Greed and the Crisis

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Ahneella on paskainen loppu.

The greedy end up in shit. (Finnish proverb)

The question I propose to explore tonight is whether the current economic crisis is also a moral crisis – that is, whether moral failure, in particular greed, is in part responsible for the economic situation. My initial thought, believe it or not, was to answer in the negative. But the more I read about how we ended up in the current situation, the more plausible it became that in a morally better world, some of the crucial choices would simply have been made differently. The final straw, however, was a discussion with a dearly beloved relative of mine – through marriage, I must say – who teaches accounting at a business school. She insisted that there is nothing wrong with CEOs of banks – solvent, bailed out, or failed – seeking and being paid as large bonuses as they can get, and exploiting every loophole in the law to avoid paying tax on them. Indeed, she said, that's what she was advising her students to do. That's how the market works. Now, this relative is not a bad person, nor in any way stupid. Indeed, she has done many morally admirable things that I wouldn't have done. But her advice, no doubt given by nearly everyone teaching the people in charge of our money, is a counsel of greed. Acting in accordance with such ideas has played a large, perhaps decisive role in getting us in the trouble we find ourselves in.

To make the case that a moral crisis is a causal factor in the economic crisis, I'll begin by considering the difference between what I'll call healthy self-interest and greed or avarice. Defenders of greedy behaviour tend to run them together, as if it didn't matter how we pursue profit. I'll then talk about what the debt crisis is and how it came about, focusing mostly on the American case, but with some reference to Ireland as well. In a nutshell, new financial innovations made it possible to distribute the risk and reward of lending with interest far and wide, providing an incentive for reckless lending. When the housing bubble burst, it turned out that the risk had been multiplied as it spread through the financial system, with the result that relatively small losses at the beginning of the chain threatened to bring the whole edifice down. Institutional and individual greed played an important role in this – had various people and companies limited the pursuit of profit by the legitimate expectations and needs of others, at least much of the mess could have been avoided. We can say with confidence that had the ethos of greed been absent, the crisis would either not have taken place or would have been milder. In the final section, I'll make some suggestions about how we might get people to align their pursuit of self-interest with the common good.

1. Greed

Let me begin with a few words about greed. Greed, in philosophical terms, is a so-called *thick concept*, a concept that is at the same time descriptive and evaluative. If you say that someone is greedy, you convey to others that she is likely to pursue what she takes to be in her material self-interest. At the same time, you evaluate her negatively – you imply or implicate that her desire for wealth is *excessive*, that there's something to be said against such pursuit of self-interest, morally speaking. Let's say, to begin with, that someone is greedy if she aims to maximize her own profit without regard for what is due to others, or more broadly without regard for the needs of others.

I emphasize the evaluative aspect of the notion of greed, since it is vitally important to distinguish between pursuit of self-interest as such and pursuit of self-interest that disregards the legitimate claims or needs of others. A lot of the time the pursuit of self-interest is not only morally acceptable, but actually produces morally desirable outcomes, as Adam Smith and others argued.[1] Self-interest guides people to use their abilities in ways that others are willing to pay the most for, and thus, ideally, in ways that maximally benefit others, assuming that what people are willing to pay for is what benefits them. Everybody wins when those good at baking bread bake bread, and those good at maths develop smartphones, all out of self-interest.

But there is a big difference between such mutually beneficial individual pursuit of wealth and greed. This can be the case even if pursuit of self-interest harms the interests of some others. Suppose a good baker expands her business due to popularity, with the result that a less good baker goes under. Must the good baker be greedy – couldn't she limit her production and share the market? Well, she could, but the losing baker has no moral claim to stay in business, if customers prefer and freely choose another, and hence no claim on the good baker to stop expanding, if she likes to. Such competition benefits customers, who get better product cheaper (making standard background assumptions). So there's no reason to think that someone who pursues her self-interest effectively in fair competition is greedy. That's the truth in free market ideology.

It is evident that if we interpret charitably people who say that greed is good, they are in fact talking about this sort of pursuit of self-interest, but doing so in a misleading way that elides the distinction between healthy and excessive selfishness. Conflating the two is a

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[1] This is not to say that Smith thought greed is good. For his way of making the distinction between greed and prudence, see Wight 2005.

favourite rhetorical trick of market fundamentalists. For example, couple of months ago Greg Smith, the former head of Goldman Sachs' equity derivatives business in Europe, resigned from his job and wrote an editorial for the *New York Times*, decrying the changes in the company's corporate culture that meant the clients' interests didn't figure in the way Goldman did business any more. As he put it, "It's purely about how we can make the most possible money off of them."[2] What Smith was saying in the piece was essentially that the clients of an investment bank have a legitimate expectation that the bank will do its best to serve their goals, not try to bamboozle them if they can, as Goldman had evidently been doing. (I'll return to this soon.) The right-wing response was not long forthcoming. In the *Washington Post*, Jennifer Rubin ridiculed Smith:

> Next thing you know car dealers will be trying to sell you cars others don't want, realtors will be pushing you to buy a more expensive home … No one in the interview seems to have asked [Smith] if he had objections to trying to maximize profit legally.[3]

In the same spirit, when the influential Chicago school economist Milton Friedman was asked at a TV interview whether he thought greed was a problem when millions live in poverty, he responded:

> Is there some society you know that doesn't run on greed? You think Russia doesn't run on greed? You think China doesn't run on greed? What is greed? Of course, none of us are greedy, it's only the other fellow who's greedy. The world runs on individuals pursuing their separate interests. The great achievements of civilization have not come from government bureaus. … [T]he record of history is absolutely crystal clear, that there is no alternative way so far discovered of improving the lot of the ordinary people that can hold a candle to the productive activities that are unleashed by the free-enterprise system.[4]

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[2] 'Why I Am Leaving Goldman Sachs', *New York Times*, March 14, 2012, A27.

[3] http://www.washingtonpost.com/blogs/right-turn/post/breaking-up-with-goldman-sachs/2012/03/14/gIQAJJSOCS_blog.html?tid=pm_opinions_pop.

[4] The interview can be found on YouTube: http://www.youtube.com/watch?v=RWsx1X8PV_A.

For Rubin and Friedman, it seems, anything that is not prohibited by law is morally equivalent. Self-interest equals greed equals private enterprise. If fleecing customers the best you can by exploiting information asymmetries and developing a better product than the competition are morally on a par, either neither is bad or both are. If you reject unrestricted pursuit of self-interest, on this picture, you reject market economy altogether, since without competition and self-interest there is no market economy. Since market economy is good, what we would ordinarily describe as greed is good, at least as long as no laws are broken.

I believe we should not be making excuses for greed. There are significant moral distinctions to be made within legally permitted behaviours. There are many ways to go about maximizing profit, and only some of them are compatible with personal or professional integrity and honouring the claims others have on us. If we're willing to use those that are not, we are indeed greedy and morally criticisable. I don't mean, of course, that it's always easy to say when the pursuit of self-interest crosses the line, since it's not always easy to say what integrity demands or what claims others have on us. For a simple beginning, we might use a version of the Golden Rule as a rule of thumb: if you would yourself resent someone else maximizing their profit in the way you're tempted to do, were the roles reversed, it would probably be greedy to yield to the temptation. Note that what you'd resent is different from what you'd want – you might not want to be beaten in a fair competition, but you wouldn't resent the winner, if you're at all reasonable.

I want to emphasize that avoiding greed goes beyond respecting people's rights. If you're hiking with some friends and happen to be the first to come upon some wild strawberries, you have a moral right to take them all for yourself, but it would still be greedy for you to do so. The sense in which others have a claim to limit our pursuit of material self-interest is thus broad, and its strength varies with the kind of relationship we have with each other. It also varies with how acute our own need and the need of others is. If your family is

starving, it is not greedy to push very hard to get what you need, perhaps even if you have to break the law. If others are starving and you're not, keeping what would otherwise be a normal level of resources for yourself may be excessive.

These sources of variation hint at a deeper account of what makes some desires for wealth inordinate. Aquinas says that the greedy or covetous desire temporal, corruptible things at the expense of the eternal things. In secular terms, we might say that desire for material things is inordinate when it is incompatible with the ethically significant relationships we have with other people, whether it is as friends, participants in a fair competition, or citizens. The greedy substitute material wealth for the very sort of thing it is supposed to serve as a means to, performing our various social roles well, discharging our responsibilities to others (and ourselves) – being a good friend, father, manager, professor, or citizen.

Greed does not come alone. Aquinas cites St Gregory, who wrote about "the seven daughters of avarice": treachery, fraud, deceit, perjury, restlessness, violence, obduracy in regard to mercy. Aquinas explains that the greedy, in order to make their gains, must harden their heart to the needs of others; they can't rest, since the always want more; they can't be trusted, since they are willing to deceive to get what they want. All this is true, but I believe the greed has other daughters as well having to do with how we process information. It can lead to wilful ignorance and lack of curiosity: we don't want to hear that the party is going to be over, and shut our minds to uncomfortable information. A related form of self-deception is wishful thinking. We like to think that we will get what we want, and nobody will be hurt.

So my question today is: is the vice of greed, thus understood, a cause of the debt crisis, or the 'Great Recession', as some are calling it? To answer that question, we need to understand in some detail what the crisis is and how it came about.

2. The crisis

I am not an economist. Nor can I speak from personal experience of debt – I happen to have none, since I don't own a house, and I drive an old Golf. But I've been following the news like everyone else, and have been doing a little reading up for this talk. So this is going to be at best an interested amateur's take on the situation. I'll talk a bit about both what happened in the US and here in Ireland.[5]

What is the crisis? It's not that individuals, companies, and states are in debt. Most of them always are. It's that the level of debt is so excessive that it prevents them from normal functioning. One result of this is that instead of improving their situation, many are digging an ever deeper hole for themselves, without making a dent on the principal. At the same time, because debts aren't being paid back, lending institutions are in trouble, with the result that new credit isn't available or is expensive even for those who are not deep in debt, which makes it harder for business to grow or families to make major purchases. Hence, demand is low, business bad, and tax intake down, forcing states to cut spending even if they're not in trouble with sovereign debt.

How did we get to this? Well, obviously part of the story is that the individuals, companies, and states borrowed money. You don't get into debt otherwise. But again, having debt isn't a problem or a crisis. It often makes sense to borrow now, invest it into something that makes you richer, such as new equipment or an asset that goes up in value, and pay back later – you'll make an overall profit. And if you don't make a financial profit, you gain in non-monetary terms, for example by enjoying the possession of a house whose mortgage you pay off little by little. Nor is it a problem if others owe money to you, especially if you're an

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[5] The following narrative draws liberally on Barnett-Hart 2009, European Commission 2010, Ferguson 2010, Lanchester 2010, Lewis 2010, Lewis 2011, Smith 2010, Stiglitz 2010, Whelan 2011, and numerous newspaper and online sources.

institution like a bank that charges an interest on the debt. That way you'll get a share of the gains the borrower makes with your money in compensation for it being tied up and the risk of not being paid back. Thus debt can be good for everyone, and there need be nothing either prudentially or morally problematic with it.

So the real question is: how debt become a problem? The short answer is that many people made bad investments with borrowed money. As a result, they found themselves in a position in which they were unable to pay back what they had borrowed. The lenders, in consequence, were in trouble, too. Somewhat ironically, the worst off were the very institutions that specialize in lending money: banks, using the term broadly for financial intermediaries. Part of the problem was that they were highly leveraged, meaning that their assets – in the bank's case, loans to others – exceeded their liabilities – deposits and bonds sold to investors – by a very small margin. If liabilities exceed assets, a company becomes insolvent, and can't go on doing business. For a highly leveraged company, the safety margin is thus very low. A company whose assets are loans to others is particularly vulnerable: if only a small fraction of the loans are not paid back, it goes under. And that's what happened to trigger the current crisis: enough people defaulted, or fell behind, on their loans, in particular loans that were or derived from mortgages sold to poor people (even though they only constituted 3% of mortgages in the US), that a number of banks became insolvent or near enough so.

But why did so many people default on their mortgages, and how could that affect so many financial institutions, such as investment banks and pension funds, that had no dealings with people buying a house? This is where the plot thickens. It's not that there first was an economic crisis, which caused people to lose jobs so that they couldn't keep up with their loans. That happened later. The people whose default triggered the crisis in the US were people who were poor to begin with. In the early 2000s, it was nevertheless shockingly easy

for them to get a loan (as it was in Ireland). This pushed up house prices, which encouraged construction of new houses. But why did the banks lend to people with poor credit history or income, sometimes on quite generous terms, when it meant taking on a high risk of default on these so-called subprime mortgages, were the house prices to stop rising (as they would have to, since neither the number of buyers nor people's incomes were rising to keep pace) or were there to be an independent downturn? The answer is that they believed it wasn't risky after all, because they could sell the risk on to others, thanks to new financial innovations.

In traditional banking, a local bank would hold the mortgage it had given to a homeowner, which gave it an incentive to be very careful to lend. But starting in the 80s, investment banks would buy bundles of mortgages from the originating banks, securitize them, and sell them on to institutional investors as mortgage bonds. These bundles contained more and less risky loans in different 'tranches', the more risky bottom tranches paying a higher interest rate to compensate for the risk.[6] To create what is known as a collateralized debt obligation or CDO, investment banks take tranches off a number of different mortgage pools and put them together to create a new, supposedly less risky product. To see how this is meant to work, consider a simple example. Suppose you're buying ten eggs from a farmer you've never met. There's a chance that they've gone bad, though egg rating agencies tell you that the farmers around here are generally pretty reliable. If you have the chance to buy an egg each from ten different farmers, however, it's much less likely that they've *all* gone bad. Similarly, perhaps mortgage holders in Florida or California are at risk of defaulting, but, the reasoning goes, surely not mortgage holders *both* in Florida and California will, so a *diversified* pool of risky loans from both – a collateralized debt obligation – is less risky than

[6] The risks come in different varieties: credit risk of defaulting, prepayment risk of the borrower paying back the principal before maturity (thus paying less interest over the life of the loan), interest rate risk of an adverse change during the life of the loan, and so on.

the individual loans. Credit ratings agencies accepted this kind of reasoning, and thus gave CDOs made up of BBB-graded subprime mortgages an AAA-rating, meaning they considered it as safe an investment as US treasury bills.

So, clever securitization made risky mortgages a more attractive investment, increasing demand and thus producing an incentive for originating banks to hand out more risky loans. Another new instrument, the credit default swap or CDS, made giving and buying them even more attractive. Again, the basic idea is sensible. Say I lend a million euro for a year to a friend starting up a business at a 10% interest rate. I expect to make 100 000e profit, but of course I can't be quite sure that the business won't fail catastrophically – in the worst case, I stand to lose the million. But maybe you're more confident of my friend's business, and offer to take on the risk of default for a fee of 5%. That is, in the case of default, you'll pay me the million, but I have to pay you 50 000e, reducing my profit. But what the hell – I still make a profit, and I don't have to worry about default. In effect, I'm making a risk-free profit. (Unless, of course, you default as well, but let's not worry about that for now.) As long as I can find someone to sell me a CDS, I have every financial incentive to give out as many loans as possible – it's like printing money.

And why did people sell such insurance to banks? For one thing, new mathematical models were supposed to be able to put a price on these and other derivatives. For another, the underlying CDOs and other instruments were rated by supposedly impartial and reliable credit ratings agencies such as Standard and Poor's and Moody's. And finally, the traders themselves didn't take a personal risk – nor indeed the companies that were 'too big to fail'. Even if it all went wrong, somebody else would pick up the bill. (This is what is known as 'moral hazard'.) At first, all went well. In the early 2000s, insurance companies like AIG made hundreds of billions in premiums paid on credit default swaps. So attractive was the business that they began to sell so-called *naked* credit default swaps to buyers who didn't own

the assets in the first place. This is where we reach pure betting. Suppose Deutsche Bank owned a pool of subprime mortgages worth 10 million dollars. For a small premium, say 50 000 dollars, AIG would sell a CDS on that pool to a third party hedge fund, or in fact to a number of them. This is like selling a theft insurance on *my* car to, say, ten *other* people – if the car is stolen, the insurance company has to pay out to ten people instead of one. (The attraction is that as long as it isn't, ten people instead of one pay the premium.) Similarly, if the subprime mortgages went bad, AIG would have to pay millions to a lot of buyers, multiplying the cost of default.

And of course, the subprime mortgages did go bad. People with low incomes simply couldn't keep up with their payments, especially since many loans had low 'teaser-rates' that went up after a couple of years. The new financial innovations had spread the risk of default far and wide, so a chain reaction was triggered. House prices fell, leaving many homeowners in negative equity. Some originating banks had held on to the loans and were highly leveraged, with the result that they became insolvent. Investment banks like Lehman had held on to some mortgage-backed assets, and made significant losses or toppled over. Banks and funds all over the world that had bought the CDOs were in trouble. Institutions like AIG who had sold insurance on subprime assets founds themselves owing billions all of a sudden (especially to clever investors who had figured out the crash would come and bought naked CDSs on it with all they had). Given the esoteric and off-balance-sheet nature of many of the transactions based on the subprime mortgages, no one knew how exposed others were, so banks didn't want to lend to each other. Rating agencies looked like incompetent fools.

At this point, governments and central banks stepped in, holding wads of taxpayer money. They had ignored warnings of a housing bubble, and encouraged borrowing money by keeping interest rates low, helped by the inflow of Chinese money. In the US in particular, successive administrations had left monitoring derivatives transactions to the banks

themselves, deregulated investment banking, and refrained from exercising even the regulatory powers granted in existing laws, all in the belief that markets functioned best when left to themselves. Now governments panicked. In the US, the Bush administration rushed in to take over AIG, paying out the foolishly given insurances in full, so that gamblers like Goldman Sachs made tens of billions, and supplied cash to banks that had taken hits, taking a share in return.

Given the size of its economy and tax base, the US could absorb the cost of rescuing the big banks and insurance companies, even on terms disadvantageous to the taxpayer. In Ireland, the situation is different, as we know. As I understand it, the crisis here was simpler. As in the US, cheap credit drove up the price of houses, and banks were willing to lend to everyone, including property developers. Regulators looked the other way and politicians failed to invest the tax windfall productively. With cheap foreign labour, record numbers of houses were built on absurdly expensive land, though population and incomes unrelated to houses weren't growing much. Inevitably, the housing bubble burst, leaving recent house buyers in negative equity and property developers with ghost estates. The banks held worthless assets, and were themselves billions of euro deep in debt to German, British, and French bondholders, unable to borrow for day-to-day needs after the global crisis deepened following Lehman's collapse in September 2008.

As in the US, the government stepped in, or perhaps I should say stepped in it. As we know, on September 30, 2008, the Irish government, in particular Brian Lenihan, made what may be the worst single economic decision in the history of the world, guaranteeing €440bn worth of liabilities at Irish banks in order to boost confidence in them. As it turned out, they weren't worth any confidence. They weren't just illiquid (short of cash), but insolvent. They had to be nationalized and their books cleaned by setting up NAMA to buy billions of euro worth of bad loans. The senior bondholders who had bet that Irish property prices would keep

on rising were paid back fully by the state, as if the bet hadn't been lost at all. For pleasure of watching the failed confidence trick, the Irish taxpayer will pay, it seems, with years or decades of austerity. One trick did work: Lenihan magically converted a housing debt crisis into a sovereign debt crisis. (To be sure, there are people like Patrick Honohan and the Irish Times' Dan O'Brien who believe that the government would have had to bail out the bondholders with or without the guarantee. But this is just excuse-making. Certainly Angela Merkel could make stern noises, but without the bailout, Ireland would probably still have a relatively low budget deficit and the ability to borrow in the sovereign bond market.)

3. Moral causes

Suppose the account I've given of the nature and proximate causes of the crisis is along the right lines. Does greed enter into the picture, and if so, how and where? It is obvious that the parties to the transactions were motivated by self-interest, but as we've seen, there's a big difference between that and greed. What I'm going to do is look at all the links in the chain reaction and ask whether and to what extent their behaviour is attributable to greed. So I'll examine borrowers, mortgage lenders, investment banks, ratings agencies, investors, and finally governments from this perspective. I believe we can meaningfully attribute qualities like greed to institutions and collectives as well as individuals – institutions can behave greedily even if none of the individuals who make it up does. So I'll switch freely from one to another as the discussion requires.

Let's start at the beginning, namely the borrower. In the US, the crucial case was someone with a low or uncertain income who takes out a large loan to buy a house. In the boom years, such a person is inundated with offers to borrow cheaply, or at least apparently cheaply, and sees the value of other people's houses go up at a fast pace. The odds are that she is poorly educated, or at least lacks a solid understanding of modern finance – after all,

who doesn't? Some right-wing commentators place the blame for the crisis on such people living beyond their means, no doubt in part because in the US the holders of subprime mortgages are disproportionately non-white. It is of course true that a lot of people bit off more than they could chew, but let's think a bit further. Why does the US or Ireland have a lot of poor, uneducated people who must take a loan that is huge relative to their income in order to buy a house of their own? Because of historical injustice – in the US slavery and discrimination, in Ireland the class system – and the absence of fair equality of opportunity. In a more just society, there wouldn't be many people needing subprime lending in the first place. Directly or indirectly, these people are victims of the greed of others, of the lack of political will to provide equally good chances to everyone regardless of their parents' wealth. Given that the weight we must give to the needs of others in order to avoid being greedy diminishes when our own situation worsens, I don't think there's much moral blame to be apportioned here. The situation may be different with middle-class people taking advantage of the higher value of their house to buy investment properties. They may have fallen for the charms of that ninth daughter of greed, wishful thinking that house prices can only go up.

Banks come in different varieties. In the US, the first stage were mortgage originators, the banks that gave the loans. Given that they had willing third-party buyers for the loans, as we've seen, they had the incentive to sell as many as possible, skimming off as high fees as possible. Here we find clear cases of greed – deceptive lending practices and absurdly risky loans. Banks came up with the so-called 'liar loans', mortgages that required no documentation of income. They gave out loans without even the name of the debtor or address of the residence, just a postal code! There was a product called "interest-only negative-amortizing adjustable-rate subprime mortgage" – a loan for the full value of the house for which you initially paid nothing, not even interest, which was simply added to the principal. Illegal immigrants picking strawberries bought houses for hundreds of thousands of

dollars, and Las Vegas strippers bought investment properties (Lewis 2009). Clearly, there was no thought given to what would happen to either the people who would inevitably default or the people who would invest in the mortgage-backed securities. A non-greedy mortgage originator, if there could be such a thing, would have considered what the social function of such banking is – providing an opportunity for people to enjoy their future earnings now and helping them manage the risk of a large investment – and pursued her self-interest in ways that would support rather than hinder that goal. Without the vice of greed on the part of mortgage originators, investment banks would have had no pig to put lipstick on.

In Ireland, the big money wasn't just in handing out mortgages but in loans to property developers, which at the peak constituted two thirds of all lending in Ireland (Gerlach 2011). The Anglo-Irish Bank notoriously pushed loans on a very skimpy basis. I've seen a documentary in which a former property developer says he got €220m for a Smithfield development after a couple of breakfasts at the Shelbourne. Now that developer is bankrupt, the development worth a fraction of its cost, and Anglo nationalized. To be sure, it's not so easy to say whether this is stupidity or greed; perhaps both reinforced each other.

Next up in the American food chain are investment banks like Goldman Sachs, securitizing and bundling mortgages and other loans and selling them to investors. Their employees and executives are the ones who benefited most from the bubble, and subsequently the bailout. So it is perhaps not surprising that it is here that we find the largest failures of professional integrity and all the daughters of avarice at work from dawn to dusk. To begin with, creating new derivatives and other instruments is not itself problematic. But the use to which they were put cannot be explained by healthy pursuit of self-interest. First, as Greg Smith admitted, the investment banks abused the trust they invited their clients to place in them by disguising the risk of the securities they were selling. Second, part of how this was done was systematic manipulation of the ratings agencies, who no more understood what was

in the CDOs than ordinary investors. This lead to underestimating risk, which in turn resulted in overpricing the assets. Goldman Sachs was like a used car dealer who knows the body is rusted through but covers it with new paint and manages to fool both the buyer and the NCT for long enough to collect the cash. (You might think that by this analogy, once caught the investment banks would have to pay back the money. That's not how it works. Under Obama, financial fraud prosecutions have fallen to a third.) Even when it doesn't violate the letter of the law, this kind of behaviour neglects legitimate claims of clients, who will have to place trust in investment banks working in their interest. As business ethics people like to say, professionals have a fiduciary duty towards those who depend on their advice. A non-greedy investment bank – or just a 'long-term greedy' one, as Goldman Sachs once advertised itself to be – would not deliberately hide risk. It would make less money in the short run, of course, but then it would not need to raid the taxpayer's purse either from time to time.

The third clear instance of greed in investment banking was and is regulatory interference. Investment banks lobbied hard to prevent regulation of derivatives, for example regulations requiring sellers of credit default swaps to hold capital reserves in case they have to pay out, as sellers of ordinary insurance must. In the US, they had allies in influential economists, such as the now thoroughly discredited Alan Greenspan and Larry Summers, who was bizarrely chosen by Obama as chief economic advisor in spite of evident and dangerous incompetence. In Ireland, too, the Anglo-Irish chairman Sean Fitzpatrick argued that regulation would "stifle business", slowing down the stellar growth. In hindsight, I think we'd all be happy if somebody had slowed Anglo down. A bank that doesn't intend to take advantage of information asymmetry and lack of competition has no need to object to regulation designed to prevent such activity.

The credit ratings agencies were not only fools, but to at least some extent complicit in the scam. Companies that were selling trust, portraying themselves as honest and careful,

turned a blind eye to manipulation, since they reaped good short-term rewards for doing so. When the Congress later held hearings on the crisis, their CEOs explained that they were simply offering constitutionally protected 'opinions' that nobody should really base their investment decisions on. (Never mind that many investors, such as pension funds, have rules permitting investment only into what the ratings agencies say is safe.) Such agencies, again, have a potentially useful function in the economic system, namely providing reliable and impartial information about the risks of investment. Were they not greedy but pursued profit in accordance with their function, they would not let themselves be swayed by the incentives provided by the investment banks.

By the time we get to investors, moral flaws are less obvious. Some institutions were, to be sure, taking excessive risks with other people's money. But often they were sold a cleverly disguised faulty product, certified by a supposedly independent agency as safe. In some cases, there was a kind of naïveté involved. For example, German banks threw the hard-earned money of depositors to anything that got a good rating from the agencies, trusting that they were playing by the rules. Michael Lewis relates how bewildered investment bankers laughed at the gullibility of 'Düsseldorf', who would buy anything they dreamed up. Should the investors have suspected that it was all too good to be true? That's no doubt true in some cases. I'm inclined to think that a non-greedy European bank would not have bought Anglo bonds, but rather exercised due diligence and looked at where the money was going.

I've talked a lot about institutional greed, but behind much of it was individual greed, fuelled by dubious inventions in remuneration. Many studies have called into question the effectiveness of paying management in stock options, which incentivises a quarterly focus on stock price rather than the long-term health of the company, not to mention the long-term health of the economy as a whole. Executives may have realized that the housing bubble would burst, but as long as it didn't, they earned handsome bonuses in millions or hundreds of

millions, bonuses they wouldn't have to pay back even if the company were to crash. And of course many seem to have convinced themselves that they actually deserve the 'compensation'. The moral obscenity of building ever bigger mansions with money wrangled out of people who have now lost their homes does not seem to register.

Finally, though governments and their members may not themselves have been greedy – Ireland may be a special case here, unfortunately – their choices often fostered the ethos of greed. In America, repeated tax cuts for the rich since Reagan provided an additional incentive to make more, more, more money. The political rhetoric of the right pretends that all the rich are 'innovators' and 'job creators', while the lack of access to health care or decent education forces the poor the fight for the crumbs fallen of the high table. The badly designed bailouts only increased moral hazard, risk-taking in the certainty that others would pick up the tab in the case of losing the bet.

In Ireland, we know the ethos of greed reached the highest offices in the land. From an outsider's perspective, the number of former Taoiseachs and ministers hauled in front of tribunals is comical. If the elected representatives of people use their position for personal enrichment at the expense of ordinary people, why would businessmen hold themselves to higher standards? As if personal example wasn't enough, Ireland as a country has pursued its self-interest at the expense of others with its now sacrosanct low corporate tax rate. Another daughter of greed motivated Fianna Fail governments to feed the flames of the housing boom with tax breaks to friendly developers. After the first incarnation of the Celtic Tiger had keeled over and exports dried up, housing became the main engine of credit-fueled growth and easy tax income. A less greedy government wouldn't have postponed hard choices to the future, which only made them so much harder.

I've said some harsh things about the Irish government, but the crisis has also been made worse by what we might call the greed of Frankfurt. We know that the ECB and the German government successfully threw the kitchen sink at the Irish to prevent any haircuts for speculators in the failed banks, because it would have threatened the stability of the euro and of course the balance sheets of European banks. The benefits, if any, went to the eurozone in general, and the cost to the Irish taxpayer. Recall those daughters of avarice, violence and obduracy with respect to mercy. I believe we see their hand in this show of force at the Irish expense. And still the Irish will never be able to pay it all back, especially with austerity strangling demand and murdering growth.

4. Capitalism Without Greed?

I've been making the case that greed has indeed been a contributing factor to the debt crisis. I'm not saying it's the only one – sheer stupidity and hubris also played a role, and perhaps long-term trends in capitalist economy, such as globalization, concentration of wealth and concentration of power in the hands of the wealthy. But in any case, private vice in this form does not lead to public benefits. So how do we temper it? In a related context, Philip Pettit (1997) distinguishes two ways of designing institutions so as to make them corruptibility-proof: screens and sanctions. Screening means ruling out options or agents, sanctioning changing the incentive structure at different institutional positions. If the world were divided into greedy and non-greedy individuals, we might theoretically reduce the odds of crisis by kicking out the greedy ones from financial institutions and politics. Alas, that is not how it works. As situationist social psychologists keep insisting, situational factors play a far more important role in determining our behaviour than we are willing to accept, except perhaps in our own case (see e.g. Doris 1998). You know how it works: if you keep a wallet you found on the ground, you're greedy, if I keep one and get caught, I only succumbed to temptation this one time. However, experimental evidence suggests that we're all likely to respond to

incentives in a similar fashion, though of course there are always a handful of saints and sinners who predictably respond in character. And how could we tell which individuals are the incurably greedy ones, except perhaps by their very desire to work in finance?

So we're better off screening out options and changing incentives on the assumption that pretty much anyone will fall for temptation if it's there. What we need to do is, in short, provide incentives to pursue self-interest consistent with the social function of the different institutions, and take at least the worst options off the table altogether. I can only make a few suggestions. Start with banking. The most obvious screen is separating retail banking from investment banking, looking after ordinary people's money from the gambling casino. The US did this after the Great Depression and gradually undid it in time to contribute to the Great Recession. Since it's been done before, it should be possible to do it again. As to incentives, one key problem in the crisis was that the sellers of loans, securities, and derivatives are able to hide information about their risks from the buyers, and had a financial incentive to do so. To remove this temptation, what is needed is more transparency, which requires efficient and efficiently enforced regulation. Such regulation is not a fetter on the market, but rather a condition of the market working as it should and prices reflecting genuine value of the assets. Risk-diminishing regulation is justified in any case by the negative externalities – costs on third parties – that the derivatives trade evidently has.

Next, option pay is an idea that works in theory (all right, given some false assumptions), but not in practice. I believe we've conclusively seen that it provides the wrong kind of incentive. Theoretically, the market should correct itself, and there are indeed a few instances now of stockholders rejecting this form of executive pay. But this will work much better if all the companies must play by the same rules. It is up to proper economists to work out the details of which kind of compensation scheme would redirect self-interest in the direction of mutual benefit, but clearly something of this sort needs to be done. Such reform

would reduce the profits made by bankers of all kinds, therefore reducing the incentive of the inherently greedy people to take up banking. Perhaps they would be content to play at a real casino instead, which would be good for us all.

The credit ratings agencies, for their part, allowed greed to blind them from the flaws of complex securities and derivatives, because they were in effect paid to certify them as safe. There's a surprisingly simple solution to this problem, a solution we've long been using when we buy cars or electronics. After all, magazines and websites that review and rate such goods perform the same function as the ratings agencies: they tell us which claims made by the seller are worth trusting and which not. But the difference is that they are paid for by the customers. You wouldn't buy an Audi on the basis of a review paid for by Audi, so why would you buy a bond on the basis of a rating paid for by the seller? If the buyers paid for the ratings, the agencies would have an incentive beyond maintaining their questionable reputation to ensure that they get it right, and would surely be more suspicious of what investment banks tell them. This is a straightforward case of redirecting pursuit of self-interest in a way that transforms it from greed to healthy selfishness.[7]

Finally, there is the role of governments in fostering the ethos of greed. Rhetoric is easy enough to change – indeed, Barack Obama and even Enda Kenny speak a different language than their predecessors – but the real message is sent by policies. As Joseph Stiglitz notes, "When we tax the returns of speculation at much lower rates than the income of those who work hard for an income, not only do we encourage more young people to go into speculation, but we say, in effect, that as a society we value speculation more highly" (Stiglitz 2010). Most egregiously, governments tolerate individuals and companies fraudulently operating from tax havens. Why? Nothing worth losing would be lost if Cayman Islands were

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[7] This suggestion was born out of a conversation with Vili Lähteenmäki.

bombed into oblivion and the cream of Monaco high society frogmarched into labour camps. In the same spirit, moral hazard would be reduced if executives of failed companies were politely but firmly invited to participate in any bailout with a large portion of their earnings – certainly expropriating the bonuses received while running the company into the ground would be required by the notion of personal responsibility.

I want to finish with a speculative note. There was one branch of the banking industry that did fairly well in the crisis, namely Islamic banking. Islam, as we know, is not a greed-friendly religion, and prohibits charging interest on loans. Nevertheless, bankers in Islamic countries have come up with alternative ways of making banking profitable – of course not nearly as profitable as Western banks, but still a solid and rapidly growing business. There is no room for exotic derivatives – you'd probably end up beheaded if you tried to sell the mezzanine tranche of a subprime CDO in Iran. Consequently, the risks and rewards are smaller and more transparent. Now here's my question: why is there no such thing as Catholic banking? After all, the Church is not such a friend of usury either. The Irish banks might try to be the pioneers in pursuing temporal goods in a way that doesn't reject eternal goods. In the long run, that might benefit even those of us who have no higher religion than humane justice.

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