

# **THINKING ABOUT THE FINANCIAL AND ECONOMIC CRISIS: SOME BRIEF NOTES ON ITS CAUSES AND REMEDIES**

Ricardo F. Crespo

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An economic crisis is an unexpected phenomenon with strong consequences for nations, institutions and people's wealth, habits, and behaviors. It departs from the 'normal' evolution of the affairs foreseen by economic theory. It makes the claim for new theoretical explanations. It surprises the economic agents (individuals, firms and governments) that try to ascertain what kind of phenomenon they are facing in order to decide the appropriate actions to undertake. It calls for revisions of theory, plans and expectations. Overall, a crisis calls for an explanation which clarifies its causes.

This is not an easy task. Social phenomena are not easily analyzed given their complexity. John Maynard Keynes, an expert in economic crisis, has frequently warned about the reflective, complex, variable, heterogeneous, discrete, discontinuous, and incommensurable character of the social and economic material. These traits make explanation by causes and prediction highly difficult.

Throughout centuries of philosophic thought, social philosophers have held a wide range of social ontology and methodology positions. They go from social atomism – a position that social phenomena are the sole result of compiling individual

actions – to social holism – a position that the social realm has its own rules and characteristics independent of the rules and characteristics of the individuals who composed it.

Notwithstanding, beyond our position on social ontology, it is clear that social phenomena are, at least, intricate phenomena. Thus, any analysis of the current financial and

economic global crisis must search for a web of causes. Consequently, it is really surprising that the analysis and proposals of solutions to the crisis have been up to now mainly technical. We should also be cognizant of other kinds of causes and the need for other kinds of remedies.

#### Five levels

In this paper I will consider five levels of causal analysis progressively deeper but simultaneously complementary: technical, psychological, moral, historical, and philosophical. There are probably other perspectives – e.g. cultural, ethnic, sociological – I think, however, that those five levels will sufficiently help to expand our vision of the crisis.

#### Technical level

Most of today's opinions on the crisis focus on this level which, while real, is likely the most superficial. A set of techniques, as systems of financial evaluation, accounting norms, incentive systems, and low interest rates, fostered the evolution of the crisis and made its detection difficult. Agents, like horses with blinkers, went on directly and unavoidably towards the cliff without major accountability. They generated growing vicious cycles that nobody individually and intentionally created. Friedrich Hayek speaks about the 'spontaneous order' that rather automatically emerges in societies as soon as the information disseminates and as people

adapt to the conditions meant by this information. Paraphrasing Hayek, we can also speak of 'spontaneous disorders'.

### Psychological level

There are a lot of references to the optimistic climate of the ups and the mass behaviors or panics during the downs. These feelings exaggerate the movements that deal with the crisis. The aversion to risk is a strong sentiment which accelerates the fall. The crisis is a crisis of confidence. Keynes was also an expert on the feelings that exert influence on economic agents: innate urge, whim, fear, sentiment. For him the crisis would not have been something new and surprising. This is a point also exploited by a new economic current: behavioral economics (Daniel Kahneman, Amos Tversky, Richard Thaler). Robert Shiller is one of the current economists who has emphasized the role of psychology in the present crisis.

Psychology not only accelerates the crisis but also makes it difficult to overcome it. People fear spending money and thus reinforce the fall. This is why Keynes advised promoting public spending in order to sort out the problem. We need to recover confidence and this greatly depends on what people can perceive. We need to send signs of confidence. Timing is crucial; as time goes by people forget their failures.

Psychology, however, is not the ultimate root of the crisis. Artificial hopes and fears would not have arisen if some events had not motivated them. We need to deepen the analysis.

### Moral level

The President of France, Nicolas Sarkozy, for example, developed a moralist discourse on the crisis. Muhammad Yunus and Joseph Stiglitz also stress morality. Amartya Sen refers to a moral and legal vacuum. We hear of fraud, short-term views, irresponsibility and greed. However it should probably be added that in this crisis there is much mediocrity, work badly done. A lot

of people realized that something was not working quite well but they did not want to stop to think about it (laziness or their complicity with egoist or pragmatic concerns won them over). On the contrary, from a moral point of view, we need a set of virtues to ensure a prosperous economy: as laboriousness, excellence, frugality, thrift, honesty, and a spirit of service.

This is a relevant point because we cannot solve moral problems with technical remedies. This is why regulations only intended for control are not the only way out; they may even be a refuge for the unscrupulous. Regulations seem to be helpful when they also aim to shape virtues and characters, which is what is apparently lacking. Even some people question or assert that the crisis stems not from a lack of intervention but from the very intervention of states in the economy. Following this thread virtues are shaped more efficaciously by education, understood in the Greek sense of *paideia*, the shaping of character, than by regulation. At least, regulation must be complemented by actions that foster morality. Uncontrollable passions, however, are always present in humankind. Why then do we not live in a perpetual state of crisis?

#### Historical level

This level is probably not deeper than the other but concurrent. Without falling into historical reductionisms we must take into account that the historical character is a clear aspect of the humanity. Human time is different from the mere passage of natural time.

The historical analysis may be tackled in two ways. First, carrying out a survey on the facts that led to the crisis: technical elements, mistakes (mere errors or moral mistakes) of persons or institutions, psychological individual or massive reactions, fortuitous facts; there is a history of the crisis. Undoubtedly, this description will help to clarify it.

Second, we must consider the phenomena of the enlargement or shortening of human time produced by human expectations.

After the crisis, many scholars have begun to wonder why some actions were not taken before. Indeed, there were some voices that had warned about an imminent decline and nobody had denied the need for the actions they had proposed. However there is a matter of timing. The Ancient Greeks used the term *kairos* that means the opportune time. We need to learn how to discern the adequate moment to act.

Besides, the speed of contemporary life, its 'instantaneism', induces 'short-placism', oblivion of the past; we are anchored in the present. This acceleration of time goes against calm and serenity, attitudes lacking in the crisis.

#### Philosophical level

The previous historical analysis feeds into a philosophical perspective, mainly anthropological. This crisis manifests the futility of an excessive reliance on instruments. Students of master degrees want to learn almost exclusively the use of tools. Plato in the *Protagoras* has warned about this desire of replacing uncertain hazard by the predictability of technique. This undertaking is partial and is thus unrealistic. It may be dangerous, reminiscent of typical movies in which Faust-like experiments get out of control. To think that technique is the only rationale (including the market as conceived by standard economics), is fascinating for its simplicity and pragmatism but it is a problematic simplification. The only part of humanity able to be analysed in only technical terms is pure biology. In the human realm psychological and moral rationalities, not to mention cultural and ethnic factors, are more important.

The success and exactness of technique are attractive and have pushed former moral sciences – ethics, politics, economics – to a greatly technical development. We should remember that this technical development is partial. From a descriptive or explicative point of view it is insufficient. From a normative point of view technical (or instrumental) rationality must serve the ends of

practical rationality which is the uncertain rationality of real human actions.

#### The role of the economists

Economists were the stars of the crisis. They are supposed to be the experts in these affairs and to be the guardians of prosperous economies. The crisis was predicted by only a few of them and the economic academia did not convincingly and timely warn about the dangerous situation. This is because economists are not used to considering more than the technical aspects of phenomena.

Thus, in regards to their education, it would be important to expand the content. Economics should not be taught in isolation but rather within the framework of a school of social thought. Before technical tools economists should learn Political Philosophy, History, Sociology, Psychology, Anthropology, and Moral Philosophy. Lionel Robbins, who coined the most common current used definition of economics (a technique of allocating means to satisfy given ends), realized and proposed these enhancements. Great economists were great because they were humanists first and foremost: for example, Adam Smith, John Stuart Mill, Carl Menger, Ludwig von Mises, John Maynard Keynes, Friedrich von Hayek, Joseph Schumpeter, and Herbert Simon. We need humanistic economists.

#### Conclusion

Current policies concerning the crisis are focusing on technical instruments. In order to provide sustainable remedy for the crisis they should ponder this whole web of causes and their corresponding remedies. Psychological, moral, cultural and historical causes need psychological, moral, cultural and historical remedies, not only technical because they all are at the root of the crisis and technical causes are more superficial than these. If we only tackle the crisis by regulations and public spending it will surely repeat itself.

The crisis is a manifestation of an attitude of people toward their own life. A worldview that assigns technique an exaggerated subsidiary role by relying on it more than is sensible; this induces a separation between moral life and business and therefore leads to irresponsibility. The technical instruments, lacking conscious human reflection about their limits and responsible use, rather automatically take the first steps toward crisis; current 'instantaneism' and human psychology aggravate the situation. Little disorders finally lead to a general spontaneous disorder: we have a crisis.<sup>1</sup>

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#### Note

<sup>1</sup> I am indebted to Juliet Kunkel for stylistic corrections of a former version of the paper.