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The End of Growth was officially released this week! To celebrate, this month's Museletter includes a new extract from the book, along with our accompanying animation Who Killed Economic Growth. Finally I have included a new piece encouraging a positive political response to the economic crisis.

Haircuts for All . . . or Free Money?

From The End OF Growth Chapter 6

To get past the wall of potential financial-monetary collapse, governments would have to resort to extraordinary emergency measures. In the best instance, this would create time and space to begin coming up with long-term, infrastructural responses to declining energy supplies and climate change—responses involving the redesign of transport systems, power generation and transmission systems, food systems, and so on. Of course, there is no guarantee that time, once gained, will be well spent. Nevertheless, in principle the wall can be traversed.

The essence of the wall is this: We have accumulated too many financial-monetary claims on real assets—consisting of energy, food, labor, manufactured products, built infrastructure, and natural resources. Those claims, essentially IOUs, exist in the forms of debt and derivatives. Our debt cannot be fully repaid: every dollar saved in the past is owed ever-multiplying returns in the future, yet the planet's stores of resources are finite and shrinking. Claims just keep growing while resources keep depleting—and real prices of energy and commodities have begun rising. At some point it will become clear that this vast ocean of outstanding claims will never be honored, and the result could be a tidal wave of defaults and bankruptcies that would sweep away most of the economy.

In theory, as Harvard economic historian Niall Ferguson points out, there are six ways of resolving a debt crisis: (1) increasing the rate of GDP growth; (2) reducing interest rates; (3) offering bailouts; (4) accepting fiscal pain—reductions in benefits and standard of living; (5) injecting more money into the economy; or (6) accepting defaults, "including every type of non-compliance with the original terms of the debt contract."[1] If the premise of this book is correct and it has become nearly impossible to grow GDP, then we can eliminate option (1). Interest rates (2) cannot realistically be reduced lower than zero, which is essentially where they are now (for banks—though credit card interest rates are still in the range of 20 percent). As the debt problem worsens, bailouts (3) become more expensive and less effective. The austerity option (4) is distasteful to everyone and can only be pursued aggressively at the risk of a breakdown of social cohesion. Government printing of money (5) is frowned upon by trading partners and inflates away savings. Option (6), widespread defaults, could lead to a broad-scale failure of the monetary-financial system, so it will likely be avoided, except in limited circumstances.

Currently governments are dithering with all of these options, applying them in an *ad hoc* and piecemeal fashion. However, two of the six have at least a theoretical capability of being implemented in a fairly dramatic, strategic way if and when the crisis becomes otherwise unmanageable. These strategies would consist of a modified debt jubilee (a form of default, option 6), or a bout of inflation through the creation of non-debt-based currency (option 5). Both would come with major risks, but either could, in principle, buy time for the implementation of a more fundamental reform of the entire economic system.

A modified debt jubilee could take the form of a universal "haircut"—a term currently being used in financial circles to describe a situation where the market value of securities being held by financial firms as part of their net worth is significantly reduced. In the strategy being proposed, the "haircut" would apply to all financial claims. Government by edict would reduce all debt by a certain percentage—let's say, somewhere between 75 and 90 percent. At the same time, all investments and savings accounts above a certain figure (allowance would have to be made for pensioners and low-income individuals) would get the same treatment. The process would be complicated and unpopular, especially among those with the most to lose, but it might help get us past the wall. It would reduce economic activity significantly—that's going to happen anyway, even in the best instance—but it would also remove the overhang of debt that threatens to bring down the entire economy.

How might this work? Let's say, as a starting point, that we wanted to protect all assets below a certain level. In the U.S., perhaps all assets below $25,000 could remain untouched. Then, one simple way to administer the "haircut" would be to slice a decimal place off everyone's debts, savings, and other accounts. If you had a $250,000 mortgage, it would be knocked down to $25,000—but your $20,000 savings account would survive unscathed, as it fell below the $25,000 limit designed to protect pensioners and other low-income individuals. Your debt overhang would have shrunk from $230,000 to $5,000. A wealthy person who had gained $5 billion through investing in hedge funds would now have only $500 million. A business that owed $750,000 in loans would now owe $75,000. And so on.

The net result would be a "re-set" in the relationship between claims and real assets, bringing that relationship back into a somewhat more workable balance. Of course, this "re-set" would be hugely controversial, confounding . . . and painful.

Sound far-fetched? Certainly, an action like this would not be undertaken unless other tactics had failed. It would yield winners and losers: although everyone would feel the effects, the impact would be uneven. At first glance, it seems those with the fewest assets and highest debts would suffer least. A more likely outcome would be widely distributed dislocations, unemployment, and so on, so there would be plenty of suffering to go around. But, this "re-set" would give us the opportunity—if we took advantage of it—to restructure our economic and financial systems to be more sustainable and resilient.

The second strategy would consist of governments or central banks creating debt-free money. This is how economist Richard Douthwaite, founder of the organization FEASTA and editor of the book *Fleeing Vesuvius,* describes it:

> The solution is to have central banks create money out of nothing and to give it to their governments either to spend into use, or to pay off their debts, or give to their people to spend. In the eurozone, this would mean that the European Central Bank would give governments debt-free euros

> according to the size of their populations. The governments would decide what to do with these funds. If they were borrowing to make up a budget deficit—and all 16 of them were in deficit in mid-2010, the smallest deficit being Luxembourg's at 4.2 percent—they would use part of the ECB money to stop having to borrow. They would give the balance to their people on an equal-per-capita basis so that they could reduce their debts, or not incur new ones, because private indebtedness needs to be reduced too. If someone was not in debt, they would get their money anyway as compensation for the loss they were likely to suffer in the real value of their money-denominated savings. Without this, the scheme would be very unpopular. The ECB could issue new money in this way each quarter until the overall, public and private, debt in the eurozone had been brought sufficiently down for employment to be restored to a satisfactory level.[2]

An alternative would be to pass laws against usury (for example, any interest rate greater than 20 percent would become illegal), then print enough money to accelerate inflation beyond 20 percent. People's debts would decline over time, as would the value of money being held. The government could spend money into existence for social welfare programs, thus ensuring that retirees and other vulnerable groups don't get hit too hard.

In the U.S., a version of the "free money" strategy is being advocated by Ellen Brown, author of *Web of Debt*. Brown argues that the United States Congress has the constitutional authority to coin money, but historically has needlessly delegated the power of money creation to the banking system—and, since 1913, to the Federal Reserve. The Federal government has on occasion created money directly, without borrowing—notably to finance the Civil War. The Federal Reserve's second bout of quantitative easing, in 2010, was essentially a version of this strategy: the Fed bought government debt with money created on the spot, and interest from the debt will be rebated to the Treasury. However, Brown argues that the best way to pursue this option would be for the government itself to directly issue debt-free money, rather than for the Fed to do it through a more circular means.

The objection usually raised against government "printing" of large amounts of new money is that this would be highly inflationary: the U.S. economy could suffer the same fate as Weimar Germany, with its currency becoming virtually worthless and all savings being wiped out in the process. Brown disagrees:

> "Adding money ("demand") to an economy with high unemployment and unused productive capacity serves to increase productivity, increasing goods and services or "supply." When supply and demand increase together, prices remain stable. And adding money to the money supply is obviously not hazardous when the money supply is shrinking, as it is now. . . . Financial commentator Charles Hugh Smith estimates that the economy now faces $15 trillion in writedowns in collateral and credit. If those estimates are correct, the Fed could, in theory, print $15 trillion and buy up the entire federal debt without creating price inflation. That isn't likely to happen, but it does make for an interesting hypothetical."[3]

Over the short run, emergency measures could include the Fed buying up short-term municipal bonds in order to ease state and county fiscal crises, and the European Central Bank doing something similar with bonds of member nations, creating money to fill the gap left by the contraction in the money supply which resulted from the financial crisis of 2008 and that has led to soaring budget deficits.[4]

Another related, longer-term measure that could help, according to Brown, is the establishment of state or provincial banks. Currently, North Dakota has the only stateowned bank in the U.S., established by the state legislature in 1919. The bank's original purpose was to free farmers and small businesses from indebtedness to out-of-state bankers and railroad companies. By law, the state deposits all its funds in the bank, and deposits are guaranteed by the state. The Bank of North Dakota is a bankers' bank, partnering with private banks to loan money to farmers, real estate developers, schools and small businesses. It also purchases municipal bonds.

What would be the advantage to the state of having of such a bank? With fractional reserve lending, banks extend credit (create money as loans) in amounts equal to many times their deposit base. If a state owns its bank, it need not worry about shareholders or profits, so it could lend to itself or to its municipal governments at zero percent interest. If these loans were rolled over indefinitely, this would be essentially the same as creating debt-free money.[5]

Clearly, none of these strategies can solve the long-term problems of declining energy and minerals, rising population, and worsening environmental crises. They are merely ways to avert the looming wall of monetary-financial collapse. Once we have bought some time, we must begin to redesign certain basic structures of the economy that currently function properly only in a context of constant growth.

One of these structures consists of the money we use.

References

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GDP IS DEAD: Will the world be happier without it?

Memo to politicians: Stop promising to grow GDP and start targeting social benefits you can actually deliver—or prepare to face angry mobs. Nothing grows forever on a finite planet, not even the US economy.

It's not surprising that everyone from President Obama to Michele Bachmann is assuring the electorate that he or she can deliver more GDP growth. When GDP numbers are up, more jobs appear and investments reap higher returns. When GDP is down, economic mayhem ensues.

Yet there are signs that more GDP growth may not be in the cards, regardless whose economic remedy is chosen. In fact, the day may have arrived when GDP itself has outlived whatever usefulness it ever had.

GDP (Gross Domestic Product) is a number indicating the total spending occurring in a national economy annually. Since WWII, policy makers have used GDP as their primary index of national economic health. During the late 20th century, with the world awash in cheap energy to fuel ever more industrial output and transport-driven trade, the numbers kept going up—and most economists concluded they'd continue doing so forever.

A few contrarians (including Robert F. Kennedy, in 1968) suggested that relying on GDP wasn't a good idea. Although soaring numbers lead to financial euphoria, they can hide social ills like growing inequality; moreover, GDP fails to distinguish between waste, luxury, and the satisfaction of basic human needs. Perversely, GDP often rises during wars or after environmental disasters, due to increased government spending.

Despite criticisms, economists and policy makers have stuck with GDP—perhaps because tracking a single number makes their jobs easier.

But now, the US may have reached its practical GDP limit. The bursting of a once-in-a-lifetime credit bubble, the maxing out of consumer borrowing and spending capacity, and tightening global resource constraints (showing up as stubbornly high oil prices) have caught national economic output in an undertow. Much of the rest of the world is being drawn in, with Greece, Ireland, Portugal, Spain, and Italy swirling ever closer to the drain. During the past two years, Americans bought an anemic recovery—a few hundred billion dollars' worth of GDP growth—but at the cost of trillions in added government debt.

Now, as Washington descends deeper into partisan acrimony, efforts to generate further growth with yet more debt have become political orphans that no Republican and few Democrats will claim as their own. If the "recovery" was all smoke and mirrors, we've just run out of mirrors.

Trapped in a failed paradigm

That means hard times lie ahead. People instinctively know what to do in hard times: consume less and save more. But these sensible responses will—guess what?—hammer down GDP even further.

There's no way out of this dilemma if we stay trapped in our current economic paradigm. More government debt and spending give only temporary symptomatic relief, while slashing government spending greases the chute to economic hell for millions of poor and middle-class families. We have arrived at a historic moment when none of the solutions we are familiar with works, and we are forced to examine our basic premises. Premises like these:

- The notion that we can run an economy sustainably by perpetually increasing the rate at which we extract and burn non-renewable resources such as petroleum;
- The notion that we can use debt as money—a practice founded on our assumption that the economy will always grow, enabling us to repay both debt and its accrued interest; and
- The notion that we should chart our progress as a nation just by totaling up how much money we are spending annually.

That last premise is important because what we as a society choose to measure influences what we aim for and what we value. If what we care about most is increasing spending and consumption, then we are setting ourselves up for two big failures—the failure to solve real human problems that have nothing to do with consumption, or that may be worsened by certain kinds of consumption; and the failure to accomplish what we are trying to do (perpetually grow GDP and consumption) because *it can't be done*. Again, nothing grows forever on a finite planet.

Indicators and targets help us set our agenda and tell us how we are doing at fulfilling it. With GDP, we get both a warped agenda and misleading feedback.

After GDP—happiness?

Proposals for a broader-based economic metric date back at least to 1972, when economists William Nordhaus and James Tobin suggested the Measure of Economic Welfare (MEW)—which Herman Daly, John Cobb, and Clifford Cobb refined in 1989 as the Index of Sustainable Economic Welfare (ISEW). The aim of these early alternative indicators was to deduct defense spending and the costs of environmental degradation from GDP, and add the unpaid services of domestic labor.

In 1995 the think tank Redefining Progress took MEW and ISEW a step further with its Genuine Progress Indicator (GPI), which adjusts not only for environmental damage and resource depletion, but also for income distribution, volunteering, crime, changes in leisure time, and the lifespan of consumer durables and public infrastructures. GPI gained more traction than either MEW or ISEW, and is now used by the scientific community and many governmental organizations globally (for example, the state of Maryland is now using GPI for planning and assessment).

Coincidentally, 1972—the year MEW was proposed—also marked the date when the tiny Himalayan kingdom of Bhutan started moving to build an economy based on what King Jigme Singye Wangchuck called "Gross National Happiness." Seeking to preserve traditional Buddhist values in an increasingly globalized world, this tiny country set out to develop a survey instrument to measure its people's general sense of well-being.

Until recently the subject of happiness was avoided by social scientists, who lacked good ways to measure it; however, "happiness economists" inspired by Bhutan's experiment have found ways to combine subjective surveys with objective data on lifespan, income, and education, making a national happiness index a practical option.

Though Bhutan's economy is still based on subsistence agriculture and has a relatively low GDP, the Bhutanese people rank among the top 20 happiest in the world. This contrasts with the US, which delivers much less happiness per unit of GDP. In his book *The Politics of Happiness*, former Harvard University president Derek Bok traced the history of the relationship between economic growth and happiness in America. During the past 35 years, per capita income has grown almost 60 percent, the average new home has become 50 percent larger, the number of cars has ballooned by 120 million, and the proportion of families owning personal computers has gone from zero to 80 percent. But the percentage of Americans describing themselves as either "very happy" or "pretty happy" has remained virtually constant, having peaked in the 1950s. Our economic treadmill is continually speeding up due to GDP growth and we have to push ourselves ever harder to keep up, yet we're no happier as a result.

The thinking behind Gross National Happiness is catching on. Harvard Medical School has released a series of happiness studies, while British Prime Minister David Cameron has announced the UK's intention to begin tracking well-being along with GDP. Sustainable Seattle has launched a Happiness Initiative and intends to conduct a city-wide well-being survey. Thailand has instituted a happiness index and releases monthly GNH data. Britain's New Economics Foundation publishes a "Happy Planet Index," which "shows that it's possible for a nation to have high well-being with a low ecological footprint." And a new documentary film called "The Economics of Happiness" argues that GNH is best served by localizing economics, politics, and culture.

Whatever index is settled upon to replace GDP, it will be more complicated than the current one-dimensional metric. But simplicity isn't always an advantage, and the additional effort required to track factors like collective psychological well-being, quality of governance, and environmental integrity may be well spent.

This is what we must do

Milton Friedman once wrote: "Only a crisis—actual or perceived—produces real change." Absent a crisis, politicians and economists will cling to GDP even if it is flawed and superior alternatives exist. It's familiar, it's simple, and it is embedded in all our existing economic institutions.

But crisis is upon us. For the past two decades, GDP growth in the US has mostly been captured by the financial industry. Today, unemployment is stubbornly high, while household net worth is plummeting. Further growth appears obtainable only through huge government deficits and ballooning debt. Government spending has been the only thing keeping the economy on life support, but governments across Europe and in the US have hit a crisis of confidence, both with the financial markets and constituents. We're at an economic dead end. We seem to be on track for a political and social train wreck of dashed expectations and seething public rage. Think Tahrir Square times a thousand. The only way to manage this situation will be to change the goals and rules of our national game.

Here's what might happen. Following widespread outbreaks of public dismay over austerity packages designed to reduce government deficits, world leaders issue an announcement that GDP is being phased out. There's plenty of political cover for this: in 2008, French president Nicholas Sarkozy convened "The Commission on the Measurement of Economic Performance and Social Progress," chaired by American economist Joseph Stiglitz, which enumerated the failings of GDP. Leaders can point to the Commission's conclusions, and tell their people that the goal of the new economic indicator will be to track and obtain broader social and environmental benefits without expanding government debt.

A direct suggestion to President Obama: Convene economists of all stripes now to come up with that alternative indicator. They could start by surveying work already done, then make adjustments as necessary. We need an agreed-upon metric that's ready to go when crisis strikes—and crisis is just around the bend.

After the announcement would come the work of re-aligning incentives, regulations, taxes, and spending to deliver improvements in happiness and sustainability. That will mean, among other things, changing financial rules to stop enriching banks and speculators preferentially (which increases GDP but often ends up just hiking economic inequality while failing to deliver any general benefit). One strategy to accomplish this might be to charge a small tax on all purely financial transactions, with the proceeds used to reduce income taxes.

We know from numerous studies that people are happiest when they feel in control of their lives, when they have opportunities to help shape the rules they must follow, and when they feel that those rules are fair. This means that policy makers must find ways to step aside and let the shift away from GDP be driven by people acting within their local communities where their voices can be heard.

No doubt a period of experimentation will be required. That's why it's important to start a general economic reform by changing our primary economic indicator: as the numbers come in, we'll see which policies make us happier and which ones don't. Altogether, this economic transition is likely to take two or three decades. It may be hard at first, but society will have set itself on a different trajectory—increasing human satisfaction, health, and well-being, while reducing humanity's impact on the environment.

If our current crisis is being driven by limits both to debt and natural resources, then one might wonder whether there are limits also to progress in the social and cultural spheres. Could we eventually reach the limits of human happiness?

Maybe. But that would be an interesting problem to have.