real-world economics review, issue no. 78
subscribe for free

Causes and consequences of President Donald Trump

Ann Pettifor [PRIME (Policy Research in Economics) UK]

Introduction and context: 2016, the year that shook the foundations of globalisation

2016 was a year of momentous events for the United States. A major insurgency was triggered by resistance to the utopian ambitions of economists, financiers and politicians – namely, to detach markets – in money, trade and labour – from the US's regulatory democracy. Americans reacted to an economic system that appeared to many to be beyond the control of public authorities, and beyond that of democratically elected politicians. Both Democrat and Republican administrations had presided over a steep rise in inequality. At the same time while millions of middle class Americans were impoverished or made insecure by "liberalized" finance, or globalisation, the system fabulously enriched the 1%. Exposed, through no fault of their own, to the 2007-9 financial crisis and its aftermath, many experienced the economic system as threatening to their life chances, their incomes, their futures, and their way of life. Despairing of their democracy, and of politicians and political institutions, Americans turned to a "strong man" – a billionaire who led them to believe that he alone could protect them from the predations of markets in trade and labour.

The rising tide of American nationalism and populism, was manifest in the slogan: "America First". The determination to build walls against migrants and free trade represents a major challenge to the utopian ideal of "globalisation". For some time now advocates of globalisation have complacently believed that the globalised financial system is a given, and unchallengeable. President Bill Clinton embraced globalisation as the overarching solution to the country's problems – the "bridge to the twenty-first century".[1] Tony Blair told the Labour Party Conference in 2005 that there was no need to stop and debate globalisation: "you might as well debate whether autumn should follow summer." Like many others Blair ignored the rising threat to globalisation: nationalism. In a 1940 lecture delivered at Bennington College, Karl Polanyi, the political economist and author of *The Great Transformation* (1944)[2] argued that:

> "The more intense international cooperation was and the more close the interdependence of the various parts of the world grew, the more essential became the only effective organizational unit of an industrial society on the present level of technique: – the nation. Modern nationalism is a protective reaction against the dangers inherent in an interdependent world.

---

[1] Quoted in George Packer, 31 October, 2016: *Hilary Clinton and the Populist Revolt.* The New Yorker. http://www.newyorker.com/magazine/2016/10/31/hillary-clinton-and-the-populist-revolt
[2] Karl Polanyi, 1944, *The Great Transformation*, Beacon Press, 1957, p. 114.

> The apparently simple proposition that all factors of production must have free markets implies in practice that the whole of society must be subordinated to the needs of the market system."[3]

On the opening page of his book Polanyi explained that society "inevitably... took measures to protect itself" from job and income losses, and from economic forces that generated anxiety, insecurity, risks and threats. Self-protection would invariably take the form of a counter-movement to *laissez faire*, or self-regulated markets. The movement, Polanyi argued, can be spontaneous, often leaderless and attracts supporters from all classes. Unlike Marx, Polanyi believed that the counter-movement could include the business and finance sectors. These, as Fred Block has argued need protections, or

> "limits, especially regulatory initiatives, to avoid destructive social, environmental, and economic consequences."[4]

Back in May 2016, pollster Nate Silver analysed Trump's primary campaigns and noted that the "movement" to elect Donald Trump as President was diverse.

> "As compared with most Americans, Trump's voters are better off. The median household income of a Trump voter so far in the primaries is about $72,000, based on estimates derived from exit polls and Census Bureau data. That's lower than the $91,000 median for Kasich voters. But it's well above the national median household income of about $56,000. It's also higher than the median income for Hillary Clinton and Bernie Sanders supporters, which is around $61,000 for both."

Trump either won, or closely contested all the US's traditional manufacturing states Ohio, Wisconsin, Indiana and even Michigan, where union voters did not support Clinton as they had Obama and where trade was a big issue. Silver writes:

> "The slower a county's job growth has been since 2007, the more it shifted toward Trump. (The same is true looking back to 2000.)
>
> …The list goes on: More subprime loans? More Trump support. More residents receiving disability payments? More Trump support. Lower earnings among full-time workers? More Trump support. 'Trump Country,' as my colleague Andrew Flowers described it shortly after the election, isn't the part of America where people are in the worst financial shape; it's the part of America where their economic prospects are on the steepest decline."[5]

---

[3] Karl Polanyi,1940, in the first of Five Lectures at Bennington College on *The Present Age of Transformation: The passing of 19th century civilisation.* Re-published by Policy Research in Macroeconomics (PRIME) in February, 2017. http://www.primeeconomics.org/articles/our-polanyi-week-the-1940-bennington-college-lectures
[4] Karl Polanyi, as above, Lecture Three of Five Lectures at Bennington College.
[5] Nate Silver, 9 January, 2017: *Stop Saying Trump's Win Had Nothing to do with Economics.* Accessed 15th February, 2017. https://fivethirtyeight.com/features/stop-saying-trumps-win-had-nothing-to-do-with-economics/

Two days after the presidential election, Politico noted that “between 2007 and 2014, the median incomes of white males without college degrees fell by 14 percent. Trump carried them by nearly 40 points Tuesday.”[6]

The “counter-movement” was not confined to the US. Nationalist, right-wing, anti-globalisation and even fascist movements are active across Europe, as this goes to press.
The slogans used by Trump: “Make America Great Again” and “America First” did not just echo the fascist-leaning Charles Lindbergh’s 1930s “America First” campaign in support of Hitler. It was also a theme of the far-right French presidential candidate, Marine Le Pen’s: “On est chez nous” in 2017 and of the Italian leader, Silvio Berlusconi’s earlier “Forza Italia”. The UK’s Brexit campaign slogans included: “Take Back Control”, “Take Back Our Country” and “Britannia waives the rules”. They all represented an attempt by political leaders of insurgencies to use the nation as a “protective reaction” against unfettered globalised markets in capital, trade, and labour.

In this essay we hope to trace the underlying and deep-seated economic causes that led to this rise of nationalisms and protectionism.

From beasts on an 18th-century Pacific island to today’s globalised financial markets

Back in the 1770s a story circulated about two families of “beasts” – goats and dogs – placed on a remote Pacific atoll, Juan Ferdinand island, by Spanish and English sailors. In a natural condition of scarcity, the goats and dogs fought viciously over food, but ultimately learned to live in harmony – without political interference – or so we are led to believe. The author of an influential dissertation on the Poor Laws used this experience as an incentive for the alleviation of poverty. Hunger he argued,

> “will tame the fiercest animals, it will teach decency and civility, obedience and subjection, to the most brutish, the most obstinate, the most perverse."

In this tale, and in the political economy that emerged from it, lay the origins of a theory that underpins classical and neoliberal political economy to this very day. Namely that without government interference, self-regulating markets in money, trade and labour may become vicious and unsettled, but can ultimately be expected to reach a state of equilibrium. The author of the pamphlet was one Rev. Joseph Townsend and the 1786 publication was his *Dissertation on the Poor Laws.*[7] Despite its relative obscurity, the *Dissertation’s* contribution to political economy represented a decisive episode in the history of economics, as Philipp H. Lepenies explained in a 2014 paper.[8]

Townsend made the “scientific” case that hunger, or scarcity, represented a “natural law” that governed human appetites and markets for food:

---

[6] Carl M. Cannon, 10 November, 2016. Real Clear Politics, *How Trump Won.* http://www.realclearpolitics.com/articles/2016/11/10/how_donald_trump_won_132321.html. Accessed 15 February, 2017
[7] Joseph Townsend, 1786. *A Dissertation on the Poor Laws*. http://socserv2.socsci.mcmaster.ca/econ/ugcm/3ll3/townsend/poorlaw.html
[8] Philipp H. Lepenies, 2014. *Of goats and dogs: Joseph Townsend and the idealisation of markets – a decisive episode in the history of economics*. Cambridge Journal of Economics, 38 (2): 447-457.

> "There is an appetite, which is and should be urgent, but which, if left to operate without restraint, would multiply the human species before provision could be made for their support. Some check, some balance is therefore absolutely needful, and hunger is the proper balance; hunger, not as directly felt, or feared by the individual for himself, but as foreseen and feared for his immediate offspring. Were it not for this the equilibrium would not be preserved so near as it is at present in the world, between the numbers of people and the quantity of food."

In other words, it was not men, but the *natural* fear of hunger that governed markets for scarce food. Polanyi noted that:

> "Hobbes had argued the need for a despot because men were like beasts; Townsend insisted they *were* actually beasts and that, precisely for that reason, only a minimum of government was required."[9]

Lepenies believes that Malthus plagiarised Townsend in his famous *Essay on the Principle of Population* – which is "similar" to Townsend's Dissertation,

> "not only in their argument, ideas and structure but in their use of the device of scientific abstraction and generalisation. It is therefore not Malthus alone who should be revered as the father of modern economic logic and market fundamentalism but also Townsend."[10]

Townsend was also a close friend of Jeremy Bentham who quoted at length the example of goats and dogs in his Pauper Systems Compared of 1797 (Quinn, 2001).[11]

For Townsend, society, as fundamentally biological, was best left as a self-regulating system that when untouched by political intervention, will tend toward equilibrium and order. His crude and brutish conception of self-regulating markets – previously understood as embedded in regulated social and political institutions – was to inform much of classical and neoclassical economics, and has persisted to this day in market fundamentalism.

More recently Townsend's theory was extended from labour and trade markets and applied to markets in money – with devastating economic and political consequences. It was the application of this flawed theory to the monetary system that led, I will argue, to recurring and catastrophic financial market failures, and ultimately to the election of President Donald Trump.

The neoclassical conception of money

Adam Smith first conjured up the idea of money as a "veil" over economic activity when he asserted that money is "a *neutral* medium that facilitated exchange on the 'great wheel of

[9] Karl Polanyi, 1944.*The Great Transformation*, Beacon Press, 1957, p. 114.
[10] Philipp H. Lepenies, as above.
[11] Cited in Lepenies, as above.

circulation'".[12] Paul Samuelson explained to millions of students of his Economics 101 textbooks that:

> "Even in the most advanced industrial economies, if we strip exchange down to its barest essentials and *peel off the obscuring layer of money*, we find that trade between individuals or nations largely boils down to *barter.*"[13]

While the classical or neoclassical school of economists pay little attention to "neutral" money or to "the obscuring layer of money" in designing models of the economy, they simultaneously conceive of it as akin to a commodity and therefore, as Samuelson explains, as a form of barter. Money, in their view, is representative of a tangible asset or scarce commodity, like gold or silver. As with corn for example, money in this orthodox view, can be set aside or saved, accumulated and then loaned out. Savers lend their surplus to borrowers. Bankers, Krugman and Wells argue in their textbook, Macroeconomics,[14] are mere intermediaries between savers and borrowers.

Because neoclassical and some post-Keynesian economists conceive of money as like gold or silver, having a scarcity value, they theorise as if money is subject to market forces. In other words, as if money's "price" – the rate of interest – is a "natural" price, subject to the law of supply and demand, rather than a socially constructed "price" on every loan determined by risk assessors in banks. Many argue that like commodities, the supply of money or savings can become scarce. In February, 2017, the British government's Chancellor was quoted in the Financial Times as saying (to MPs clamouring for extra funds): "There is no pot of money under my desk."[15] Mrs Thatcher in a speech to the 1983 Tory party conference echoed the neoclassical theory that money exists as a consequence of economic activity when she said:

> *"The state has no source of money, other than the money people earn themselves*. If the state wishes to spend more it can only do so by borrowing your savings, or by taxing you more. And it's no good thinking that someone else will pay. That someone else is you. There is no such thing as public money. There is only taxpayers' money." (My emphasis.)

This misunderstanding of the nature of money and of a monetary economy is entrenched in classical and neoclassical (neoliberal) economic theory. It helps explain the "blind spot" that economists have for money, banks and debt, and for the finance sector.

The economist Andrea Terzi, explains the difference between a monetary economy and a non-monetary economy:

> "When people save in the form of a real commodity, like corn, the decision to save is a fully personal matter: if you have acquired a given amount of corn, you have the privilege of consuming it, storing it, wasting it, as you please, without this directly affecting other people's consumption of corn. *Only if you*

---

[12] Adam Smith.
[13] Paul Samuelson,
[14] Krugman and Wells, Macroeconomics, 4th Edition. https://www.amazon.co.uk/Macroeconomics-Paul-Krugman/dp/142928343
[15] George Parker, Jim Pickard and Gemma Tatlow, in the Financial Times, 21 February, 2017: *Hammond Warns No "Pot of Money" for Extra Budget Funds*. https://www.ft.com/content/6c786540-f844-11e6-bd4e-68d53499ed71

> *decide to lend it will you establish a relationship with others.*
>
> In a monetary economy, saving is not a real quantity that anyone can independently own, like corn or gold or a collection of rare stamps. In a monetary economy, as opposed to a non-monetary economy, saving is an act that [establishes a relationship with others]... in the form of a financial *claim.*
>
> Unlike a commodity such as corn, financial saving always appears as a financial relationship, as it exists only as a claim on others, in the form of banknotes, bank deposits or other financial assets. Personal savings are claims of one economic unit on another, and any change in savings entails a change in the relationship between the 'saver' and other economic units. This does not appear on national accounts, which only expose aggregate values.
>
> If we then look at savings by zooming out of the individual unit and considering the interconnections between units and between sectors, we find that each penny saved must correspond to a debt of equal size. A banknote is a central bank's liability. A bank deposit is a bank's liability. A government security is a government liability. A corporate bond is a private company liability, and so on. This means that when we discuss financial savings we are also discussing debt. Every penny saved is someone else's liability ... every penny saved is somebody's debt.
>
> In a monetary economy, savings do not fund; they need to be funded."[16]

"Nixon Shock" as lightning rod for international financial liberalisation

On the evening of Sunday, 15 August 1971 in a TV announcement, and without consulting allies or the IMF, President Nixon unilaterally dismantled the architecture of the international financial system. At the time, the "Nixon Shock" represented the biggest sovereign default in history, and was a reckless decision the foolhardiness of which President Donald Trump (up until this point) has failed to match. Its effect was to accelerate the process of de-regulation by restoring *private autho*rity over the finance sector, and to trigger recurring financial crises.

The Bretton Woods system had been carefully constructed by an international gathering of economists, including Britain's JM Keynes and Harry Dexter White of the United States, at a grand New Hampshire hotel in 1944.[17] The international financial architecture constructed at Bretton Woods was a response to the recurring crises of the 1920s and 30s under the deeply flawed gold standard. That in turn was based on a fallacious understanding of the nature of money as a commodity, gold; and not as a socially constructed system of obligations and claims; assets and liabilities; debits and credits, all managed by regulatory democracy.

[16] Andrea Terzi, 2015, *The Eurozone crisis: debt shortage as the final cause*. Contribution to a panel at INET Annual Conference, Paris, 8-11 April, 2015.
[17] Ed Conway, 2014, *The Summit: The biggest battle of the Second World War – fought behind closed doors.* Little, Brown

One of the primary motivations behind the construction of Bretton Woods was Keynes' and White's determination (backed by President Roosevelt) to restore *public authority* over the monetary system and to thereby restore policy autonomy to democratic governments. The latter had been stripped of such autonomy by the mobility of capital, and by the exercise of *private authority* over the creation of credit and the determination of interest rates. Keynes and White understood that fundamental to the restoration of public authority over finance was the introduction of controls over the mobility of capital.

The process of dismantling Bretton Woods began almost as soon as agreement had been reached at the conference hotel. Roosevelt had barred private bankers from attending the 1944 conference, but this did not deter their lobbying. An IMF Working Paper explains that both Keynes and White realized that "capital controls would not be effective unless applied 'at both ends' of the transaction, and their original plans therefore mandated IMF member countries to cooperate in enforcing each other's measures."[18] But as the IMF documents "last minute intervention by powerful New York bankers… succeeded in watering down these proposals, and in the final version of the IMF Articles agreed at Bretton Woods on 22nd July 1944, capital controls were not included as a permanent feature of the international financial landscape."[19]

In this otherwise excellent paper by the IMF's Ghosh and Qureshi the authors, like many other economic historians, overlook the "Nixon Shock". Yet the collapse of the Bretton Woods system in 1971 represents a decisive episode in the process of financial globalisation begun soon after Bretton Woods, and with it the corresponding weakening of regulatory democracy. As the OECD explains:[20]

> "the easing of capital controls, and the international branching of business firms or establishment of their finance companies, made domestic regulations easier to circumvent by conducting financial transactions outside national boundaries."

Up until the early 1970s, financial systems in most western, democratic economies were governed by the regulation of market forces, enacted within the policy-making boundaries of democratic nation states. These included: interest rate controls; securities market regulations; quantitative investment restrictions on financial institutions; line-of-business regulations and regulations on ownership linkages among financial institutions; restrictions on entry of foreign financial institutions; and controls on international capital movements and foreign exchange transactions.

According to the OECD:[21]

> "Direct controls were used in many countries to allocate finance to preferred industries during the post-war reconstruction period; specialised credit institutions have also been in place to ensure access to credit by smaller

[18] IMF Working Paper February, 2016, by Atish R. Ghosh and Mahvash S. Qureshi *Capital Controls What's In a Name? That Which We Call Capital Controls.* https://www.imf.org/external/pubs/ft/wp/2016/wp1625.pdf
[19] As above
[20] Edey, Malcolm and K. Hviding (1995), *An Assessment of Financial Reform in OECD Countries*, OECD Economics Department Working Papers, No. 154, OECD Publishing. doi:10.1787/515737261523 https://www.oecd.org/fr/eco/monetaire/35235099.pdf
[21] As above.

> enterprises; restrictions on market access and competition were partly motivated by a concern for financial stability; protection of small savers with limited financial knowledge was an important objective of controls on banks; and controls on banks and financial institutions were frequently used as instruments of macroeconomic management."

The "interventions of bankers" and the establishment of the Eurodollar market in the late 1960s, led to the removal of controls over the mobility of capital.[22] Democratic governments were gradually stripped of the powers of oversight and of *the management* of the financial equivalent of the Juan Ferdinand island.

From the perspective of Keynes, the consequences were entirely predictable: recurring financial crises. These began at the periphery of the global economy (in indebted third world countries) but gradually moved to the core of the global economy: the Anglo-American economies. These recurring crises after the "liberalisation" of the 1970s are best illustrated by this chart from Reinhart & Rogoff's book: *This Time is Different.*

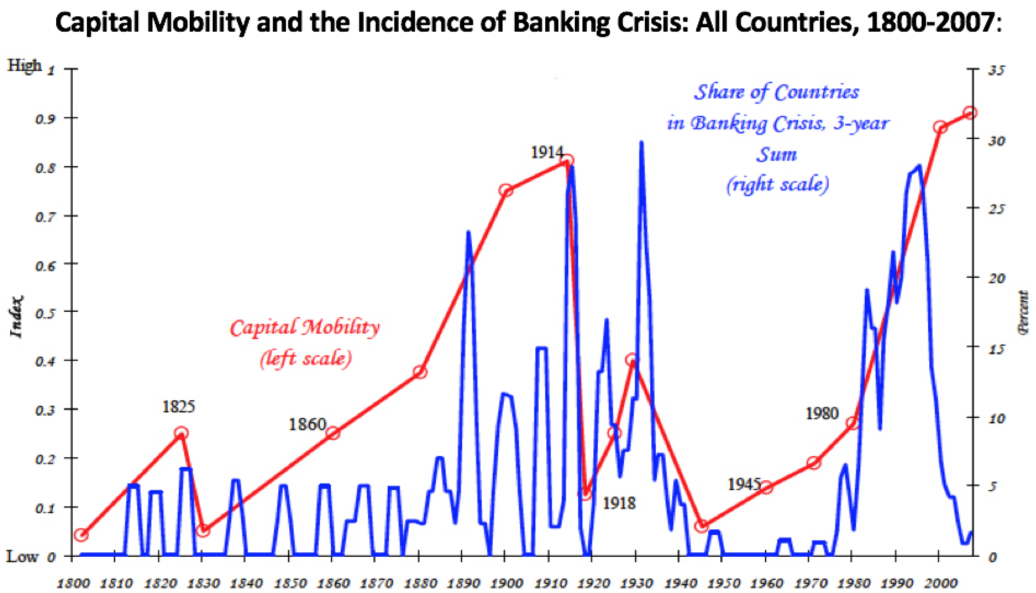


Chart taken from "This Time is Different: A Panoramic View of Eight Centuries of Financial Crises" by Carmen M. Reinhart, University of Maryland and NBER; and Kenneth S. Rogoff, Harvard University and NBER.

In Britain one of the most significant de-regulatory measures was introduced in 1971, the same year as the "Nixon Shock", and was dubbed "Competition and Control" (CCC or "the New Approach"). It was "the biggest change in monetary policy since the Second World War" and is often described by economists as "all competition and no control" over credit creation.

[22] Eric Helleiner, 1995, pg 152 *Great Transformations: A Polanyian Perspective on the Contemporary Global Financial Order* file:///Users/annpettifor/Downloads/9379-15190-1-PB.pdf

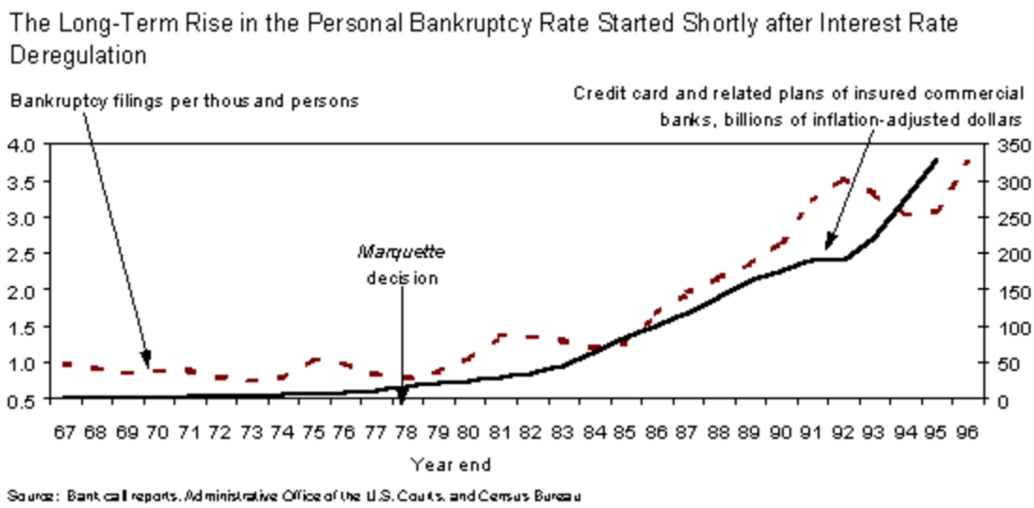
Duncan Needham, of the Cambridge University Centre for Financial History, has written at length on the subject, and argues that:[23]

> "CCC swept away the restrictions on... bank lending to the private sector, that had been in place for much of the 1960s. Henceforth, bank lending would be controlled on the basis of cost, that is, through interest rates. Loans would be granted to those companies and individuals that could pay the highest rate rather than those that fulfilled the authorities' qualitative criteria. By allocating bank credit competitively 'on the basis of cost', CCC replaced years of credit rationing 'by control'."

CCC was not a success. While it aimed to control "the money supply", the effect was the opposite. The money supply grew by 72 percent as commercial bankers engaged in a wild lending spree, and two years later inflation peaked at 26.9 percent.

The ending of restrictions on bank lending in the UK was paralleled in the United States by the Supreme Court's Marquette decision, which initiated interest rate deregulation.[24]

"Price" or the rate of interest, was to become to bank borrowers what "hunger" was to the goats and dogs on Townsend's Juan Ferdinand island. The FDIC charts the immediate impact interest rate deregulation had on bankruptcy filings:



Back in Britain the inflation caused by financial deregulation of lending in the 1970s, and the impact of high real rates of interest on bankruptcies of firms did not trouble a conservative government Minister, Lord Cockfield who said:

---

[23] Duncan Needham, September, 2012. *Britain's money supply experiment, 1971-73* University of Cambridge, http://www.econsoc.hist.cam.ac.uk/docs/CWPESH%20number%2010%20Sept%202012.pdf

[24] FDIC, Diane Ellis, March, 1998: *The Effect of Consumer Interest Rate Deregulation on Credit Card Volumes, Charge-Offs, and the Personal Bankruptcy Rate.* https://www.fdic.gov/bank/analytical/bank/bt_9805.html

> "Control of the money operates through the simple but brutal means of butchering company profits. Ultimately insolvency and unemployment teach employers and workers alike that they need to behave reasonably and sensibly."[25]

As Needham writes:

> "With nominal interest rates peaking at seventeen percent as the authorities tried to rein in the money supply, and the pound at its highest level since 1975, company profits were indeed butchered."

Cockfield's words echoed those of the 18th-century father of market fundamentalism, Joseph Townsend. He believed that like bankruptcies in the market for money, hunger in the market for food:

> "will tame the fiercest animals, will teach decency and civility, obedience and subjection, to the most brutish, the most obstinate, the most perverse."

It was these ideas, and their related policies that led to high, real rates of interest after 1971 and to the build-up of the overhang of private debts that ultimately became unpayable, leading to recurring financial crises, and to the catastrophe of 2007-9. Self-regulating financial markets, "untouched" by elected governments have for more than 30 years inflicted loss and suffering on populations around the world. As Karl Polanyi predicted, these societies, in a "counter-movement" to globalisation and recognising the failure of democratic governments to protect societies from the depredations of self-regulating markets, have reacted by electing "strong men" (and women) that do offer protection. Donald Trump posed as a strong protector, and won the support of those Americans "left behind" by globalisation.

Author contact: ann.pettifor@primeeconomics.org

SUGGESTED CITATION:
Ann Pettifor, "Causes and consequences of President Donald Trump", *real-world economics review*, issue no. 78, 22 March 2017, pp. 44-53, http://www.paecon.net/PAEReview/issue78/Pettifor78.pdf

[25] Duncan Needham, 2014, p. 134: *UK Monetary Policy From Devaluation to Thatcher, 1967-82*. Palgrave Macmillan.