Living in a World of Pain

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Physicians by their very nature are healers. Their mission is to alleviate unnecessary pain, as well as to provide a better quality of life for their patients. Sometimes they are successful; other times they are fighting a losing battle. In the end, though, everyone must succumb to their mortality.

Pain is often nature's way of letting us know that something is out of balance or is in danger of being seriously compromised. Although it hurts, it is an early warning system that can help to prevent further damage. We cannot claim the same degree of engineering in the financial markets that has been applied to the human body, but the principles are the same.

During the financial panic of 2008-2009, many observers pointed to the stock markets as the cause of the debacle. In fact, the markets were acting more like a thermometer, letting the world leaders know just how sick the global financial system was at the time. The media tends to give the stock market premier billing during times of crisis, however, there is usually a lot of collateral damage to report when a dropping Dow makes the Nightly News.

For example, during 2008, the S&P 500, a proxy for the U.S. stock market declined by 37%. Foreign markets tanked by 43%, with commodities and real estate losing 46% and 41% respectively that year. The pain applied by the financial markets in 2008 was said to presage a second Great Depression. Policy makers responded forcefully to the global financial meltdown. Unfortunately, their solution has given rise to the Occupy Wall Street movement and its attendant frustration that government cares more for its moneyed institutions than it does the working class.

Physicians know that there is a time to medicate a problem, and there is a time for surgery. The policy response to the financial panic was to essentially medicate the problem by throwing hundreds of billions of dollars propping up the banking and financial system. Their response was what you would expect from a typical cyclical downturn, not a fundamentally broken financial system.

What was required was major surgery. Policymakers missed the grand opportunity to restructure the financial system in such a way as to reduce systemic risk to all participants. Banks that were deemed too big to fail should have been broken up. The whole concept of government guarantees should have been reexamined in the light of moral hazard. We will continue to experience heightened volatility in the markets until we begin to see structural change in our financial, as well as social institutions.

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