2 Narratives of the Global Financial Crisis

“I think one of the things this country really, really needs, and still doesn’t have, is a narrative of what happened and why. What you’re seeing in the country now I think is inchoate anger. They’re just mad. They don’t really know what they’re mad about or who they’re mad on, except bankers, and apparently incompetent politicians. But it is an inchoate anger because the story is just not well understood.” (Blinder 2010)

The final report of the National Commission on the Causes of the Financial and Economic Crisis in the United States (Financial Crisis Inquiry Commission, or FCIC) was published in January 2011. Based on several hundred public hearings and interviews and millions of pages of emails and other documents, the commission staff examined, with particular emphasis on the role of complex derivatives and the US mortgage market, the causes of the financial crisis. It also explored why certain financial institutions had failed or might have failed without government support. The quote from US economist Alan Blinder at the beginning of this chapter was taken from an FCIC interview, and the FCIC report does in fact present a central narrative of the US financial crisis. Interestingly, four out of ten FCIC commissioners dissented from the report. While three of these four could agree on a second narrative, one commissioner – Peter J. Wallison – published his own report, totaling three narratives of the financial crisis from the FCIC alone (Financial Crisis Inquiry Commission 2011). Another three years later, academics, finance professionals, regulators and policymakers still cannot agree on the exact roots and causes of the crisis. As one might expect, some crisis narratives pushed the window for new regulation wide open, while others blocked it up completely, suggesting that regulation had caused the crisis and emphasizing that markets should regulate themselves. As Blinder’s statement indicates, given the public anger over bank bailouts and rescue programs, it might have been best – at least from a political rationale – to blame any group for causing the crisis. However, public finger-pointing at either the rating agencies or the investment banks, or even

26 Phil Angelides, Brooksley Born, Byron Georgiou, Bob Graham, Heather H. Murren, John W. Thompson signed the report; it was not supported by Keith Hennessey, Douglas Holtz-Eakin, Bill Thomas, Peter J. Wallison.
financial regulators, was neither feasible nor possible: The financial crisis of 2007ff. was just too complex to allow a simple explanation. Apparently, the 21st century financial system that broke down in 2008 had had many architects, including mega-banks and gigantic insurance companies, but also national financial regulators and global policymaking elites. When the risks materialized during 2007 and 2008, the causes were so intertwined that responsibilities were difficult to assign (Admati and Hellwig 2013, 199).

The OCC’s Martin Pfinsgraff has identified four schools of thought, each putting another narrative of the crisis center-stage. As stated by the first school, the crisis was caused by the bad behavior of banks and mortgage originators; it can accordingly be traced back to remuneration and lending practices. School number two emphasizes the role of the US government, more specifically the government-sponsored enterprises (GSEs) Fannie Mae and Freddie Mac. According to this second narrative, the GSEs not only promoted private homeownership, but actively “subsidized and encouraged lax lending practices” (Pfinsgraff 2012, 2), ultimately creating the mortgage bubble. School number three focuses on the rating agencies, i.e. the Nationally Recognized Statistical Rating Organizations (NRSROs), blaming them for understating the risks associated with certain derivatives products. School number four redirects our focus to the role of US regulators, as they did not anticipate and prevent the crisis: According to this line of argument, each respective agency “either lacked appropriate authority, was incompetent, or both” (ibid.). As these four schools of thought focus on the behavior of the actors involved – implying that the crisis would not have happened if they had only behaved differently – we want to term all explanations that fall into Pfinsgraff’s categories behavioral narratives of the crisis, contrasting them to the systemic narratives of the crisis. As we will see, this distinction is crucial: Not only do most reform debates shift from one side of the continuum (behavioral) to the other (systemic), gradually objectivizing over time (Mayntz 2010b, 11f.). More importantly, these types of narratives have fundamentally different implications for reform. Defining frames, or setting schemata of interpretation in Goffman’s sense (Goffmann 1974, ch. 2; Soros 2010), determines the future policy options of governments; therein, the “period of

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27 In a speech in 1994, President Clinton summoned the close relationship between private homeownership and the American Dream: “Today I want to talk with you about the dream of homeownership and the larger American dream of which it is a part and what we can do together to keep the economic renewal that began 21 months ago going. […] I think we all agree that more Americans should own their own homes, for reasons that are economic and tangible and reasons that are emotional and intangible but go to the heart of what it means to harbor, to nourish, to expand the American dream” (Clinton, 1994).

28 Soros adds a third narrative, stating that the crisis can neither be explained with behavioral nor with systemic factors, but with interpretations, dogmas or paradigms: “[I]t’s the ideas or theories that guided the people […] it’s the theories adopted by both the regulators and the market participants that proved to be false. It is the Efficient Market Hypothesis and the Rational Expectations Theory” (Soros 2010).