A System Designed to Crash

David Korten on why a money system dependent on constant growth can't last.

This is the twelfth of a series of blogs based on excerpts adapted from the 2nd edition of Agenda for a New Economy: From Phantom Wealth to Real Wealth. I wrote Agenda to spur a national conversation on economic policy issues and options that are otherwise largely ignored. This blog series is intended to contribute to that conversation. —DK

The unrealistic expectation that money should grow effortlessly in perpetuity [see my last blog] is more than an issue of unrealizable expectations. It combines with a Wall Street controlled debt-based money system to create an imperative for the economy to grow the profits of bankers, and thereby the richest among us, to keep the financial system, and thereby the economy, from collapsing.

It is odd that we experienced a financial collapse in 2008 because of a credit crunch, a shutdown on lending, at a time when the world was already awash in money. BusinessWeek's July 11, 2005, cover story shouted "Too Much Money" and spoke of a savings glut. Its June 11, 2008, European issue reiterated the theme: "Too Much Money, Inflation Goes Global."

Most discussion of the financial crisis focuses on the details and misses the big picture. First, much of the money was tied up in the Wall Street casino rather than facilitating productive activity in the real economy and was simply pumping up a phantom wealth bubble. Second, virtually every dollar in the system was borrowed, because in our money system, banks create money by lending it into existence. When this debt is used to inflate financial bubbles and support Ponzi schemes, eventual default is inevitable.

Third, Wall Street and the Federal Reserve are joined in an alliance to keep "wage inflation" below the level of growth in the real cost of living. This assures that the benefits of productivity gains all go to owners rather than being shared with workers. It also keeps inflation confined to financial bubbles that inflate the phantom wealth financial assets of the rich.

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Furthermore, it forces the bottom 90 percent of the population—the people who make their living by producing real goods and services—into debt at usurious interest rates to the top 10 percent to cover daily basic daily expenses. Inevitably, the amounts owed exceed the borrower's ability to repay. The lenders then stop lending and foreclose on the assets of the desperate borrowers.

When a loan is repaid or goes into default, the debt is canceled and the money supply shrinks by that amount. Most loans continue to be repaid, but if new loans are not being issued, the demand for real goods and services falls because people don't have the money to pay for them. As demand falls, businesses lay off workers, who then join those pushed into default.

The problem appears to be a lack of money, even though the total money in circulation is far more than enough to cover real-wealth exchanges in a rational real-wealth economy. The money, however, is locked up in the Wall Street casino economy rather than circulating in the real Main Street economy. Pouringpublic bailout money into Wall Street serves only to reflate the bubble. It does nothing to revive the real economy.

The demand by Wall Street for the eventual repayment with interest of nearly every dollar in circulation means that to avoid collapse, the economy has to grow to generate demand for new borrowing to put new money into circulation to pay the interest due to bankers on already outstanding loans. This demand for perpetual growth simply to keep the bankers solvent results in a serious distortion of society's economic priorities.

When the credit funds current consumption and phantom wealth speculation, the result is ever-increasing debt, inequality, destruction of the natural environment, erosion of the social fabric, and ultimate default.

Rather than maximizing real well-being, policy makers are compelled to focus on avoiding economic collapse by growing the money economy. A debt-based money system can make sense when the credit funds real investment. When the credit funds current consumption and phantom wealth speculation, the result is ever-increasing debt, inequality, destruction of the natural environment, erosion of the social fabric, and ultimate default.

For too long, we have put up with a money system designed to grow the financial assets of rich people at the expense of assuring continuing cycles of economic boom and bust, confining billions to lives of desperation, and reducing Earth to a toxic waste dump. We can do better.

Growth in GDP creates the illusion that we are getting richer, even as we accelerate our material, social, and spiritual self-impoverishment as a species. Fortunately for our common future, people everywhere are waking up to the reality and challenging conventional economic wisdom. They are focusing their attention on rebuilding their communities and local economies to improve human security, health, and happiness without regard to how this impacts GDP, corporate share prices or other bogus indicators of economic well-being. It is an important beginning.

An obvious next step is to replace GDP and other financial indicators with indicators of the health of our children, families, communities, and natural systems as the basis for assessing the economy's performance. We may then notice that destroying living wealth to create financial wealth is an act of collective suicidal insanity and begin treating money as a useful tool for managing our economic choices rather than as the end to be maximized.

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