

Jon Emaldi Abasolo

BANKING AND FINANCIAL CRISES

Can a never-ending story change?

1630
1720
1929
1987
2000
2007



Desclée De Brouwer

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To my family

I will only mention the closest, beginning with Ane, the driving force of a project which includes Garazi, Julen, Iur, Arrate, David, Irati and fairly soon another newcomer. Also closest are Maria Dolores, Mikel, Borja, Eli, Aitor, Ana, Iker, Argizka, Ander, Ane Maite, Oscar, Miren, Jorge, Mariló and Juanma. And those who are with us, but not present, Ane's father, Jaime, and my parents, Maite and Jon.

A short list in a big family is not that short, I'm afraid.

I must also thank Joseba Madariaga, who enrolled me in DBS and has encouraged once and again the approach I follow in this book. And Josu Irigoyen, my boss in the Studies Department of Caja Laboral, where I learned to investigate off the beaten track.

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Foreword

Jon Emaldi was born in Portugalete (Bizkaia) in 1959. Married to Ane Pereira, his colleague and best friend from university times. They have two daughters, two sons-in-law and two young grandchildren.

A cooperativist at heart, during his university degree in Business Administration his first contact with cooperativism was a course on Basque Cooperativism in University of Deusto's Sociology faculty. He began his career in the International Studies Department of Leeds Polytechnic, now Leeds Metropolitan University. With the help of Maria Moissa, a highly motivating professor in Leeds Poly, he got to know the British Coop, including a visit in 1982 to Rochdale in Manchester. Soon after his pilgrimage to the birthplace of the modern cooperative movement, he began his long career in LABORAL kutxa, the cooperative bank of the MONDRAGON Group: he joined Caja Laboral –now LABORAL kutxa– in 1983. He has been working there in different fields of the banking industry, from marketing to strategy, from retail network to quality management.

This text aims to be an educational book. Its first target is to provide a textbook to his students of Finance at Deusto Business School–DBS, trying to transmit a critical view on the explanations usually given about the recurring crises, and by doing so he follows the thesis of some great economists, past and present, like John Kenneth Galbraith or Carmen Reinhart, who concluded that the real causes of financial and banking crises seldom appear. In most episodes, partakers, policymakers, regulators, and investors large and small, feel more at ease sharing explanations, or justifications, which could be grouped under the label of the “*This-Time-Is-Different*” syndrome, as Carmen Reinhart and her co-author Kenneth Rogoff have very convincingly shown.

Carmen M Reinhart, at present Vice President and Chief Economist of the World Bank Group, has grown strong roots in Basque soil. She was invested Doctor Honoris Causa in Economics at Euskal Herriko Unibertsitatea –the Basque Public University– in 2012. Her roots in the Basque Country are not rhetorical, as she has planted in the *arboretum* of the University a sprout

of the *Tree of Gernika*, the main symbol of Basque traditions and values. Those traditional values are *freedom, and solidarity and defence of the people next-door* while at the same time *openness to the world at large. Ethics of work well done* as well. Together with sound and healthy *scepticism*, not bad ingredients to work on controlling economic bubbles and manias.

1

The Crises of the Past

“Any history of the classical tradition in economics must, after considering the essential ideas, examine the way it was defended. There is, to be sure, a defense implicit in the explanation of the system itself; economic theory combines interpretation with justification” (Galbraith 1991, 113).

1.1. The stylized facts on financial crises according to Galbraith

The term *stylized facts* was introduced by Nikolas Kaldor in 1961, on a debate about economic growth theory. He understood that theory should begin with a summary of the most relevant facts. Kaldor said that economists should be free to start off with a simplified view of the facts and concentrate on tendencies, ignoring individual detail. *Stylized facts* in economics are conclusions based on empirical findings. Most of these facts come from statistical calculations. Their interpretation is that coming from *hard facts*, they are also “*hard*” basis for generalizations. They face problems though: even getting to the essence, many times they contain inaccuracies or even mistakes. Well renowned economist question whether they are facts at all, but in order to extract operative conclusions, or lessons from the past, they are effective enough.

On *Financial Euphoria*, Galbraith concludes in 1990 that “...*recurrent lapses into financial dementia have not changed in any truly operative fashion since the Tulipomania of 1636 – 1637*” (Galbraith 1994, 106). Stylized facts he stresses, and we extract, are the following:

1. Financial disaster is quickly forgotten.
 - Faith in the inherent knowledge of the market itself.
 - It all begins with a brilliant innovative discovery. A desirable innovation.