Infinite Debt

How unlimited interest rates destroyed the economy

by Thomas Geoghegan

Harper's Magazine Essay (April 2009)

As I walk through the Loop in Chicago, I wonder how many people I pass are caught up in lawsuits. In a Whitman mood, I try to guess from each face who's being hauled into court to pay off a debt. According to a front-page story in the Chicago Tribune last June, the number of collection cases before the circuit court of Cook County came to over 130,000. That's double the number of cases in 2000, and well before the meltdown: obviously the number is even higher now. At the Daley Center, across the street from my office, I can watch hundreds of these cases go to judgment in half an hour: in go the debtors, out go the lawyers to garnish people's wages. And then there are the home foreclosures, some 44,000 of them in 2008. The number of collection and foreclosure cases in this one county - 174,000 - is equal to the total number of people in three entire Chicago wards: every man, woman, and child. I stress "child" in particular, since the banks give out credit cards like candy.

Yes, 174,000 cases - and that was before the economy tanked. These are not old-fashioned collection cases either. Typically, the banks are enforcing arbitration awards handed down by "private arbitrators" who more or less work full time for the banks. So the banks can sue anyone anywhere in any court in America without having to provide a witness or prove a case.

The pain of all this may get much worse. If deflation comes (even in a mild form), it means each dollar of debt will be harder to repay. That's why populists in the 1890s took up their pitchforks: deflation made it increasingly difficult to pay off the principal on their loans. But at least in the time of William Jennings Bryan, they were only paying back at five percent. While we deflate, creditcard holders will be paying off at rates of twenty percent to 35 percent, and 1890s-type deflation would make the rate feel more like 35 percent to fifty percent.

What's the worst of all the legal changes that fill up collection courts? There are so many, but I'd pick the legalization of usury. It's the form of deregulation that not only drove us into debt but also sped up the loss of the manufacturing jobs that created our middle class - that, in short, brought about our current Time of Troubles.

That's what I tried to tell the people at the Catholic Worker Movement.

It was last September, and around the block from our little soup kitchen, Wall Street was about to collapse. I was supposed to give the Friday night reflection right under the little room where Dorothy Day used to live. It's a puzzle about the Catholic left in New York, or at least they baffle the Catholic left in Chicago. In New York, it's all gentle and anarchist; and in Chicago, even on the Catholic left, it's all about, well, organization - our little door-to-door canvassing. In imperial New York, this Chicago-type organizing seems a little ridiculous.

Most of the anarchists here were elderly, over seventy, like the average age of nuns. It was odd to see a few young blonde girls. Someone said they were from Germany. In fact, even some of the older people spoke German. The German girls, gorgeous, looked like they had stepped off the tennis court. They were here on some kind of fellowship. Their experience of America would be serving up soup in SoHo.

So on this holy night when Wall Street was on fire, I told this little story: One day in late 2000, I got a call from Monsignor John Egan, a labor priest and civil rights activist who had marched with Saul Alinsky. When he hit old age with his bad heart, he'd try to get people to join committees by saying, "Oh, Sue" - or Bill or Jean or Tom - "it's probably the last thing I'll ever ask of you". He made these requests for years. But in what was really the last time, he wanted me to help him fight a new kind of loan - payday loans at rates of 100 percent or 500 percent or 700 percent, which were increasingly on offer in Illinois. I was astonished. For a guy like Jack Egan, who had marched with Walter Reuther and Martin Luther King Jr, this seemed like such a minor issue. Who'd even take out a payday loan?

Now, years later, when there are well over a thousand of these loan agencies in Illinois, and Jack Egan has long since died, I wish I could say: "O Monsignor, you were right". He could see, years before the rest of us: this fight against the banks was like the fight to unionize, it was like the civil rights movement. He knew, as the rest of us did not, where an Alinsky, a Reuther, a King would be - they'd be marching on the banks.

Some people still think our financial collapse was the result of a technical glitch - a failure, say, to regulate derivatives or hedge funds. All we need is a better chairman of the SEC, like brass-knuckled Joe Kennedy, FDR's first pick. It's personnel - it's Senator Gramm's fault. Or it's Robert Rubin's fault.

In fact, no amount of New Deal regulation or SEC-watching could have stopped what happened. Hedge funds in themselves did not cause Wall Street to collapse. Some New Deal-type regulation was actually introduced in recent years, but it failed to do much: think of the Sarbanes-Oxley Act of 2002, which made CEOs swear an oath that their financial statements were not fraudulent. No, the deregulation that led to our Time of Troubles was of a deeper, darker kind. The problem was not that we "deregulated the New Deal" but that we deregulated a much older, even ancient, set of laws.

First, we removed the possibility of creating real, binding contracts by allowing employers to bust the unions that had been entering into these agreements for millions of people. Second, we allowed those same employers to cancel existing contracts, virtually at will, by transferring liability from one corporate shell to another, or letting a subsidiary go into Chapter Eleven and then moving to "cancel" the contract rights, including lifetime health benefits and pensions. As one company after another "reorganized" in Chapter Eleven to shed contract rights, working people learned that it was not rational to count on those rights and guarantees, or even to think in these future-oriented ways. No wonder people in our country began to live for the moment and take out loans and start running up debts.

And then we dismantled the most ancient of human laws, the law against usury, which had existed in some form in every civilization from the time of the Babylonian Empire to the end of Jimmy Carter's term, and which had been so taken for granted that no one ever even mentioned it to us in law school. That's when we found out what happens when an advanced industrial economy tries to function with no cap at all on interest rates.

Here's what happens: the financial sector bloats up. With no law capping interest, the evil is not only that banks prey on the poor (they have always done so) but that capital gushes out of manufacturing and into banking. When banks get 25 percent to thirty percent on credit cards, and 500 or more percent on payday loans, capital flees from honest pursuits, like auto manufacturing. Sure, GM is awful. Sure, it doesn't innovate. But the people who could have saved GM and Ford went off to work at AIG, or Merrill Lynch, or even Goldman Sachs. All of this used to be so obvious as not to merit comment. What is history, really, but a turf war between manufacturing, labor, and the banks? In the United States, we shrank manufacturing. We got rid of labor. Now it's just the banks.

Which is why the middle class is shrinking. Basically, we're all waiters now; we're bowing and scraping and working for the banks. Look closely at any American, and it's even odds that he or she, directly or indirectly, is somehow employed by the "financial services sector", which covers insurance and real estate and financial instruments of any kind. As brokers, lawyers, loan collectors, loan consolidators, secretaries at big investment firms, chauffeurs of private limousines, or even the high-tech types who exist solely to service banks - all of us, millions of us, are part of it, living off it in some way, as three generations ago we lived off manufacturing.

Yes, we should have more regulators, many more; but as long as capital gushes into the financial sector, the speculators, the gamblers, will continue to outnumber the regulators who can watch them. In 2002 and 2003, financial firms took more than forty percent of the profits that accrued to US corporations - that's according to the Bureau of Economic Analysis. Anyway, the point is that forty percent is more than double the share the financial industry was taking - about eighteen percent - when Ronald Reagan left office and interest rates were just beginning to really climb. And the Bureau of Economic Analysis may be understating how much of the economy is now based on finance. Think of the growth of the health-insurance industry, for example. Or think of GM, which, like GE, really makes its money by running a bank on the side. "After a while", said a friend from Detroit, "the only reason they were making cars was so they could make loans".

Everything followed from this. The bloating of the financial sector helped create the growing US trade deficits, which brought in a flood of cheap money for borrowing - which helped further bloat the financial sector. Look at the timing. The big trade deficits came at about the time the caps on interest rates came off, in the late 1970s. Capital flowed out of manufacturing, with its "low" profits, and into the financial sector, where profits were much higher. We became less competitive in manufacturing because we could not accept the lower rate of profit - not vis-a-vis our competitors in Mexico, but vis-a-vis our competitors in New York City.

Who helped the financial sector make too much? We did. In a sense, we use our credit cards to help liquidate our own jobs, the kind we used to have in Michigan and Ohio. By little teaspoons, the people who go into debt for kitty litter pull a bit more capital out of one sector and pour it into another,

Who's to blame? Let's start with the lawyers. Yes, once again, as with everything, lawyers are to blame. I blame the lawyers because the financial sector would not have been able to crowd out manufacturing without three major changes in the law.

First, and worst of all (as I always have to say, being a labor lawyer), we lost the right to organize. That's a long story, but over the years employers found out they could just ignore the Wagner Act and fire pro-union workers right before so-called secret-ballot elections: they found out there was no real limit on what they could use as threat. And the result is that people in this country can't get a wage increase. They can't get a wage increase despite all our gains in productivity. That's not supposed to happen. But that's what did happen. The Economic Policy Institute reports that, since 1972, the median hourly wage for men has remained basically flat, and has actually declined for the bottom fifth of workers. (Women saw more of an improvement, but that's only because women were grossly underpaid in 1972.) What is more astonishing is that in this very same period, when workers were losing financial ground, their productivity - their output per hour - nearly doubled. They were doing twice as much work for the same wage or less.

I hope Ayn Rand, if she were still alive, would be at least a little shocked.

At any rate, the wage stagnation that resulted from the inability to organize goes a long way toward explaining the current situation. People took their "cut" of productivity by going into debt. You may object: "Why did people have to go into debt? After all, family income went up." That's true, but only because more family members were working - and working longer hours. The income "gain" was illusory. The more hours people worked, the more they had to pay out in day care, in transportation, in eating at fast-food restaurants; that is, in outsourcing their private lives to vendors. I could go on about this: how we need more cars to get more family members to work, and so on. Let's just say that the longer we're away from, home, the less we really take home at the end of the day.

This growing gap between how much we produced and how much we earned led to a bizarre paradox: as the economy grew, individual people were actually becoming worse off. Even people who were making more money were living in a way that put them deeper in debt. I think many of these people, strung out, began making wild consumer purchases as objective correlatives for the fact that they had no time to consume. It seems that the less time there is to consume, the more consumers spend.

I have briefly mentioned the second big legal change: over the past forty years, employers have found ways to cancel any earned right, of any kind, at any time. I'd say that with a competent lawyer any employer can cancel any promise to any worker. As a result, people learned it was not rational to save. In particular, right around the time Reagan took office, companies began to figure out that they could go in and out of Chapter Eleven in order to dump their obligations not just to workers but also to retirees. As a labor lawyer, I saw firsthand in bankruptcy court the shocking way in which companies could cancel retirees' health, severance, and pension rights, though some were federally insured. Although we now think of the middle class as a debtor class, people came into these Chapter Eleven cases not as debtors but as creditors - yes, creditors, because big wealthy companies owed them pensions. By the time the "reorganizations" were over, the creditors had managed to hang on to five cents on the dollar, maybe ten. Often the companies weren't "bankrupt". The parent firm was simply shutting down the subsidiary and taking all the loot. The shock of all these lost property rights turned into anti-wisdom that the old steelworkers passed down to their children and grandchildren: "Why save? There isn't any point." Sure people stopped saving. Planning for the future no longer made much sense.

At this moment - the late 1970s - as people lost their right to organize, as they lost their rights as creditors in court, they were just in time to trade in their union cards for credit cards.

That's the third big change, which came along with the other two: the legalization of usury. That process of legalization was complex, and happened over the course of several years at both the state and federal levels, but I'd say the breakthrough, the case that made it all possible, was Marquette National Bank vs First of Omaha Service Corporation, a

1978 Supreme Court opinion. Alas for us who love him, the decision was written by Justice William J Brennan, who seems in this case to have taken a little nap. Minnesota was trying to impose its law against usury on an out-of-state bank. The Court held that Minnesota could not cap the credit card of a Nebraska bank, because both banks were subject to the National Banking Act of 1864, which allows national banks to charge interest at the rate set by the state "where the bank is located", regardless of the laws in the state where the bank is actually lending money. So it became the law of the land: the old, state-mandated top rates of nine percent or so were gone; now, thanks to the Supreme Court and the National Banking Act of 1864, there were no effective caps on what the big national banks could charge credit-card holders. Now we're all shoveling billions into the banks, and there's no way working people who can't get a raise will ever climb out of debt. And that leads to an unhappy thought: Who turned the United States into a debtors' prison? Maybe it was Lincoln, who first enforced the act. Yes, it is tempting to blame a Republican.

The change in credit-card caps also had a bad effect on the moral character of the nation. Because interest rates were so high, the banks no longer wanted borrowers with good moral character. Look at the way lending has changed just since the time I was in law school in the early 1970s. Even then, the mantra of my teachers in contracts and commercial paper was: "The loan must be repaid!" I have a friend, a professor, who still quotes that refrain. But it's out of date. At interest rates of 25 percent, or fifty percent, or 500 percent, lenders don't really want the loan to be repaid - they want us to be irresponsible, or at least to have a certain amount of bad character.

I like to tell people that to find out what deregulation of usury did to us, they should check out the next Christmas showing of It's a Wonderful Life. Remember, Mr Potter the bad banker would not make loans, while the tender-hearted George Bailey always would. Mr Potter wanted references. He wanted character. Mr Potter was the bad guy because the loan must be repaid!

But Mr Potter was lending at an interest rate of something like two percent. At those rates, he wanted to be repaid. But now Mr Potter would have more choices. If he could charge 35 percent, he might not necessarily think, "The loan must be repaid" - at least not right away. And if he can charge 200 percent, he actually may not want the loan ever to be repaid. I had a retired schoolteacher in my office the other day whose husband is deep into Alzheimer's. The two had taken a loan for $1,700, somehow managed to pay back $3,000, and still they had not even begun to pay off the principal. That's not uncommon in our post-Mr Potter world.

But that's just interest. Along with the collapse of anti-usury laws, we have also seen the deregulation of virtually everything else bankers do. Now banking is a fee-based business, too. First, people run up huge interest debt, and then they start making overdrafts and bouncing checks, and then come the hidden fees. There are overdraft fees, fraud-detection fees, and fees the banks just make up for no reason at all. I have a client with twenty-seven payday loans. I told her to stop paying any of them. "You paid enough. Close your bank account." But she couldn't. Her bank had decided that she had no right to close her account. And sure enough, as each of the twenty-seven checks came in and bounced, the bank charged her a whopping fee.

These are the same banks that begged her as a taxpayer to give them bailout money.

It may be hard to grasp how the dismantling of usury laws might lead to the loss of our industrial base. But it's true: it led to the loss of our best middle-class jobs. Here's a little primer on how it happened.

First, thanks to the uncapping of interest rates, we shifted capital into the financial sector, with its relatively high returns. Second, as we shifted capital out of globally competitive manufacturing, we ran bigger trade deficits. Third, as we ran bigger trade deficits, we required bigger inflows of foreign capital. We had "cheap money" flooding in from China, Saudi Arabia, and even the Fourth World. May God forgive us - we even had capital coming in from Honduras. Fourth, the banks got even more money, and they didn't even consider putting it back into manufacturing. They stuffed it into derivatives and other forms of gambling, because that's the kind of thing that got the "normal" big return; that is, not five percent but 35 percent or even more.

Go back to the top and repeat the sequence. It was what scientists call an autocatalytic reaction. It just kept going. All of that cheap money would have been a good thing if it had gone into manufacturing. But it didn't. The capital inflows from the big trade deficits couldn't go into manufacturing because the returns in banking were just too high. And because this autocatalytic reaction kept going - as long as there was the imbalance between finance and industry - the system could not readjust or stabilize. The bigger the deficit, the bigger the capital inflow; and the bigger the capital inflow, the bigger the financial sector became; and the bigger the financial sector became (relative to manufacturing), the bigger the trade deficit became.

And meanwhile, we lost more and more skill-based jobs. Oh, we had jobs, and even jobs that required college and postgraduate educations. But we stopped being skill-based workers. We became "knowledge workers", dependent on the financial sector. And knowledge workers, unlike skill-based workers, don't have the bargaining power to get higher wages out of rising productivity. What can they withhold? They can't withhold knowledge. And since they have nothing to withhold, it's much trickier for knowledge-based workers to get a higher wage. And if there are fewer skill-based workers, it becomes harder to raise wages in general. And if it's harder to raise wages, then more of us go into debt.

Joseph Schumpeter, the great economist, long ago criticized the theory of what he called "the vanishing investment opportunity", which attempted to explain why the global economy had come to a halt in the 1930s. The theory was that capitalism required a constant stream of new products to invest in, and once that stream ran out, capitalism would collapse. But Schumpeter was certain that the supply of new things to bet on would never run out, because technology, and capitalism's inherent creative dynamics, would always provide anther investment opportunity. Of course, Schumpeter was writing about the manufacturing sector. In Capitalism, Socialism, and Democracy (1942), his most famous work, he barely mentions banking, which has come to dominate our system. And with no cap, with no limit on the bloat, the financial sector faces the same problem as manufacturing - especially now that it has managed to extract all of the value from manufacturing. That is, the financial sector constantly needs new "products". So we came up with more derivatives. We had always had futures, but now we had futures about futures. We have long had futures on the weather; for example, there is a weather index. But now we have futures on the weather futures. These are the "products", not widgets, et cetera, that our form of financial capitalism makes. This is what our country makes now; new products on which to place our bets.

One might ask what labor was doing. Well, labor was out marching against NAFTA. That was helpful, wasn't it? In the early 1990s, the AFL-CIO spent more time trying to stop NAFTA than pushing for a bill that would allow workers to organize freely and fairly without being fired. And if Big Labor didn't even care that much about the right to organize, it had no concern at all about the bloating of the financial sector.

Yet that bloat is precisely what wrecked the US labor movement, maybe for good. Of course there is still an industrial sector. In fact we have ended up with a far bigger manufacturing sector than we deserve, in part because we don't have the competition we should have from Mexico and Canada. I mean, imagine us going up against the European continent, like the United Kingdom did. The Midwest would look like the north of England.

Didn't labor care?

No, all they cared about was Mexico, and never mind that the trade deficits were much greater with Canada. Labor, apparently, isn't troubled when we lose our jobs to white people. I am waiting for the day when the AFL-CIO leads a march up to Toronto. But the trade deficits we run with Mexico and Canada - and far more serious, with China and East Asia, as well as Saudi Arabia - arise in major part because of the returns to finance.

"Well", you might say, "that's the area in which we're more competitive globally". And it's true: we are competitive globally, though not because of a special skill we have but because relative to other countries we make finance so much more profitable.

But this is a fake "comparative advantage". And as trade deficits rise and cheap money gushes in, it's killing the country.

The labor movement should have been a guardian of manufacturing. Instead, it looked the other way. I now see the potential for a revived labor movement, based on service-sector unions. But a labor movement based on the service sector can never truly "come back" as a real force for social democracy. Don't misunderstand: I represent service-sector employees, plenty of them. I love the Service Employees International Union, which I think is a labor movement in itself. I recognize that the SEIU can raise the wages of janitors and maids, in some circumstances at least.

But in a developed country, no labor movement can succeed if it loses its base in manufacturing. The reason is this: although service-sector unions can raise the wages of the working poor, they don't do much for the middle class. A labor movement that has lost its base in manufacturing will never be a "player" in setting the wage levels in either sector - manufacturing or service.

In Germany and France, the concessions the trade unions get in manufacturing become a kind of guideline or signal as to what "everyone else" should get. What IG Metall employees get affects what German professors and diplomats get. That's because the trade unions in manufacturing have skills they can withhold and can bargain more effectively for the slice that they should get from rising productivity. That may not be money. It could be leisure. That's why some people in the United States scoff that European labor isn't keeping up in income; although the data behind this criticism is disputed, another answer is that Europeans are taking a higher income in the form of leisure. With no base in manufacturing, a labor movement in the United States will never be able to get either more cash or more leisure, even if productivity rises. It's fine to organize people in services, who have no skills they can withhold. But that will never bring back a labor movement that can raise wages in a spillover or indirect way for the white-collar middle class.

It would be wrong for me to say that all this deregulation is turning the country into a casino. But I will say this: it's starting to turn Chicago into a casino. Look, I love it anyway, but it's not the same city. Once we made drills. Now we make derivatives. That's why the Financial Times has a bureau here. It's all going on, Sodom-like, a few blocks from my law office, over in the CME, which is the name for what is in effect a joint venture between the old Chicago Board of Trade and the Chicago Mercantile Exchange.

I'm no Luddite on derivatives. Who'd deny a derivative to a farmer raising corn? "I will sell you a pork belly at 5.2 Euros on Saint Crispin's Day in 2013". It's a good thing. Devout Mormons used to do it. In the olden days, derivatives were harmless little bets that helped producers take risks. But in our time, people are using derivatives to make much bigger bets, not to "help producers" but as a locust-like alternative to producing anything at all. As the lucre from the financial sector piles up, the traders in Chicago take out bits of it to make wilder and wilder bets.

What did we bet on? I don't mind futures on the weather, or futures on interest rates, or even futures on the fluctuations of the price of bleacher seats for Cubs games, but I really have trouble with futures on the futures, bets on the outcomes of all the bets. That's to me what seems like Babylon, if the Babylonians had behaved as badly as we do and had gotten rid of their usury laws.

By 2007, the "notional" value of all these bets came to $516 trillion - a number that even theoretically is hard to ponder. And that is all capital that could have gone into real things we could have sold abroad. The money we bet in Chicago is the money we should have been investing in Detroit. And I know they're lunkheads in Detroit, but the lunkheads ended up running the auto industry because the smart people, the Harvard dropouts and the autodidacts from Texas Tech, decided that the real money wasn't in starting software companies or running telcos but in derivatives.

We set up the incentives to keep our best and brightest out of Detroit. In June 2008, even in a bad year for Wall Street, 39 percent of the Harvard graduating class went directly into consulting or the financial sector, and many others will go a few years later, after graduate school. The percentages are probably the same or worse for Princeton, Yale, and other elite schools. Of course, there are lunkheads in this group, too, but it shows where in general the talent's going.

In Europe, by contrast, kids from elite schools still go into jobs at utilities. Yes, seriously, bright Europeans still work for the electric company. They certainly work for BMW and Daimler AG. In the United States, our kids - once they shed their dreams of working for Goldman Sachs - end up in wealth management and handle private clients with $150 million or more. Or at least they used to.

They don't come to Chicago to trade. That's too crude. The kids who do the trades come from Ohio State and the like; in a relative sense, they come up from the streets.

The son of a friend of mine just moved here. He said he's now met a lot of Chicago guys, aged twenty-eight, twenty-nine, who came out of schools like Miami of Ohio and the University of Oklahoma. They have no real jobs that he can identify. But they seem to be making $120,000 or more. "I can't figure out", he said, "what any of them do".

I know what they do: they run errands for the traders. In a sense, these kids catch flies for Howard Hughes, though their bosses are smaller-time operators, and they deal with a lot less regulation than Hughes ever had to.

No, these guys are no Howard Hugheses. They're the equivalent of scalpers for the Bulls games. You can see them lined up in the cold on Friday night outside the Funky Buddha Lounge. Even on Friday night, they're still on their cell phones as they check out the girls.

Well, I don't mean to sniff. God help us, we older people live off the kids who are making the big bets. It was the scalpers who sold the financial instruments to the Ivy League kids. I'd rather not think about it. But even on WFMT, the fine-arts radio station; they have ads for something called "The Chicago School of Trading", where older versions of those same cell-phone checkers and fly-catchers will "mentor" you as you learn how to make wilder and wilder bets. And it's chilling to think that some young woman is putting down her viola and enrolling as a student trader even as I sip my Starbucks and listen to Vivaldi.

For a while, after Obama's election, Chicago seemed so nice and clean. For a while, the national press (or the New York Times) was full of coochy-coos about how simple and plain and hardworking Chicago is, and how the election of "Chicago's President" will help purify our character. Of course there is snickering about the Machine: "Oh, Alderman X, he got $50 slipped to him during the intermission of Verdi's Falstaff". Or: "Someone got a job on a garbage truck and he didn't have to take an exam".

But that seemed harmless, even charming - at least until the blowup about Governor Blagojevich made all this corruption seem psychotic.

Still, as much as we need to fumigate our state government, it's far from the only evil in the air. Indeed, because we focus so much on political corruption, the press out here rarely if ever says a thing about the financial gambling all over town. It seemed bizarre that the people in powdered wigs in Washington and New York started applauding our simple and plain Midwestern values as if they would purify the jaded East. Still, I know Chicago will suffer, too, in the Time of Troubles now at hand.

It's obligatory in an article like this for the writer to present a Plan. I know at this point some readers will blow up: "Wait, it's only now, at the end, you're offering a Plan?" A critic once made this point about a book I wrote - that I presented the problem without offering a plan, except at the end, in the last chapter.

Anyway, here's the Plan.

First, we have to pass a new type of law against usury that accepts the world in which we all live now. The saintly Illinois Senator Dick Durbin has proposed an amendment to the

National Banking Act, to put a cap on interest at 35 percent. But that would let too many banks go on as before. Here's an alternative: let's cap interest at nine percent, then let a federal agency give exemptions to applicants - banks - that want to raise rates up to Durbin's limit (I would stop at twenty percent).

To get the right to this higher rate of twenty percent, however, the bank would have to demonstrate each year, to a federal agency, that it has a reputation for honesty and fairness and that it had not been found guilty of any fraudulent or bad-faith practices, such as the use of hidden fees or charges, or the unfair garnishment of someone's pension. I'm aware that this standard is vague. I suppose few licenses would be denied. But the very existence of this procedure - and the right of you and me to email our gripes to a federal agency with the power to exert extreme pressure - would have a chilling effect on banks and keep them from getting too near unconscionable conduct or charging the highest possible rates.

Second, we should have state-owned banks like the German banks known as the Sparkasse. Maybe each of the fifty states could charter its own bank. Each would issue credit cards at a rate much lower than what the private banks charge. Also: no fees at cash machines, no oppressive collection cases, no gratuitous destruction of people's credit ratings. The catch is that, as in Germany, the US Sparkasse would lend only to the most creditworthy people. That is, the state banks would set benchmarks not only for how the private banks should behave but how the people should behave as well.

Third, we should have at least one or two "public guardians" as directors at the banks and other financial firms we have bailed out with $700 billion in taxes and all the money the Fed has printed. Every financial company into which we have "injected equity" should be required to have government-appointed directors, up to a third of the board. We can use these directors to nudge (if not dictate) what the banks and firms should do. For example, the directors should work to bring down credit-card rates. Through guardians, we can lower rates, bank by bank, by moral suasion and a certain built-in pressure rather than by external decree. The guardians should also demand of us good character if they bring down the rates. "Our directors" should help push capital into manufacturing. Of course, there has to be a reasonable profit, but sometimes a reasonable profit can be three percent instead of thirty percent.

Fourth, we should require the banks we bail out to cancel an appropriate amount of consumer debt - especially in instances where people would have paid back the principal by now had the interest rate been more reasonable. My retired schoolteacher, the one with the husband who is deep into Alzheimer's and who has already paid $3,000 on a $1,700 loan, should be let off the hook. The banks we have bailed out should follow the Golden

Rule: just as their own debts have been written down or paid off, so they in turn should do unto others.

Finally, we should think about ways to "inject equity" directly into the accounts of working people rather than into banks. The best way to do this is to announce a plan to raise the gross replacement rate of Social Security from 44 percent to something closer to 65 percent, which is still short of the rate in many European social democracies. We can afford this as much as or more than they can.

We could aim to reach that goal gradually, over the next twenty years, but even announcing the goal encourages future-oriented thinking. It would encourage people to believe that they could invest in real things again, instead of pinning their hopes on the false and predatory promise of a big, Vegas-style payout. The promise of a real public pension that people can live on would lead fewer of us to chase bubbles in good times, even as it gave all of us the confidence to keep spending when times were bad.

Schumpeter feared that this kind of countercyclical thinking by people on the left would lead to a stagnating form of socialism, or even the end of capitalism. But socialism, in the state-run form he anticipated, is not inevitable, or even desirable. Social democracy, European-style, which Schumpeter did not expect, is desirable. Sure, I'd like the European governments to run up a bit of public debt to pump up demand over there - I don't think that's so immoral. What's immoral is to pump up demand, as we have, by handing out easy money at high interest and driving people into debt.

Even in Babylon they spared people that kind of captivity. We now have to ensure our own country does the same.

———

Thomas Geoghegan, a lawyer in Chicago, is the author of many books, including Which Side Are You On? Trying to Be for Labor When It's Flat on Its Back (2004) and, most recently, See You in Court: How the Right Made America a Lawsuit Nation (2009).