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**‘Habitation versus Improvement’
and a Polanyian Perspective on Bank Bailouts**

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‘Habitation versus Improvement’ and a Polanyian Perspective on Bank Bailouts

Abstract

The bank bailouts enacted by the Brown Government in the wake of the 2007 credit crunch have had a distinctive political character. Despite the Government’s pronouncements on the merits of swift and decisive interventions, I argue that this does not amount to a return to the interventionist regulatory form associated with post-war British welfare capitalism. The Polanyian distinction between ‘habitation’ and ‘improvement’ is used to show that the bailouts were designed by contrast to defend the underlying deregulatory logic of the existing financial regime. The only real change of note was to forcibly uncover the often hidden influence of the state in the making and regulation of an ostensibly market-led neoliberalism and the creation instead of a much more overt state-led neoliberalism. Habitation strategies were incorporated into a structure of financial deregulation, making it more rather than less difficult to rejuvenate state capacities consistent with enhancing societal welfare. The bank bailouts offered short-term salvation for distressed firms within the financial sector without providing the state with socialised control over the conduct of banking business in order to promote forms of social policy consistent with post-war British welfare capitalism.¹

Introduction

In an infrequently referenced chapter from *The Great Transformation*, Karl Polanyi quoted directly from a 1607 Lords' Report in an attempt to capture the problems which arise when society is subjected to economic transformation.² The Report stated that such dynamics evoked competing objectives: 'The poor man shall be satisfied in his end: Habitation; and the gentleman not hindered in his desire: Improvement'. Polanyi (1957 [1944], p. 34) paraphrased the passage to highlight 'the tragic necessity by which the poor man clings to his hovel, doomed by the rich man's desire for a public improvement [of the economy] which profits him privately'. He then turned the tension between habitation and improvement into a general explanation of the social disruptions which follow when the encroachment of market logic assimilates increasing elements of everyday life to the price system. Improvement passes as a synonym in the rest of *The Great Transformation* for the wilful extension of market logic in the name of economic progress, whilst habitation describes attempts to seek shelter in government interventions from the coordination of economic activity by price signals alone (Polanyi, 1957 [1944], pp. 68-76 and 223-36 respectively).

In what follows, I use the Polanyian perspective of 'habitation versus improvement' to shed theoretical light on the British Government's decision to counteract the effects of the credit crunch with increasingly large bank bailout packages. Massive amounts of public money were made available to rid banks of their bad debts. In particular, banks used concerted state support to immunise their underlying balance sheet positions from their failed investments in mortgage-backed securities and from the related effects of the short-selling of their stocks. The Government took partial

ownership of banks in order to protect banks' balance sheets from the full implications of subjection to the price system. However, ownership was not translated into control of the level at which banks price their lending business. As a result, banks' customers continued to have their economic activity regulated by market logic imposed by banks even as the banks themselves escaped such regulation.

Set within the context of Polanyi's theory of economic development, this amounts to an obvious historical anomaly. The clearest signs of habitation in Government policy in the context of the credit crunch involved the use of taxpayer money to fund the public rescue of banks from the consequences of their own market-based mistakes. The contemporary equivalent of the seventeenth century 'poor man' was required to finance the habitation of the contemporary equivalent of the seventeenth century 'gentleman'. This historical role reversal folded the process of habitation into that of improvement and left significant numbers of people wholly unprotected by Government policy – even as they contributed to the tax returns which financed that policy.

Set within Polanyi's theory of market formation, however, the image of an obvious historical anomaly is much less apparent. He rejected the idea which emerged out of the Austria of his youth that the instantiation of markets simply follows the manifestation of spontaneous order. Instead, he attempted to show how the reproduction of markets requires concerted and often coercive state intervention, memorably arguing that "Laissez-faire was planned" (Polanyi, 1957 [1944], p. 141). Governments often present the reproduction of markets for ideological purposes as market self-regulation, but that does not diminish the state's rule-making influence

over the way in which market outcomes are allowed to encroach upon everyday life as a means of producing compliance to a particular social order (Vogel, 1998, pp. 258-61). From a Polanyian perspective, the most significant change associated with the bank bailouts in Britain was from an ostensibly market-led neoliberalism to a much more overtly state-led neoliberalism.³

The word ‘ostensibly’ is significant in this regard, because it enables the bailouts to be conceptualised as an act of revelation. The banking crisis engendered by failing mortgage securitisation businesses and short-selling of bank stocks merely re-emphasised by bringing to the surface a fundamental fact of market life: i.e., the role of state institutions in the sustenance of free financial markets. The basic *modus operandi* of such markets is conventionally assumed to follow not from state decree but from being populated by rational and self-disciplined financial actors. The dynamics which led to the credit crunch have provided a rather different understanding of the underlying conditions of neoliberal finance, but the Polanyian perspective advanced here shows that it was never a credible explanation anyway.

Three sections follow in an attempt to expand on such a claim. The first analyses the content of the British Government’s assistance to banks so as to assess the character of its efforts to clear up the banks’ self-made mess. The second retells the story of the interventions from a Polanyian perspective which highlights the tensions between habitation and improvement. The third focuses on the possibility that these tensions are themselves magnified when the former is incorporated into the latter. I conclude that the bank bailout packages contain the seeds of social instability when viewed from this perspective.

The Bank Bailout Packages

Mortgage securitisation techniques work by bundling together many individual mortgages into securities whose returns are higher the riskier the underlying mortgage loans. The loan volumes required to facilitate expanding mortgage securitisation businesses reordered the underlying risk structure of mortgage lending during the house price bubble which ended in Britain in 2007. Aggressive lending allowed loan-to-value levels to rise to as high as 125% of the purchase price of the house on the expectation of continued further increases in house prices. Such lending ensured that record volumes of mortgage advances were maintained for as long as the house price bubble remained afloat, thus leading to further house price rises and the continued profitability of trading mortgage-backed securities. Yet, at the first sign that house prices had stopped rising, confidence waned in the continued viability of a mortgage lending market which had been bloated by aggressive lending. This in turn undermined the structure of UK house prices, resulting in a record annual decline of 15.9% in 2008 and a related precipitous fall in the market value of mortgage-backed securities.

The various elements of the bailout packages were all oriented in their separate guises towards a single objective. They were designed to remove market-purchased mortgage-backed securities from banks' balance sheets at a price significantly above that prevailing in the market after the collapse of the house price bubble. The presence of those securities on banks' balance sheets – the now infamous 'toxic

assets' of public discourse – affected all banks' perceptions of each other's creditworthiness. The knowledge that all banks were exposed to some degree to the falling value of mortgage-backed securities meant that they demanded greater assurances from one another that the asset-side of their balance sheets was not going to completely implode and cause them to default on short-term loans secured through the inter-bank lending market. Yet, these were precisely the assurances that banks could not give without revealing stock market-sensitive information about the true scale of their losses. It is this which led to the seizure of short-term inter-bank credit functions and the emergence of the credit crunch. Moreover, short-sellers on the stock market reacted to the refusal of banks to provide credit to one another as an open admission that asset-side implosion was a distinct possibility. The ensuing positions short-sellers took against the prevailing price of bank stocks seriously weakened the liability-side of banks' balance sheets, thereby accentuating the difficulties on the asset-side and further eroding the health of the credit market.

With the prospect of a wholesale meltdown of the banking system apparently too real to ignore, the Brown Government stepped in with a series of imaginative interventionist measures to guarantee short-term credit flows to banks. In doing so it called upon the financial power of the state to override the price signals which were hampering banks' room for manoeuvre on both the asset-side and the liability-side of their balance sheets. It acted decisively to ensure that the fate of the banks was not left to market logic alone. The liability-side was given state protection against adverse price movements on the open market through the announcement in September 2008 of a simple four-month moratorium on short-selling 34 financial stocks (BBC

News, January 5 2009). The asset-side was afforded similar protection, albeit via more complex means.

The template for such protection was established by the introduction of the subsequently extended Special Liquidity Scheme in April 2008 (Bank of England, 2008). The Scheme enabled the Bank of England to issue bonds written against British government debt and to swap these bonds for banks' failed mortgage-backed securities. Crucially, the swaps took place at the equivalent of around a four-fifths discount on the market price of Government debt (Muolo and Padilla, 2008, pp. 274-5). In other words, the banks' 'paid' at most only around a fifth of the market value of the bonds to revitalise their balance sheets in the face of the damage caused by overloading them with toxic assets. The remainder of the bonds' market value was, in effect, a direct credit gift from society as mandated by Government policy.

The British Government has appropriated public money which might otherwise have been used for alternative redistributive purposes in order to socialise the losses banks have incurred through their global trading strategies. This should be seen as a redistributive strategy in its own right. But even though it is redistribution based on clear and authoritative state interventions it would be incorrect to view these developments as a return to a style of macroeconomic governance associated with post-war British welfare capitalism (Finlayson, 2009). There is nothing classically Keynesian in the content of the bank bailout packages, despite them having been introduced through something which looks like a debt-financed Keynesian stimulus. The classical Keynesian strategy was to ensure that state interventions generated a combination of product prices and wages from paid work which allowed low- and

medium-income people to maintain high levels of consumption demand. Whilst activated through similar policy means, the bank bailout packages seek merely to ensure that those same people remain linked to the banks' activities in speculative asset markets (Crouch, 2009).

The difference between the interventions associated with post-war British welfare capitalism and the bank bailout packages is exemplified by the fact that the latter contained only a one-way override of the price system. The suspension of market self-regulation through the price mechanism extended only as far as restoring the health of the banks' underlying balance sheet positions. Banks benefited from the short-selling moratorium which protected the liability-side of their balance sheets from the price signals emerging from the stock market; they also benefited from being able to swap pristine government bonds for failed mortgage-backed securities in order to protect the asset-side of their balance sheets from the price signals emerging from the secondary mortgage market. Yet, there was no reciprocal protection for bank customers as banks changed the terms on which they were willing to price credit. Credit became markedly more expensive than it was for the duration of the house price bubble as banks retrenched their lending strategies, increasing the cost of mortgage repayments at exactly the time that house prices were falling. Even when the Brown Government purchased stakes in banks using public money it did not cash-in its ownership rights as direct control of the price signals emerging from banks (Financial Services Authority, 2009). The subversion of market logic occasioned by the bank bailout packages was therefore distinctly partial.

Polanyian Insights on the Bank Bailouts

Polanyi worked with a broad conception of money, labelling it, along with land and labour, a ‘fictitious commodity’. All three share the same character under capitalism of being bought and sold as if they were commodities without first having been produced for sale (Polanyi, 1957 [1944], p. 72). In Polanyi’s formulation, money has an existential essence related to its social function as a store of wealth. This predates its subjection to the ‘commodity myth’ and its appropriation in late capitalism for strategies aimed at profiting from trading monetary values (Polanyi, 1982, p. 46). The creation of markets for the self-valorisation of money is a recent development in economic history and the creation to that same end of the appearance of *self-regulating* markets coordinated simply by price signals is a more recent development still (Braudel, 1982; Michie, 2001; Fraser, 2005).

In this way, money relations – what typically in political science is known as ‘finance’ – have been increasingly disembedded from society. Polanyi described disembeddedness (1957 [1944], p. 68) as a situation in which markets become ‘more than accessories of economic life’. Apparently self-regulating markets impose themselves on society via price signals by requiring individuals to become functional to their operation. In perhaps his most evocative description of the tendency, he argued (1957 [1944], p. 41) that it amounted to ‘no less of a transformation than that of the natural and human substance of society into commodities’. He attributed such a shift to the desire for improvement: the willingness to view the economy, not as a process for satisfying social needs, but as a site for transposing other people’s labour into self-valorising money through changes to financial prices.

Polanyi believed (1957 [1944], p. 40) that the coordination of everyday life by the price system led necessarily to an ‘avalanche of social dislocation’. He further argued that this would be detrimental to the habitation strategies of the vast majority of ordinary people. In order to secure both their livelihoods and their lives against the commodifying effects of price signals, ordinary people should be expected to seek ways of using the state to subvert the pristine nature of the price system (Inayatullah and Blaney, 1999, p. 328). From a Polanyian perspective, state overrides of price signals related to finance are consistent with attempts to *re-embed* money relations within society – i.e., ensuring that money relations are functional to the expansion of societal welfare, rather than society being functional to the self-valorisation of money.

The credit crunch of 2007-2009 certainly produced a context in which the Brown Government appeared to endorse the legitimacy of habitation strategies. At the very least, we witnessed the effect on the price system predicted by Polanyi’s habitation approach. The Government used significant sums of public money to underwrite banks’ balance sheet positions against the consequences of shifting price signals in both the secondary mortgage market and the stock market. These are protective interventions which impede the logic of market self-regulation associated with improvement. So far, so good – apparently – when trying to match the Brown Government’s interventions with Polanyi’s explanation of how money relations are re-embedded within society.

However, difficulties arise in extending the analogy when we consider the *contents* of the habitation strategies. Pushing the analysis in this direction reveals not a

straightforward repetition of the process described in Polanyi's historical example, but what in effect are two entirely separate processes. Polanyian habitation emphasises society as a whole as the originating site for the subversion of price signals, in addition to assuming that enhanced societal welfare will result from successful protection against adverse price movements. This is because the fictitious commodification which accompanies the extension of market self-regulation into ever more areas of everyday life produces *human* tensions that the market mechanism alone cannot resolve (Hechter, 1981, p. 424; Baum, 1996, p. 4). The pressures for habitation must therefore emerge from sources which manifest these human tensions (Polanyi, 1957 [1944], p. 131). The character of protective legislation in the context of the credit crunch could hardly have been more different. Despite post hoc rationalisations from the Government that they were pro-growth and therefore pro-society interventions, in the immediacy of their enactment they were designed solely to alleviate the *balance sheet* tensions which would have arisen from a refusal to offer banks the preferential treatment of temporary respite from market self-regulation. At no stage were the human tensions which emerge in general from the commodity myths of market self-regulation the focus of policy.

The Government repeatedly insisted after it acted to ameliorate banks' balance sheet distress that inactivity was not a viable alternative. This appears to be a reasonable position to take, especially in the context of the Icelandic experience of wholesale economic dislocation and the destruction of personal wealth when the banks could not be bailed out.⁴ However, my argument is that the character of the bank bailout packages is just as important politically as their fact. What is most interesting in this respect is that the Government's presentation of the choice between policy inactivity

and policy activity in effect reduced to two different ways of ensuring the continued exposure of society to the commodity myth. This most basic of all the features of Polanyian improvement was simply never challenged.

The decision to have done nothing would most likely have accentuated the credit crunch. The most obvious result – as best we can deduce – would have been a sharp increase in the cost of mortgage credit and an enhanced need amongst owner-occupier households to rely on commodified labour to meet mortgage repayments. Yet, the policy action chosen by the Brown Government had noticeably similar effects. The terms on which the banks were bailed out did not include the appropriation for society of banks' pricing functions. As a consequence, customers were faced with the same sort of increase in the cost of credit as would likely have occurred in the 'no action' scenario. In addition, the expansion of public borrowing to finance the bailouts has the opportunity cost of future cuts to other government programmes. As this will almost certainly involve more restricted manoeuvre for welfare-enhancing expenditures, individuals' ability to satisfy their welfare needs will in the future depend ever more on the income generated from paid work. This in turn will mean an intensification of labour commodification, the only difference to doing nothing being the delayed timing of when the intensification kicks in as the constraints on welfare-enhancing expenditures stretch out in the future.

The Defence of Disembedded Money Relations

In strict Polanyian terms the habitation demands to which the Brown Government acceded in its management of the credit crunch do not deserve the name 'habitation'. They better fit his description (1957 [1944], p. 37) of 'a reactionary interventionism' in which a clear strategy for enhancing societal welfare is subordinated to 'an easy prevailing of private interests'. The fact that the Government chose not to complement its ownership stakes in banks by immediately assuming control of the price level at which customers borrowed from banks is important in this respect. Such control would have been the normal expectation of nationalisation as the Treasury bought into banks on behalf of the state, but the model of nationalisation the Government chose in practice amounted to nothing more than state-led neoliberalism. It inserted the state in place of a temporarily missing market in private credit flows, as distinct from using the state to challenge the very premise of credit market self-regulation. In effect, it required taxpayers to pay heavily for ensuring that the banks' privileged position in the relationship with their customers remained much as it has been since the liberalisation of that relationship really took off in the 1980s. The irony of this situation is that taxpayers and bank customers are often exactly the same people. Thus, the bank bailout packages manifest a Government-brokered context in which the majority of British households will have to contribute to financing their own continued subjugation in their everyday relationship with banks.

In my reading of events, the public underwriting of banks' balance sheet positions offered protection *for* the long-term trend towards financial deregulation not *against* it. They were normalising interventions aimed simply at the immediate stability of

the system, where the underlying conception of ‘normal finance’ was one in which a price-emitting system suppresses societal expectations about the possible reinvigoration of British post-war welfare capitalism. The structures of that regime relied for their internal coherence on the deliberate embedding of money relations within an economy oriented specifically to the expansion of consumption possibilities for low- and medium-income members of the population (Pierson, 2006, pp. 46-8). The embedding of money relations within society requires the regulation of financial prices and, more broadly, a regulatory ethos which consciously sets out to subvert market logic in order to exercise social control over price signals emerging from banks. The bank bailout packages introduced by the Brown Government made no such incursions against market logic. They ensured that money relations remained obdurately disembedded from society throughout the introduction of the bailouts, even as public money was called upon to prop up a faltering system of ostensible market self-regulation.

It is for this reason that I distance myself from all possible Keynesian interpretations of the bailout packages and adopt a Polanyian interpretation instead. Keynesian interpretations (e.g., Ambachtsheer et al, 2008, p. 49; Morris, 2009, p. 123; Read, 2009, p. 201) highlight the size of the bailouts and their implications for aggregate levels of public expenditure, but the fact that their introduction did not include any provisions for reversing the disembeddedness of money relations is much more pertinent. No truly Keynesian strategy for re-regulating finance could ever leave such conditions intact (Keynes, 2006 [1936], p. 259). Yet, this does not mean that an alternative Polanyian interpretation can be imposed in its place in any straightforward manner. At the very least, the relationship between the disembeddedness of money

relations and the Brown Government's enactment of policies of habitation is not simply as Polanyi described it in *The Great Transformation*.

The character of the bank bailout packages is consistent with the appropriation of the mechanism of habitation in the interests of preserving the character of the existing drive for improvement. No longer is habitation necessarily related oppositionally to improvement in the struggle for society to impose its interests in the re-embedding of money relations. Instead, it has been co-opted as a means of guaranteeing that the long-term trajectory of a distinctively neoliberal improvement process is not blown off course by a little local difficulty within the banking sector. The systematic failure of banks' over-investment in what are now worthless mortgage-backed securities could have been interpreted as evidence of essential flaws infecting the whole system of disembedded money relations, but instead the Government chose to present it as a weakness of particular managerial strategies within the banking sector.

The long-term implications of the bank bailout packages are also likely to impede future successful enactments of genuine Polanyian habitation strategies. The bailouts have released the banks from the responsibility of facing up to their own mistakes in misreading the price signals emerging from the mortgage securitisation market. But they have done so at the cost of significantly increasing the level of outstanding government debt. The need to pay down this debt will seriously inhibit any future programme designed to enhance societal welfare in the manner of genuine habitation. According to Polanyi (1957 [1944], p. 3, p. x), such situations arise after the process of labour commodification has reached a tipping point at which it 'annihilat[es] the human and natural substance of society', whereupon it creates 'a ruthless abnegation

of the social status of the human being'. But the long-term implications of financing the bailouts through government debt suggests that the future lives and livelihoods of more and more people will be increasingly conditioned by how they position themselves in relation to price signals emitted by the labour market. It thus becomes possible that the tipping point will come clearly into view as the process of repaying the accumulated debts ratchets up the degree of labour commodification across British society as a whole. This suggests that the distorted habitation strategies enacted in response to the credit crunch could well lead to escalating demands for genuine Polanyian habitation at exactly the moment that constrained public finances make such initiatives impossible to fund.

All of this points to a potentially important social contradiction which exists at the heart of the Brown Government's bank bailout packages. Yet, this in itself might come as little surprise. The adoption of a Polanyian perspective on any aspect of modern economic life immediately raises the possibility of its incorporation into a contradictory social whole. In Polanyi's account (1957 [1944], p. 210), such contradictions arise when governments issue special favours to certain interests in terms of providing protection from a system of price-emitting markets whilst stopping short of extending those same favours to everyone. This is certainly the case in the preferential treatment offered to banks in an attempt to alleviate a balance sheet mess of their own making. Indeed, the impact of the bailouts on the public finances will likely ensure that this asymmetric arrangement becomes even more pronounced in the future as the opportunity costs of the bailouts undermines the viability of protective social spending.

Conclusion

In the immediate aftermath of the bank bailouts, much of the broadsheet commentary embraced the notion that the speed and the scale of the interventions marked a decisive end to the previous era of neoliberal regulation. In his respected *Financial Times* column, Martin Wolf (March 25 2008) went as far as to hail the death of the very idea of free market capitalism. For many people of a progressive political orientation, this was the one silver lining of the gloomy economic outlook which accompanied the recessionary impact of the credit crunch. I have used the foregoing pages to argue that any such celebration is premature. The character and the content of the Government's interventions are more important than their speed and their scale. At most they seem to signal a move from an ostensibly market-led neoliberalism to a much more obviously state-led neoliberalism. They do not preserve Polanyi's understanding of the oppositional essence of habitation and improvement. Instead, they turn habitation strategies into a functional accessory of the broader trajectory of improvement. In practice, this has meant rescuing banks from their own mistakes whilst passing on the costs of those mistakes to society in the form of further fictitious commodification. Government interventions have breathed new life into the effects of state-supported and state-sponsored market self-regulation rather than killing them off.

Notes

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² That chapter is called 'Habitation versus Improvement', a title I have borrowed for this piece.

³ I would like to thank Magnus Ryner for first suggesting this characterisation to me in response to a paper delivered at Oxford Brookes University in September 2008.

⁴ I am grateful to one of the anonymous referees for requiring me to focus on this point.

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