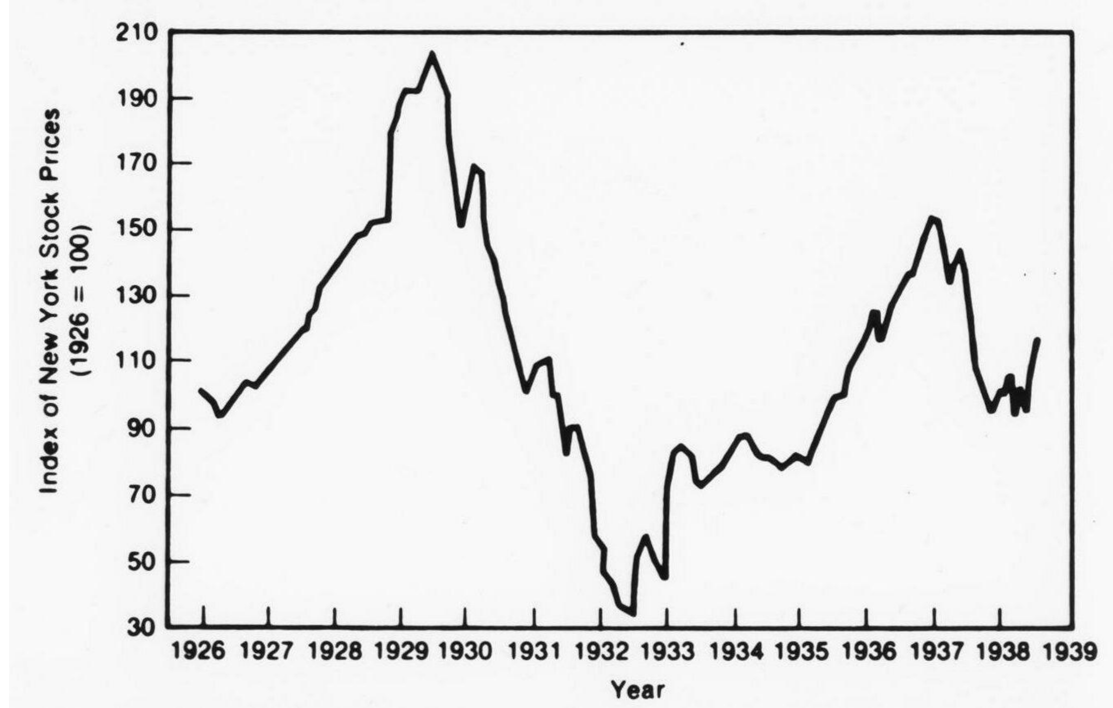
Roosevelt's words are somewhat chilling for two reasons: the first is that clearly history can and does repeat itself. The second, closely linked, is that we appear to be incapable of learning by our mistakes. 76 years on, Roosevelt's words and actions could equally have come from the present US President: indeed, in slightly different terms, they have.[17]

2. The situation today

Equity markets and the banking industry. In the first 17 months from the 1929 peak, the New York stock exchange fell by just over half (Graph 1). It then recovered very slightly – the blip towards the end of 1930 – before continuing its decline: by mid-1932, i.e. before Roosevelt's presidency, the stock market had shed around 85% from its peak value! As a result of Roosevelt's election – and, prior to that, his acceptance of the nomination – the stock market recovered sharply.

17 In the 10 months of his Administration, various measures, or at least the promise of them, have, in part, been announced: at best, the jury is still out.

Graph 1. The New York Stock Exchange index around the Great Depression

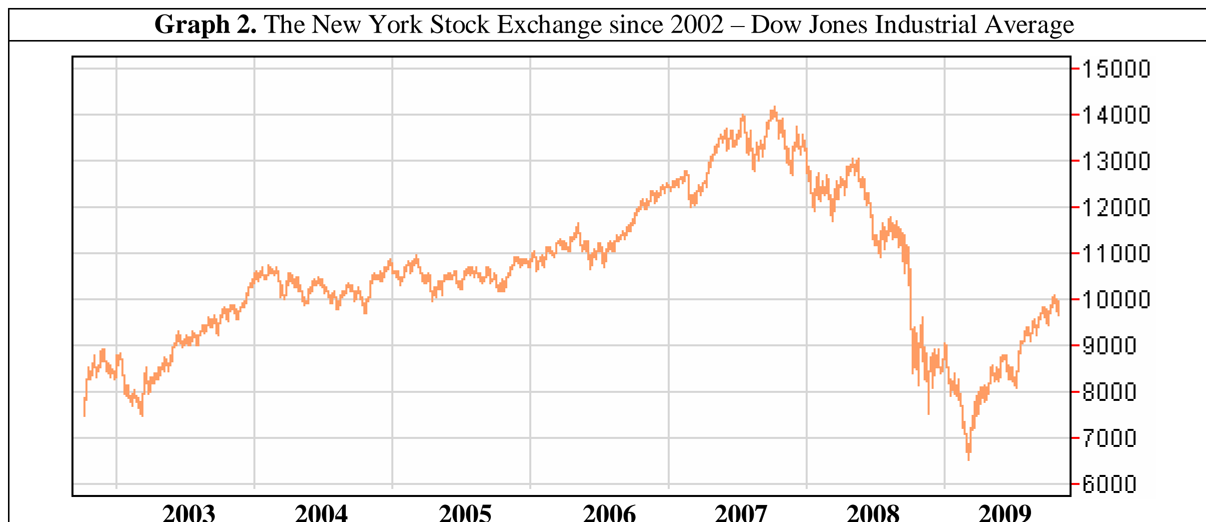


In the same 17-month period, since its peak in late-2007, the Dow Jones Industrials actually declined somewhat more (Graph 2), losing 54% of its value, but has also, in comparison, fared much better since: it now stands "only" around 30% below its all-time peak and 50% above its 2009 trough. It is extremely unlikely, therefore, that the index will decline to anywhere near the 2,000-mark, which would be the equivalent level of 1932.

In much the same way, at least 2,500 banks (accounts vary) failed in the United States alone during the Great Depression; granted that many of these were much smaller than today's conglomerates, and none were anywhere near the relative size of, for example, Bear Stearns, Lehman Brothers et alia. Equally, as bank concentration has continued since the 1980s, there are "only" just over 7,000 US commercial banks and 9,500 savings and credit institutions – in France, these total just on 800. However, since September 2007, only 142 US banks and 36 credit unions have failed;[18] this number excludes the likes of Bear Stearns which, by being bought by other institutions, have not officially failed.

18 Of which, 25 and 15 respectively in 2008, and, to date, 115 and 19 respectively in 2009.

Graph 2. The New York Stock Exchange since 2002 – Dow Jones Industrial Average



Prices, output and unemployment. As described earlier, prices fell and unemployment rose in both depressions, while GDP went in divergent directions. Initially, the measures taken recently in the United States and in Europe may well lead to short-term deflation, but there are also indications that, in the mid-term, the situation will reverse and relatively strong price rises will result. Indeed, there is a much greater concern within the minds of central bankers of the effects of deflation than its counterpart, since the downward spiral is so much harder to contain. In fact, but almost entirely due to the return of oil prices' pre-summer 2008 peak (the classical basis effect), US inflation turned negative in March 2009 (year-on-year). There are, however, indications that this negative trend has reversed and that inflation may well return to zero by the end of the year. Largely unchallenged, however, is the forecast of a worldwide decline in output this year, the first such since reliable data have been collected. Here too, however, recent forecasts are more optimistic than only six months previous.

Rising unemployment, however, remains a serious risk, but this too should be put in perspective. At the height of the Great Depression, almost 13 million Americans were out of work, equivalent to just under a quarter of the working population. As of September 2009, just over 15 million are unemployed, but this "only" constitutes around 10% of the working population.[19] This said, the increase in the number of unemployed over the past two years of just under 8 million is, naturally, worrying.[20]

Nevertheless, the situation of the non-working population in 1929 was very different to that of today. The only major industrial country to pay unemployment benefit was the United Kingdom: started in 1911, there were already 2 million recipients by 1921, consisting largely of those who sustained injuries during World War I. In America, the state of Wisconsin started a scheme in 1932, but it was not until 1935 that the Social Security Act effectively forced all states to provide benefit. Even then, most women and blacks were excluded as were many job categories, for example the farming industry. Consequently, only around 50% of the working population were eligible to claim benefit. In addition, 50% of the senior citizens were estimated to live in poverty, with little hope of state aid. It was left to private benefactors to provide some solace, a tradition which remains valid in the United States today; incidentally, social benefits are still not a contractual right there, and can be withdrawn at any time.

It is hardly surprising, therefore, that the discontent and resulting social unrest during these previous crises were both substantial and violent. With, in addition, farmers going out of business – their declining income could not cover their outstanding debt payments – food became scarce and the means to buy it scarcer. Food kitchens were set up throughout the country, large numbers of the population moved to the cities in desperation and were forced to live in squalor, and there was serious rioting and looting. In several countries, the army was called in to contain the rioting; there were deaths. In comparison, for most of us, a similar situation is largely as equally inconceivable as is a financial meltdown, but, that notwithstanding, people have taken to the streets in protest in several countries. The anger was – for good reason – initially directed towards the banking industry, but, as the crisis deepens, at least in Europe, not only may the mood become more ugly, but also the reasons for discontent will change. There remains the danger that today's politicians will be unable to quell this anger.

Money. Unlike in the 1920s, where, according to Friedman and Schwartz, the Federal Reserve was at least partly to blame for its inactivity, this criticism cannot be levied against today's guardians, or against other European governments

19 A quarter out of work would, today, imply over 38 million unemployed!

20 The number of employed has declined less, since 600,000 jobs have been created during this time span.

and central banks. The US Administration has already made available two very large bailout packages, and has indicated that a third may be necessary and that it would also be forthcoming. Although welcome, these packages will need, at some time in the future, to be paid for. As the US Administration does not apparently intend to significantly reduce its total war effort, but at the same time has pledged to increase social benefits (for example, nationwide medical coverage), it will have to either resort to printing money, to borrow money or to raise taxes – or all three. In December 2008, the strongest increase in M1 ever was recorded – 31% at an annual rate over the previous six months; however, it has grown by only 4% since (to September 2009).

Table 3 summarises these indicators for the three periods under review.

Table 3. US cycles compared

	Measure	Long Depression	Great Depression	Present (since September 2007)
Equities	Peak to trough	n.a.	–85%	–54%
Financial inst.	Total failings	ca. 100	2,500–5,000	178
Inflation	Average	–3.0% p.a.	–6.7% p.a.	1.9% p.a.
Unemployment	Peak rate	14%	24.9%	9.8%
GDP per capita	Average growth	+2.0% p.a.	–8.1% p.a.	–1.5% p.a.
Money supply	Average growth	+2.6% p.a.	–7.0% p.a.	+6.5% p.a. (M2)

Equally – or perhaps more – worrying is the rise in US credit market debt: this now (2nd quarter 2009) totals $52.8 thousand billion, equivalent to 348% of nominal GDP! As can be seen from Table 4, the largest increase is in that incurred by the Federal government and there is little indication that this will substantially lessen in the short term. Incidentally, the table does not include the US government's pledge to support the obligations of Freddie Mac and Fannie Mae, which total just over $5,000 billion: this obligation is seen to be tantamount to nationalisation of the companies, so that ultimately the taxpayer will bear the risk of any default.

Table 4. US debt

Held by:	End-2007 (in $ bn)	End-2008 (in $ bn)	Percentage change
Households	13,765	13,821	+0.4
Non-financial businesses	10,594	11,096	+4.7
Financial sectors	16,177	17,217	+6.4
State & local government	2,192	2,240	+2.2
Federal government	5,122	6,362	+24.2
Total[1]	**49,866**	**52,593**	**+5.5**
[1] Differences are debt to the rest of the world (ROW).			

Thus the US government is printing money and increasing its debt in more or less equal degree: it may thereby hope to avoid raising taxes, but what it will find difficult to avoid is inflation. Given that one of the major lessons of the Great Depression is the danger of deflation, it may well be that the authorities hope that both trends will "cancel out".

The substantial increase in both money and credit is one major dissimilarity with previous crises. Another, and equally disquieting, one is the level of household debt, especially when measured against households' net worth. Net worth – i.e. the total of all tangible and intangible assets net of all outstanding debt – has, in nominal terms, with the exception of 2001 and 2002,[21] climbed constantly in the United States since World War II. Naturally, some of this increase can be explained by inflation: nonetheless, prices increased between 1950 and 2007 by 770%, whereas net worth increased by 5,200% in the same period!

However, in 2008, US net worth declined by a staggering 17.9%, from around $63 trillion (1 trillion equals 1,000 billion) to under $52 trillion, wiping out the gains over the previous three years. Almost a quarter of the loss can be attributed to the fall in real estate prices, and twice that in equities and mutual funds.

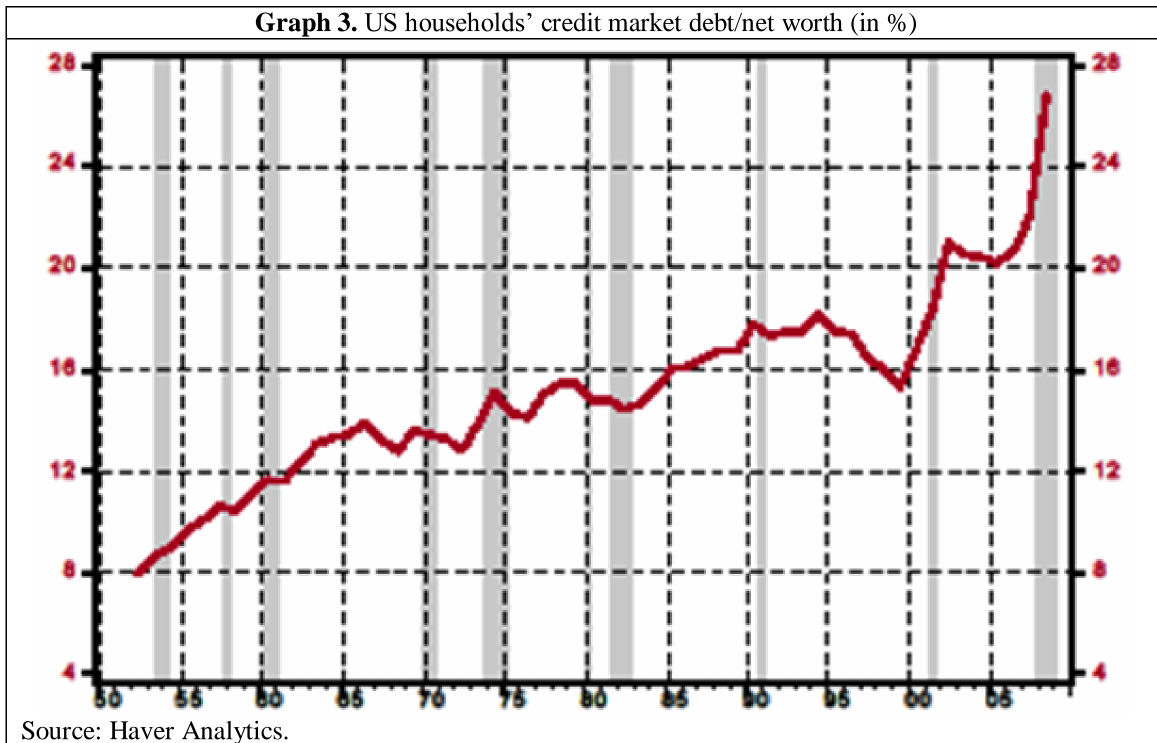
Consequently, although debt remained fairly constant, and indeed the growth rate is at a post-war low, the debt to net worth ratio has climbed to around 27% (Graph 3). The economic situation of households is hardly likely to improve in 2009 and may indeed worsen.

At debt ratio levels of around one third, real estate repossessions would become commonplace, all the more so should inflation require money to be tightened and mortgage rates to rise. As far as

21 At the time this was seen to be a possibly disconcerting downward trend.

households' unearned income is concerned, increasing interest rates will bring only a little comfort, since their saving ratio, although it has risen recently in recent quarters from its nigh-on zero rate of the past decade, remains in low single digits.

Graph 3. US households' credit market debt/net worth (in %)



Source: Haver Analytics.

As mentioned earlier, Irving Fisher (1933) cited a chain of nine events during the Great Depression. They were:

1. debt liquidation and distress selling;
2. contraction of the money supply as bank loans are paid off;
3. a fall in the level of asset prices;
4. a still greater fall in the net worth of businesses, precipitating bankruptcies;
5. a fall in profits;
6. a reduction in output, in trade and in employment;
7. pessimism and loss of confidence;
8. hoarding of money; and
9. a fall in nominal interest rates and a rise in deflation-adjusted interest rates.

Of these, with the exception of the money-related events (2 and 8 above), most have been or are being experienced during the present crisis. Also – and hopefully an unlikely scenario – deflation will need not only to arrive but also persist in order to counteract the rapid fall in nominal interest rates to their present historical lows.

Consequently, are we then not likely to find ourselves in a similar situation as in the early 1930s? There are some arguments which speak against such an argument: for one, there is greater communication and concerted coherent action amongst central bankers, international institutions and even politicians. Extreme political ideologies of the 1930s have largely disappeared in the western world. Finally, abject poverty, caused largely by the absence of a social safety net, is no longer the threat that it was.

However, there are new threats which must be faced: consumer spending in many parts of the world must decline – or at least slow in growth – as markets become saturated and as population growths slow. Pension schemes, which have become another safety net on which many of us rely, are in serious financial trouble: in many cases, the coverage ratio has dropped below either mandatory or prudent levels. The age pyramid is turning into a cylinder and is trending to narrow further at the base: senior citizens live longer, but are more care-intensive and therefore, in pure economic terms, more costly. At the same time, the ratio of the working population to dependent population is falling quickly, with calculable risks.

None of these problems – with perhaps the exception of those recently faced by pension schemes – are a direct result of the present crisis, but they will play an exacerbating role. As these problems must anyway be faced sooner or later, it can only be hoped that they will not have a direct bearing on short-term developments.

Conclusion

The paper is entitled, "Crises and (the absence of) ethics" and there has been little mention of the latter. In theory, they have not been too far away: recall that Roosevelt cited them, as did Fisher and, recently, Barack Obama. The "Jean Duponts" of this world are rightly indignant at the immoral attitudes of senior bank staff and their defence of a salary structure that rewards the greedy. However, we should also be honest with ourselves. Greed is, and will remain, one of the seven deadly sins, and most of us are guilty of it at some time in our lives. Madoff, as perhaps the most prominent example, sold products that banks were only too happy to embrace, and their customers were equally happy to let them manage affairs so long as the returns kept coming in.

The Germans and Americans, to name the two most voluble opponents of tax havens and tax evasion, were quite happy to let sleeping dogs lie until they felt that political profit could be made. After all, the OECD's report (and the recommendations therein), "Harmful Tax Competition: An Emerging Global Issue", was already approved by the OECD Council on 9 April 1998! As a result, there was, apparently, first a black list, then a grey one and, since 2 April 2009, countries have moved from one to another and then been removed altogether. A simple glance at the list of investments possible today,[22] some of which seem little better than placing a bet in a casino, illustrates the risks many of us are still prepared to take if, as is the case with high volatilities and leverages, the potential gains are sufficiently tempting. Of course, we don't expect to lose!

In especially the Anglo-Saxon economies, banks and building societies not only offered – and continue to offer! – to provide mortgages of up to 90% of the property value, they also, as this asset class continued to appreciate strongly, made further mortgages available which many promptly took at favourable rates and then spent on consumer goods. This had already been the case in the late 1990s, but memories, when tempted, are short! Interest payments in the United Kingdom are correspondingly high – when compared against disposable income – but, to date, mortgage rates remain low. Should inflation return in the near to mid-term, and, with it, higher interest rates, economic disaster and home repossession for many is bound to become a reality.

The signs have always been there for those willing to see: the reader is referred to any of the BIS Annual Report's Conclusions written over the past decade, where the warning finger of the then Economic Adviser, William White, was raised on much of that covered in this paper.

22 For example, the Union Bank of Switzerland (UBS) offers 82 different products for 6 asset classes.

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