John Kay, *Other People's Money: Masters of the Universe or Servants of the People?* Profile Books: London, 2015; 356 pp.: ISBN 1610396030; ISBN13 9781610396035, RRP AUD23.99.

Reviewed by: Jocelyn Pixley, *Macquarie University, Australia.*

John Kay is best known for pithy *Financial Times* columns. His book – *Other People's Money: Masters of the Universe or Servants of the People?* – captures the disquiet and disgust (if not disaffection) experienced ever since the Global Financial Crisis (GFC). Kay focuses on the purposes and multifarious activities of the financial sector and decries, early on, the fact that that only 3% of bank business is lending for the production of goods and services. For lay people and scribblers like me dismayed that banking is even less publicly responsible than before 2007, this insider's stern response offers a lot of answers and, among the welter of critical books, offers much to appreciate.

To knock the sector down to size, Kay dismisses its academic support industry via Larry Summers' term of 'ketchup economics' for 'finance theory and monetary economics' (p. 5). But so far from conceited professors having a 'causal' role in the GFC, Kay argues that finance is neither unique nor the *Masters*, as alleged (cf. p. 59; but see also pp. 64–66). To this end, he highlights banks' and investment banks' dubious business models: including mismanagement, conflicts of interest, diversification into areas about which senior managers knew zero and the demise of the partnership model.

Kay avoids catch-all terms like neoliberalism, making gestures to the pro-market ideology of Thatcher and Reagan. He prefers looking at the 'mechanisms' that produce so many financial crises (p. 43). This stress on actions and threats (not ideology alone) is important. Hence, for the past decades of calamities, he starts with the 1982 South American government defaults, pointing out that the Fed, the IMF and the US Treasury only bailed out the US banks from their carry trade in Mexico and elsewhere, foreshadowing a pattern. I'd note that this occurred only after Fed Chair Volcker raised the US interest rates ruinously. Kay rightly argues that 'risk' was mistreated as a 'commodity' (pp. 56–57) in the growing 'risk' markets. He makes similar criticisms to those of Alan Blinder (2013) against the tactics of Summers, Bob Rubin and Greenspan to silence Brooksley Born, a regulator wanting to retain and increase regulations on derivatives of derivatives. She lost. Alongside Bernanke's praise of commodified risk and his alleged Great Moderation, to Kay, Tim Geithner, then head of the NY Fed, Greenspan, Summers, Rubin and Don Kohn of the Fed's board were all wrong! Kay is not just irritated by 'errors', he emphasises that financialisation has also caused a great deal of social damage.

Derivative markets played a main role in the GFC. Add to that, the sector sought profits via dangerous leverage. Apart from some heroes, Kay dismisses the ideas that more 'clever' people and greater speed of information are beneficial overall (p. 111). He explains profits by factors like gaining 'the Edge' – from Madoff illegalities to knowing what other players are doing, citing Keynes' beauty contest analogy. Financial firms became oligopolistic owing to advantages of scale in market-making. To me, though, even if Warren Buffet is the 'sage' he sanctifies, he is successful only because his huge funds can also move markets. Another nice earner is in regulatory arbitrage: thus, credit default swaps started out this way by exploiting the differences between banks and insurance firms' rules

– questionably legal – and London was softer than Wall Street (pp. 121–124). The response was more rules but, as a whole, arbitrage is only another 'dispiriting waste'. Kay also fingers accounting and 'the Bezzle' that relies on years passing before the theft is uncovered, as was the case with Enron. Kay regrets originally supporting 'mark-to-market' accounting (pp. 128–132) and suggests that the dot-com bubble was a Ponzi/Madoff scheme, 'fuzzily' legal. He attacks the 'wilful blindness' to inconvenient questions, a 'casual lack of concern for the truth' in the conglomerates that rely on cross-subsidies from 'dull' retail banking to trading. Shareholders were victims in the global crises caused by senior staff (pp. 136–139). Governments, such as the UK, even claimed that their bailouts made 'small profits', whereas the Irish bailout was catastrophic; any future 'guarantee' (of the European Central Bank or the Bank of England) could also prove similarly disastrous.

In all, claims like Goldman Sachs & Co.'s to be 'doing God's work' in their alleged 'capital allocation' (pp. 160–161) amounted to only 10% revenues in the early 2010s, whereas the bulk of revenue is from secondary market trading. In any case, Kay shows that the largest US corporations self-finance and/or engage in finance engineering, and small and medium business funding also changed from banks to venture capital, until that became private equity. Kay singles out German-speaking regions in Europe as the 'stars of the *Mittelstand*', financed by parts of the banking system that were less touched by the GFC than Deutsche Bank and several *Landesbanks* (pp. 166–169). Kay gives much more useful detail.

Naturally, we can debate whether his answers are adequate. To be fair, Kay is speaking to a general public, yet even then the way he talks about 'liquidity' is somewhat odd. It's fine that Kay uses homely analogies to provide a sense of the mess he is describing, but this helps him maintain that finance is not 'special'. For example, supplies of milk (p. 88) are said to resemble the supplies of (bank or finance market) 'liquidity' – when there is not enough, there is a run on the bank (or the dairy). That is like a truism, but it avoids the differences between a product or service market and a money market. The *social structures* of these markets are quite different, as economist André Orléan (2014) shows, drawing on sociology. The dairy is a seller, and consumers of milk are buyers. Prices change in a glut or dearth although monied buyers usually remain. But in a *money market*, the alleged commodities (inherent promises of money, not really risk, 'packaged' into derivatives) are bought and sold by the exact same traders. More buyers than sellers push up the price (a bubble) but situations easily arise when they all become sellers and a run can ensue. That market stops altogether. The social structure of money markets suggests that buyers and sellers are able to keep the game going: Kay suggests a reduction, because there is 'an illusion' that supplies will continue, although, like milk, he argues that liquidity is good for 'society as a whole' (p. 95). He misses JM Keynes' equally homely analogy that shows the social structural *dangers* of liquidity. The farmer cannot sell the farm to trade 'liquid' assets for one week and return to farming the next week. Worse, particular liquid assets may no longer be saleable, whereas all consumers need food – so if, as Kay says, banking is not 'special', why is the mainstream notion of the 'real economy' so undermined in money market crashes?

A related problem is Kay's discussion of the 'functions' of finance. He states that an 'Investment Channel' is needed to 'channel the savings of individuals into fresh investment of businesses, home-owners and governments … or so it should be', but that former 'search and stewardship' is now diverted (pp. 141–144). 'Delusions of grandeur', as well as 'avarice', set in. In this discussion, much is repeated from earlier sections of the book. Banks are now sales shops engaging in abuses resulting from commissions, short-term horizons and conflicts of interest. Pension funds have outsourced to asset managers, with similar abuses and annual charges aiming to benefit 'senior management' (p. 209). With the 'Deposit Channel', Kay extolls the many benefits of technological change. Whereas Bitcoin (part 'visionary, part fraudulent' (p. 187)) only reproduces 'a commodity – currency – that has long existed', the 'deposit channel' will disappear in a few decades because its link to the payment system is disappearing.

To me, these tortured descriptions rely on the term 'intermediation' and channel metaphors. We can agree on abuses, the 'Jekyll and Hyde' character of financialisation (pp. 188–213) and Kay's dismissal of the idea that the US governments were solely 'responsible' for pushing home-ownership, since that was set well before the 1970s.

But what are the 'channels' of which he writes? Kay curiously avoids the way that loans create deposits. The 'payment system' in effect rests on money creation through the issuing of debts of banks, near banks and governments. On the one hand, money is used in exchange for goods (food!) and services, and no one can survive without money for exchange. On the other (a hand Kay sits on), money is debt with diverse contractual promises to pay in the future.[1] Governments commit to paying through tax collection if state money becomes inflationary, and banks do so through legal contracts that debts will be serviced. 'Near money' is created via roundabout ways in 'near' or shadow banking. The GFC was pre-eminently a run on the near 'money markets' – the defaults started there. These were the crazed derivatives of packaged derivatives of promises to pay or service loans.

To Kay, the 'savers' need ministering, but criticising derivatives does not lead us to savers. Instead, it takes us a long way back to property/house borrowers and fast forward to taxpayers. Both are debtors. People lost because banks can insist they be owed by all sectors – however foolish, pushy, even corrupt bank loans are. Banks and near banks make advances – that is, they create money (when asked) – by lending, whether with bank licences or in the shadow or near money networks using close substitutes. Banks claim to guarantee these advances, but that claim is hollow. Worse, the finance sector prefers governments to avoid any economic creation that relies on taxes to service state money, its debt issues. Indeed, governments must create unemployment to prevent wage inflation. Rising wages, banks relentlessly insist, are the main cause of inflation of the value of the debt owed to banks. Conveniently, their asset inflation is not mentioned. But a low-wage, heavily indebted population cannot service loans. No matter, government will pick up the bill, further abusing those low-waged taxpayers. The modest savers are stuck now, as Kay shows, mostly in voracious asset fund managers. He bemoans the resulting lack of economic activity but underplays how the stagnant economy of underemployed (over-taxed) workers suits employers and *rentiers* very nicely. The title *Other People's Money* is awkward (if catchy) and gives no answer as to why banking prefers low economic activity, without considering the interdependencies in money creation that sociologist Georg Simmel (1907[1990]) identified over a century ago: it is the community (taxpayers) that guarantees the 'deal' between creditors and debtors. This may be in the huge credit card industry, less formal 'near money' IOUs, surrogate moneys or very old 'bucket shops', or former hire purchase/credit instalments. Loans create deposits so that the saver has a very modest role; the loan brings in a stream of interest payments. All we can say is that money is a relationship, even if, as Kay argues, it is treated as 'someone's money'.

Who are these 'other people'? Kay misses the most 'divisive' class and state conflicts, unlike Dr H. C. Coombs, Governor of the RBA, who collected his essays on central banking also as *Other People's Money* (1971). In criticism of Keynes who had a far more social view (than Kay), Coombs argued *multiple forms* of inflation and deflation rested on class/money conflicts and state pork barrelling or war finance, always disruptive and likely to be insoluble even when tempered. Coombs stressed, unlike Kay (or others), where and how money is created or not.

With Kay's policy section (pp. 215–310) – we see the two-handed economist back in action, in recapping many of his earlier complaints of corruption. His three main points are as follows:

> **One]** Regulation is too extensive (not simple) and intrusive – yet regulators are captured by the finance industry. He bemoans what were personal ties. To Kay banks used to maintain mutual expectations (pp. 217–236) in either gentile or Jewish bank-owning families – they were 'collegial' or potentially self-regulating, yet even back then, insider dealing, and market manipulation were 'rife'.
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> **Two]** In the interactions between economic policy and finance – the latter became an instrument of policy and the consequences of extolling the finance sector as an economic policy vehicle are mostly malign. Both economic policy and financialisation are 'misconceived' and there is 'too much' sanctifying of banking's contribution as an arm of economic stimulus for beneficial outcomes like decent job-creation in new enterprises. 'Too little' use of financialisation as an instrument of policy is preferable, since as Kay well shows, banks have had deleterious not beneficial economic and social effects.
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> **Three]** Kay suggests government meddling should go only to 'productive intervention' into the structure and incentives of the line management in banking and all its other segments (such as credit-rating firms). The rest, he assumes, can be safely left to the 'market', although as I mentioned above, Kay did not distinguish between producer and money markets.

On securities, the New Deal set the framework – with attractions and flaws! Metaphors of playing field and 'mantras' of liquidity, price discovery and transparency were mostly about protection of the market, not the consumer. This is an excellent point, like Kay's attacks on the aim to promote 'confidence' in the industry. It also led to a huge (legal) compliance industry and relentless lobbying. He gives much detail on Basel, with little global cooperation against light touch rules, and defends a Hayekian critique of insufficient information at the centre.

On problems of economic policy, Kay devotes much space to Greenspan (linking him to Ayn Rand's 'cult', curiously not to Hayek's penchant for arbitrage) and to monetarism (pp. 240–241). According to Kay, quantitative easing was like 'pouring public money into a leaky conduit' and fostered asset inflation (true). He asks if a central bank is necessary (p. 245) and notes interest rate changes have economic and distributional effects. So far, so good, but he does not mention deflation or that the Fed and RBA have Full Employment remits, which is to avoid that unmentioned deflation which lost out, crucially in the 1970s (until the GFC: see Pixley, 2018).

Reforms proposed by Kay (p. 270 on) are based on criticising obvious criminal malpractices and the sector's complexity, which he sees as being completely at odds with the sector's primary function, '… to benefit the users of financial services' (p. 276). He wants to change the 'culture' and is bored by tirades against rules from the finance sector. It is true that rules have decreed compliance not 'values' – but Kay says that decent values must be 'internalised' in bank management. Governor Coombs always doubted the possibility that banks would 'internalise' cautious and beneficial norms. He based this doubt on evidence of Australian bank intransigence from the 1890s to the wartime expansion of bank lending into consumer price inflation (not benefitting the war effort) and on, to his postwar days.

While I applaud John Kay's dismay at banking, unfortunately, Australia ended the GFC with 'simple rules' (such as Kay favours) – that ended in terrible outcomes. Why? The Australian Labor Party Prime Minister Gillard's finance reforms in 2012–2013 legislation, notably based on the aim of serving the best needs of each client, were strongly resisted. The incoming right-wing Liberal National Party (LNP) government attempted to reverse them. At least that legality still exists on the statute books, but evasion was facilitated through the LNP's severe cutbacks in resources for the already weak regulators which are supposed to supervise the financial system. For some years after 2014, this Australian government and banks resisted a Royal Commission into 'misconduct' in the finance sector. The Royal Commission started only in early 2018. Banks' senior management, the Royal Commission found, treated the judiciary with 'total disregard' because banking has little effective supervision.[2] Banks are the largest and most influential businesses in Australia (and are even more so in the UK). But under Australia's 'simple rules', senior management had wilfully decided to 'rip off' the bank clients (with LNP blind eyes): lying to outback Indigenous communities about funeral insurance; charging for services never given, particularly remarkable when it did so long after the clients in question were dead. Like John Kay, Royal Commissioner Hayne has (at least to October 2018) met this savage, ruinous financial 'influence' by speaking only of 'greed' and a 'culture of banking' (and illegal instances). But the problem is not going to be resolved by denouncing 'greed' or 'culture'.

Apart from Indigenous societies, it is hard to find another social structure in which 'greed' doesn't feature as a major organising element, but very differently: for example, a feudal structure has greed most prominent among warlords/aristocrats for gaining power and status, and among the top priests for instilling devotion and obedience. Early states like ancient Egypt or China had fabulously wealthy rulers and officials. Peasants had a grim time. Max Weber laboured on the tiresome question of greed in the 1900s capitalist structure and came up with *The Protestant Ethic and the Spirit of Capitalism*. There is a culture of capitalism based on profit-seeking (that he imputed to Protestants who amassed wealth on the backs of workers, to prove they were 'saved' from damnation). Given any laxity, banks also put profits above all else and yet are the main 'corporations' bailed out.

Capitalist money involves specific deals between governments and banks, namely, licences to create most of the money we use, partly on government debt. If that 'truism' (Morgan Ricks (2016) overestimates its acceptance) is ignored, we endure inevitable panics among financial markets. Various ways to temper panics have occasionally been found, for example, in efforts to limit or promote (as needed) bank money creation – mostly by central banks which are self-financing. After the calamities that started with the actions of the US Federal Reserve Chairs Burns and Volcker, many governments copied the US' hiving off of supervision from central banks into state agencies. Nostrums from 'ketchup' economics did influence these new regulators (markets were efficient; there are no bubbles). Central banks' lender of last resort function withered, notably their requirements to investigate banks' books, over which senior management and boards have direct responsibility. States designed finance regulators to be weak via 'ketchup'.

Kay is shocked that no major US or UK executive was jailed after the GFC; many fear that the Australian Royal Commission will similarly require no sanctions. Nothing is helped by ignoring the centrality of money in economic survival or by holding naïve views of banking and governments.

Notes

1. Two central banks (the Reserve Bank of Australia (Kent, 2018) and the Bank of England (McLeay et al., 2014)) discuss money creation.
2. The current LNP Coalition Prime Minister Scott Morrison played a role in thwarting the Royal Commission into banking, along with the LNP's former Prime Ministers Abbott and Turnbull. See Martin (2018) on unwinding Labor rules against 'financial kickbacks' and its 'clients' best interests test' (the latter of which only just survived); see also Ferguson (2018).

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