

MONEY MATTERS

# IS CAPITALISM MORAL?

A CONVERSATION

JOHN GRAY, JAGDISH BHAGWATI & BERNARD-HENRI LÉVY, WITH STEPHANIE FLANDERS

The John Templeton Foundation recently asked more than a dozen leading scholars and public figures to write short essays responding to the question, “Does the free market corrode moral character?” Templeton also sponsored an event in London on this subject in early December, from which the conversation below is adapted.<sup>1</sup>

**Stephanie Flanders:** It is an intriguing moment to discuss whether capitalism is moral or, more broadly, whether it conduces to moral behavior. Had we done so a year ago, we would have been concerned with how the great wealth produced by market economics affects our souls, and how globalization affects poverty and inequality. Today, however, we’re more liable to focus on how the market has affected our wallets and retirement accounts, the ethics of greed before the meltdown, and those of regulation and moral hazard ever since. One has the sense that an entire era of pro-market orientation around the world has ended, and that is certainly a conversation changer.

**John Gray:** Current circumstances are bound to change a conversation about capitalism and morality, but they do not change what is most basic to the question: that all humanly acceptable economic systems make use of human motives that are morally questionable.

Classical economics and the liberal theory from which it comes have always understood, going back to the 19th century if not before, that economic systems must harness the strongest human impulses, not merely the most noble ones. So all humanly acceptable economic systems are morally corrosive to some extent simply because they enable selfishness to benefit the selfish, for example. Thus, any position stating that one type of economic system is ethically pure while all the rest are no good is indefensible.

That does not mean, however, that all economic systems are morally equivalent. Some economic systems are universally bad. Communist central planning was monstrous because its utopian aspirations demanded too much in terms of human knowledge and motivation; it tried to prohibit one morally questionable impulse, self-interest, through another, coercion. The result was a kind of parody of *laissez faire* capitalism, with vast corruption, low standards of living, ecological devastation and huge loss of life.

But the collapse of communism did not usher in a period of pragmatism and moderation as one might have expected, but rather a new utopian delusion—that of a global free market. Of course the pure free market is like pure communism in that it has never existed and never will exist.

Forced to choose between utopias, I would choose the free market variety, for two reasons, one that is obvious and one that perhaps is not. Free market utopianism is bound to be more productive and less destructive of human life—that’s clear. It’s also bound to be more unstable, however. Communism hung around for more than seventy years and destroyed many generations of human beings; the central role of coercion made it morbidly stable. The free market delusion bruited about after the collapse of communism has already ceased to exist. There is no longer a major economy in

the world that is a free market economy like that of the United States and Britain even a few months ago.

As important, the ideal of such an economy is, as you suggest, eroded. Here is where the crisis is relevant. We now have mixed economies with the state playing a profoundly and increasingly important role. I do not expect in my lifetime any reversion to the kind of economies that existed even a few months ago. The crisis is too large for that and will require too much state intervention.

**Stephanie Flanders:** So where does that leave us? You say that the crisis has brought an end to the Anglo-American free market economies that we had just a few months ago. So is the economy now more moral, or less?

**John Gray:** The underlying moral message of the crisis, it seems to me, is not about capitalism but about utopias. People like utopias. They imagine that utopian thinking embodies a noble human impulse when in fact it has been horribly destructive of human well-being and human freedom. The market fundamentalist utopia that has just come crashing down fed hubris as much as it enabled greed. It promoted a short-sighted snatching after virtual wealth based on pyramids of debt.

We should be seeking not a utopia but a realistic arrangement recognizing that all economic systems that work tolerably well will be morally mixed. Which human virtues are assaulted most by any given economic arrangement will depend on time, place and circumstance. The thing to keep in mind always is that economic systems do not create human nature; rather, they provide a context for how it plays out. It is human nature that creates economic systems, and out of the crooked timber of humanity, as Kant put it, nothing straight can be built.

**Jagdish Bhagwati:** Indeed, I have long argued that human nature affects the way we behave in markets far more than markets affect our human nature, and I will return to that important point later. But, as regards the effect of the financial crisis on how we think of markets today, I do not take the apocalyptic view that the crisis has undermined markets and killed for good the “Anglo-Saxon” or, better still, “Anglo-American” embrace of markets. When the dust settles, a saner analysis of what happened will be possible, and will occur for at least two reasons.

First, the Anglo-American or Thatcher-Reagan era of “market fundamentalism” was more rhetoric than reality. Neither managed, after all, to reduce the share of public expenditure in GNP. Mrs. Thatcher did take on the socialist embrace of ownership of the means of production and of militant trade unionism, but Britain never shifted to the opposite pole of “market fundamentalism.”

Second, the financial crisis underlines not problems with markets generally, but the difference between the non-financial and financial sectors. I have argued that one common factor in recent financial crises had been that financial innovation (such as derivatives and credit default swaps) had gotten ahead of comprehension, so that few realized the huge potential downside of things going wrong. Whereas with manufacturing innovation the problem was one of “creative destruction”—how to prevent Luddite reactions to benign, prosperity-enhancing developments—in the financial sector the problem was one of potential “destructive creation.”

But why did this happen? Largely because of a U.S. Treasury-Wall Street complex. Robert Rubin went from Goldman Sachs to the Treasury and then to Citigroup; Henry Paulson went from Goldman Sachs to Treasury and will likely return to Wall Street. This is inevitable: You must understand Wall Street to work with it. But the result was that Wall Street’s euphoria about financial innovation was never effectively challenged by anyone credible. Clearly, then, a lesson of this crisis is that we need

truly independent experts who understand Wall Street but are not part of it to be charged with reducing the range of the unknown.

As for the effect on the use of markets generally, it would be absurd to think that anyone serious will now oppose freer trade or reject cap-and-trade systems for controlling carbon emissions since it uses the market principle, to take just two examples. I therefore question also John Gray's view that the end of communism gave rise to a new utopian delusion in the West, that we shifted from the communist utopia to the free-market utopia. If anything, we shifted from that utopian thinking to a more pragmatic approach to markets, for the most part. That is certainly what happened in India and China. These giants had been snoring for three decades and finally woke up because they shifted from crippling "anti-market fundamentalism" to a pragmatic center.

**Bernard-Henri Lévy:** I agree that all the available alternatives to the free market, especially the Marxist one, provided solutions that were worse than the problems they pretended to solve. But the idea of getting rid of the free market, and of attributing to it the moral corrosion of society, was also an idea characteristic of the *dirigiste* fascist regimes of the 20th century that did such enormous harm. We do not often think about it, but the principle of free exchange, of a free market, affects freedom generally, including the human will to create beauty, to invent and to heal. The murderous command economies of the 20th century produced millions of corpses, but they produced no great art, no great music, no great medical advances.

Still this idea, that it is the market that corrupts, has not gone away despite the destruction and cultural sterility it has caused. When the anti-globalization movement claims that market capitalism brings misery, it is just false. These are provincial people, seeing the world only from the Western point of view. They do not go to the places where the market has not yet introduced its principles and its laws and see that these are the places where misery is the deepest. There is no society where people are more greedy, violent and insular than the so-called archaic societies, which are fairly said to be pre-capitalist or pre-market. So clearly, these vices and defects are not invented by the market.

Nonetheless, I also agree that the capitalist free market as it has existed in recent years was absolutely unsustainable, and we have now seen this. It has been the reign of greed, or of the Greek philosophical notion of *thumos*, that of the competitive spirit, which is the expansion of the ego. The free market, according to Hobbes and others, is supposed to create an appreciation for the interests of others. This version of the market instead created a disgusting indifference to the fate of others, especially of the poorest others.

**Stephanie Flanders:** So the system in its recent form was immoral?

**Bernard-Henri Lévy:** I would not put it that way. Markets bring prosperity, but those who ruled the markets in recent decades did not give a damn if they created prosperity. They equated making money with producing wealth, which is not at all the same thing. It was the reign of an utter and unbearable egoism, and we see its remnants still in the psychology of the bailout behavior of Secretary Paulson and his associates. I understand completely the anger of the average American, seeing how investment bankers and hedge fund operators have taken the gains for themselves and managed to socialize the losses. This simultaneous privatization of profit and communalization of losses is a pure scandal. And there has been something really shocking in the way Mr. Paulson has switched his gun from one shoulder to the other, as we say in France, going from a producer of crisis to one who would save us from it. The shoulder changed, but it is the same gun, and the same person is holding it.

But again, we must understand what this means. The market does not corrode moral character; rather it is the decline of the moral values of democratic society that has corroded and is still corroding the free market system. That is why, as Ernest Renan once said, an intellectual and moral reform has to be the first step toward rebuilding our free market. This is the only available and moral solution we have.

**Jagdish Bhagwati:** This is an important point that we have made twice already this evening. There seems to be a tendency to think that somehow markets make people greedy. This is a kind of vulgar-Marxist fallacy, that where you work and what you do there define your values. But this is surely not so. We get our values from a variety of places. Some get it from their family (though sometimes you rebel against what your parents believed); others from their community. Yet others get it from their religion. For many, too, literature is a source for understanding ethics, as in the great Russian novels of Tolstoy and Dostoevsky. Where you work is hardly the only or usually the most important thing.



*No end in sight: Former Treasury Secretary Henry Paulson at a press conference in March 2008. [credit: REUTERS/Jason Reed]*

**John Gray:** Well, true, but can I just mention Bernard Mandeville here? In his famous *Fable of the Bees* Mandeville said that markets are very good and useful things, but they do corrode traditional virtues. They depend on greed, vanity, selfishness and more. So I can't at all accept the idea—nor could any sociologist—that markets are neutral institutions that you can use in any way you like, any more than I accept that central planning could be neutral.

**Jagdish Bhagwati:** But, John, the very fact that there are different types of capitalism makes my point. I am not saying that markets are morally neutral, that they are no more than a blank canvas on which people inscribe their virtues and flaws. I am simply saying that markets do not dominate the production of values.

Take for instance the way the Japanese deal with inequality of pay in their firms; it's very different from what you get in the United States. Where does that come from? It comes surely from some value structure outside the market. Substantial egalitarianism is also part of the Scandinavian culture which affects their form of capitalism, and so on and on from culture to culture.

**Stephanie Flanders:** So you reject the Marxist idea that we are what we produce or consume.

**Jagdish Bhagwati:** That's right. Calvinists, the Jains of Gujarat where Mahatma Gandhi came from, and Simon Schama's Dutch burghers were embarrassed by their riches and by the poverty in their societies, so they practiced what we now call Corporate Social Responsibility. They accumulated capital but spent their wealth, not on themselves, but on doing good.

**Stephanie Flanders:** But many would argue that what we produce and consume does have important moral dimensions. In his Templeton essay on this subject, Robert Reich argues that one of the morally troublesome aspects of the market is that it shields people from the moral consequences of their decisions as consumers.

**Jagdish Bhagwati:** Reich is merely describing what everyone who has moral views on our responsibility to the poor countries has to resolve in their behavior as consumers of goods imported from these countries. I care deeply about labor standards in the poor countries, but I also know that the surest way to raise wages and also labor standards in poorer countries is to open our markets to their products and create demand for their workers. So, unlike Reich, I feel completely blame-free about buying cheap goods from the poor countries; indeed, I feel virtuous about it instead.

This doesn't mean, of course, that I will not object strenuously to goods being produced in conditions that remind me of Chadwick's harrowing accounts of factory labor in the first flush of the Industrial Revolution. But again, the question as to how we best ensure this outcome is a matter for legitimate debate; and I think there are better ways of doing this than boycotts and trade sanctions.

**Stephanie Flanders:** It's morally relevant, though, how we behave.

**Jagdish Bhagwati:** Indeed, but my moral behavior reflects my understanding of the economic consequences, and also my sense of my own options. When I am being badgered to buy only more expensive "fair trade" coffee or fashions, where the producers are paid a premium over the market price, this is tantamount to my being asked to pay a subsidy to these particular producers. If you wish to indulge your altruism that way, fine. But why should I be bamboozled, or bludgeoned, into accepting your brand of altruism?

I'm a free moral agent, and there are hundreds of ways in which I could be altruistic. Rather than pay this subsidy, I may want to build a playground or aid a civil society group fighting HIV/AIDS. I don't agree with the notion that if I don't buy fair trade coffee somehow I am acting immorally, any more than I would presume to put down as morally defective those who would like to spend their altruistic moneys on fair trade coffee.

**Stephanie Flanders:** You all agree, I think, that some kind of market system is the least bad moral choice, and that the one we've had lately registered toward the low end in terms of the kinds of behaviors it tolerated, enabled and rewarded. I'm not sure there is agreement about the fairness of the financial sector bailout, but I'd be interested to hear your views on what reforms we need to produce a better market system—better morally as well as more effective economically.

**Bernard-Henri Lévy:** I'm optimistic about the future, even though, as I have suggested, I am frustrated with the bailout so far. The public money that has gone to the banks, in France as well as in Britain and America, has not been tied sufficiently to real reform. The banks have been recapitalized by government purchases of their toxic products, given huge loans for questionable collateral, but have not yet been asked specifically to change their ways.

I realize that these are stopgap measures simply designed to keep things from getting worse, to avoid a real panic. My optimism comes not from any of this, nor from the position that the problem is just in the financial sector and everything else is fine—I don't believe that—but because I sense the return of politics. The free market system liberated itself too much from politics, and American leaders have had the courage to see and say that. A moral and intellectual reform means also a political reform, and this is in our future. Those who invented the free market, Adam Smith and others, knew that the real core of economics is politics, not in the sense of bureaucracy or the overwhelming weight of the state, but in its rules, in the checks and balances among the state, the individual and social institutions like banks and the rest. So banks cannot be given public money just to act as a treasurer and keep it all under their feet or up their arse. The money has to circulate; it is the lifeblood of a peaceful, prosperous democratic society. Government cannot bail out banks only to

look on while they keep credit frozen.

**Stephanie Flanders:** Are you agitated about the bailout, Jagdish? Is it immoral?

**Jagdish Bhagwati:** No, “immoral” is not an appropriate term here. A bailout is now a matter of necessary prudential action; it is moral under the circumstances. Many people are offended because they hate to think that the fat cats who helped cause the crisis are being bailed out while so many less wealthy innocents suffer. They would rather see that those who are into stocks and bonds be put in stocks and bonds. But think of it as triage: You have to toss one person from the boat, so will you choose the emaciated man in distress who is too weak to row, or the strong, well-nourished fellow who can help you survive?

Part of the distaste for the bailout also comes from the fact that, for some time now, we have been witness to CEOs in manufacturing firms getting out of failing firms with large sums of money from stock options while the rank and file go down the tubes. This offends the notion of ethical behavior on which all schoolchildren in the West are brought up: that the captain goes down with the ship while the passengers get away in lifeboats. Here, instead, the CEOs get away in lifeboats while the workers go down with the firm!

**Stephanie Flanders:** But your argument would be that this reflects on the personal moral quality of the CEOs, not necessarily that of the capitalist system.

**Jagdish Bhagwati:** Not quite. There are, of course, crooked CEOs, and there will always be some malfeasance no matter how much we regulate. But the financial incentive structures, which are grafted on to the capitalist system, can either promote or constrain such crookedness. Thus, everyone thought that if CEOs and senior management got stock options, this would create incentives to improve firm performance. It did when things went well, but if the firm is failing, then CEOs with insider information are in a position to sell stock before the price collapses. Clearly, incentive systems must be devised with both normal and distress conditions in view.

**John Gray:** Well, let me address your original question, Stephanie, by making three brief proposals toward intellectual and hopefully some kind of practical reform. The first is, just as Bernard-Henri has remarked, that we stop referring to Adam Smith as an unqualified apologist for the free market. If you actually read Adam Smith, not only *The Wealth of Nations* but also *The Theory of Moral Sentiments* and the *Lectures on Jurisprudence*, you find that he was one of the sharpest, most astute critics of the then-emerging market system. It’s a fundamental error to think that Adam Smith did not recognize the morally corrosive effects of market institutions and market life. Indeed, he proposed a national militia on Swiss lines not for reasons of defense, but because he thought it promoted virtues that the market undermined.

Second, back by way of the question about the American commitment to free markets being an ideology or not, I think it’s important to avoid too much looseness in talking about markets and market economies. There are indeed several types of capitalism in the world, and only a few of them, the ones that have recently begun their collapse, are properly called free markets—not because they are entirely and utterly free, for there is no such thing, but because of how those who manage, justify and support them think about them and explain them to themselves and others.

Does China have a free market economy? Does Russia? They have a type of capitalism that is quite different from the central planning that went before in both cases. But no economist or sociologist

would call these free market economies, and they don't use that kind of language themselves—which brings us back to the ideology point.

I do think we have here, or at any rate had, a case of ideological thinking. If you favor the extension of markets into areas of life where they are not appropriate, you can only justify that by reasoning that markets are always more efficient than government. That's ideology.

Moreover, both the Bush Administration and the Clinton Administration before it were ideologically committed to free market capitalism as a missionary project. It wasn't simply a way of organizing American social and economic life; they were constantly haranguing the rest of the world to adopt the American way of doing things because they said it was universally the best. This is the clearest hallmark of an ideology one could ever expect to find.



*Adam Smith [credit: © Bettmann/CORBIS]*

And it is one I reject: No type of capitalism is always and everywhere the best. In this world we recognize, or ought to recognize, a diversity of human purposes and goals and interests and values. That is why the flexibility of market systems commends itself; the market, precisely because it is imperfect and never at rest, can accommodate social orders that prioritize value differently. And that is why it is tragic, indeed absurd, when the idea of the market is turned into a one-size-fits-all form of universal ideology.

The same is even true, by the way, within a society. As some of the defenders of capitalism have recognized—Hayek, for example—rewards in any kind of market system, but especially in a mainly free or deregulated one, do not, should not and cannot correspond to public judgments of merit. Any far-reaching attempt to align economic rewards with some abstract judgment about what people somehow deserve leads to one form of tyranny or another. It entrenches existing standards, undermines productivity and restricts freedom. That is why our problems today will not be resolved by a softer, gentler, nicer type of capitalism that is more philanthropic. It's the hard, tough aspects of capitalism, in which it deviates from standard ideas about merit and just desserts, that should be defended by defenders of capitalism—the tough bits, not the easy bits. We must defend ambiguity and imperfection, not because we like them, but because attempts to escape them make everything worse.

**Bernard-Henri Lévy:** This advice, that we accept not just the inevitability of imperfection but also its benefits, is very important. Of course Adam Smith did not make the free market into an idol; no serious theoretician of economics ever did that. The proper way to think about the free market, as well as the proper way to think about democracy, is that both are ideals we strive for but can never reach. It's a continual process, without end, which means that just as it is not such a bad system, it of course cannot be completely good. From Adam Smith to David Ricardo to Benjamin Constant to Karl Marx there has always been this double bind. The system is not so bad; it enables civilization by providing a way to mediate the normal and natural brutality of competition for scarce resources. But it always seems to teeter at the edge of an abyss.

**Stephanie Flanders:** And your third point, John?

**John Gray:** It follows from the second, and it is where geopolitics comes into our discussion. The American missionary project met with resistance, and we see today that the parts of the world which resisted the full incorporation of American practices are now saying that they would be much worse off in this global crisis had they listened to the sirens of the Washington Consensus. This implies that we're seeing not just a global financial crisis, but also a geopolitical shift.

**Stephanie Flanders:** What does it mean if America no longer has the moral authority, or perhaps even the money, to preach to the markets? Does that make the world a better place or a worse place?

**John Gray:** A better place in one sense and very possibly a worse one in others. It's better because this silly, infantile ideology has collapsed and we won't see it again in our lifetimes. It could be worse because no one knows how the crisis will be resolved. Rather than global cooperation we may see something more like the 1930s, which can be even worse than the reign of the free market I have criticized and opposed: We could see the classical phenomena of protectionism and competitive currency devaluations among the various forms of state capitalism, which is basically all we've got now.

**Jagdish Bhagwati:** As I argued earlier, we are experiencing a temporary setback mainly in the financial sector, and we will come to understand it and put it right. I don't think we have a full-fledged systemic crisis on our hands. Let me be specific—let's take trade, for example.

Macroeconomic crises are not good times to promote trade liberalization, but I doubt we will move backwards into more protection. There is not a single policymaker in the world who is unaware of the mistakes of the 1930 Smoot-Hawley tariff and wants to repeat them. The G-8 and G-20 keep reaffirming their intention to keep protectionism at bay, and thanks to the WTO there are also many institutional obstacles, designed precisely thanks to the interwar experience of unconstrained tariff-raising, to prevent a virulent outbreak of protectionism.

Some of the pessimism today, as well, comes from an obsession with the United States and how the ideological "American" shift to markets has been discredited because of what has happened in the United States. We hear repeatedly this foolish phrase "Washington Consensus", which reinforces the notion that America is the fountainhead of liberal reforms. That is nonsense. Liberal reforms in most countries arose from a realization that the illiberal policies embraced by anti-market fundamentalists had failed, and a move to pragmatism was necessary. Washington's rhetoric was not the key factor. I can testify to that for India for sure; the reforms were home-grown. And I am equally certain that no matter how much some French intellectuals and American leftists decry liberal reforms, policymakers in developing countries will not renounce the policies that have produced for them such enormous gains in prosperity and, as a result, are finally pulling many out of poverty.

Look, people are not going to close down a system they see as working. They will fix its soft underbelly of financial-sector weaknesses, just as Asians fixed what caused the 1997 Asian financial crisis, without sacrificing the benefits of more liberalized trade. So I stress again that we're probably a little too much under the influence of the current crisis and a little too much obsessed by America.

All that said, I would also point out that all this has a very high moral profile. Liberal reforms and the embrace of globalization as an opportunity rather than a threat are leading to a vast reduction of poverty. Data on gender equality, child labor, health and other social issues also indicate that market-oriented reforms—not Wild-West libertarianism, but market-oriented reforms with global reach—are

a very good way to proceed to achieve widely agreed moral ends.

**Bernard-Henri Lévy:** This is good advice too, I think, not to obsess about America and to see the bigger picture. And this bears another moral implication as well. This trial the world is now going through cannot be put only on the head and shoulders of America. The origins of this crisis are complex, and there is plenty of blame to go around. Beyond and really behind the subprime mess was the fact that China refused to devalue the yuan in order to advantage its exports. This led to a highly distorted pattern of international capital flows that has contributed to the global economic situation. Then there is the speculation in the price of oil, which involves the Russians, the Venezuelans, the Iranians and others, which has driven up the price of food and hurt the poorer countries. Many share responsibility for what has been happening.

**John Gray:** I agree with that, to a point. America has been and remains a pivotal power in the world economy in many ways, through the IMF, for example, which imposed various policies in Argentina and Indonesia and other parts of the world. But more than that, it's a complex matter to assign blame because their guilt is connected with what we did. For example, we outsourced our manufacturing industry and our pollution and our ecological problems to China.

Now, I'm not saying we shouldn't have done it. I'm not saying Wal-Mart is evil, or that allowing American dependency on inflows into its government bond market from China and elsewhere was utterly foolish. Nonetheless, all these economies are locked together in mutual dependency. So there is shared blame at several levels. And there is also a tremendous paradox lurking just behind the curtain, if you like that sort of thing: We're now hearing many calls that China should assume a burden of reflation, that it should spend into deficit to help get the world economy moving again. That would be the sensible thing to do, but think what we're asking: We're appealing to the Chinese Communist Party to re-float the global capitalist economic system. For a connoisseur of paradox, there's a certain pleasure to be derived from that situation.

**Stephanie Flanders:** The issue of shared responsibility raises an interesting point: How does the perceived decline of, if you like, international fraternity affect our ability to manage a much more interdependent global economy? Does it make it harder for countries to work together at times like this?

**John Gray:** It is harder when a shift of power is occurring in the world. America has been a global hegemon for most intents and purposes. As it becomes weaker, power is diffused, and certainly issues will arise about the sustainability of American power in a context in which it is critically dependent on capital inflows from countries, some of whose leaders do not share America's interests or values. Of course it's harder for a concert of three, four, five or six big powers to coordinate effectively, especially when there are smaller, semi-outlaw powers like Venezuela, Iran and perhaps Russia trying to upset the apple cart. That's obviously one of the ways in which the waning of American power is worrying, and certainly that worry, too, bears a moral quotient.

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1. To read the essays or to see a video of the London event, visit [www.templeton.org/market](http://www.templeton.org/market).