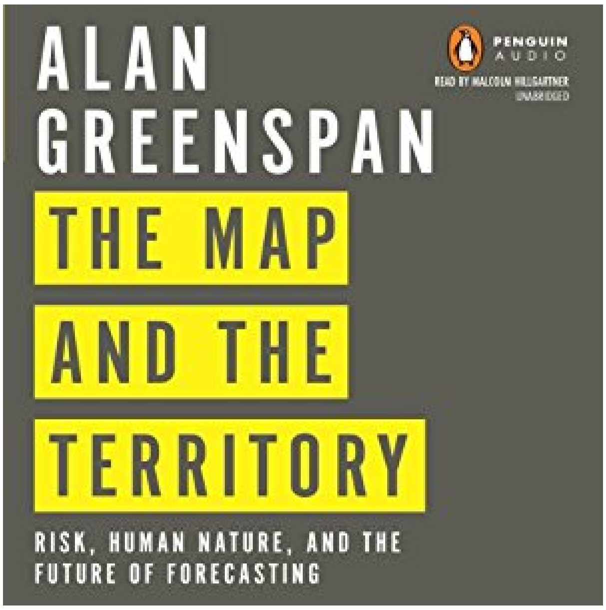
The Map And The Territory: Risk, Human Nature, And The Future Of Forecasting



Synopsis

Like all of us, though few so visibly, Alan Greenspan was forced by the financial crisis of 2008 to question some fundamental assumptions about risk management and economic forecasting. No one with any meaningful role in economic decision making in the world saw beforehand the storm for what it was. How had our models so utterly failed us? To answer this question, Alan Greenspan embarked on a rigorous and far-reaching multiyear examination of how Homo economicus predicts the economic future, and how it can predict it better. Economic risk is a fact of life in every realm, from home to business to government at all levels. Whether we're conscious of it or not, we make wagers on the future virtually every day, one way or another. Very often, however, we're steering by out-of-date maps, when we're not driven by factors entirely beyond our conscious control. The Map and the Territory is nothing less than an effort to update our forecasting conceptual grid using twenty-first-century technologies. It integrates the history of economic prediction, the new work of behavioral economists, and the fruits of the author's own remarkable career to offer a thrillingly lucid and empirically based grounding in what we can know about economic forecasting and what we can't. The audiobook explores how culture is and isn't destiny and probes what we can predict about the world's biggest looming challenges, from debt and the reform of the welfare state to our competition with China to natural disasters in an age of global warming. No map is the territory, but Greenspan's approach, grounded in his trademark rigor, wisdom, and unprecedented context, ensures that this particular map will assist in safe journeys down many different roads, traveled by individuals, businesses, and the state.

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Customer Reviews

"The Map and the Territory" is a string of loosely connected musings about the economy, economic forecasting, and the impact of the financial crisis. If you have read an economics book in the last 10 years, you will not find much new here. The jacket advertises the book as the result of "a rigorous and far-reaching multiyear examination of how Homo economicus predicts the economic future, and how it can predict it better." I am not convinced that is true. The book is simply too generalized and disjointed to be influential in any sense.Greenspan touches on a number of topics, but there are better books on each subject. For example, his discussion of how growth in government benefits has crowded out private savings is the better handled in Edgar Browning's, "Stealing From Each Other." Acharya and Richardson's "Restoring Financial Stability" and "Regulating Wall Street" are still the best books on the financial crisis and how to prevent another. I expect "The Map and the Territory" to sell wildly, but most readers will find that it does not live up to the hype. Greenspan most likely has very interesting things to write, but sadly he has not produced them here.

The most obvious lesson for aware readers is that Greenspan is among the luckiest apple-polishers in US history. Greenspan claims to be an advocate of global free markets and economic meritocracies driven by minimally regulated private sector enterprise; supporting that belief is widespread agreement that Greenspan's most notable "successes" are saving US finance in 1987, and the Clinton years. As with many political figures, facts on file do not match their memories. The Crash of '87 was the market response to uncertainties caused by five years of debt-fueled federal binge spending and speculation in high risk securities. Greenspan's response was Keynesian; he pumped as much public money into the market as it took to maintain the facade of integrity in finance. By 1987 politicians had redefined financial services from necessary parasites to the foundation for all that is good about America. By the end of 1988 well-employed Americans lived falsely optimistic lives in a false economy propped up by massive public debt. The people Greenspan needed to please were pleased, and so politicians and the corporate welfare classes tended to grade Greenspan's performance in the range A+++ to A++. A different parallel reality tended to be unacknowledged. The middle class was shrinking as the quality of jobs declined. Risks to taxpayers increased as the quality of securities declined and government debt exploded. Still, Greenspan apparently felt the transfer of wealth from middle class consumers to parasitic financial services industries needed more accelerant, so The Maestro continued to weaken quality constraints on credit and debt claiming rational markets would check financial avarice. The direct result was that after 1987 inflation moved from shopping baskets to assets, a class of goods not typically covered in month-to-month inflation measures, and which could therefore be allowed to continue unremarked by most "experts" in the art of economics. Massive asset inflation after 1987 provided the pretend security for the real leverage that fueled the doubtful boom of the 1990s which set the stage for the housing bubble that followed. As happened in the 1980s when the federal debt binge combined with loosened shackles on financial avarice to create a feel-good economy, the 1990s boom was built on private debt, asset inflation and even fewer shackles on financial avarice to create a feel-good economy. 'The 1980s and 1990s economies felt real, our jigged measures show growth, so it was real,' remains the position of most "experts" trained in finance and economics. The 1990s boom is The Maestro's second widely proclaimed triumph. That The Maestro ignored history and real time lessons of the dot.com bubble didn't surprise sentient Greenspan Watchers. There is an argument for the belief that the lessons of the dot.com bust - speculators can lose money on Wall Street - do not transfer well to the housing bubble and bust. Because of the obviously larger implications to the nation's financial infrastructure, there is no argument supporting Greenspan's failure to address the risks of the speculator-driven housing bubble that put at risk most of the assets of millions of citizens. The traits that appear to define Greenspan are 'self-serving' and 'hypocrite'. No senior official in US history advocated keeping government out of the economy more frequently, but through the end of his eighteen year tenure at the FED no official in US history intervened in private enterprise to the extent Greenspan did. No senior official in US history survived a similar number of years talking one set of values while practicing a polar opposite set of values to cover the damage caused by their public views. The Maestro's career is a testament to sycophancy to political power regardless of costs to the nation. But I digress... Back to the book: buy it if you are a dyed in the wool fake-conservative seeking bathroom reading defending pillar to post thinking and reactionary management. People with math and logic skills sufficient to overcome their worst political instincts can also use this book in their bathrooms, but there are more comfortable and lower cost alternatives.

I read this book from the perspective of an investor who specializes in real estate investment trusts (REITS). I was a REIT investor in 2008 when the economy failed, as I am today. I was near the financial center of the financial collapse of 2008 and able to observe it closely as it unfolded. Earlier in my career I worked as an IT company owner who studied the progress of business in the USA and globally by observing my client companies' businesses through the computer systems I developed.Thus, I have a close up view of the financial collapse and a broad-based view of the real world economy that underpins it. This perspective has made me a successful investor. But I do confess to having been blindsided by the 2008 collapse, as Mr. Greenspan and most professional economists were. This book explains Mr. Greenspan's opinion as to why so many professional economists were caught napping during the Great Recession that began in 2008 and casts its long shadow over the economy today and for years to come.Mr. Greenspan gets right to the heart of the question:=====On the face of it, the financial crisis also represented an existential crisis for economic forecasting. I began my postcrisis investigations, culminating in this book, in an effort to understand how we all got it so wrong, and what we can learn from the fact that we did..... What went wrong? Why was virtually every economist and policy maker of note so off about so large an issue?=====Mr. Greenspan begins to answer the question with with an essay on investor psychology, popularly known as "animal spirits" that delves into the psychological reasons why investors may commit or withhold their capital from the economy. That is followed by a chapter on banking regulation. Then there is a discussion on statistical analysis followed by a rambling chapter on THE ROOTS OF THE ECONOMIC CRISIS:=====The toxic securitized U.S. subprime mortgages were the immediate trigger of the financial crisis, but the origins of the crisis reach back to the aftermath of the Cold War. The fall of the Berlin Wall in 1989 exposed the economic ruin produced by the Soviet bloc's economic system.=====Mr. Greenspan then proceeds to explain his theory of why the recovery remains so tepid five years later:=====That business had become markedly averse to investment in fixed long-term assets appears indisputable. The critical question is why? Although most in the business community attribute the massive rise in their fear and uncertainty to the collapse of economic activity, many judge its continuance since the recovery took hold in early 2009 largely to be the result of widespread government activism in its all-embracing attempt to accelerate the path of economic recovery and regulate finance. The evidence tends to largely support the latter judgments.=====And yet it's curious why the stock market crashed and the economy failed in 2008 during an era of business-friendly governments (i.e. the Clinton Administration and the Conservative Republican Congress followed by President Bush whom I voted for twice).During the 11.5 years between August 5, 1997 (the date of the first tax cut) to January 1, 2009 --- while taxes were cut to 80-year lows and numerous free trade agreements were enacted --- the S&P500 fell from 952 to 825, losing 13% of its value in non-inflation adjusted terms and 34% when adjusted for inflation.I would postulate that the economy failed in 1998 through 2008 for reasons unknown to theoretical economists like Mr. Greenspan who perhaps don't have direct experience with the real world economy of factories, offices, stores, and property:1. Beginning in the late 1980s the consumption side of the economy was stunted by massive dis-employment of the American workforce. The job losses were due to combinations of factors including globalization that allowed jobs to be relocated overseas; by consolidations of employment in mergers and acquisitions; by improvements in machine technology and automation; and by work force reductions that replaced many senior career people with hourly contract workers.2. These millions of Americans were removed from the labor force for reasons that might be considered to be good or bad, necessary or unnecessary, depending on one's point of view. An entire vocabulary of euphemistic terms like "rightsizing, downsizing, offshoring, outsourcing, early retirement, work force reductions, reengineering" was invented to explain the dis-employment phenomenon. Labor force participation peaked in 1999.3. In order to fight rising unemployment Alan Greenspan lowered interest rates, believing that lower rates would boost corporate cash flows by allowing corporations to refinance their debt. The increased cash flows were supposed to encourage American companies to invest in expanding their businesses and hiring more American workers. President Bush also asked Congress to cut income taxes on capital gains and dividends to further boost business cash flow under the theory that it would be reinvested in growing the business.4. Lowering interest rates and cutting taxes failed to grow the economy (in contrast to the success of these policies in reviving the economy during Reagan's years) because by 2000 many American companies were moving production overseas and hiring foreign labor to replace American workers.5. Consumer demand slackened due to the falling incomes of those put out of work or afflicted with falling wages.6. With consumer demand falling, investors could not profit by investing in expanding production of goods and services. So, instead of creating real wealth by building factories that hire employees to produce goods and services, capital became disproportionately invested into real estate and leveraged real estate derivatives like collateralized debt obligations (CDOs) and credit default swaps (CDS).7. By the summer of 2007 the accumulation of job losses from layoffs and involuntary retirements made it impossible for large numbers of people to pay the mortgages on their homes.8. When homeowners defaulted on their mortgages due to job losses, the leveraged CDO and CDS derivatives became defunct. The CDO's and CDS's had puffed up the asset ledgers of the banks. When they became worthless the banks discovered that they had more liabilities on their books than assets.9. The banks became insolvent and the stock market crashed. Business stopped dead in its tracks. The injection of several trillion dollars of printed/borrowed paper money by the government resuscitated the economy. Without that infusion many more banks and businesses might have failed, further escalating unemployment.10. Five years later the jobs-creating side of the economy remains sluggish even though corporate profits are soaring as are the stocks of publicly traded companies. Is employment sluggish because:----- A) Business won't invest in creating jobs because it is afraid of the allegedly "anti-business" policies of President Obama.----- B) Business isn't creating enough new jobs due to offshoring of jobs formerly done in the USA, redundancies created by mergers and acquisitions, improvements in technology, and early retirements.Mr. Greenspan view is through a political lens requiring him to accept theory A). But perhaps theory B) is also entitled to due consideration.

I expected Alan Greenspan's years of experience and wisdom to come together in some kind of "ah ha" moment. This is really just a compilation of economics and statistical vignettes. Lots of interesting stuff, but no real message in conclusion.

3 stars mainly for the effort, as I found the book largeley disappointing. Mr. Greenspan tries - but fails - to justify his mistakes with the fact that "no-one knew" what was going to happen. Fair enoguh, but that's not an issue worth writing a book about, especially so when the author's primary interest is pointing the finger of blame somewhere else.

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