

# A Chronicle of the Age of Consequences

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## Chapter 7

### Black September

Over the span of five days in mid-September, America made a mighty lurch into the Age of Consequences.

It began with the dramatic announcement early on Monday morning, September 15<sup>th</sup>, that the venerable investment house Lehman Brothers had filed for bankruptcy.

This was dramatic news because it was widely expected that someone would save Lehman from this fate – either the federal government or another financial institution. That had been the pattern up to that point. In March, the collapse of Bear Stearns – another of the Big Five investment firms (along with Goldman Sachs, Morgan Stanley, and Merrill Lynch) – had been narrowly averted by its government-financed fire sale to a major bank. Then, during the first week of September, the mortgage giants Freddie Mac and Fannie Mae were saved from collapse with an outright takeover by the federal government. Next, Merrill Lynch foundered, prompting its quick sale over the weekend. Everyone assumed the sinking Lehman Brothers would be next.

Instead, it was deliberately ‘allowed’ to fail. The U.S. Treasury Department decided to withhold the type of financial support it had been willing to extend to other institutions, which, when no bank stepped up to the plate, forced Lehman Brothers into bankruptcy.

I heard the news while preparing breakfast for my family. It was just another day in all respects, with school lunches to make and chores to complete – except for what I heard on the radio. Merrill Lynch gone in a puff of smoke? Bankruptcy for the 158-year old Lehman Brothers? I remember thinking: “That doesn’t sound good.” But I assumed it was just more black clouds in a steadily darkening economic horizon. By the end of the day, however, I understood that this was no simple storm. Like a thunderclap, the stock market had fallen 500 points, wiping out nearly \$1 *trillion* of paper wealth. News reports had begun calling the day’s events “unprecedented” and “the worst day on Wall Street since 1929.” As I listened, I couldn’t shake a sinking feeling in my stomach.

The news got worse. On Tuesday, the government reversed course and bailed out a giant insurance corporation called AIG with an \$85 billion loan. Henry Paulson, the Secretary of the U.S. Treasury, said AIG was “too big to fail.” I wasn’t sure what that meant, but it quickly became the watchword of the unfolding financial meltdown. Suddenly everybody – except Lehman Brothers apparently – was “too big” to be allowed to fail. Money flew out Treasury’s door as it moved desperately to head off what was quickly becoming a cascading crisis of panic on Wall Street.

By Friday, it was so bad that Paulson decided to go to Congress with a demand for *\$700 billion* to ‘bailout’ endangered financial institutions, all of whom were too big to fail apparently. It was the only way, he insisted, to avert a total collapse of the American financial system.

Wow.

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In the span of just five days, we went from Business-As-Usual on Wall Street, albeit with some annoying storm clouds raining on its free market ideology, to the verge of total financial collapse. And it wasn't just Wall Street – the effects of this meltdown immediately destabilized markets and financial institutions around the planet. Iceland's currency, the krona, for example, became practically worthless overnight, requiring swift action on behalf of Iceland's government. Similar stories poured in from all points of the global compass.

In other words, what happened on 9/15 wasn't simply a thunderclap of immense proportions, but more akin to a nuclear explosion – one whose destructive radioactive effects will be felt, I'm certain, for a long, long time.

And just like that a sixth warning light, in the shape of a \$ sign, flashed into existence on the dashboard of the speeding vehicle called '*civilization*.'

Flying to Sacramento, California, on the following day to attend a conference, I scooped up newspapers in the airport, including one that shouted: "*The Week That Changed America*." On the plane, I digested the grim analyses.

"This past week marks a decisive turn in the evolution of American capitalism," wrote David Wessel of *Wall Street Journal*. "Gone is the faith, shared by the nation's leadership, that the best road to prosperity is to unleash financial markets to allocate capital, take risks, enjoy profits, absorb losses. Gone is the belief that markets correct themselves when they overshoot."

The *Associated Press* described the bankruptcy filing of Lehman Brothers as "one of the most momentous days in Wall Street history since legendary banker J. Pierpont Morgan helped broker the rescue of financial markets during the Panic of 1907."

Steven Pearlstein of the *Washington Post* wrote: "This is what a Category 4 financial crisis looks like. Giant blue-chip financial institutions swept away in a matter of days. Banks refusing to lend to other banks. Russia closing its stock market to stop the panicked selling. Gold soaring \$70 in a single trading session. Developing countries' currencies in a free fall...What we are witnessing may be the greatest destruction of financial wealth that the world has ever seen...Corporate wealth. Oil wealth. Real estate wealth. Bank wealth. Private equity wealth. Hedge fund wealth. Pension wealth."

*Time* magazine said this: "We are all going to pay the consequences"... "Whatever politicians do now, we as a society are going to be poorer than we are."

And this: "Coping in this new world will require adjustments by millions of Americans. We all will have to start living within our means – or preferably below them."

Double Wow.

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What the hell happened? Why did things unravel so quickly? How did this financial house-of-cards come to be built? Well, as far I can discern there two main reasons for this crisis, one short-term and one long-term.

The short-term explanation can be summed up in one word: *greed*.

Banks, financial houses, hedge funds, investors, mortgage companies, home buyers and sellers – in short, millions of Americans – got so caught up in the national real estate frenzy of the past five years that they began to make very unwise decisions, including massive dice-rolling with something called ‘sub-prime’ lending. The steady rise of real estate prices had encouraged all sorts of speculation, including the highly risky business of selling mortgages to people who, basically, couldn’t afford them. These mortgages were in turn bundled into ‘securitized’ packages that were resold to investors in a bewildering array of shapes and sizes. Things became so complex that ultimately no one knew what was going on anymore.

But it didn’t matter. People were getting rich (some anyway). Gold fever raged across the nation.

In 2007, however, the ‘sub-prime’ dice began to come up sevens as the real estate market began to cool. Housing prices flattened, and then began to fall – a lot. No longer able to simply ‘flip’ a house for a tidy profit, home owners began to default on their mortgages instead – and the ripple effect quickly cascaded up the line to the very banks, investment houses, insurance companies, and other institutions that had enabled the buying frenzy in the first place.

By early 2008, everyone’s luck turned very, very bad. Assets became “toxic” – an apt description given the radioactive sequence of events that began to unfold. Bad mortgages, for example, became lethal to the investment house Bear Stearns, requiring its rescue (too big to fail). But this was just a sign of things to come – the toxic effects of so much greed would quickly spread throughout the financial system, creating a chain reaction that would lead directly to the nuclear explosion of 9/15.

In fact, that day’s events, in their suddenness, their emotional and financial toll, and the outrage they engendered, reminded me of 9/11 all over again – with one big difference: this was no terrorist attack by foreigners.

*We did this to ourselves.*

(The mind shudders at the incalculable combined cost to America of 9/11 + 9/15 in terms of money, suffering and loss of prestige – one wonders if our nation can ever recover).

The long-term explanation of what happened, briefly, is this: our chickens came home to roost. For decades, we’ve been constructing an economy, and a culture, built on cheap credit, easy living, endless shopping, and deficit spending. Along the way, we virtually stopped making things, preferring to become a ‘service’ economy, with plenty of leisure time, content to get everything from the food we eat to the electronic playthings we apparently require from overseas. In the process, we became a different nation than what we were only sixty years

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earlier. To many observers, we also became dissolute – susceptible in our private lives to precisely the type of avarice that consumed Wall Street.

For example, not long after 9/15, James Kunstler wrote this harsh assessment in his blog: “We’re not the same nation that crowded around the old radio consoles for Franklin Roosevelt’s fireside chats. Back then, we were mostly a highly-disciplined, regimented, industrial society full of citizens who mostly did what they were told to do, and mostly trusted in authority. Today we’re a nation of tattooed barbarian “consumers” with no impulse control, a swollen sense of entitlement, ruled by a set of authorities ranging from one G.W. Bush to the grifter-billionaire pantheon of Wall Street CEOs...”

Or how about this tough post-9/15 assessment by columnist Jack Smith of the *Fort-Worth Star-Telegram*, who sees current events as evidence of America’s irresponsible behavior in general, including:

- Record budget deficits under George W. Bush resulting from excessive tax cuts coupled with runaway spending, including the war in Iraq;
- Our failure to craft long-term solutions to Social Security and Medicare;
- An ineffective energy policy, with a gross underemphasis on conservation;
- A health-care industry that somehow manages to be high-cost and exclusionary (46 million Americans are uninsured);
- Lavish salaries for Wall Street but incremental growth (or none) for Main Street;
- A bitterly divided Congress, locked in partisan conflict.

“We need to ask ourselves,” he concludes, “whether we are increasingly becoming a nation of selfish, shortsighted people who lie about our incomes to avoid taxes or buy homes we can’t afford, irresponsibly ring up huge credit-card debts in our quest for instant gratification; insist on cutting federal income-tax rates and expanding deductions but aren’t willing to take the tough fiscal actions needed to slash federal budget deficits; complain about high energy costs but buy 4,000-square-foot homes and drive behemoth gas-gulpers; and fail to vote in local elections but gripe when City Hall doesn’t do what we want.”

Wow. Those are some nasty chickens.

For a calmer, though no less disturbing, analysis, I opened a new book titled *The Bridge at the End of the World*, by Gus Speth, dean of Yale University’s famous School of Forestry, and a prominent leader in the environmental movement for decades. His previous book, *Red Sky at Morning*, raised the alarm about climate change well before a certain former vice-president of the United States made headlines with an award-winning documentary on the same topic.

I had purchased Speth’s book as part of my ongoing research into the Age of Consequences (no spy thrillers for me, apparently) and decided to bring it to Sacramento in hopes it might shed some light on the week’s tumultuous events. So, after checking into the hotel, I stepped outside into the soft California air, book in hand, and sank into a comfortable chair in the patio, a cup of high quality coffee in tow. I knew I was being coddled by the sweet life – just the sort of perfect day to read about the failure of modern American capitalism.

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I didn't have to wait very long. Within a few pages, I was staring at a graphic representation of what Speth calls the "Great Collision." There were sixteen graphs in all – each featuring a sharp exponential curve upward from left to right, as if they were ocean waves slapped against a cement wall ("storm surge" I thought). Each represented a different alarm bell: global population growth, CO2 concentration in the atmosphere, total real GDP, damming of rivers, paper consumption, biodiversity extinctions, great floods, fertilizer consumption, decline of fisheries, and so on.

After this graphic shocker, Speth gets right to his main point: "My conclusion, after much searching and considerable reluctance, is that most environmental deterioration is a result of systemic failure of the capitalism that we have today and that long-term solutions must seek transforming change in the key features of this contemporary capitalism."

He lays much of the blame for our troubles on the "growth imperative" – the economic theology that says unending growth is the ultimate objective, or 'summum bonum,' of everything we do. He cites historian J.R. McNeill: "The overarching priority of economic growth was easily the most important idea of the twentieth century."

He quotes another historian, Richard Hofstadter: "Almost the entire span of American history under the present Constitution has coincided with the rise and spread of modern industrial capitalism...Although it has been said repeatedly that we need a new conception of the world to replace the ideology of self-help, free enterprise, competition, and beneficent cupidity upon which Americans have been nourished since the founding of the Republic, no new conceptions of comparable strength have taken root."

And with economic gain came environmental loss.

One response was environmentalism, which sought to stem the destruction of nature. Although it was an energetic response to the rise of industrial capitalism, Speth notes, in the end, it failed. "Our efforts have not succeeded," Speth writes, "the evidence is in. We have won many victories, but we are losing the planet."

Here is his quick list of why environmentalism failed: (1) it believed problems could be solved within the current economic system; (2) it was incrementalist – meaning it tried to solve problems one at a time; (3) it dealt with effects instead of causes; (4) it believed that problems could be solved without significant changes in lifestyles or threats to the growth imperative; (5) it saw solutions as non-political; (6) it lost touch with the grassroots; and (7) it never shook its faith in regulation, bureaucracies and experts.

There was one more reason: "My generation is a generation of great talkers, overly fond of conferences," he concludes. "We have analyzed, debated, discussed and negotiated these global issues almost endlessly. But on action, we have fallen far short."

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And where environmentalism fell particularly short, says Speth, was in counteracting the creation of a materialist, consumerist nation whose appetite for MORE would ultimately endanger the natural world the environmentalists were determined to protect.

Speth notes that the economist John Maynard Keynes saw this brand of trouble coming way back in the 1930s. Once man solves his economic problem (food, shelter, etc), Keynes argued, he will be faced with his “permanent problem – how to use his freedom from pressing economic cares...how to live wisely and agreeably and well.”

Keynes foresaw our reluctance to solve this problem. In his 1933 essay “Economic Possibilities for our Grandchildren,” he wrote: “For at least another hundred years we must pretend to ourselves and to everyone that fair is foul and foul is fair; for foul is useful and fair is not. Avarice and usury...must be our gods for a little longer still.”

And the chickens took flight.

What Keynes couldn't foresee, of course, was the scope and scale of our avarice and what it would do to us economically and spiritually – or that things might actually collapse before they got better. That's the legacy of 9/15 – a very foul day – whose toxic effects are spreading far and wide. We are likely entering a global recession. This means things will point downward for a while – possibly a long while.

Maybe that will be a good thing in the long run, I don't know. No one does. But we shouldn't be surprised – Speth notes that even Adam Smith, venerated by free-market advocates everywhere, assumed that economic decline at some point was inevitable.

Speth finishes his book in a hopeful mood, noting that many new efforts are being proposed as alternatives to the “growth imperative.” His list includes: Civic Environmentalism; Deliberative Democracy; Glocalization; The Great Transition Initiative; Constrained Pluralism; Capitalism 3.0; The Great Work; The Earth Charter; The Great Turning; and something called Consciousness I, II, and III.

But here's the most hopeful quote I found in the entire book. It's by economist Milton Friedman, the archangel of the free market/growth imperative ideology that dominated the past half-century, ironically enough:

“Only a crisis – actual or perceived – produces real change. When that crisis occurs, the actions that are taken depend on the ideas lying around. That, I believe, is our basic function: to develop alternatives to existing policies, to keep them alive and available until the politically impossible becomes politically inevitable.”

Indisputably, the crisis is happening. The question is: what good ideas do we have lying around?

I have one – which I'll delve into at a later date – though I didn't find it in Speth's book, which had taken me three days to finish. It took that long because I had to weave it into the conference schedule – I was attending the 4<sup>th</sup> Annual Peak Oil conference. It had been a fascinating

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discussion. Many speakers used Peak Oil as a prism by which the current crisis on Wall Street could be viewed – as another type of deficit spending, for example.

Some commented on how our insatiable thirst for fossil fuels had fed our avarice HUGELY on all levels of American society. Oil was the lubricant for the engine of growth, they said. It brought us amazing prosperity – but it also brought us bottomless greed. It was truly a Faustian bargain – of which we are only now beginning to pay the price.

Meanwhile, the consequences of 9/15 continued to spread outward like a viral infection. I followed its progress in the papers and on TV. Remedies were coming fast and furious, each at extraordinary price tags. Their effectiveness could not be surmised – mostly they felt like prayers.

That's ok – we need a prayer. It had been a bad month to be an uncritical believer in American-style capitalism. Our faith had been rocked to the core, and our avarice exposed in the process. The chickens began to land as the finger-pointing began in earnest. But the truth is we're all to blame.

*We did this to ourselves.*