BOWLING GREEN DAILY NEWS

‘End of Alchemy’ focuses on economic crisis

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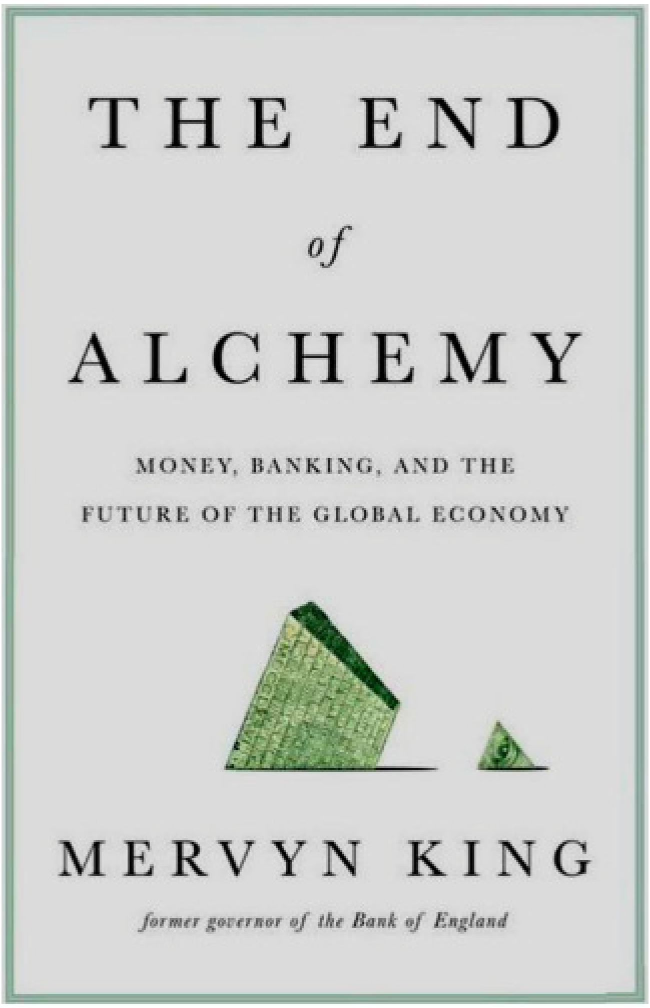
“The End of Alchemy: Money, Banking and the Future of the Global Economy” by Mervyn King. New York: W.W. Norton & Co., 2016, 448 pages, $28.95.



“It was the best of times, it was the worst of times, it was the age of wisdom, it was the age of foolishness, it was the epoch of disbelief, it was the epoch of incredulity...”

Only a few pages into “The End of Alchemy: Money, Banking and the Future of the Global Economy,” it becomes abundantly clear why Mervyn King chose this particular Dickens quote to begin his foray into the conflagration of events that led to the greatest economic downturn since the Great Depression. In many respects, the sentiment perfectly captures the decisions, circumstances and reactions fueling the perfect storm that came crashing down around us in 2008. A synthesis of history, sociology, psychology, economics and politics, King has written a primer that should be required reading for anyone who is involved in financial transactions – especially those involving other peoples’ resources.

“The End of Alchemy” is extensively researched, with 26 pages of source notes and a 22-page bibliography at the conclusion of the introduction and nine chapters comprising the main text. Although the prose can be rather dense in some places, overall the narrative is accessible to anyone with a rudimentary understanding of basic economics and the motivation needed to reflect on the ideas and concepts King articulates in meticulous detail. It also helps if you have at least a passing knowledge of the complicated context that forms the architecture upon which much of his thesis rests.

At the heart of King’s treatise are three fundamental shifts in policy that seemed to yield exceptionally-desirable results for about three decades – before inherent systemic flaws precipitated one of the most profoundly-devastating economic disasters since the 1930s. The first shift occurred when most of the developed countries gave their central banks previously-unprecedented latitude to set financial policies in a worldwide attempt to thwart a more-or-less global inflation rate that seemed to be spiraling out of control. The second shift involved multinational agreements between the industrialized nations to standardize monetary exchange rates and therefore expedite the movement of capital across international borders. This strategy culminated in the creation of the European Union and reinforcement of the U.S. dollar as the world reserve currency.

The third and perhaps most questionable shift, at least when viewed in retrospect, was the wave of deregulation freeing up financial institutions to offer new and increasingly complex investment products and services in the late 1990s and early 2000s. The basic premise behind this fundamental policy change was fairly straightforward – or so it seemed to those responsible for developing, advocating for, and ultimately passing the legislation that made this final alteration (or nail in the coffin, depending on your perspective) a reality. The plan was to minimize overall risk by spreading it across a diverse range of investments. But risk is still risk, regardless of how it is parsed, compartmentalized or diluted within a diverse range of financial products that became incrementally more convoluted as the creativity of a relatively few innovators with somewhat dubious motives was allowed to go virtually unchallenged.

"Risk, luck, fate, uncertainty, probability theory – we all have names for the game of chance," King explains in "Radical Uncertainty: The Purpose of Financial Markets," the fourth chapter and one I found particularly instructive. "Most decisions in life involve risk. Sometimes we embrace it, as when we enjoy a bet on the Grand National or the Super Bowl, and sometimes we avoid it, as when we insure our houses against fire. The playing of the hand we are dealt can be a pleasure in a game of bridge and a burden in life. We accept that Lady Luck has her part to play in our personal lives. But we cling to the 'illusion of certainty' in monetary matters."

Of course, many purported insulators against risk often reveal their true efficacy (or lack thereof) given sufficient time and trial by fire. As King astutely observes in regard to the precursors to the Great Recession, the problem was that built-in vulnerabilities in the system on a more macro scale were not immediately evident except to a relatively few economists who were looking in the right place and using the appropriate metrics. But their voices were consistently drowned out by the unbridled enthusiasm of those who saw no end to the extraordinary growth the global markets seemed to be exhibiting as a direct result of the three shifts previously described. Lurking just beneath the surface, however, were hidden dangers related to mounting risk precipitated, in large measure, by emerging and deepening inequalities between national economies the global banking system was, and is, increasingly unable to support. All of this, by the way, was driven by a seductive illusion of invulnerability, strength and even expansion many in the financial community were working hard to sustain.

King is currently the Alan Greenspan Professor of Economics at New York University. He is also a professor at the London School of Economics. He served as the governor of the Bank of England from 2003 to 2013. Educated at King's College, Saint John's College and Harvard, his resume includes teaching appointments at the University of Birmingham, Harvard and MIT (where he once shared an office with Ben Bernanke, future chairman of the U.S. Federal Reserve Bank). In 2015, he was listed as the 11th most influential person in the world in economics and banking by Financial Centres International.

What I have presented here is only a superficial interpretation of the many arguments King puts forth in this intriguing must-read for anyone seriously interested in getting to the heart of what caused the economic crisis from which we are still recovering. From the disappearance of manufacturing jobs to the runaway cost of college tuition, the repercussions of the Great Recession continue to resonate through our society, affecting us individually and collectively. King hopes we will learn from the lessons of the last few decades so we can avoid making the same mistakes again. He is probably more optimistic than I am; I recommend this one highly.

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