COLUMBIA
JOURNALISM
REVIEW
Strong Press, Strong Democracy

Economic Crisis, The Audit — November 8, 2011 08:01 PM

Audit Notes: What Would Hammurabi Do?, *WSJ* + OWS, Fisking Davidson

By Ryan Chittum

Nassim Nicholas Taleb doesn't pussyfoot around in his *New York Times* op-ed arguing that we should "End Bonuses for Bankers":

> Instead, it's time for a fundamental reform: Any person who works for a company that, regardless of its current financial health, would require a taxpayer-financed bailout if it failed should not get a bonus, ever. In fact, all pay at systemically important financial institutions — big banks, but also some insurance companies and even huge hedge funds — should be strictly regulated.
>
> Critics like the Occupy Wall Street demonstrators decry the bonus system for its lack of fairness and its contribution to widening inequality. But the greater problem is that it provides an incentive to take risks. The asymmetric nature of the bonus (an incentive for success without a corresponding disincentive for failure) causes hidden risks to accumulate in the financial system and become a catalyst for disaster. This violates the fundamental rules of capitalism; Adam Smith himself was wary of the effect of limiting liability, a bedrock principle of the modern corporation.
>
> Bonuses are particularly dangerous because they invite bankers to game the system by hiding the risks of rare and hard-to-predict but consequential blow-ups, which I have called "black swan" events.

But my favorite part of the op-ed is the *Times* paraphrased pull-quote (pull-paraphrase?):

> What Hammurabi would have done to restrict Wall Street risk-taking.

Taleb would get Babylonian on them:

> Nearly 4,000 years ago, Hammurabi's code specified this: "If a builder builds a house for a man and does not make its construction firm, and the house which he has built collapses and causes the death of the owner of the house, that builder shall be put to death."
>
> This was simply the best risk-management rule ever. The Babylonians understood that the builder will always know more about the risks than the client, and can hide fragilities and improve his profitability by cutting corners — in, say, the foundation. The builder can also fool the inspector; the person hiding risk has a large informational advantage over the one who has to find it.

— *The Wall Street Journal* editorial page looks for a sliver of common ground with Occupy Wall Street and finds it in opposition to corporate welfare:

> The Occupy Wall Street protesters aren't good at articulating what they want, but one of their demands is "end corporate welfare." Well, welcome aboard. Some of us have been fighting crony capitalism for decades, and it's good to have new allies if liberals have awakened to the dangers of the corporate welfare state.
>
> Corporate welfare is the offer of special favors—cash grants, loans, guarantees, bailouts and special tax breaks—to specific industries or firms. The government doesn't track the overall cost of these programs, but in 2008 the Cato Institute made an attempt and came up with $92 billion for fiscal 2006, which is more than the U.S. government spends on homeland security.
>
> That annual cost may have doubled to $200 billion in this new era of industry bailouts and subsidies. According to the House Budget Committee, the 2009 stimulus bill alone contained more than $80 billion in "clean energy" subsidies, and tens of billions more went for the auto bailout and cash for clunkers, as well as aid for the mortgage industry through programs to refinance or buy up toxic loans.

I'm guessing the proposed alliance fell apart in the third paragraph where the *WSJ* puts clean energy in scare quotes.

— Josh Bivens of the liberal Economic Policy Institute takes issue with much of Adam Davidson's debut column in *The New York Times Magazine*.

> He covers a lot of ground, so my list of disagreements is going to be scattershot, but here's a quick taxonomy. First, I don't buy his characterizations about what is generally agreed upon and what is seriously contested among economists. Second, he really undersells how well studied the concept of providing Keynesian-style fiscal support to ailing economies is. Finally, he doesn't help readers in their attempt to make an evidence-based decision on what is easily the most important economics question today: Should Congress and the Administration be spending more to help

> lower today's 9 percent unemployment rate?
>
> Let's start with the general - Davidson portrays economists as hopelessly divided and unsure about whether or not debt-financed spending and tax cuts (i.e., something like another Recovery Act, which I'll just call "fiscal support" from now on) could lower today's unemployment rate, but relatively united when it comes to how to reform taxes and education and health care systems.
>
> This is the reverse of the truth - there is wide agreement that debt-financed fiscal support in a depressed economy will lower unemployment. Now, it's true that there are holdouts from this position. And others who think the benefits of lower unemployment are swamped by the downsides of higher public debt (they're wrong, by the way). But, the agreement* is much more widespread - ask literally any economic forecaster, in the public or private sector, that a casual reader of the Financial Times has heard of if, say, the Recovery Act boosted economic growth. They will all tell you "yes."

(h/t Mike Konczal)