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Green New Deal Funding: Remember Finance is a Public-Private Franchise, Not a Big Broker in the Sky

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It is common to hear people claim or assume that finance is about 'intermediation,' a matter of channeling scarce funds from virtuous private savers to needful end-users. The picture behind this assertion is that of a gargantuan private broker – the financial system as massive 'go-between.' But modern financial systems are much more about credit-*generation* than *intermediation*, and they are more public than private. Funds, moreover, are anything but scarce – that's why we have bubbles and busts.

We need a new metaphor.

In my view and that of one of my frequent collaborators, a modern financial system is best modeled as a public-private franchise arrangement. The franchisor is the sovereign public, acting through its central bank or monetary authority. The franchised good is the monetized full faith and credit of the sovereign – its 'money.' And the franchisees are those private sector institutions that are licensed by the public to dispense, in the form of currency-denominated spendable credit, the franchised good.

Like any good franchisor, a public acting through its central bank or monetary authority acts to maintain the 'quality' of the good that its franchisees distribute. In the contemporary 'developed' world, the quality in question has been understood primarily in terms of over-issuance. The central bank's task has been understood in modulatory (rather than allocative) terms, the primary objective

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being to prevent consumer and, in some enlightened jurisdictions, asset price inflations and hyperinflations.

Two conceptual errors, one of them partly corrected since 2008, the other one not, seem to have hampered the 'quality control' efficacy of many central banks and monetary authorities – particularly that of the U.S., the Fed – in the pre-2008 period.

The first error was the tendency to think of 'inflation' as a disease only of consumer goods and services markets but not commodity or financial asset markets. Hence pundits, politicians, and even some central bankers crowed of a 'great moderation' featuring 30 years' low consumer price inflation even as asset and many commodity prices rocketed to previously unimagined heights. The crash was the consequence.

The second error was to think the financial system's modulatory and allocative challenges mutually orthogonal, such that the former might be handled through leverage-regulatory, liquidity-regulatory, and traditional monetary policy instruments wielded by the franchisor through its central bank, even while leaving credit-allocative functions primarily if not entirely to privately owned franchisee institutions.

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While the first error has come to be more or less widely acknowledged since the crash of 2008, finding expression in a 'macroprudential turn' on the part of central banks and coordinate financial regulators, the second error seems to have remained overlooked. But the hard truth is that without affirmative effort to channel finance capital to the 'real' sectors of the economy, glutting toward the financial sectors is all but inevitable, rendering the modulatory task all but impossible.

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Good modulation requires good allocation.

The reason for this, in turn, is that modern macro-economies are beset by multiple collective action problems, many of them recursive, in the financial and 'real' sectors alike. Solution of collective action problems requires well-conceived and well-targeted exercises of collective agency – the things sovereigns and franchisors do. Our federal government is simply our most inclusive collective agent.

Much of my academic and policy work is devoted both to elaborating and substantiating the foregoing claims and to designing means of addressing the problems they highlight. Where finance is concerned, the latter accordingly are means of bringing the public back into allocation in ways that don't *arbitrarily* 'pick winners and losers.'

In theory, the means to which I allude could be adopted by central banks themselves, in effect bringing-in politics-implicating functionalities without thereby having to implicate or exacerbate partisan divisions. In the US context, however, institutional history and 'path-dependence' suggest that a new public instrumentality, operationally situated between the Fed and the Treasury, probably would be the simplest way to put allocation at the service of modulation, thereby completing the job of what might be called 'deep' financial reform shown to be necessary by 2008.

One possibility would be to establish what my collaborator and I call a National Investment Authority (NIA), which, as the foregoing should indicate, is rather more than a mere 'investment-' or 'infrastructure-bank.' It would optimally bridge fiscal and monetary policy, in a division of labor apportioning more 'purely' political allocative questions to the former, more technical modulatory questions to the latter, and more neutral allocative questions, sounding in solutions to collective action problems, to the new institution.

This is anything but an 'alien' idea where America's public-private franchise form of finance is concerned. To the contrary, it amounts to a *restoration*.

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Alexander Hamilton's first Bank of the United States combined central banking and development finance functions in distinct departments of one institution during the first years of our republic. His successor Albert Gallatin's second Bank of the US did the same on a yet larger scale. Scarce wonder that these two visionaries' statues stand on either side of the Treasury Department in

Washington, or that their remains rest similarly in the south and north cemeteries, respectively, of historic Trinity Church in lower Manhattan.

Closer to the present, the War Finance Corporation ('WFC') of the First World War era, then Herbert Hoover's and Franklin Roosevelt's Reconstruction Finance Corporation ('RFC') of the New Deal and Second World eras mobilized public and private capital alike in the cause first of rebuilding, then of massively multiplying, the nation's infrastructural and manufacturing capacities.

In its day, the RFC was by far the largest financial institution in the world, rightfully dwarfing all Wall Street banks. It made investments as small as $20 loans to African American barbershops in Los Angeles and as large as the multimillion-dollar infrastructure projects for which the New Deal is renowned to this day. The RFC also financed projects in every Congressional district in the country and always operated 'in the black,' plowing the returns on its investments back into yet further investments.

The RFC's 'virtuous circle' of investment, profit, and reinvestment was the balance sheet equivalent of America's economy itself during this historic high-growth period of our national history. And as history tends to rhyme, if not to repeat, I suspect we shall be seeing an RFC-descendant, like the aforementioned NIA, playing a critical role in the Green New Deal now ahead of us. For the Green New Deal too will fund projects in literally every precinct of the country, in the names of both justice and democracy. And it will mobilize public and private capital alike in the cause just like its predecessor did.

As the work I've just referenced shows, this will be good not only for the Green New Deal mobilization, but for our nation's financial system as well.

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Group of dollar bills background. GETTY

It will restore our sovereign citizenry – our financial system's ultimate 'franchisor' – to its proper role at the head of that system. *Our Green New Deal, in short,* will proceed on the strength of our *finance*.

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