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978-0-521-14711-8 - Obama's Bank: Financing a Durable New Deal
Michael Likosky
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1 Introduction

I started researching this book in 1997 as I watched the East Asian currency crisis unfold. I was writing my doctoral dissertation at Oxford University on the role of Silicon Valley firms and the United States government in that regional crisis. At the time, I saw the crisis across the Pacific as, in part, an American crisis. We had contributed to the East Asian Miracle, while at the same time creating a brittle economic and social environment both in Asia and at home. In turn, our subsequent policies addressed, prolonged, and ultimately deferred aspects of the crisis itself. Since the early 1980s, we had progressively divested from our own real economy in America. In doing so, we had redirected our financial and political energies overseas, promoting globalization. We benefited some and disadvantaged others, both at home and abroad.

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When the dot-com boom/bust cycled through the United States, I was in San Francisco. My first spurt of writing happened as I watched our underlying crisis deepen. We razed communities to create dot-com paper wealth. Although many Silicon Valley firms continued to produce real value, the boom cultivated paper wealth as a mix of readily available finance for business plans, resulting in stock market growth. That crisis and its aftermath continued to erode the foundations of our national economy while financing production abroad to meet steroid-induced consumer demand at home.

Matters after the dot-com bust only grew more serious. Our foreign policy squandered the global goodwill, resiliency, and solidarity that emerged in the face of 9/11; we had demonstrated our national mettle and quickly rallied without losing sight of the gravity of living with the reality of terror, while our leadership steered us elsewhere. We found ourselves mired in an unpopular war. Spending on destruction and consumption overtook productive investment not only in America but abroad. With the subprime mortgage crisis and the engineering of a growing middle-class opportunity, our government and financial institutions debased the American Dream by remaking it into a Ponzi scheme.

Until this year, though, it had mainly been a book about perpetual deepening crisis without a clear prospect for recovery. It had attempted to explain, with some exasperation, how the Great Depression had been caused by a partnership between government officials and well-placed private

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commercial interests. This partnership had impeded rather than advanced the public interest, ultimately resulting in systemic crisis. At the time, the drivers called the pre-crisis economy laissez-faire to downplay the role of government. In a related manner, today we talk about a free market or globalization to play down the role of public policy during our boom time. We blame the crisis on deregulation, the retreat of the state from the economy. However, just as in the early twentieth century, an activist state underpins our economy in good times and bad, in boom and bust.

My own hope with the Obama approach to the crisis is not that we vilify government-industry relations or quixotically aim to do away with them. Instead, the purpose of writing this book is to advocate bringing to the fore their justification. In other words, why should we use companies as policy organs? Moreover, *public-private partnership* (PPP or P3) is now a term very much in vogue. Yet, this and similar terms are catch-all words with little meaning, except in reference to ways specific partnership-based programs or projects are structured. This book focuses on how to model partnerships so as to advance their public interest aims.

Furthermore, partnerships have been used extensively throughout American history, from the railroads to the Second World War, from the Internet to the Iraq War. They were central to the East Asian Miracle and regional crisis. The European Union has pursued them to integrate Central and Eastern Europe into the expanded union. As these

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varied examples demonstrate, in practice partnerships both solve and cause problems. They can advance or retard the public interest. With our recovery, reinvestment, and growth strategies premised increasingly on partnerships, the stakes are high in modeling them appropriately. This means not only clothing them in high purpose but also making sure that the financial and corporate, civil and political plumbing are well thought through and attuned to meeting actual need. Partnerships invariably claim to produce public goods, but in practice their benefits can be reduced to profits and their gains privately held and largely short lived.

One of the most important institutional mechanisms for conceiving and directing partnerships has been government investment banks. In the United States, such banks were used during the First and Second World Wars. In foreign policy, we established the Export-Import Bank during the Great Depression and then the Overseas Private Investment Corporation in the early 1970s. These public financial institutions aim to use private firms as foreign policy organs, sometimes with success and other times causing damage. And, perhaps largest in scale and subject to much controversy has been the World Bank, founded by the victors of World War II to lay the foundation for postconflict economic stability and growth. Since the 1980s, the World Bank has redirected its efforts away from promoting government projects and toward partnerships. A similar timeline of support has occurred within public regional development banks representing every continent, the African

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Development Bank, Asian Development Bank, European Investment Bank, and Inter-American Development Bank.

The Obama Infrastructure Bank idea and the Clean Energy Bank proposals now on the table are essential for devising effective partnership-based growth. They base themselves explicitly on the international infrastructure banks. The idea is to turn this foreign policy model inward to reinvest in the American economy. However, thus far we have spoken about these international banks in unrealistic terms, focusing more on how their most un-self-reflective advocates understand them, rather than on how they function in practice. We have compounded this distortion by doing the same with public-private partnerships. We must learn from international experience and take the issue of institutional design much more seriously than we have thus far. This book advocates for a single mega-bank combining traditional infrastructure sectors along with clean energy in far greater depth than currently envisaged. The Obama Bank should gather together all bond- and subsidy-financed federal projects. We should expect the bank to produce public goods, to solve real-world problems, and to coordinate and reintegrate our national economy.

The book starts on the campaign trail with then-Senator Barack Obama's speech in Janesville, Wisconsin, introducing the Infrastructure Bank. The third chapter turns to the origins of partnerships and a bank within the Democratic Party as a response to Reagan Revolution–led privatization. The next chapter returns to President Obama's economic

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philosophy, placing it within the context of twentieth-century views on the appropriate role of government in the economy.

We then turn, in Chapters 5 through 7, to discuss how P3s evolved internationally since the 1980s to become a cornerstone of American foreign policy. Chapter 8 focuses specifically on how to approach transparency within P3 projects. It draws on the work of Supreme Court Justice Louis Brandeis aiming to make Gilded Age P3s more accountable.

Next, in Chapters 9 through 11, we turn back to the international experience with P3s, focusing on the role of contracts in catalyzing projects. Partnership contracts were essential for turning the page away from unequal colonial bargains. However, more recently, countries have sought to rebalance many of the enduring inequalities associated with extractives and infrastructure contracts through renegotiations. A series of lessons are drawn from three decades of experience with P3 contracts for the United States.

Lastly, drawing on domestic and international experience with P3s, a series of specific recommendations are advanced for modeling our national infrastructure bank so as to promote effectively the public interest. Attention is paid to institutional design, the modeling of P3 projects themselves, and also how to build upon the successes of our recovery to date.

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2

The Janesville Plan

I. Obama's Axioms

On February 13, 2008, then-Senator Barack Obama delivered a speech that marked a turning point in his candidacy, one that helped propel him into the presidency and came to define at least his first year in office. On the factory floor of the General Motors assembly plant in Janesville, Wisconsin, Obama pivoted away from being the sole candidate to have opposed the Iraq War and toward positioning himself as the forceful champion of America's economic recovery. In this landmark speech, Obama argued for redirecting our energies away from reconstructing Iraq and toward reinvesting in America, proposing a national infrastructure reinvestment bank to direct these efforts.

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By the time Obama took office as president roughly a year later, our national ailment had became synonymous with a financial contagion originating in the subprime mortgage sector. In line with this diagnosis, our economy was undergoing a course of capital injections initiated under the previous administration into blue-chip financial institutions and the market-dominant insurance firm AIG. Obama's apparent decision not to disrupt this treatment predominated the twenty-four-hour news cycle. However, despite the exasperation caused by bipartisan bailouts, non-performance-based bonuses, and Washington–Wall Street teamwork, it is nonetheless useful to take a Copernican view of things. The subprime mortgage crisis, although disastrous, is a symptom of a much larger, graver chronic illness.

The Obama capital infusion was a stimulus package, not an extension of the Bush administration bailouts. It marked a sharp break. Viewed through the lens of the Janesville speech, which would become a template for his inaugural address, Obama's handling of the banking crisis looks different than typically portrayed by pundits. The infusion, while still worthy of debate like much else, is not designed to restore the Wall Street status quo. Instead, it should be viewed as an attempt to redirect lending practices. The argument here is that Obama has been recapitalizing the banks so that they can serve specific public policy purposes, namely financing a new approach not only to our domestic economic renaissance but also to our foreign commercial policy.

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For this reason, the bank and AIG stimulus should not be dismissed outright as restoring the pre-crisis Wall Street status quo. Instead, we should be engaging in a debate over the public policies that actually underpin them with an eye toward whether the capital infusion itself is the appropriate means to accomplish the intended aim. In other words, we must determine what these policies actually are and ensure that public and private tools are in place that are tailored to advancing them. This is a prerequisite to devising appropriate accountability measures.

The Janesville Plan set forth the basic axioms of the Obama administration's approach to recovery and reinvestment. Obama prefaced his Janesville speech by stating, "What I really want to do is talk from the heart about where I want to take this country."[1] Thus, one might look to Janesville to give definition to that enigmatic Obama principle of empathy.

Obama began by telling the audience not to expect the rousing speech delivered a day earlier to a full-capacity audience of nearly twenty thousand in Madison, the capital city of Wisconsin and a university town, at the Kohl Center, the University of Wisconsin's sports stadium, which was named for the state's U.S. senator and department store magnate. Instead, Obama would "take it down a notch," giving "a little more detail." On *Hardball* that night, Chris Matthews described the speech this way: "He's saying: I better move from the great speechmaking to the nuts and bolts to show the beef here to mix the metaphor."[2] It was no accident that

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Obama chose to deliver his speech, assessing our economic predicament and proposing a policy agenda to lead us out of it, on a factory floor in the Rust Belt. In fact, his competitor at the time, then-Senator Hillary Rodham Clinton, the next day waved boxing gloves above her head on the factory floor of another General Motors assembly plant a couple states over in Lordstown, Ohio, saying, "We need a fighter and a champion in the White House again for the American people."[3] With sports utility vehicles behind him, Obama spoke to an audience of around six hundred autoworkers.

Obama dispelled the still-persistent and prevalent myth that the subprime mortgage meltdown caused the crisis. Instead it was "the straw that broke the camel's back." In fact, the crisis was "the culmination of decades of decisions that were made or put off without regard to the realities of a global economy and the growing inequality it has produced." As a result, the central job of government was to restore equal opportunity. Obama spoke compellingly about how the root of our crisis lay in government decisions to advance domestic and international policies that privileged corporate profits and the interests of the wealthy over worker jobs and fair wages. In other words, the crisis was not caused by the government passivity associated with the commonplace idea that it was the absence of government, its retreat through deregulation, that alone allowed the market to grow out of control. Moreover, it was not simply a banking crisis, arising in the financial sector and destined to be solved there. Instead, the government actively promoted policies driving a

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