

Review

# The theory of banking: Why banks exist and why we fear them

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Banks are generally considered by most people to be utilities that allow the transmission of value on a daily basis in modern society, but they also seem to create devastating events like credit crises by the manufacture of credit. How this power originated in human society is of interest. Most animals produce some degree of savings, either in caching from one season to the next or for later in one season. Often these savings are an intergenerational transfer for the initial survival of young as in some wasps, or in a later use by the same individual who produces the savings either in the same year or the next as in many birds. The evolution of the bank, of institutions for organizing the savings of groups of humans has had a number of separate points of origin in history in various societies in antiquity and most recently during the Middle Ages in Europe. The history of banking illuminates the nature of contemporary fears about banks. Why banks are seen as necessary and deserving of saving or protecting during economic crises often seems a matter of faith or dogma than of necessity. This explains why neither Bush nor Obama's advisors, nor the EU have crafted as bold actions in the present crisis as FDR took in his Bank Holiday and that regarding the Gold Standard. Similar actions are necessary as is massive employment, but attitudes towards banking prevent such measures. Instead central banks are lending free money to banks who buy government bonds and make profits from the interest, any yet they fail to lend to produce work. This failure is inherent in the nature of reverence of banks.

**Key words:** Banking origins, banking theory, history of credit, surplus, money.

## INTRODUCTION

### **“REPRESENTATIVE MONEYS ARE NOTHING BUT THE MANIFESTATION OF DEBT” (GALIANI).**

Most traditional societies (what we used to call primitive) have mechanisms for saving and then distributing such savings over time within the group. Individuals in traditional societies produce certain savings for particular recurring purposes, as in a replacement fund to replace the minimum materials for survival, or in a peasant society, a rental fund paid to those who hold control of land, creating a fund of power (Wolf, 1966). In ancient societies, those of complex nature, we find institutions

that function to the same end to organize savings and redistribute them over time for specific use by different actors. Savings can be transferred in different forms in different cultures over time as Einzig (1947) and Herskovits (1940) demonstrated. What we are concerned with is not the outward form of saving and investment, nor the physical features of transfer, such as, stone wheels in Yap, paper money in China, commercial drafts and bills of exchange or banknotes. What are important are the ideas that stand behind such manifestations of behavior and the social power that banking creates. The reason why we fear banks is the same reason they exist

and why they come to dominate society. In the 1940s, Rist (1940) attempted to extend the survey of monetary theory that Monroe (1923) had produced as a means of defining the process involved in the evolution of modern banking theory. Here the author will define a more uniformitarian view across time, civilizations and cultures.

Analyses of economic trends and phenomenon across time are few in number; those across time and culture are rare. It is unfortunate that the recent Reinhart and Rogoff (2010)'s paper has been found to be flawed as it calls into question the reliability of such studies. It is not important to know why Reinhart and Rogoff (2010)'s paper is incorrect or why the authors of the critique (Herndon et al., 2013) have pointed to a number of methodological, statistical errors and problems in interpretation of data. What is of significance is the role of debt in their paper and in later publications. As will be discussed here, debt has replaced inflation. The fact that most Americans' income has been stagnant since the 1970s (Johnston, 2013) has meant they have replaced earnings with debt to be able to own homes, go on vacations and afford a middle class lifestyle. While debt has increased dramatically, assets of all classes from gold to homes have appreciated tremendously and while there has been some deflation since the credit crisis began in 2008, it has not been sufficient to place most Americans' needs within their income. We will require significant deflation to achieve that end or a commensurate increase in incomes to match the gap between say, house prices and savings and income. Eccles (1951) argued that inequality had a role in bringing on the Great Depression. But deflation, as seen during the Great Depression, resulted in a drop of inequality (U.S. Congress Joint Economic Committee, 2010) and that would be a positive outcome as seen below.

The ability to save and transfer wealth is at the core of the successful society. Some simple bee species have queens who are able to produce a brood at the beginning of spring and these mature to help her enlarge the group but they are not able to store food to survive a winter and only the queen is able to sustain herself by a form of hibernation until the next spring. Honey bees have achieved the level of organization to sustain a population from one spring to another by caching the products of plants in the form of honey (Wilson, 1975). In like measure, human societies as they become more densely populated are characterized by a greater ability to produce resources that can sustain complexity and specialization over time allowing for other sustaining adaptations like buildings and institutions. This achievement, the production of surpluses, was the great invention of the Neolithic period some 10,000 years ago.

## THE SURPLUS AND REDISTRIBUTION

Every traditional society since the beginning of the

Neolithic engaged in the production of surpluses. The evidence for this is in the granaries found in the earliest sedentary dwellings. A necessary component to successful food production, which was the hallmark of the Neolithic transition from hunting and gathering where surpluses seldom existed (though evidence for incipient saving can be found in the caches in walls and floors of paleohunter caves (Harrington, 1960) was the saving of some grain for spring planting. We assume from the archaeological evidence that the transition was gradual with hunters and gatherers harvesting natural stands of grains and then weeding out those plants that did not produce edible products and finally selecting seeds from those plants that produced the most abundant crops. A process of domestication and human selection created the food producing explosion beginning some 12,000 years ago (Lamberg-Karlovsky and Sabloff, 1974).

Saving some of the harvest for planting seed or regulated consumption over unproductive months led to common family and tribal surpluses managed by clan elders and ritually dispersed as we see in ethnohistorical documentation of Melanesian "Big men" (Codrington, 1957) or is recorded from pre-dynastic Egypt (Wilson, 1951). Banks today are essentially this redistribution element; people pay into a common stock and withdraw their share when needed. The history of Western banking since the 14<sup>th</sup> century bears this out. The collapse of the harvest could be hedged by the surplus to some extent and our earliest documents written in the Middle East are ledgers recording the collection of surpluses and the transfer of credits on production (Kramer, 1981). The failure of the harvest could only be protected by the intervention of the spirit world and the actions of shaman and priests were the first attempts at making predictions on productivity (Childe, 1953).

Trust in the spirits and in the efficacy of the shaman and priest gave some confidence to people, though both still often failed. The credit of the common store could sustain families in lineages whose harvests failed or were attacked by pests. Reliance on kinship ties to compensate for losses was the foundation of credit within groups and the faith in kinship bonds is the true meaning of the word "credit" (Firth and Yamey, 1964). In many traditional settings, however, the means to exchange varies considerably allowing a kind of everyday fiat money and credit as temporary extensions of value. Douglas called some of these mechanisms "primitive rationing," and their application provided a unique look at the diversity of types of "money" as well as credit instruments in the traditional world (Douglas, 1967). In a cross-cultural analysis we cannot speak of one theory of money, nor of one idea of value. As Herodotus tells us, for example, the Spartans used iron as the medium of exchange and forbid the entry of gold and silver into their city. All societies appear to have some object(s) wherein its ideology resides value; as among the Trobriand Islanders where certain yams become tokway and can be used in

reciprocal exchange (Lee, 1959), and while taro is the main food source, yams are eaten but have symbolic value and taro does not.

Simmel (1907) argued that money provided an abstraction, an anonymity which "liberated" humans from kin-based distinctions. This idea has had considerable power among some theorists of the role of money in social complexity (Turner, 1986; Maurer, 2006). But this is largely an ideological perception and not one based on any specific knowledge of the evolution of the role of money in early societies; for example, before Sumer or in pre-Dynastic Egypt. In fact, we find contemporary social relations built on the structure of kinship and not the atomized ideal associated with modernity.

*"The unit of the ancient society was the family, of a modern society, the individual. The movement of the progressive societies has been uniform with respect to the gradual dissolution of family dependency and the growth of individual obligation in its place" Sir Henry Maine, Ancient Law, 1861.*

Maine's dictum stands in most economic theory today as the foundation for market economy. However, wealth transfers in modern societies undermine this theory. In 1901, 90% of German-Americans died testate compared to only 21% of "Yankees". German-Americans tended to cluster in family communities and to control the transfer of wealth generationally. This changed from 1901 to 1981 where German-Americans died testate at 75 to 80% and "Yankees" at 44% by 1930 and 66% by 1981. State interference in wealth transfers in America has been insignificant as it has the effect of taxes (Clignet, 1998).

The inheritance of wealth provides each generation with means to control resources and American inheritance has shaped our political and economic institutions. Hentricks (2007) found that bequests and retirement wealth characterized the top 1% of the population over time.

In many contexts, money is a representation of allegiance and power; its use, persistence and acceptance in exchange is a demonstration of obedience and alliance as when the American rebels formed the alliance that was the American Revolution against Great Britain in 1776 (Newman, 1990). Similar variations in acceptance occurred during the American Civil War with the printing of the "Confederate" dollars and interest bearing notes (Lerner, 1955; Makinen and Woodward, 1999). Acceptance and circulation of money represents not only an abstraction of value but the nature of power. Study of the effects of western currencies among native peoples under colonial conditions is a study of power as much as concepts of convertibility. The idea of "special purpose" money vs "general purpose" money (Dalton, 1965; Strathern, 2005) should be seen in this context.

Today many people collect forms of money as a fetish whose "value" often resides as much in prestige of

possession of a new form (derivatives, for example, where people bought this instrument without any understanding of its structure or nature (Tett, 2009; Caldararo, 2009) than its ability to be a medium of exchange. Value is culturally constructed behavior and depends on ideas that structure cultural performances. Among the Bella Coola, for instance, the value of a copper depends on the past behavior of its owner. This means how much has to be "put into it" by giving away gifts that assign value to it (Lee, 1959; McIlwraith, 1948). When European traders flooded the territory of the Bella Coola with manufactured coppers, no inflation or deflation resulted as these new coppers had no performed history. The same is true of our financial instruments: the value of a derivative product secured against loss in another asset by an investor depends on the accepted representation by the seller of the derivative that it will produce sufficient value return in the event of loss in the asset. This is dependant on the performance of the seller inherent in his or her representation of the financial instrument and those on which the seller can convince the buyer they can command (Callon, 1998; Caldararo, 2011). One can note the construction of Asset Backed Securities by Paulson for Goldman Sachs clients that were even recognized by the creators and sellers as near worthless and they bet against them. Details are in Felix Salmon's April 16, 2010 article in Reuters ("Goldman's Abacus Lies"). This is parallel to hedge funds and other sellers of financial schemes and instruments, like the behavior of Bernard Madoff and may require performances in court to represent the values involved to existing cultural norms. Such representations include things like the off balance sheet devices used by Enron and "transfer pricing" by corporations which distort the value of companies' profits (surplus) creating false representations. Here we have to distinguish between Schumpeter's (1939) "excess speculation" that causes booms and panics, and Cipolla's (1976) idea of "investment opportunities." One is directed primarily to gambling and paper windfalls, while the other creates excess productive capacity for growth but has eventually benefits.

More pertinent to today's credit crisis is a discussion of the history of money among the Daribi of Melanesia (Counts and Dorothy, 1970). David and Dorothy Counts studied the use of indigenous money among the Kaliai and described it as general purpose money similar in every way to that of industrialized nations. When outside money was introduced it was assumed that a crisis would result. Instead this foreign money, Australian dollars, was interchangeable. Robbins and Akin (1999) go to great lengths to explain how later the Counts and David (1977) found the Kaliai had drastically changed their attitudes about money once independence was to take place and new money was set to become the official tender. Ideas of the "rule of money" became a new context of exchange that had been smooth and continuous since the introduction of Australian money came to circulate with

the indigenous money, the vula. Robbins and Akin (1999) argue that different kinds of exchange are linked to relationships and kinds of objects among the Kaliai and even the use of their own traditional money threatened these associations at times. Robbins and Akin (1999) rely on the “spheres of exchange” idea of Bohannon (1959) modified by later information from African studies.

The Melanesian situation cannot be used without reference to the power context of the colonial situation, as seems the case in other locations. Where people have no stable customary associations with the value of money, which applies to the Kaliai transition from the original description by the Counts and Dorothy, (1970) to the later political reorganization (Count and Count, 1977), they will respond by transferring value to social relations or their surrogates in institutions (kin groups, sodalities, unions, mutuals, etc.). Every monetary transaction has elements of social relation embedded in it, from the “tab” in a bar to credit in the corner grocery in a working class neighborhood. An example is a study of a grocery owner in San Francisco who lent money by keeping tabs for residents and workers. While no interest was applied to balances, individual tab owners were pressured to pay down amounts by reducing available new credit (Caldararo, 2004). Similar bar tabs are referred to in a new book of cuneiform translations from the Achaemenid Empire (George et al., 2011).

But when the social or political context changes, as seen in Germany during the 1920s and early 1930s in the post-WWI period when the value of money fell in the context of a political crisis, the emphasis of social relations and money changes (Schnable, 2004). Also, the obverse can occur where the value of money is contained, as during the Great Depression in the USA, but its use and frequency of circulation is curtailed. People responded by replacing money (official fiat money) with social relations (unions, families, etc.) or with local money (depression script) or contextual credit (“Hobo money”) (Richey, 2007). Today, we see the same process taking place in Europe where the continued existence of the euro is causing people to respond to economic exchange by reforming social contexts, especially in Greece.

In some views of the theory of money, for example, at the time of John Law, money was considered elastic, as was credit its adjunct. It was considered by Law to exist only to serve the needs of trade and exchange, so that it would expand and contract given the production of goods and services, their consumption and the process of exchange to further trade. In fact, Law went so far as to claim that all money belonged to the king or state and that its manipulation (augmentation and diminution) was necessary for prosperity (Rist, 1940). Inflation and deflation could be used to prevent certain pernicious behavior, hoarding on one extreme and speculation on the other. But the control of this elasticity has as often been abused as it used to benefit society. We can compare

the experience of the past 400 years in the west to that of the Roman Empire and see similar tendencies in this regard (Rostovtzeff, 1957). To deflate money depreciates the savings of the many who are prudent, and as Adam Smith (1776) noted, no nation can be long prosperous unless its citizens can be confident in the security of the fruits of their labor. Instruments of credit and paper money are intended in many theories of money to speed its use and reduce the tendency to hoard. This is different from when during periods of deflation money appreciates in value.

Following Law’s logic one might assert that all exchange of representative money is dealing in debt, unless one is dealing in barter or precious metals or gems. In this line of reasoning, when exchanging representative money, whether one respects the face value of fiat money in transactions, accepts letters of credit or tranches of bundled mortgages, the medium is a form of debt; the most common today in America is the exchange of Federal Reserve notes which cannot be redeemed for silver. In essence we might look at the various grouping of such representative money in the form of the money supply, called M1 (total cash in circulation and checks), M2 (M1 plus savings accounts in commercial banks) and M3 (M1 + M2 plus liquid assets such as Treasuries, Agencies, savings bonds, commercial paper, bankers acceptances, Eurodollar holdings of US residents, derivatives and swaps). Ultimately in this view, every dollar bill is a debt the taxpayer/citizen has allowed his or her government to assume by circulating the currency.

Money supply tracking was confident prior to 1982 when it began to fluctuate unaccountably, with M1 rising in 4 weeks 12.6% (Gartner, 1982). The Fed and most economists began to deemphasize M1 after this and more attention was placed on M2 which seemed more stable but by the early 1990s, according to H.C.K Liu (2002), its use was undercut by an increasing volume of alternative saving outlets and M2 was showing increased velocity. From September 1979 to September of 1985, the M1 grew at an annual rate of 8.3% compared with the previous five years when the rate was 6.2%. Some economists attributed the failure of stability on the abandonment of gold as an anchor limiting the issue of currencies. For example, David Fand argued (Brookes, 1985) in reference to the 93 years of Milton Freidman’s monetarist research model, “It is clear that the tenets of monetarism hold only when the dollar is convertible (with gold) and that when the dollar is convertible, monetarism is irrelevant.”

Today hedge funds and other investors bet on minor movements in prices to make profits, financial entities and investment banks bundle thousands of loans into securities (ABS) and when these fail, as they did in the recent credit crisis, individual investors lose their money or the federal government buys them. The theory behind this betting and bundling is that it reduces volatility in markets and produces more credit. Given that we can

hardly call the period since the relaxation of rules on finance beginning in the 1970s to 2009 as stable, or not characterized by volatility (Friday, 1987; S&L collapse in 1990s; Dot come crash, etc.) one has to ask what does support this theory. The idea that it provides more credit for consumer goods and housing is curious, since extending credit must be based on some rational assumption of repayment. The design of the subprime loans and the extension of credit card debt in the past two decades was beyond the ability of most borrowers to repay. Thus encouraging this debt was irrational. However, given that modern global economies are based on consumer society, in that context it is logical, if not rational. As demonstrated in the author's 2004 book, consumer society is only one possible way to organize a complex society; the current dilemma is how to modify this consumerism to something less destructive and wasteful.

It is argued that inflation has remained low during the past 20 years, at least since the Carter Presidency and Volker instituted new Fed policy. What has happened is that the wages and earning power of the average American has remained static since 1968 (Haskins, 2011 at <http://www.brookings.edu/press/Books/2009/creatinganopportunitysociety.aspx> and Mendelsohn, 2011); yet demand has remained high over this period, even given recessions, and continues today while we have over 8% unemployment and have been varying between 8 and 9 for two years. Inflation has been under control in recent decades given that demand, which has commanded production (supply), has been sustained because credit has been extended to the average American allowing them to continue to buy goods even though their incomes and savings have been static at a time when jobs are being off shored to less expensive manufacturing and service economies keeping real prices low. Thus instead of inflation we have debt. Antony Herrey, in a letter to the Financial Times (March 16<sup>th</sup>, 2013), argues that this debt can be seen in the inflation of value in the stock market. He notes that on October 9<sup>th</sup> of 2007 the stock market was at 14,146.53 and gold at \$738.70 an ounce, a quotient value of 19.17. On March 8<sup>th</sup> of 2013 the Dow closed at 14,397.07 and gold was at \$1,579.02 or a quotient of 9.12 of the Dow in terms of gold. One can say that the stocks have lost about half their value since 2007 by this measure.

In the face of hundreds of thousands of foreclosed homes, of Bank of America (Rupp, 2011) bulldozing empty foreclosed homes, one has to ask, how is necessary this? Do we have a housing crisis or a space crisis, since banks set the bar for what kind of construction builders can finance? Perhaps the banks are missing the point. Why have our houses become so big, why are we not building more rental housing? As for consumer goods and the billions of written off credit card balances the banks have charged against profits sine 2007, we have to ask was this necessary? While millions

of American jobs were off shored to Asia, Americans were encouraged to go into debt to buy the products they used to make. Wealth inequality has increased dramatically since the 1970s (Sherman and Stone, 2010) and especially between ethnic groups (Kochhar et al., 2011). This makes no sense. It parallels what happened in the Roman Republic according to Rostovtzeff (1957) where taxation was gradually shifted to the working and middle classes to the detriment of small business and farming and fueled the instability that furthered the Civil War and the rise of Augustus and what Rostovtzeff calls Roman State Capitalism. So why do we follow the banks?

In studying changes in the surplus and its distribution in different societies with a variety of social organization and economic means, some students of behavior have found significant associations in stability and structure of societies over time. Sahlins (1958) in an analysis of Polynesian societies found that there was a close relationship between surplus production and the degree of social stratification. That is without redistribution mechanism; an increased surplus increases inequality and stratification. Hole (1974) and Toynbee (1966) suggest that a change in the amount of the surplus and failure of redistributive mechanisms in tradition resulted first in expansion and then destructive warfare, both internally and externally in sumer. In like manner, we can consider the increase in notional value of equities, bonds, derivatives, property, commodities and other financial instruments, as an increase in the idealized surplus which drove consumption. The distribution of this surplus has not been uniform, rather has increased the wealth inequality of the world's economies. This is especially problematic given that most earners' incomes have been stagnant and their consumption over the past two decades largely financed by debt. Wilson (1951) found the same relation in Egypt and one can argue, from similar historical and ethno-historical data that India's apparent stability was based on an unchanging surplus and like European Feudalism, an inherent social inequality structure that could be stable only while the surplus as also stable. This argues for considerable stress in India's future that can be seen presently growing.

Cipolla (1976) has shown that before the Reformation, ecclesiastical hand holding in Europe ranged between one-third and one half of the land. One effect of the Reformation was the expropriation of church lands in the Protestant areas which greatly spurred economic development and production, along with the new wealth from the colonies and slave labor in mines and plantations provided the financial basis for the Industrial Revolution. Yet we might also attribute a major role to education. While Florence in 1313 established the first public schools and mass education, it was not until after the Reformation that education was widely extended in Protestant countries, while Catholic countries lagged far behind (Cipolla, 1976).

Thus in this section we have associated banks (as a

behavior of saving) with the surplus of society, both through the production of debt and the control of wealth over generations as a means of preserving both the surplus and debt it represents over time. We fear the loss of the surplus, yet banks assume the ideal of its preservation and transition; they have come to stand against the feared failure of crops, loss of wealth in a herd of cattle or a buried trove of silver, that is, of wealth over time, of labor's treasure.

## THEORIES OF VALUE OR MAGIC

Essentially banks have played three roles since the invention of value over 5,000 years ago. The basic idea is to be able to transform something of use, a crop, items of manufacture, animals, minerals, etc. into a device that can be transferred over time and space easily. Herodotus tells us that the Spartans refused to allow gold or silver into their city as they recognized the ability of these metals to corrupt people and undermine the solidarity of Spartan life. This awe of the metals was associated with the symbol of value, but not central to it. Rather, the creation of money reflects the ability of humans to abstract an amount of value (crop, etc.) and to displace it in an equal form in time and space. This is a magical transformation and yet that process is found in other animals who cache food over time and space (Vanderwall, 1990; von Frisch, 1979; Caldararo, 2009a; Caldararo, 2009b).

Banks have functioned over the past 500 years in the modern form of their existence as entities to provide three main functions: a utility to process payments for goods and services in a community; a repository of credit where people deposit their gains for future use; and a means of distributing those deposits as loans to innovators or producers for future gain. Banks create credit by loaning out more money than they take in via a scheme of probability in demand deposit turnover that has worked well for over 500 years (Samuelson, 1976). It does sometimes fail and then banks fail.

As mentioned, crops sometimes fail and the surplus is lost. This is a catastrophe and every good shaman knows how to associate positive outcomes with his abilities and to distribute to others (they failed to pray correctly, did not sacrifice in the right amount, etc.) the negative outcomes. The author has demonstrated how the creation of wealth, like the saving of the ill by priests, is embedded in magic in many societies and how people in the past 2 centuries have responded to the market and to its salesmen is very much like how people react to religion (Caldararo, 2011). Bankers are priests of finance and we fear their power over the surplus.

The Soviets tried to create a banking system, the Gosbank, to act in this same fashion, but it could not function as more than a utility and state credit agency due to its lack of independence (Degross, 1964). Banks

in a capitalist society compete with governments to produce credit; kings and republics need credit and though they can produce coinage and print money. The theory of banking has shown that they lack the magic of independent credit production, the proverbial "golden goose."

Banks's function partly to provide funds for investment by innovators was central to how Schumpeter (1939) saw evolution being driven in capitalism. New techniques and new products drove old, inefficient means out of the market and better products had the same effect, though this last is often questionable as most products succeed by virtue of novelty alone at the bidding of advertising. But historically banks have had two general avenues of operation, one to be a repository of capital where traders or producers could with confidence deposit gold, silver or coin and receive a note indicating the amount deposited and date. The note was a surety that the capital would be in the bank when the depositor required it. Van Dillen's (1934) comprehensive study of the origins of modern banking demonstrated that some banks were not honest in this course, but even the Bank of Amsterdam lent these funds for profit.

The other avenue of operation of banks was as creator of circulating credit, a bank-note which the bank makes on deposit to exchange "on sight" to any demand for that capital deposited (as circulating credit). A trader or producer might deposit a sum and then use the bank-note to purchase some service or commodity. He signs the note endorsing its transfer to the seller, the seller can then take the bank-note to the bank which issued the note and retrieve the capital. The bank may have lent out the capital in the meantime, but has sufficient funds, theoretically, to cover the transaction. The question then is has the bank created money? One might agree that it has provided credit. If that credit is useful and results in innovation or increased productive capacity that is useful (has a market) then the bank's credit is repaid with interest. If there is a failure to repay then not only does the bank have a net loss in credit (unless secured in some fashion) and a loss in potential profit (and other opportunities) but no new productivity has resulted. The store of deposits and investors' shares may not have been lost but the bank's operations may fail if credit does not produce profit. No matter what form of representative money is produced, as Galiani (1750) noted in the opening quote in his, *Della Moneta*, it is a debt.

It is obvious that the role of money can vary as a purchasing agency or a storage of value, but types of money can lose value whether they are paper units, debased coinage, silver or gold units. Precious metals go up and down in value. Rist (1940) called John Law a "currency crank" and defined this as one who creates a scheme to utilize the public as a means of transferring value in the economy. That such schemes often work temporarily, as Law's did, only encourages others as convertibility will vary over time and given circumstances.

Creators of financial instruments should be considered in the same framework; their inventions often succeed for a time, but usually create serious disruptions in economies as Schumpeter (1939) noted in the period before the Great Depression and in other financial panics. So what is the responsibility of such innovators for their products?

This addresses the central issue of banking, for the bank is an association of partners who have submitted some amount of capital for the formation and operation of the bank. They take the risk that there will always be sufficient deposits to pay any number of demands at any one time; the failure of this probability then falls on them to satisfy the shortfall. As long as the bank's loans are paid with interest, the proposition of the bank is successful; if they fail and demands are many then the bank fails and the partners many become bankrupts. Still, have they created money? If so, how does this differ from a king who simply debases his currency? It is certain that if a king fails to pay he cannot become bankrupt; he may ravage his lenders and place them in irons, or like Argentina in the 1990s, simply ignore his debt and create new bonds to over old ones. The faith in lenders or in his people to pay the debt is then central to his success.

The ultimate decision in these two cases can only be determined by examining the grounds of each. If the bankers' loans are made good then they have practiced good banking and the benefits of their art result in more commerce and manufactures which all the country enjoys to some minor extent. If the king, as for example, Ferdinand and Isabella, borrow money or print it to pay for the discovery of the Indies and are successful the same result takes place. So we can see that the only difference is in not means but ends, for while some might argue that kings can change the law to legalize their actions, bankers also through buying influence can change laws as they did in the 1990s overturning the provisions of the Glas-Steagall Act. This allowed more risk and then in the debt crisis their influence, supported by the awe of banking, allowed them access to the full faith of government to support their failure. Essentially all credit today is backed by the taxpayers either in supporting collapsed banks and depositors' accounts or in the courts where the cost of disputation falls ultimately on the government. Just as in the collapse of Long Term Capital Management in 1998, it was the guarantee of the government that staunches the disaster (Partnoy, 2003).

In addition to these examples, there is another: the operation of the "mutual" from their first appearance in complex society in Rome in the Republican period (Rostovtzeff, 1957), to their existence today as credit unions for different labor groups. These financial institutions have functioned to provide credit for their members. We might find their origins in the kinship responsibilities and reciprocities of traditional societies (Goody, 1971). We find even today in some cultures individuals operating as middle men in the transfer and

deposit of sums of money. They are traditionally held to be responsible and believed to possess an integrity that is unimpeachable; their function is one that is crucial to many elements of social economic life. This aura of responsibility and morality is shared by modern bankers to some extent. An example of this system became a focus of concern after the 9/11 events (Frantz, 2001), but the Middle Eastern examples, called hawala, show the simple origins of banking (Passas, 2003).

Value as an indeterminate concept or entity can be seen as mana in the Melanesia interpretation by Codrington (1957). A banker can produce value by lending someone for the purchase of a house, say \$100,000 and then charging interest at repayment over 30 years. Depending on the interest rate the value created by the loan and interest can be as much as 3 times the value of the loan, thus creating 3 times the original value. This loan can be sold and resold on expectation of payment of the loan at the interest rate over the period. Another form of magic is when a property is appraised at sale or construction. An appraiser may value a property on expectation of sale in a certain prophesied market at a certain value and this, blessed by a banker is then the value of the property for the purpose of gaining a loan or finding a buyer. As we have seen in the recent subprime mortgage meltdown, reality can be far different from the image of value prophesied by the appraiser and banker. Nevertheless, these values were treated as real by people who bought homes, took out loans and by the investors who bought the derivative tranches. It did, however, evaporate as clearly as the ectoplasm of a ghost.

## **ALIENATION OF THE SURPLUS OR DIVISION OF COMMONS**

The transition from the clan common holding of the surplus to the property of a single clan or specific group within a sedentary village required the legitimacy of either religion or law, most likely both. Even through the Old Kingdom and the First Intermediate Period in Egypt surpluses were considered common property held in trust by the political representative, the Pharaoh (Wilson, 1951).

In the Middle Ages runaway serfs built up communities of vagabonds who made goods and traded food and other goods, eventually creating villages and towns based on their guilds' power against the Church and nobles. Cipolla (1976) argues that from the fifth to the eleventh century "there were practically no financial mechanisms to facilitate the transformation of saving into investment." The life of Godric of Finchdale (born towards the end of the eleventh Century) typifies the rise of traders with their peddlers' packs of items as they tramped across Europe (Pirenne, 1933). Eventually two great guild bodies arose in conflict, the guild of producers

(crafts) and that of merchants. Both tried to build up stores of credit to purchase power in their struggle for ascendance.

Unlike the struggle envisioned by Marx, this struggle was not workers vs owners as both the producers (craftspeople mainly) and merchants were free of the control of others or ownership. Perhaps if Marx had not placed so much emphasis on his conception of class society his analysis might have been more useful and durable. The contest for credit, however, was a struggle of trust and organization. Much of Adam Smith's *Wealth of Nations* (1776) is taken up with this issue in the struggle by various businesses eventually using monopoly and the control of government to this end.

Cipolla (1976) begins his tracing of credit formation in Europe from the deferred payments for goods (sale credits) sold between producers, consumers and traders where we have some basic documents from the Middle Ages (Postan, 1973). These informal agreements evolved into the basis for the contract in dividing profits and spreading risk in trade. Innovations were introduced so that by the 10<sup>th</sup> century the *contratto di commendas* appear (called the *collegantia* in Venice). These were essentially transparent, social agreements made in public. Cipolla (1976) produces one from Genoa in 1198 A.D. where two merchants and the humble towns people agree to a contract where the people provide the cash for a trading venture and the merchants agree to a specific division of the profits if there are any. There are many agreements of this type that have come down to us from this period, of a democratic and free exposition of the extension of credit and division of profits. But Cipolla also shows how investment became increasingly private, organized around kinship of certain families by the late 13<sup>th</sup> century with the *compagnia* or *corpi di compagnia* replacing the more open *collegantia*. So what begins as an open social compact becomes more secretive and limited.

In the later Middle Ages the merchants, or a class of them, won eventually and did so by establishing mechanisms in which credit could be cached confidently over time and transferred across the geography. The check (that is, a circulating credit) was one vehicle for this, but the idea of credit and of personal responsibility was what gave the foundations of the first banks in merchant houses their great victory over the crafts guilds. Both guilds were engaged in the discipline of their members as can be seen in the charters and rules governing membership, fees and fines for progressing in them and punishments for behavior considered to be detrimental to the guilds. Benham (1931) gives verbatim the edicts, ordinances, rules and fines of the cardmakers beginning in 1628 when they received their royal charter, and these are typical of other guilds.

This struggle among the guilds of craftspeople and the traders intensified into the Renaissance and by the time of the Reformation great houses of merchants had

evolved into trading banks with the effect of a division between the traders and these incipient banks (Pirenne, 1933). Machiavelli tells of the brutal city warfare between factions in Italian towns struggling over the wealth produced by rising capitalist industry and trade. Bankers like the Medici could use their credit to buy the services of mercenaries as could the crafts guilds and a caste of warriors nearly became established in Europe in the Middle Ages. One group formed as a "company" was the Catalan Grand Company. This was fashioned from veterans of the wars of the Sicilian Vespers (1282-1302) and led by Roger of Flor. Hired by the Byzantine Emperor Andronicus II in 1302, it operated in Greece where it achieved major successes. The company remained together after Roger's murder in 1305. It had formal statutes, and possessed its own seal. Its success was assured after it defeated the Duke of Athens at the battle of Kephissos in 1311, and the Catalans remained dominant in Greece until the 1380s. In Italy in 1339 another group, the Company of St George, formed of Swiss, Germans, and Italians, came close to defeating Milan. The Great Company, founded in 1349 by Werner of Urslingen, had a continued existence under several leaders until 1363. Large profits were made from booty and taking of prisoners who were held for ransom and by exacting protection money from the cities (Mallett, 1974). As Cipolla (1974) notes, transfers of wealth are either voluntary or compulsory. Voluntary transfers include gifts, charity, doweries and gambling. Compulsory include taxation, plundering, highway robbery and theft. The laws of the Ine of Wessex distinguished between these only by the number of men involved. Less than 7 was that of thieves, between 7 and 35 was the work of gangs, and 35 or more was a military expedition. Extracting wealth from producers is often accompanied by means of violence or fraud, the ends are the same.

Within the rising class of merchants in localities and regions there early began to appear divisions of interests in price and finance and there came to be established a class of local official brokers, the *Unterkauf* in Germany and the *sensales* in Venice, who represented local interests in trade and banking (Pirenne, 1933). One might say that the attack on traditional forms of money changing and transferring like the *hawala* and the *fel qian*, is reminiscent of earlier Medieval struggles in banking on national schemes. While the one undertaken after 9/11 was ostensibly due to the terrorist attacks, such excuses to standardize communal means of saving and credit are not new. Several are examined in the volume edited by Firth and Yamey (1964).

The struggle for authority is often the focus of most histories of Europe, as in that between the kings and Popes (Bryce, 1956), but the conquest of credit is a seldom told tale and one that has played a central role in the development of nations and industries. Most recently the role of venture capital has been seen as a formative element in the rise of new technologies since the Second



World War (Jacobs, 1969), but the flow of capital is a powerful motive force that has yet to be given its due in the history of human affairs.

We see this struggle breaking out especially during periods of recession or depression (Schumpeter, 1939), but the great periods of upheaval are characterized by coalitions of sectors, for example in 1789 of the professions like the Jacobins led by the doctor Marat and made up of urban elite of philosophers of a more federalist bent, or the Girondists (led by lawyers, merchants and publishers) more regional in view were allied with the lumpen masses and working proletariat against royalty and nobility (Michelet, 1972; Kropotkin, 1927);, in 1848 a divided professional class across Europe allied partly with royalty and partly with the lumpen and proletariat due to the increasing pressures in innovations in industry as Robertson (1952) so brilliantly describes, or in the American period of Progressivism with the professions allied against monopoly and banking (Starr, 1985).

Perhaps these diverse interests explain why revolutions are so seldom successful, but why the technological transformations of the 19<sup>th</sup> century produced a class of professionals who defined by their identity the solidarity necessary to establish a new way of life in the middle class (Moraze, 1966). This triumph was based, however, on a long history of opposition to the ancient authority of feudalism and the solidarity of pioneers. As Coulton (1925) detailed, the destruction of feudalism created the first wave of pioneers within Europe in the 13<sup>th</sup> century to the 15<sup>th</sup> with runaway serfs and freed serfs forming the backbone of new settlements, existing independently and in opposition often to the old. Some of these settlements were authorized by secular princes, some by investors, but the settlers were men and women who verged on the edge of lawlessness. This pattern continued in America and is one reasonable explanation for the success of the American Revolution and America's continue tradition of anti-authoritarianism, though denominationalism has certainly been a powerful contributory force (Niebuhr, 1957).

As mentioned above, however, one victory of capital was at the end of the Reformation with the dissolution of the wealth of the churches. Cipolla (1976) finds that the percentage of clergy at the end of the 17<sup>th</sup> century was about 1% of the European population and the income of the church was one source of power that contested for control with the guilds, the kings and the nobility. The wealth of the church has been free of taxation in America and its share of the surplus has grown unchecked (Dreiser, 1931).

## **BANKERS VS ALL OTHERS**

Certainly within the struggle of the guilds, as have been defined, there are other motivations, nationalism, racism, religious intolerance. There are other struggles of lan-

downers versus merchants, both wholesale locally and exporters that Adam Smith (1776) uses as a vehicle for explaining the effects of price on surpluses. The guild of bankers is also at war against itself or capitalism would not evolve as Schumpeter (1939) has so clearly recognized. The failure of Marxist and capitalist philosophers of the 19<sup>th</sup> and 20<sup>th</sup> centuries was their joint dependence on the concept of the duality of social struggle: capital vs labor. The result was the Soviet Union- a dictatorship of labor and Nazi Germany- a dictatorship of capital. What is needed is a more complex paradigm; one that can integrate variations like Japan, contemporary China, Sweden and India. The author attempted to produce such a model in his 2004 book. The real battle is over how to divide the surplus and who should get what portions of it. The destruction of kinship ties results not only in the elimination of the solidarity of groups but of the traditional means of sharing the surplus, especially in the atomization of the peasantry (Wolf, 1966).

This war continues today in a struggle over the wealth of society.

Doctors, whose education can go on for 10 to 15 years before they can practice, lawyers whose education seldom lasts half that long have recently been in conflict over quality of treatment and outcomes in medical procedures which has resulted in a significant reduction in the freedom of doctors to increase their income given rising litigation and insurance costs. However, when compared to the education of bankers, financial advisors and hedge fund managers, the educational experience of these professionals can include an MBA but often ends at a BA, the education of lawyers and doctors seems a poor investment indeed. Given the fact that many players involved in mergers and acquisitions, arbitrage and the production of contracts for IPOs, derivatives and packaging ABS are lawyers who profit from the results, the group of practitioners in the financial sector has a spotty training background (see: <http://www.independent.co.uk/student/career-planning/getting-job/its-not-easy-to-become-a-hedge-fund-manager--you-need-passion-and-instinct-775907.html>). While statistics are rare on actual education backgrounds of financial professionals, expectations in government documents indicate formal training requirements (<http://www.bls.gov/oco/ocos301.htm>). If their activities are so questionable in terms of outcome as described above, why have they dominated the division of the fruits of our economy for the past 30 years? Can it be that the primitive aura still functions in present modernity?

Cipolla (1976) has explained the role of the professions in reinforcing the prestige of the upper classes, but also in how they have appeared and asserted themselves in various societies or failed to do so. The struggle of the professions is an essential element to understand the history of the West.

Like all contests for control of society and its fruits, each contender must clothe their interests in symbols of

the society at large or represent these symbols in such a way as to recruit as many allies as possible to their cause. After the collapse of Republican government with the victory of Sulla, Roman society became bitterly divided in the struggle of one ambitious general or another who could rally factions of the old Republican parties, but the outcome was always the conquest of society and its wealth under one authority; only Pompey makes the mistake of taking the symbols of Republican government for the reality of power (Marsh, 1927). This same contest goes on today for the fruits of society and the bankers are ascendant because they are associated with the magic of profits and the benefits of the surplus. But this dominance is challenged by another group of professionals, the CEOs whose pay and benefits have also risen enormously in the past three decades (Murphy and Zabjnik, 2007).

### **DEBT, THE SURPLUS AND THE CURRENT CRISIS**

While the initial acts of the Bush administration was to save the banks with a variety of emergency measures including TARP, the underlying problem was employment and debt. As Irving Fisher had noted in the 1930s, the only way out of the debt spiral is employment which produces consumption and debt reduction. Instead, both the Bush and Obama administrations focused on the banks and investors rather than employment and innovation. As Keoun and Kuntz (2011) have shown in an analysis published in Bloomberg, support for the banking "aristocracy" from the Bush and Obama administrations was over \$1.2 trillion. Other support also benefited this same group, including the bail-outs of AIG and GM. This is only a fraction of the subsidies the banking and finance industry receives from the government. Probably the biggest share is the socialization of mortgage debt by Fannie Mae and Freddie Mac (as of March 2012 about 60% according to Report of the Board of Governors of the Federal Reserve System).

Current discussions on the world's financial condition seem to agree on two points: we have avoided an economic depression like that of 1929-1939, but that we came out of a recession which has not fully begun a consistent recovery. Over the period of "recovery" each stock market's drop has caused some reflection and we should consider that we are tracking the Great Depression. In this the author agrees with Krugman (2012). But does the data concerning depressions vs recessions really support such a conclusion? (see Chapter 5 for a full discussion of this question). In his 1933 article in *Econometrica*, Irving Fisher argued, against considerable skepticism, that policy actions by FDR had averted any further drop in the economy. Using a number of graphs he showed that deflation had not only halted but that there was a significant reflation. This is a key turning point; it did not stop job losses, but further substantial

deterioration in the stock market as the July 1932 41% drop did not take place and other asset classes also stabilized. It did define a change in the underlying economic activity of the nation. Saving the banks was the primary action undertaken by the FDR administration in 1933-4 and this had little effect on employment or recovery according to the comprehensive survey of Hawley (1968). Most of the production and employment data indicate that recovery did not take place until government spending increased demand in the private sector mainly after the 1937 "recession within the depression." Some economists have charged that FDR's spending did not end the Depression, and assert that only the war spending in the 1940s accomplished that (Shlaes, 2007). Of course, this belies the fact that the war spending was also government spending.

In October 2008 the Dow fell by 42% comparing nicely with the 47% drop in the Dow in Oct 1929, Banks stopped lending after the Crash in 1929 as they have today. No amount of Central Bank activity either in the US or Europe has been able to change this situation due to the massive bad debt still on bank's balance sheets and the perceived instability of the economy. It threatens the very existence of the EU. It took nearly 4 years for unemployment to reach 25% in 1933 after the Crash. Today, most estimates are at nearly 10% with underemployment bringing the total to over 16%. The growth in unemployment and its sustained level has outstripped any recent recession according to a New York Times article (Rampell, 2010). Given the slope of this trend we can expect the worst yet to come. We are three years into the cycle as Schumpeter (1939) has described the variations in business activity.

What Fisher argued was that by March 1933 liquidation of the massive debts produced by runaway "bad banking credit" had reached about 20%, while the same action had increased the dollar by 75% so that real debt had increased by 40%. But FDR's fiscal policies, including dropping the Gold Standard resulted in a reversal of deflation. Fisher projected that had FDR not acted as he did no bottom would have been reached in 1933 but a continued spiral down, Schumpeter's "creative destruction" as was characteristic in all earlier depressions with growing bankruptcies, unemployment and starvation.

The Bush Administration's actions under Hank Paulson were similar to those of FDR in that they acted to stop deflation which saved many large banks, but since then Obama's tax cuts and tax credits have done little, even an estimated 8 trillion in loans assumed or underwritten by the Federal Home Loan Association and the Fannie Mae and Freddie Mac have only expanded credit to financial institutions with little effect on employment. Housing prices will continue to fall and deflation will advance until massive employment can be created. The proposal in 2010 of a lending bank that will leverage some amount of money (proposed at \$50bn) to create such employment would have been a good step but

about \$950 billion short if a \$1 trillion amount of spending is expected as Paul Krugman has argued is necessary (Krugman, 2009).

While there was a drop in average wealth inequality after the Great Depression 90% of taxpayers in 1929 had lower disposable incomes than they had in 1922. The top 1% of taxpayers increased their disposable income by 63% and corporate profits increased by 62%. The losers were in the middle class as Krugman (2011) notes. Hendricks (2007) found that bequests and retirement wealth characterized the top 1% of the population over time.

All this supports the theory that panics and stock market crashes are similar to ritualized wealth transfers from commoners to elites in primitive societies (Caldararo, 2009b). So one might say the system is working perfectly.

## CONCLUSION AND THE FUTURE

This brings up the question of, do we need banks? As mentioned above the Soviets failed to produce a vibrant banking system and state controlled or partially owned banks as in Germany or Sweden have not fared much better than regulated banks in other countries, though highly regulated Canadian banks have. The rationale for the creation of the Federal Reserve System was to stabilize the banking industry and that, theoretically would benefit all citizens (Board of Governors, 1939). But the balancing of risk, like the creation of credit requires a supra societal entity whether divine or state, one with the stature Durkheim (1915) argued could capture the confidence of people, not that he considered this in relation to banking. However, the management of risk and purity is so contained in traditional society and seems to still be necessary today as Douglas (1966) argues. In the past 100 years only credit unions have escaped the ravages of collapse and ruin seen in the banking and savings and loan industry. Perhaps if we look at the history of banking in the Middle Ages and early modern period, the function of banking and risk was attendant to the expansion of industry and its ups and downs part of the necessary crises of innovation and creative destruction (Schumpeter, 1939). We have socialized the risk of banking under the concept that the existence and freedom of banks is necessary and benefits society in general much more than the cost of that risk. This is a generally unexplored assumption, though the experience of the Common Good Bank of the Friends (Spademan, 2006) might provide an experimental bit of evidence in this regard. We have to keep in mind that the Quakers founded Barclays Bank and that no restraint or philosophy will be perfect to force banks to function for communities. This relates best to the history of credit unions (Moody and Gilbert, 1984). The history of banking provides a rather less optimistic assessment (Rist, 1940).

It may be that the socialization of losses in banking only encourages risk and that protection of deposits and other support for saving should be limited to credit unions and other financial entities whose function is only as utilities. It seems today we need more than just measures to hold up a stagnated and weakened banking sector. We need a bank holiday, but this will have to go beyond the efforts of FDR in the 1930s. Nearly all the efforts to avert economic disaster since 2008 have been aimed to prop up the banking and finance industry under the theory that those efforts would prevent a depression and jump start the economy by promoting economic growth through loans and financial stability. This has failed as banks have stopped lending, not only in the USA but in Europe; the result of a globalized banking industry, in fact, many European banks received Fed support in the crisis. Banks continue to require Fed support by a near zero Fed interest rate and substantial aid from the Treasury in borrowing privileges. The banks, especially the largest American and European banks are comparable to Japanese "zombie" banks of the last two decades. Bank liabilities including non-performing loans in and outside of the residential mortgage industry and securitized bonds and derivatives have mounted, with problems in foreclosure procedures and lawsuits on the securitized loans transferred to the GSAs leading Freddie Mae and Fannie Mac to sue some for irregularities (see Lex Column, the Financial Times 6 September 2011 referring to the US Federal Housing Finance Agency's lawsuits against 17 financial institutions). Banks are holding foreclosed homes off the market to keep the value of existing inventory from falling even further and destabilizing the housing market in general. A bank holiday can resolve the present logjam by seizing the largest of these zombies like Bank of America and selling off their assets, writing off bad loans and splitting them into smaller banks. A stripped down and revitalized industry can result. This is ever more needed as we see rising numbers of home owners "underwater" on their loan to home value as reported in the Wall Street Journal (Timiraos, 6 September 2011) and the need for refinancing which the banks cannot produce. European banks are parking increased amounts of cash in the European Central Bank (see article by Ralph Atkins in the Financial Times, 6 September 2011) much like American banks have been doing over the past two years indicating an exceptional reluctance to lend to other banks, a clue to their fears of the stability of the banking industry.

Both Kenneth Rogoff and Gregory Mankiw argue that the country needs inflation to solve the debt problem (<http://www.bloomberg.com/apps/news?pid=newsarchive&sid=auyuQIA1IRV8&refer=home>). In the context of the Great Depression, Fisher approached a simpler problem and solution. What Fisher argued was that by March of 1933 liquidation of the massive debts produced by runaway debts "bad banking credit" had reached about 20%, while the same action had increased the dollar by

75% so that real debt had increased by 40%. But FDR's fiscal policies, including dropping the Gold Standard resulted in a reversal of deflation. Fisher projected that had FDR not acted as he did no bottom would have been reached in 1933 but a continued spiral down, Schumpeter's "creative destruction" as was characteristic in all earlier depressions with growing bankruptcies, unemployment and starvation.

It was obvious to Fisher that a reversal of the deflation was not enough, but that employment on a massive scale was necessary. The actions of Paulson, Bush's Treasury Secretary and Summer, Obama's Treasury Secretary have saved the economy from deflation, but no action like FDR's Gold Standard action has been considered. Simply pumping credit into the banks and the stock market speculators can only delay disaster. It is the nature of the power of money and credit that governs action here. In the first part of the Middle Ages the kings were strong enough to defy popes and even besiege Rome and storm the Vatican. By the later Middle Ages the popes had become so powerful that they possessed armies and could excommunicate kings, some of whom were forced to beg forgiveness. When bankers in the Middle Ages lent money to kings who then defaulted, the bankers could not foreclose; they had no armies to enforce their loans, and they often were bankrupted in the deal. Later, they learned they could join together and deny credit to nations and thereby bring kings to heel. As Financial Times writer, Philip Stephens reports in his September 13th 2011 column, nations across the globe have caved to the efforts of today's financiers whose collective efforts, led by "shop steward" Bob Diamond of Barclays Bank have undermined plans to regulate the industry and prevent a repeat of the cycles of credit booms and busts. By the modern period the new excommunication has become the credit rating and nations totter and politicians fall at the whim of the new pontiffs of debt.

Attempts to eliminate debts in traditional societies were often associated with customary means of doing so. While they were not always personal, for example, debts to the priesthood described by John A. Wilson in his book, *The Burden of Egypt*, University of Chicago Press, (1951), debtors could appeal to various officials for relief. Thorkild Jacobson reproduces letters concerning debts and debtors in early Akkadian letters (before 2,000 B.C.E.) in his book, *Letters from Mesopotamia*, University of Chicago Press, 1967.

Where such means fail, as in the development of complex societies like ours and that of Rome, for an ancient example, they become the basis for bitter social conflict. Italian historian Guglielmo Ferrero (his two best know books in English are *Greatness and Decline of Rome* in 5 volumes, 1909 and *Characters and Events in Roman History* which resulted from a series of lectures he gave in the USA at the invitation of President Theodore Roosevelt), argued that the rising debts in Rome due

partly to the Punic Wars and the destruction of Italy at the hands of Hannibal, left the average Roman peasant destitute. Debts mounted and the vast lands conquered by the wars were controlled by the rich and rising Knight class of investors and bankers. With no state money allocated to rebuild the countryside moneylenders gained control of great tracts of land.

Land redistribution laws and debt relief were proposed by a number of Tribunes, all were assassinated by the Senatorial Optima party to preserve the riches accumulated during and after the wars. Livius Drusus in 91 B.C.E. proposed a new law to abolish all debts, redistribute lands and spread the vote to all Italians. He too was assassinated and this murder led to increasing unrest and eventually to the great Social War two years later. At the end of this terrible war, laws passed during the consulship of Marius abolished three quarters of all debts and gave the vote to most Italians. These concessions and promises of reform led to the end of the war but soon afterward the kinds of swindles that led to the problem returned.

We should see that debt destabilizes social relations and undermines economic planning and creates uncertainty. Credit can be an effective means of promoting development of products and normal needs of capital improvements and distribution, but our current situation is built not of this kind of debt but of debt constructed from unrealistic projections of earnings and through financing unsustainable lifestyles.

As Ferrero shows, rising inequality produces the conditions for unsustainable debt where a nation's wealth is mismanaged to the benefit of a few at the detriment of the future of the commonwealth. While we may not imagine a horrific consequence as the Roman Social War, we are certainly aware of a rising feeling of unrest that shows we have approached a meridian of instability that cannot be contained.

Debt is difficult to erase, but it can be done. We have seen, as the FT reports on page one of its December 31, 2011 issue, a loss of 6.3 trillion dollars wiped off markets in 2011. The economic system did not collapse as a result. If the same amount was to be erased from world debt in the form of an Argentine-like debt restructuring of the 1990s, we could exit our immediate problem. This could be done by the IMF issuing new bonds that would be paid for by an international transaction tax on all financial transfers. EU debt, from Greek debt to Portugal would be simply repackaged. We should keep in mind that Britain's WWI debt is yet to be paid off; it was repackaged with no maturity debt in the 1930s. Britain did not go broke as a result. It is unlikely that the "shadow banking" system (see FT article by Tracy Alloway, 29 December 2011) could avoid such a tax if pursued by the technology allowed under America's Patriot Act and instituting such control would greatly stabilize the world economic system. What is interesting about the shadow banking system is its parallel to the problem bankers had

in the Middle Ages when kings and nobles would seize their assets. The invention of the letter of credit allowed wealth (gold, silver, property, etc.) to be hidden in a piece of paper and one could escape with a fortune in the lining of a coat. Today, billions can be hidden in a few lines of code hidden anywhere, best perhaps in hyperspace.

A new banking holiday and credit action as FDR accomplished is unlikely today due to current attitudes concerning bankers and banking, even though it is the only way to eliminate the “too big to fail” banks and the threat they pose to national economies. But why was FDR able to utilize governmental power to act to reorganize banking? It seems likely that it was partly because he enjoyed significant popular support or the support of powerful unions, though this obviously played a role. Rather the panic that the Hoover administration had been unable to control was spreading (Hawley, 1968). The fact that it began in the states first and in Canada may have been a factor. The much more powerful effects of mass media today and a near unified political position of the major parties and commentators are a more likely source to examine for this ability to staunch the mass fears that undermined the stature of banking in the early 1930s.

Today we still fear bankers because of their magical power over the economy and their ability to transfer wealth over distances including time, geography and from one form into another. They are modern alchemists, shaman and priests wrapped in the guise of salesmen and math wizards. They view the future in movements of capital in housing and the stock market and they can project a loan of a small sum into grand profits by the spiritual transformation of amortization. They are truly the anointed ones and within the temples of finance, that serve as the most prominent buildings of modern society; they store the prestige of power that can transform a community from poverty to prosperity. The Occupy Wall Street movement of the past year may express displeasure, dismay and anger at the financial world, but it still is held in check by the mystery of capital.

The challenge of finance in the 21<sup>st</sup> century will be the transformation of banking into a more transparent and rational system. If that can be done, will we lose the “magic?” Hart (1986) has argued that modern monetary policy is less flexible than Trobriand Islanders’ institutional economic practice because it is “still governed by a quasi-theological dogmatism.” Here the author has described this dogmatism and the inherent instability this dogmatism creates. Hart focuses on theories of money produced by this dogmatism and the influence of contradictory powers between states and markets, as the central problem in modern economies; while the author thinks it is the dogmatic foundation itself, as he has coined it, the “secular theology” of modern economics. As we have seen recently, states are no longer capable of contending with corporations in the control of market influences. We have entered the era of “too big to fail”

corporate structures that tower over states in political and economic power. The future of democracy and capitalism lies in the possibilities of how people can assert their self-determination within the challenges and constraints of global quasi-state corporate entities. Like Hart (1986), the author has seen in Japan (Caldararo, 2003) an example of balancing corporate and local powers and limiting excesses of laissez faire capitalism. He agrees also with Hart that anthropology can provide a means of study to other potential examples.

An additional problem is that contemporary economists and philosophers continue to define events in the context of a dogma of progressive modernity. This idea ignores past civilizations’ relevance as models of today’s trends and argues that modernity is a product of certain historical events that took place only in the West in the past 500 years. A new version of this view argues that this modernity has spread globally and been influenced by cultural differences to produce “multiple modernities” (Sachsenmaier et al., 2002). While the idea of modernity is derived from the work of Weber (Eisenstadt, 2002), it is based on the ethnocentric proposition that social reflexivity first appeared in the West as an existential vision of reality (Faubion, 1993). This argument ignores the demonstration by Wilson (1951) that such reflexivity can be demonstrated as early as the First Intermediate of ancient Egypt. Weber cannot be blamed for having overlooked this information as it was not available at the time he was writing. Comprehensive analysis of prehistoric findings related to trade and production argue for earlier world systems and periods of “modernity” (Frank, 1993).

A central problem in this idea of modernity lies in the definition of civilization. Not only do we have the domestication of plants and animals appearing long before cities as defined by 19<sup>th</sup> century historians, but complex methods to produce fine textiles are in evidence among the Swiss Lake Dwellings and other Neolithic settlements thousands of years before Dynastic Egypt or Sumer (Barber, 1991). We need a new definition of civilization, one where sedentism produces complex patterns of organization and economic life. Complex buildings, carts and metallurgy are present prior to 4,000 B.C.E. (Piggott, 1965) in Europe along with massive megalithic structures before 8,000 (Savory, 1968) and pottery in the “early Neolithic.”

What is a complex social organization? For animal life in general, Wilson (1975) uses a broad set of criteria encompassing the routine social nature of life and contrasts with some other definitions that include the specializations of individual members whether as castes or classes within a variable population. Allee (1958) distinguishes social behavior from group contexts where there is clear evidence of a division of labor. In humans, the contrast between complex societies and simpler ones like hunter-gatherers is often defined by numbers or density of population combined with technological means

to food production, and linked by students of Leslie White, from his original conception regarding culture (1949) with differences in energy use.

On a basic level, some hold that the analysis of complexity begins with the principle on which a book by Rubenstein and Wrangham (1986) is organized, mating patterns and the ecological context (examples, monogamy, polygamy, predation). The idea of complex societies is often conflated with the idea of civilization so that some definitions of civilization leave out some societies as in Childe's (1963) position where writing is an essential component which excludes societies like the Inca where he did not consider the quipu to be a writing form. Other definitions like that by Wagner (1960) and Wittfogel (1953) inevitably rest on urbanism which to many would leave out the Maya. Lamberg-Karlovsky and Sabloff (1974) applied an inclusive definition of the measures of the interrelatedness of several factors as a system: stratification, population size, density, (strength of ruling polity (what Blackham, 1961 called political discipline)), trade, size and role of markets, technological advances and others. This approach they felt could be used cross culturally but has not come into general agreement since. Nevertheless, this approach does mesh with that of Toynbee (1958) where he treats civilizations as species of human achievement compared to simpler societies. Adams (1966) placed special emphasis on the common regularities in early civilizations focusing on division of labor, stratification and political institutions.

We must distinguish between a civilization of the Neolithic with the first "towns" and urban life, that is sedentism, pottery, buildings, megalithic stone ceremonial structures, plant and animal domestication, trade and complex products like textiles before 3,500 B.C.E. and a new civilization after this date of human domestication. The development of war into the organization of capture of humans for their control as beasts of burden and wealth producers takes place at this time. A central change in the character of society takes place where the human as "other" is created and this has tremendous moment for humanity for the next four and a half millennia. This introduces us to what Norbert Wiener made famous in his 1950 book, *The Human Use of Human Beings*, as the central theme of society. Under this view of human society the two world wars of the Twentieth Century can be seen as simply tribal wars of European cultural patterns. The present dominant paradigm of history is that modernity is the creation of European culture through the industrial revolution and has only taken place once in human existence. The author does not think this is a tenable theory.

This progressive modernity denies the possibility that contemporary institutions and their future are bound up in patterns of social behavior that have produced similar instances of modernity in the past and that the failure to resolve central contradictions of these factors (example, inequality of wealth) has led to cycles of collapse and

renewal (Frank, 1993). History has come to be viewed in terms of ideologies rather than common historical institutions and as such actual behavior patterns are ignored for the greater emphasis on ideological motivations (as in the work of Fukuyama, 1992; Huntington, 1996).

It is the rarity and the fragility of complex human societies that is overlooked in this view. Also, there is an inevitability that is embedded in both capitalist and socialist ideology that presumes complexity is the essence of human destiny. It also ignores the fundamental processes of exploitation that produce complexity and continually reproduce inequalities in wealth and privilege. At the root of this is the division of labor. The idea that the division of labor began with that between men and women is well established in the minds of most people (de Beauvoir, 1952; Engels, 1942), but the origins of more complex uses of humans is not. Durkheim (1933) describes the historical development of this complexity in labor.

In looking at the Australian Aborigines we find a long established people in one ecological setting, perhaps more than 50,000, but they did not develop complex society or domestication of animals and plants. There are many ways of explaining this: one would be that given Boasian anthropology we can see that there is no imperative to take on the strategy of complexity. Hunting and gathering has been the most successful mode of environmental adaptation for humans and the most sustainable. However, one can also argue that spiritualism or naturalism, the effort to direct human energies to dance, music, ideology and the study of the environment, can also be a valid supporting mechanism for social life that institutions of complex society may not even provide efficiently. A third explanation is possible, that the domestication of animals leads to the human use of human beings and a division of labor that becomes as an organization on exploitation of labor as that of the domestication of animals. The author has described elsewhere how self-domestication can be shown to have produced many unique characters in human physiology (Caldararo, 2005) and that our social complexity is an intensification of that self-domestication as we see in ants and bees (Caldararo, 2011, 2012).

One can argue, as some social scientists have, that the division of labor between men and women in the early family can be an exploitive model for inequalities and asymmetries in complex society. As Berndt (1981) has shown the data we have on aboriginal social relations between the sexes is contradictory and unreliable at best. Overall it seems to show that relations between men and women were fairly egalitarian (Kaberry, 1939; Wilson, 1988), although that idea is fraught with idealized political confusion. Nevertheless, the future of human wealth inequalities and social asymmetries lies in the ideology of the division of the surplus and its uses.

Forms of magic have defined the division of the surplus in the past and they do so in the present. The existence

of banks and the ability of financial institutions to produce forms of money and credit are embedded in magical thinking and continue to dominate society, producing booms and busts, panics and irrationality. Arguments that state banking institutions cannot act as efficiently as private ones also ignore the fact that both fail. The nature of banking is based on the ancient idea of growth as the necessary core value in society. A society that is not growing is considered to be stagnant or dying and this idea is an essential element of Neolithic domesticated thinking: the surplus must always be growing as the population (Hutchinson, 1967). It is opposed to the ideology of hunters and gatherers, where sustainability is the core value, things being the same, being preserved, not overusing and man as a part of nature as opposed to Neolithic thinking that man conquers and dominates nature. Perhaps this is not fair to all Neolithic cultures or one might argue really a characteristic of more intensive horticultural Bronze Age cultures, but emphasis is in the idea of control and that resides in domestication of the natural world and that of man, thus the Neolithic.

In answer to the question, "What is the function of banking? We can generally answer that it serves to facilitate the distribution of the surplus, daily, annually and across generations. Complex societies do not need banking institutions. The Inca were capable of providing resources for the needs of a complex state in pre-Columbian times. They used the surplus to build transportation networks, housing, ceremonial and military structures and arm and field numerous armies (de la Vega, 1589-1616; Steward and Faron, 1959). They were a dynamic and expansionist society much like the young Spanish kingdom that conquered them with "guns, germs and steel" as Diamond (2005) as put it. Modern financial institutions, like their earlier counterparts, seem to exist to produce credit beyond the actual surplus and this credit, whether used by inept emperors, wastrel kings, ambitious popes, "value" driven CEOs or questionable representatives of citizens too distracted to care or avoid the results. This process often does not produce debt, disaster and instability as much as opportunity. When a major bank like J.P. Morgan loses 2 billion dollars gambling in derivatives with "excess deposits" they are entrusted with, one sees these deposits are misallocated segments of the world surplus and were used not to produce innovations or new productivity, but to satisfy the inherent risk associated with the contemporary culture of banking and finance. Entrepreneurs and inventors exist without bankers (example, Gutenberg and Archimedes). The question is not whether banks should exist but who should control the surplus of society, how it should be divided and who should suffer when it is put at risk.

The banks are not too big to fail, but to survive. Banks may disappear in the 21<sup>st</sup> century. For over a century they have been propped up by governments and taxpayers. They appear now as a liability for the future. Their function is already being taken up by internet

venues where credit and exchange take place without the banking institution. Banks in some form seem likely to continue as in credit unions where they serve specific populations or localities. Government support and insurance should continue for this utility function. The extension of present Google and Facebook "banking and finance" potential and entities like Kickstarter will be expanded in the future and should be stand alone self-insuring units. The potential for cell phone banking, especially in Africa and India will greatly change the nature of money and credit. How this unfolds, as community mutuals or centralized "too big to jail" megabanks will define the nature of exchange in the 21<sup>st</sup> century. For more details on banking and the origins of the credit crisis see the author's book (*The Anthropology of the Credit Crisis: Magical Thinking, Irrationality and the Role of Inequality*, Caldararo 2012).

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