# Gruesome Growth

No enterprise is an island.

Every enterprise sits within a larger social reality, what we call society. From society, enterprises draw sustenance, everything they need to survive. Take this sustenance away, enterprises founder, then die, just like fish out of water.

What do enterprises need from society? They need, of course, people able to perform enterprise work. The more able employees a society has to offer, the better off enterprises will be. To make the most of these employees, this "human capital," enterprises also need financial capital. They need money for equipment and supplies, for offices and payroll, for production and marketing. Without adequate capital, human and financial, no enterprise can hope to succeed.

Not all enterprises with adequate capital, of course, always succeed. Many fall short. Some fail because they do not organize themselves for effective operation. But even wonderfully effective enterprises can — and do — fail. An enterprise can assemble a wonderfully talented workforce. An enterprise can outfit that workforce with the finest tools and resources. An enterprise can sweep away the hierarchical underbrush that keeps employees from doing their best. An enterprise can get everything right and still flop miserably for one reason and one reason alone. If not enough customers who want an enterprise's products can afford to buy them, the enterprise will fail. Always.

In desperately poor societies, nations where people have precious little wealth to spend, enterprises will always struggle to gain a foothold. The same struggling will take place in societies where the wealth available to spend suddenly starts shrinking, during, for instance, a recession or depression. A society where wealth contracts severely may see even its grandest enterprises fumble and fail.

Modern societies, naturally, do their best to prevent their stocks of wealth from contracting. But no modern society aims merely to maintain existing wealth. Modern societies, even those that have already amassed considerable wealth, all aim to generate new wealth. And this drive for greater wealth makes sense. No society, after all, has yet achieved perfection. We all live in societies that can be improved, and wealth helps the improvement process along. Opportunities for progress, as economist Robert Frank points out, "are greater in a rich society than in a poor one."



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"A richer society," Frank explains, "has more resources for medical research, more resources for rapid transit, more time for family and friends, more time for study and exercise — and more resources for better insulated houses and cleaner, more fuel-efficient automobiles."[1]

If we want our lives to be improving, we need our economies to be generating new wealth. Almost all economists, whatever their political inclinations, start from this assumption. But economists, after starting from this assumption, soon part company — over questions about how wealth, new and old, ought to be distributed. No society can generate significant stocks of new wealth, many economists argue, without allowing existing wealth to concentrate. Other economists vigorously disagree.

How exactly *should* wealth be distributed? Does existing wealth need to be concentrated — or shared — to create new wealth? Or does distribution matter at all? These are important questions. They've been vexing economists — and societies — for centuries.

THE CLASSICAL ECONOMISTS, THE THINKERS who laid the foundations of modern economic thought, cared deeply about distribution. Two hundred years ago, these early economists saw the distribution of income between social classes "as a central determinant" of how rapidly new wealth would accumulate.[2]

David Ricardo, the English businessman who would author, in 1817, one of the most important early texts of economics, placed considerable emphasis on the distribution of wealth between landlords and capitalists. Landlords, argued Ricardo, wasted their wealth on personal luxuries. Capitalists, by contrast, invested whatever wealth came their way in productive enterprises, where more new wealth could be created. Economies, Ricardo concluded, grow more efficiently when dollars accumulate, as profits, in capitalist pockets. The more rent money fills landlord pockets, the less vital an economy will be.[3]

Karl Marx, writing a generation later, would share Ricardo's assumption that distribution matters. But Marx, writing early in the Industrial Age, saw the relationship between capitalist and worker, not the link between landlord and capitalist, as modernity's driving force. That relationship — "the distribution of income flows going to labor and capital" — determined, for Marx, how rapidly wealth accumulates.[4]

Marx and like-minded critics of the world's new industrial order would raise unsettling questions about these income flows, questions about justice and injustice that more status quo-oriented economists, later in the nineteenth century, would do their best to slide off the table. These new "neoclassical" economists broke with the classical tradition. They dismissed distribution as essentially irrelevant.[5] A thousand dollars in one pocket, they believed, would always buy the same amount of goods and services as a thousand dollars in ten pockets. So why bother with distribution? Their new orthodoxy — that distribution need not trouble serious students of how economies grow — soon dominated the emerging academic discipline of economics. Discussions about income and wealth distribution, notes historian James Huston, largely "disappeared from economics texts."[6]

Outside the ivory tower, meanwhile, concerns about distribution would not disappear. In the late nineteenth century, with giant fortunes rising across the industrial world, with enormous power concentrating in the hands of small numbers of exceedingly affluent people, many less than exceedingly affluent people were beginning to consider questions about distribution among the most relevant a society could ever ask.

The exceedingly affluent could hardly ignore this growing public unease. They needed to be able to rebut their critics. They needed an unapologetic justification for the widely unequal distributions of income and wealth that had so many people around them apprehensive and upset. This justification would emerge in the late 1800s. Economies, admirers of grand fortunes began to argue, need capital to grow and prosper. But capital can never accumulate without some people becoming wealthier than others. The resulting inequality, friends of the fortunate contended, ought to be welcomed, not feared. If wealth was concentrating, then capital was accumulating.[7] If capital was accumulating, better tomorrows were sure to follow.

This aggressive, in-your-face defense of inequality thrilled the colossally wealthy. But reasonable and responsible business and political leaders recoiled from it. Intense inequalities, these more sober leaders understood, gave radical critics of the existing social order powerful ammunition. Society's elites could not afford to be seen cheering on inequality. The Russian Revolution, and the later onset of the Cold War, would only reinforce this conviction. The capitalist West, clear-headed business and political leaders realized, could never win Cold War hearts and minds by defiantly defending inequality. The inequalities of Western capitalist society didn't need to be defended. They needed to be placed in context.

The context would come, midway through the twentieth century, from Simon Kuznets, a widely respected, Ukrainian-born Ivy League economist. Kuznets, as part of a body of work that would earn him a Nobel Prize, essentially delinked modern market economies and inequality. Kuznets described inequality as an inevitable, but purely transitional, consequence of industrialization. Agricultural nations moving into the industrial age, he counseled, would always see levels of inequality rise, mainly because people working in the emerging modern sector of the economy would always outearn people still working in the traditional agricultural sector.[8] But this inequality eventually fades away, Kuznets argued, as industrializing nations mature. More and more people, as economies develop, become part of the modern wage economy. Incomes, across society, start equalizing. The more market economies evolve, the more equal they become.[9]

The eminent Kuznets made his case in a landmark 1955 presidential address to the American Economic Association. His thesis proved enormously appealing to America's Cold Warriors. Market economies now had no need to feel defensive. Inequities might still scar the United States, but America would ultimately outgrow them.

"Equity will follow growth," Kuznets seemed to be saying to the Cold Warriors, "so there is little reason to worry about it."[10]

American economic realities, meanwhile, seemed to be proving Kuznets right. In the 1950s, America was becoming more prosperous *and* more equal. The nation could stand tall, a proud beacon to the world. Just follow us, America's leaders could say proudly to the Cold War world, we know the way to tomorrow.

That way, two decades later, would seem less certain. By the mid 1970s, America's march to shared prosperity had stalled. Poverty, noted one esteemed economist, Arthur Okun, a former chairman of the Council of Economic Advisers under Lyndon Johnson, "remains the plight of a substantial group of Americans." Large disparities in income distribution, Okun wrote in 1975, "continue to mar the social scene."[11]

Inequality, apparently, wasn't just some nasty, transitional phase that market economies, once mature, put behind them. Indeed, the liberal Okun argued, inequalities come naturally to market economies. These inequalities, he added quickly, need not — and should not — be meekly accepted. Smart societies can — and should — take steps to lessen inequality. But any steps that reduce inequality, Okun argued, also reduce economic efficiency. The more a society pushes for an equitable distribution of income and wealth, the less robustly that economy will create wealth, "largely because income redistribution reduces the incentives for work and investment."[12]

Personally, Okun noted, he might prefer otherwise, but, in real life, "the conflict between equality and efficiency is inescapable."[13] A wise society, he contended, accepts the inevitability of this conflict and goes about making do by making tradeoffs, sometimes accepting less growth to help make society more equal, sometimes accepting less equality to keep the economy growing. Decent societies, Okun believed, search for balance between equality and growth. Out of these balancing acts, he hoped, would come more decency. By making smart tradeoffs, Okun contended in his 1975 book, *Equality and Efficiency*, an affluent nation like the United States could even eradicate poverty.[14]

*Equality and Efficiency* did not, as Okun had hoped, help eradicate poverty. The book instead helped eradicate the campaign against poverty. Conservatives turned Okun's carefully argued case for thoughtful tradeoffs into an admission, by liberals, that any attempts to make America more equal — by, for instance, expanding aid to poor people — would inevitably backfire on everyone, the poor included, by slowing economic growth. Armed with Okun, conservatives confidently blamed the "stagflation" of the 1970s on excessive social spending and "invoked" Okun, in the years ahead, to rationalize America's "growing concentration of wealth."[15]

"By the mid-1980s," economists Randy Albeda and Chris Tilly would later point out, "most economists agreed that the key problem facing the U.S. economy was stagnant growth, not rising inequality."[16]

America needed to get growing again, mainstream economists in the 1980s asserted, and that meant accepting inequality. An America that prudently embraced inequality — that gave the wealthy ample incentives to become wealthier — would, over time, bring joy to all Americans. Everyone would become richer, mainstream economists agreed, if only we let some people become richer than others.

Conservative politicians loved this simple formulation. Liberals would be intimidated by it. Any step toward a kinder, gentler society now seemed suspect. So liberal leaders, for the most part, stopped stepping. They would join with conservatives, in the late 1970s and early 1980s, to make America safe for great fortunes. Conservatives and liberals, together, would vote to reduce taxes on the rich and regulations on corporations. They then sat back and waited for the payoff, the "bigger economic pie" America's mainstream economists promised, a pie big enough to ensure average Americans much larger servings than they had ever before enjoyed.

The payoff did not come, not in the 1980s, not in the early 1990s. By the mid 1990s, a new generation of economists was doubting that inequality would ever pay off. Inequality and growth do not, these skeptical scholars began demonstrating, march hand in hand. Nations that smile on concentrations of wealth and income, they amassed evidence to show, do not automatically become more productive.

One major study, published in 1994, compared growth and income distributions in fifty-six different nations. Those nations that displayed the widest income gaps, the study found, actually grew their gross domestic economic pies the most slowly.[17] Other studies piled up similar findings. By 1997, Princeton economist Roland Benabou could count at least thirteen different "cross-country empirical analyses," all performed in the 1990s, that demonstrated "a negative effect of inequality on growth."[18]

Statistics gathered from within the United States backed up these international findings. Economist Larry Ledebur compared growth rates in eighty-five U.S. urban areas. The wider the income gap between cities and their suburbs, he found, the slower the growth in income and jobs.[19]

By century's end, the evidence appeared overwhelming. Clearly, noted a 1998 paper for the Federal Reserve Bank system's annual summer retreat, "the older view, that greater inequality is associated with faster growth, is not supported by the data."[20]

America's corporate leaders would pay these new findings next to no attention. They would continue to toast the same concentrations of wealth economists were now roasting. The hundreds of millions of dollars pouring into America's executive suites, business commentators exclaimed, were working miracles. They amounted to a "secret weapon contributing to the unprecedented recent growth of the U.S. economy."[21]

"Rather than demonstrating rampant greed," *Chief Executive* magazine would exult in 1999, "today's CEO pay packages have helped the U.S. achieve glory as the unchallenged leader of the world's economy."[22]

*CHIEF EXECUTIVE*, WE NOW KNOW from our post-Enron perspective, had everything backwards. The "glory" the American economy achieved in the 1990s — the gloriously high corporate earnings, the gloriously soaring share prices — did indeed demonstrate "rampant greed," a greed that drove executives, accountants, bankers, and lawyers to lying and larceny and whatever else it took to keep their personal gravy trains rolling.

We also know, from the 1980s and 1990s economic record, that growth and inequality run on separate tracks. During these two decades, inequality rose over periods of years when the economy grew and also rose during periods when the economy contracted.

"The lesson is simple," note economists Randy Albeda and Chris Tilly. "The relationship of growth to distribution is neither a tradeoff nor an automatic cause-and-effect."[23]

Economies can grow in societies that are becoming more equal. Economies can shrink in societies where wealth is concentrating. Equality does not automatically frustrate growth. Inequality does not automatically spur it.

Given these realities, does the distribution of wealth and income, within a society, really matter? Does the level of inequality within a nation make a substantial impact on how well, or poorly, a nation creates wealth? Levels of inequality most certainly do make an impact, argue Albeda and Tilly and like-minded economists, but that impact depends, within each society, on the overall institutional and political environment, on who gets to define the ground rules.[24] Different rules produce different rates of economic "growth."

Why should that be? If we pause to consider just what economists mean when they say an economy is "growing," the reasons become fairly clear. Economies that are "growing" are simply producing more goods and services than they previously produced. Economies that are producing fewer goods and services are shrinking, not growing.

How can economies produce more goods and services? In several ways. An economy can grow if more people within a society start working. With more people working, more goods and services will be produced. An economy can also grow if people already working start working longer hours. Finally, and most importantly, an economy can grow if the people in it become more productive, if they can produce more goods and services in the same amount of time.

How can people become more productive? They can receive training that improves their skills. They can reorganize how they work and become more efficient. They can get their hands on better tools and equipment. They can explore exciting new technologies. They can be pushed to work harder or, conversely, inspired to work more creatively.

In the abstract, any of these steps can increase the volume of products and services a society produces. In actual practice, societies mix and match these approaches to economic growth, and no two societies ever come up with the same mixes. These varying approaches to growth, in turn, have varying impacts on equality. Some game plans for growth will tend to increase economic inequality. Others will leave societies more equal.

In the early days of the Industrial Age, in the United States and in Europe, the powers that be followed what might be called a brute-force game plan. They would grow their economies — that is, produce more goods and services — by working as many people as long and as hard as they could possibly work them. Early industrializing societies threw everyone they could into the workforce, even children. We look back today on these societies and shake our heads in disbelief. Twelve-year-olds working dawn to dark. How could civilized nations countenance such brutality? In fact, at the time, the powerful didn't just countenance such brutality, they lustily defended it.[25] They resisted, with all their might, any attempts at outlawing child labor. If children were not permitted to work, elites argued, who would bring home the bacon for families headed by widows?

No widows, the opponents of child labor shot back, should be forced to sacrifice their children to the industrial mammon. Society had a moral obligation to guarantee a basic level of decency to every family.

Back and forth went debates just like this, in every nation that stepped into the Industrial Age. New rules had to be set for this new age, rules that would determine just how goods and services would be produced — and each rule would have consequences for the distribution of wealth and income. If, for instance, a society resolved to stretch a well-knit safety net, to make sure all widows and children were guaranteed sustenance, resources would have to be found to hold that net in place. New revenues would have to be raised. New taxes would have to be levied. The wealthy might even have to part with a substantial share of their incomes. Any societies that resolved to take these steps, to protect the weak and tax the wealthy, would, over time, move toward greater equality.

On the other hand, in societies that strung only half-hearted safety nets, fewer families at the economic margins would ever see help. More people would feel pressured to seek work, at whatever wage they could get. Desperate new workers would flood the job market, depressing wage rates and, in the process, enriching the owners of industrial empires. These societies, over time, would become more unequal.

Battles over safety nets, over taxes, over every economic rule imaginable, would be fought — and refought — throughout the nineteenth and twentieth centuries in all the societies we now call the developed nations. By the 1990s, these years of conflict had produced two fundamentally different sets of rules in the market economies of the developed world, two decidedly different perspectives on how best to produce more.

In most of Western Europe, the rules would privilege equality. In the United States, the rules would welcome and encourage the concentration of wealth and income.

On nearly every significant rule-making question, Western Europe seemed to answer one way, the United States another.

Would the safety net be taut or torn? The Europeans stretched safety nets taut and strong enough to cushion most all of life's stumbles and slumps. Unemployed European workers, for instance, could collect jobless benefits that equaled up to 90 percent of their last paychecks.[26] These benefits could run, in nations like Belgium and Denmark, as long as the workers remained jobless.[27] In the United States, by contrast, two-thirds of the workers who lost their jobs in the 1980s and 1990s collected no unemployment benefits whatsoever.[28] Those fortunate enough to find help received no more than 50 percent of the previous pay — and that benefit would be cut off after six months.[29]

What about jobs themselves? How secure would they be? In the United States, government placed almost no restrictions on a company's ability to dismiss workers "at will," without any meaningful advance notice or severance.[30]

In Europe, workers could not be cavalierly fired. Under French and German law, employers had to be able to demonstrate, in a court of law if necessary, the economic necessity or "social acceptability" of any layoff. In most of Europe, no worker could be laid off without advance notice, with the length of the notice usually tied to a worker's job tenure. An experienced white-collar worker in Belgium, for instance, would be entitled to a year's advance notice before any layoff could take place. Many European nations also *mandated* severance pay, more than a half-year's worth in some cases.[31]

And how much would jobs pay? In market economies, of course, governments don't determine wage levels, not directly at least. But governments can have a huge indirect influence on wages, based on the rules they establish for labor relations. In nations where workers can organize themselves into unions, free from employer and government interference, workers will always make more in wages than workers in comparable nations where rights to organize are not respected.

In the United States, by the 1980s, laws no longer adequately protected basic worker rights to create and join unions. Employers, throughout the closing decades of the twentieth century, routinely fired rank-and-filers active in union organizing campaigns. If these illegal firings weren't enough to intimidate workers, employers would threaten to shut down their operations if workers opted for union representation, another illegal maneuver. And if workers were somehow able to win union representation, despite these illegalities, they still had to get their employer to sit down and bargain in good faith. Many employers in newly organized workplaces, some 40 percent of them, didn't.[32] Workers could file complaints against all these "unfair labor practices," of course, but complaints typically took years to work their way through the legal process.[33]

By 1985, not surprisingly, only 17 percent of America's civilian wage and salary employees belonged to unions. In Germany, that same year, 40 percent of employees belonged to unions.[34] But even these figures understated the incredibly wide difference between union influence in the United States and union influence in Europe. In the United States, unions typically bargain contracts that apply only to the employees of a specific employer. In Europe, unions typically bargain collective wage agreements that apply to entire industries. At century's end, just 14 percent of workers in the United States were covered by union-negotiated wage agreements. The coverage rate in France, Germany, and Belgium: 90 percent.[35]

The ongoing assault on worker rights in the United States, Ohio Congressman Dennis Kucinich would tell a labor gathering in 2001, amounted to "a means of redistributing the wealth upwards."[36] And in the United States, as opposed to Europe, most wealth that worked its way upwards stayed there. The tax rules saw to that. In 1997, wealthy taxpayers in the United States paid, on paper, 39.6 percent of their income over $263,750 in national income taxes. The top marginal tax rate in Germany that year ran 53 percent. The top rate in France: 57 percent.[37]

All these many different rules — on safety nets, on wages, on taxes — would create by century's end one distribution of income and wealth in Western Europe, quite a different distribution in the United States. By the early 1990s, American men in the top 10 percent of income-earners took home 5.6 times more per hour than men in the bottom 10 percent. In France, that gap stood at 3.2 times, in Germany 2.7 times.[38] By the mid 1990s, 27 percent of American households fell within a generally accepted definition of middle-class status. That is, just over a quarter of households in the United States had incomes no more than 25 percent less or 25 percent more than the income of the typical American household.[39] In Germany, by contrast, 44 percent of households could claim this middle-class status. In Sweden, 53 percent of households made within 75 and 125 percent of the nation's median household income. In other words, the middle class share of Swedish society almost doubled the middle class share in the United States.[40]

European nations, clearly and without a statistical doubt, sliced their economic pies into pieces that were considerably more similar in size than the pieces of America's economic pie. But the cheerleaders for corporate America, we need to remember, never promised Americans a pie with equal pieces. They promised a bigger pie. If America cheered on the rich in their efforts to become even richer, the promise went, those rich folks would bake up a pie big enough to give everybody a king-sized piece. The pieces in that pie wouldn't be anywhere near equal in size, but why care about that? Even the smallest piece in

America's pie would be bigger than the pieces people elsewhere would be getting. That was the promise. That promise would not be met. The unequal American economy did, as promised, grow in the 1980s and 1990s. But so did the more equal economies of Western Europe.[41] And those more equal economies delivered, for average people, bigger pieces of pie than the pieces served up to average Americans.

In 1995, the wages and benefits of manufacturing workers in the United States, once the world's highest, ranked thirteenth in the world. German workers pulled in the equivalent of $31.88 in wages and benefits in 1995, American workers only $17.20. Workers from throughout Western Europe — from Switzerland, Belgium, Austria, Finland, Norway, Denmark, the Netherlands, Sweden, Luxembourg, and France — all outpaced American manufacturing workers.[42]

The next five years would see the U.S. economy boom to record levels. But that boom did not send American workers back to the top of the international scale. In 2000, according to U.S. Bureau of Labor Statistics data, hourly compensation costs for manufacturing workers in the United States still averaged 17 percent less than costs in the former West Germany.[43] And that was after adjusting the figures to dollar equivalencies, a statistical move that exaggerated compensation in the United States, because the value of the dollar had risen considerably against other currencies.

The United States, to be sure, remained the richest nation in the world. No nation produced more goods and services than the United States. And therein lay the irony. In the richest nation in the world, as economists Gary Burtless and Timothy Smeeding would note, the "incomes of low- and even middle-income Americans are below those of residents in industrialized countries that are poorer than the United States."[44]

Indeed, if the value of what America's economy produced in the 1990s had been distributed more equally, say as equally as in Germany, the average American worker would have been nearly 20 percent better off than the average German worker.[45]

European workers, amazingly, weren't just earning higher incomes than comparable workers in the United States. They were working fewer hours to make those higher incomes. Americans, the International Labor Organization reported in 1999, were putting in, on average, eight more weeks worth of time on the job every year than their counterparts in France and Germany.[46]

Americans, by century's end, were eating from the developed world's most unequal economic pie. But who had time to measure?

WESTERN EUROPEAN NATIONS, WE SHOULD PAUSE TO NOTE HERE, had not become paradises on earth by the start of the twenty-first century. Europeans did not live equal or problem-free lives in the 1980s and 1990s. They just led lives that were *more* equal and *more* problem-free than lives led in the United States. But inequalities in Europe remained profound, as the continent's critics were quick to point out. The distribution of wealth, columnist Robert Samuelson correctly noted midway through the 1990s, is "wildly unequal in all advanced societies."[47]

Commentators like Samuelson argued that whatever equality Europe had achieved had come at the expense of jobs for European workers. Europe's high taxes, tough restrictions on business, and strong labor unions, they contended, had "discouraged job creation" in the name of enhancing "economic equality and job security."[48] Americans might have a less equal society, the argument went, but at least they had jobs.

Americans defensive about inequality in the United States found this notion — that Europe had traded off jobs for greater equality — irresistibly attractive. They held to it with an almost religious intensity, in total disregard of the actual official unemployment numbers. One top analyst from Wall Street's Goldman Sachs, interviewed for a *New York Times* article published early in 2002, asserted, for instance, that "there's not one country in Europe that doesn't have a higher unemployment rate" than the United States.[49] In fact, the actual figures told an entirely different story. Official unemployment in the United States, at that moment, was running at 5.7 percent. At the same time, the United Kingdom (5.1 percent), Sweden (4.7 percent), Portugal (4.4 percent), Denmark (4.4 percent), Austria (4 percent), Ireland (3.9 percent), Norway (3.6 percent), and the Netherlands (2.2 percent) were all running lower official rates of unemployment.[50]

European nations, by doing more than the United States to keep incomes equal, had not created perfect places to live and work. But Europe had managed to create, in the late twentieth century, societies that worked substantially better for average Europeans than the United States worked for average Americans. Working people in Europe made more than working people in the United States and labored fewer hours. Most average Europeans could move through their lives, from cradle to grave, seldom if ever feeling financially desperate. Even in rough times, their incomes would be protected, their health care covered. They could be doing better economically, of course, but they were doing, overall, just fine, thank you, particularly compared to their American counterparts.

Their bosses could not make the same claim. By every measure, corporate movers and shakers in Europe lagged behind their counterparts in the United States. American business leaders made more than European business leaders, had considerably more influence over the political process, and just generally enjoyed more leeway to do what they wanted when they wanted to do it.

Europe's elites knew what they were missing. At Davos, the Swiss resort where global corporate and government leaders started gathering annually in 1982, as well as at other forums and venues, elite Europeans imbibed the American way — and chafed at their second-class status. They resolved, throughout the 1980s and 1990s, to roll back the rules that made doing business on their continent so much more difficult than doing business across the

Atlantic. And they made progress in that effort. Rallied on by free marketeers like Britain's Margaret Thatcher and Germany's Helmut Kohl, the member nations of the European Common Market would approve "radical changes" in their economic governance. They would push down European throats as big a dose of Americanism — anything-goes markets stripped of government regulation — as they could get the people of Europe to swallow.[51] They would bring into being a European Central Bank that would follow tight-fisted interest rate policies, even if that meant, as it did, pushing up jobless rates.[52] And they would slash tax rates on the highest European incomes.[53]

European executives, with these new incentives in place, would soon start playing American-style "restructuring" games with their companies and their employees. They would plot and consummate mergers, $800 billion worth in 1999 alone.[54] They would downsize.[55] They would catch up, as best they could, with their U.S. counterparts. Some, like Jean-Marie Messier, would mimic the every move of their American CEO heroes.

Messier, in the late 1990s, wheeled and dealed an obscure French water utility into a global media giant, Vivendi Universal. Along the way, he "parroted American business jargon with the exuberance of a convert," taking on massive corporate-America-style debts as he merged his way to "synergy" and greatness.[56] Messier enjoyed the perks of greatness, too, with a $17.5 million corporate pad on New York's Park Avenue.[57]

Messier's good buddy, Thomas Middelhoff, the top executive at Bertelsmann, a German media company, went even further down the American corporate road. Middelhoff described himself as "an American with a German passport" and made English his company's official language.[58] He would follow the U.S. corporate model step by step, buying up companies to inflate Bertelsmann's revenues, always maneuvering for his ultimate endgame, a massive public offering of his company's stock. His wheeling and dealing would turn Bertelsmann into the world's third-largest media company.[59]

In Switzerland, another ardent admirer of American executivedom, Percy Barnevik, styled himself Europe's answer to Jack Welch, the fabled General Electric CEO. Barnevik chaired the Zurich-based ABB Ltd., one of the world's biggest engineering companies, and preached an American-style gospel of maximizing shareholder value.[60] He also did his best to maximize his own personal value, awarding himself a $120 million pension.

For Europeans, all this American-style executive grasping would be too much to bear.[61] Average Europeans fought back. In France, where polls showed that nine of ten adults considered downsizing by profitable companies "unacceptable," consumers would boycott Danone, a food company that slashed payroll to boost earnings. The boycott so infuriated the powerful chairman of one key French bank, Jean Peyrelevade, that he promptly announced he would double his consumption of Danone's yogurt products.[62]

But Europe's top executives would have to do a lot more than up their yogurt intake to get their continent aboard an American-style corporate express. In the end, they would not prove equal to the task. By 2003, Europe's top American-style executives had almost all flamed out. In Switzerland, CEO Barnevik resigned after ABB's share prices dropped 60 percent.[63] Shareholders took back more than half his $120 million pension, and Swiss government officials began a criminal investigation against him. Barnevik would claim he was guilty only of giving himself an "American payment system in a European environment."[64] In France, Jean-Marie Messier lost his CEO perch, midway through 2002, after a year that saw the heavily indebted Vivendi lose $41 billion.[65] Messier, an American-style CEO to the bitter end, walked off with $17.8 million in severance.[66]

But the most fascinating flameout would belong to Thomas Middelhoff, the top executive at Bertelsmann. Middelhoff was ousted shortly after Messier, but Bertelsmann, unlike Vivendi, had not yet started to implode before the ax came. The ax fell on Middelhoff, a *Wall Street Journal* analysis would later explain, because the good burghers on the Bertelsmann board feared that their American-style CEO was, by placing profits first, last, and always, destroying their venerable company's "corporate philosophy of using business as a means of paying for good deeds."[67]

That philosophy meant a great deal to the Bertelsmann board. Back in the mid nineteenth century, company founder Carl Bertelsmann had envisioned his new publishing business as an instrument "to better society, not increase profits." The company would become, before 1900, one of the first German firms to provide employees pensions and disability protection. Bertelsmann workers would later become the first in Germany to enjoy paid vacations. Under Reinhard Mohn, the great-grandson of founder Carl Bertelsmann, this tradition would continue. Deep into the twentieth century, just about half the company's annual earnings went into employee profit-sharing plans.[68]

Mohn, eighty-one in 2002, felt that tradition threatened by CEO Middelhoff's American ways. He would engineer, halfway through the year, Middelhoff's ouster by the Bertelsmann board.[69] A worker representative on the board, Erich Ruppik, would later explain where Middelhoff had gone so wrong.

"When he stepped on the gas," Ruppik noted, "he forgot about taking the employees along."[70]

In Europe, as Jean-Marie Messier, Percy Barnevik, and Thomas Middelhoff would learn to their chagrin, an equality-minded culture had simply become too embedded to be swept away by corporate executive superstars. Going forward, Europeans believed, was something that executives and employees ought to do together, not apart.

THE CORPORATE SCANDALS THAT BROKE into the headlines early in the twenty-first century would make a powerful impression on European public opinion. Europeans, already intensely suspicious of American-style approaches to economic growth, saw the Enrons and the WorldComs — and their European clones — as the inevitable outcomes of a capitalism "that rewarded greed and short-term gain and turned high-flying chief executives into celebrities."[71]

In the United States, the scandals elicited a far different reaction. Few political or corporate leaders felt any obligation, in Enron's wake, to question America's basic approach to wealth creation. They blamed bad apples instead. They also worried. Americans, they feared, might overact and, in their zeal to prevent future Enrons, change the basic rules that America's elites had spent a generation perfecting, rules that locked into place what some economists had come to label "the Wall Street model."[72]

This Wall Street model started taking shape in the 1970s, America's years of economic "stagflation," a time when interest rates, prices, and jobless rates were all, for the first time ever, rising at the exact same time. Most economists, ever since the work of John Maynard Keynes in the 1930s, had become convinced that governments could keep economies on a more or less even keel by increasing government spending whenever the private economy turned sluggish. But stagflation did not seem responsive to what had become the standard solutions.[73] Government couldn't solve stagflation, critics from Wall Street charged, because government had become the problem. Government needed to get out of the way, to free the free market from years of red tape and regulations.

At one level, this Wall Street critique merely recycled themes that elite interests had been expounding ever since the earliest days of the Industrial Era. On another level, this critique offered something new, a more sophisticated case for embracing inequality.

This new case for inequality — the "Wall Street model" — argued that America's future prosperity would depend on the nation's ability to become more productive. We would only grow the economy, the model's champions contended, if we first increased productivity. And how could we increase productivity? Nations become more productive, the Wall Street model postulated, when they invest in technologies that help workers produce more goods and services.[74] Consequently, the Wall Street model posited, smart societies do everything possible to encourage increased investment.[75]

But investments can't increase unless a society boasts a growing pool of savings that investments can be drawn from. Americans, the Wall Street model argued, weren't saving enough. Indeed, the model charged, the government was making the problem worse — by spending too much and taxing incomes at too high a rate. High taxes, Wall Street insisted, keep affluent families from saving as much as they otherwise would. High spending levels, they added, generate budget deficits, and the government, once in deficit, has to borrow to keep operating. The more the government borrows, the more demand for the dollars that banks have available for lending. The greater this demand, the higher the interest rates on loans. The higher these interest rates, the less borrowing by businesses — and the less investing business will be likely to do.[76]

How to break this grisly cycle? Just stop taxing and spending. Be nice to businesses. Encourage them to invest.

In the closing decades of the twentieth century, America's political leaders would swallow and follow the Wall Street model. They would lower taxes and federal spending. They would "free" business from regulations that limited profit potential. They would take steps that kept wages depressed. Rising wages, Wall Street preached, would only encourage inflation. In the name of fighting that same inflation, political leaders would even applaud Federal Reserve Bank moves that kept the economy from "overheating," even if those moves jacked up jobless totals.

All these policies, to the naked average citizen eye, could sometimes appear contradictory. To encourage savings, for instance, lawmakers would enact tax cuts that put more dollars into wealthy people's pockets. But lawmakers, at the same time, would refuse to boost the minimum wage — and place more dollars in poor people's pockets. What sense did that make? And if higher wages needed to be resisted because they might inflame inflation, why give corporations tax breaks for raising executive pay?

The more average Americans tried to find the rhyme to Wall Street's reason, the more curious the Wall Street model began appearing. How could so many clever and celebrated people be following such an internally incoherent set of policies?

In reality, the Wall Street model did have an internal logic to it, a consistency that never flagged. Within the Wall Street model, any course of action that might end up concentrating more wealth into the pockets of rich people would be good. Any course of action that might narrow the gap between rich people and everybody else would not.

Welfare "reform" that would shove poor moms into the job market, good. A job market flooded by former welfare recipients would depress wages, increase corporate earnings, keep share prices — and, naturally, executive stock option windfalls — rising.

Trade agreements that would smooth the way for U.S. corporate investment in foreign lands, good. American companies, after the passage of the North American Free Trade Agreement, wouldn't even have to move their plants to take advantage of lower wages outside the United States. They could depress wages just by threatening to move.

Lower spending on domestic social programs, good. In the name of balancing the budget, safety net programs for working families would be sliced to inadequate shreds, increasing the pressure on bread-winners to work more hours, at rock-bottom wages.

Deregulation, good. In deregulated industries, a handful of corporations would soon come to totally dominate the market. A sure prescription for higher corporate earnings, higher share prices — and more top executive windfalls.

Tax cuts for the wealthy, the best of all. In the short run, such cuts would mean immediate increases in the annual disposable income of wealthy households. In the longer run, cuts in the taxes levied on wealthy people would shrink government revenues and make deep cuts in safety net programs inevitable. That, of course, would mean more desperation out among working families — and a workforce even more agreeable to whatever wages employers might choose to pay.

By century's end, America's political elites had delivered almost everything Wall Street wanted. And these Wall Street-friendly policies had their intended effect: They helped wealthy Americans amass incredibly large fortunes. Immense new pools of capital were now available for investing in a more productive America. These pools of capital should have, according to Wall Street theorists, fueled a productivity revolution. But the significantly more productive America promised by the Wall Street model never appeared. In 2000, the Economic Report of the President would note that productivity in the United States had increased 2.05 percent a year in the 1990s, an increase over the 1980s rate, but a rate well under the 3.07 percent annual productivity gain of the 1960s.[77]

In the 1960s, Wall Street's critics noted pointedly, the United States had followed economic policies that violated almost every basic precept of the Wall Street model. In that 1960s decade, wages rose and great fortunes didn't, an economic cardinal sin according to 1990s Wall Street economic orthodoxy. To add insult to injury, careful analysts were able to trace much of the productivity growth that did take place in the 1990s to decisions made back in the 1960s and 1970s, *before* boosters of the Wall Street model started calling all the nation's economic shots.[78]

Overall, productivity gains in the last quarter of the twentieth century, years of growing inequality, amounted to less than half of the productivity gains of the century's third quarter, years of growing *equality*.[79] The United States, by following the Wall Street model, by encouraging, wherever possible, the concentration of wealth, had actually ended up placing a brake on productivity growth. Something had gone terribly wrong. But what? The Wall Street model's champions didn't stop to ask. We should.

MANY OF US HOLD, IN OUR MIND'S EYE, a delightful image of how science leaps ahead. There, beside a gorgeously sunlit meadow, sits young Isaac Newton under an apple tree. With a bonk, a red delicious bounces off Newton's noggin. What's this, he wonders. Gravity, he exclaims! One thing leads to another, and three centuries later people are standing on the moon.

We tend to overlook, in our popular culture and political discourse, everything that comes between the bonk and the moon ride. In the real world, scientific progress requires relentless research, not sunlit meadows. And relentless research, in our modern world, has always required government support. Historically, over the past hundred years, government dollars have bankrolled most of the scientific research that has fueled America's productivity progress. In fact, according to one 1997 study, nearly three-quarters of the "main science papers cited in American industrial patent applications" are based on research financed by government or nonprofit agencies.[80]

Private corporations, over the years, have generally made a much more limited contribution to basic research and development, or "R&D." Such research takes both time and money, and few corporations feel inclined to spend either on ideas that may or may not work out profitably.

"Really good research has always been the stepchild of the corporation," notes David Isenberg, himself a veteran of one of the handful of corporations, AT&T, with a well-regarded R&D history.[81]

Good basic research, scientists like Isenberg contend, can only thrive in institutions with enough patience to stick with research over the long haul. Government agencies and universities can fit that bill. So can private companies without any real competition in their industries. AT&T, for instance, built the world-acclaimed Bell Labs — where Isenberg worked — during its years as the government-regulated telephone monopoly. IBM and Xerox, two other companies with long R&D histories, spent decades without serious competition in their respective industries. They "provided stable, comfortable homes for many of the nation's brightest minds."[82]

These corporate homes, by century's end, no longer offered scientists much comfort. In a corporate America almost completely preoccupied with generating king-sized quarterly earnings gains, research that might deliver productivity gains down the road in some distant future held somewhere close to zero appeal.

"We've reached a point where R&D inside a corporation is fundamentally impossible," Peter Cochrane, the former chief technologist at BT Labs, a telecom think tank, noted bluntly in 2001. "The financial people want you to pick the winners. You can't."[83]

America's corporate executives, at the turn of the century, desperately needed winners now, not later. What good was research that might translate into breakthroughs twenty years down the road? In twenty years, someone else would be CEO, someone else would be reaping a stock option windfall if that research actually paid off. In this environment, top corporate officials had no patience whatsoever with researchers who yearned to follow their hunches, to whatever deadends or brilliant inventions those hunches might lead. Corporate America, instead, pointed researchers to the quarterly bottom line and ordered them to produce. These marching orders, within corporate research centers, would produce considerably more frustration than insight. Top researchers, by the early twenty-first century, were mourning an era that appeared forever lost.

"In the old days, there was a spirit about it — a spirit of free innovation," Robert Lucky, a distinguished scientist at Bell Labs, would tell reporters in 2001. "Research was an end in itself. Today, that's not true at all. Profitability is the end."[84]

Research that couldn't deliver profits, on a timely regular schedule, held no allure for corporate executives, who, on a timely regular schedule, expected to be cashing out one ample option payoff after another. These ample payoffs both outraged and enticed corporate scientists. On the one hand, these researchers couldn't stomach what windfall-driven decision making meant for their freedom to pursue their intellectual curiosity. On the other hand, many researchers were intrigued by the prospect of hitting some option jackpot themselves. Over one eighteen-month period near century's end, 15 percent of the Bell Labs research team jumped ship "after glamorous startups promising quick-hit riches lured them away."[85]

"Research for the sake of research gave way to innovation with a payoff," summed up the high tech trade journal, the *Net Economy*. "Greed won out."[86]

The lure of big payoffs actually devastated intellectual research communities both inside *and* outside corporate America. Greed, after all, could not be quarantined to the private sector. In the late 1990s, at the height of the boom years, academic research centers the nation over watched researchers bail out to grab their piece of the windfall action. Academics "who had the skills," noted Sreenath Sreenivasan, a Columbia University tech guru, "wanted to be out there making money."[87]

And if you wanted to be making money, education was certainly not where you wanted to be. In the boom years, education would not boom. Federal expenditures on education and training, over the century's last quarter, actually dropped, as a share of gross domestic product, by 50 percent.[88] That decline, a stunning marker of education's true "priority" status in the 1980s and 1990s, would frustrate educators enormously.

But many economists would be frustrated, too, especially those who had been studying just what makes one society more productive than another. These "New Growth" economists directly challenged the core assumption of the Wall Street model, the notion that capital investments drive productivity growth, end of story. Investments, the New Growth economists readily agreed, surely do play a significant role in enhancing productivity, but so do several other equally important factors, most notably the presence of a skilled, well-educated workforce. New technologies, the New Growth economists explained, cannot by themselves make a workplace more productive.[89] New tools and techniques need to be massaged in the workplace, adopted to real life situations, refined and tweaked in ways that make them more useful. That massaging only takes place if employees bring a quality set of skills to the workplace.[90] Investments in new technologies, in effect, only pay off if employees have been well educated and trained.

At one level — the rhetorical level — America's top corporate leaders understood this connection between productivity progress and education. The 1980s and 1990s saw an enormous outcry, from corporate suites, for better schools. In 1983, the release of *A Nation At Risk*, a landmark report engineered by the U.S. Department of Education, triggered a barrage of special commissions that aimed to improve the quality of American education, many of them chaired by corporate leaders. These executives would intone, at every opportunity, the absolute centrality of education to America's economic future. For the United States to prosper, they agreed, every child had to be educated.

But education, in the end, costs, and corporate America would not be willing to pay the price. The Wall Street model did not envision a bigger federal commitment to education. Federal spending needed to be slashed, not increased. If spending were increased, after all, how could taxes be cut, how could wealth be accumulated? In the 1980s and 1990s, the nation's leaders would talk the talk about education. They would not walk the walk.

By century's end, fewer young Americans, not more, would be getting a full and complete education. The federal Pell Grant program, an effort designed to help low-income families send their kids to college, covered 98 percent of public college tuition in 1986. In 1999, the program covered only 57 percent.[91] Many low-income families could not afford to pick up the difference, even with loans. The predictable result: In 2002, research by economists Michael McPherson and Morton Owen Schapiro documented "that the percentage of high-achieving students who do not enroll in college is five times higher among those who are poor than those who are rich."[92]

Numbers like these, argue economists not enthralled by the Wall Street model, help explain why unequal nations don't grow economically as well as nations where wealth is more equitably distributed.[93] In nations where wealth concentrates at the top, more people lower down on the economic ladder simply "lack access to the education and training that would enable them to contribute to economic growth."[94]

WISE GOVERNMENTS, THE NEW GROWTH THEORISTS TELL US, invest in education. But wise governments also understand that productivity gains won't blossom without a wide range of investments in other public goods as well. Some of these investments — government support for cutting-edge scientific research, for instance — create the knowledge we need to become more productive. Other expenditures, like dollars for plugging potholes, make more prosaic contributions. These create and maintain the "infrastructure" that helps us work more efficiently. Without an adequate infrastructure, modern economies crumble.

"Consider what would happen to economic growth," economists Barry Bluestone and Bennett Harrison asked at the turn of the century, "if the interstate highway system were suddenly to disappear, or narrow down to one lane in each direction."[95]

In the decades right after World War II, the United States systematically invested in infrastructure, in everything from sewage to cyclotrons, and the nation would become substantially more productive. In the closing decades of the twentieth century, the nation would shortchange these investments. In the 1970s, federal spending on infrastructure averaged over 2.5 percent of the nation's gross domestic product. By the late 1990s, that share had dropped to just 1.5 percent, an investment shortfall that equaled hundreds of billions of dollars — and amounted to a huge drag on technological progress.[96]

A perhaps even more significant drag, some analysts suggested, was coming from *within* enterprises. A healthy economy, these analysts noted, certainly needs a solid, supportive infrastructure. But the infrastructure that supports our workplaces may not, in the end, limit our technological progress as much as the relationships within our workplaces. A solid educational infrastructure, for instance, can keep enterprises supplied with employees who have the knowledge and skills that enterprises need. But enterprises need to be able to tap this knowledge effectively, or else these skills will go to waste.

New technologies, analysts explain, can't just be forced *upon* a workplace. They need to be fine-tuned *in* the workplace, with the active involvement — and cooperation — of workers and managers alike. In modern corporate America, unfortunately, workers and managers have not been in a cooperating mood. Decades of growing economic inequality have, as we have seen, nurtured defective, not effective, enterprises. In these defective enterprises, enterprises where loyalty had been downsized and looted away, workers have little reason to help with fine-tuning new technologies.[97]

But corporate America's productivity problem actually goes far beyond sullen workers. In a corporate America more interested in squeezing workers than involving them, employers have as little incentive to think seriously about improving productivity as employees. The more depressed employers are able to keep wages, the less their incentive to invest significantly in higher productivity. Why invest in new technologies when old technologies, thanks to cheap labor, remain quite profitable?

Employers who share rewards with workers, by contrast, must think seriously about improving productivity. To compete successfully in the marketplace, Barry Bluestone and Bennett Harrison have pointed out, companies that pay higher wages "have to find ways to use their workers more effectively."[98] Rising wages, adds *Business Week*'s Aaron Bernstein, can actually "spur productivity growth."[99]

If Bernstein's observation accurately reflects reality, productivity gains should be meager in those economic sectors where wages are low — and that is, in real life, exactly the case. In the United States, the two economic sectors with the worst wages, the service and retail sectors, have registered the smallest gains in productivity.[100] Could this low productivity in service and retail simply reflect the hard-to-automate, one-on-one nature of service and retail work? Possibly. But if that were the case, then service and retail work the world over, and not just in the United States, would lag in productivity. The service and retail sectors, however, do not lag behind in productivity everywhere across the world. In some societies, service and retail show significant productivity gains. These societies share one common trait: They pay decent wages for service and retail work.

In Germany, service sector productivity, in the 1970s and 1980s, grew seven times faster than service sector productivity in the United States. Over this same period, service sector wages rose in Germany more than twice as fast as they rose in the United States.[101]

LOW WAGES CAN POWERFULLY UNDERMINE whatever incentive an employer may have to make investments in productivity. Low wages also have a broader and, perhaps ultimately, even more damaging impact: They reduce the demand for goods and services an economy produces.

Demand matters, and much more so than the Wall Street model suggests. The model, as we have seen, treats interest rates as the essential element that determines economic growth. If businesses can borrow money at reasonable interest rates, they will. They'll use this borrowed money to make investments. These investments will grow productivity and, eventually, the economy. All will be well — if interest rates are only kept low. But businesses, in actual practice, will only make investments that will help them produce more products if they see a demand for these additional products. If that demand appears unlikely to materialize, businesses simply don't invest, no matter how low interest rates may be. In the Great Depression, interest rates crashed to under 1 percent. But businesses did not rush to borrow, even at these low rates. They saw no demand.[102]

During the 1930s, the years of the Great Depression, British economist John Maynard Keynes helped policy makers understand this demand dynamic. If average people had more income, Keynes argued, they could afford to buy more goods and services, in the process boosting demand and restoring the overall economy to better health. In this demand equation, Keynes and his followers added, the distribution of a society's income mattered mightily. Dollars in average people's pockets would always do more to rev up demand than dollars in rich people's pockets because poorer people tend to spend a larger *share* of their income on goods and services than richer people. The more shared a nation's income, the less concentrated a nation's wealth, the greater the demand for goods and services.[103] Inequality, simply put, saps demand. Equality boosts it.

In an economy where demand is rising, businesses see sales to be registered, if they can only produce more goods. So they invest in their workers. Productivity advances. More goods are produced. And these goods sell, because people can afford to buy them. Businesses prosper. They hire more workers. Workers prosper. The more workers prosper, the more goods and services they buy — and businesses prosper even more, all thanks to a distribution of wealth and income that encourages a healthy flow of dollars into average people's pockets. No rocket science here. Just plain common sense.

"Indeed," as economists Barry Bluestone and Bennett Harrison have quipped, "most business leaders would like to see higher wages — at every company save their own."[104]

This tension stalks every modern market economy. In the abstract, every business wants customers with lots of cash in their wallets. The more cash available to be spent, the more sales likely to be recorded. But businesses don't see all people as customers. Businesses see some people — the people they hire — as workers. The more dollars individual businesses put in the pockets of these people, their workers, the fewer dollars these businesses may see in profits.

Individual businesses, as a consequence, have an ever-present incentive *not* to raise wages. But if every business were to succumb to the low-wage temptation, all businesses would be worse off, since one employer's workers are another employer's customers.

So what do businesses do? Do they act in their overall best interest or in their individual self-interest? Left to their own devices, history has shown, individual businesses almost always follow their individual self-interest. They seek to minimize their wage obligations. They create, in so doing, an enormous downward pressure on demand that, sooner or later, sends the overall economy into a tailspin.

History also shows, fortunately, something else. Societies do not leave individual businesses to their own devices. Countervailing social forces, most notably trade unions, emerge. These unions organize to take wages out of competition. Where they succeed, individual businesses cannot gain a competitive advantage by shortchanging their workers. They must compete on some other basis, by producing, for instance, better quality goods and services or by producing goods and services more efficiently. Societies that set stiff wage standards, in other words, give all businesses an ongoing incentive to pay close attention to what consumers want — and operate as productively as possible.

In the United States, right after World War II, stiff wage standards would be set. Unions would set them. By the mid 1950s, over one out of every three private sector workers in America belonged to a union. The nation's labor movement had never been stronger. Unions, with this strength, would help stretch a tight safety net all across the American economy. The minimum wage climbed steadily in the 1950s and 1960s, reaching, in 1968, its highest inflation-adjusted point ever. Minimum wage workers that year made $1.60 an hour, enough to push a family of three 18 percent *over* the official poverty line.[105] This rising floor under wages, coupled with stiff tax rates on the nation's highest incomes, created by the end of the 1960s the most equal income distribution in modern American history, a distribution that kept demand high and steady. Between 1947 and 1973, points out long-time Labor Department analyst Paul Ryscavage, every family seemed to be "sharing in the income-producing capacity of the economy."[106]

"The nation's economic pie was getting bigger," adds Ryscavage, "and everyone was helping themselves to a larger and larger piece of the pie."[107]

But then, in the 1970s, the tide turned. American businesses, for the first time in years, began facing real competition in global markets, from the newly vibrant European and Japanese economies. Cheap fuel, meanwhile, had disappeared, after the OPEC nations flexed their oil-producing muscles. The decent wages that America's major corporations had been paying suddenly appeared to be unnecessary extravagances. By the mid 1970s, corporate leaders were talking openly about creating a "union-free environment." Together with like-minded politicos, they pressed for a new American economic order.

The Wall Street model gave the campaigners for this new order all the ideological cover they would ever need. Rising wages, the model argued, ought to be seen as a catalyst for inflation, not as an essential source of demand. The new Reagan Administration would take this advice to heart. The minimum wage would rise, nineteen days before Ronald Reagan's 1981 inauguration, to $3.35. That would be the last minimum wage hike for nearly a decade. By 1991, the real value of the minimum wage had fallen 16 percent below 1981 levels.[108] By 2001, minimum wage workers earned, after adjusting for inflation, 35 percent less than minimum wage workers earned in 1968.[109] In the new century, minimum wage workers who worked full-time, year round, ended up with incomes that left them 22 percent *under* the poverty line for a family of three.[110]

The sinking real value of the minimum wage would place downward pressure on all wages.[111] Still more downward pressure would come from two decades of outright assault against organized labor. President Reagan would set the tone, in 1981, by hiring "replacement workers" to permanently displace over eleven thousand striking air traffic controllers.[112] That move signaled a landmark about-face in America labor relations. For over forty years, ever since the 1935 passage of the Wagner Act, the basic legislation that protects workers' right to organize, employers had rarely tried to break strikes by permanently replacing strikers.[113] President Reagan's open defiance of this established labor relations practice gave corporate threats to fire strikers a powerful credibility — and that credibility would blunt the effectiveness of the strike as an antidote to corporate power. In 1995, only thirty-two strikes involving at least a thousand workers took place in the United States. Twenty years earlier, eight times that many strikes involved a thousand workers.[114]

Year by year, in the 1980s and 1990s, the wage standards established in the 1950s and 1960s collapsed a little bit more, and with this collapse came a widening gap in America's income distribution. More income concentrated at the top. Fewer dollars trickled down to the bottom. Between 1980 and 1999, the value of the minimum wage fell 18 percent. CEO pay rose, those same years, by 882 percent.[115] By century's end, in a United States where unions represented less than 10 percent of America's private sector workers, decent wage standards could simply not be maintained.

Some policy makers did worry deeply about this collapse of wage standards. They feared a potentially catastrophic drop in consumer demand. Workers, U.S. Labor Secretary Robert Reich reminded the nation halfway through the 1990s, "are also consumers, and at some point American workers won't have enough money in their pockets to buy all the goods and services they are producing."[116]

Even some business leaders worried about America's enormous income imbalances.

"This is going to blow up in our faces," Lucent Technologies chairman Henry Schacht warned in 1998, "There is no way a society can have this much of its accumulated wealth distributed to these few people."[117]

But the blow-up did not come. Demand did not drop precipitously, or even at all. The economy kept growing right into the new century. Why no collapse? Why no horrible stumble? What happened?

Debt happened. Working families kept demand up for America's products and services by racing deeper and deeper into debt. By 1998, America's average household carried "a debtload that approaches its annual income."[118] The entire American economy balanced perilously on an ever-growing stack of credit cards and home equity loans.

This massive debt should have started alarm bells ringing on Wall Street. By century's end, after all, champions of the Wall Street model had been banging the drums for savings, not spending, for over twenty years. America would prosper, they had asserted over and over, when savings started accumulating, savings that could be translated into productivity-boosting investments. But America's massive indebtedness in the 1980s and the 1990s rang no bells, mainly because the debtors, to Wall Street eyes, didn't matter. The debtors were working families, and Wall Street had never expected working families to do any savings heavy lifting. Wall Street had always expected savings to come from affluent families. The growing indebtedness of working families simply became, for Wall Street, another excuse to target more tax breaks to the affluent. How else would the United States be able to increase the pool of savings available for investment?

So the tax breaks — for the wealthy — continued to flow. America continued to become more unequal. This growing inequality, in turn, stimulated still more indebtedness. Households, as economist Ted Schmidt points out, don't make consumption decisions just on how much money they have. They base their consumption decisions, to a large degree, on how much affluent households are spending.[119] The greater the level of inequality in a society, the more powerful the pressure on lower-income families to spend what they don't have. In the boom years, this pressure helped push indebtedness in average American households to record levels — and helped ensure that the sum total of savings in the United States would not rise. Debt at the bottom, in effect, canceled out surplus at the top. The glory years of the Wall Street model would end without any aggregate gain in American savings.

Wage cuts, giveaways to wealthy taxpayers, and smaller safety nets, Wall Street had promised, would deliver unto America massive new accumulations of capital for productive investment. Wage cuts, tax giveaways, and smaller safety nets would deliver, in the real economy, no such thing.

In fact, the Wall Street model would deliver unto America the exact opposite of productive investment. The Wall Street model would deliver speculation.

DOWN THROUGH HISTORY, WEALTH HAS at times concentrated at enormously rapid rates. Down through history, societies have also at times gone off on spectacular speculative binges. These times almost always turn out to be one and the same.

Inequality seems to inevitably breed speculation. Let great wealth accumulate at a society's summit and great speculative bubbles will soon blot out the economic horizon. In the 1630s, the huge fortunes that had found their way into the purses of Holland's finest families fed a tulip bubble so outrageous — a handful of flowers could cost $40,000 — that the bursting of that bubble sent the Dutch into deep depression.[120] Eighty years later, the fantastically flush French and English deep-pocket set chased after New World land with a manic intensity that sent deeds soaring to tulip-like levels. In the 1840s, another speculative frenzy exploded, this time around railroads, as the great fortunes of the early Industrial Revolution stoked the fires of the Great British Railway Mania. In the United States, after the Civil War, the first American men of fortune in the modern Industrial Age would catch the same railroad mania. Their speculative fever would rage on and off for thirty years. America's railroad bubble would finally burst, for good, in 1893 — and help trigger a depression that lasted a good part of a decade.[121]

The 1920s would see another epoch of rapidly concentrating wealth in the United States, an epoch that would end with America's most fabled bursting bubble of them all, the 1929 stock market crash. In that bubble's wake would come the longest and deepest depression in American history.

What explains this link between speculation and concentrating wealth? Why does an overabundance of dollars in a limited number of pockets almost always produce wild flights of economic fancy?

To understand speculative fevers, we actually need to look first at households where pockets *aren't* overflowing. In societies where wealth is concentrating at the top, households further down the economic ladder will have less wealth to spend on goods and services. Those with wealth, in turn, will have little reason to plow that wealth into productive investment, simply because little demand will exist for the goods and services that productive investment might produce. But large wealth-holders have to do something with all their dollars. They can, after all, only personally consume so much. So what happens with these dollars that wealthy people cannot consume and cannot invest productively? The wealthy plow these dollars into speculation. The speculative schemes they "invest" in may pay off, and if they do, how wonderful for the wealthy. The schemes, of course, may also flop. But if they do flop, no big deal. The money lost doesn't really matter — not to wealth-holders who have money to burn.

Most of us never experience this sensation of having "money to burn." We work hard for our paychecks. We depend on every dollar. We can't afford to risk any significant chunk of our savings. The wealthy can. They can afford to chase speculative investments that offer big returns — and so they do. Chases can be thrilling.

People of modest means do sometimes find themselves in a similar situation — the same situation that wealthy people experience every day — and these people of modest means typically behave, in these rare situations, the same way rich people behave. Consider the $2 racetrack bettor who cashes out a totally unexpected $100 daily double winner. What normally happens next? Our lucky winner, who seldom ever bets more than $2 in any one race, suddenly turns around and starts laying down $10 and $20 bets. And why not? Our bettor did no work to earn that $100 of daily double winnings. Our bettor has no sweat equity invested in that $100. Those dollars amount to "play money," so our bettor plays. All lucky bettors act the same way. They routinely risk their surprise winnings in ways they would never risk a paycheck.

Wealthy people are life's lucky bettors. They may indeed work hard, but no one makes megamillions punching a time clock or billing hours. Grand fortunes only emerge when someone somehow is able to leverage someone else's labor. A factory owner pockets a dollar on every item workers fabricate. A department store magnate pockets a dollar on every purchase sales clerks register. An heir inherits a great many dollars all at once. These are dollars that can be risked freely, even wildly. They are less than real. They are, in every unequal society, the kindling wood for speculative fires.

The more unequal a society, the more kindling wood, the more fires. In the 1980s and 1990s, kindling wood abounded — and so did speculation.

The wealthy of these years speculated on commodities. In 1994, for instance, trading in crude-oil futures and options on the New York Mercantile Exchange quadrupled the total amount of crude oil the entire world that year actually produced.[122]

They speculated on currencies. The World Bank, by the latter years of the century, was estimating that 95 percent of the thousand-plus billions of dollars in daily global currency flows amounted to pure speculative trading.[123]

They speculated on real estate. In Manhattan, wealth's world capital, clothing mogul Tommy Hilfiger picked up a Fifth Avenue apartment for $10 million in 1999. The next year, he put that same apartment up for sale at $20 million.[124]

But, most of all, the wealthy speculated on stocks. The closing years of the twentieth century will forever be remembered for the wildest, zaniest, most bizarre speculative binge in American financial history.

The binge began, innocently enough, in 1982. On Friday morning, August 13, the Dow Jones Industrial Average, the marquee measure of Wall Street's daily ups and downs, stood at 776.92, after a modest drop the day before. The Dow would never sit that low again. Friday's trading brought gains, so did the next week's. More gains came in the months ahead. By year's end, the Dow would top 1,000. The "greatest bull market ever" had begun.[125] Nothing would stop this raging bull. The market would drop suddenly in 1987. But that drop would prove only a pause. By August 1989 the market had regained all the ground lost in 1987. Half a dozen years later, in 1995, the steady climb would take an even steeper turn up — into territory not seen since the 1920s.

That turn would come when Netscape Communications, the company behind the first commercial software for browsing the World Wide Web, stunned Wall Street with the first dot.com initial public offering. On August 9, 1995, Netscape offered 5 million shares to investors at $28 each. By day's end, those shares would be selling for more than twice that. Netscape, a company that had never made a profit, would suddenly be worth $2.2 billion.[126] No major company, in stock exchange history, had ever debuted so stunningly.

The wild bull ride would now be on, with steady helpings of fresh IPOs keeping the bull suitably energized. The Nasdaq composite index, the best measure of the high-tech sector, jumped 23 percent in 1996.[127] The next year saw still more gains. Veteran Wall Streeters were starting to get alarmed. Such increases, they feared, could not be sustained.

"Today," Peter Bernstein, a mutual funds director, told the press midway through 1997, "the market has begun to penetrate into zones of irrationality."[128]

Bernstein hadn't seen anything yet. In 1997, Nasdaq would finish up 22 percent for the year, then follow that with an even more incredible 40 percent advance in 1998. The next year couldn't possibly top that. It did. The Nasdaq rose 86 percent in 1999.[129]

High-tech telecommunications and software companies led the way. Qualcomm ended 1999 up 1,882 percent, Sprint PCS up 357 percent, Oracle up 263 percent.[130] Even more amazing were the run-ups of companies that were fledgling, at best, by every normal economic measure. Yahoo, the Web search engine, boasted all of 803 employees in February 1999, a smaller workforce than a run-of-the-mill manufacturing plant. Wall Street valued Yahoo at $34 billion. E-Bay, the online auction house, employed only 130 people. Wall Street investors valued E-Bay at $11 billion, a total that made each employee worth $86 million.[131]

Share prices couldn't possibly climb any higher. Of course, they did. Priceline, a dot.com that hawked cut-rate air travel tickets, would be "worth more at its peak than every U.S. airline put together."[132]

Over the second half of the 1990s, *Business Week* would later note, all stocks together "racked up five consecutive calendar years" of annual returns that topped 20 percent, "three years more than ever before."[133] By March 2000, the ratio of stock prices to corporate earnings had "reached more than twice its historic average." The bubble, measured by that historic average, had inflated the value of stocks "on the order of $10 trillion, more than $30,000 for every person in the country."[134]

Some Wall Street watchers, amazingly, were convinced that nothing but even brighter stock market days lay ahead. In August 2000, one of the most celebrated of these optimists, James Glassman, the co-author of *Dow 36,000*, would debate one of Wall Street's few wet blankets, Barton Biggs, a Morgan Stanley strategist, before an audience of well-heeled listeners at a resort in Idaho's Sun Valley. Biggs preached caution and gloom — and lost the debate, in an audience vote, by an 85 to 3 margin. Afterwards, one of the eighty-five came up to Biggs's wife Judith.

"I'm worried about your husband," the listener noted caringly. "I think he's lost touch with things. He's out of date."[135]

Investors had little patience for skeptics like Biggs, little patience for anyone who stood — or fell — in the way of hitting still another big stock market score. In the middle of the market mania, on March 25, 1997, one market veteran, a forty-eight-year-old trading assistant named Paddy Grieve, fell suddenly to the New York Stock Exchange trading floor, right next to the spot where he had been working the past twenty-five years. Grieve's co-workers gave him CPR. The rest of his fellow traders nearby paused for a moment, then went on shouting out their trades. Doctors at a downtown hospital would later pronounce Grieve dead from a heart attack.[136] Who could blame the traders for ignoring Grieve? They couldn't help him. But they could certainly help themselves. There was work to be done, there were fortunes to be made.

Fortunes for Wall Street players of every sort.

"Everybody here is overpaid, knows they are overpaid, and is determined to continue to be overpaid," as one Wall Street player, Julian Robertson, told the *Washington Post.*

Robertson, the top gun at Tiger Management, a high-risk investment house, expected to personally score, the *Post* reported in 1998, "well above $500 million this year."[137]

Few of Robertson's colleagues and competitors would be *that* overpaid. But they did quite nicely nonetheless. In 1999, one securities company alone, Merrill Lynch, handed five top executives at least $14 million each.[138]

The market would peak one year later, in March 2000. By April 2001, stocks had lost $4 trillion of their peak, an amount that topped the combined gross domestic products of Britain, France, and Italy.[139] By June 2002, the market was off $6 trillion, a third of its total value.[140] Smiley-faced commentators did their best to minimize this loss. Nobody actually lost $6 trillion, they argued. The lost value had only existed "on paper." True enough, but the modern world revolves around paper. Wall Street's collapse meant that millions of workers would have to delay their retirements — or start them with a fraction of the nest-eggs they thought they had accumulated. Thousands of other Americans lost their jobs, as companies rushed to cut costs and get their share prices inching up again.

Other Americans lost their dream — of becoming rich.

Throughout the boom, fast-talking operators had peddled that dream all across America. One of these operators, Wade Cook, America's top promoter of "investment self-help instruction," conducted thirty-two hundred investing seminars in 1997 alone. Investors, to attend one of these seminars, paid $5,695 per person. Students could also, of course, invest in handy investment vehicles Cook was happy to make available to his budding investing talents. In all, observed *New York Observer* columnist Christopher Byron, Cook "talked nearly 400,000 would-be investors out of $100 million in 1997."

"What we're seeing here, folks," an amazed and amused Byron noted, "is the birth of America's first vertically integrated moron-milking machine."[141]

Scam artists have been milking "morons," of course, ever since time began. Here in the United States, scam artists even occupy an honored place in our folklore. We all enjoy Hollywood movies about dashing fast-talkers who can, just by flashing a smile, separate the unwary from their wallets. But fast-talkers like Wade Cook aren't, in the final analysis, what made the great 1990s stock market boom the greatest scam of all time. The Cooks were just small fry. The real schemers weren't two-bit grifters. The real schemers were the deep-pockets behind America's most revered financial institutions.

By the final quarter of the twentieth century, the United States had evolved the most sophisticated system for generating investment capital the world had ever seen, or so proclaimed America's business elites. America was creating wealth, they marveled, because America appreciated the wealthy — and had created a financial superstructure that enabled the wealthy to translate their fortunes into investments that enrich the lives of all Americans. Thanks to this marvelously efficient superstructure, they continued, any American with a business idea worth exploring could get a shot at success. America had created, in a sense, an entrepreneurial heaven on Earth.

Throughout the boom years, appropriately enough, any would-be entrepreneurs entering this heaven would usually be met first by a class of wealthy individuals known collectively as "angels." These angels sported no halos, only thick money belts. By the mid 1990s, federal officials had accredited some 250,000 of them. These angels had the green light to invest in "unregistered securities," to buy, in other words, a piece of the action in fledgling new companies. And invest they did. By 1996, wealthy angels were plowing about $20 billion a year into start-ups.[142]

Additional dollars for fledgling companies would come from "venture capitalists," professional investors who rounded up chunks of investment cash from various deep-pocket sources and, like individual angels, bought stakes in new businesses. Venture capitalists would emerge, in the 1990s, as the princes of America's financial landscape. The most celebrated of them, John Doerr of Silicon Valley's Kleiner Perkins Caufield & Beyers, began venturing in 1980. By 1990, his venture capital firm was claiming credit for birthing new companies that had created over $30 billion in stock value.[143]

Angels and venture capitalists prepped up-and-coming entrepreneurs for the big time. But to break into that big time — to actually issue stock to the investing public — entrepreneurs needed to tap into still another key financial player, the Wall Street investment bank. These "banks" did no normal banking. They took new companies "public," by selling shares in them to outside investors. From these sales, the theory went, new companies would gain the wherewithal to revolutionize the marketplace with bright new ideas. The economy, infused with these ideas, would throb with new energy. Businesses would grow more productive. Everyone would benefit.

But everyone would benefit, business leaders lectured lawmakers, only if government also did its part — by helping wealth accumulate. By following the Wall Street model, lawmakers were informed, they could keep America's financial system suitably greased and running smoothly. Tax cuts would ensure that angels and venture capitalists had enough spare cash to invest. Low wages would help keep corporate earnings rising. Rising earnings, in turn, would keep corporate stocks attractive to investors and expand the market for the new companies Wall Street investment houses brought "public."

Lawmakers, suitably impressed by this Wall Street logic, did their best to cooperate. They did their greasing, then sat back and watched capital surge through America's private investment channels. In 1990, venture capitalists invested $3.7 billion in fledgling companies. In 1999, venture investments totaled $45 billion, a twelve-fold increase.[144] In 2000, some seven hundred venture capital firms were sitting on $105 billion.[145]

"Venture cash is transforming half-formed ideas into world-beating products and services," *Business Week* exulted.[146] Venture capital, exclaimed *Worth*, is playing "a vital role in the U.S. economy, funding start-up companies and nurturing them with money, experience, and connections."[147] And investment banks, cheerleaders added, were taking those companies the final mile, getting them to market where they could raise the cash they needed "to finance growth or crucial research and development."[148] Over the course of the boom years, investment banks would bring the shares of more than five thousand companies to market, in stock offerings that raised over $300 billion.[149]

"We're the only country in the world," joked Clinton Treasury Secretary Lawrence Summers, "where you can raise your first $100 million before you buy your first suit."[150]

The picture the cheerleaders painted could hardly have been more appealing. Bright, talented, energetic entrepreneurs overflowing with revolutionary, paradigm-smashing great ideas. Angels and venture capitalists, wise in the ways of business, sharing their dollars and wisdom with tireless but inexperienced entrepreneurs. Investment bankers taking young entrepreneurs by the hand onto Wall Street, showcasing their fresh and exciting new ideas to investors all across the nation and even the world.

A pretty picture indeed, but one that in no way reflected reality. The American capital-generating process that evolved in the 1980s and 1990s had next to nothing to do with nurturing up-and-coming entrepreneurs or bringing world-beating products to market. America's capital-generating process did not generate a more productive economy. The process generated, instead, big paydays for the financial movers and shakers involved. Nothing else mattered.

Venture capitalists, flush with the cash the Wall Street model kept pumping into their pockets, behaved like any $2 bettor after a big daily double win. They laid bets — big bets — on as many fledgling companies as they could find. They then pushed these new companies to "go public" and start selling shares of stock as soon as possible. Why delay? Why waste time trying to figure out if the new company had a product or a service people really wanted to buy? Windfalls awaited, just an IPO away.[151]

Mentoring? Who had time for mentoring wet-behind-the-ears entrepreneurs? Venture capitalists, the Harvard Business School's D. Quinn Mills would later point out, were more into "bullying" their eager young entrepreneurs than mentoring them.[152] They demanded that entrepreneurs make ridiculously premature investments in mass marketing. Million-dollar Super Bowl commercials always made sense to the venture capitalists. How else was a company that hadn't yet proved any ability to survive in the marketplace going to be able to create a buzz loud enough to attract investors' attention?

Investment bankers played equally unhelpful games. Out the windows went the standards — the "due diligence" — meant to assure that only legitimate companies were brought before the investing public. Investment bankers were supposed to set a fair initial share price for any new issue they brought to market. In the boom years, notes D. Quinn Mills, they "grossly underpriced" their IPOs instead, then used that bargain-basement price in an "elaborate system of favor-trading" that "diverted money away from the entrepreneurs" into the pockets of the bankers' "high-roller clients." These high-rollers, typically the top executives of major corporations, would be allotted IPO shares at below-market rates. They would promptly unload these shares, scoring huge personal profits, when the IPO actually went public and started soaring. And investment bankers, naturally, did their best to make sure the IPO shares would soar. They promoted the new stocks "with hype dressed up as research" and aggressively marketed the shares to mutual funds that "were all too happy to goose their own near-term results by providing buy-side support."[153] These games could be incredibly lucrative, for almost everyone involved. One investment bank client, WorldCom chief executive Bernie Ebbers, made a crisp $10.6 million between 1996 and 2000 just by flipping IPO shares allocated to him by Citigroup. Officials at Citigroup would later deny they had done anything in the least bit improper. Rewarding wealthy clients with IPO shares, they told reporters, was simply standard Wall Street operating procedure.[154]

Venture capitalists did quite nicely as well, as the rise and fall of eToys, a typical overhyped dot.com retailer, would illustrate. In 1997, a venture capital firm named Idealab shelled out a half-cent a share to buy a $100,000 stake in the fledgling eToys. The dot.com would go public almost two years later, opening at $20 a share and closing its first day at $76. Later in 1999, Idealab would unload over 3.8 million of its eToys shares, at prices as high as $69. Total profit for the venture capitalists from Idealab: $193 million.[155] eToys would later go bankrupt.

America's financial movers and shakers did not, of course, only bankroll fresh-faced entrepreneurs and fledgling start-ups. Wealthy individuals and investment bankers stood equally ready to supply the capital that established companies needed to expand their operations. These investments in established concerns, the claim went, enhanced productivity and created jobs. But wealthy individuals and investment bankers had no more interest in nurturing productivity than they had in nurturing start-ups. In their investing, they targeted precious little capital into long-term investments that could result in significant, long-term productivity gains. They rushed instead to make the investments that promised the quickest and fastest payoffs. In the process, they would generate some of the most colossal — and wasteful — marketplace gluts the world had ever seen.

ONCE UPON A TIME, the residents of the United States had to make do with just one major long-distance telephone company, AT&T. The 1980s added MCI and Sprint to the mix. By the mid 1990s, that mix had multiplied many-fold. Phone lines, corporate America had discovered, weren't just for talking anymore. In the emerging Information Age, they could carry data, too, huge globs of bits and bytes. And the amount of data flowing through Wired America, anyone in an executive suite with a mouse and half a brain could clearly see, was only going to expand exponentially. Yesterday's wires brought voices into America's homes. Tomorrow's wires would bring, via broadband connections, the grandest fortune-making opportunity since Microsoft!

Into America's neighborhoods, to seize this opportunity, would rush over a dozen telecommunications companies, each with grandiose visions for national fiber optic cable networks. Miles and miles of fiber would go down, in, and under America's byways and highways, in a furious race to string together the fastest, widest national networks money could buy.

Money would prove to be no object. By the 1990s, after all, America's wealthy had plenty to burn. They poured these plentiful dollars into "telecom," the shorthand for America's hottest investment ticket. No one with cash seemed to want to sit on the sidelines. Microsoft co-founder Paul Allen invested $1.65 billion in a broadband company called RCN. Cable TV magnate John Malone poured $1.5 billion into a pair of telecoms known as ICG and Teligent.[156] Telecoms would borrow billions more from wealthy investors via the bond market. The industry's outstanding debt, $75 billion in 1995, would shoot up to $309 billion in 2000.[157]

The more cash Wall Street raised, the more cable telecoms kept laying. They would lay, in all, about 80.2 million miles of optical fiber from 1996 through 2001, enough to loop the globe over three thousand times.[158] Traffic to fill all these lines, the telecoms believed, at least initially, would surely materialize. But the traffic would never come, not in amounts near heavy enough to fill all the new cables dug into America. By early 2002, only 2 to 5 percent of all the fiber laid down by the telecom building boom would actually be carrying any voice or data.[159] The entire telecom boom, a J. P. Morgan analyst would tell the *New York Times*, had been "a phenomenal miscalculation."[160]

Telecom executives would do everything they could to stave off the inevitable popping of their bubble. They would try slashing prices to boost traffic and revenue. But the price cuts only led to price wars that, the *Washington*

*Post* later reported, “eventually left many companies with barely enough revenue to pay operating expenses, let alone interest on their huge mounds of debt.”[161] With revenues shrinking, the wire-happy telecoms would become even more desperate. They would, as we have seen, cook their books. But that move backfired, too, in a string of headline-grabbing scandals that would eventually deflate the telecom balloon by an incredible $2 trillion.[162]

Telecom’s wire woes would soon spill over into the wireless world. Cellular companies, facing competition from desperate, rate-cutting land-line telecoms, would find themselves forced to slash rates, too. Their revenues soon plummeted, as did revenues at Cisco Systems and other big telecom equipment suppliers. Cisco had invested hundreds of millions in ambitious telecom national networks and, on top of that, had loaned telecoms hundreds of millions more to buy Cisco equipment. The tanking telecoms would eventually leave companies like Cisco holding the bag.[163] In the first quarter of 2001, Cisco revenues fell 30 percent. The company laid off eighty-five hundred workers. Nortel, the top supplier of fiber optic networking gear, would see even more striking revenue reverses — and lay off twenty thousand workers.[164]

Overall, analysts reported in March 2002, close to six hundred thousand workers saw their jobs disappear when the telecom bubble burst.[165] American business had never seen an industry collapse so dramatically. On the list of the twenty-five biggest bankruptcies in U.S. history, telecoms, by August 2002, held ten slots.[166]

Amid the carnage, a host of telecom notables would walk away bruised but content. Qwest chairman Joseph Nacchio and co-chairman Philip Anschutz pocketed nearly $2.3 billion dumping big chunks of their Qwest shares before their company, one of the industry’s giants, started collapsing. Top executives scored phenomenal paydays even at second-tier telecoms. James Crowe, the CEO at Level 3 Communications, walked into the sunset with $115 million.[167] Jack Grubman, the Wall Street research analyst who kept urging investors to buy up telecom shares even as the industry was collapsing, averaged $20 million a year during telecom’s biggest bubble days. He left his Wall Street employer, Salomon, in 2002. As a parting present, Salomon forgave a $19 million personal loan Grubman had received from the company. Citigroup, Salomon’s owner, also handed Grubman a reported $12 million worth of Citi stock.[168]

Reporters started detailing these sorts of giveaways midway through 2002 in a series of thoughtful analyses that tried to trace just how the telecom debacle had unfolded. But one aspect of the story puzzled perceptive journalists like Gretchen Morgenson of the *New York Times*. They could understand why analysts like Jack Grubman would keep pushing telecom shares as a “buy” long after he knew the telecom game plan no longer made any business sense. They could understand why the investment banks like Salomon, Grubman’s employer, did their part to keep up pretenses. Grubman helped Salomon collect nearly $1 billion in investment banking fees. And reporters could even understand why deep pockets like Paul Allen and John Malone so unquestioningly poured billions into hare-brained telecom business plans. In any mad rush for fortune, reporters reasoned, sound judgments will always be suspended. But what about the telecom executives, the CEOs who kept announcing plans to lay more wires even after they knew, beyond any possible doubt, that the industry had already laid far more capacity in the ground than consumer demand could possibly fill. Why did these CEOs behave so irresponsibly?

In August 2002, this final puzzling piece fell into place. Gretchen Morgenson discovered that top executives of established telecom giants like Qwest, under the table and out of sight, had been cutting purely personal "sweetheart deals" with start-ups that supplied telecom equipment. The start-ups, Morgenson revealed, would sometimes give big-time telecom executives stock options "in exchange for an established executive's participation on an upstart company's advisory board."[169] Other times, start-ups would let executives in on IPO shares at bargain-basement prices. The telecom executives, however they received their start-up stakes, now had a personal incentive to help their favorite start-up's shares shoot up in price — and they had, at the same time, the power to provide the start-ups exactly the contracts they needed to build share price momentum. Nearly every contract to lay unneeded and unjustifiable cable capacity sent some start-up's share price soaring — and enriched the telecom CEO who had the contract let.

The industry analysts who helped Morgenson piece together this incredible story of telecom conniving and corruption could, in retrospect, only shake their heads.

"Looking back," noted one, Susan Kalla, "it looks more and more like a pyramid scheme."[170]

THE STOCK MARKET ISN'T, OF COURSE, supposed to be a con game. The stock market is supposed to be America's investment crown jewel, the source of the capital American businesses need to become ever more productive. In the 1980s and 1990s, this widely accepted notion — that the stock market actually serves a vitally important productive function — turned out to be the biggest con of them all.

In modern American business life, as opposed to modern American business folklore, corporations seldom look to the stock market for the capital they need to enhance their operations. Companies raise most of the capital they need internally, out of their own revenues. To raise any additional investment dollars, firms typically go first to commercial banks, or sell bonds. But companies do also float occasional new issues of their stock. And these new issues, in the twentieth century's closing years, did serve a definite business function. They served, in case after case, to bail executives out of the messes they had made with their mergers.

Big-time merger-and-acquisition sprees, in the closing years of the twentieth century, almost always left America's big-time executives saddled with staggering loads of corporate debt. Early on in the boom years, executives realized they could neatly offset, or at least reduce, those staggering debts by playing games with Wall Street. The process couldn't be simpler. An executive multimillions in debt would have his company issue new shares of stock that, once gobbled up by investors, would return multimillions to company coffers. The executive would then use these multimillions to pay down the company debt, in effect trading creditors for shareholders. The multimillions these shareholders paid for their shares, analyst Christopher Byron noted in 1997, essentially provided indebted companies with "a free loan that never has to be paid back."[171]

Those who celebrate Wall Street as a marketplace miracle that keeps companies well stocked with capital never seem to pay much attention to this sort of wheeling and dealing. They simply assume that dollars investors spend to buy shares of stock end up helping companies produce more goods and services. But the overwhelming bulk of stock market trades do not even involve transactions between a company and investors who want to buy shares of the company's stock. The overwhelming bulk of trades are simply transactions between one temporary owner of shares and another. Ninety percent of all stock market trades, notes St. Johns University economist Gary Mongiovi, "involve nothing more than the speculative reshuffling of the ownership of corporations."[172]

In effect, notes Columbia University's Louis Lowenstein, stock trading has become a game of "musical shares." The same shares are traded again and again. In the process, Lowenstein points out, "nothing is created."[173] Nothing useful. Nothing but fortunes.

The more trading, naturally, the more opportunities for making fortunes. The more bets you make, the more likely one bet will pay off big. In the boom years, bets on stocks bounced back and forth between investors at dizzying rates. In the early 1960s, shares on the New York Stock Exchange turned over at a 14 percent annual rate. By the late 1980s, stocks were turning over, going from one owner to another, at a 95 percent annual rate.[174] At century's end, shares of the very hottest stocks, like Amazon.com, would be turning over at a 100 percent rate *every two weeks.*[175]

None of this feverish speculation added an ounce of productive value to America's economy. In fact, this feverish speculation subtracted from America's productive might. Every trade, every churn of shares from one share owner to another, swallowed up time and resources that could have been put to far more productive use. The billions upon billions wasted away on this speculative trading amounted, as Adrian Slywotzky, a partner at Mercer Management Consulting noted in 2002, to "a massive redeployment of capital and people from fundamentally productive activities to fundamentally unproductive activities."[176]

How much capital, how many people hours, have been wasted away over the last quarter century? Economists may one day give us an answer.[177] We need here note only that Wall Street promised us economic growth, not economic waste. Let wealth concentrate, we were assured, and America's incredibly sophisticated financial markets would render unto us investments that would keep the United States the most productive of nations. Our representatives in Congress and our leaders in the White House believed in the Wall Street model. They took steps — everything from cutting taxes on the wealthy to freezing the minimum wage — that encouraged great wealth to concentrate. And great wealth did concentrate, at levels not seen in the United States since just before the Great Depression.

In return, great wealth gave us speculative waste, not productive investment, more economic waste than any generation of Americans had ever seen.

We should have expected no less. Con games never serve any productive purpose. Con games never create wealth. They concentrate it.

WEALTH THAT CONCENTRATES MUST BE PROTECTED, and protection costs. A great deal.

In early twenty-first century Manhattan, the ultimate in protection for wealthy households, a "safe room," ran $400,000 and up. A typical bulletproof, steel-reinforced safe room sported its own phone line and power generator, a computer that could lock and unlock almost any door in the house, and an "oxygen scrubber" to keep air inside the safe room from getting stale. A wealthy household could, if so inclined, accessorize a safe-roomed house with floor board stress detectors, burglar alarms for dresser drawers, and motion detectors that could tell the difference between pets and people.[178]

Security experts who install safety accessories like these now make up one of the nation's fastest-growing professions. Over one and a half million Americans currently work in private security. Over a half-million other Americans work in public law enforcement.[179] None of these security personnel, private or public, work at jobs that produce any of the goods and services we normally associate with a growing economy. Instead, they work to make sure that other people end up in a place — prison — where they can't make much of a productive contribution to the economy either. And that mission they have completed exceptionally well. America's inmate population jumped from just under two hundred thousand in 1970 to just under 2.2 million in 2002.[180] Law enforcement, overall, cost the nation $6 billion in 1968. The 2003 estimate: $210 billion.[181] The nation's *total* annual protection bill, the outlay for both public *and* private security, has surpassed a quarter trillion dollars.[182]

This oversized sum, analysts note, represents an enormous missed opportunity. The dollars we spend on security — if spent on something other than security — could make an important contribution to helping the economy become more productive. Just imagine "the boost in productivity that might occur," ask economists Randy Albeda and Chris Tilly, "if the money spent both privately and publicly to hire additional security and police were spent to hire child care workers."[183]

So what conclusion should we draw? Are we as a nation just wasting all the hundreds of billions we spend on "additional security and police?" Or do outlays for security, unlike outlays for speculation, serve a useful and absolutely essential social purpose?

That depends — on the level of outlay. Expenditures on security certainly do carry a socially redeeming value that speculative outlays can never match. No decent society can possibly stand by and let people be mugged and robbed. To be productive, people need to be safe. Resources spent keeping people safe do make an economic contribution, and a necessary one at that. But the resources we devote to security also exact a price. Societies that are fixated on protecting wealth are not creating wealth. The more societies have to spend on security to keep people safe, the less their capacity to help people become more productive. Societies that *don't* have to devote massive resources to security clearly have an economic leg up on societies that do.

We live today, the adage goes, in a dangerous world. Yet some nations in this dangerous world have been able to keep their populations safe *without* having to spend massively on security. Indeed, many societies that don't spend massively on security appear distinctly safer than other societies that do. The United States, for instance, spends far more on prisons than all other industrial nations. Six hundred of every hundred thousand U.S. residents lived behind bars in 1995. France only incarcerated ninety-five people per hundred thousand population, Sweden only sixty-five, and Japan only thirty-seven.[184] Did going to the immense expense of keeping all these law-breakers behind bars leave Americans safer? In the mid 1990s, a girl or a woman in the United States was four times more likely to be murdered than a girl or woman in Sweden, five times more likely to be murdered than a girl or a woman in France, and seven times more likely to be murdered than a girl or woman in Japan.[185]

How can some nations spend so little on security and still be safe? Some nations, analysts answer, are more equal than others. Crime rises in unequal societies. Where "the rich have more to protect and the poor have less to lose," note economists Randy Albeda and Chris Tilly, "crime goes up."[186] And crime keeps going up, other analysts add, as the gap between rich and poor widens. That gap, not poverty itself, is what drives crime rates. Indeed, poor societies can be safe societies, if people in them see that life's hardships are shared more or less equally. But where "rewards are inequitably distributed," as psychologists Martin Daly, Margo Wilson, and Shawn Vasdev have observed, "escalated tactics of social competition, including violent tactics, become attractive."[187]

Over the years, several other scholars, including the Nobel Prize-winning economist Amartya Sen, have traced the relationship between murder, the most violent of crimes, and income inequality. High poverty rates, these studies have shown, don't necessarily produce high homicide rates. High rates of inequality do. How equally or unequally resources are distributed, concluded one review of this research published in 2001, more powerfully impacts "levels of lethal violence in modern nation states" than "the average level of material welfare."[188]

For a case in point, look south. Look to Brazil.

By global standards, Brazil can actually claim to be an affluent nation. On a per capita income basis, Brazil rates higher than 77 percent of the rest of the world, and many nations, in proportional terms, have more people living in poverty than Brazil.[189] But no nations display a more striking gap between rich and poor. In Brazil, the richest 10 percent of families make nearly 50 times what the poorest 10 percent make.[190]

Amid this stark inequality, Brazilians spend $2 billion a year on private security arrangements.[191] In Sao Paulo state, a third of local residents "pay security guards to watch over their homes."[192] Sao Paulo's people have reasons to be nervous. The homicide rate in Sao Paulo city tripled in the 1990s. Kidnappings in Sao Paulo have become so common that some plastic surgeons now "specialize in treating wealthy victims who return from their ordeals with sliced ears, severed fingers and other missing body parts that were sent to family members as threats for ransom payment."[193]

Meanwhile, over in Brazil's second largest city, Rio de Janeiro, carjackings were taking place so often, by the late 1990s, that police officials assured affluent drivers that they wouldn't "be fined for running red lights at night." Thousands of those drivers took no chances. They armored their cars, typically at $35,000 per automobile. Motorists interested in "anti-explosive gas tanks," sirens, and other extras had to pay double.[194]

"Soon the haves will circulate throughout the city in personal tanks," Sao Paulo novelist Ignacio de Loyola Brandao predicted right before the century turned.[195]

That prediction would turn out to be somewhat off base. Brazil's wealthy took to the air, in the early years of the twenty-first century, not tanks. By mid 2002, Sao Paolo could claim the world's busiest helicopter traffic, with twenty-four times more helipads than New York. Sao Paulo businessmen rode helicopters every day, a *Washington Post* correspondent reported that year, "from their fortified offices to their fortified homes." In their walled neighborhoods private armies patrolled "behind electrified fences."[196]

"We have become prisoners in our own homes," Ellen Saraiva, the wife of one top Brazilian executive, admitted to a reporter. "One of my daughters is studying abroad right now, and as much as I miss her, it makes me feel at peace to know she is not here living through this nightmare."[197]

Thoughtful Brazilian economists had nightmares, too. In some countries, they knew, people woke up every morning thinking about what they could be doing at work to be more productive. Brazilians woke up thinking about what they could be doing to survive.

IN JAPAN, AT CENTURY'S END, few people woke up worrying about survival. And nobody was making fortunes armoring cars, mainly because the Japanese entered the twenty-first century with one of the world's lowest crime rates.[198] Families in Japan did not live behind electrified fences, shielded by private security armies. They lived, instead, about as equally as any people in the developed industrial world. In Brazil, the richest tenth of families made almost fifty times more than the poorest. In Japan, people at the top tenth of the income ladder made just over four times more than people at the bottom.[199]

Just 2 percent of Japanese households, in 1997, lived on less than $16,000 a year — and the exact same percentage, only 2 percent, made more than $160,000. Most Japanese families, over half, lived right in the middle, on between $35,000 and $75,000 a year.[200]

None of this equality evolved by accident. The modern Japanese did not inherit a remarkably equal society. They created it, after 1945, in a nation that had been pounded into rubble. World War II, points out journalist Kevin Sullivan, had destroyed nearly "all personal wealth" on the Japanese islands, "leaving Japan's aristocrats and peasant farmers alike struggling for the same food scraps in the bombed-out ruins."

"From that starting point," Sullivan notes, "Japan set out to rebuild itself as a land where everyone was equal."[201]

The American army of occupation would help drive the equalizing process, by breaking up Japan's massive rural estates and sharing the land with average farmers.[202] Japan's new lawmakers would do their part as well. They taxed the wealthy at stiff rates and stretched a well-knit safety net for the poor.[203] Even Japanese business leaders, prodded by labor and public opinion, made important contributions to a more equal Japan. Their companies offered workers lifetime job security. And Japanese banks, notes American economist Dean Baker, "were expected to extend loans to major employers, even those losing large amounts of money, to keep unemployment low."[204] All these steps, taken together, created a society with no "exclusive Beverly Hills or desperate Bronx slums."[205]

This equality would help nurture an incredibly productive society. In the 1970s and 1980s, Japanese enterprises won world-wide reputations for quality and efficiency. Japanese products captured growing shares of one global product market after another, in everything from stereos to motorcycles. Year by year, exports rushed out of Japan at ever faster rates. Japan's trade surpluses mounted, as did the value of the Japanese yen. Interest rates, meanwhile, dropped to the developed world's lowest levels. The nation's bankers could hardly believe their good fortune.

"Japanese banks overflowed with money," writes economist William Stewart, "much more than they could accommodate by relending in Japan itself."[206]

Bankers, in other words, had "money to burn," and, in the late 1980s, this money did what money to burn always does: ignite a wild speculative fire. In Japan, that fire raged from 1986 into 1991 and ended with a substantial collapse in real estate and stock market prices. Banks were suddenly left holding portfolios thick with burnt-out investments.

Japan's economy spent the rest of the 1990s trying to recover. Shares on the Japanese stock exchange never did. They lagged the entire decade — at the same time share values in the United States were soaring. What was Japan's problem? Smug American corporate leaders felt they knew exactly what was wrong. Japan had become too equal. The Japanese, American business observers asserted, needed to wake up to modern global realities. They couldn't possibly "continue to subsidize the poor through a 50 percent income tax on wealthy citizens" and expect to grow their economy. Japan needed to realize, once and for all, that a 70 percent tax on inherited wealth represents "outdated and excessive government interference" on the incentive to invest.[207]

"Nothing in America or Europe matches the rot in the state of Japan," echoed an editorial in the British *Economist.* Japan "needs to make the difficult choices that will bring efficiency and long-term growth." And that meant privatizing public services and deregulating businesses.[208] Many high-ranking Japanese office-holders would agree with this diagnosis. Japan, they concluded, could no longer afford equality.

"It's difficult for a government official to advocate income inequality," acknowledged Kenji Umetani, a director in Japan's economic planning agency. "But when we are designing the future structure of the Japanese economy, we have to make some adjustments to the existing structure that will necessitate an acceptance among Japanese people of greater income dispersion."[209]

Early in the twenty-first century, Japan's new prime minister, Junichiro Koizumi, would set about to make these adjustments. He would encourage Japanese corporations to downsize, just like American corporations. He would applaud policy moves that promoted "wage restraint" and kept job growth depressed.[210] Business leaders exulted.

"In seven or eight years," predicted Shoji Hiraide, the general manager of one of Tokyo's grandest department stores, "Japanese society will look much more like Western society, with gaps between rich and poor that can be clearly seen."[211]

That prospect left the people of Japan singularly uneasy. Some Japanese business executives might be upset "about the tiny gap" between their pay and the pay of their employees," noted Hiromitsu Ishi, a Japanese university president, "but most Japanese people like the notion of a not-so-uneven income distribution."[212]

The Japanese people had reason to appreciate their nation's unusually equitable income distribution. Equality had been good to average families in Japan, even during the "crisis" years of the 1990s. Joblessness in Japan, the *National Catholic Reporter*'s John Cort would note in 1998, had increased over the decade, but, at 4.3 percent, still stood lower than joblessness in the "booming" United States. And Japanese workers earned more than their American counterparts, 17.7 percent more for factory work.[213]

"Japan's problems," agreed Ezra Vogel, the director of Harvard University's Asia Center, "have been grossly exaggerated." Most Japanese "are happy with their quality of life, which includes a low crime rate, low unemployment and excellent schools."[214]

But what about Japan's stagnant stock market? What about the economic "crisis" that Prime Minister Koizumi insisted could only be fixed by adopting America's Wall Street model? That "crisis," observers like John Cort charged, impacted "mainly the rich and those who aspire to be rich."[215] Average Japanese faced no crisis. In the 1990s, they held their own.

Japanese elites did not. On the global stage, they lost ground. In the 1990s, top Japanese executives watched their American counterparts take home paychecks that tripled — and then tripled again — executive paychecks in Japan. Prime Minister Koizumi promised relief for these frustrated Japanese corporate leaders. He would force a break with hide-bound Japanese traditions. He would totally overhaul Japan's "crisis"-ridden economy.[216] Or so he pledged. But Koizumi would fall short. By 2003, his efforts to engineer a seachange in Japan's economy had failed. Japan would not swallow the Wall Street model. The Japanese people would taste Wall Street's medicine and spit it out.

In growing inequality, average Japanese people sensed a threat to their economic well-being. But they sensed other dangers as well. And they were right to worry. Unequal societies pay a price that can't always be measured in mere dollars and cents and yen. To these costs we now turn.