BEFORE AND AFTER CRISIS:
WALL STREET LIVES ON

DOUG HENWOOD

My assignment for this volume was to write about Wall Street before and after The Crisis. My first thought was, that’s easy. Before The Crisis, Wall Street was the most powerful economic, political, and social force in the US. After The Crisis, Wall Street is the most powerful economic, political, and social force in the US. Ok, next essay.

Actually I must confess to being a little surprised at this outcome. I’ve never been one to believe – and I do mean believe, in the sense that it’s often a faith for which supportive arguments are mobilized after the fact rather than a logical conclusion following an evaluation of the evidence – in the fragility of the capitalist order or the tenuousness of US imperial power. The left is full of crisis mongers who’ve seen one coming every day for the last thirty years. But I did think that Wall Street was, to turn its own jargon back on itself, in for a bit of a haircut after the financial crisis and the ensuing recession. I’d assumed that its power, prestige, income, and freedom to manoeuvre would be scaled back, if not to the levels of the early 1950s, at least to something less than the lordly dominance it’s enjoyed since the bull market in stocks took off on the afternoon of August 12, 1982.

But that seems not to have happened. Wall Street has used the crisis, if not to enhance its power at least to demonstrate it. Also striking, though a bit off-topic, was the inability of all the death-agony Marxists who’d been waiting for something like this since 1929 to make any political hay with it.

There are several dimensions to Wall Street’s rise to pre-eminence over the last few decades. One can simply be measured in money. For example, in almost every year since the US national income accounts begin in 1929, securities and commodities brokers have been the highest-paid of the almost 90 industries reported by the Bureau of Economic Analysis.¹ The only exceptions were in the late 1940s and early 1950s, when they were beaten by their industrial cousins in holding companies and investment offices. But
the securities industry’s premium has grown enormously over time. From 1929 through 1939, it was 237 per cent of average pay. It fell during the Second World War and the immediate postwar decades, at just under 180 per cent of average pay. But with the takeoff of the bull market in 1982, the premium began to swell, crossing 300 per cent in 1992 and 400 per cent in 2006. It fell back some in 2008, to a mere 409 per cent. It fell further in 2009, to 366 per cent, which may look like a substantial decline, but is still higher than any year before 2004. These numbers refer to the royalty of the financial sector, of course, but the story for the sector as a whole is very similar, if less dramatic.

Or take profits. As the bull market was about to take off in 1982, the financial sector claimed 12 per cent of pretax profits in 1982; that nearly tripled to 34 per cent at the 2008 peak. It fell by more than half in the heat of the crisis, to 15 per cent at the end of 2008 – but as of the beginning of 2010, it was back up to 34 per cent.

Or take the proliferation of assets. Financial assets of all kinds – not just debt, but equities and everything else the Federal Reserve counts in its flow of funds accounts – were equal to 462 per cent of GDP in 1982. That measure rose steadily for the next 25 years, more than doubling to a peak of 1,058 per cent of GDP in 2007. The ratio came down a bit with the early stages of the financial crisis, but bottomed in the first quarter of 2009 and has risen ever since. It is substantially higher than in 2006, what seems like near the peak moment of the bubble.

So here’s the story the numbers tell us: whereas from the 1930s through the 1950s, Wall Street was something of a not very visible back office for capitalism (whose denizens lived well, but not large), since the 1980s especially, they’ve accumulated an enormous amount of wealth, and with it, more and more power and prestige. I will address below what led to this, but here are some personal anecdotes to support the numbers. Until the 1980s, a few people would migrate from Yale to the financial sector on graduation – I did, actually, but it was a brief, low-paying diversion – but it was hardly a flood. Only one of my undergraduate friends came out of a Wall Street family; they lived well, but not all that differently from everyone else. They had a house in the Hamptons, but it had been passed down through the family. The patriarch who first bought it went bankrupt in the Great Depression and moved out there as a low-cost refuge. Now, there’s no data on that house, but the neighbouring property is valued by Zillow.com at $22 million.

As Kingman Brewster, Yale’s genteel upper-crust president in the early 1970s put it in my freshman facebook (back when that was a document on
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paper), the days when people rolled like bowling balls from Wall Street in New Haven to Wall Street in New York were past. ‘Enjoy the privilege of doubt’, he further counselled us. The year before, in 1970, Brewster, who could count two passengers on the *Mayflower* among his ancestors, had said: ‘I am appalled and ashamed that things should have come to such a pass in this country that I am sceptical of the ability of black revolutionaries to achieve a fair trial anywhere in the United States’. It is impossible to imagine the president of Yale saying anything like that today. Nor is it possible to imagine any Yale president cutting back on the number of ‘legacies’ – undergraduates admitted largely because their parents went to Yale and gave it lots of money – as Brewster did. The US bourgeoisie has changed substantially in the last 40 years.

When Brewster encouraged incoming students to doubt, Yale’s endowment was worth less than $500 million. Just fourteen years later, Yalies were indeed rolling like bowling balls from one Wall Street to the other: one-third of Yale’s graduating class applied for a job at First Boston – not much doubt there.

SO WHAT EXACTLY DOES WALL STREET DO?

Let’s be generous and concede that it does provide some financing for investment. But an enormous apparatus of trading has grown up around it – not merely trading in certificates, but in control over entire corporations. I think it’s less fruitful to think of Wall Street as a financial intermediary than it is to think of it as an instrument for the establishment and exercise of class power. It’s the means by which an owning class forms itself, particularly the stock market. It allows the bourgeoisie to own pieces of the productive assets of an entire economy. So, while at first glance the tangential relation of Wall Street, especially the stock market, to financing real investment might make the sector seem ripe for tight regulation and heavy taxation, its centrality to the formation of ruling-class power makes it a very difficult target.

On the whole, the financial sector has surprisingly little to do with raising money to finance real corporate investment. It rarely has. That’s especially true of the stock market. Even in the boomiest moments of the late 1990s dot.com bubble, IPOs financed only a small fraction of corporate investment – about 5-6 per cent – and initial offerings were far outweighed by stock buybacks. Between 1995 and 2000, corporate stock buybacks were 3.5 times as large as IPOs.

Or, looked at another way, if you combine net equity offerings (which, given the heavy schedule of buybacks over the last quarter century, have been negative most of the time since 1982), takeovers (which involve
the distribution of corporate cash to shareholders of the target firm), and traditional dividends into a concept I call transfers to shareholders, you see that corporations have been shovelling cash into Wall Street’s pockets at a furious pace. Back in the 1950s and 1960s, nonfinancial corporations distributed about 20 per cent of their internal funds (profits plus depreciation allowances) to shareholders. In the 1970s, that fell to 15 per cent, which helped create the sour mood on Wall Street in that decade. (That’s the decade average. It fell below 8 per cent in 1976.) After 1982, though, the shareholders’ share rose steadily. It came close to 100 per cent in 1998, fell back to a mere 25 per cent in 2002, and then soared to 126 per cent in 2007. That means that corporations were actually borrowing to fund these transfers to shareholders. This fell during the crisis, bottoming at 21 per cent in mid-2009, but as of the beginning of 2010 it had recovered to 47 per cent.

Businesses do get outside financing, but the most important source of that is old-style banks, with so-called commercial and industrial (C&I) loans. C&I loans began contracting in nominal terms at the end of 2008, and fell an average annual rate of 21 per cent in the first five months of 2010.

For a long while, shareholder ownership was more notional than active. After the 1929 crash, Wall Street sort of receded into the background, giving us the Golden Age of Galbraith’s managerial capitalism. But when economic performance faltered in the 1970s, when the Golden Age was replaced by Bronze Age of rising inflation and falling profits, Wall Street, meaning shareholders, finally asserted itself. They unleashed what has been dubbed the shareholder revolution, demanding not only higher profits but a larger share of them. The first means by which they exercised this control was through the takeover and leveraged buyout movements of the 1980s. By loading up companies with debt, they forced managers to cut costs radically and ship larger shares of the corporate surplus to outside investors rather than investing in the business or hiring workers. This cost-cutting mania helped drive the outsourcing movement.

The 1980s debt mania came to a bad end, as highly leveraged companies found themselves unable to cope with the early 1990s recession. So the shareholder revolution recast itself as a movement of activist pension funds, led by the California Public Employees Retirement System (CalPERS). The funds lobbied management, drew up hit lists of badly run companies, and generally pushed the idea that firms should be run for their shareholders. It had some successes. Compensation structures were rejiggered to emphasize stock over direct salaries; the idea was to get managers to think and act like shareholders, since they were materially that under the new regime.

But pension fund activism sort of petered out as the decade wore on.
Managers still ran companies with the stock price in mind, but the limits to shareholder influence have become very clear since the financial crisis began. Managers have been paying themselves enormously while stock prices languished. If the stock price wasn’t cooperating, well, options could always be back-dated. The problem was especially acute in the financial sector: Bank of America, for example, bought Merrill Lynch because its former CEO, Ken Lewis, coveted the firm, and if the shareholders had any objections, he could just lie to them about how sick the brokerage firm was. It was as if the shareholder revolution hardly happened, at least in this sense.

THE FINANCIAL REVOLUTIONARY

It is worth a closer look at the financial revolution that began in the 1980s. To concentrate the inquiry, one could do little better than study the intellectual evolution of one of its prime theorists, Harvard Business School professor Michael Jensen.

To set the scene, the financial world of the 1970s was, from an elite point of view, a nightmarish thing. Economic growth was weak, labour productivity was sagging badly, and the stock and bond markets were disaster areas. So was real wage growth, but that’s not the kind of thing that bourgeois pundits worry about. They did worry about the fact that stocks, as measured by the S&P 500 index, lost almost 3 per cent of their real value in the 1970s. A portfolio of long-term Treasury bonds lost 32 per cent of their value. Corporate profitability, which was 7.6 per cent in 1969, fell by half to 3.8 per cent in 1980. This was nothing less than a social emergency. Deregulation, by stimulating competition and disciplining workers, would, it was assumed, turn this mess around.

Along with those transformations in the political realm came major transformations in the relationship between stockholders and management, between Wall Street and the Fortune 500. After the crash of 1929, Wall Street was in deep disrepute, and shareholders were mostly passive creatures who quietly collected their dividends and hoped for the best. The post-Second World War boom was kind to them, and rewarded their passivity; managers ran firms with little outside interference. As economic and financial performance deteriorated in the 1970s, Wall Street and the people who are paid to think for the owning class began scheming.

Prominent among the schemers was Michael Jensen, who developed a finance-based theory of corporate governance that would become exceedingly influential in the 1980s. As I put it in my book Wall Street: ‘Though it took some time to evolve to full ripeness, Jensen’s argument is,
in a phrase, that stockholders can’t trust the managers they’ve hired to run their corporations, and a radical re-alignment is in order.  

Starting with a 1976 paper co-written with William Meckling, Jensen began what would amount to a fifteen-year rethink of the modern corporate form. In the first paper of the series, Jensen and Meckling wonder why it is that shareholders entrust the companies they own to a bunch of managers they don’t know, a slate of people with their own interests and agenda. Managers would prefer a comfortable, well-compensated life without a bunch of shareholders breathing down their neck. It would be much more pleasant to buy a corporate jet than pass the cash along to shareholders. Or it might be ego-gratifying for a CEO and his inner circle to expand aggressively even if the effort isn’t likely to be all that profitable. Shareholders, who should come first, often came last. But having identified the problem, Jensen and Meckling really didn’t have much of a solution, though they did suggest that managers be required to hold both the stock and the debt of their firms so they weren’t tempted to screw either class of outside financial interests.

A few years later, though, Jensen thought he’d found the magic bullet: the leveraged buyout (LBO). Firms, especially older ones in mature industries that generate more cash flow than they can profitably reinvest, should join with an investment boutique like Kohlberg Kravis Roberts (they were the stars of the 1980s – today’s counterpart would be a group like Blackstone), borrow gobs of money from institutional investors, and take their public firms private. The large debt load would assure that outside investors got plenty of cash, and assure that managers, facing huge interest bills, wouldn’t waste money on perks or bad investments. Managers would be paid mostly in stock options rather than cash, which would inspire them to great feats of creativity and make them think like stockholders and not high-end welfare queens. After an appropriate course of slimming – meaning reduced investment, layoffs, outsourcing, speedup – firms would go public again, lean, mean, and massively efficient. Managers’ options would turn wonderfully profitable.

Things didn’t work out as planned. Though a few early deals went well, at least for investors, as the 1980s progressed, the deals got more bloated and inappropriate, and the increase in indebtedness drove a lot of firms to the wall with the advent of the early 1990s recession: there just wasn’t enough cash to cover the interest bill and keep the doors open.

Despite the institutional evolution from the standard public corporation to the LBO’d firm, Jensen always held shareholder rights to be sacrosanct. Why the shareholder, and not workers, customers, or society, should be the ultimate constituency of the corporation is something Jensen never addressed.
He did, however, direct considerable vitriol at those nonshareholder interests in response to a critique of his work – the enemies of economic progress were ‘striking Eastern Air Lines pilots, Pittston Coal miners, [and] New York Telephone employees, who seem perfectly content to destroy or damage their employer’s organization while attempting to serve their own interests. Ralph Nader’s consumer activist organization is another example’.

A few years later, Jensen came around to celebrating failure, though failure of a certain kind: if firms can’t make it, they should go. If they’re too big, they should shrink. If they’re too weak to go it alone, they should merge.

This is in some sense a development of his earlier themes, but with far more emphasis on managing the exit of capital from dying sectors or enterprises than on the revival of sagging ones.

Jensen was rather quiet during the late 1990s, but after the corporate scandals of the early 2000s, like Enron and WorldCom, he began thinking publicly again about the complexities of running large joint-stock companies. While still holding to the centrality of the stock market, he did allow that managers paid in equity had an interest in manipulating the books to get and keep the stock price up. But, on the other hand, responsible managers had a duty to ‘just say no’ to Wall Street’s pressure for quick profits; their real duty should be to maximize a firm’s market value over the long term. How, or why, managers should say ‘no’ to their alleged overseers, isn’t clearly revealed.

In the wake of WorldCom and the rest, Jensen also discovered that there were costs to ‘overvalued equity’. Managers and boards would do anything, even committing crimes, to maintain an inflated stock price. (Jensen meant accounting crimes, of course. Interestingly, one of the sponsors of his 2004 work was BP, a firm that would later become famous for committing crimes far more serious than cooking the books.) Jensen professed to be mystified as to why short-sellers couldn’t cure the problem of overvaluation – surely these profit-seeking sharks could find overvalued firms and sell their stock aggressively in the hope of making money on their collapse. Since the shorts couldn’t do it, and managers have no interest in doing it, the task of managing down an inflated stock price falls to the board of directors – who should think about talking openly to the short-selling community to get the job done. Why boards should do this is another undisclosed detail of Jensen’s argument – or, for that matter, how a group that meets about one day a month can know what’s going on inside the corporation they’re supposed to run. Perhaps aware of the tightness of the corner he’s painted himself into, Jensen is reduced to an almost prayerful demand: ‘We must stop creating and consuming the heroin’, the heroin being all the gaming that surrounds an
overvalued stock price.

Given Jensen’s history, the notion of an overvalued stock price is rather strange: thirty years earlier, he declared the efficient market hypothesis (EMH) the best-established principle in the social sciences. If the EMH were true, sustained overvaluation would be impossible, since wise market players would see through accounting tricks and pummel the inflated shares back to earth. To followers of the EMH, the stock market was the best real-time grading system for corporate performance that could be imagined. Add that to the faith in the paramount position of the stockholder in the economic hierarchy and you have a perfect theoretical rationale for the financialized capitalism that has evolved over the last three decades. Of course, the slump of the early 1990s was proof that Jensen’s prescription of heavy debt loads was a potentially fatal one, and the slump of the early 2000s was proof that loading up managers with stock also had its problems. And the bust of the late 2000s is proof that the whole strategy of financialization hasn’t worked out as planned.

I recently emailed Jensen for his thoughts on recent financial history, since he’s published nothing since 2006. The response of one of the prime intellectual architects of financial and corporate policy over the last few decades had nothing to say: ‘I have not been working directly on the financial crisis since I have been devoting my time to leadership, integrity and a value-free approach to values. My time is totally committed to these matters and I do not have the time or interest in discussing the crisis’.

A value-free approach to values, which presumably means more than shareholder value. Being hegemonic means never having to say you’re sorry.

RESTRUCTURING US CAPITALISM

Of course, to review this history isn’t to suggest that Jensen was personally responsible for the course of the last three decades; not even an esteemed professor at the Harvard Business School is that powerful. There were many other personalities and impersonal forces that shaped it. But it should serve to remind us that the crash of 2008 had a long pedigree.

And Jensen was dealing throughout, if not productively, with some real problems. Who should own and run a capitalist enterprise and how? What is the role of non-owners, if any? How do all the various actors keep each other in check in a system that reveres and unleashes self-interest? What to do with companies, sectors, and regions that have fallen on hard times?

Rather than being purely parasitical – which it often is – Wall Street was also at the centre of the restructuring of US capitalism since the early 1980s.
You could even date the origin of Wall Street’s top-down revolution to the New York City fiscal crisis of 1975, when a cadre of bankers essentially took over city government and began the long campaign of austerity for the poor and subsidized gentrification that has characterized urban policy ever since. All the financial machinations theorized by Jensen helped lubricate the aggressive restructuring of US industry and labour relations since the early 1980s – decreased job security, disappearing benefits, outsourcing, the whole familiar package. These transformations do a lot to explain the 90 per cent rise in productivity between 1982 and 2010, nearly three times the increase in real compensation, 34 per cent. No wonder profitability rose so dramatically.

Of course, a system based on high levels of mass consumption – both to sustain aggregate demand and perform political legitimation – had to do something to compensate for the squeeze on mass purchasing power that delivered the increase in profitability and the rise in elite incomes. (A measure of the latter: average real incomes of the bottom 90 per cent rose 13 per cent between 1982 and 2007 – that’s a cumulative total, not an annual average – compared with 407 per cent for the richest 0.01 per cent.13)

Wall Street was very helpful in squaring that circle by providing truly heroic doses of credit to US households. With so much money accumulating at the top in need of profitable outlet, and so much need accumulating below, the financial sector was there to mediate. Between the first quarter of 1983 and the peak in the second of 2008, residential mortgage debt increased by $9.6 trillion, and consumer credit by another $2.2 trillion. That brought total household debt from 65 per cent of after-tax income to 134 per cent. Debt, measured both in nominal dollars and relative to income, fell in the two years after the bubble burst, but remains extraordinarily high. Right now, it doesn’t look like the debt creation machinery can be fired up to anything like its former pace – but how will the circle remain squared? The only option for capital might be a massive austerity plan for the working class – wage cuts, tighter credit, and lower levels of consumption – but will that be economically or politically sustainable? Few people in US public life are asking this question.

Certainly not anyone on Wall Street, where it looks like the good old days are back (for Wall Street, that is), with profits surging and bonus packets bursting at the seams. How have they done that? Not by financing an economic recovery, that’s for sure. Commercial and industrial lending, as was pointed out earlier, has been contracting hard. Overall, borrowing and lending have contracted markedly. The swing in credit flows is truly remarkable. At the peak of the bubble in the third quarter of 2007, there was
$5.4 trillion in new borrowing and lending throughout the US economy. In the last quarter of 2009, that had contracted to -$841 billion (the negative number meaning that more old debt was paid off or written off than new loans were extended). But almost all the borrowing was by the US government, and almost all new lending by the Federal Reserve. Outside those two public entities, new borrowing and lending was close to -$2 trillion (again, meaning more old debt disappeared than new debt was created).

The residential mortgage sector is entirely a ward of the state now; almost all new mortgage lending as of early 2010, what little there was, was underwritten by Washington. So with so little normal financial activity going on, how is Wall Street making money? In part by underwriting its own rescue – many big banks have been floating stock and bond issues to rebuild their capital base, and the investment banks have been taking their usual cut. And they’ve been trading for their own accounts and that of their customers. Not all that long ago it seemed like the hedge fund industry, if not exactly a goner, was going to be on a radical weight reduction regime. No longer. Though some funds blew up, the survivors look to be doing quite well for themselves.

Wall Street demonstrated its immense political power during this crisis. In July 2010, after enormous amounts of dickering, Congress passed and the president signed a bill, now nicknamed Dodd-Frank, creating a new regulatory architecture. While Dodd-Frank will change the way Wall Street does business to some extent, bankers headed off the biggest threats, and security analysts estimate that the hit to profits will be less than 10 per cent. Banks will be required to boost their capital – though this is part of an international effort through the Basel Committee, coordinated through the Bank for International Settlements. Banks will be forced to stop trading on their own account (the so-called Volcker Rule, named after former Federal Reserve chair Paul Volcker), and will also be required to spin off part of their derivatives business into separately capitalized subsidiaries. But regulators will have to devise specific rules based on the legislation, an activity in which bank lobbyists will no doubt figure prominently. And the rules won’t go into full effect for four to five years. The hodge-podge of regulators – the Fed, the Securities and Exchange Commission, the Commodity Futures Trading Commission, the Comptroller of the Currency, just to name a few – will be left largely intact, though they will be encouraged to consult more closely. That is less than Bush’s Treasury Secretary Henry Paulson wanted to do: in a Treasury paper issued late in his term, Paulson proposed creating a single overarching regulatory authority. Insurance will still be regulated at the state, and not the federal, level.
Regulators will be given the power to wind down large, system-threatening institutions before they go under instead of during or after their failure. But a $19 billion levy on the banks to prepay the costs of such resolutions was dropped – the same day that the House killed an effort to extend unemployment benefits, amidst the worst outbreak of long-term unemployment since the 1930s. Dropped as well was Obama’s original proposal for an independent and powerful consumer financial protection agency; instead, a new body will be created inside the Fed, an institution not previously known for its attentiveness in protecting consumers from hungry bankers.¹⁷

Soon after the House passed the bill, Treasury Secretary Timothy Geithner went on Lawrence Kudlow’s TV show to correct the perception, common in the so-called business community, that the administration is anti-business.¹⁸ The choice of outlet is interesting: Kudlow, a former Reagan administration budget official, is a militant supply sider and all-around right-winger with a one-dimensional worldview. Geithner appealed to that dimensional singularity by assuring Kudlow and his CNBC audience that the administration plans to keep a lid on the favourable tax treatment of capital gains and dividends, and emphasizing that ‘this president understands deeply that governments don’t create jobs, businesses create jobs’. The administration has a ‘pro-growth agenda’, which is a phrase that Kudlow loves to use himself. But despite all these efforts to placate capital, capital remains fairly hostile to the administration and its modest regulatory efforts – which will, no doubt, prompt further efforts by Obama & Co. to placate business, efforts that will never satisfy, and will so have to be repeated … and repeated.

So in return for hundreds of billions of dollars in public funds used to keep the financial system from going under, the banks will emerge from this crisis largely unscathed. One reason for this is Wall Street’s skill at lobbying, and its ability to spread huge amounts of cash around Washington. As Public Citizen documented, between 1998 and 2008, Wall Street spent $5 billion in campaign contributions and deployed 3,000 lobbyists across Capitol Hill to get its way.¹⁹ While $5 billion sounds like a lot, it was less than a third of the Goldman Sachs bonus pool for 2009, and spread out over a decade. Wall Street has a lot of money, and Congress can be bought on the cheap.

But, as I argued earlier, Wall Street also represents the commanding heights of the economy, the central mechanism by which ruling-class economic power is formed and exercised. It’s only surprising to people who don’t understand this that Washington dances so faithfully to the bankers’ tunes.
WE THE PEOPLE

Alas, it’s not just about ruling class power. We must be honest with ourselves, though, and recognize the deep conservative streak in much of the US population. In February, for example, Gallup released a poll showing that over half – 57 per cent to be precise – of Americans are more worried that there’s too much regulation of business by government than too little; just 37 per cent believe the reverse. Not quite a quarter, 24 per cent, think that government should be more involved in regulating business; more than twice that many, 50 per cent, think it should be less involved. This comes after three decades of experience with deregulation, in which finance has repeatedly blown up, electricity has gotten more expensive, E. coli-infested hamburgers have sickened hundreds of thousands of people, and the airline industry has, on balance, lost more money than it’s made throughout its entire history as a commercial enterprise.

Of course, there are contradictions. When you ask people specific questions about regulation, such as about finance, you get friendlier responses. But the more general poll taps into the common sense or gut reaction of the American popular mind, which is what makes it so easy for the right to shoot down even specific attempts at regulation.

On a somewhat cheerier note, Gallup also recently reported that 36 per cent of Americans have a positive image of socialism. But 95 per cent have good feelings about small business, 86 per cent about free enterprise, 64 per cent about capitalism, and 49 per cent about big business. It may be that every time Fox News labels Obama a socialist, that improves collectivism’s image among Democrats. Sadly, this means that handing out buckets of money to Wall Street to restore the status quo ante bustum is now synonymous with socialism in the popular mind. Maybe not. So this poll suggests that the prospects for the left in America aren’t completely hopeless – just partially so.

The recession probably ended, at least in some formal sense, in mid-2009, and the economy has been stabilizing ever since. But the recovery, such as it is, is likely to be weak and stumbling, and it could take five years or more to recover the 8.4 million jobs lost in the recession. Indeed, the long-term employment picture in the US is remarkably bad. Because the weakest expansion in modern history was followed by the worst recession since the 1930s, total employment in June 2010 was 2 million below the peak reached in 2001. Barring an unlikely major acceleration of job growth in the second half of 2010, the first decade of the 21st century will be the first decade in which employment contracted since 1900, when accurate statistics first became available. In the face of this, the radical left, much of which has
been angling for a crisis as some sort of *deus ex machina* event that would cause the scales to fall from the eyes of the masses and embrace socialism, has been unable to make any political headway in the US at all. In fact, most of the radical political energy in the US so far is coming from the right. This actually isn’t all that uncommon. Economic troubles generally increase the vote for far-right parties in European elections but not far-left parties. The rise of the Tea Partiers in the US, reminiscent of the rise of militias and Ross Perot during the economic troubles of the early 1990s, not to mention the election of Ronald Reagan in 1980 after the stagflationary crises of the 1970s, only shows that a similar pattern operates in the US.

Maybe years of stagnation will change the political landscape in ways friendlier to the left. But as this is written, three years after the onset of a financial crisis, Wall Street looks to have consolidated its power. Stranger things have happened, no doubt, but it’s hard to think of one at the moment.

NOTES

1 The count of industries and their exact names have changed four times over the years, with breaks in 1948, 1987 and 1998. The ratios reported in the text are based on splicing the series together.


5 By 1985, the endowment had doubled in nominal terms – which sounds nice, but that was well behind the pace of inflation. That real underperformance didn’t last for long. The endowment was soon on a tear, beginning the transformation of Yale into a university attached to a hedge fund. It passed $5 billion in 1997, $10 billion in 2000, and $20 billion in 2007. It too has fallen back, to $16 billion at the end of the last fiscal year, which takes it back to its 2005 level, when the university was practically begging for quarters on the street. Yale now feels very poor, and is cutting the budget and laying off staff.


7 The computations are my own. The nominal values of the S&P 500 index are deflated by the Consumer Price Index; the return excludes dividends. The bond return measure is based on a notional 8 per cent coupon Treasury bond whose value is adjusted according to market interest rates; it assumes that interest payments are reinvested in the mythical portfolio. Because of timing, taxes and fees, actual returns for real investors would be lower than
this theoretical value. Corporate profitability is defined as profits before taxes from the national income accounts divided by the value of the tangible capital stock from the Federal Reserve’s flow of funds accounts, both for nonfinancial corporations.

8 For more on Jensen, see Henwood, *Wall Street*, pp. 265-77. The complete works of Jensen can be found at http://www.people.hbs.edu/mjensen.


14 The calculations are my own, from the Federal Reserve’s flow of funds accounts.

15 Dodd for Connecticut: Senator Christopher Dodd, whose state is home to a good deal of the hedge fund industry, and Frank for Massachusetts: Representative Barney Frank, whose state is home to a number of large mutual fund and money management firms.


17 For the original Obama proposal, see US Department of the Treasury, *Financial Regulatory Reform: A New Foundation*, available at http://www.financialstability.gov. Obama has shown none of the toughness in dealing with Congress that earlier presidents have shown in pushing their agenda. Even with a large Congressional majority, Obama has been more timid with the legislative branch than his predecessor was with a slim majority. And next to a master like LBJ, Obama is a piker. By this, I don’t mean to imply that Obama is some sort of closeted radical – he isn’t. But his weakness in fighting for what is supposedly his own agenda, and his eagerness to compromise with the opposition party, is striking in purely partisan political terms. For an interesting speculation on what Lyndon Johnson would have done to pass Obama’s alleged domestic


