

A Study of Market Failures in the Globalized Economy with Commentary: A Comparative Review of How Markets Fail: The Logic of Economic Calamities and Freefall: America, Free Markets, and the Sinking of the World Economy

Alexander Alkhabbaz

Written with and under the sponsorship of Richard J. Hunter, Jr.
Professor of Legal Studies and Economics
Seton Hall University

Especially since the 1990s, nations around the world have been ever more connected in a process called globalization: socially, politically, and more importantly, economically. National markets have been interconnected through trade, debt, investment, and membership in a variety of international organizations, such as the International Monetary Fund, the World Bank, and the World Trade Organization.

Globalization reflects a core belief that the world is becoming more homogeneous and that distinctions between national markets are not only becoming less relevant, but for some products or services, distinctions based on traditional concepts such as national borders and “sovereignty” will actually disappear.

Kenichi Ohmae, a Japanese management *guru*, coined the phrase “borderless world” to describe the globalization phenomenon. Much of our understanding about globalization comes from the writings and research of Professor Ohmae, found in four important books: *The Mind of the Strategist*; *The End of the Nation State*; *The Borderless World*; and *Triad Power*.

According to Professor Ohmae, the process of globalization progresses in five steps.

1. Exporting, using the distribution system of a business found in the host country;
2. Exporting, setting up a distribution system in the host country;
3. Manufacturing and distributing products in the host country—but maintaining a company’s ties with its “home” country, perhaps by acting as or identifying as a subsidiary corporation or entity of the parent company;
4. Insiderization, becoming like any other manufacturing concern located in the host country—acquiring the identity of a national company or entity;
5. A fully globalized company—operating in many host countries simultaneously—where it may be difficult to ascertain the country to which a fully globalized company is attached. (Generally, Ohmae, 2005).

Globalization and free markets have been looked upon as a well-matched pair; however, the economic crisis which began in mid-2007 and continued into 2008 showed that markets *can* fail, and when one market fails, many will fall with it. This review will examine the 2007-2008 crisis and the failures that occurred afterwards in order to answer the question: *why and how markets fail in today’s era of globalization*. This review will examine two important works, *How Markets Fail* by John Cassidy (2009) and *Freefall: America, Free Markets, and the Sinking of the World Economy* by Joseph E. Stiglitz (2010). The authors provide their own insights and offer some possible suggestions for avoiding similar problems in the future.

How Markets Fail by John Cassidy was inspired by the consequences of modern-day financial calamities and systemic collapses. Cassidy was born 1963. He is a British-American journalist who has amassed an impressive journalistic resume as a staff writer at *The New Yorker* and as a contributor to *The New York Review of Books*. Cassidy previously served as an editor at *The Sunday Times of London* and as a deputy editor at the New York Post. Cassidy received his undergraduate education at University College, Oxford, and earned masters degrees in journalism from Columbia University and in economics from New York University.

In addition to *How Markets Fail*, Cassidy is the author of *Dot.com: The Greatest Story Ever Sold*, examining the dot-com bubble, a historic speculative bubble covering roughly 1997–2000—with a climax reached on March 10, 2000, when the NASDAQ peaked at 5,132.52.

The context of *How Markets Fail*, its “spark,” is ignited by a critique of *neoliberalism*, a political/economic theory asserting that personal liberty is maximized by limiting government interference in free markets. In recent

times, neoliberalism has been most often associated with promotion of free trade. Neoliberalism is essentially about making trade between nations easier, and assuring freer movement of goods, capital, and enterprises so as to find cheaper resources and inputs, thus maximizing profits and increasing efficiency. Adherents to the neoliberal philosophy argue for the removal of barriers to free trade, such as tariffs, regulations, certain standards, laws, legislation and regulatory measures that inhibit the free flow of capital, and for the elimination of restrictions on capital flows and investment. (Hunter & Lozada, 2014).

In addition, Cassidy provides a sobering critique of the “Chicago School”—representing the *neoclassical* school of economic thought associated with the work of the faculty at the University of Chicago, notable for its alternative to *Keynesianism*—the philosophy which touted direct governmental involvement in the economy, especially during periods of significant economic downturns. Cassidy then provides a detailed illustration in the trends of modern economics before explaining the current financial crisis.

Martinez and Garcia (2014), admittedly no fans of the either neoliberalism or neoclassicism, outline the main points of neo-liberalism to include:

1. PROMOTING THE RULE OF THE MARKET, essentially liberating "free" enterprise or private enterprise from the bonds imposed by the state. Main points emphasized in the discussion of the “rule of the market” include: greater openness to international trade and investment; moves at de-unionization; elimination of price controls; and freedom of movement for capital, goods, and services.
2. CUTTING PUBLIC EXPENDITURE FOR SOCIAL SERVICES, such as education and health care, so as to cut budgets and eliminate fiscal deficits.
3. DEREGULATION OF THE ECONOMY, by reducing government regulation in most areas of business operations.
4. PRIVATIZATION, selling state-owned enterprises and certain government-provided services to private investors, resulting in destatism of the economy.
5. DOWNPLAYING THE CONCEPT OF "THE PUBLIC GOOD" or "COMMUNITY" and replacing it with "individual responsibility."

How Markets Fail is divided into three parts: reality-based economics, *utopian*-based economics (Cassidy uses the term in a quite ironic sense, as we shall see), and a discussion of current “economic calamities.” As the title would suggest, the economy is the focus more often than not, but a number of chapters are devoted to specific economists and their influences. Utopian economists are mentioned prominently in this book, and men like Friedrich August von Hayek, as representatives of the “Austrian School,” embracing a “*laissez faire*” approach, merit special consideration. Hayek himself was awarded the Nobel Prize in Economics in 1974 and was a prominent member of the Chicago School along with Milton Friedman. Hayek’s theories embraced a sharp criticism of socialism and state central planning. Hayek’s views, most notably found in his 1944 book, *The Road to Serfdom*, were especially influential in shaping the economic policies of both British Prime Minister Margaret Thatcher and U.S. President Ronald Reagan. (Economist, 2015).

In *Freefall: America, Free Markets, and the Sinking of the World Economy*, Joseph E. Stiglitz presents a comprehensive review of the economic recession of 2008, a critique of the policies and practices put into place by the Federal Reserve during the administrations of both George W. Bush and Barack Obama, and finally offers solutions that Stiglitz considers more practical to reverse and prevent recessions in the future.

Joseph Eugene Stiglitz, born February 9, 1943, is an American economist and a professor at Columbia University, who has authored or co-authored twenty-eight books in the field of economics and public policy. He was awarded the Nobel Prize in Economics in 2001 and the John Bates Clark Medal, an award second only in prominence to the Nobel Prize, in 1979. Stiglitz was a former senior vice president and chief economist at the World Bank and is a former member and chairman of the Council of Economic Advisers under President Bill Clinton. Professor Stiglitz's most important contribution to the economic policy debate has been in helping define a new economic philosophy, termed a “third way,” somewhere in the policy recesses between the philosophies of Keynes and Hayek, which postulated still an important, but somewhat more limited, role of government in the economy. However, Stiglitz also notes that while unfettered or unregulated markets often did not work well, the government was not always able to correct the limitations or dysfunctions of markets to any significant extent as well.

Stiglitz is known for his critical view of the management of globalization, of free-market economists, whom he calls “free market fundamentalists,” and of some international institutions like the International Monetary Fund

and the World Bank. Stiglitz points out in *Freefall* that the crisis was mounting well before 2007-2008, and even “names names” of individuals, institutions, and policies which share the blame for the decimation of the world economy. The structure of the book is straight-forward. Stiglitz begins with an introduction to the crisis, moves to a discussion of how it was handled, addresses the larger systemic macro and micro problems underlying the crisis, and then concluding with the postulate that change is necessary, Stiglitz provides clear, however somewhat controversial, solutions for the future in the context of a globalized economy.

Stiglitz presents several key themes within the book. The first theme revolves around the crisis itself and its historical context. Stiglitz notes that the housing collapse, often touted as the root cause of the crisis, was not an isolated incident in American economics. In fact, just eight short years before the crisis of 2007-2008, the tech bubble had popped, but this was not nearly as crippling as the housing bubble. He asserts, “The richest country in the world was living beyond its means” (p. 2). In fact, the practice of borrowing and consuming “as if [...] incomes were growing” (p. 2) led the American economy to move from one bubble to the next. Stiglitz rightfully points out that one of the differences between the 2007-2008 crisis and other crises was that the 2007-2008 crisis took place in the midst of globalization and another was that the 2007-2008 crisis was deeper and more systemic than other crises.

Stiglitz underscores the global nature of the crisis by pointing out that U.S. debt was now being sold to other countries in the form of our Treasury or *T Bills*, and states “nearly a quarter of U.S. mortgages had gone abroad” (p. 21). Another key characteristic of what made the crisis different is how other countries acted during the crisis. In the Great Depression, America was still essentially an isolationist country, and the actions of other nations did not affect the American economy to any large extent. However, in 2008, most European nations, as well as many developing nations, were thrown into an economic recession which diminished the overall global economy in which America was fully immersed. More specifically, there was a “global lack of aggregate demand—the total of all the goods and services that people throughout the world want to buy” because countries were stockpiling their money in reserves to “set aside for a ‘rainy day’” (p. 20).

In short, globalization had made the 2007-2008 crisis much more complex (and deeper) than any other economic crisis to date. There was one other key difference: after most of the previous crises, governments (most especially the United States) had intervened and had taken steps to regulate markets in order to fix specific dysfunctions. However, after the 2007-2008 crisis, “Wall Street” and their free market allies pushed instead for the further *deregulation* of the market on the principle that the market itself was not flawed.

Stiglitz is also a fierce critic of the theory of a “perfect market”—one in which the following conditions theoretically prevail: perfect market information is available to all market participants; no single participant with market power is able to set prices; non-intervention by governments; no significant barriers to entry or exit exist; equal access to factors of production (land, labor, capital, and managerial ability); profit maximization; and no externalities (defined as third party (or spill-over) effects arising from the production and/or consumption of goods and services) for which no appropriate compensation is paid. (E.g., Mathiessen, 1997/2015).

Stiglitz asserts that the idea of a perfect market is fundamentally flawed because of the intervention of human interests. Without the type of regulation that was put in place in other crises, bankers and banks would continue their skewed practices and flawed policies in a failing system, operating under false assumptions.

Freefall highlights the responses of *both* the Bush and Obama administrations and argues how they fell short of addressing the root causes of the problem. Stiglitz is a fierce critic of the policies of the Bush Administration for further aggravating the problem by maintaining the position “that there was only a ripple in the housing market and that few homeowners would get hurt” (p. 28). The Bush administration inflicted further damage on the economy when, in February of 2008, Bush “passed a \$168 billion tax cut [...], he refused to believe the economy was headed for recession” (p. 29). By leading the American public to a false sense of security, President Bush ultimately further damaged the economy. Stiglitz points out that time after time, the Bush administration propounded policies that favored the “rich,” and refused to help the working and middle classes, who were in the most need of help. Stiglitz notes that the Bush administration focused on “corporate welfare, [it] reached new heights—the amounts spent were beyond the imagination of anyone in any prior administration” (p. 38).

Therefore, Stiglitz concludes that the Bush administration implemented precisely the wrong policies in order to combat the crisis. The Obama administration continued many of these policies—especially in the area of taxation.

From the outset in *How Markets Fail*, Cassidy outlines key elements of utopian economics (again, his term), which in this case, places secular faith in the perfectibility of the market and in an axiom that “unregulated markets work perfectly.” Cassidy criticizes that while utopian economics *may* work well in an ideal universe (he actually is quite skeptical), it fails to produce or achieve anything in reality. Cassidy analyzes utopian economics and reinforces his ideas with many examples taken from the writings of many prominent economists.

Adam Smith, of course, is one of the prime originators of the core belief in the free market economy. The “invisible hand” of the market became the guiding and influential metaphor that carries on to even today in a discussion of the role of government in the market. Cassidy quotes Smith: “It is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner, but from their regard to their own interest” (p. 32). Cassidy asserts, however, that the “invisible hand” is not absolute—even Smith would allow that the government should have *some* role in the market when it was likely that a financial calamity was going to occur.

A famous utopian, as Cassidy describes him, or believer in the free market that took Smith to another level, was Friedrich August von Hayek. In terms of the invisible hand, Hayek may be considered equally as the proponent of a merged political-economic theory, although Hayek contributed most directly to the economic theory that price conveys a signal for the markets, a rationale that is still used in today’s free market economic theory. Hayek made note that although the state may have a lot more information than the individual, it cannot possibly have *all* the information. Hayek thus concludes that the state cannot and should never set prices. (Generally, Hudik, 2014).

Another is Milton Friedman. His economic/political philosophy extolled the virtues of the free market economic system with minimal intervention by the government. He asserted that individualism (as opposed to collectivism) was the bedrock upon which America was founded on—at least in popular belief and culture. Friedman taught at the University of Chicago for more than three decades. Friedman received the 1976 Nobel Prize in Economics. Friedman's challenged what he later called "naive Keynesianism" and opposed Keynesian interventionism into the economy. During the 1960s, Friedman promoted an alternative macroeconomic policy to Keynesianism known as "monetarism"—stating that the main function of the government is to focus on the monetary supply, and the rest of the economy will take care of itself. Although Friedman expressed his opposition to the existence of the Federal Reserve System, he argued that, given that it *does* exist, a steady, small expansion (or perhaps contraction) of the money supply was the only wise policy for the government to follow, depending on the exact circumstances found in the economy.

Friedman was no stranger to politics either. He was a major advisor to President Ronald Reagan and British Prime Minister Margaret Thatcher. In his 1962 book, *Capitalism and Freedom*, Friedman advocated policies such as a volunteer military, freely floating exchange rates, abolition of medical licenses, a negative income tax, and school vouchers—policies that have become the staples of modern libertarianism as well. Friedman juxtaposed his ideas on deregulation and privatization with communism or state control of the factors of production. Penn Bullock (2009) comments that Friedman’s ideas concerning monetary policy, taxation, privatization, and deregulation greatly influenced official government policies, especially during the 1980s. His monetary theory significantly influenced the Federal Reserve's response to the global financial crisis of 2007–08.

Friedman touted the *efficient market hypothesis (EMH)*—that all market participants receive and act on relevant information as soon as it becomes available so that financial institutions get prices correct, and even more, that prices can be predicted. He argued that financial markets are tied to economic fundamentals. Gene Grossman, currently a Professor of International Economics at Princeton University, and Joseph Stiglitz vigorously disputed this theory. Others have joined in their criticisms. (Wojcik, Kreston & McGill, 2003).

The financial crisis of 2007–08 led to renewed scrutiny of the hypothesis itself. For example, Brian Milner (2009) noted that “The shaky hypothesis that had long dominated academic thinking about the markets has finally been buried under an avalanche of unforeseen calamities, uncontrolled greed and other seemingly irrational behaviours it couldn't possibly explain.” Market strategist Jeremy Grantham stated flatly that the EMH was responsible for the current financial crisis, claiming that belief in the hypothesis caused financial leaders to have a “chronic underestimation of the dangers of asset bubbles breaking.”

(Quoted in Nocera, 2009). Financial journalist Roger Lowenstein (2009) likewise blasted the theory, declaring “The upside of the current Great Recession is that it could drive a stake through the heart of the academic nostrum known as the efficient-market hypothesis.”

Former Federal Reserve Chairman Paul Volcker added that "clear that among the causes of the recent financial crisis was an unjustified faith in rational expectations [and] market efficiencies." (Volcker, 2011). "By 2007–2009, you had to be a fanatic to believe in the literal truth of the EMH," noted Laurence Siegel (2010).

At this point, let us return to Stiglitz once again. Another key theme advanced by Stiglitz is the idea that the economic system, as a whole, is a failed system. He identifies the process called *securitization* as the root cause of the crisis—what he calls “the great scam of the early twenty-first century” (p. 77). Securitization is the process of taking an illiquid asset, or group of assets, such as mortgages, and through financial engineering transforming them into a marketable security. [Financial engineering is a multidisciplinary field involving “financial theory, the methods of engineering, the tools of mathematics and the practice of programming.” (Beder & Marshall, 2011)]. In terms of Stiglitz’s argument, the key example of securitization was the mortgage-backed security or MBS. The process is explained by Gallant (2007) as follows:

“First, a regulated and authorized financial institution originates numerous mortgages, which are secured by claims against the various properties the mortgagors purchase. Then, all of the individual mortgages are bundled together into a mortgage pool, which is held in trust as the collateral for an MBS. The MBS can be issued by a third-party financial company, such a large investment banking firm, or by the same bank that originated the mortgages in the first place. Mortgage-backed securities are also issued by aggregators such as Fannie Mae or Freddie Mac.”

More specifically, Stiglitz asserts that “the mortgages had been [...] passed on to all manners of banks and investment funds around the country [and] sold around the world” (p. 77). He furthers his argument:

“The securitization process supported never-ending fees, the never-ending fees supported unprecedented profits, and the unprecedented profits generated unheard-of bonuses, and all of this blinded the bankers. [...] They may have suspected that it was unsustainable [...] and it was unsustainable” (p. 79).

Additionally, bankers were being offered incentives to push these problematic mortgages on unsuspecting “fools who could be sold the toxic mortgages and the dangerous pieces of paper that were based on them” (p. 91). Bankers, along with the rating agencies who were put in place to stop these very types of practices, were paid to take part in this mortgage scheme and reaped enormous profits.

Stiglitz identifies the source of the “scam” as the 1999 repeal of the *Glass-Steagall Act of 1933* during the Clinton Administration. The original legislation was put in place to separate commercial and investment banks so as “to avoid the clear conflicts of interest that arise when the same bank issues shares and lends money” (p. 162). Glass-Steagall essentially set up a “regulatory firewall between commercial and investment bank activities, both of which were curbed and controlled. Banks were given a year to decide on whether they would specialize in commercial or in investment banking.” (Heakel, 2015). The 1999 repeal resulted in the re-merger of commercial and investment banking functions, which violated the second purpose of the *Glass-Steagall Act*:

“To ensure that those entrusted with caring for ordinary people’s money [...] didn’t engage in the same kind of risk-taking as investment banks—which aim primarily to maximize the returns of the wealthy” (p. 162).

In short, this major dysfunction in the banking sector of the American economy, which many European nations rushed to copy (most especially Ireland), subsequently became *their* problems as well. It permitted the “rich to become richer” through deregulation of the banking sector and encouraged schemes such as the MBS scam which directly resulted in the demise of both Lehman Brothers and Bear Stearns in the fall of 2008. Oppositely, this left small to medium-sized businesses and the low to middle-classes in potential financial ruin, facing both corporate and individual bankruptcies and massive mortgage foreclosures.

At this point, we return once again to Cassidy. One of the key points raised in *How Markets Fail* was *spillovers* of the kind that benefit large corporations and which may negatively affect smaller ones or their employees. Spillovers are economic events in one context that occur because of something else in a seemingly unrelated context. (Kim et al., 2014). Cassidy argued that the problem was that many big corporations were motivated by managing their “private costs” and neglected social ones. Social costs do not directly affect these corporations, but private costs do.

As a result, market prices often do not normally take into account these important social costs. Ignoring social costs in establishing prices produces a dysfunction in the market system, and as a result, wrong signals are being sent out regarding the true or “real costs” of a business operation or of its products or services.

The problem of spillovers has been addressed by British economist Professor Ronald Coase (1910-2013) who was a Professor of Economics at the University of Chicago Law School and later at the University of Buffalo. Coase argued that the government should enforce laws to avoid negative spillovers from occurring, establishing the case for the corporation to pay the “real costs” of operating in a marketplace. Another adjunct to the spillover theory is that more often than not, free markets may lead to the creation of monopolies and oligopolies. In these circumstances, the monopoly or oligopoly (a small number of sellers) would seek to control wages and salaries, to further eliminate competition, and cause consumers to fall victim to their predatory tactics. Social costs are the farthest from their corporate minds.

Professor George Akerlof, the husband of current Federal Reserve Chair Janet Yellen, who shared the 2001 Nobel Prize in Economics with Michael Spence and Joseph Stiglitz, notes that market systems are operated on the basis of information, and wrong information leads to unacceptable outcomes. In what can best be described as a spillover, hiding product information leads to unfavorable outcomes for the consumer and sends the wrong signal to the market. In terms of financial markets, circumstances where corporations keep vital information from investors often leads to an excess of irrational buying or selling that may lead to a financial crash. Another spillover effect occurs where so-called *noise traders*, a term used to describe investors who may choose to make decisions without the benefit of fundamental data and who “generally have poor timing, follow trends, and over-react to good and bad news,” irrationally participate in financial markets. (Investopedia, 2015).

Cassidy also references the point that generalizations based on uncertainty within a market system may lead to the possibility of wrong decisions being made. Hyman Minsky, an economist at Washington University in St. Louis, Missouri, who also taught at the University of California at Berkeley, argued that a key mechanism that pushes an economy towards a crisis is the accumulation of debt by the *non-government sector*. He identified three types of borrowers that contribute to the accumulation of insolvent or “bad” debt: hedge borrowers, speculative borrowers, and *Ponzi* borrowers. Minsky states that individual investors tend to make smart decisions, although at times they may engage in risky behavior when the market is doing well. These risks lead to an excess of buying (and borrowing) which then leads to a bubble. Once in a bubble, Minsky argues that investors tend to more conservative and may decide to pass up opportunities that may actually have benefitted them. The continuation of the bubble results in an accumulation of unsustainable debt, and may lead to a recession or even in the extreme, to a depression. Capitalism may be seen as bipolar by nature, exhibiting huge swings in the capital and financial markets, and thus the capitalist system needs the intervention of government to control it from both the extremes of good times and bad times. “A fundamental characteristic of our economy,” Minsky wrote in 1974, “is that the financial system swings between robustness and fragility and these swings are an integral part of the process that generates business cycles.” (Quoted by Mihn, 2009).

And now, we return one final time to Stiglitz. On a global scale, Stiglitz believes that the world economy is facing several critical challenges: the global gap between demand and supply, climate change, uneven world-wide interest rates and consumption, low productivity rates (Samuelson, 2015), coupled with low rates of employment participation, global economic inequality, and financial instability. Similarly, he believes the American economy faces many of these same long-term problems: low rates of employment participation, off-shoring of jobs coupled with a lack of technical innovation in core industries, growing income inequality, a growing retirement-age population (putting an enormous strain on governmental programs), necessary retooling the energy sector, addressing environmental challenges and injustices, and inefficient health care and education systems. These problems have been addressed in the past in a piecemeal fashion by both the world and the United States; but in Stiglitz’s opinion, no one has addressed the long-term problems in a correct manner. Proving that he can do more than provide a laundry list of societal ills, Stiglitz offers some advice to those in the financial- sector, along with governments around the world.

The first solution for Stiglitz is to continue to implement intelligent financial sector regulation by the government. He points out that because of America’s recent history of hostility to the role of government in the economy, many in the general public have been conditioned to equate “regulation” with the terms “socialism,” “the nanny state,” and even “nationalization”—terms which “carry with them emotional baggage that makes clear thinking difficult” (p. 197).

The 2007-2008 crisis seemed to contradict the ideas of those who would have otherwise “been the greatest critics of government activism,” (p. 199) as it became obvious that something had to be done. Stiglitz believes, however, that policies chosen in the crisis were implemented incorrectly.

He believes that the government should be involved in the dealings on Wall Street (and in the larger economy) in four comprehensive ways: maintaining full employment and a stable economy, which means “design[ing] regulations that limit the damage resulting from market mispricing” (p. 202); promoting innovation through government-supported research and protecting intellectual property by restructuring the patent system; providing social protection and social insurance “against many key risks that individuals face, such as unemployment and disability” (p. 203); and preventing exploitation by private firms, mortgage companies, credit card companies, and banks.

In his comments about how economics and politics should intertwine, Stiglitz argues for a “*New Capitalism*,” which includes “a new set of social contracts based on trust between all the elements of our society, between citizens and government, between this generation and the future” (p. 209).

Stiglitz also calls for transparency within the economic and financial systems globally and in the United States. Stiglitz points out that “no one would have put their money into Wall Street if they knew it was making such poor investments” (p. 155). In his opinion, the lack of transparency can also be seen as deception, and he supports his theory by noting that banks “moved risk off the balance sheet so no one could appropriately assess it” (p. 156). Stiglitz calls for creating policies to make “cooking the books to hide from investors what is going on [...] illegal” (p. 159). Furthermore, loopholes, such as offshore banking, should be shut down so the practices of “money laundering, tax evasion, regulatory evasion, and other illicit activities” (p. 160) by wealthy Americans can be curtailed in order to promote greater economic equality.

Similarly, Stiglitz calls for a “*New Economic Order*” on a global scale. Recall that Stiglitz may be considered as one of the preeminent “global insiders.” Akin to his suggestions for the American economy, Stiglitz calls upon better global governance to be put in place by the G-20 and the IMF. Once again, Stiglitz questioned the policies and strategies in the post-World War II era. After colonialism was dismantled in the 1960s, as a spate of independent developing countries began to emerge, the IMF and World Bank imposed “financial-sector deregulation, privatization, and trade liberalization,” which all “came to be seen as instruments of post-colonial control” (p. 220). Developing countries were forced to follow in the shadows of American economic policy and it produced the same results as it did in the United States. Stiglitz calls for the IMF and World Bank, institutions largely created by the United States, to discontinue these harmful policies and to end the blind faith in the idea of unbridled free market capitalism. In hand with the *New Economic Order*, Stiglitz emphasizes the need for a *New Global Reserve System* on the order of the ideas presented by “a UN commission of experts on the restructuring of the global financial and economic system, which [he] chaired” (231). His strongest argument is stated as follows:

“Developing countries, China foremost, today holds trillions of dollars in reserves—money they can draw upon in the event of a crisis, such as the Great Recession. [...] I emphasized that this crisis exposed the problem of a global insufficiency of aggregate demand. [...] Annual emissions of a new global reserve currency would mean that countries would no longer have to set aside part of their current income as protection against global volatility—instead, they could set aside the newly issued “money.” This would thereby increase global aggregate demand and strengthen the global economy” (p. 231).

Furthermore—and this will no doubt be quite controversial—this new currency cannot be the dollar because of instability in the past. A new global reserve currency would mean in America “the value of the dollar would decrease [...] and there would be less need for the government to run a big deficit to maintain the economy at full employment” (p. 233).

Some Brief Personal Reflections

John Cassidy’s *How Markets Fail* argues just how neo-classical economics doesn’t supply answers at all in terms of reality. Utopian based economics, worshipping at the altar of free market capitalism, and touting a radically diminished role of the government, as advocated by Hayek, Friedman and others, led to the near worldwide financial collapse that the United States experienced and which many European nations (most especially Greece) are still experiencing. The only way to move past it is, ironically, by understanding what we shouldn’t expect from an economic system. A reality-based economic system should be considered.

As Cassidy notes, “... it is essential to put Wall Street in its place and confront utopian based economics with reality-based economics” (p. 346) that will correctly state risks involved and which will correctly evaluate the ability of individuals and institutions to withstand financial risks and shocks as experienced in 2007-2008.

In both books, the authors offer a different perspective but advance several common themes which explain why markets failed. The authors represent the views of economists who posit that markets will once again fail on a global scale unless significant changes or reforms are implemented. Both Cassidy and Stiglitz believe that government must play a significant role in implementing these changes. Both Cassidy and Stiglitz believe that unless systemic changes come about, a new crisis will certainly develop because financiers are too greedy, the system is corrupt, and the economy is unsustainable in its present form. All in all, it is safe to say that Cassidy and Stiglitz believe that something must change in the realm of economic policy in order to have a well-functioning and sustaining economy that is both profitable and “works” for everyone. Elements of the free market have been deemed “too big to fail”—even in the face of real failure—so it will be up to a new generation of economists to prevent further failures by accepting the role of both a reality-based free market capitalism and an enlightened and renewed government working together to assure its success for all market participants—not just those who have benefitted most in the past.

Works Cited

Primary

- Cassidy, John. (2009). *How Markets Fail: The Logic of Economic Calamities*. New York: Farrar, Straus and Giroux.
 Stiglitz, Joseph E. (2010). *Freefall: America, Free Markets, and the Sinking of the World Economy*. New York: Norton, 2010.

Secondary

- Beder, Tanya S. & Marshall, Cara M. (2011). *Financial Engineering: The Evolution of a Profession*. Hoboken, N.J.: John Wiley & Sons.
 Bullock, Penn. (2009). “Bernanke’s Philosopher.” Reason.com, at <http://reason.com/archives/2009/11/17/bernankes-philosopher>.
 Economist. (2015). Website, at <http://www.economist.com/economics-a-z/h>.
 Gallant, Chris. (2007). “What is Securitization?” Investopedia, at <http://www.investopedia.com/>.
 Heakal, Reem. (2003). “What was the Glass-Steagall Act?” Investopedia, at <http://www.investopedia.com>.
 Hudik, Marek. (2014). “Utopian Thinking in Economics.” Charles University, Mires Institute Working Paper Series, at http://papers.ssrn.com/sol3/JELJOUR_Results.cfm?code=B4.
 Hunter, Richard J., Jr. & Lozada, Hector. (2014). “A Primer on Tariff and Non-Tariff Barriers to International Trade: (Hopefully) A Common Sense, Non-Technical Discussion from a U.S. Perspective.” *Journal of Social Economics*, 2(2), pp. 37-53, available at <http://www.rassweb.com>.
 Kim, T., Maskus, K. & Oh, K.-Y. (2014). “Effects of Knowledge Spillovers on Knowledge Production and Productivity Growth in Korean Manufacturing Firms.” *Asian Economic Journal*, 28, pp. 63-79.
 Lichtell, Louis. (1996). Obituary. “Economist Who Decoded Lending Trends,” at <http://www.nytimes.com/1996/10/26/us/h-p-minsky-77-economist-who-decoded-lending-trends>.
 Lowenstein, Roger. (June 7, 2009). Book Review. “The Myth of the Rational Market.” *Washington Post*, at <http://www.rationalwalk.com/?p=1871>.
 Martinez, Elizabeth & Garcia, Arnoldo. (1996). “What is Neoliberalism? A Brief Definition for Activists,” at <http://www.corpwatch.org/article.php?id=376>.
 Mathieson, M. (1997/2015). “The Perfect Market Economy.” *The Encyclopedia of Corporate Governance*, at http://e.viaminvest.com/B10CompetitionInProductMarkets/App10PerfectMarketModel/Exhi_Perf_market_econ.asp.
 Mihn, Stephen. (2009). “Hyman Minsky and Financial Instability Hypothesis, at [http://www.softpanorama.org/Skeptics/Financial_skeptic/Casino_ca\[pitalism/Critics](http://www.softpanorama.org/Skeptics/Financial_skeptic/Casino_ca[pitalism/Critics).
 Milner, Brian. (July 3, 2009). “Sun finally sets on notion that markets are rational.” *The Globe and Mail*, at www.theglobeandmail.com.
 Nocera, Joe. (2009). “Poking Holes in a Theory on Markets.” *New York Times*, at www.nytimes.com/2009/06/06/business/06nocera.html.
 Ohmae, Kenichi. (2005). *The Next Global Stage: The Challenges and Opportunities in our Borderless World*. Upper Saddle River, N.J.: FT Press.
 Samuelson, Robert J. (February 23, 2015). “Middle Class squeezed by slow productivity growth.” *Asbury Park Press* (on line), at <http://www.app.com>.
 Siegel, Laurence B. (2010). “Black Swan or Black Turkey? The State of Economic Knowledge and the Crash of 2007-2009.” *Financial Analysts Journal*, 66(4), pp. 6-10.
 Wojcik, Dariusz, Kreston, Nicholas & McGill, Sarah. (2003). “Freshwater, saltwater, and deepwater: Efficient market hypothesis versus behavioral finance.” Working Paper in Employment Work and Finance 12-03, at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2008788
 Volcker, Paul (October 27, 2011). Book Review. “Financial Reform: Unfinished Business.” *New York Review of Books*.