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Chasing Stiglitz

Obama's economic team is missing the one guy who's been right all along.

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OK, enough with the Obamamania already. I have a major bone to pick with our all-praised president-elect. Where, Mr. Obama, is Joseph Stiglitz? Most pundits have pretty much gone ga-ga over your economic team: The brilliant Larry Summers as head of your National Economic Council. The judicious Tim Geithner as Treasury secretary. The august Paul Volcker as chair of the newly formed Economic Recovery Advisory Board. But lost amid the cascades of ticker tape is the fact that, astonishingly, you didn't hire the one expert who's been right about the financial crisis all along—and whose Nobel Prize-winning ideas will probably be most central to fixing the global economy.

This is not speculation. A source close to Stiglitz told me Thursday that the Columbia University economist has been left out in the cold, even though he was expecting at least an offer. (Stiglitz, traveling in Brazil, could not be reached.) Especially since Stiglitz supported Obama long before most of the others named to his cabinet (at a time when Summers was a key advisor to Hillary Clinton). "Who knows why? Obama has been choosing center-right people," said the source, an associate of Stiglitz's who would speak only on condition of anonymity. She went on to say that Stiglitz's long-time enmity with Summers—whose ideas, Obama said last week, "will be the foundation of all my economic policies"—may be a factor. "Larry's had it in for Joe for decades," she said.

No surprise there. Stiglitz, more than anyone on the Washington scene, was the biggest fly in the ointment of "free-market fundamentalism" pressed on the world in the '90s by Summers, Geithner and their mentor, former Treasury secretary Robert Rubin—advice that has now contributed to the worst financial crisis since the Great Depression. It's not just that Stiglitz's Nobel-winning work, building on John Maynard Keynes's insights, uncovered profound fallacies in the Reagan-era idea that markets, especially in finance, can always correct themselves (good call, Nobel committee). In his writings and speeches since serving as chairman of Bill Clinton's Council of Economic Advisors and then chief economist of the World Bank, Stiglitz has been the leading voice opposed to the mindless liberalization of capital flows that brought us to where we are today.

In a spate of books, essays and speeches dating from the early '90s, Stiglitz denounced Rubin's support for repeal of the Glass-Steagall Act, which separated commercial from investment banking for precisely the reasons we are now witnessing on Wall Street: new "full-service" banks would seek to hype companies that their stock-market side underwrote and issue loans to them even if they were not credit-worthy. "The ideas behind Glass-Steagall went back even further [than the 1929 crash] to Teddy Roosevelt and his efforts to break up the big trusts," he wrote presciently in "The Roaring Nineties" (2003). "When enterprises become too big, and interconnections too tight, there is a risk that the quality of economic decisions deteriorates, and the 'too big to fail' problem rears its ugly head." Unfortunately, Stiglitz wrote, his worries "were quickly shunted aside'" by the Clinton Treasury team. Earlier, in his book

"Globalization and its Discontents" (2002), Stiglitz became the most prominent voice in Washington to say plainly that free-market absolutism, which began with the Reagan revolution and continued under Clinton (who upon being elected declared the era of "big government" was over), was ill-founded theoretically and disastrous practically. "In 1997 the IMF decided to change its charter to push capital market liberalization," he wrote. "And I said, where is the evidence this is going to be good for developing countries? Why haven't you produced some research showing it was going to be good? They said: we don't need research; we know it's true. They didn't say it in precisely those words, but clearly they took it as religion."

As far back as 1990, Stiglitz argued in a paper (it can be found on The Economist's Voice Web site at www.bppress.com) against securitizing mortgages and selling them because "when banks retained the mortgages which they issued, they had greater incentives to screen loan applicants." He asked, again with startling prescience: "Has securitization been a result of more efficient transactions technologies, or an unfounded reduction in concern about the importance of screening loan applicants?" None other than Milton Friedman, the founding father of the free-market era, told me in an interview before he died that Stiglitz also had been more correct than everyone else about how to transform Russia into a market economy when he argued that institution-building and creating regulatory authorities were an important preliminary step. "In the immediate aftermath of the fall of the Soviet Union, I kept being asked what the Russians should do," Friedman told me in 2002. "I said, 'Privatize, privatize, privatize. I was wrong. Joe was right. What we want is privatization, and the rule of law."

The son of a schoolteacher mother and insurance-salesman father, Stiglitz grew up in one of the grittiest industrial cities in American—Gary, Indiana—and was shaped by the social inequality and labor strikes he observed there. (Yeah, he's a liberal; am I wrong in suggesting, in the wake of this disaster, that we can use the L word as something other than an epithet again?) In 2001, Stiglitz shared the Nobel Prize for Economics for pioneering work in which he argued that financial markets especially are prone to act on imperfect information, leading to unnecessary panics, manias and bubbles and necessitating government intervention.

Like Keynes himself, who fought successfully to block "hot money" at the postwar Bretton Woods conference in 1944, Stiglitz understood the problem of international capital flows like few others of his era. As his longtime collaborator Bruce Greenwald—another Columbia professor who, by the way, is a conservative Republican—puts it: "You need radical global reform" to correct chronic imbalances in capital flows, all of which Stiglitz has laid out in his book, "Making Globalization Work." "There's no chance these guys are going to do what's necessary," with the possible exception of Summers, says Greenwald. And without those additional steps, he warns, the fiscal stimulus that the Obama administration is now putting its hopes on won't avert the devastating recession to come. "Unemployment is going to go to 6½ percent, then to ten percent by the end of 2010. When it goes to 14 percent by 2012, Obama and the Democrats are going to be toast." (Neither the Obama transition team nor Summers immediately responded to a request for comment.)

Keynes is dead, but we still have Joe Stiglitz. And so the question is: what is he doing in New York? Sure, I know the rap on Stiglitz: while he's personally a gentleman, he's too often "off the reservation," won't stay on the message, and doesn't play well with others—especially Summers. (Summers is said to have pressured former World Bank president Jim Wolfensohn to fire Stiglitz in the '90s; he left under pressure in late 1999.) Unquestionably, Stiglitz has occasionally gone overboard in his criticisms, such as when he suggested, outrageously, that the eminent economist Stanley Fischer—a former senior IMF official who taught both Summers and Fed Chairman Ben Bernanke at MIT—had pushed for capital-markets liberalization in the '90s so he could secure a fat job at Citigroup afterwards. But Obama has made a point of declaring that he wants dissonant voices in his administration. So why not Joe Stiglitz?

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