The Great Divide

No one today can deny that there is a great divide in America, separating the richest – sometimes described as the 1 percent – and the rest. Their lives are different: they have different worries, different aspirations, and different lifestyles (pxi).

Those in the 1 percent and even more in the upper 1 percent debate what kind of jet airplane to buy, the best way to shelter their income from taxes and so on… (pxi). The level of inequality in America is not inevitable; it is not the result of inexhorable laws of economics. It is a matter of policies and politics (pxii).

Inequality has become urgent even among the 1 percent. Increasing numbers of them realize that sustained economic growth, upon which their prosperity depends, can't happen when the vast majority of citizens have stagnant incomes (pxii).

In the decades after World War II, the country grew at its fastest pace, and the country grew together. Regarding inequality, the Chicago Nobel Prize winner, Robert Lucas, put it forcefully: "of the tendencies that are harmful to sound economics, the most seductive and poisonous is to focus on questions of distribution (pxv).

With stances like Lucas's so fashionable in the economics profession it is little wonder that economists paid almost no attention to growing inequality in the country. This neglect meant that ultimately they couldn't provide a good explanation of what was going on in the economy, they couldn't grasp the implications of growing inequality (pxv).

Almost all of us, including those in the 1 percent, would actually be better off if there were less inequality. We are not seeking to wage a new class war, but rather to establish a new sense of national cohesion , one that had waned since a great divide opened up in our country (pxvi).

The strength of the United States has always been its "soft power", and most notably, its moral and economic influence, the example it gives to others and the influence of those ideas. Unfortunately, because of growting inequality, the American model has not been delivering for most of the population (pxvi).

The typical American family is worse off then they were a quarter a century ago, adjusted for inflation. An economic model that doesn't serve a majority of its citizens is unlikely to be a role model for other countries to emulate (pxvi).

The 2008 crisis was not an act of God, like a once in a hundred year flood or earthquake. It was something that we did to ourselves; as with outsized inequality, it was the result of politics and policies. Many ordinary Americans have become dissillusioned with the political process: in the aftermath of the 2008 crisis, hundreds of billions went to save the banks and little went to help homeowners (pxviii).

Timothy Geithner and Larry Summers were among the architects of deregulation that helped foment the crisis – the obama administration opposed efforts to restructure home mortgages, to relieve millions of Americans who had suffered predatory and discriminatory lending by the banks (pxviii).

During the past decade, four of the central issues facing our society have been the great divide – the huge inequality has is emerging in the United States and many other advanced countries – ecomonic mismanagment, globalization, and the role of the state in the market (pxix).

But while politics has been part of the cause of our current troubles, it will only be through politics that we will find solutions; markets by themselves won't do it. Unfettered markets will lead to more monopoly power, more abuses by the financial sector and more unbalanced trade relations (pxix).

Stiglitz, Joesph (2016). The Great Divide. W W Norton and Company, USA.

it will only be t hrough reform of our democracy that we will be able to heal the great divide and restore the country to shared prosperity (pxix).

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Showing Cracks

Before the crisis, there was a party going on – only a few at the top were invited, but the rest of us would be asked to pay the bill. Unfortunately, those who were supposed to make sure that the economy was kept on an even keel were too closely connected to those throwing the party (p3).

The making of the Great Recession is intimately connected with the making of the great divide. There was a major economic boom during the 90s, fueld by a tech bubble in which technology stocks soared in price. But after the bubble burst, the economy slid into recession in 2001 (p3).

The George W. Bush administration's all purpose remedy was a tax cut aimed at the very wealthy. Seldom had so few gotten so much from so many. Inequality weakens demand and the economy. America's growing inequality was moving money from the bottom of the pyramid to the top, and since the top spend less of their income than those at the bottom, this weakened overall demand (p4).

The most effective tools for strengthening demand and improving equality are tax and expenditure policies decided by congress and the administration. When these policies are inadequate they put an undue burden on monetary policy, which is the responsibility of the Federal Reserve (p5).

There is more than a small dose of hypocrisy on the part of those who advocate free markets, evidenced in the Great Recession. The seeming advocates of free market economics are more than willing to accept government assistance – including massive bailouts (p5).

The money goes to the top with everyone else picking up the tab. Deficits are not necessarily a problem: not if the money is spent making investments and especially not if this spending occurs when the economy is weak (p8).

But the Bush deficits were especially problematic: they occurred during a time of seeming prosperity, even if that prosperity reached only a few corporations and pocket books of the 1 percent. The Bush years were marked by growing inequality which he neither recognized nor did anything about – except to make it worse (p8).

The median income of the typical American fell under Bush – and that was true even before the recession made things much worse. Even the IMF recognise that inequality is associated with instability. The making of the 2008 crisis exemplifies how this happens (p9):

Central banks create bubbles in respnose to a weakened economy born of growing inequality. The bubble eventually bursts and wreaks havoc in the economy. Rather than regulations that would stabilize the economy and protect ordinary citizens, we got deregulation that led to instability and left American's prey to the bankers (p9).

To understand the makings of the Great recession, one has to go back in time, to the deregulation movement that was given such a boost by President Reagan (p9).

The deregulation itself began under Reagan with the appointment of Alan Greenspan, but it continued under Clinton including the destruction of the regulatory walls between investment and commercial banks (p10).

The financial sector is emblematic of what has gone wrong in our economy – a major contributor to the growth of inequality, a major source of instability in our economy, and an important cause of the economy's poor performance over the last three decades (p11).

As we have seen repeatedly, the financial sector doesn't perform well on its own; it requires strong regulations, effectively enforced, both to prevent it from imposing harm on the rest of society and to make sure that it actually performs the functions that it is supposed to perform (p11).

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The United States used its sway as the sole remaining superpower to advance its economic interests – or more accuratly, to advance the interests of its large and powerful corporations. And among these perhaps the most influential was the financial sector (p11).

The United States pushed countries to liberalize their financial markets. The result: country after country faced crises – including some of the countries that had been doing so well before they liberalized their financial markets (p13).

They impose excessive charges on merchants that act like a t ax on every credit card transaction. A tax that enriches the coffers of the banks rather than the well-being of society. In competititive markets the charges inevitably get passed on in the form of higher prices to be paid by ordinary citizens (p13).

The excessive risk-taking in the financial sector, combined with its success in curbing regulations led to the most severe crisis in three quarters of a century. The crisis was predictable and predicted. As always, it is the poor who suffer most from such crises. They lose their jobs and face protracted unemployment (p14).

14 million homes were foreclosed between 2007 and 2013. Quantitiative easing focuses more on restoring prices in the stock market than restoring lending to small and medium sized businesses, and as a result was more effective in restoring wealth to the rich than in benefiting average Americans (p15).

The financial sector pushed inequality-increasing policies and developed an ideology to support them. It pushed the idea that markets on their own lead to efficient and stable outcomes, and on that assumption governments should liberalize and privatize. It has contended that monetary policy should focus on inflation and not job creation (p15)

Transparency

There is a broad understanding that market economies work best with transparency – it is only with good information that resources can be well allocated. But while markets masy preach transparency for others, they do what they can to limit it for themselves, after all, with transparent and competitive markets, profits are driven to zero (p16).

Government is supposed to weigh in to countervail these trendancies towards secrecy. But this won't happen if government is captured by business, and especially financial markets. Unfortunately, the Obama administration failed to use the 2008 crisis to make markets more transparent.

The Role of Economists

When an ordinary business fails there are consequences for its owners and their families but typically not for the entire economy. As our political leaders and the banks themselves said, we cannot allow any of the big banks to fail (p16). But if that is the case then the must be regulated (p17).

For if they are too big to fail, and they know it, excessive risk-taking is a one-sided bet: if they win, they keep the rpofits; if they lose, taxpayers pick up the tab. Dodd-Frank, the financial sector reform bill, did nothing to address the too-big-to-fail problem (p17).

One area where it made progress was to circumscribe the ability of federally insured financial instititions from writing derivatives – those risky products that had led to the collapse of AIG and the largest bailout in the history of the planet (p17).

But Congress, with language written by Citibank itself, repealed even this provision in 2014, without even any hearings! The influential documentary Inside Job threw light on what has been going on in the economics profession (p17).

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Economists are wont to say that incentives matter, it is the one thing that economists all agree on. The financial sector provides ample rewards for those who agree with them: lucrative consultancies, research grants and the like. The documentary raises the question: Could this have influenced some economist's judgement (p17)?

Responses to the Crisis

Virtually any eco nomist who did not blindly believe in the virtues of the free and unregulated markets saw the writing on the wall. Yet the Fed chair Ben Bernanke would blithely claim that the risks were "contained" (p17).

The Fed and the Treasury took a 180 degree turn and bailed ot AIG, the most expensive bailout in human history, an amount of corporate welfare to one firm that exceeded that given to the millions of poor Americans over years and years (p18).

Most American's incomes are back to the level of 1992 – two decades ago. Trillions have been unnecessarily lost by following the 1 percent's agenda. Bailing out the banks didn't mean bailing out the shareholders, the bond holders and the bankers. But that's what we did (p19).

When the IMF, the world bank or the US government lends money to other countries, we impose conditions – we want to make sure that the money is spent in the way intended. The irony is that the U.S. Treasury is among those most insistent on such conditionality. But when it came to imposing conditions on U.S. banks, Treasury demurred (p19).

But because we imposed no conditions, t he money went instead to pay mega-bonuses – clearly undeserved – to the bankers. Years after the crisis, lending to small and medium size businesses is still far below what it was before the crisis (p19).

The Fed lent money to the banks at a zero interest rate, which they then lent out to the government and big businesses at far higher interest rates. Even a 12 year old could make money that way (p20).

The government stealthily arranged for the bad mortgages to move off the banks' books onto the government balance sheet. Put baldly, Americans were cheated. Had the banks been charged what they should have been, our national debt would be lower and we would have more money to invest in education, technology and infrastructure (p20).

Like so many of the economic policies designed by and for the 1 percent , it relied on trickle down economics: throw enough money at the banks, and everyone will benefit. It didn't work out that way, and predicably so (p20).

While hundreds of billions went to the banks, a fraction of this was allocated to help homeowners – around 10 billion. Wasting money on banks might be necessary to save the economy and any fine tuning of the bank rescue programs apparently was viewed as a luxury we could not afford (p21).

But exactly the oppositie attitude was taken in regard to homeowners and ordinary citizens: we had to proceed carefully, so as not to make any mistakes. Terms like "moral-hazard" were through aroiund glibly, even though the real moral hazard issue was that of the banks, which had been rescued time after time (p21).

Bad bank practices had large repurcussions elsewhere (p22).   Even when it passed in 2010, the regulatory reform bill – Dodd Frank was recognized to be at most a cup half full. No sooner was it passed than the banks began efforts to water it down (p22).

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They initiated efforts in Congress to repeal key provisions and finally in December 2014 they were successful in rolling back a key provision regulating derivatives. Few outside the financial sector believe that we have really elmininated a significant risk of another meltdown (p23).

Of the discussions that have centered on how to prevent banks from doing hardm to the rest of society, almost no attention has focused on how to make banks actually perform the critical functions that they neeed to perform if the economy is to function well (p23).

The financial sector has a long established proclivity for exploitation – for taking advantage of others, whether it's in the form of market manipulation, insider trading, abusive credit card practices, monopolistic anticompetitive practices or deiscriminatory and predatory lending (p23).

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Capitalist Fools'

In 1987, the Reagan administration decided to remove Paul Volcker as chairman of the Federal Reserve board and appoint Alan Greenspan in his place. Volcker had done what central bankers are supposed to do (p40). On his watch, inflation had been brought down from 11 percent to 4 percent.In the world of central banking that should have earned him a A+++ rating and assured his reappointment (p41).

But Volcker also understood that finanical markets need to be regulated. Reagan wanted someone who did not believe any such thing. Greenspan presided over two bubbles. After the high-tech bubble burst in 2000-2001, he helped inflate the housing bubble.

Tearing Down the Walls

In November 1999, Congress repealed the Glass Steagall act – the culmination of $300 million worth of lobbying by the banking and financial industries. Glass Steagall had long separated commercial banking from investment banking (p42).

It had been enacted after the Great Depression and was aimed at curbing the excesses of that era, including grave conflicts of interest. The most important consequence of the repeal of Glass Steagall was they way it changed an entire culture (p43).

Commercial banks are not supposed to be high risk ventures; they are supposed to manage other people's money conservatively. It is with this understanding that the government agrees to pick up the tab if they fail. Investment banks on the other hand have traditionally managed rich people's money (p43).

When repeal of Glass Steagall brought commercial banks and investment banks together, the investment bank culture came out on top. There was a demand for high returns that could only be obtained through big risk taking. Self-regulation is preposterous, as even Alan Greenspan eventually conceded (p43).

Applying the Leeches

President Bush and his advisors seemed to believe that tax cuts for the rich where the cureall for any economic disease – the modern day equivalent of leeches. The Bush administration was providing an open invitation to excessive borrowing and lending – not that American consumers needed any more encouragement (p45).

Faking the Numbers

On July 30, 2002, in the wake of a series of major scandals – notably the collapse of WorldCom and Enron – Congress passed the Sarbanes-Oxley Act. This made it clear that there had been serious problems with our accounting system (p45).

Accounting is a sleep-inducing topic for most people, but if you can't have faith in a company's numbers, then you can't have faith in anything about the company at all. A collateral problem with stock options is that they provide incentives for bad accounting: top managers have every incentive to provide distorted information to pump up the share price (p45).

Letting it Bleed

The final turning point came with the bailout package of 2008, that is, with the administrations response to the crisis itself. But it didn't address the underlying reasons for the loss of confidence. The banks had made too many bad loans (p46).

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No one knew what was the truth and what was fiction. The bailout package was like a massive transfusion to a patient suffering internal bleeding – and nothing was done about the source of the problem, namely all those foreclosures (p47).

The administration talked about confidence building, but what it delivered was actually a confidence trick. If the administration had really wanted to restore confidence in the financial system, it would have begun by addressing the underlying problems – the flawed incentives and the inadequate regulatory system (p47).

The truth is that most of the individual mistakes boil down to just one – a belief that markets are self-adjusting and that the role of the government should be minimal. The embrace of America – and much of the rest of the world – of this flawed economic philosophy made it inevitable that we would eventually arrive at the place we are today (p48).

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The Economic Consequences of MR. Bush

When we look back some day at the catastrophe that was the Bush administration, we will think of many things: the tragedy of the Iraq war, the shame of Guantanamo and Abu Ghraib, the erosion of civil liberties (p27).

We will also think of a tax code that has become hideously biased in favour of the rich; a national debt that will have grown to 70 percent; a swelling cascade of mortgage defaults; a record 850 billion trade deficit and oil prices that are higher than they have ever been (p27).

There is no threat of America's being displaced as the world's richest economy. But our grandchildren will still be living with , and struggling with , the economic consequences of Mr. Bush.

Remember the Surplus?

Alan Greenspan worried aloud about how he'd ever be able to manage monetary policy once the nation's debt was fully paid off. By the time George W. Bush was sworn in, the tech boom was over. The NASDAQ fell 15 percent in a single month and no one knew for sure the effect the collapse of the Internet bubble would have on the real economy (p29).

It was a moment ripe for Keynesian economics, a time to prime the pump by spending more on education, technology and infrastructure – all of which America desperately needed, and still does. The country could well afford to ramp up domestic investment in these key areas. Doing so would have staved off recession in the short run while spurring growth in the long run (p29).

The first major initiative pursued by the president was a massive tax cut for the rich, enacted in June 2001. Those with incomes over a million got a tax cut of $18,000 – more than 30 times larger than the cut received by average Americans (p30).

The inequities were compounded by another tax cut, in 2003, which skewed even more heavily toward the rich. These tax cuts mean that the average reduction for an American in the bottom 20 percent will be a scant $45 whole those with incomes of more than $1 million will see their tax bills reduced by an average of $162,000 (p30).

America's class structure may not have arrived there yet, but it's heading towards the same direction as Brazil's and Mexico's (p30).

The Bankruptcy Boom

In breathtaking disregard for the most basic rules of fiscal propriety, the administration continued to cut taxes even as it undertook expensive new spending programs and embarked on a financially ruinous "war of choice" in Iraq (p30).

A budget surplus of 2.4 percent of gross domestic product, which greeted Bush as he took office, turned into a deficit of 3.6 percent in the space of four years. The United States had not experienced a turnaround of this magnitude since the global crisis of World War II (p30).

Tax breaks for the president's friends in the oil and gas indiustry increased by billions and billions of dollars. Defence expenditures increased by 70 percent , t hough much of the growth wasn't helping to fight the War on Terror at all, but was being lost or outsourced in failed missions in Iraq (p31).

In a nutshell, money was being spent everyplace except where it was needed. Little has been done about our decaying infrastructure – be it the levees in New Oreleans or bridges in Minneapolis. You'll still hear some loudly argue that the administration's tax cuts were meant to stimulate the economy, but that was never true (p31).

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Bush's own fiscal irresponsibility fostered irresponsiblity in everyone else. Credit was shoveled out the door and subprime mortgages were made available to those who could not afford them. Credit card debt mounted to a whopping $900 billion by the summer of 2007 (p31).

Americans took advantage of the low interest rates, signed up for new mortgages with "teaser" initial rates, and went to town on the proceeds. All of this spending made the economy look better for a while. But the consequences for families would become apparent within a few years, when interest rates rose and mortgages proved impossible to repay (p32).

And Then There's Iraq

The war in Iraq has cost the country dearly in blood and treasure. Government figures officially acknowledge that more than half a trillion dollars has been spent by the U.S. "in theater". The total costs of the Iraq war mount, even by a conservative estimate to at least 2 trillion (p33).

It is natural to wonder, What w ould this money have bought if spent on other things? U.S. aid to all of Africa has been hovering around $5 billion a year, the equivalent of less than two weeks of direct Iraq-war expenditures (p33).

Had even a fraction of that 2 trillion been spent on investments in education and technology, or improving our infrastructure, the country would be in a far better position economically to meet the challenges it faces in the future (p33).

For a sliver of that 2 trillion we could have provided guaranteed access to higher education for all qualified Americans. In retrospect, the only big winners from the war have been the oil companies, the defense contractors and al-Qaeda (p33).

The continuing reliance on oil, regardless of price, points to one more administration legacy: the failure to diversify America's energy resources. So many gifts to the oil industry wre included in the president's 2003 energy bill that John McCain referred to it as the "No Lobbyist Left Behind" bill (p35).

Contempt for the World

America's budget and trade deficits grew to record high under President Bush. Deficits don't have to be crippling in and of themselves. If a business borrows to buy a machine, it's a good thing, not a bad thing. In the end, Mr. Bush failed to impose American dominance but he did succeed in weakening cooperation (p36).

The administration's basic contempt for global institutions was underscored in 2005 when he named Paul Wolfowitz as the president of the World Bank. Widely distrusted from the outset, and soon caught up in a personal controversy, Wolfowitz became an international embarrassment and was forced to resign his position hafter less than two years on the job (p36).

Meanwhile, we have become dependent on other nations for financing our own debt. Today, China alone holds more than $1 trillion in public and private American IOUs. Cumulative borrowing from abroad during the eix years of the Bush administration amounst to some $5 trillion (p37).

Just as Guantanamo and Abu Ghraib have eroded American moral authority, so the Bush administration's fiscal housekeeping has eroded our economic authority (p37). What is required is not spending money that we don't have, increasing taxes on the rich, reducing corporate welfare, strengthenening the safety net for the less well off, and making greater investments in education, technology and infrastructure (p38).

We'll have a better chance of getting others to open up their markets if we ourselves act less hypocritically – that is, if we open our own markets to their goods and stop subsidizing agriculture (p38).

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The Anatomy of a Murder: Who Killed America's Economy?

The blame should be centrally placed on the banks and the finanical sector broadly, and the investors.

The banks were supposed to be experts in risk management. They not only didn't manage risk; they created it. The stock options that they used to pay some of their senior executives provided incentives for bad accounting, including incentives to engage in extensive off-balance-sheet accounting (p51).

The only defense that the bankers have is that investors made them do it. Their investors didn't understand risk. The reality is that the banks exploited this investor ignorance to push their stock prices up, getting higher short-term returns at the expense of higher risk (p51).

If the banks were the main perpetrators of the crime they had many accomplices. Rating agencies played a central role. They believed in financial alchemy and converted F-rated subpriime mortgages into A-rated securities that were safe enough to be held by pension funds (p52).

This was important because it allowed a steady flow of cash into the lending market, which provided the fuel for the housing bubble. Mortgage brokers played a key role. They wre less interested in originating good mortgages than in originating many mortgages (p52).

Some of the mortgage brokers were so enthusiastic that they invented new forms of mortgages. These low- to no-documentation loans came to be called liar loans. This was an "innovation" but there was a good reason why such innovation hadn't occurred before (p52).

The transaction costs generated by writing mortgages provided a strong incentive to prey on innocent and inexperienced borrowers. For instance, by encouragi ng more short-term lending and borrowing, entailing repeated loan restructurings , which helped generate high transaction costs (p52).

The regulators too were accomplices to the crime. They should have recognized the inherent risks in the new products. They should have done their own risk assessments rather than relying on self-regulaton or on the rating agencies (p53).

The regulators deceived themselves into thinking that if only they ensured that each bank managed its own risk then the system would work. Amazingly they did not pay attention to systemic risk. Though concerns about systemic risk constitute one of the primary rationales for regulation in the first place (p53).

The repeal of the Glass Stegall act played an especial role not just because of the c onflicts of interest it opened up but also because it transmitted the risk taking culture of investment banking to commercial banks, which should have acted in a far more prudent manner (p53).

There should have been tougher enforcement of anti-trust laws. Banks were allowed to grow to be too big to fail – or too big to be managed. and such banks have perverse incentives because of the insurance policy that too big to fail brings with it (p53).

There is one other set of accomplices – the economists who provided the arguments that those in the financial markets found so convenient and self-serving. These economists provided models – based on unrealistic assumptions of perfect markets – in which regulation was unnecessary (p54).

Modern economic theories had explained how flawed these earlier "neoclassical" models were. But these insights were completely ignored. Many of the most popular economic theories aided and abetted regulators, investors, bankers and policymakers – they provided the rationale for their policies and actions (p55).

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They made the bankers believe that in pursuing their self-interest, they were, in fact, advancing the well-being of society. Our regulatory authorities allowed the financial markets to use the abundance of funds in ways that were not socially productive (p55).

They allowed the low interest rates to feed a housing bubble. They had the tools to stop this, They didn't use the tools they had. The American economy, like the Latin American economies of the 1970s, seemed to be doing well, because the housing bubble fed a consumption boom, as household savings fell all the way down to zero (p56).

Not only did they fail in their regulatory role, they became cheerleaders for the bubble that eventually consumed America. When asked about a possible bubble, Greenspan suggested there was none – only a little froth. That was clearly wrong (p56).

The Fed argued that you could not tell a bubble until after it burst. That was correct. But one can make strong probabilistic statements (p56). All policy is made in the context of uncertainty. House prices, especially at the lower end, soared, yet the real incomes of many Americans stagnated (p56).

Government is also to blame for doing too little. Conservative critics believe that government is to blame for doing too much. It is America's fully private financial markets that invented all the bad practices that played a central role in the crisis (p58).

When government encouraged home ownership, it meant permanent homeownership. It didn't intend for people to buy homes beyong their ability to afford them. The poor would losed their life savings as they lost their home (p58).

There is one more important culprit, which, in fact, has played a key behind-the-scenes role. America's political system, and especially its dependence on campaign contributions. This allowed Wall Street to exercise the enormous influence that hit has had, to push for the stripping of regulations and to the appointment of regulators who didn't believe in regulation (p59).

The bankers were maximising their incomes, given the rules of the game. The rules of the game said that they should use their political influence to get regulations and regilators that allowed them to walk away with as much money as they could (p59).

The politicians responded to the rules of the game. They had to raise money to get elected, and to do that, they had to please powerful wealthy constitutents. There are those now who would like to reconstruct the system as it was prior to 2008 (p60).

Banks that arre too big to fail will be allowed to continue little changed. They will continue to be able to gamble, and they will continue to be too big to fail. Accounting standards will be relaxed to give them greater leeway (p60).

Little will be done about incentive structures or even risky practices. If so, then another crisis is sure to follow (p60).

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How to Get Out of the Financial Crisis

Over the past 30 years, market economies have faced more than 100 crises. That is why government regulation and oversight are an essential part of a functioning market economy (p61). Without them there will continue to be frequent severe economic crises in different parts of the world (p62).

The troubles we now face were caused largely by deregulation and low interest rates. Low interest rates and easy access to funds encouraged reckless lending, the infamous interest-only, no-down-payment, no-documentation subprime mortgages (p62).

Not only are the poor losing their homes, they are also losing their life-savings.The assumption that house prices could continue to go up at a rapid pace looked particularly absurd in an eco nomy in which most Americans were seeing their real incomes declining (p63).

Investment banks bought the original mortgages, sliced and diced the risk, and then passed them on – or at least as much as they could. Our bankers forgot that their job was to prudently manage risk and allocate capital (p63).

They became gambling casinos – gambling with other people's money, knowing that the taxpayer would step in if the losses were too great. Loose money and light regulation were a toxic mix. It exploded (p63).

What made America's recklessness truly dangerous is that we exported it. Thanks to globalization, Wall Street was able to sell off its toxic mortgages around the world. It appears that about half of the toxic mortgages were exported. Had they not been, the US would have been in even worse shape (p63).

Our financial and economic systems are closely intertwined. Banks all over the world lend and borrow from each other; they buy and sell complicated financial instruments – which is why bad regulatory practices in one country can infect the global system (p64).

1. Recapitalize the banks: The government needs to provide equity. In return, it should have voting stakes in the banks it helps. Three questions are raised: is it fair to the taxpayer and the society? Is there enough oversight and restrictions to make sure that the bad practices of the past do not recur? and is there enough money (p65)? The banks are so nontransparent that no one can fully answer the question, but what we do know is that the gap in the balance sheet is likely to get bigger (p66).

2. Stem the tide of foreclosures.

3. Pass a stimulus that works.

4. Restore confidence through regulatory reform.

5. Create an effective multilateral agency.

Most Americans believe that Wall Streeters are likely to put their self-interest ahead of the country.

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Of the 1 Percent, By the 1 Percent, For the 1 Percent

The upper 1 percent of Americans are now taking in a quarter of the nation's income every year. While the top 1 percent have seen their incomes rise 18 percent over the past decade, those in the middle have actually seen their incomes fall (p88).

In terms of income equality, America lags behind any country in the old and ossified Europe, as President George W. Bush used to deride. Among our closest counterparts are Russia and the oligarchs, and Iran. The justification the economists came up with was "marginal-productive theory". This theory associated higher incomes with higher productivity and a greater contribution to society (p89).

It is a theory that has always been cherished by the rich. Evidence for its validity however, remains thin. Those who have contributed great positive innovations to our society have received a pittance compared with those responsible for the finanical innovations that brought our economy to the brink of ruin (p89).

Growing inequality is the flip-side of something else – shurnk opportunity. Many of the distortions that lead to inequality undermine the efficiency of the economy (p89).

Monopoly power and preferential tax treatment for special interests undermine the efficiency of the economy. A modern economy requires "collective action" – it needs government to invest in infrastructure, education and technology (p90).

America has long suffered from underinvestment in infrastructure – look at the condition of our highways and bridges, our railroads and airports. Further cutbacks in these areas lie ahead. The more divided a society becomes in terms of wealth, the more reluctant the wealthy become to spend money on common needs (p90).

Economists are not sure how to explain the growing inequality in America. One reason why we have so much inequality is because the top 1 percent want it that way. Much of today's inequality is due to manipulation of the financial system, enabled by changes in the rules that have been bought and paid for by the financial industry itself (p91).

Wealth begets power which begets more wealth. Citizens United has enshrined the right of corporations to buy government, by removing limitations on campaign spending. The personal and the political are today in perfect alignment (p92).

Virtually all U.S senators and most of the representativesin the house are members of the top 1 percent and know that if they serve the top 1 percent well they will be rewarded by the top 1 percent when they leave office (p92).

Given the power of the top 1 percent, this is how you would expect the system to work. With the top 1 percent in charge, and paying no price, the notion of balance and constraint goes out the window. Of all the costs imposed on our society by the top 1 percent, perhaps the greatest is the erosion of our sense of identity, in which fair play, equality of opportunity, and a sense of community are so important (p93).

The wealthiest often stand actively in the way of policies that would improve the life of people in general. The top 1 percent have the best lifestyles, the best houses, the best education and the best doctors, but there is one thing that money doesn't seem to have bought: an understanding that their fate is bound up with houw the other 99 percent live (p94).

Throughout history this is something that the top 1 percent eventually do learn. Too late (p94).

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The 1 percent's problem

Consider the Walton family: the six heirs to the Wlmart empire possess a combined wealth of some 90 billion dollars, which is equivalent to the wealth of the entire bottom 90 percent of U.S society. Many at the bottom have zero or negative net worth, especically after the housing bubble (p95).

As Warren Buffet put it: “There's been class warfare going on for the last 20 years and my class has won”. While the rich have been growing richer, most Americans have been unable to maintain their standard of living, let alone to keep pace. A typical full-time male worker receives the same income today has he did a third of a century ago (p96).

The evidence from history and from around the modern world is unequivocal: there comes a time when inequality spirals into economic dysfunction for the society, and when it does, even the rich pay a steep price (p96).

When one interest group holds too much power, it succeeds in getting policies that help itself in the short term rather than help society as a whole over the long term. This is what has happened in America when it comes to tax policy, regulatory policy, and public investment (p96).

It is not an accident that the current recession, like the Great Depression, was preceded by large increases in inequality. Even if Mitt Romney chose to live a much more indulgent lifestyle, he would spend only a fraction of his wealth in a typical year to support himself, his wife and their several houses (p97).

But take the same amount of money and divide it among 500 people, say in the form of jobs paying 43,400 dollars apiece – and you'll find that almost all of the money gets spent (p97).

The relationship is straightforward and ironclad: as more money becomes concentrated at the top, aggregate demand does into a decline. Unless something else happens by way of intervention, total demand in the economy will be less than what the economy is capable of supplying – and tha means growting unemployment, which dampens demand even further (p97).

In a broad sense, “rent seeking” defines many of the ways by which our current political process helps the rich at the expense of everyone else. The money is siphons from poor and middle class Americans through predatory lending practices, can be thought of as rents (p99).

In their simplest form, rents are nothing more than redistributions from one part of society to the rent seekers. Much of the inequality in our economy has been the result of rent-seeking because rent seeking distibutes money from those at the bottom to those at the top (p99).

Rent seekers make nothing grow. Efforts are directed toward getting a larger share of the pie rather than increasing the size of the pie. Countries rich in natural resource are infamous for rent seeking activities. It's far easier to get rich in these countries by getting access to resources at favorable terms than by producing goods or services that benefit people and increase productivity (p99).

When corporate CEOs argue that wages have to be reduced or that there must be layoffs in order for companies to compete – and simultaneously increase their own compensation – workers rightly consider what is happening to be unfair (p100).

In a society in which inequality is widening, fairness is not just about wages and income, or wealth. It's a far more deneralized perception. Do I seem to have a stake in the direction society is going or not? Do I share in the benefits of collective action, or not? If the answer is a loud “no”, then brace for a decline in motivation whose repercussions w ill be felt economically, and in all aspects of civic life (p101).

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Those at the top can take comfort in knowing that their chances of downward mobility are less in America than they are elsewhere (p101). We've been inculcated with notions of "civic virtue". It is our responsibility to vote (p101).

But civic virtue is fragile. If the belief takes hold that our political and economic systems are stacked, individuals will be released from their civic obligations. Deceptive credit card practices and predatory lending have leeft Americans more boradly with a perception that banks are not to be trusted (p101).

Economists often underestimate the role of trust in making the economy work. If every contract had to be enforced by one party taking the other party to court, our economy would be in gridlock. Nowhere is trust more important than in the public sphere and politics (p102).

There, we have to act together. It's easier to act together when most individuals are in the same boat, at least in boats within a range of like sizes. But growing inequality makes our fleet look different. It's a few mega yachts surroiunded by masses of people in dugout canoes, or clinging to floatsam – which helps explain our vastly differing views of what the government should do (p103).

The 1 percent in generations past often knew better. They knew that if there wasn't a solid base there would be no top of the pyramid. Franklin D. Roosevelt knew that the only way to save an esentiall capitalist America was not only to spread the wealth through taxation and social programs, but to put restraints on capitalism itself, through regulation (p104).

Roosevelt and Keynes, while reviled by the capitalists, succeeded in saving capitalism from the capitalists (p104).

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Slow Growth and Inequality are Political Choices, We Can Choose Otherwise

Those who strive not to think about inequality suggest that this is just about the "politics of envy". Those who discuss the issue are accused of fomenting class warfare. But as we have come to grasp the causes and consequences of these inequities we have come to understand that it is not about envy (p105).

Too much of the poverty at the bottom of the income spectrum is due to economic discrimination and the failure to provide adequate education and healthcare to the nearly one out of five children growing up poor (p105).

We used to think of ourselves as a middle class society, where each generation was better off then the last. It used to be understood that the best way to grow was to build out from the middle – rather than trickle down from the top (p105).

The children of the poor can afford neither the advanced degrees that are increasingly required for employment nor the unpaid internships that provide the alternative route to "good" jobs. America is unique among the advanced countries in not recognising access to health care as a basic human right (p107).

The real strength of the United States is derived from its "soft power", not its military power. But growing inequality is sapping our standing in the world from within. Can an economic system that provides so little opportunity – where real median income is lower today than it was a quarter-century ago – provide a role model that others seek to emulate, even if a few at the very top have done very well (p109)?

An economic system that ensured access to jobs with decent pay would not spend so much on prisons – in some states spending on prisons has at times exceeded that on universities. It pays to invest in people.

And because so much money at the top comes from expolitation, higher taxes at the top do not seem to have much of an adverse effect on economic performance. The 700 billion dollar bank bailout pales in comparison to what the bankers' fecklessness has cost our economy and our society. – trillions of dollars in lost GDP, millions of Americans thrown out of their homes and jobs. Yet few in the financial world have been held accountable (p112).

Similarly, by taxing land, oil and minerals more and forcing those who extract resources from public land to pay the full value of these resources, which rightly belong to all the people, we could then spend these proceeds on public investments – educations, technology and infrastructure – without resulting in less land, less oil or fewer minerals (p113).

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Inequality Goes Global

No one even mentions the notion of trickle-down economics anymore, and few are willing to argue that there is a close congruence between social contribution and private rewards. One cannot really claim the world is “flat” when a typical African receives investment in his or her human capital of a few hundred dollars, while rich Americans get a gift from their parents and society in excess of half a million dollars (p115).

Overall, the private sector in Europe and America has been unable to create many good jobs since the beginning of the current century. Those suffering the most are the young whose life prospects will be badly hurt by the extended periods of unemployment they face today (p116).

While Western leaders talked about a new emphasis on growth and employment, they offered no concrete policies backing these aspirations.

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Inequality is a Choice

Starting around the fall of Communism in the late 1980s, economic globalization accelerated and the gap between nations began to shrink. While the gap between some regions has markedly narrowed, huge gaps remain (p119).

Overall equality across humanity, considered as individuals, has improved very little. 8 percent of humanity takes home 50 percent of global income; the top 1 percent alone takes home 15 percent. Income gains have been greatest among the global elite and the great "emerging middle classes" in China, India, Indonesia and Brazil (p119).

Who lost out? Africans, some Latin Americans, and people in post-Communist Eastern Europe and the former Soviet Union. Income inequality first started to rise in the late 70s and early 80s in America and Britain. Within the last decade, income inequality grew even in traditionally egalitarian countries like Germany, Sweden and Denmark (p120).

The gross domestic product of the United States has more than quadrupled in the last 50 years, and nearly doubled in the last 25, but as is now well known, the benefits have gone to the top – and increasingly the very, very top (p120).

Ninety-five percent of all income gains since 2009 have gone to the top 1 percent. The typical American man makes less t han he did 45 yesars ago, after adjusting for inflation. Men who graduated from high school but don't have a four-year college degreee make almost 40 percent less than they did four decades ago (p121).

American inequality began its upswing 30 years ago, along with tax decreases for the rich and the easing of regulations on the financial sector. That's no coincidence. It has worsened as we have underinvested in our infrastructure, education and health care and social safety nets (p121).

Rising inequality reinforces itself by corroding our political system and our democratic governance. And Europe seems all to eager to follow America's bad example. The embrace of austerity, from Britain to Germany, is leading to high unemployment, falling wages and increasing inequality (p121).

Officials like Angela Merkel and Mario Draghi argue that Europe's problems are a result of a bloated welfare spending. But that line of thinking has only taken Europe into recession and even depression. That theings may have bottomed out is little comfort to the 27 million people out of a job in the EU (p121).

On both sides of the Atlantic, the austerity fanatics say, march on: these are bitter pills to swallow to achieve prosperty. But prosperity for whom (p121)?

Excessive financialization – which helps explain Britain's dubious status as the second-most-unequal country after the United States – also helps explain the soaring inequality. American innovations in rent seeking have gone global (p121).

Inequality and poverty among children are a special moral disgrace. They flout right-wing suggestions that poverty is a result of laziness and poor choices: children can't choose their parents. None of this is inevitable. Some countries have made the choice to create more equitable economies (p122).

Sourth Korea, where a half-century ago just one in 10 people attended college, today has one of the world's highest university completion rates.

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Democracy in the 21st Century

Thomas Piketty sheds new light on the “reforms” sold by Ronald Reagan and Margaret Thatcher in the 1980s as growth enhancers from which all would benefit. Their reforms were followed by slower growth and heightened global instability, and what growth did occur benefited mostly those at the top (p123).

What we have been observing – wage stagnation and rising inequality, even as wealth increases – does not reflect the workings of a normal market economy. The problem is not with how markets should work, but with our political system, which has failed to ensure that markets are c ompetitive, and has designed rules that sustain distorted markets in which corporations and the rich can exploit everyone else (p124).

Simple changes, Piketty points out, such as higher capital-gains and inheritance taxes, greater spending to broaden access to education, rigorous enforcement of anti-trust laws, corporate governance reforms that circumscribe executive pay, and financial regulations that rein in banks’ ability to exploit the rest of society – would reduce inequality and increase equality of opportunity markedly (p125).

If we get the rules of the game right we might even be able to restore the rapide and shared economic growth that characterized the middle calss socieities of the mid 20th century. The main question confrinting us today is not really about capitalism in the 21st century. It is about democracy in the 21st century (p125).

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Phony Capitalism

There is no such thing as a “purely” capitalist system. We have always had a mixed economy, relying on the government for investment in education, technology and infrastructure. The most innovative and successful industries in America, tech and biotech, rest on foundations provided by government research (p127).

It is better to tax bad things than good things – to tax pollution and speculation rather than say work and savings. It is also better to tax things like land, oil and other natural resources, which don’t disappear when they are taxed (p127).

Taxes should encourage things that are of widespread common good and discourage those that are costly to our society. Globalization has given companies like Apple and Google new opportunitiesto dodge taxes by claiming that their immense profits originate not from the ingenuity of their American researchers, but from a few employees scattered across low-tax jurisdictions such as Ireland (p128).

The most successful entrepreneurs have figurred out how to create barriers to competition behind which they can earn huge profits. It is not a surprise that the world’s richest person, Bill Gates, earned his fortune through a company that has engaged in anticompetitive practices in Europe, America and Asia (p128).

In many cases, oil, gas and mineral companies don’t actually own these resources, they simply exstract them from publicly owned land while paying just a fraction of their true value. The best solution to this inequity would be a fair and efficient auction, which would guarantee the public the full return on these assets (p129).

While most Americans acceept the general principle that the rich should pay a larger fraction of their income in taxes, our system departs markedly from this principle in practice. The very richest pay a lower percentage of their income than do the merely rich – and their reported income is often a fraction of their actual income (p129).

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Equal Opportunity, Our National Myth

President Obama's second inaugural address used soaring language to reaffirm America's commitment to the dream of equality of opportunity: He said "We are true to o ur creed when a little g irl born into the bleakest poverty knows that she has the same chance to succeed as anybody else, because she is an American, she is free, and she is equal, not just in the eyes of God but also in our own" (p159).

The gap between aspiration and reality could hardly be wider. Toda y, the United States has less equality of opportunity than almost any other advanced industrial country. Study after study has exposed the myth that America is a land of opportunity. This is especially tragic (p159).

While Americans may differ on the desireability of equality of outcomes, there is near-universal consensus that inequality of opportunity is indefensible. The Pew Research Center has found that some 90 percent of Americans believe that the government should do everything it can to ensure equality of opportunity (p159).

Rags to riches stories were not a deliberate hoax, but given how they've lulled us into a sense of complacency, they might as well have been (p160). Another way of looking at equality of opportunity is to ask to what extent the life chances of a child are dependent on the education and income of his parents (p160).

Is it just as likely that a child of poor and poorly educated parents gets a good education and rises to the middle class as someo ne born to middle-class parents with college degrees? Even in a more egalitarian society, the answer would be no (p160).

Discrimination is only a small part of the problem. Probably the most important reason for lack of equality of opportunity is education: both its quantity and quality. After World War II Europe made a major effort to democratize its education system. We did, too, with the GI bill, which extended higher education to Americans across the political spectrum (p160).

Children in affluent families get more esposure to reading and less exposure to environmental hazards. Their families can afford enriching experiences like music lessons and summer camp. They get better nutitition and health card, which enhance learning, directly and indirectly (p161).

Unless current trends in education are reversed, the situation is likely to get even worse. In some cases it seems as if policy has actually been designed to reduce opportunity: government support for many state schools has been steadily gutted over the last few decades – and especially in the last few years (p161).

Meanwhile, students are crushed by giant student loan debts t hat are almost impossible to discharge, even in bankruptcy. This is happening at the same time that a college education is more important than ever for getting a good job (p161).

Young people from families of modest means face a Catch-22: without a college education, they are condemned to a life of poor prospects; with a college education, they may be condemened to a lifetime of living on the brink (p161).

Those at the top have the connections and social captial to get oppoprtunities. Those in the middle and the bottom don't. Americans are coming to realize that their cherished narrative of social and ecomonic mobility is a myth. Grad deception of this magnitude are hard to maintin long (p162).

Without substantial policy changes , our self-image, and the image we project to the world, will diminish – and so will our economic standing and stability. It is unconscionable that a rich coiuntry like the United States has made access to higher education so difficult for the bottom and middle (p162).

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There are many alternative ways of providing universal access to higher education. A more educated populaton yields greater innovation, a robust economy, and higher incomes. We will never fully succeed in achieving Mr Obama's vision of a poor girl's having exactly the same opportunities as a wealthy girl. But we could do much, much better, and must not rest until we do (p163).

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Student Debt and the Crushing of the American Dream

Before the housing bubble burst in 2007, banks persuaded low and moderate income homeowners that they could turn their houses and apartments into piggy banks. They seduced them into taking out home equity loans – an in the end, millions lost their homes (p165).

In other cases, banks and mortgage borkers pushed aspiring homeowners to borrow beyond their means. The wizards of f inance, who proded themsleves on risk management, sold toxic mortgages that were designed to explode (p165).

They bundled the dubious loans into complex financial instruments and sold them to unsuspecting investors. Everyone recognizes that education is the only way up, but as a college degree becomes increasingly essential to making one's way in the 21st century economy, education for those not to the manner born is increasingly unaffordable (p165).

Student debt for graduates exceeds 26,000 dollars, about a 40 percent increase in just seven years. But an "average" like this masks huge variations. America is distinctive among advanced industrialized countries in the burden it places on students and their parents for financing higher education (p165).

America is also exceptional among comparable countries for the high cost of a college degree, including at public universities. Average tuition, and room and board, at four-year colleges is just short of 22,000 dollars a year, up from under 9000 dollars in 1980-81 (p166).

Like much else, the problem of student debt worsened during the Great Recession: tuition colsts at public universities increased by 27 percent in the past five years – partly because of cutbacks in government support – while median income shrank (p166).

In California, invlation adjusted tuition more than doubled in public two year community colleges, and by more than 70 percent in four year public schools from 2007-2012 (p166).

With costs soaring, incomes stagnating, and little help from government, it was not surprising that total student debt, around 1 trillion dollars, surpassed total credit card debt last year. Responsible Americans have learned how to curb their credit card debt but the challenge of controlling student debt is even more unsettling (p166).

Curbing student debt is tantamoundt to curbing social and economic opportunity. College graduates ear 12,000 dollars more per year than those without college degrrees; the gap has almost tripled just since 1980. Our economy is increasingly reliant on knowledge related industries (p166).

No matter what happens with currency wars and trade balances, the United states is not gong to return to making trex tiles. Unemployment rates among college graduates are much lower than those with only a high school diploma (p166).

To be competitive in the 21st century is to have a highly educated labour force, one with college and advanced degrees. Instead, we are foreclosoing on our future as a nation. Those with large debts are likely to be caustious beforre undertaking the additional burdens of a family (p167).

But even when they do, they will find it more difficult to get a mortgage. And if they do, it will be smaller, and real estate recovery will consequently be weaker. One study of Rutgers University graduates showed that 40 percent had delayed making a major home purchase, and for a quarter, the high level of debt had an effect on household formation or getting further education (p167).

As has been repeatedly observed, all of the economic gains since the Great Recession have gone to the top 1 percent and student debt is almost impossible to discharge in bankruptcy proceedings. Even when

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for-profit schools didn't deliver what they promised and didn't provide an education that would let the borrower get a job that paid enough to pay back the loan (p168).

We should cut off federal suppport for these for-profit schools when they fail to gradudate students, who don't get jobs and then default on their loans (p168).

The combination of predatory for-profit schools and predatory lenders is a leech on America's poor. These schools have even gone after young veterans who served in Iraq and Afghanistan. There are heart-rending stories of parents who co-signed student loans – only to see their child killed in an accident or die of cancer or another disease – and, like students, they can't easily discharge these debts (p168).

The government shouldn't be profiting from our poorest while subsidizing our richests (p169).

Along with tougher regulation of for-profit schools and the banks they connive with, and more humane bankruptcy laws, we must give more support to middle-class families struggling to send their children to college, to ensure that they have a standard of living that is equal to their parents (p169).

Some wo nder how the American ideal of equality of opportunity has eroded so much. The way we finance higher education provides part of the answer. Student debt has become an integral part of the story of American inequality (p169).

Robust higher education, with healthy public support, was once the linchpin in a system that promised opportunity for dedicated students of any means. We now have a pay-to-play, winner-take-all game where the wealthiest are assured a spot, and the rest are compelled to take a gamble on huge debts with no guarantee of a payoff (p169).

Even if compassion isn't a factor – even if we focus just on recovery now and growth and innovation tomorrow – we must do something about student debt. Those concerned about the damage America's growing divide is d oing to our ideals and our moral character should put student debt at the top of any reform agenda (p169).

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Justice for Some

Most people evicted from their homes have not been paying their mortgages, and, in most cases, those who are throwing them out have rightful claims. But Americans are not supposed to believe in justice on average. We don't say that most people imprisoned for life committed a crime worthy of that sentence (p171).

The U.S. justice system demands more, and we have imposed procedural safeguards to meet these demands. But banks want to short-circuit these procedural safeguards. They should not be allowed to do so (p171).

It was widely known that banks and mortgage companies were engaged in predatory lending practices, taking advantage of the least educated and most financially uninformed to make loans that maximized fees and imposed enormous risks on borrowers (p171).

But banks used all their muscle to stop states from enacting laws that curtail predatory lending. With one out of four mortgages in the US underwater – more owed than the house is worth – there is a growing consensus that the only way to deal with the mess is to write down the value of the principal (p172).

America has a special procedure for corporate bankruptcy, called Chapter 11, which allows a speeedy restructing by writing down debt, and converting some of it into equity. Lenders complain that such a law would violate their property rights. But almost all changes in laws and regulations benefit some at the expense of others (p172).

When the 2005 bankruptcy law was passed, lenders were the beneficiaries, they didn't worry about how the law affected the rights of debtors. Growing inequality, combined with a flawed system of campaign finance, risks t urning America's legal system into a travesty of justice. Some may call it the "rule of law", but it would not be a rule of law that protects the weak against the powerful. Rather, it would enable the powerful to exploit the weak (p173).

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The One Housing Solution Left: Mass Mortgage Refinancing

A mass refinancing program would work like a potent tax cut. Refinancing would also significantly reduce the chance of default for underwater homeowners. With fewer losses from posat loans burdening their balance sheets, lenders could make more new loans, and communities plagued by mass foreclosures might see relief from blight (p175).

Well over half of all American homeowners with mortgages are paying rates that would appear to make them excellent candidates to refinance. Many of those with stable jobs, good credit scores, and even a modest amount of home equity have already done so. But many others can’t refinance because the collapse in housing prices has wiped out their home equity (p175).

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Inequality and the American Child

Children, it has long been recognized, are a special group. They do not choose their parents, let alone the broader conditions into which they were born. They do not have the same abilities as adults to protect or care for themselves (p178).

That is why the League of Nations approved the Geneva Declaration on the Rights of the Child in 1924, and why the international commu nity adopted the Convention on the Rights of the Child in 1989. Sadly, the United States is not living up to its obligations. In fac t, it has not even ratified the Convention on the Rights of the Child. The US, with its cherished image as a land of offportunity should be an inspiring example of just and enlightened treatment of children (p178).

Instead, it is a beacon of failure – one that contributes to global sluggishness on children't rights in the international arena. Though an average American childhood may not be the worst in the world, the dispartiy between the country's wealth and the condition of its children is unparalleled (p178).

About 14.5 percent of the American population as a whole is poor, but 19.9 percent of children - some 15 million individuals – live in poverty. Among developed countries, only Romania has a higher rate of Child poverty (p178) (p178).

The U.S. rate is two-thrirds higher than that in the United Kingdom, and up to four times the rate in the Nordic countries. For some groups, the situation is much worse: more than 38 percent of black children and 30 percent of Hispanic children, are poor (p179).

None of this is because American's don't care about their children. It is because America has embraced a policy agenda in recent decades that has caused its economy to become wildly unequal, leaving the most vulnerable segments of society further and further behind (p179).

The growing concentration of wealth has meant less money to spend on investments for the public good, like education and protection of children. As a result, America's children have become worse off. Their fate is a painful example of how inequality not only undermines economic growth and stability but also violates our most cherished notions of what a fair society should look like (p179).

Nearly one in five poor American children are disagnosed with asthma, a rate that is 60 percent higher than that of nonpoor children. Learning disabilities occur almost twice as frequently among children in households earning 35000 dollars a year than they do in households earning more than 100000 dollars a year (p179).

And some in the U S congress want to cut food stamps – on which some 23 million American households depend, threatening the poorest children with hunger. These inequalities in outcomes are closely tied to inequalities in opportunities. Inevitably, in countries where children have inadequate nutrition, insufficient access to health care and education, and higher exposure to environmental hazzards, the children of the poor will have far different life prospects from those of the rich (p179).

And partly because in America a child's lifetime prospects are more dependent on his or her parents' income and education than in other advanced countries. The US now has the least equality of opportunity of any advanced country (p180).

At America's most elite universities, for example, only around 9 percent of students come from the bottom half of the population, while 74 percent come from the top quarter (p180). Most societes recognize a moral obligation to help ensure that young people can live up to their potential (p180).

Some countries even impose a constitutional mandate for equality of educational opportunities. But in America, more is spent on education of rich students than on education for the poor. As a result, the US

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is wasting some of its most valuable assets, with so me young people turning to dysfunctional activities (p180). American states like California spend about as much on prisons as on higher education and sometimes more (p180).

Without compensatory measures – including preschool education, ideally beginning at a young age – unequal opportunities translage to unequal lifelong outcomes. That should be a spur to policy action. Indeed, while inequality's harmful effects are wide-reaching and impose huge costs on our economies and socieities, they are largely avoidable (p180).

The extremes of inequality observed in some countries are not the inexorable result of economic forces and laws. The right policies – stronger safety nets, progressive taxation, and better regulation can reverse these devastating trends (p180).

To generate the political will that such reforms require, we must confront policymakers' inertia and inaction with the grim facts of inequality and its devastating effects on our children. We can reduce childhood deprivation and increase equality of opportunity, thereby laying the ground work for a much more just and prosperous future – one that reflects our own avowed values. So why don't we (p180)?

Of the harm that inequality inflicts on o ur economies, politics, and societies, the damage done to children demands special concern. Whatever responsibility poor adults may bear for their lot in life, children't circumstances are thrust upon them without any sort of choice (p181).

Children, perhaps more than anyone else, need the protection that rights afford – the U.S. should be providing the world with a shining example of what that means (p181).

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Ebola and Inequality

The ebola crisis reminded us once again of the downside of globalization. Not only good things cross borders more easily than ever before; but so do malign influences like environmental problems and disease (p182).

The crisis also reminded us of the importance of government and civil society. We do not turn to the private sector to control the spread of a disease like ebola. Rather, we turn to institutions – the Center for Disease Control and Prevention in the United States, the World Health Organization, and Médecins Sans Frontieres, the remarkable group of doctors and nurses who risk their lives to save other in poor countries around the world (p182).

Even right-wing fanatics who want to dismantle government institutions turn to them when facing a crisis like that caused by ebola. Governments may not do a parfect job in addressing such crises, but one of the reasons that they have not done as well as we would hope is that we have underfunded the relevant agencies at the national and global level (p182).

Where the private sector does play an essential role – vaccine development – it has little incentive to devote resources to diseases that afflict the poor or poor countries. It is only when advanced countries are threatened that there is sufficient impetus to invest in vaccines to confront diseases like ebola (p183).

This is not so much a criticism of the private sector; after all, drug companies are not in the business out of the goodness of their hearts, and there is no money in preventing or curing diseases of the poor. Rather, what the Ebola crisis called into question was our reliance on the private sector to do things that governments perform best. It appears that with more public funding, an Ebola vaccine could have been developed years ago (p183).

America's failures in this regard have drawn particular attention – so much so that some African countries are treating visitors from the US with special precautions. But this just echoes a more fundamental problem: America's largely private health care system is failing (p183).

True, at the top end, the US has some of the world's leading hospitals, research universities, and advanced medical centers. But though the US spends more per capita and as a percentage of its GDP on medical care than any other country, its health outcomes are truly disappointing (p183).

American male life expectancy at birth is the worst of 17 high-income countries – almost four years shorter than that in Switzerland, Australia and Japan. And it is the second worst for women, more than five years below life expectancy in Japan (p183).

Other health metrics are equally disappointing, with data indicating poorer health outcomes for Americans throughout their lives. And for at least three decades, matters have been getting worse (p183).

Many factors contribute to America's health lag, with lessons that are relevant for other countries aswell. For starters, access to medicine matters. With the US among the few advanced countries that does not recognise access as a basic human right, and more reliant than others on the private sector, it is no surprise that many Americans do not get the medicines they need (p184).

Almost half of the 50 US states reguse to expand Medicaid, the health financing program for America's poor. The US has one of the highest rates of childhood poverty among advanced countries, and lack of nutrition and healthcare in childhood has lifelong effects (p184).

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Meanwhile, America’s gun laws contribute to the highest incidence of violent deaths among advanced countries, and its dependence on the automobile underpins a high rate of highway fatalities (p184).

America’s outsize inequality is a critical factor in its health lag. With more poverty, more childhood poverty, more people without access to healthcare, decent housing, and education, and more people facing food insecurity, it is no surprise that US health outcomes are bad (p184).

But health outcomes are also worse in the US than elsewhere for those with higher incomes and insurance coverage. Perhaps this is realted to higher inequality than in other advanced countries. Health, we know, is related to stress. Those striving to climb the ladder of success know the consequences of failure (p184).

In the US, the rungs of the ladder are father apart than elsewhere, and the distance from the top to the bottom is greater. That means more anxiety, which translates into poorer health (p184).

Good health is a blessing. But how countries structure their health care system and their society makes a huge difference in terms of outcomes. America and the world pay a high price for excessive reliance on market forces and an insufficient attention to broader values, including equality and social justice (p184).

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America's Socialism for the Rich

With all the talk of "green shoots" of economic recovery, America's banks are pushing back on efforts to regulate them. While politicians talk about their commitment to regulatory reform to prevent a recurrence of the crisis, this is one area whee the devil really is in the details – and the banks will muster what muscle they have left to ensure that they have ample room to continue as they did in the past (p192).

The old system worked well for the bankers, so why should they embrace change? Indeed, the efforts to rescue them devoted so little thought to the kind of post crisis financial system we want that we will end up with a banking system that is less competitive, with the large banks that were too big to fail even larger (p192).

Officials know that if they wait too long, zombie or near-zombie banks are likely to "gamble on resurrection". If they take big bets and win, they walk away with the proceeds; if they fail, the government picks up the tab (p193).

This is not just theory; it is a lesson we learned , at great expense, during the savings-and-loan crisis of the 1980s. When the ATM machine says "insufficient funds" the government doesn't want this to mean that the bank, rather than your account, is out of money (p193).

In a financial restructuring, shareholders typically get wiped out, and bondholders become the new shareholders. Sometimes the government must provide additional funds, sometimes it looks for a new investor to take over the failed bank (p193).

The Obama administration has, however, introduced a new concept: too big to be financially restructured. The administration argues that all hell would break loose if we tried to play by the usual rules with these big banks (p193).

Markets would panic. So, not only can't we touch the bondholders, we can't even touch the shareholders – even if most of the shares' existing value merely reflects a bet on a government bailout. The Obama administration succumbed to political pressure and scaremongering by the big banks (p193).

As a result, the administration has co nfused bailing out bankers and their shareholders with bailing out the banks (p193). Restructuring banks gives a chance for a new start: new potential investors will have more confidence, other banks will be more willing to lend to them, and they will be more willing to lend to others (p193).

But with Obama's strategy, costs are very high – and so far, it has not achieved its limited objective of restarting lending. The taxpayer has had to pony up billions and has provided billions more in guarantees – bills that are likely to come dure in the future (p194).

Rewriting the rules of the market economy is worse than financially costly. Most Americans view it as grossly unjust, especially after they saw the banks divert the billions intended to enable them to revive lending to payments of outsized bonuses and dividends (p194).

Tearing up the social contract is something that should not be done lightly. But this new form of ersatz capitalism, in which losses are socialized and profits are privatized, is doomed to failure. Incentives are distorted. There is no market discipline (p194).

The too-big-to-be-restructured banks know that they can gamble with impunity – and, with the Federal Reserve making funds available at near-zero interest rates, there are ample funds to do so. Some have called this new economic regime "socialism with American characteristics". But socialism is concerned with ordinary individuals (p194).

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By contrast, the United States has provided little help for the millions of Americans who are losing their homes. Workers who lose their jobs receive only 39 weeks of limited unemployment benefits, and are then left on their own. And when they lose their jobs, most lose their health insurance, too (p194).

America has expanded its corporate safety net in unprecedented ways, from commercial banks to investment banks, then to iineurance, and now to automobiles, with no end in sight. In truth, this is not socialism, but an extention of long-standing corporate welfarism (p194).

The rich and powerful turn to the government to help them whenever they can, while needy individuals get little social protection. We need to break up the too-big-to-fail banks; there is no evidence that these behemoths deliver societal benefits that are commensurate with the costs they impose on others (p194).

And if we don’t break them up, then we have to severely ljmit what they do. They can’t be allowed to do what they did in the past – gamble at others’ expenses (p195).

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A Tax System Stacked Against the 99 Percent

Oliver Wendell Holmes said, that taxes are the price we pay for a civilized society. But in recent decades, the burden for paying that price has been distributed in increasingly unfair ways (p196).

About 6 in 10 of us belive that the tax system is unfair – and they're right: put simply, the very rich don't pay their fair share. The richest 400 individual taxpayers, with an average income of more than 200 million dollars, pay less than 20 percent of their income in taxes – far lower than mere millionaires, who pay about 25 percent of their income in taxes, and about the same as those earning a mere $200,000 to $500,000. In 2009, 116 of the top 4000 earners – almost a third – paid les than 15 percent of their income in taxes (p197).

What should shock and outrage us is that the top 1 percent has grown extremely rich, the effective tax rates they have to pay have markedly decreased. Our tax system is much less progressive than it was for much of the 20th century. The top marginal income tax rat e peaked at 94 percent during World War II and remained at 70 percent through the 1960s and 1970s; it is now 39.6 percent (p197).

Tax fairness has gotten worse in the thirty years since the Reagan "revolution" of the 1980s. Citizens for Tax Justice, an organization that advocates for a more progressive tax system, has estimated that, when federal, state and local taxes are taken into account, the top 1 percent paid only slightly more than 20 percent of all American taxes in 2010 (p197).

With such low effective tax rat es it's not a huge surprise that the share of income gong to the top has doubled since 1979, and that the share going to the top 0.1 percent has almost tripled, according to the economist Thomas Piketty (p197).

Most of the Western World has experienced an increase in inequality in recent decades, though not as much as the United States has. But among most economists there is a general understanding that a country with excessive inequality can't function well; many countries have used their tax codes to help "correct" the market's distribution of wealth and income (p198).

The United States hasn't – or at least not very much. The low rates at the top serve to exacerbate and perpetuate inequality – so much so that among the advanced industrial countries, America now has the highest income inequality and the least equality of opportunity (p198).

This is a gross inversion of America's traditional meritocratic ideals – ideals that our leaders, across the spectrum, continue to profess (p198).

Over the years, some of the wealthy have been enormously successful in getting special treatment, shifting an ever greater share of the burdgen of financing the country's expenditures onto others. Ironically, this is especially true of some of our muntinational corporations, which call on the government to negotiate favorable trade treaties that allow them easy entry into foreign markets and to defend their commercial interests around the world (p199).

But then use these foreign bases to avoid paying taxes. General electric has become the symbol for multinational corporations that have their headquarters in the United States but pay almost no taxes. G.E. has not broken any laws but the sparse taxes they've paid violate most American's sense of fairness (p199).

For the rich, hiding their assests has become an elite sport. Many avail themselves of the Cayman Islands or other offshore tax shelters to avoid taxes to the United States. So too, capital gains have to be reported as income only when they are realized (p199).

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And if the assets are passed on to one's children or grandchildren at death, no taxes are ever paid, in a peculiar loophone called the "step-up in cost basis at death". The tax privileges of being rich in America have extended into the afterlife (p199).

As Americans look at some of the special provisions in the tax code it is no wonder that they feel disillusioned with a tax system that is so riddled with special rewards. Most of these tax-code loopholes and giveaways did not materialize from thin air of course – usually, they wre enacted in pursuit of, or at least in response to, campaign contributions from influential donors (p200).

It is estimated that these kinds of special tax provisions amount to some $123 billion a year, and that the price tag for offshore tax loopholes is not far behind. Eliminating these provisions alone, would go a long way toward meeting deficit-reduction targets called for by fiscal conservatives who worry about the size of the public debt (p200).

Yet another s ource of unfairness is the tax treatment on so-called carried interest. Some Wall Street financiers are able to pay taxes at lower capital-gains tax rates on income that comes from managing assets for private equity funds or hedge funds (p200).

But why should managing financial assets be treated any differently from managing people, or making discoveries? Of course, those in finance say they are essential. But so are doctors, lawyers, teachers and everyone else who contributes to making our complex world work (p200).

They say they are necessary for job creation. But in fact, many of the private equity firms that have excelled in exploiting the carried interest loophole are actually job destroyers; they excel in restructuring firms to "save" on labour costs, often by moving jobs abroad (p200).

Economists often eschew the word "fair" – fairness, like beauty is in the eye of the beholder. But the unfairness of the American tax system has gotten so great that it's dishonest to apply any other label to it (p200).

Traditionally, economists have focused less on issues of equality thatn on the more mundane issues of growth and efficiency. But here again, our tax system comes in with low marks. Our growth was higher in the era of high top marginal tax rates than it has been since 1980 (p200).

Economists – even at traditional, conservative international institutions like the International Monetary Fund – have come to realize that excessive inequality is bad for growth and stability. The tax system can play an important role in moderating the degree of inequality. Ours, however, does remarkably little about it (p200).

One of the reasons for our poor economic performance is the large distortion in our economy caused by our tax system. The one thing economists agree on is that incentives matter – if you lower taxes on speculation, say, you will get more speculators (p201).

We've drawn our most talented young people into finanical shenanigans, rather than into creating real businesses, making real discoveries, providing real service to others. More efforts go into "rent seeking" – getting a larger slice of the country's economic pie – than into enlarging the size of the pie (p201).

Research in recent years has linked the tax rates, sluggish growth and rising inequality. The low tax rates at the top were supposed to spur savings and hard work, and thus economic growth. They didn't (p201).

The household savings rate fell to a record level of near zero after President George W. Bush's two rounds of tax cuts, in 2001 and 2003. What low rates at the top did do was increase the return on rent seeking. It flourished, which meant that growth slowed and inequality grew (p201).

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This is a pattern that has now been observed across countries. Contrary to the warnings osf those who want to preserve their privileges, countries that have increased their top tax bracket have not grown more slowly (p201).

Another piece of evidence is here at home: if the efforts at the top were resulting in our entire economic engine's doing better, we would expect everyone to benefit. If they are engaged in rent seeking, as their incomes increased, we'd expect that of others to decrease (p201).

And that's exactly what's been happening. Incomes in the middle and even the bottom have been stagnating or falling (p201).

Aside from the evidence, there is a strong intuitive case to be made for the idea that tax rates have encouraged rent seeking at the expense of wealth creation. There is an intrinsic satisfaction in creating a new business, in expanding the horizons of our knowledge, and in helping others (p201).

By contrast, it is unpleasant to spend one's days fine-tuning dishonest and deceptive practices that siphon off money from the poor. A vast majority of Americans would, all things being equal, choose the former over the latter (p201).

But our tax system tilts the field. In increases the net returns from engaging in some of these distasteful activities and it has helped us become a rent-seeking society. We could have a tax system that encourages good things like hard work and thrift and discourages bad things like rent seeking, gambling, financial speculation and pollution (p202).

Such a tax system could raise far more money than the current one – we wouldn't have to go through all the wrangling we've been going, fiscal cliffs, and threats to end Medicate and social security. We would be in a sound fiscal position, for at least the next quarter-century (p202).

The consequences of our broken tax system are not just economic. Our tax system relies heavily on voluntary compliance. But if citizens believe that the tax system is unfair, theis voluntary compliance will not be forthcoming (p202).

More broadly, government plays an important role not just in social protection, but in making investments in infrastructure, technology, education and health. Without such investments, our economy will be weaker, and our economic growth slower (p202).

Society can't function well without a minimal sense of national solidarity and cohesion, and that sense of shared purpose also rests on a fair tax system. If Americans believe that government is unfair – that ours is a government of the 1 percent, for the 1 percent, and by the 1 percent – then faith in our democracy will surely perish (p202).

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Globalization Isn't Just About Profits. It's about Taxes too.

The world looked on agog as Tim Cook, the head of Apple, said his company had paid all the taxes owed – seeming to say that it paid all the taxes it should have paid. There is a big difference between the two. It's no surprise that a company with the resources and ingenuity of Apple would do what it could to avoid paying as much tax as it could within the law (p203).

While the Supreme Court, in its Citizens United case, seems to have said that corporations are people, with all t he rights attended thereto, this legal fiction didn't endow corporations with a sense of moral responsibility. To be everywhere when it comes to selling their products, and nowhere when it comes to reporting profits derived from those sales (p203).

Apple, like Google, has benefited enormously from what the US and other western governments provide: highly educated workers trained at universities that are supported directly by government. The basic research on which their products rest was paid for by taxpayer-supported developments – the Internet, without which they couldn't exist (p203).

Their prosperity depends in part on our legal system - including strong enforcement of intellectual property rights; they asked, and got, government to force countries around the world to adopt our standards, in some cases, at great cost to the lives and development of those in emerging markets and developing countries (p204).

The brought genius and organizational skills for which they justly receive kudos. But while Newton was at least modest enough to note that he stood on the shoulders of giants, these titans of industry have no compunction about being free riders, taking generiously from the benefits afforded by out system, but not willing to contribute commensureately (p204).

Without public support, the wellspring from which future innovation and growth will come will dry up. It is time the international community faced the reality: we have an unmanageable, unfair, distortionary global tax regime (p204).

It is a tax system that is pivotal in creating the increasing inequality that marks most advanced countries today – with America standing out in the forefront and the UK not far behind. It is the starving of the public sector which has been pivotal in America no longer being the land of opportunity – with a child's life prospects more dependent on the income and education of its parents than in other advanced countries (p204).

Globalization has made us increasingly interdependent. These international corporations are the big beneficiaries of globalization. Our multinationals have learned to exploit globalization in every sense of the term – including exploiting tax loopholes that allow them to evade their global social responsiblities (p205).

The U.S. by itself could go a long way to moving reform along: any firm selling goods could be obliged to pay a tax on its global profits, at say a rate of 30 percent, based on a consolidated balance sheet. The U.S. would set itself up as enforcing a global minimum-tax regime. Some might opt out of selling in the U.S. but it is doubtful (p206).

To say that Apple or Google simply took advantage of the current system is to let them off the hook to easily: the system didn't just come into being on its own. It was shaped from the start by lobbyists from large multinationals (p206).

Companies like General Electric lobbied for, and got, provisions that enabled them to avoid even more taxes. They lobbied for, and got, amnesty provisions that allowed them to bring their money back to the U.S. at a special low rate (p206).

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They t hen figured out how to comply with the letter of the law, while avoiding the spirit and intention. If Apple and Google stand for the opportunities afforded by globalization, their attitudes towards tax avoidance have made them emblemeatic of what can go and is going, wrong with that system (p206).

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Fallacies of Romney's Logic

Mitt Romeny's acerbic attack against the 47 percent of Americans who allegedly don't pay income taxes and are dependent on government has rightly given rise to a storm. It suggests that large numbers are freeloaders (p207).

The irony is that it is people such as Romney who are freeloading: the taxes that he has said he is paying are far less, as a percentage of income, than those of people with substatially less income. And contrary to what some of them would like to believe, no one makes it on his own (p207).

Even if they don't inherit their wealth, success in business requires a rule of law, an educated workforce, a public infrastructure, all of which are provided by government. Even innovators such as Google have done what they did only by building on the work of others (p207).

Before Google could create the Internet's most popular search engine, someone had to create the Internet – and it was government that did that. But the fallacies of Romeny's logic run deeper. First, even those who don't pay income taxes pay a host of other taxes including payroll, sales, excise and property taxes (p208).

Many of those receiving "benefits" paid for them – through social security and Medicare contributions. They're not free riders. Government has done a better job of providing these benefits than the private sector (p208).

Let's remember why these programs were started. The private sector left most elderly bereft of support, the market for annuities essentially didn't exist, and the elderly couldn't afford health insurance (p208).

Even today, the private sector doesn't provide the kind of security that social security provides – including protection against market volatility and inflation. And transaction costs of the social security administration are markedly lower than those in the private sector – not a surprise, since their objective is to maximize these costs. Transaction costs are their profits (p208).

Second, many of those receiving benefits are our young – providing them with education and healthcare are investments in our future. America is the country with the least equality of opportunity of any of the advanced countries for which there is data (p208).

While the American dream may have become a myth, it doesn't have to be that way. Children shouldn't have to depend on the wealth of their parents to get the education or health care they need to live up to their potential (p208).

Third, an efficient system of social protection is an important part of any modern society – necessary to enable individuals to take risks. Again, the market failed to provide adequate insurance, for instance, for unemployment or disability (p208).

That's why the government stepped in. Those receiving those benefits typically paid for them, either directly or indirectly, through contributions they or their employer made on their behalf to these insurance funds (p208).

But providing social protection against these rirks too can make for a more productive society. Individuals can take on more high-return, high-risk activities if they know there is as safety net protecting them if things don't work out (p209).

It's one of the reasons that some economies with better social protection have been growing much more rapidly than the United States, even during the recent recession. Fourth, many of those at the bottom – who have become so dependent on government – are there partly because government has failed in one way or another (p209).

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It has failed to provide them with skills that would make them productive, so they could earn an adequate living. It has failed to stp banks from taking advantage of them through predatory lending and abusive credit card practices (p209).

It has failed to stop for-profit schools from taking advantage of their aspirations to move up in the world through education. Finally, we are a community – and all communities help those who are less fortunate among them (p209).

If our ecomonic system results in so many without jobs, dependent on the government for food, then government has to step in. Our economic system has not worked in the way it should: It has not created jobs for all those who would like to work. Many of the jobs that have been created do not pay a livable wage (p209).

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The Wrong Lesson From Detroit's Bankruptcy

The distressing facts about Detroit are by now almost a cliché: 40 percent of streetlights are not working, tens of thousands of buildings are abandoned, schools have closed, and the population declined by 25 percent in the past decade alone (p216).

The violent crime rate last year was the highest of any big city. In 1950, when Detroit's population was 1.85 million, there were 296,000 manufacturing jobs in the city; as of 2011, with a population of just over 700,000, there are few than 27,000 (p217).

Failures of national and local policy are by now well known: underinvestment in infrastructure and public services, geographic isolation that has marginalized poor and African-American communities in the Rust Belt, intergenerational poverty that has stymied equality of opporttunity and privileging moneyed interests over those of workers (p217).

Detroit's travails arise in part from a distinctive aspect of America's divided eco nomy and society. The country is becoming vastly more economically segregated, which can be even more pernicious than being racially segregated (p217).

Detroit is the example of the seclusion of affluent elites in suburban enclaves. There is a rationale for battering down the hatches: the rich thus ensure that they don't have to pay any share of the local public goods and services of their less well-off neighbours, and that their children don't have to mix with those of lower socioeconomic status (p218).

The trend toward self-reinforcing inequality is especially apparent in education, an ever shrinking ladder for upward mobility. Schools in poorer districs get worse, parents with means move out to richer districts, and the divisions between the haves and have nots grow even larger (p218).

Residential segregation along economic lines amplifies inequality for adults, too. The poor have to somehow manage to get from their neighbourhoods to part-time, low-paying, and increasingly scarce jobs at distant work sites (p218).

Combine this urban sprawl with inadequate public transportation systems and you have a blueprint for transforming working-class communities into depopulated ghettos (p218).

The poor are not only geographically isolated, but politically ghettoized aswell. The result is a separate, poorer inner city with a dearth of resources, made even worse because industural plants that provided the core of the tax base are shut down (p218).

Disintegration of Detroit precedes the conflicts over social-welfare programs and race relations and reaches back into the postwar decades, a time when the roots of deindustrialization, racial discrimination, and geogrphic isolation were planted (p219).

Lacking regional poltitical unity, there is no overall structure to improve the infrastructure and public services between poorer inner cities and affluent suburbs. So the poor fall back on what means they have, which is not good enough (p219).

Cars inevitably break down and buses are late, making workers appear to be "unreliable". But what is really unreliable is the design of the city. No wonder America is becoming the advanced industrial country with the least equality of opportunity (p219).

The same skewed priorities that have gutted Detroit at the local level are echoed at the level of national policy. Every country, every society, has regions and industries whose stars are rising, and others that are in decline (p219).

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Silicon Valley has, for some time, been America's rising star. With technological change and globalization though, the Midwest's compartive advantage as a global manufacturing hub has ebbed,. Markets, however, often don't do a good job of self-rejuvenation (p219).

Rather than deal purposefully with this changing economic landscape with useful policies encouraging the growth of other industries, our government spent decades papering over the growing weaknessess by allowing the financial sector to run amok, creating "growth" based on bubbles (p219).

We didn't just let the market run its course. We made an active choice to embrace short-term profits and large-scale inefficiency. America has an urban renewal program, but it is aimed more at restoring buildings and gentrification than at maintaining and restoring communities (p220).

American workers were sold "free" trade policies on the promise that the winners could compensate the losers. The losers are still waiting. Of course, the Great Recession and the policies that crated it have made things much worse (p220).

The mortgage bankers marched into large sections of some of our cities and found them good subjects for their predatory and discrimminatory lending. Once the bubble burst, those cities were abandoned by all but the debt collectors and foreclosure sheriffs (p220).

Rather than saving our communities, politicians focused more on saving the bankers, their shareholders, and their bondholders. The situation may be grim, but all is not lost for Detroit and other cities facing similar problems. The question facing detroit now is how to manage bankruptcy (p220).

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In No One We Trust

In America today, we are sometimes made to feel that it is naïve to be preoccupied with trust. Our songs advise against it, our TV shows t ell stories showing its futility, and incessant reports of financial scandal remind us we'd be fools to give it to our bankers (p223).

The last point may be true, but that doesn't mean we should stop striving for a bit more trust in our society and our economy. Trust is what makes contracts, plans and everyday transactions possible, it facilitates the democratic process from voting to law creation, and is necessary for social stability (p223).

It is trust more than money, that makes the world go round. Unfortunately, however, trust is becoming yet another casualty of our country's staggering inequality. As the gap between Americans widens, the bonds that hold society together weaken (p223).

As more and more people lose faith in a system that seems inexorably stacked against them, and the 1 percent ascend to ever more distant heights, this vital element of our institutions and our way of life is eroding (p224).

The undervaluing of trust has its roots in or most popular economic traditions. Adam Smith argued forcefully that we would do better to trust in the pursuit of self-interest than in the good intentions of those who pursue the general interest (p224).

If everyone looked out for just himself, we would reach an equilibrium that was not only comfortable but also productive. To the morally uninspired, it's an appealing idea: selfishness as the ultimate form of selflessness (p224).

But events and economic research over the past 30 years have shown not only that we cannot rely on self-interest, but also that no economy, not even a modern, market based economy can function will without a modicum of trust – and that unmitigated selfishness inevitably diminishes trust (p224).

The banking industry had long been based on trust. You put your money into the bank, trusting that when you wanted to take it out in the future, it would be there. A vast majority of the business of banks was conducted on the basis of assumed mutual accountability, and a sense of responsibility (p224).

At their best, banks were stalwart community institutions that made judicious loans to promising small businesses and prospective homeowners. In the years leading up to the crisis though, oiur traditional bankers changed drastically, aggressively branching o ut into other activities, including those historically associated with investment banking (p224).

Commercial lenders hard-sold mortgages to families who couldn't afford them, using false assurances. They could comfort themselves with the idea that no matter how much they exploited their customers and how much risk they had undertaken, new "insurance" products – derivatives and other chicanery – insulated their banks from the consequences (p225).

If any of them thought about the social implications of their activities, whether it was predatory lending, abusive credit card practices, or market manipulation, they might have taken comfort that, in accordance with Adam Smith's dictum, their swelling bank accounts implied that they must be boosting social welfare (p225).

We now know that this was all a mirage. Things didn't turn out well for our economy and society. As millions lost their homes during and after the crisis, median wealth declined nearly 40 percent in three years. Banks would have done badly too had it not been for the Bush-Obama mega-bailouts (p225).

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The cascade of trust destruction was unrelenting. One of the reaons that the bubble's bursting in 2007 lead to such an enormous crisis was that no bank could trust another. Each bank knew the shenanigans it had engaged in and so knew that it could not trust any other bank (p225).

Interbank lending froze, and the financial system came to the verge of collapse, saved only by the resolute action of the public, whose trust had been most abused of all. There had been earlier episodes when the financial sector showed how fragile trust was (p225).

Most notable was the crash of 1929, which prompted new laws to stop the worst abuses, from fraud to market manipulation. We trusted regulators to enforce the law, and we trusted banks to obey the law. The government couldn't be everywhere, but the banks would at least be kept in line by fearing the consequences of bad behavour (p225).

Decades later, however, bankers used their political influence to eviscerate regulations and install regulators who didn't believe in them. Officials and academics assured lawmakers and the public that banks could self-regulate (p225).

But it all turned out to be a scam. We had created a system of rewards that encouraged shortsighted behaviour and excessive risk-taking. In fact, we had entered an era in which moral values were given short shrift and trust itself was discounted (p226).

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