

# OUR NOT-SO-GREAT DEPRESSION

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A FAILURE OF CAPITALISM: THE CRISIS OF '08 AND THE DESCENT INTO DEPRESSION. By *Richard A. Posner*. Cambridge, Massachusetts, and London: Harvard University Press. 2009. Pp. xix, 346. \$23.95.

“The world’s banking system collapsed last fall, was placed on life support at the cost of some trillions of dollars, and remains comatose. We may be too close to the event to grasp its enormity.” (p. vii).

“The production of books on financial crises is counter-cyclical.”<sup>1</sup>

## INTRODUCTION

*A Failure of Capitalism* by Richard Posner<sup>2</sup> is not a great book, and it does not pretend to be one.<sup>3</sup> Posner summarizes the economic crisis of 2008–09 and considers proposals to reduce current suffering and avoid future recurrence (p. xvi). But when the book’s final edits were made in February 2009, it was still too soon for authoritative solutions or full accounts of what had happened.<sup>4</sup> Instead, Posner wrote a conspicuously contemporary—and thus incomplete—description of the crisis as it looked to him at the time (p. xvii).

Now one year later, readers may need a reminder about the value of Posner’s quick-baked efforts. His book was one of the first to describe the crisis, and it is a work of fluid prose and potent intellect, written by a scholar with immense personal knowledge and easy access to nationally prominent macroeconomists.<sup>5</sup> In the first wave of academic writing about the crisis, Posner’s book is by far the most accessible, and it is also one of the best.<sup>6</sup>

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1. CHARLES P. KINDLEBERGER & ROBERT ALIBER, *MANIAS, PANICS, AND CRASHES: A HISTORY OF FINANCIAL CRISES* 7 (5th ed., Wiley & Sons, Inc. 2005) (1978).

2. Judge, Court of Appeals for the Seventh Circuit; Senior Lecturer in Law, the University of Chicago Law School.

3. See p. xv (asserting only that “there can be value” in a book like this).

4. P. ix. By way of perspective, scholars still debate the causes of each economic downturn back to and including the Great Depression of the 1930s. Pp. 193–94, 261.

5. Cf. pp. xviii–xix (listing prominent scholars who aided Posner’s book in various ways).

6. Other books of particular value to me include GEORGE COOPER, *THE ORIGIN OF FINANCIAL CRISES: CENTRAL BANKS, CREDIT BUBBLES AND THE EFFICIENT MARKET FALLACY* (2008); KINDLEBERGER & ALIBER, *supra* note 1; PAUL KRUGMAN, *THE RETURN OF DEPRESSION ECONOMICS AND THE CRISIS OF 2008* (2009); and most especially a volume from New York University’s Stern

But such works have short shelf lives. For example, some of Posner's arguments are already superseded, having been either accepted or debunked by macroeconomic experts and unforeseen events.<sup>7</sup> A review of Posner's book might perhaps be written to catalog which of his claims remain valid and which fell flat, thereby describing the crisis more fully and measuring the accuracy of Posner's hurried sketch.

This Review takes a different path and addresses two longer-term questions near the core of modern government.<sup>8</sup> First, does the recent economic crisis prove that market actors act irrationally? Second, does it show that small-government, "Chicago-School" deregulation should be abandoned? The answers to those questions will chart the future of economic governance and will frame many decades of debate over what the present crisis means.

Such issues are also vital to Posner's book. Posner is probably the most famous leader of America's law-and-economics movement, and he has raised a longstanding voice against broad governmental regulation.<sup>9</sup> His title "A Failure of Capitalism" thus leads readers to ponder whether we should have less capitalism, whether such failures occur rarely or often, and whether they can be avoided or must be grimly endured.

From the perspective of conventional politics, Posner's book is unorthodox and even surprising. For example, he does not follow conservative monetarists in blaming the crisis solely on errors of the Federal Reserve, nor does he think that unaided markets will set our economic ship aright (pp. xii, 2). Yet we shall see that Posner also has not abandoned his famous enthusiasm for unrestrained supply and demand; far from it. As with other "Free Marketeers," a persistent issue that looms over Posner's analysis is how much market ideology may be salvaged after the world's highly developed markets have collapsed.

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School of Business, *RESTORING FINANCIAL STABILITY: HOW TO REPAIR A FAILED SYSTEM* (Viral V. Acharya & Matthew Richardson eds., 2009). For a staunchly monetarist view of the crisis, see JOHN B. TAYLOR, *GETTING OFF TRACK: HOW GOVERNMENT ACTIONS AND INTERVENTIONS CAUSED, PROLONGED, AND WORSENE THE FINANCIAL CRISIS* (2009).

7. For one possible example of this, compare Posner's account of bank insolvency as a principal cause of the downturn, pp. 63, 67, with evidence that even though at least some banks are now succeeding, economic conditions remain uncertain, Graham Bowley, *2 Giants Emerge From the Ruins on Wall Street*, N.Y. TIMES, July 17, 2009, at A1; Eric Dash, *Four Banks Are the First To Pay Back Aid Money*, N.Y. TIMES, Apr. 1, 2009, at B3; Eric Dash, *10 Large Banks Allowed to Exit U.S. Aid Program*, N.Y. TIMES, June 10, 2009, at A1 (describing early repayment of government funds, which Posner could not have foreseen); Michael J. de la Merced, *Profits at Two Banks Mask Signs of More Trouble Ahead*, N.Y. TIMES, July 18, 2009, at B1 (noting banks' large profits).

8. This choice is partly a reflection of my own limited skills and information. *Cf. infra* Part IV (discussing the value of "lawyerly generalism"). Also, the necessity of any law review's publication schedule presents an awkward forum in which to debate factual details, as my time-bound misperceptions in 2010 might fare no better than Posner's in 2009. Although Posner asserts a need to write before "hindsight will rewrite history," p. xvi, readers who want solid, conclusive accounts of what happened may simply have to wait.

9. See, e.g., Mitu Gulati & Veronica Sanchez, *Giants in a World of Pygmies? Testing the Superstar Hypothesis with Judicial Opinions in Casebooks*, 87 IOWA L. REV. 1141, 1166 (2002) (listing Posner as "among the most prominent proponents of the Chicago School of Law and Economics").

This Review proceeds in four steps. Part I summarizes Posner's account of how the economic crisis happened. Although such content will be familiar to some readers, Posner's descriptions fill the largest part of his book, and they form an obvious predicate for his distinctive conclusions.

Part II considers market rationality and avoiding economic crises in the future. Before reading Posner's book, one might have assumed that "housing bubbles" and "financial crashes" necessarily implied some level of irrational optimism or panic.<sup>10</sup> Indeed, scholars in behavioral finance and behavioral law and economics view the 2008 crisis as conclusive evidence that markets can be warped and buckled by human emotions and cognitive failures.<sup>11</sup> Posner rejects this view out of hand. Instead, he claims that private actors behaved rationally throughout the current crisis, and that they cannot be blamed for systemic consequences of their actions. By contrast, I suspect that Posner's claims of market rationality are premature and incomplete. Because I cannot myself specify exactly which market participants were rational in 2008, however, I will examine how Posner's *assumptions* about market rationality might affect policies to avert future crises.

Part III concerns governmental intervention to remedy our current crisis. Posner divides economic downturns into two categories and says that we are in a "depression," not merely a "recession" (pp. ix–x, 9–11). Based on the strength of those labels, Posner recommends massive government spending, permissive monetary policy, and assorted regulatory interventions. Such conclusions may seem congenial to liberal economists and politicians at present, but uncertainty in identifying depressions may erode common ground all too quickly. Regardless of its politics, I suggest that Posner's approach to depressions and recessions is unworkable. Even for a general readership, more realism about antidepression politics is needed to analyze governmental decisions before, during, and after an economic crisis.

By way of conclusion, Part IV maps the limits of inexpert macroeconomic analysis like Posner's and—even more—this Review itself.<sup>12</sup> Macroeconomic theories that describe how billions of individuals, millions of entities, and hundreds of governments buy, sell, hire, work, and circulate money are almost absurd in the breadth of their ambition. Yet Posner is right that macroeconomics is as vital to global productivity as weather predictions are to agricultural societies.<sup>13</sup> He is also right to stress the need for "concise, constructive, jargon- and acronym-free, non-technical, unsensational, light-on-anecdote" analysis (p. xiv). A deeper question, however, is why Posner

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10. See, e.g., KINDLEBERGER & ALIBER, *supra* note 1, at 9–11.

11. See, e.g., Erik F. Gerding, *The Subprime Crisis and the Link between Consumer Financial Protection and Systemic Risk*, FLA. INT'L U. L. REV. (forthcoming 2009), available at [http://works.bepress.com/cgi/viewcontent.cgi?article=1003&context=erik\\_gerding](http://works.bepress.com/cgi/viewcontent.cgi?article=1003&context=erik_gerding).

12. Despite Posner's expertise in other fields of economics, his book self-consciously represents an "outsider's perspective" with respect to macroeconomic issues. P. xv. To be clear, the author of this Review boasts a far broader scope of economic inexpertise.

13. See p. 116 (noting that macroeconomic downturns can cause massive economic disruption, political instability, and geopolitical shifts); cf. pp. 117–18 (comparing economic predictions to weather forecasts).

should be the one writing such work, instead of professional economists and financial journalists. Aside from Posner's evident speed and skill, his own reply is that most experts' writings "are by authors with an axe to grind" (p. xiii). This uncharitable characterization will prompt readers to ask whether Posner himself has left all his axes at home. As it happens, he has not, but neither have I.

### I. POSNER'S DEPRESSION

Let us start by reviewing some basic elements of the economic crisis, which are now well known.<sup>14</sup> Housing prices rose, and then they fell. Banks and other financial institutions overinvested in mortgages, and were then crippled when borrowers defaulted and real estate collateral dropped in value. Financial institutions' losses raised credit costs for numerous businesses and individuals, which reduced consumption, production, and employment across the country. The mix of these real and expected consequences reinforced each other and caused massive declines throughout the economy.<sup>15</sup>

This simple account raises harder questions. Why did housing prices rise and fall? Why did financial institutions overinvest in mortgages? And why were defaults and lower property values such a surprise? Posner offers a multipart explanation, which generally tracks that of most analysts.<sup>16</sup> The Federal Reserve and foreign investors increased the availability of cash, which let financial institutions lend money cheaply. Commercial banks had become decreasingly regulated for several decades, and their competition with unregulated financial institutions increased appetites for high-risk, leveraged investments. Advanced and highly complex securitization techniques raised demand for subprime mortgages because they let lenders create relatively safe investment instruments from a pool of risky assets.<sup>17</sup>

14. See pp. 1–2, 6, 13–14, 16, 34–35.

15. Losses to financial institutions may cause especially grave economic consequences because, if producers and consumers cannot afford credit, then they must reduce their production and consumption respectively. In turn, workers cannot be paid if there are reductions in purchasing and production. Such downturns may then cause more loan defaults and tighter credit standards, even as layoffs further dampen consumer spending, thus causing the cycle to spin even farther downward.

16. See p. 284 ("[T]here were failures of the free market, failures of economic science, failures of government—and some bad luck into the bargain."); see also pp. 23, 38–40, 53.

17. The key technique here involves "tranches" of mortgage-backed securities, which may be unfamiliar to some readers. For a simplified example of how tranches work, imagine a pool of subprime mortgages that is estimated to lose 20% due to defaults. If this pool were sold to investors through ordinary shares, then we would expect each share to lose 20%—a uniformly unsafe investment. By contrast, imagine that the mortgage-based shares were split into five equal tranches of seniority, such that the lowest 20% of shares would lose all of their value before the second-lowest tranche of shares could lose even a penny. This technique would create an *extraordinarily* risky asset from the lowest class of shares; indeed, this tranche will lose everything if our estimate is accurate. The highest tranche might be entirely safe, however, because these shares would lose nothing at all unless defaults hit an unlikely 80% of the pool's value.

To glimpse tranching's true complexity, imagine splitting our imaginary pool's middle tranche of securities into five tranches, thereby concentrating the risk to that middle tranche within the lowest of our newly created "subtranches." (If our mortgage pool lost between 40 and 60%, the bottom

When these factors combined with our national confidence in real estate investments, and with the biases of realtors, mortgage agents, and security-rating agencies, it is easy to see how the “housing bubble” emerged.<sup>18</sup> An unprecedented number of borrowers sought land with fervor that was matched by ever-increasing property prices. And lenders gave loans even to people who might default because (a) high-risk loans could be securitized to serve broader investment goals and (b) so long as the underlying property increased in value, distressed borrowers could always sell their land in order to retire unsustainable loans. These dynamics further amplified demand for real estate, raised property prices, and fed a continuing upward cycle that made many people, on every side of these transactions, very wealthy indeed.

Despite this seemingly happy story of profitable homeowners, lenders, agents, and investors, mistakes were made. Lenders lacked reliable models to predict how many subprime borrowers would default, and many of these new borrowers were unpredictably more risky than prior mortgagors (pp. 23, 58–59). Securitized mortgages made things worse. Securitization meant that dispersed security holders could not renegotiate loans to avoid foreclosure if property prices dropped and borrowers could not resell land to cover their mortgage; such foreclosures could consume 20 to 60 percent of a property’s value, making lenders’ losses that much higher (pp. 59–60). More importantly, risk-segregated securities obscured exactly which investors would bear the uncertain risks of debtor default. Many security holders responded by purchasing investment insurance from American International Group (“AIG”), but this created even more complexity in assessing whose money was at stake if land prices dropped.<sup>19</sup>

Posner offers a distinctive explanation for why sophisticated investors placed so much money on risky bets. Posner notes that investors must try to make money while the sun shines, even when they know that darkness is coming.<sup>20</sup> He also hints at conflicts of interest within and outside financial institutions that may have led employees to maximize their own benefit

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subtranche would decline first, without affecting any other subtranche, then the second-lowest subtranche, and so on.) Sometimes, even subtranches were themselves tranced, each time with the same goal of transforming assets with uniform risk levels into a range of different securities with different risk levels. *Cf. infra* note 19 (discussing how credit-default swaps intersected with mortgage-based securities).

18. Pp. 20–22, 46–49. *See generally* KINDLEBERGER & ALIBER, *supra* note 1, at 131 (“One of the great clichés in finance is ‘Land is a good investment, the price of land always increases.’”).

19. The main instruments here were “credit default swaps.” These allowed owners of mortgage-based assets to pay AIG a periodic fee, and AIG agreed to cover losses on those assets if a predefined credit event occurred (e.g., a default). Pp. 56–59. Through these arrangements, AIG drew fees from owners who expected to make money on their assets, and owners shifted some of their downside risks to AIG—at least so long as AIG was able to pay. Complexities in this story arose from the fact, unknown at the time, that AIG amassed far more liabilities in credit default swaps than it could cover, thus making uncertain the value of AIG’s financial “insurance.” Also, pools of credit default swaps were themselves securitized in order to be bought and sold. For an excellent, albeit somewhat technical, explanation of credit default swaps and their lack of transparency, see RESTORING FINANCIAL STABILITY, *supra* note 6, at 236–41.

20. Pp. 88–92. Again, readers must recall that the real estate boom was for many investors a remarkably long and sunny day.

while harming their employers, perhaps by generating fees and short-run profits from securities that would lose their value during an economic downturn.<sup>21</sup> Finally, Posner compares the economic crisis to national security threats.<sup>22</sup> As with Pearl Harbor and the terrorism of September 11th, everyone in society has a strong stake in being safe from attack, yet the costs and benefits of action by particular individuals and groups are so widely shared that no one may have adequate incentives to do what is necessary.<sup>23</sup> Posner sees similar coordinative problems in systemic financial failures. Many investors and entities had an incentive to avoid economic collapse, but for any one of them, the costs of action were too great compared to the likely individual benefits.

In 2005, housing prices started leveling off, and over the next two years, the Federal Reserve raised interbank interest rates with mild effects on mortgages (pp. 118, 120–21). By the summer of 2007, a few mortgage-heavy investment funds went bankrupt, and the nation's largest private mortgage company barely avoided that fate. Then came the flood. In March 2008, Bear Stearns collapsed, then government-sponsored mortgagers Fannie Mae and Freddie Mac, then Lehman Brothers and Merrill Lynch, then AIG. Declining housing prices spread throughout securities markets to strike banks, brokerages, institutional investors, insurance companies, and almost everyone else. Transactional speed and uncertainty regarding complex financial instruments only exacerbated such losses' size and scope. As available credit declined, so did stock and bond markets, consumer spending and confidence, production, and employment, thus creating a spiral of economic downturn.

## II. WHO'S RATIONAL, WHO'S TO BLAME?

After surveying this economic wreckage, many readers will wonder who is responsible and why preventive measures weren't taken. Posner quotes prominent skeptics from 2002 to 2005 who warned in varying detail of the economic crisis to come (pp. 77–78, 119, 124–25, 132, 138–39, 252). How were these warnings ignored? Posner highlights two potential culprits—private financiers who overinvested in risky mortgages and public officials who let them do so—but he offers a radically different analysis of each.

On one hand, Posner allocates “primary *responsibility* for the depression” to the private financiers (p. 284), who were by far the best informed, highest paid, most capable participants in the crisis. Posner believes that financial leaders “must have” known about the destructive economic risks they incurred (pp. 78, 284), yet he denies that private actors can be “*blamed*

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21. See pp. 93–100.

22. Pp. 122–23; cf. RICHARD A. POSNER, PREVENTING SURPRISE ATTACKS (2005) (applying economic analysis to intelligence reform).

23. Posner also uses Pearl Harbor and September 11th to illustrate how governmental entities can also fail to guard against catastrophic risk. See pp. 122–23, 141–42.

. . . implying moral censure [] any more than one can blame a lion for eating a zebra” (p. 284).

By contrast, Posner lays ultimate blame for the financial crisis upon the “inexcusable” “blunder[s],” “overconfidence,” and “insouciance” of public officials and academic economists, even though these individuals (especially the academics!) may not have technically caused the crisis (pp. 118, 274, 286, 289, 328). This Part examines the basis for Posner’s conclusions and traces their implications for policies to avoid future crises.

#### A. *Desperately Seeking Zebras*

Posner’s argument about blameless financiers is somewhat more plausible than his metaphor of lions and zebras would suggest. Posner does not mean to imply, for example, that financiers are evil beasts who only fear the lash.<sup>24</sup> He simply defends the role of “killer instincts” in business affairs. Market capitalism needs self-interest if individual profits are to coordinate supply and demand at efficient prices. Thus, greed may not quite be ‘good,’ insofar as it prompts theft and fraud alongside competition and hard work. But rational self-interest within legal limits is the engine of capitalist economics, and Posner will not hear it disparaged as an avaricious, immoral, “unquenchable thirst for easy profits” (p. 285). Easy profits are what market economics is all about.

Even if capitalism is a lion’s game, however, Posner’s metaphor seems misplaced in this context.<sup>25</sup> The crisis of 2008–09 was not marked by blood-thirsty lions munching on zebras. (Though we shall consider some lions who indeed made a killing.<sup>26</sup>) On the contrary, this financial hunt was ineffective, with most lions stalking shadows, biting their own paws, and then begging for handouts. As Posner notes, the downturn has brought its share of popular attacks on big business, and some of these have gone too far (p. xiii). Yet the real question in this crisis is not why financiers were so unkind, it is why they were so unwise. How could financial experts let such massive amounts of money disappear?

In considering this question, there is one category of explanation that Posner strongly rejects: that financiers made irrational mistakes. Of course some past business decisions now look rather dumb, but Posner insists that

24. *But cf.* p. 112 (dismissing as futile efforts to “alter the mentality or character of businessmen”). If taken too far, to insist on the intractability of businessmen’s ethical mindset might have grim implications for the regulation of fraud and other disfavored business practices. *See generally* KINDLEBERGER & ALIBER, *supra* note 1, at 145 (“Corruption can’t be measured unless an economy or a society has laws or norms or rules that distinguish permissible from illegal or immoral behavior. . . . Moreover within a country the laws and the norms about non-acceptable behavior change over time . . .”).

25. This Review offers no occasion for plumbing the metaphorical consequences of splitting the economic world into two species, nor for asking what sort of person might qualify as Posner’s “zebra.”

26. *See supra* note 21 and accompanying text (discussing the possibility that some financiers imposed “agency costs” and reaped significant benefits by pursuing their own short-term interests to the detriment of their employers’ longer-term interests).

negligibly few of them were caused by private decision makers' stupidity, emotional excess, or optimistic bias. Posner's hyperrationalist confidence is distinctive if not unique in this context. Many economic analysts, for example, invoke words like "mania," "panics," and "irrational exuberance" to represent emotionalized herd mentalities that seem to determine many financial trends.<sup>27</sup> A wave of studies in behavioral economics and finance proffers experimental evidence of cognitive biases and emotional reactions that unconsciously distort seemingly reasoned, deliberate decisions.<sup>28</sup> And even inexpert readers might imagine that financial decision makers' years of success with complex securities and risk-management bred confidence, which later became distortive overconfidence and arrogance.

Posner disagrees and expresses almost reverential doubts that "failures of rationality, or the intellectual deficiencies of financial managers whose IQs exceed my own were major factors in the economic collapse" (p. 77). Although Posner acknowledges that "[e]motion does play a role in the behavior of businessmen and consumers," he claims that emotion "is not necessarily or even typically irrational. It is a form of telescoped thinking" (p. 82). Unfortunately for Posner's argument, however, to characterize emotions themselves as "typically" rational—anger, elation, arrogance, and depression—is to strip those words of their recognized meaning.<sup>29</sup>

Posner's claims about irrationality mimic the atheist who, when asked about God, said "I have no need of that hypothesis."<sup>30</sup> Likewise, Posner labors to explain financiers' decisions in the crisis without resorting to irrationality. Where any private decision may be explained by reference to rational or irrational motivations, Posner chooses the former; and although this may seem like unproved dogma, I cannot myself debunk it. Information about the decisions and motives of private decision makers ranging from corporate officers to traders to investors to home owners is simply unavailable today. Instead of debating such hidden facts, this Section explores the

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27. See, e.g., KINDLEBERGER & ALIBER, *supra* note 1.

28. See, e.g., Hal R. Arkes & Catherine Blumer, *The Psychology of Sunk Cost*, 35 ORGANIZATIONAL BEHAV. & HUM. DECISION PROCESSES 124, 127–28 (1985); Werner Güth et al., *An Experimental Analysis of Ultimatum Bargaining*, 3 J. ECON. BEHAV. & ORG. 367 (1982); Daniel Kahneman et al., *Fairness and the Assumptions of Economics*, 59 J. BUS. S285, S291 tbl.2 (1986); Christine Jolls, *Behavioral Law and Economics* (Yale Law Sch., Pub. Law Working Paper No. 130, 2006), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=959177#](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=959177#).

29. There is one point where Posner seems more conciliatory about the possibility of irrational market behavior, as he suggests that "the line between the rational and the irrational is at best unclear." P. 85. But that claim is not, as Posner claims, a "reason for not placing much weight on the irrational aspects of economic behavior." P. 85. Nor would the fuzziness of the lines separating rational and irrational behavior support Posner's insistence that financiers exhibited none of the latter. For excellent background on emotions' connection to law, see Laura E. Little, *Negotiating the Tangle of Law and Emotion*, 86 CORNELL L. REV. 974 (2001) (reviewing THE PASSIONS OF LAW (Susan A. Bandes ed., 1999)). See also *id.* at 977, 988–90, 995 (discussing Richard A. Posner, *Emotion versus Emotionalism in Law*, in THE PASSIONS OF LAW, *supra*, at 309).

30. See p. 85 ("[T]he current depression can be explained without hypothesizing irrationality . . ."); p. 112 ("There is no need to bring cognitive quirks, emotional forces, or character flaws into the causal analysis."); see also ROGER HAHN, PIERRE SIMON LAPLACE 1749–1827: A DETERMINED SCIENTIST 172 (2005) ("I have no need of that hypothesis.").

policy implications of *accepting* Posner's ultrarational assumptions. If all market participants were indeed rational in 2008, what would that mean for preventing future crises?

To answer, let us consider four "rational" causes of the downturn, all of which seem plausible, and none of which is exhaustive or exclusive. This Section considers three factors associated with private actors, while the next Section focuses on the role of governmental errors. Posner's analysis does not offer great detail regarding different market-rational explanations of the crash. Yet each of these four appears at least briefly in his analysis, and each has important and distinctive policy consequences.

First, let us imagine that market participants were just extremely unlucky. Every contingency plan leaves unmet contingencies, and no one ever considers deeply "what's the *worst* that could happen?" If one imagines aggregate economic conditions as rolling a million dice, maybe this crisis was comparable to all snake eyes, an incredible bout of tough luck that any rational person would bet hard against.<sup>31</sup>

Posner sometimes hints that the economic crisis worked like this. For example, he compares the downturn to life insurance companies whose meticulous actuarial calculations are rendered useless by a nuclear blast.<sup>32</sup> And he stresses that the crisis was exacerbated by such improbabilities as a protracted presidential election, a lame duck president, and holiday shopping that was shortened by a late Thanksgiving (pp. 139–40). Of course, no one thinks that the crisis was *all* bad luck, but it is easy to think that chance played some part. And to that extent, one might wonder how policy makers should adjust to future episodes of unfathomably bad fortune. Phrased differently, how much should future governments pay to safeguard against rolling a million ones? Not much, it might seem.<sup>33</sup> There are plenty of catastrophes to worry over, and many of them seem more probably devastating than our million-dice hypothesis. Thus, if the economic crisis was just luck, the best preventive response might be no response at all.

A second rational cause of the crisis might be a deliberately chosen absence of information. Rational actors almost certainly lacked important information about economic conditions, and such ignorance may not have been simple oversight or mistake. Instead, market actors may have been unable or rationally unwilling to pay for such hypothetically salvific information. For example, our imaginary dice might have been secretly loaded to roll ones, but that fact itself might have been very expensive to

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31. The actual improbability of economic collapse is of course unknown; it might be much more or less likely than my million-dice hypothesis. I should note, however, that the higher the odds of crisis become, the less explicable it becomes for financiers to ignore them. To appease gambling specialists, I should also explain that rolling a million ones technically counts as a half-million pairs of "snake eyes."

32. Richard A. Posner, *A Failure of Capitalism: "Tail Risk," Economists' Predictions, and Credit-Default Swaps*, THE ATLANTIC, June 3, 2009, [http://correspondents.theatlantic.com/richard\\_posner/2009/06/tail\\_risk\\_economists\\_predictions\\_and\\_credit-default\\_swaps.php](http://correspondents.theatlantic.com/richard_posner/2009/06/tail_risk_economists_predictions_and_credit-default_swaps.php).

33. Technically, answering this question depends on how often and quickly the dice are rolled. If such frequency approaches infinity, then even tiny risks can be significant.

discover. Here again, rational market participants might bet heavily against rolling a million ones, despite failing to examine the seemingly normal dice. Under this scenario, the economic crisis was theoretically evitable, but it was not in fact avoided because the relevant information remained rationally undiscovered by market participants.

At first glance, readers might think that Posner's account minimizes the role of informational problems, because he insists that financially stretched banks "must have known" that they would collapse if housing prices sank by 20 percent (pp. 78–79). Even homebuyers must have known that they were buying in an inflated market and that they risked default (pp. 101–04). On the other hand, Posner suggests that market participants did not know the degree of "correlated risk" faced by the financial system, that is, the fact that multiple banks overinvested in the same real estate assets, or that AIG took on more of those risks than it could ever hope to cover (pp. 56–57). Perhaps such crucial facts were not known, even assuming rational market participants, because they were too expensive for uncoordinated individuals and entities to discover.

Insofar as informational deficiencies explain the economic crisis, the policy response is obvious. To overcome informational costs requires forced disclosure and centralized access, and although Posner mentions both solutions, there are devils in the details. For example, although historical economic analysis might reveal in the present crisis exactly what information was missing, when, and with respect to whom, it seems prohibitively hard to guess what essential information will be obscured the next time around. Today's informational silver bullet might turn to copper in future crises, and vice versa. Moreover, our current downturn accompanied efforts by market participants to manipulate less regulated entities and less regulated financial instruments (pp. 27–28, 44–46, 58, 110–11). Unless the government could somehow force disclosure of nearly all information about nearly all investors, any new regulatory regime must face similar risks of private avoidance and a sense of false security.

Another issue is whether information should be released to private markets, thereby exposing confidential investment strategies, or should be collected in governmental bureaucracies. Posner flirts with the latter as he briefly contemplates an economic Central Intelligence Agency (pp. 101–04). We will soon discuss the general costs and benefits of governmental involvement in economic affairs.<sup>34</sup> For now, it is enough that changing informational policy may sometimes help to avert future crises, but success is uncertain and complexities abound. This is because, unlike casino dice games, market economics is a decentralized global enterprise built on much trickier variables than the distribution of weight on a cube. The challenge for policy makers of deciding exactly what information is required, and of enforcing such rules, may be harder than Posner's analysis implies.

A third rational cause of the crisis is imperfectly allocated incentives. Posner analyzes part of this problem as "agency costs," where components

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34. See *infra* Section II.B.

of an organization pursue individual interests that may diverge from the organization's collective interest (pp. 222–23). For example, a trader might promote mortgage-based securities to maximize her commission-based salary despite potentially devastating risks to her employer. A different type of incentive problem concerns “external costs” or “externalities,” where decision makers ignore the impacts of their choices on other parties (pp. 106–08). For example, a bank might deny a credit applicant without considering that decision's full effect on the economy at large. This occurs because only some of the credit line's social value is captured by the bank's interest rate and fees.

From a certain point of view, agency costs—or even outright conflicts of interest—are analogous to the informational problems we have discussed. If employers or investors knew that employees and officers were abusing their interests, then they might react with appropriate hiring, management, or wage decisions. A rational employer might or might not choose to pay for costly bureaucratic mechanisms to control particular agents, but if one assumes full information on the subject, it is hard to see any special justification for governmental intervention. The real-world problem is that such information is not available. Firms often do not know which of their agents can be trusted and which cannot. And although they theoretically could learn such information and respond, the costs of doing so are often too great in practice.

Managing externalities is perhaps the classic justification for governmental regulation. For example, the massive spillover effects that flow from healthy or unhealthy financial institutions are the basis for current banking regulation, and similar arguments might support much more of the same. As Paul Krugman wrote: “[A]nything that has to be rescued during a financial crisis, because it plays an essential role in the financial mechanism, should be regulated when there *isn't* a crisis so that it doesn't take excessive risks.”<sup>35</sup>

A major catch for externality-based regulation, however, concerns its limits. In an interconnected economy, everything has external consequences, from banks to automobile-makers to law schools to coffee shops. Determining whether external costs support particular regulatory efforts is more complex than simply identifying an externality, or even identifying a big one—though those steps can also be controversial. The other side of such regulatory equations is the effectiveness of governmental response, which the next Section considers in detail.

### B. *Damned Zookeepers*

A fourth rational-markets explanation for the crisis is governmental error. Posner particularly identifies for criticism the deregulation of financial institutions and permissive monetary policy (pp. 46–47, 105). In his view, these mistakes allowed and encouraged financial institutions to make risky

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35. KRUGMAN, *supra* note 6, at 189–90.

investments without adequate reserves. Because banks and other financial institutions were freed from regulatory reins and flushed with easy money, they undertook excessive debt and pursued high-interest, high-risk investments. Posner does not absolve banks of their *responsibility* for making such decision, but he does shift the *blame* for the economic crisis to governmental agents.

Posner's stark double standard for private and public decision makers seems unsupported. I have already suggested that a "high-altitude" narrative cannot dispel impressions that market participants acted irrationally during the crisis.<sup>36</sup> More importantly, the previous Section's three hypothetical arguments for rehabilitating private actors' rationality can also be applied to public officials. Recall, for example, the possibility that rational private actors were wildly unlucky, the victims of unimaginable improbability. If that "tough luck" defense is used to exculpate corporate officers, traders, investors, banks, insurance companies, and mortgagors, why not public servants? Indeed, I have argued the opposite: If the crisis rose from simple and extraordinary bad luck, then to add future governmental safeguards against remote improbabilities of this scale might be impossible and unwise. Likewise, the absence of governmental safeguards *in the past* against rolling a million ones should merit only light blame or none at all.

Our second hypothesis was that private actors might have blamelessly lacked information that was too expensive to gather. But one must also consider informational problems facing the government. Posner knows that it is easy with hindsight to argue that financiers should have seen that their investment choices were foolish. Yet if one rejects overinformed second-guessing with respect to private actors, there are again parallels for government actors. Indeed, a parity between private and public officials is especially apt given the revolving door among private and public seats of authority (pp. 238–40). Many private financiers believed (rationally or otherwise) that real estate markets would not destroy global financial markets, and such individuals did not abandon those beliefs as they took public office. Just as private actors continued to invest, following prior success without knowledge that failures were imminent, public officials continued to lower interest rates, deficit spend, and deregulate, following prior precedents and ignorant of the coming crash. In hindsight, neither private nor public actors seemed to plan enough for contingencies that they all failed to predict.

As a side note, let me stress that comparisons to private actors do not neglect the government's special, though narrow, role in collecting and distributing certain market information. What is unknown, however, is whether the hypothetical silver bullet of information that would have let rational market participants avoid the economic crisis was within or without the

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36. See *supra* note 30 and accompanying text (comparing Posner's belief in rational markets to the faith of a zealous atheist).

government's responsibilities.<sup>37</sup> Working from Posner's low-resolution narrative of what happened, it is altogether possible that the missing information was some tightly guarded, confidential secret firmly gripped by private hands and inaccessible to any legally authorized inquiry.<sup>38</sup> Thus, it is not clear whether any "moral" duty to discover salvific information rested with government bureaucrats or with comparably bright, inquisitive, and motivated private information-seekers. Whereas the government's responsibilities appear in statutes and regulations, a financial lion's duty under market economics is to make rational decisions and help produce wealth. And however hard it may be to believe market actors met that duty in 2008, if we accept Posner's assumptions about market rationality, we should reconsider his implication that the government should be "*blamed*" for not discovering and acting upon information that market participants also did not discover or act upon.

Under our third rational-markets hypothesis, private and governmental actors are also comparable with respect to misaligned incentives. We have seen that agency costs can be recharacterized as informational costs, in the sense that rational actors use flawed incentive structures because they lack knowledge that employees will abuse their employers' interests.<sup>39</sup> Such logic applies equally well to governmental decision makers, who also cannot guess how financial employees might abuse their employers.

The other incentive problem, externalities, might seem quite different for private and public actors. Externalities are classically viewed as effects on social welfare that private actors cannot be expected to contemplate, and for which public officials are thus the only hope (pp. 107–08). From the government's perspective, however, externalities are extremely hard to distinguish from "internal costs" that—under a capitalist system—must be managed by private actors. Consider banking: the availability of credit carries massive consequences for businesses throughout the economy, and some of those effects are not fully conveyed by interest rates and fees. Does that mean that the government should manage every American credit transaction? Not at all. Would-be regulators have the unenviable task of identifying externalities, accompanied by the even-less-enviable task of addressing such problems without distorting "internal" costs allocated to the private sector (pp. 236–37). Indeed, insofar as one criticizes government for *not* making good decisions with respect to the crisis of 2008, that may prove hard to reconcile with suggestions that government should become more involved in business affairs and managing externalities. An economic

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37. Of course, I understand that the *Economist* and Roubini predicted the housing crisis and the bubble. Pp. 123–26. Yet the information that remained hidden is what, by hypothesis, would have been sufficient to *persuade* decision makers that such predictions were factually correct.

38. Cf. p. 144 ("Investment banks, hedge funds, mortgage originators, and other financial firms conceal information about business strategies that might help competitors, and avoid, as far as the law permits (and sometimes farther than it permits), disclosing adverse information about the firm's prospects.")

39. See *supra* Section II.A.

surgeon with shaky hands and a kitchen knife sometimes acts best by acting least.

### C. Learning to Run Our Zoo

My goal is not to debate the factual accuracy of Posner's assumptions about market rationality or governmental effectiveness. Instead, I merely flag such issues because any strong belief in the rationality of market participants narrows available reasons to explain the crisis, and also narrows policies to prevent future crises. A crucial task for quantitative and anecdotal researchers is to explore empirically—as Posner's book does not—whether market participants *actually were rational* in 2008, and whether public officials discharged their responsibilities so poorly that the scope of regulatory and monetary governmental activity should be trimmed.

The risk of accepting Posner's analysis at face value is that it applies unduly high standards of rationality and low standards of social value to private market participants, while applying opposite low and high standards to governmental actors. For Posner, market agents are defensibly uninformed, and after all, lions will be lions. Yet governmental agents are "blamed" for their imperfections and seem duty bound to save us from ourselves.

Without detailed information, the truth seems more moderate. Perhaps some causes of the crisis could have been known and prevented by market participants and the government alike; other factors may have been foreseeable and avoidable for one group or the other; and some factors may have been unknowable and unavoidable for everyone involved. Financial and macroeconomic historians may someday discover the truth about who is responsible and who should be "blamed." Even today, however, it seems obvious that neither government officers nor markets are perfect, and analysis of long-term safeguards must not expect them to be so.

## III. BIG GOVERNMENT, ONLY BRIEFLY

This Review has thus far addressed Posner's backward-looking account of how the current crisis happened, and forward-looking ideas for preventing future crises. By contrast, this Part considers Posner's proposals for our current economic recovery.

Crucial to Posner's policy analysis is his effort to distinguish "recessions," which happen somewhat regularly, and true "depressions" like the 1930s and today (pp. 9–11). To combat *recessions*, Posner implies that the government should not do that much (pp. 9–10). Low interest rates and deficit spending, for example, are among Posner's main causes of the modern crisis (pp. 29–34, 105). He explains that, in trying to lift the economy out of modest downturns, the government made credit too easy and thus helped to inflate a destructive housing bubble.

By contrast, Posner believes that government must be quick and aggressive in responding to *depressions*, using a combination of interest rates and

fiscal policy to staunch deflationary risks at nearly any cost (pp. 1–7). Posner warns that if deflation were to take hold, that could spark a devastating cycle of reduced spending, production, and employment. And such risks can be especially alarming when financial institutions are threatened because the main tools of federal monetary policy operate through the banks. If banks are unwilling to lend, then the Federal Reserve may be unable to increase credit and spur economic recovery by giving them more cash. In circumstances like these, stimulus through government spending becomes even more important (pp. 63–68).

For readers who see Posner as an economic conservative, his embrace of deficit spending will draw close attention.<sup>40</sup> Indeed, Posner’s main criticism of government programs before February 2009 concerns their delay and mildness (pp. 68, 149–50, 168–69, 180, 187). Posner also discusses the then-pending American Recovery and Reinvestment Act of 2009, which attempts stimulus through a mix of tax cuts, public-works programs, and transfer payments such as welfare and unemployment benefits.<sup>41</sup> Posner supports such legislation as an extraordinary measure made necessary by extraordinary circumstances.<sup>42</sup>

Despite the undeniable political appeal of tax cuts, Posner criticizes them as the mildest, least desirable form of depression relief because they take effect only slowly and may prompt greater savings instead of greater spending (pp. 165–69). On the other hand, Posner finds that public-works spending, even when directed to “worthless projects[,] can be an effective and, paradoxically, a rather cheap response to a depression” (p. 177). He also endorses transfer payments, despite severe reservations that political forces can make welfare programs destructively persistent after a depression has ended (pp. 169–70).

It is all too easy to judge Posner’s proposals by reference to conventional politics. Readers who support the Obama Administration and liberal economics might embrace Posner’s analysis as a welcome contribution.<sup>43</sup> Others might attack Posner as a dismissibly false conservative, whose professed pragmatism is just a fig-leaved lean to the left.

My concerns with Posner’s distinction between recessions and depressions are more conceptual and practical in nature. Although Posner acknowledges that economists lack an established definition of the word “depression,” his book offers the following: “I would define it as [1] a steep reduction in output that . . . [2] threatens to cause deflation and creates [3]

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40. See, e.g., Robert M. Solow, *How To Understand the Disaster*, N.Y. REV. BOOKS, May 14, 2009 (reviewing *A Failure of Capitalism*).

41. American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, 123 Stat. 115.

42. Posner thus rejected “pure monetary” solutions, and “automatic stabilizers” of reduced income tax, increased unemployment benefits, and ordinary market forces that might ordinarily take up economic slack. Pp. 170–71, 202–07.

43. Cf. Solow, *supra* note 40 (discussing *A Failure of Capitalism* in the context of the Obama stimulus package).

widespread public anxiety and, [4] among the political and economic elites, a sense of crisis that evokes extremely costly efforts at remediation” (p. x).

Posner’s eagerness to define the indefinable owes to more than exuberant iconoclasm at breaking “taboo[s] in respectable circles” (p. ix). Posner defines and persistently uses the term “depression” because for him—at a personal level if nothing else—it marks an economically and biographically important distinction. “[N]o one who has lived through the modest downturns in the American economy of recent decades could think them comparable to the present situation” (p. ix). And never before has Posner promoted such massive governmental intervention in the economy. Hence the pressing need to differentiate recessions and depressions.

Posner’s subjective ‘Wow!’ may not represent an enduring contribution to economic analysis, and his distinction between recessions and depressions has become only more elusive as time has passed. When Posner wrote in February 2009, he could not know that economic conditions were leveling off, and that some indicators would soon improve. Thus, although Posner was careful to avoid suggesting that the modern economy would suffer protracted unemployment like the Great Depression, his very commitment to using the word “depression” now seems a bit dramatic.<sup>44</sup>

Not only does the current crisis seem hard to categorize as a “depression,” rather than a “severe recession,” but Posner’s definition also presents a more generally awkward tool for economic analysis. Imagine, for example, a future economic downturn. Consistent with Posner’s first two criteria, output declines rapidly, and (as is quite normal) that decline “threatens” deflation. Policy advisers wish to know whether to implement depression-appropriate governmental intervention, or to embrace recession-appropriate constraints. Under Posner’s definition, such advisers can do no more than gauge the public’s “anxiety” and elites’ “sense of crisis” (p. x). By logical extension, there is a risk that if elite politicians decided to *treat* an economic downturn as a depression, by proposing major governmental interference and stirring public response, then the downturn might be *defined* as a depression regardless of economic realities.

The problem with Posner’s definition is that it identifies depressions based principally on emotional reactions. For other economic analysts, emotional circumstances might indeed be crucial, as harbingers of a panicked stampede, which in turn might tilt an ordinary downturn toward a crash. A main theme of Posner’s analysis, however, is that our depression does *not* stem from irrational panic, and that the explanatory force of private parties’ irrationality is at most marginal. Thus, my concern is not just that policy makers cannot apply Posner’s definition of depression. The definition’s psychological focus seems contrary to Posner’s assumptions about market rationality itself.

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44. The quotation that begins this Review illustrates the point. Posner writes that “We may be too close to the [economic crisis] to grasp its enormity.” P. vii. It might seem less sensational to suggest that we’re too close to grasp the downturn’s enormity *or its mildness*.

Posner's wavy line between recessions and depressions also affects his approach to Part II's safeguards against the next crisis. Although Posner accepts that *government spending* in a depression will inevitably be hurried and inefficient, he sees no benefit in hurried, imperfect changes in *regulatory policy*. In the short run, Posner not only opposes "reorganization" of financial regulations—to solve what he describes as "fragmentation of regulatory authority, . . . turf wars, yawning regulatory gaps . . . , and an inability to aggregate and analyze information"—he also opposes quick "reregulation" of the financial industry to remedy the decades of "excessive deregulation" that helped cause the current crisis (pp. 289–91). On the contrary, Posner in the near term proposes only "piecemeal reforms" that, by his own account, are nothing more than "pretty small beer" (p. 296).

The proffered explanation for Posner's antireform reluctance stems from his view that we are in a depression, a true "economic emergency" that has overtaxed the government's intellectual resources and foreclosed any adequate regulatory response.<sup>45</sup> Posner also more cheerily suggests that the "government responses to the depression that are, or soon will be, under way are enough for now" (p. 303), and that President Obama's "regime change" needs a chance to "show what it can do within the existing regulatory framework."<sup>46</sup> As we shall discuss in the Conclusion, there is more at stake in Posner's analysis of reregulation than he lets on. For present purposes, however, one may simply question how policy makers can ever know when the elusive 'right time' for reregulation and reorganization has arrived. If the government waits until our current "depression" fades to "recession," using Posner's definitions, we may face a long and perplexing wait indeed.

Perhaps Posner never meant for his definition of depression to be taken so seriously; maybe it was never intended to describe a stable category, much less to guide economic policy making. Yet even for a generalist and inexpert audience, Posner's undertheorized line between recessions and depressions is unhelpful. Among the most important lessons from this crisis is the immense difficulty for public and private actors in trying to determine the seriousness of economic problems and how to respond. If Posner neither identifies depressions accurately, nor fully acknowledges policy makers' challenge in doing so, then the lasting value of his approach must shrink accordingly.

#### CONCLUSION: HISTORY AND HINDSIGHT

Although this Review has stressed my concerns and disagreements with Posner's book, what matters more are our similarities and common ground. For example, Posner and I both focus on three central topics: what caused this crisis, what might prevent future episodes, and how to promote

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45. *E.g.*, pp. 251, 291, 302, 330.

46. P. 293. The most that Posner is willing to consider is a 9/11 Commission for Economics, p. 228, though he has elsewhere taken a notably dim view of the actual 9/11 Commission's work. *See* pp. 249–250, 291. *See generally* POSNER, *supra* note 22.

economic recovery. This Review's last, almost indelicate topic is why such vital economic questions should be analyzed by a Seventh Circuit judge, or by a simple law professor like myself.

Professional macroeconomists are, in Krugman's words, "quite capable of writing books that no one can read," but they also write prose that is clear and accessible.<sup>47</sup> Business academics have similar qualifications, and the front-line perspective of financial journalists and business people can also add value.<sup>48</sup> Given this abundance of credentialed talent, what role is left for inexpert commentary like Posner's book and this Review?

Although Posner directly considers this "why me" question, his two-part answer needs elaboration. First, Posner laments a dearth of substantive analysis that is not jargoned or "insiderish" (p. xiv). Taken literally, however, this argument overlooks experts who write with grace, and it makes a virtue from outsiders' necessary lack of expertise. Second, Posner claims that many expert authors have "an axe to grind" (p. xiii). But such attacks on the motives of expert authors seem almost uncharitable, and perhaps naive about Posner's own intellectual purity.

This Conclusion expands each aspect of Posner's self-defense, and offers his book as living proof that intellectual lawyers can contribute to macroeconomic debates despite an embarrassing deficit in credentials. First, on the subject of "insiderism," lawyers are analytical generalists by tradition and training. The structure of the United States judiciary is remarkably lacking in specialization, for example, and fields of legal scholarship and education are far less regimented than other intellectual disciplines. As a result, even the highest levels of legal discourse emphasize accessibility to an arguably hypothetical audience of interested, intelligent, yet also inexpert readers. Posner has made his career—indeed he has made several careers—as an unsurpassed practitioner of this art, synthesizing and digesting hitherto unfamiliar topics into increasingly comprehensible forms.

Nor is Posner's generalism the mere absence of technical lingo or unintelligible arcana. His eclectic range of experience lets him confront new materials with a mix of confidence and self-criticism that mirrors the attitudes and aptitudes of idealized lawyers, professors, and students. As a true champion of lawyerly generalism, Posner has sparked debates with economists, philosophers, historians, psychologists, and many others. In none of those discussions has Posner possessed the specialized expertise of other commentators. Yet his analytical and critical talents have made his contributions consistently useful, without the need for field-specific originality or narrowly focused scholasticism.

*A Failure of Capitalism* exemplifies Posner's virtues as an academic generalist, as the book elevates discussion of our economic crisis above any sensationalist "orgy of recrimination against Wall Street" (p. 285). Posner thus offers a self-conscious effort to transcend populism without alienating a

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47. KRUGMAN, *supra* note 6, at 6. Krugman himself is a writer of enviable liveliness and clarity.

48. See, e.g., *supra* notes 6–7 (collecting sources).

popular audience. And like much legal discourse, his book's greatest success lies in its implicit invitation for readers to explore unfamiliar territory and question authority, including Nobel laureates, Federal Reserve chairmen, and even Posner himself.

Posner's second self-defense, his promise not to grind axes, is accurate only to an extent. On one hand, even skeptical readers must admit that Posner's economic analysis is not driven by party allegiance; his critique of government officials applies to Democrats and Republicans with comparable vigor.<sup>49</sup> Nor is Posner captured by debates over monetarist and Keynesian economic theory.<sup>50</sup> In discussing macroeconomic crises, these can be thick chains to break, and Posner is justifiably proud to be free of them.

On the other hand, one cannot say that Posner writes without agendas and precommitments.<sup>51</sup> The fingerprints of his attraction to market capitalism, for example, appear throughout this book, and its penultimate chapter, "The Future of Conservatism," leaves no doubt about the author's points of focus (Chapter Eleven). Yet even if his work is not quite immune from intellectual hobbyhorses, Posner's pet projects remain distinctive and interesting. As I have suggested, Posner's account seems driven by a Free Marketeer's passion for deregulation and unencumbered business, yet his argument is in no sense extreme or facile.<sup>52</sup> Posner's book may thus be criticized by conservatives for going too far and by liberals for not going far enough—a range of critique that I suspect will please the author very much indeed.

Only future events will demonstrate whether Posner's equipoise is real or merely apparent. As we have seen, Posner does not allocate *any* blame to private market participants. Also, even as he endorses short-term governmental intervention to end the current crisis, he is quick to speculate about the economic aftereffects of doing so (pp. xi, 207). This leaves the distinct impression that governmental market interference is typically counterproductive and should be studiously avoided except under the exceedingly rare circumstances of a depression. It would be unfair to cast such arguments as seeking to restore small-government, "Chicago-School" deregulation as soon as our immediate crisis has passed. But we could say that Posner leaves that door conspicuously open.

Concerns about Posner's promarket ideology are only furthered by his claim that the government should do very little to regulate the financial industry until a "9/11 Commission" is convened to study the crisis (p. 228). This was the proposal of failed presidential candidate John McCain, and it

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49. See, e.g., p. 243 ("The government's inaction was . . . the product of a free-market ideology shared to a considerable extent by the Clinton Administration, and for that matter predecessor administrations going back to the 1970s, when the movement to deregulate the financial industry began. This ideological commitment was carried to new heights by the Bush Administration . . .").

50. E.g., pp. 211–12, 313–14.

51. Posner defends at least some of his precommitments under the heading of "Bayesian" priors. Pp. 310–11.

52. See *supra* Part III (discussing Posner's analysis of active government in fostering economic recovery).

seems to lack appreciable support today.<sup>53</sup> Posner's asserted need for a period of political cooling may, as he suggests, avoid errors in new financial regulations (p. 250). But Posner also knows that it may also lead to complacency, as politicians are famously hard to energize after a crisis has passed (pp. 250–51). To paraphrase Donald Rumsfeld, the public must always regulate using the government we have, not the government we want.<sup>54</sup> As a theoretical matter, we could wait for technocrats who pursue the public good but are unswayed by public fevers; however, in the economic context as elsewhere, regulation delayed is often regulation denied. Insofar as Posner's economic analysis categorically prefers governmental inaction over regulatory imperfection, that might redeem Free-Market microgovernment through the back door, despite his endorsement of substantial—though temporary, rare, and destructive—measures for economic recovery.

To clarify the role of economic ideology in Posner's analysis, consider two contrasting metaphors. Posner describes the role of leveraged investment strategies in the current crisis as analogous to navigating a canoe (pp. 131–32). He says that investors leaned increasingly far, causing the economy's financial vessel to tilt gently, until an invisible tipping point was reached and the canoe capsized. The moral of that story is quite simple: don't lean so far out of the canoe, and everything will be fine. This is a tale of capitalist perfectability, and it offers a comforting image of easy solutions near at hand.

But what if economic health is less like a canoe than a bicycle? When one begins biking, there are often training wheels, thick tires, an upright seat, and sturdy steel construction. All of these features make biking slower and easier, which helps avoid dangerous crashes. As one gains experience, however, the training wheels come off, and a wide variety of other improvements become available to make life faster and more hazardous. Clipless pedals and narrow tires are useful examples, along with efforts to shave weight off of frames and components. This Review is no place to discuss the economic significance of globalization, securitization, and other forms of financial sophistication as potentially helpful but dangerous upgrades to our capitalist bicycle. Yet it is at least clear that, for complex reasons, the field of modern finance has absorbed an ever-increasing amount of money, and has done so with the aspiration of allowing such capital to flow more quickly, efficiently, and profitably than ever before.

Under the biking metaphor, advice about economic crises may be less conceptually simple. Of course, one should ride safely, use a helmet, and suchlike. But if it is important to go fast—for an economy to grow and individuals to thrive—then a certain fatalism may also be appropriate. Even

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53. Rick Klein, *McCain Blames Greed for Wall St. Mess; Obama Blames GOP*, ABC NEWS, Sept. 16, 2008, <http://abcnews.go.com/Politics/5050/story?id=5812268&page=1>.

54. Eric Schmitt, *Iraq-Bound Troops Confront Rumsfeld Over Lack of Armor*, N.Y. TIMES, Dec. 8, 2004, at A1.

good riders have accidents, and sometimes the only hope is for good luck, a soft landing, and a quick remount.<sup>55</sup>

Yet there is one noteworthy problem with my biking metaphor. Unlike a biking accident, our national and global economies may be so highly stratified that the person who “rides” during good times is not always the same person who “falls” during bad times. Questions about distributing capitalist wealth have often been a sticking point for Free Marketeers, and Posner mentions such matters only briefly in his book.<sup>56</sup> We do not yet know exactly who profited during the housing boom, nor exactly who lost during the downturn. And this may seem unsurprising, for in times of true “crisis,” questions of survival and recovery often trump questions of distribution or fairness. As the crisis abates, however, the latter questions deserve much closer study than Posner’s framework suggests.

This brings me to my last comment about Posner’s book: its unrelenting commitment to speed. One review of *A Failure of Capitalism* aptly observed that “Judge Posner evidently writes the way other men breathe,”<sup>57</sup> and a main reason for Posner’s writing this book may simply be that he can. There are of course many issues that Posner could not explore under his self-imposed time pressure, and we may all trust that slower scholars may revise and reinforce Posner’s arguments as future circumstances require. What Posner accomplished by getting his analysis out quickly, however, was to establish himself as a contemporary public voice on macroeconomic issues. Indeed, although many authors have advertised books in blog postings, Posner may be the first legal scholar ever to advertise blog postings in the preface to his book (pp. xvii-xviii). Even before the book’s official release, Posner began writing for *The Atlantic* as a web correspondent. Two months and nearly 60,000 words later, Posner has made himself a focal point for public discourse. He now fields e-mail messages from Alan Greenspan and writes economic commentary for the *New York Times*. And although Posner will not have the last word on any of the topics he has undertaken—that will be left to a future when “hindsight will rewrite history” (p. xvi)—we all benefit from the engagement of his prolific and impressive intellect in matters of macroeconomy.

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55. Cf. ROBERT F. BRUNER & SEAN D. CARR, *THE PANIC OF 1907: LESSONS LEARNED FROM THE MARKET’S PERFECT STORM* 173 (2007) (“Though it is uncertain when and where they will align to produce a crisis, history emphasizes that financial crises occur without respect to the nature of regulations or the institutions they govern. One of the most dangerous statements in the markets is, ‘This time it’s different.’ We doubt that history will repeat itself in exactly the same way as 1907, but the drivers we generalized from that crisis can and do recur.”). Perhaps it would not mean that much to temper Posner’s analysis with a dose of fatalism. After all, Posner writes that “[c]apitalism will survive the current depression as it did the Great Depression of the 1930s. . . . because there is no alternative that hasn’t been thoroughly discredited.” P. 234. And so long as one uses a broad definition of what counts as “capitalism,” he may be right.

56. Cf. pp. 226–27, 300–01 (proposing to increase rates of personal income tax).

57. Solow, *supra* note 40.

