

## Trust versus Contract as a means of securing the implementation of Value Transfers

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**As the Financial Services industry discovered in 2008, when push comes to shove, contractual agreements cease to be worth the paper on which they are written, above all because of the evaporation of mutual trust. Can this alarming source of financial risk be remedied? And if so, how?**

*The ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood. Indeed the world is ruled by little else. Practical men, who believe themselves to be quite exempt from any intellectual influence, are usually the slaves of some defunct economist. Madmen in authority, who hear voices in the air, are distilling their frenzy from some academic scribbler of a few years back. I am sure that the power of vested interests is vastly exaggerated compared with the gradual encroachment of ideas. J.M. Keynes, *The General Theory of Employment, Interest, and Money**

**T**ransactions are a key feature of every social order, they have routinely facilitated the redistribution of goods and services on mutually acceptable basis – no less in the past than in the monetised present, now that an ever growing proportion of financial transactions have no physical substance, other than in the form of packets of data swirling round the globe through thousands of miles of glass fibre. But even if the bulk of value transfers are by now implemented on an ethereal rather a physical basis, such that debts can be settled with a blink of an eye, the discipline of economics – or rather the underlying premises of that discipline – remain largely untouched. Moreover there is a strong sense in which the roots of these premises can be traced back to Hobbes’ *Leviathan*, in which he set out an idealised model of necessary foundations of a stable socio-economic order, further supplemented a century later by Adam Smith’s vision of the ‘invisible hand’ which

he articulated *The Wealth of Nations*, so much their theses are routinely highlighted in the initial phase of Economics 101.

Hobbes' key hypothesis was that prior to the emergence of civilization mankind lived in a 'state of nature' which was as primordial as it was anarchic, given the variability of human desires, together with the need compete for scarce resources to fulfil those desires. This would of necessity have led to the social order – to the extent that it existed at all – to manifest itself as a condition 'war of all against all', in which

Even when two men are not fighting, there is no guarantee that the other will not try to kill him for his property or just out of an aggrieved sense of honour, and so they must constantly be on guard against one another. It is even reasonable to pre-emptively attack one's neighbour. In such condition there is no place for industry, because the fruit thereof is uncertain, and consequently, not culture of the earth, no navigation, nor the use of commodities that may be imported by sea, no commodious building, no instruments of moving and removing such things as require much force, no knowledge of the face of the earth, no account of time, no arts, no letters, no society, and which is worst of all, continual fear and danger of violent death, and the life of man, solitary, poor, nasty, brutish, and short. (Hobbes: XIII, 9)

From this perspective it followed that the life in the primordial state of nature and that in man-made states of civilization were the antithesis of one another. The context within which he articulated this thesis is worth noting: the immediate aftermath of England's bloody civil war. Against that background Hobbes was arguing that such a war of all against all was – or at least should be – a thing of the past, even though England had recently gone through, and managed to survive, just such a bloody exercise. Hence his arguments the Leviathan were closely related to the politics of the period, in which – amongst other things – he was challenging the premises of the Levellers, an egalitarian and hence strongly antinomian movement which had attracted a wide following during the course of the civil war. To counter their arguments Hobbes argued that the primordial of laws of nature could in no sense be properly identified as "laws", for in an absence of hierarchy, no-one was in a position to enforce them. As such he was seeking to fire a sharp shot across the bows of the Levellers, even though he comprehensively traduced key elements of their premises.

Nevertheless he did so with purpose, for even though support for the Levellers was waning his aim was to hit them below the waterline. If his hypothetical assumption that in the primordial state of nature there could be no

distinction between just and unjust, on the grounds that this was bound to be the case when everyone was considered to have a right to access all available potential resources (a careful misinterpretation of a key Leveller premise), then it followed the first and most vital step in the direction of civilization would of necessity be rooted in a denial of such premises, which would be replaced by a systematic willingness of individuals renounce their selfish rights of access to all things by brute force, in a context in which all others were prepared to – and ultimately required to – to abandon such claims. It also followed, so he argued, that once these premises were established, the *a priori* state of nature (and/or of civil war) could readily be replaced by cooperative but nevertheless hierarchically constructed Commonwealth, in the form of a systemically ordered but multi-layered Leviathan, in which a sovereign source of morally grounded authority exercised right, and indeed a duty, to command its subjects of to obey its man-made laws for the good of all concerned: in other words a resounding “No!” to the Levellers.

A century later Adam Smith took up re-cast these arguments these arguments in his equally influential arguments set out in *The Wealth of Nations* (1776), in which he went on to argue that

As every individual, therefore, endeavours as much as he can both to employ his capital in the support of domestic industry, and so to direct that industry that its produce may be of the greatest value; every individual necessarily labours to render the annual revenue of the society as great as he can. He generally, indeed, neither intends to promote the public interest, nor knows how much he is promoting it. By preferring the support of domestic to that of foreign industry, he intends only his own security; and by directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other cases, led by an invisible hand to promote an end which was no part of his intention. Nor is it always the worse for the society that it was no part of it. By pursuing his own interest he frequently promotes that of the society more effectually than when he really intends to promote it. I have never known much good done by those who affected to trade for the public good. It is an affectation, indeed, not very common among merchants, and very few words need be employed in dissuading them from it.

It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our own necessities but of their advantages. (Smith: 1776, I,2).

In many ways Smith was the founder of the discipline of Economics as we know it today. In his vision, the hierarchical nature of Hobbes' sovereign Leviathan has been almost completely discarded, and instead replaced by armies of individual mutually competitive profit seekers, be they butchers, brewers, or baker negotiating exchanges between themselves on a contractual basis. Within that context just two components of Leviathan remain in place. The first is concrete: namely the presence of a legal system to ensure that contractual agreements are enforced; the second can only be regarded as hypothetical, namely the 'invisible hand' which, he argues, routinely serves to restore equilibrium if and when there is a danger of the economic system running off the rails in an economic war of all against all.

Ever since Smith promulgated the assertion the markets of all kinds were routinely stabilised by virtue of this 'invisible hand', mathematically minded neo-classicist economists have been struggling to provide equations to explain the operation of 'invisible hand', as well as the calculation of risk, in mathematical terms. Despite numerous Nobel Prizes, their efforts appear to have had little success, as boom has repeatedly replaced by an even bigger bust, following an exponential patterns of growth during the course of the past two centuries. Could it be that Smith's invisible hands which he found he had to posit to guarantee the stability of vision of free-market economic order which he envisaged were merely a mirage? I would also add that if Smith had been more of an engineer than a theorist, and if he had therefore aware of the challenges of those building steam engines – which to be fair only really began several decades after the Wealth of Nations was published – he would have also been aware that that in the absence of mechanical regulators, steam engines could all too easily run faster and faster and faster until they exploded.

Since then built-in negative feedback mechanisms, which automatically reduce the power when the system begins to run too fast, and to increase it when the system runs too slowly, have been the order of the day in all known fields of mechanical, electrical and electronic engineering. But if all stable physical systems, whether natural or man-made, invariably include negative feedback mechanisms within themselves, such that they can restore themselves to a position of equilibrium as and when they find themselves subject to external shocks, how far – and above all how effectively – have economic theorists, and perhaps more importantly those who have built and run the contemporary global financial structure – managed to incorporate anything more reliable than the fictitious 'invisible hand' to ensure that an appropriate state of economic, as opposed to electronic, equilibrium is maintained within one of one of the largest man-made systemic structures which has ever been

constructed: a global financial system which runs on a 24/7/365 basis, and which is consequently the foundation of our socio-economic order.

### **Hobbes, Adam Smith, and the foundational premises of modern economics**

**G**iven that we owe our concept of the invisible hand to Adam Smith, it is worth going back to explore the premises on which he relied in constructing this concept. In doing so, we have to turn to an earlier publication, *The Theory of Moral Sentiments*, which begins with a dramatic proclamation to the effect that:

How selfish soever man may be supposed, there are evidently some principles in his nature, which interest him in the fortunes of others, and render their happiness necessary to him, though he derives nothing from it, except the pleasure of seeing it. Of this kind is pity or compassion, the emotion we feel for the misery of others, when we either see it, or are made to conceive it in a very lively manner. That we often derive sorrow from the sorrows of others, is a matter of fact too obvious to require any instances to prove it; for this sentiment, like all the other original passions of human nature, is by no means confined to the virtuous or the humane, though they perhaps may feel it with the most exquisite sensibility. The greatest ruffian, the most hardened violator of the laws of society, is not altogether without it (Smith: 1759)

In doing so Smith is arguing, contra Hobbes, that a sense of morality is an intrinsic dimension of the human condition, even if other original passions of human nature, is by no means confined to the virtuous or the humane. But even though he explicitly allows for such a possibility, he also acknowledges, with Hobbes, the powerful consequences of mutual competition. Hence he goes on to acknowledge that:

[Nevertheless] the rich only select from the heap what is most precious and agreeable. They consume little more than the poor, and in spite of their natural selfishness and rapacity, though they mean only their own conveniency, though the sole end which they propose from the labours of all the thousands whom they employ, be the gratification of their own vain and insatiable desires, they divide with the poor the produce of all their improvements. They are led by *an invisible hand* to make nearly the same distribution of the necessaries of life, which would have been made, had the earth been divided into equal portions among all its inhabitants, and thus without intending it, without knowing it,

advance the interest of the society, and afford means to the multiplication of the species (Smith: *ibid*)

The precise source of this invisible hand remains obscure. Nevertheless the concept subsequently appears in a much more powerful role in *The Wealth of Nations*, especially in the citation above, that even when someone engages in an economic transaction

by directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain, he is in this, as in many other cases, led by an *invisible hand* to promote an end which was no part of his intention.

In doing so he has still not defined either the nature or the effectiveness of the invisible hand, despite the key role it plays in his exegesis, as well as by those of the multitude of economists who followed in his footsteps. With such considerations in mind, in my view the most significant portion of the extract, on the basis which he justifies his own argument, on the grounds that his vision of the operation the invisible hand is

... an affectation, indeed, not very common among merchants, and very few words need be employed in dissuading them from it.

In other words Smith confirmed his concept on nominally empirical grounds, at least in the sense that merchants whom he consulted about the matter agreed that at least in their neck of the woods, the equilibrium of which he talked for them a matter of experience. However in doing so the very founder of modern economics failed to go one step further, by conducting an empirical exploration its source. Had he (or his successors) done so, they might well have been able to detect the presence of some process of negative feedback entrenched in their transactions, such that he – or they – could do away with the fictive concept of invisible hands.

However before doing so we must also consider a further key dimension of the premises on which both Hobbes and Smith based their systemic models, namely the state of play prior to the emergence of the civilizational order in the midst of which they found themselves. For Hobbes, the key to his vision of the Leviathan was that prior to the emergence of institutions of this sort, the condition of humanity was *ipso facto* in a condition of war of all against all. Smith also appears to have adopted much the same view of the *a priori* condition of mankind, but which he qualifies by inserting a process of differentiation – namely the division of labour – into the equation. As he goes on to observe:

Nobody but a beggar chooses to depend chiefly upon the benevolence of his fellow-citizens. Even a beggar does not depend upon it entirely. The greater part of his occasional wants are supplied in the same manner as those of other people, by treaty, by barter, and by purchase. With the money which one man

gives him he purchases food. The old clothes which another bestows upon him he exchanges for other old clothes which suit him better, or for lodging, or for food, or for money, with which he can buy either food, clothes, or lodging, as he has occasion.

The difference of natural talents in different men is, in reality, much less than we are aware of; and the very different genius which appears to distinguish men of different professions, when grown up to maturity, is not upon many occasions so much the cause as the effect of the division of labour. The difference between the most dissimilar characters, between a philosopher and a common street porter, for example, seems to arise not so much from nature as from habit, custom, and education.

When they came into the world, and for the first six or eight years of their existence, they were perhaps very much alike, and neither their parents nor playfellows could perceive any remarkable difference. About that age, or soon after, they come to be employed in very different occupations. The difference of talents comes then to be taken notice of, and widens by degrees, till at last the vanity of the philosopher is willing to acknowledge scarce any resemblance.

But without the disposition to truck, barter, and exchange, every man must have procured *to himself* every necessary and conveniency of life which he wanted. All must have had the same duties to perform, and the same work to do, and there could have been no such difference of employment as could alone give occasion to any great difference of talents.

As it is this disposition which forms that difference of talents, so remarkable among men of different professions, so it is this same disposition which renders that difference useful. Many tribes of animals acknowledged to be all of the same species derive from nature a distinct genius, which, antecedent to custom and education, also takes place among men. By nature a philosopher is not in genius and disposition half so different from a street porter, as a mastiff is from a greyhound, or a greyhound from a spaniel, or this last from a shepherd's dog. Those different tribes of animals, however, though all of the same species, are of scarce any use to one another. The strength of the mastiff is not, in the least, supported either by the swiftness of the greyhound, or by the sagacity of the spaniel, or by the docility of the shepherd's dog.

The effects of those different geniuses and talents, for want of the power or disposition to barter and exchange, cannot be brought into a common stock, and do not in the least contribute to the better accommodation in conveniency to the species. Each animal is still obliged to support and defend itself, separately and independently, and derives no sort of advantage from that variety of talents with which nature has distinguished its fellows.

Among men, on the contrary, the most dissimilar geniuses are of use to one another; the different produces of their respective talents, by the general disposition to truck, barter, and exchange, being brought, as it were, into a common stock, where every man may purchase whatever part of the produce of other men's talents he has occasion for (Smith: 1776, I,2).

In so arguing, uses the homogenous status natural childhood rather than that of natural primitivity as his starting point, such that he can go on to assert that the dual force custom and education are necessary prerequisite for the emergence of the division of labour, and hence 'the general disposition to truck, barter, and exchange, being brought, as it were, into a common stock': in other words the rapid emergence of a free market economy with a monetary base.

### **The significance of networks of reciprocity**

**B**ut just how sound was this assumption? Was it really the case that prior to the emergence of monetised exchanges between autonomous individuals (a further key aspect of his model) transactions were so severely hindered by the inflexibility of barter, such that socio-economic orders with which he was familiar – or at least he thought he was familiar, given the parameters of the model which he had constructed – automatically sprang into being, such that barbarity could at long last be replaced with civilisation? Or was the existence of primordial barter-only societies yet another convenient fiction, just like the invisible hand? The contemporary answer is quite clear. In her anthropological exploration of the phenomenon of barter, Caroline Humphries' conclusions could not have been more definitive

No example of a barter economy, pure and simple, has ever been described, let alone the emergence from it of money; all available ethnography suggests that there never has been such a thing. (Humphries 1992).

In his hugely illuminating analysis *Debt: The First Five Thousand Years*, Graeber goes on to outline the fruits of a huge range of ethnographic research which shows that way back into prehistory, as well as in the contemporary world, monetisation in the sense understood by Smith was in no sense a prerequisite for the implementation of complex transactions: what was far more important was relationships of mutual trust – and hence above all sense of mutual obligation – which would ensure that all debts would in due course be settled. Hence in such circumstances it was not so much either force or law which held the social order together, but debt. It is easy to see why: to be indebted to someone is to owe that person that person a favour of

some sort: in other words one is obliged to them, and one cannot refuse to offer a favour in return, always provided that one is in a position to do so. When such morally grounded debt-networks are in place, there is no need for barter: everything is available 'on tick'. Moreover when such networks are in place, no-one is ever free of debt, not because it is a burden, but rather because it is an asset: it provides an entrée to a morally grounded world of mutual exchange. Hence in such contexts no-one ever willingly settles all their debts: anyone who is debtless may indeed step out of the network may become autonomous, but in doing so he or she can no longer call on the resources of the social order – a highly undesirable position to be in. Hence most debts are *never* settled, such that when a favour is in due course returned, care is invariably taken to ensure that the lender is over-compensated, thereby promptly setting up a debt in the opposite direction.

But why do so? The answer should by now be clear: that by accruing obligations to others, and in due course by settling – better still by over-fulfilling – those debts, one gradually establishes an ever firmer position in the networks of right and obligations of which the social order is composed. Indeed that process starts with birth. From that very moment infants accrue an ever more extensive collection of debts to their parents, in return for the obligations which their parents had fulfilled in the course of bringing up their offspring; it also followed that in due course these debts would be paid off on a reciprocal basis as their parents become steadily more elderly, such that they in turn become increasingly dependent on their offspring.

Could there be a better means of implementing long-term life insurance on a mutual assurance? Nor were such networks of debt-reciprocity necessarily articulated through ties of kinship, although it goes without saying that they very often were. Nor were these networks intrinsically a matter of genetics, as evolutionary biologists regularly insist: in sharp contrast any of our predecessors, we humans have a unique capacity to create – and constantly to revise – the conceptual foundations of our own existence, and including, by definition, the social significance of kinship itself. Hence in social contexts in which networks of reciprocity are the order of the day, it is not so much our genetic heritages which lead to networks operating in this way, but rather a carefully structured morally grounded vision of give and take, and above of all of obligation and debt, which keeps the whole edifice of mutual reciprocity afloat. Moreover it is also one which incorporates its own highly effective feed-back mechanism to keep capsizes at bay.

Where such networks are in play, the worst fate which any participant in such networks of reciprocity can experience is permanent excommunication. In

practice such are rarely implemented, then only in extreme circumstances. The transgressions which lead to this ultimate sanction can vary enormously, but they typically in contexts when someone has recklessly built up huge debts to their counter-parties – which may be morally, physically or financially grounded, or a combination of all three – such that the person in question has betrayed his or her obligations to the entire network. In these circumstance that the ancient sanction of banishment is likely to come into force. Excommunication from the network is a highly effective Sword of Damocles, even if it is rarely deployed.

It follows, as innumerable ethnographic accounts confirmed, it is not so much genetics which secures the stability of such networks – even if kinship ties (as locally interpreted) provide convenient conceptual frameworks around which to construct them; rather what mattered much was more that there was a sufficient degree of mutual trust between contractors of all sorts to ensure that obligations would be respected, and hence that such debts would in due course settled, even when there was nothing in the form of a state to require that such transactions must be fulfilled as agreed. What these ethnographic accounts invariably confirm, however, is that banishment is ultimate sanction with which those who betray their obligations can expect to face: in words a highly effective source of negative feedback.

### **To what extent are foundations of modern economics fictitious in character**

All this is most alarming. Could it be that some of the key the conceptual premises on which provided the foundation of modern economics, and which – as Graeber points out – are still routinely recycled in virtually all contemporary textbooks, are entirely fictitious? Could it have been that the merchants in Edinburgh and Glasgow who Smith consulted had indeed constructed just such a coalition of reciprocity with their partners overseas? If so, their preferred methodology would certainly not have been unprecedented. Not that they were to not it at the time, but as Greif (1989, 1993) reported much more recently, his analysis of the records of Jewish traders engaged in operating long-distance trading networks along the southern shores of the Mediterranean in the 10<sup>th</sup> CE had concluded that the key to their success lay in their construction and use of what he described as trust-based ‘coalitions of reciprocity’ as means of settling their trading debts.

Of course Smith cannot be criticised for failing to take notice of Greif’s findings, which only came to light when he was able to gain access to the documents found in the Cairo Genizah two centuries later. Nevertheless if I am right in thinking

that the Scottish merchants who Smith consulted were indeed using much the same methodology, he was surely remiss in not looking much more closely at their everyday practices, rather than concluding that somehow or other ‘an invisible hand’ somehow ensured the safety and stability of their practices. Nor was that all: Hobbes’ vision of a primordial condition of a war of all against all, which also lay in the background of Smith’s model, it is now equally clear was a similar figment of Hobbes’ imagination, carefully constructed to underpin his real argument: namely that the only reliable means of keeping the resurgence of chaos was by constructing an all-powerful state to keep that prospect at bay. Hence he promoted the concept of Leviathan, envisaged as a vast multiply layered social contract, whose key role was to construct and maintain legal sanctions which would serve to ensure that economic actors of all kinds would be able conduct their contractually-based transactions on a reliable basis, given that fulfilment of those transactions would be enforced by the state.

If so, it also followed that there was no need to look back to the pre-modern period, on the grounds that prior to the invention of the use of money as an easily divisible a unit of value, and hence a ready means of settling transactions, the only way of settling exchanges of good and services was by primitive means of ‘truck and barter’. Although there were excellent grounds on which to suggest they might have been mistaken – for neither Smith nor Hobbes had any empirical grounds on the basis of which to sustain their hypotheses – their assumptions were nevertheless wholly in keeping with the premises of the European enlightenment, and hence went wholly unchallenged. But even if their premises were fictions, although necessarily invented to order to protect the conceptual integrity of their models, both fictions have turned out to have exceptionally long lives.

Of course a great deal of water has flowed under the bridge since Hobbes and Smith constructed their models: the scale of the economic order has grown exponentially since then, as has the discipline of economics, as have the regulatory capacity of contemporary Leviathans. Likewise Smith’s vision of the mysterious ‘invisible hand’ remains with us to this day, where it continues play a key role in the premises which underpin contemporary neo-classical economics. But to what extent has this fictive concept actually operated as an effective source of negative feed-back which had served to constrain over- and under-shoots in the contemporary global financial order? And more to the point, even if Smith had concluded (albeit erroneously) that it was his fictive notion of the invisible hand which was responsible for ensuring that the debts which Scottish merchants routinely generated in their long-distance trading activities were smoothly settled – much to the

bewilderment of the merchants themselves, who were wholly unaware of its presence – just how and why has this fiction lived on for two centuries, even though its alleged stabilising influence appears to have shrunk dramatically over time. As is plain as a pikestaff, booms in the financial marketplace have routinely been followed by busts for well over a century, and each time round the scale of the crash has grown along an exponential trajectory – so much so that the most recent crash rooted in the Euro-American financial services industry almost brought the global economy to its knees. Do we need any more evidence that despite (or rather because of) Smith's invention of invisible hands in an effort to provide a back-stop to explain the stability of his model, the premises of his vision – no less that the classical and the neo-classical versions of economics to which his model gave rise – lacked an effective built-in negative feedback system other than in the form of 'invisible hands'.

If so, what was missing? The answer, in my view, is twofold. If I am right in thinking that the Scottish merchants and their counterparts overseas had constructed a coalition of reciprocity along the same lines as the Maghrebi traders, as seems entirely reasonable, they were by definition not following Smith's vision of autonomous transactors bargaining constantly with one other, and in due course striking contracts with one another on a basis of *caveat emptor*. The key feature of coalitions of reciprocity is that their members are linked together in a vast network of mutual obligations, underpinned by relations of trust rather than by the unilateral, and hence trust-free, notion of *caveat emptor* which lay at the heart of Hobbes, no less the Smith's model. Moreover so long as these models remained theoretical in character, the erroneous character of several of their key concepts, which in due course became of the central premises of the European enlightenment, had very empirical consequences. Just like the Scottish traders, the key to London's financial markets was a gentleman's agreement: my word is my bond. However these agreements also had a sting carefully concealed in their tails: failure to fulfil one's agreement without good reason was contrary to the premises of a gentleman's agreement, and led to prompt blackballing. Trust had been betrayed.

Nevertheless as time passed, the individualistic, take no prisoners premises of the enlightenment proved to be steadily more corrosive. Gentlemen's agreements, as well as the club-like nature of coalitions of reciprocity, began to look terribly archaic, and in due course were swept aside in favour of thrusting modernity in the course in the aftermath of the so-called big bang on October 27, 1986, in which the London Stock Exchange ceased to function as a series of clubs, and became a private limited company instead. A truly classical market-place found itself securitised, with the result that

the trust-based negative feed-back processes which had hitherto played a salient role in sustaining its condition of equilibrium were swept aside overnight. That is not to suggest that the old-style City was an acme of perfections: financial clubbers can all too easily turn themselves into wealthy monopolists. All I am suggesting is that an all-important baby had been tossed out with the bathwater – largely because its significance remained unrecognised by the theorists of neo-classical economists, who had by this time concluded that gentlemen’s agreements had no place in thrusting modern market places.

### **The big bang and the emergence of the Qants**

**W**hilst the consequences of the big bang – which allowed London to catch up with, and in many senses to overtake the more ‘modernistic’ premises which beginning to be deployed in financial markets located elsewhere in Euro-America – to filter through the system, one of its most significant consequences was that the theories of neo-classical economics began to move out of lecture theatres and seminar rooms, and to be applied in the real world. As this happened its theorists began to construct ever more sophisticated – or to put it more accurately, mathematically abstruse – models of transactional behaviour. In doing so their models were firmly rooted in the individualistically oriented premises of the Enlightenment, on the basis of which they aimed to map the (presumptively rational) behavioural strategies deployed by individual actors as they set about negotiate their way through the ever larger – and ever more granular arenas of which the contemporary global economic order is composed. Given that financial transactions within each of these arenas are becoming ever more comprehensively digitised, and that economics has no history of engaging in empirically grounded ethnographic research, the mathematicians – most of whom were theoretical physicists by background – leapt on this numerical data as a means of creating mathematical models of the entire socio-economic order. By now they are doing so all the way from the level of the family, the work-place, the local community, the political jurisdiction within which such networks are set, and indeed of at the level of the entire global order – all at great expense, and with no qualitative content.

Precisely because it is now so heavily digitised, the financial system provides an exceptionally convenient arena within which such economo-physicists can test out their econometric models, since meta-data reporting the value, character and location of financial transactions on a global basis is now readily available on a more or less global basis. Indeed such investigations have now become the lifeblood of

contemporary mathematical economics – and hence of financial policy-making. But however comprehensive this meta-data may be, it reveals next to nothing about the inter-personal relationships which might – or might not – have underpinned these transactions. At a pragmatic level it is easy to see why: such qualitative data did not show up on the mathematicians' radars.

However the roots of this oversight had much deeper ideological roots. Once it was assumed that the social order was composed of autonomous self-programming players, all of equivalent status, such that all contractual agreements, monitored by law, would serve to ensure the stability of the financial order, such concerns were intrinsically redundant. All this suited the Quants. As far as they were concerned the rules of the game were clearly spelt out, such that they could analyse the financial metadata to see how closely matched the real world matched their algebraic and statistical conclusions.

Within this conceptual framework promises to the effect that 'my word is my bond' appeared to have been rendered wholly redundant, so much so that such outmoded premises practices could be safely consigned to the dustbin of history. Henceforward the rule of law, and above all the comprehensive documentation of contracts, invoices and receipts in every transaction, whether large or small, would serve to underpin the security of financial markets, all the way from micro- to macro-arenas. In these circumstances the Quants were in, whilst those who sought to explore the financial edifice from a systemic – and above all from a *qualitative* perspective – were pushed to one side. Instead progressive data-mining in search of greater efficiency (which often meant little more than greater profit) became the order of the day. On this basis mathematical physicists took command of large chunks of the Financial Services industry in the early years of the twenty-first century, on the grounds – amongst other things – that their carefully conceived, contractual grounded and statistically underpinned CDOs could provide a waterproof means of turning chaff into gold, thereby eliminating risk. Perpetual motion machines, no less! Unfortunately these guys were theoretical Physicists, rather than practical Engineers. All they were doing was blowing theoretical bubbles, which eventually collapsed under the weight of their own internal contradictions.

But just where did these contradictions lie? And why did the carefully constructed contractual edifices collapse with such speed? It was not just that the theoreticians had failed to take cognisance of the fat tails hiding in the statistical undergrowth of their bell curves; the real killer lay elsewhere. Since virtually all major financial institutions had joined the bandwagon, they all simultaneously

realised that they had all bought (or sold) pups. As a result the bottom fell out of the market. There were no further backstops.

### **Regulators to the rescue?**

**T**he currently preferred remedy for the resultant disasters of this appears to be more and more external regulation – just the kind of statutory poultice of which Hobbes would have approved. However there are excellent reasons why those with an engineering background would have been a great deal more sceptical. To be sure negative feedback is a prime source of regulation – but it is one which works far more effectively when built into the system itself, such that its impact is an intrinsic component of the whole operation, rather than an operation by external inspectors who are by definition less familiar with the ins and outs of just how the system works, and whose fees also add substantially to financial overheads. Such matters are now beginning to surface throughout the contemporary financial order – and no-where more so in the relatively straightforward arena of value-transfer.

As financial institutions around the globe are currently discovering, in the aftermath 9/11, the credit crunch and more recently of all, the explosion of low intensity warfare in so many parts of the globe, the regulators – the most powerful of whom are located in New York, given that the US dollar is the global medium of exchange – is becoming ever more expensive. But since the source of the regulation is external, the costs of compliance are substantial, every business in the financial services sector has an interest to comply with the letter of the law, whilst simultaneously devising strategies by means of which to work around the restraints which the regulators are seeking to impose on their business. However since these work-arounds are invariably costly to implement, they are really only suitable for high net wealth customers, who have the capacity to pay lawyers' fees for legitimising such work-arounds. It follows, by definition, that such work-arounds are entirely unsuitable for the less wealthy individuals and SMEs whose value transfers are several orders of magnitude smaller. Nevertheless all such businesses still have to carry out the costly processes internal processes of data collection, if only to assure the regulators that all is well, thereby adding substantially to their overheads. But just who meets the costs of all these regulatory requirements? Given that the overheads generated by implementation of a multiplicity of small scale transfers on behalf individuals and SMEs is immensely more expensive than a single million dollar transfer, the answer is simple: costs bear down much more heavily on

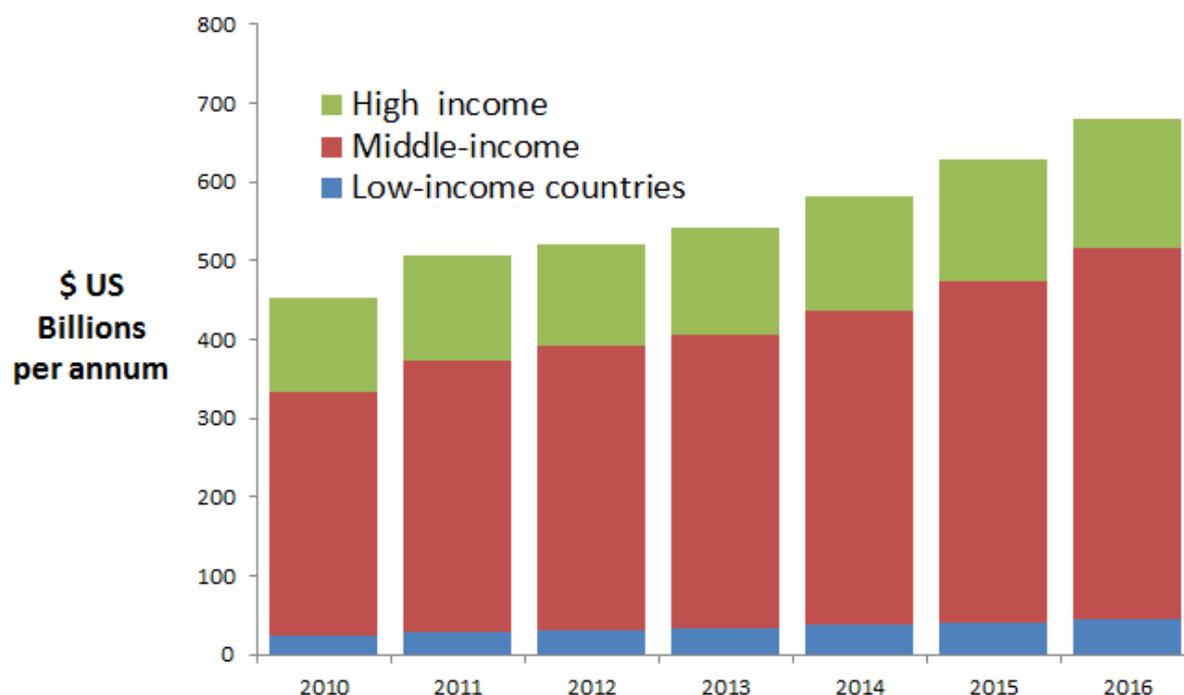
the 99% than the 1%, given that burden of regulatory costs is more or less independent of the scale of the transfer in hand. Is there any alternative available to the unwealthy? Or do the 1% have little alternative but to pay through the nose to keep the Elephants at bay?

### Issues surrounding the contemporary transfer of Migrant Remittances

In recent years the scale of the global payments has exploded, largely as a result of recent revolutions in communications technology. In the first place the sharp fall in the cost of long distance travel has precipitated a rapid growth of migration from relatively disadvantaged areas in the global South to the affluent – but nevertheless labour-hungry – destinations in the global North. Many of these migrants had to leave their families back home, given the restrictive impact of immigration controls. Secondly, and just as significantly, these developments have also precipitated a vast and ever-increasing flow of remittances back to the families which they have left behind.

**Table 1: Estimates and projections for remittance flows to developing countries**

*Source: World Bank Migration and Development Brief 22*



The World Bank (2014) recently calculated that

Remittances to developing countries are estimated at \$404 billion in 2013, up 3.5 percent compared with 2012. This is expected to accelerate to an annual

average of 8.4 percent over the next three years.... The average total cost of sending remittances fell in the first quarter of 2014, dipping below 8.4 percent; however the average cost of remittances to Sub-Saharan Africa has remained stubbornly high around 12 percent”

It also noted that

South-South remittances are either not permitted or very costly due to outward capital controls. The closure of bank accounts of money transfer operators serving Somalia and other fragile countries is also a matter of concern. Remittances provide a lifeline to fragile and conflict-affected countries, where they are more than five times larger than foreign aid, FDI and other sources of international currency put together.”

It also warns that

Anti-money laundering and countering the financing of anti-terror regulations have to be carefully balanced with the development objective of helping the poor.”

### **AML/CFT and its consequences**

**T**he value transfers precipitated by market migrant remittances are clearly big business in their own right. Moreover they also have a major impact on economic development in many parts of the global South. In the first place they deliver a huge volume globally negotiable hard currency directly in the pockets of more or less poverty-stricken families in less developed corners of the world, on a scale which is regularly substantially greater than inflows of aid and FDI; secondly migrant remittances are debt- and string-free, in sharp contrast to overseas aid and FDI, which are normally far from debt free, and all too often captured by local elites and re-cycled overseas at the earliest possible moment. Thirdly, and most startling of all, the data recently published by the World Bank, as set out in Table 1 above, is only half the picture, since it only tracks ‘legitimate’ transfers, in other words those which comply with the regulatory provisions set out in the US Patriot Act. However these provisions were in no way directed at introducing a more significant degree of negative feedback into the global economy. Passed into law immediately after 9/11, its prime objective was to curb money laundering and the financing of terrorism (AML/CFT) – and most particularly the Hawala style Informal Value Transfer networks, through which it was (erroneously) assumed that the attack on the twin towers was financed.

But whilst operators of Hawala networks rapidly found themselves being frozen out of New York’s money-markets, and in due course from the global

banking system, it did not put them out of business: rather virtually all such IVTS networks cut their links with the formal financial sector, and vanished 'underground' – where they continued to thrive. Provided that one can read between the lines, the World Bank is well aware of what is going on, especially in the sphere of migrant remittances. Its mild observation to the effect that AML/CFT regulations "have to be carefully balanced with the development objective of helping the poor" contains very clear message for those with ears to hear: namely that the criminalisation of IVTS networks have enabled the regulated dimensions of Financial Services industry to make substantial profits from providing transjurisdictional value transfers for the poorest of the poor, since IVTS networks have lost a slice of the competitive advantage which they once enjoyed – not so much because their funds were of criminal origin, but because the logistics of their informal value transfer networks were considerably more efficient services offered by their more formally constituted rivals.

Not that this was in any way the prime objective of the introduction of AML/CFT: rather it was to freeze criminals and terrorists out of global money markets, and to catch them red-handed whenever they tried to use its facilities. As such it has failed to implement its objectives. Terrorists and drugs smugglers remain as active as ever, and trust-based IVTS networks continue to thrive, albeit 'underground'. Nevertheless suspicion remains. Are their low-cost services yet another aspect of the 'dark net', supporting a world-wide web of criminal activity – as the Security Services continue to insist? Or are they, to the contrary, trust-based transactional networks whose logistical arrangements are so efficiently organised that they are in a position to undercut the overheads incurred by highly regulated and hopelessly paper-bound practices of the overground components of the Financial Services sector by a wide margin?

At an empirical level hawala networks continue to thrive, and in the migrant remittances market there are excellent reasons to suppose value transfers they implement are on a similar scale to those passing through formal channels. It is easy to see why. Transfers in the informal sector only attract a fraction of Western Union's charges (which substantially undercut those charged by Banks), but nevertheless offer a next-day delivery service even to remote destinations, no matter how small the sum transferred may be. However few members of the public have any idea as to how settlements are achieved in forex markets. In particular they have little or no awareness that even though the vast tranches of value pass through forex markets on a daily basis – no less in the informal than the formal sector – all such transactions are by definition zero sum swaps. 'The money' – in whatever form it takes – stays

put. Operators in the money market routinely aggregate many small transactions into a large tranche, whose value is in due course disaggregated at the agreed upon destination. That makes migrant remittances so difficult to deal with: most transfers are little more than a penny packets (the average is around \$200), many of the senders do not have bank accounts, and the delivery destinations are invariably both distant and remote. A logistical nightmare – at least as far as formally constituted institutions in the financial services sector are concerned. What, then, is the secret of the Hawaladars' success?

### The resurgence of Hawala

The essence of Hawala – the Arabic term for mutual exchange, whose premises are spelt out in the Shari'a – is the implementation of back-to-back swaps, currently brokered in what amounts to a clearing house in Dubai. In doing so migrant remittances transfer a huge volume of liquidity into the Indian Ocean region, which in turn serves to facilitate reverse flows of value throughout the region, thereby enabling traders of all kinds to settle their transjurisdictional invoices in hard currency. In doing so the unit of account for settlements in Dubai is typically tranches of \$100,000, a multiplicity of which will be stacked up in any given value-swap. To be sure the driving force in each direction varies sharply in character: whilst migrant remittances are typically penny packets, business settlements can often involve several tranches of \$100,000. Hawala networks consequently take the form of disaggregated information transfer systems, by means of which of which hawaladars at different levels in the system pass delivery instructions upwards through a hierarchy of nodes to Dubai – or in any other convenient location in which to implement a global swap – in the aftermath of which the value transferred is disaggregated down a parallel network of brokers who hand out the deliver the funds to the recipients designated by the sending hawaladars at the other end of the chain – as I have indicated in the highly simplified diagram below.

The key to this operation – which is normally cash-based – is two-fold. In the first place the cash does not leave the jurisdiction in which it is issued: hence whilst cash passes downwards in the left-hand jurisdiction in the diagram, but moves in the opposite direction in the right-hand jurisdictions. However the original tranches of cash dispatched by dispatching customers are not tagged in any way: rather they are simply aggregated in into larger and larger tranches, until they are disposed of into alternative local network in the aftermath of the Hawala swap – whereupon the cash is disaggregated ready for delivery to the designated recipients. But how do brokers

deal with all this untagged cash? The answer is simple: as the cash is passed the system, brokers at every level email their partners overseas, providing them with precise details of how the delivery of cash they are about to receive should be disaggregated and passed on down to the next layer of recipients. The rest is easy!

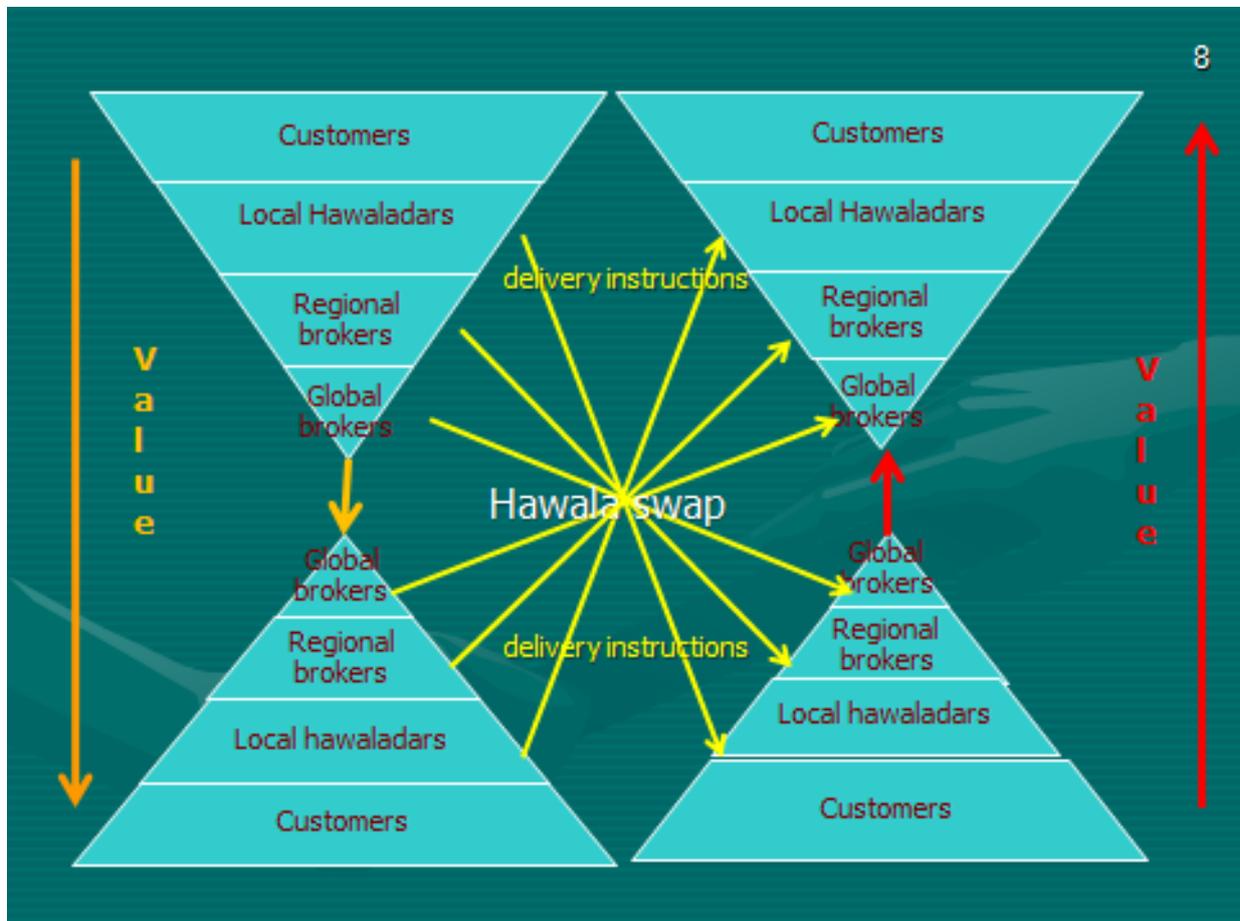


Figure 1 Diagrammatic representation of the dynamics of a transjurisdictional Hawala swap

However as far as regulators are concerned, the process of auditing of highly efficient redistribution networks of this kind is a nightmare – for the simple reason that it is a distributed system which has no central registry. As such Hawala networks are best understood information redistribution systems whose structure is akin to the internet itself – and of which no-one has a comprehensive overview. That saves a great deal of time and trouble, not least because it renders central registries redundant. Rather information transfers are implemented on a node-specific basis, in which instructions pass from node to node, and in each case directing the recipient what to expect by way of deliveries, and to where and to whom those deliveries should be passed on. In other words the each message is node specific, and avoids including information which is redundant in that context. The parallels with the

internet – the prime vehicle utilised to transfer these messages – is close. Just like the internet, Hawala networks are best understood as distributed communication systems, with no central registry; such networks are also information rich, but the data in question is scattered through a multiplicity of local nodes. They are also vastly flexible, since back-to-back swaps of the kind set out in the graphical model set out above are not only implemented on a daily basis, but are also renegotiated on a daily basis as well: no two successive swaps are ever identical. Just in the Internet's IP addressing system allows information to be delivered to the specified destination along a wide (and unspecified) route, so the specific route which any given message takes to reach its destination is close to untraceable, other than by tracing it from node to node on any specific day. All this allows data redundancy to be reduced to the barest minimum, and so long as all instructions are promptly obeyed, value transfers can be implemented on a global scale at great speed, with a minimal degree of overhead costs. No wonder Hawala networks can readily undercut their formally constituted rivals.

But is there a downside? With vast sums of money flying around the globe, surely the whole system is wide open to malfeasance, given that none of these transactions have contractual foundations, and none of the networks maintain a central registry through which to back-track malfeasance. Instead the whole structure is based on trust – in other words the promise that my word is my bond. Can this really provide a secure foundation for such a vast and complex system of value transfers? Close inspection soon reveals the secrets of their success. In the first place, all transfers are completed within twenty-four hours: as a result those involved have no opportunity to deposit the funds in the money market overnight, let alone longer, in order to take advantage of the interest so generated; and for the same reason non-delivery is immediately apparent, and can readily give rise to warning signals throughout the network – whereupon the malfeasant is likely to find himself frozen out of the system until reparations are made.

Secondly, and even more importantly, reputation is the counterpart to trust: in the absence of a reputation for honesty, no-one can survive as a Hawaladar. But even so, a Hawaladar might be tempted to run off with the loot. This is where the key backstop kicks in. Hawaladars are invariably drawn from diasporically extended *biraderis* (brotherhoods, descent groups), such that a significant portion of their counter-parties are kinsfolk; as a result they are already bound together into what Avner Greif long ago identified as coalitions of reciprocity, betrayal of which brings severe sanctions – ultimately of excommunication. Moreover the sanctions precipitated by such duplicity are in no way restricted to the malfeasant himself:

they also extend to all of his immediate kinsfolk; beyond that he can also expect to find that he is unable to find suitable brides for his sons or husbands for his daughters. Given that these sanctions can be applied on a world-wide basis in diasporic contexts, they are highly efficient. Hence malfeasance amongst Hawaladars, as amongst Greif's Maghrebi traders, and in all probability amongst Smiths' Scottish merchants, is consequently rare. In other words, coalitions of reciprocity have the capacity to give rise to a highly effective built-in source of negative feedback.

### **AML/CFT and the criminalisation of Hawala**

**N**evertheless Hawala networks were by no means alone in finding themselves criminalised as a result of the introduction of AML/CFT regulations in the aftermath of 9/11. Since then the regulators in New York and Washington D.C. have been steadily tightening the loop, such that several major international banks agreed to fines amounting to hundreds of millions of dollars in order to avoid being refused access to New York's money markets. Given the provisions of the Patriot Act, together with the fact that the US dollar remains the global medium of exchange, the United States has taken the opportunity to regulate (and/or to rig) the global payments system to suit its geo-political purposes. Those purposes now stretch way beyond AML/CFT: they now include an ever wide range financial sanctions directed against those jurisdictions of whose policies they disapprove, in an effort to bring them to heel. But just how successful has this effort to maintain a position of global hegemony proved to be?

As is now becoming clear, whilst an agreed upon unit of account a convenient means of settling transactions, those arranging their financial affairs on this basis do not need to have access to coinage, or to dollar bills to implement such settlements. Indeed as Graeber points out,

During the reign of the actual Henry II (1154–1189), just about everyone in Western Europe was still keeping their accounts using the monetary system established by Charlemagne some 350 years earlier—that is, using pounds, shillings, and pence—despite the fact that some of these coins had never existed (Charlemagne never actually struck a silver pound), none of Charlemagne's actual shillings and pence remained in circulation, and those coins that did circulate tended to vary enormously in size, weight, purity, and value. According to the Chartalists, this doesn't really matter. What matters is that there is a uniform system for measuring credits and debts, and that this system remains stable over time. The case of Charlemagne's currency is particularly dramatic because his actual empire dissolved quite quickly,

but the monetary system he created continued to be used, for keeping accounts, within his former territories for more than 800 years. It was referred to, in the sixteenth century, quite explicitly as “imaginary money,” and deniers and livres were only completely abandoned, as units of account, around the time of the French Revolution.

There is no mystery about all this. Most transactions ultimately take the form of a mutual settlement of debts, or in other words zero sum swaps of one kind or another. As a result they are inherently invisible, whether they take the form of neighbours swapping apples for raspberries over a garden fence, Hawaladars implementing back to back exchanges of value between the UK and Pakistan, or Treasurers of transjurisdictionally extended PLCs making settlements between their various divisions without having to accrue bank charges for settlements which they can implement with a stroke of a pen. Moreover formally constituted Banks do not implement their mutual settlements in cash: no less than anyone else they now do so by laying off their mutual debts against each other, and if something is left over at the end of the day they settle up with ‘imaginary money’, once again dispatched in ethereal form over the internet.

In these circumstances it was never likely that financial sanctions deployed in the aftermath of 9/11 were unlikely to have any long-term effect. Whilst the provisions of the Patriot Act were designed by the USA to destabilize the machinations of the enemies by cutting through what they identified as the ‘financial sinews’ of terrorists, drugs smugglers and so forth, they made a serious – and indeed a deeply hubristic – mistake. In seeking to maintain what they assumed to be a hegemonic position in the global order, on the grounds that the US dollar had become the global unit of exchange, they failed to realise that the key to all transactions – however denominated – is mutual trust, and by no means necessarily reliant on the transfer of tokens such as dollar bills. Hence their short-cut efforts to suppress drug-smugglers and to starve out terrorists have failed to produce the goods.

What it has done, however, is to oblige Hawaladars (and many others) to take steps to insulate themselves from the prospect of facing criminal charges money-laundering. Prior to 9/11 regional consolidating Hawaladars in the UK routinely used Securicor to deliver large tranches of cash collected from customers and sub-Hawaladars to their local bank on a daily basis, such that they were able to fulfil their transactions in the spot market in New York, whose prices they constantly monitored from an online feed. However that facility vanished following the appearance of AML/CFT, with the result that a work-around was clearly required.

Two solutions emerged. On the one hand most of the major Exchange Houses in Dubai set up wholly owned subsidiary PLCs in the UK, and having done so signed up the great majority of local Hawaladars as their agents; once this arrangement was in place lack of direct access to New York money markets was circumvented. Although they still took their day's takings to their local bank, where they deposited it in favour of the UK subsidiary of the Dubai Exchange house which had signed them up – where all the back-office transactions of the kind outlined above were implemented out of sight of the UK authorities.

By contrast the second option was to implement wholesale cash swaps within the UK, most usually in tranches of £100,000. However this rapidly became an inherently risky option: if knowledge of the prospective deal reaches the Police or the NCA – in all probability with assistance from GCHQ – an ambush is likely to be arranged. Having confiscated the cash on the grounds that it is considered to be the proceeds of crime, all the participants will be arrested and required to demonstrate that they were not engaged in money-laundering. A tough task, since in this context the burden of proof is reversed.

### **A low-cost exercise in Public Relations?**

**D**espite all the efforts which have been made to suppress Hawala networks since 9/11, the system has survived; indeed it has proved to be a reliable and exceedingly efficient global value transfer system based on trust, much to the benefit of the 99%. As such the logistics of this initiative manifestly deserves our careful attention in its own right. Secondly, and even more importantly, it has demonstrated that efforts to manipulate the operation of payments systems to freeze criminals and money launderers out of the global financial system are inherently mistaken. This is in no way to suggest that criminal malfeasance should be overlooked; rather it is to insist that much greater progress towards achieving that goal could be achieved if skilled investigators worked in cooperation with all the agencies involved in facilitating transjurisdictional value transfers, whatever form their methodologies may take, rather than threatening them with criminal charges on grounds of non-compliance with rules laid down in New York.

But whilst international banks are in a position to pay vast fines to avoid exclusion from New York money markets, if only because these can readily be recouped by raising the fees charged to their customers, Hawaladars are in no position to do so. If this is so, could it be that the whole AML/CFT enterprise is best understood as a sophisticated but low cost PR exercise, and one which is proving extremely

profitable to the authorities – given that there is no evidence to confirm that these measures have had any significant impact on terrorists and drugs smugglers' capacity to implement financial transactions?

Nor is that all, by criminalising trust-based networks of reciprocity on the grounds that Hawaladars that their record-keeping is non-compliant with banking regulations, the prospect that networks of this kind are a highly effective source of negative feedback will once again be overlooked by the high priests of economic orthodoxy. In doing so, their perspectives can only be described as myopic. In the first place ever more draconian external regulations are most unlikely to be any more effective than the 'invisible hand' when it comes achieving a greater degree of equilibrium in the financial system, given that ubiquitous work-arounds are the very antithesis in-built processes of negative feed-back. Secondly as cost of complying with regulatory required continues to escalate, efforts to suppress more personalised and hence 'informal' networks such as Hawala are actually reinforcing their significance of Exchange Houses based Hong-Kong and Dubai, if only because their substantially lower overheads continues to improve their condition of competitive advantage over the 'formal sector' rivals. Hence an ever growing proportion of South-South traders turn to Hong-Kong to settle their transactions, not least because the vast inflow of migrant remittances provides a ready source of hard-currency liquidity to keep the whole exercise in business. Meanwhile it is also worth noting that money-laundering in the reverse direction is big business in London, where vast sums from Russia, the Gulf, India, Africa and China have been transferred into the City's money markets with few questions asked about the provenance of such wealth, such that local property prices in the capital are leaping far out of control. Could this be seen as yet another instance of myopic hypocrisy?

## Conclusion

Can and should financial transactions have a moral basis? Or is it the case that in the modern world it is a great deal more rational, and hence more secure, to replace ephemeral notions of morality and trust with black letter contractual agreements? Given the complexity of the contemporary financial order, it goes without saying that parties to financial transactions will invariably need to prepare a written *aide memoire* reminding them the precise terms of their agreement. But is that a sufficient foundation for clinching the deal? Or was it the case that the shaking of hands under the premise of 'my word is my bond' was much more than an old-fashioned empty ritual?

So far as I can see the premises of contemporary neo-classical economics has little or nothing to say on this front. Instead mere *aides memoire* have in principle morphed into legal contracts, such that if anything goes wrong the matter can be settled in court. But in the real world, how often do complex transactions actually end up in court? Very rarely, I suspect, and even then by the time matters reach that stage the horse has often bolted. Moreover as we saw in 2008, when the ephemeral notion of trust evaporates, markets seize up. It follows that in the real world of finance, as opposed to the theoretical universe of economics, issues of trust, and hence of reputation, play a key role in most major transactions. 'Dodgy deals' are invariably avoided like the plague, on the grounds that the risks involved are far too great; and vice-versa, of course. I suspect that Adam Smith's merchants took precisely this view – and that if Adam Smith deemed that the stability of their transactions was due to the operation of a hypothetical 'invisible hand' it took no skin off their noses.

So how did this divergence, which is still with us to this day, come about? In keeping with the premises of the post-Christian premises of the European enlightenment, the fundamental premise of Smith's argument was that human actors autonomous beings who routinely sought to advance their personal interests on a strategic basis, the better to achieve their strategic objectives, free of the prescriptions of a highly authoritarian mediaeval Church. I have no problems with that component of Smith's premises. But could it be that that in adopting this position he inadvertently threw an all-important baby out with the bathwater – and which has been lost to the greater part of economic theory ever since? From an anthropological perspective the answer is obvious. Whilst we are all capable of acting as agents in our own cause, we are all also simultaneously social beings, constantly interacting with each other as we do so. Nevertheless we also do so in a more or less ordered way, since our behaviour is always and everywhere firmly conditioned by linguistic, conceptual and cultural codes, all of our own invention. It is those codes which provide the foundation of each and every transactional, and hence every social order which we humans have yet constructed. Moreover given that there always was, and still is, a huge degree of variation in these codes, there was and still is, all manner variations in what can be best be described as 'rules of the game'

With this perspective in mind we can begin to perceive the character of the baby which was swept away in the bathwater. One of the principal objectives of the European enlightenment was to radically change the rules of the game, and in doing so to sweep away what they identified as 'mindless superstition', and to replace it with scientifically grounded and universally applicable 'rationality'. In the

immediate aftermath of 1789, the French revolutionaries went so far as to try and re-order time itself, by giving it decimal foundations. However they soon found that the rotation of the Earth and time it took to complete its circuit round the Sun, let alone the activities of the moon could not be decimalised. As a result the 'irrational' pre-revolutionary time-frame was rapidly restored. But if similar efforts to comprehensively 'rationalise' the underlying premises of most of the social sciences have also fallen by the wayside, economic theory was and remains a manifest exception, even if it had to preserve belief in the presence of Smith's invisible hand to keep its rationalistic premises afloat.

Nevertheless its impact on the real world of transactions has been far reaching, especially in the field of microeconomics, where the deficiencies in its underlying premises remained relatively significant. However if Einstein's macro-oriented theories of relativity and hence of gravity served to show up some major deficiencies in Newtonian physics, so conventional economic theory has remained 'Newtonian' in character to this day – with disastrous consequences for those sectors of the real world of transactional activity which have been beguiled by the premises of neo-classical economics. It is not hard to see why. Once it was assumed that all those persons engaged in implementing transactions were best understood as autonomous beings, free to advance their interests in whichever way they chose, untrammelled *caveat emptor* became the name of the game. In these circumstances two issues came to the fore. In the first place sellers should not be constrained by extraneous obligations to the buyer bar those specified in the contract, on the grounds that it would undermine the scope of transactional freedom; and secondly if there was any such constraint on transactional freedom, it could only be implemented by the state, in its efforts to regulate, and hence to stabilise, the market.

But whilst the mass of the population has become used to the premises of *caveat emptor*, so much so that individual transactions based on Trust alone are now regarded as exceedingly suspicious by both regulators and jurors, as financial markets themselves have also been steadily 'modernised', and hence regulated for safety's sake, so the premises of *caveat emptor* have rapidly overtaken the underlying premise of the handshake – the word is my bond. As a result the rules of the game have changed dramatically. In an ever widening sphere of contemporary finance, and most especially in so-called investment banking, there is less and less need to play fair by the rules in order to sustain one's personal reputation for honesty and reliability, especially when it comes to dealing with regulatory requirements. What counts, instead, is a player's capacity to manipulate the rules on a profitable basis, thereby gaining access to a larger bonus, contributing to the institution's

profitability, most usually on behalf of high net wealth clients. In these circumstances conformity with the rules ceases to be a mark of respectability and trust. Rather reputational success lies in a capacity to game the rules to financial advantage, whilst carefully circumventing the restrictive trip wires which external regulators have laid out to ensnare them, more often not through every available loophole. This is *caveat emptor* run wild, a world in which evading regulatory restrictions on behalf of exceptionally well-heeled customers is the primary target.

It also follows that trust has by no means wholly evaporated since the big bang took place: rather it has moved firmly up into the stratosphere, to the domain in which the treasuries of transjurisdictional corporations implement all manner of value swaps across jurisdictional boundaries, no less internally as between their own multiplicity of subsidiaries than in even larger swaps with fellow multi-nationals, way above the heads of all the regulators. Meanwhile the premises of *caveat emptor* crawled ever more actively upwards from the bottom end of financial markets, most usually under the guise of efficiency and risk-reduction. But as more and more observers are beginning to realise, whilst the incomprehensible algorithms of the quants may serve to generate substantial profits from small shifts in value, provided that the underlying value transfers are exceptionally large, in no way do they eliminate risk: on the contrary they render themselves extremely vulnerable to Black Swans. Large systems with no built-in feed-back mechanisms are extremely dangerous, since they precipitate even bigger explosions when they run out of control. Moreover once their operators become aware of this danger, the only way to control risk of explosion is to run the system much more slowly than they had done hitherto. Austerity is by definition also a place of safety.

So how can all this be remedied? Re-writing the rules in a more effective manner is going to be a lengthy process, and as such way beyond my capacity as an anthropologist. One point is very clear, however. Risk cannot be successfully measured, let alone eliminated, by the 'efficient' means of applying ever more complex algorithms to raw data. Not that informed examination of financial data is a waste of time. However unless this is supplemented by face to face interactions between counter-parties, such that both sides get to know and hence to trust one another – which is still largely the case in indigenous financial marketplaces outside Euro-America – avoidance of risk will continue to hinder the prospect of further economic growth

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