The History *of* Debt

By Harold James

Cement or explosive, elixir or poison?

There is no end of debt in sight. However much politicians and economic analysts complain about the dangerous consequences of the buildup of government, corporate, and personal debt all over the world, we appear to need ever more debt to face the health, climate, and security challenges that are all round us. Even as activists demand a biblical cancellation of debt, that is, a jubilee, they too want more debt, because only debt—a mortgage on the future—can help meet present needs.

Looking at aggregate figures on government and corporate debt, it is easy to believe that the world is drowning in debt. That is why it is good to be reminded by books like that of Barry Eichengreen, and his co-authors Asmaa El-Ganainy, Rui Esteves, and Kris James Mitchener, that debt can play and has played a positive role over long periods of time.

Debt creates the obligations that tie the global economy together and make trade and payments possible. At the same time, the fact of debt imposes payment requirements that become uncomfortable and burdensome, especially when interest rates rise.

The fact of debt is old, as is the dilemma that it constantly produces. Scholars—archaeologists, historians—agree that debt is considerably older even than money or coins. Clay cuneiform tablets in Mesopotamia, for example, record Sumerian debt contracts measured in units of grain or animals (sheep) over five thousand years ago, around 7500–3350 BCE.

Harold James is Professor of History and International Affairs, Princeton University. This article is in part based on a chapter on debt in his new book, The War of Words: A Glossary of Globalization *(Yale University Press, 2021).*

THE INTERNATIONAL ECONOMY
THE MAGAZINE OF INTERNATIONAL ECONOMIC POLICY
220 I Street, N.E., Suite 200
Washington, D.C. 20002
Phone: 202-861-0791 • Fax: 202-861-0790
www.international-economy.com
editor@international-economy.com

That is why it is good to be reminded by books like that of Barry Eichengreen, and his co-authors Asmaa El-Ganainy, Rui Esteves, and Kris James Mitchener, that debt can play and has played a positive role over long periods of time.

The dilemma of how to understand the consequences of debt for relationships between people is also an ancient one. Debt came to be a central feature in the development of civil society, and of the concept of responsibility. It is at the heart of the moral economy.

The evolution of debt was central to a theory of ethics. All Plato's virtues—temperance, prudence, courage, and justice—can be either developed internally, from one's character or one's internal resources, or are based on external or social influences. Courage, later often redescribed as the virtue of fortitude, involved meeting obligations, and not running away from them.

Debts thus help to socialize us and bind us to others. They are one aspect that constitutes the key to human personhood, in that they provide a recognition that we are bound by our past actions, and thus have a continuous identity as a person. On that basis, promises occur between persons: you know who I am and can rely on me, even if circumstances change. Without that trust, there is endless suspicion.

Debts can also very obviously be highly oppressive, creating chains of obligation, and, in many premodern societies, bondage and debt peonage. It thus regularly deprived people of their humanity. That is because circumstances obviously do change: there are accidents, climatic and health catastrophes, and other circumstances that make it impossible to repay. Many religions, including Judaism, Christianity, and Islam, consequently evolved prohibitions against lending on interest, or usury. Islam indeed still maintains notional restrictions, and the application of Islamic law leads to the inclusion of an equity or risk-sharing element in financial instruments. Some analysts in consequence suggest that Islamic law provides a more adequate basis for a modern economy, in that it excludes debt instruments. Yet there is little evidence that Islamic law actually changes much of Muslims' financial behavior.

Thousands of years ago, there appeared an easy way of bridging the gap between debt on the one side as the progenitor of responsibility, civility, and order, and on the other as a source of individual distress and disorder: make debt the affair of governments. That was the view of classical antiquity, and it has a parallel in one modern view, which sees governments as creating a particular secure or stable asset, and thus producing a public good. *Continued on page 81*

The Devil's Excrement

What would happen if the state could not pay, and if all the paper chits were worthless? Public order would be threatened.

That experience confronted France twice in the course of the eighteenth century: first when the Scotsman John Law tried to set up a project based very much on the Bank of England model to consolidate the royal debts at the end of the spectacularly costly (and for France disastrous) War of Spanish Succession; and second with the financial experimentation of the French Revolution, when *assignats,* secured on the *biens nationaux,* were over-issued.

In 1720, Law's scheme gave rise to a host of pamphlets and caricatures in which it is the devil who creates the money that deceives. In many of the popular versions, the devil shits money: the delusion created by unbacked money is the devil's excrement.

—H. James

Scottish economist **John Law** *(1671–1729), in a portrait by Casimir Balthazar.*

Continued from page 29

In Greek city-states, the public treasury, secured in grand temples, held what were notionally loans of citizens that could be used for emergencies. These did not usually pay any interest. If the citizens lost, they had simply made a sacrifice for a greater good. The loans in this way represented one idea of civic community. The link of state debt and religion was clearly expressed in the form of the building, which much later (especially in the eighteenth and early nineteenth centuries) provided a model for bank buildings.

Debt came to be a central feature in the development of civil society, and of the concept of responsibility. It is at the heart of the moral economy.

Monarchs and absolute rulers, by contrast, would attempt to raise the same kind of credit—the distinction between that and taxation was not always clear. There was little prospect for creditors of being repaid, and so they became smarter about concealing their wealth from royal agents (in effect tax collectors). In consequence, monarchs would borrow, paying interest, from merchants in other territories, and frequently have partial or complete defaults. There was no knowing in advance precisely what challenge—usually military—the monarch might take up. And there was obviously no way to be certain that the king would make repayments according to the original contract. These defaults could not be too complete, because otherwise the king's reputation and his ability to take on more debt would be limited. But there was an arbitrariness about the process, which created uncertainty, and that translated into higher interest rates. Getting better terms for debt was a central spur to the process of creating political accountability, and even democracy.

There is a model for that move to accountability, provided by late seventeenth century England; there advocates of a new financial order looked back at late medieval Italian cities, notably Genoa. The spectacularly successful English model was then taken up, by Napoleon, who created a Banque de France on the model of the Bank of England; and in the United States, by Alexander Hamilton, who saw the federal debt created as a consequence of mutualizing state debt from the war of independence as "the strong cement of our union."

Recently, after the emergence of the European or eurozone debt crisis in 2010, and even more in response to the Covid crisis, Hamilton and his views on debt—and the whole discussion of the late seventeenth-century English "financial revolution"—resurfaced. Should there be some measure of debt mutualization in Europe? The United States pushed Europe very heavily in this direction as a way of making Europe financially more stable. After the coronavirus crisis hit, and required a common European debt instrument to finance the response, Europeans at last took up the language of the "Hamiltonian moment."

But that move was contested: Hamilton's debt gave rise to a bitter division between North and South about tariffs. In Europe, the idea of a common debt was bitterly contested, and critics, especially in northern Europe, feared that it would give rise to costly transfers. Debt can be poisonous too.

Debt on the part of the state depends on a complex network of promises and engagements. It gives the state the resources to perform its central functions—defense, the administration of law and justice—and correspondingly creates loyalty from the beneficiaries of state-provided security. That is why the choice of being Hamiltonian is so difficult: It may build new bonds, but it also presupposes some initial common sentiment. People in the past believed that they were committed to die for the fatherland, but today it is too much of a mental and emotional stretch to die for debt mutualization.

And then there was the problem of states promising too much. What would happen if the state could not pay, and if all the paper chits were worthless? Public order would be threatened. That experience confronted France twice in the course of the eighteenth century: first when the Scotsman John Law tried to set up a project based very much on the Bank of England model to

Debts thus help to socialize us and bind us to others. Debts can also be highly oppressive.

consolidate the royal debts at the end of the spectacularly costly (and for France disastrous) War of Spanish Succession; and second with the financial experimentation of the French Revolution, when *assignats,* secured on the *biens nationaux,* were over-issued. In 1720, Law's scheme gave rise to a host of pamphlets and caricatures in which it is the devil who creates the money that deceives. In many of the popular versions, the devil shits money: the delusion created by unbacked money is the devil's excrement.

Some of the refugees who fled from revolutionary France ended up in the small German court city of Weimar. Stories told about the *assignats* inspired the insertion of a monetary episode into the old German tale of Doktor Faustus. In the second part of Goethe's version, the devil, Mephistopheles, accompanies Johannes Faust to the court of a medieval emperor, in the middle of an economic downturn when the fields are fallow and industry idle. Mephisto says that paper money can be issued against precious metals in the ground, and that there is no need even to dig out the gold. All that matters is trust: money is built on debt. The result, paper money, immediately breeds confidence and sets everyone back to work. The emperor's officials report back delightedly: "The Chancellor told me, "Give everyone a high festive pleasure, make the welfare of the people, with just a few strokes of your pen." Faust responds: "Wise men will, when they have studied it, place infinite trust in what is infinite."

The episode, in Goethe's telling, is still full of resonance in the twenty-first century, and it is regularly quoted by people afraid of debt, and afraid of inflation as a quick way of reducing debt burdens. There are two responses to the concern about the abuse of monetary magic. One is to be permanently frightened by the prospect of an inflation that will wipe away not only the value of debt, but also the basis of every contract. The other is to hope that some benevolent outsider—someone who is not the devil—will take over or assume the debt. When the state is taken over by evil or self-interested personalities, it is destroyed; whereas if the state jumps in as a benevolent outsider, it appears as the rescuer, the savior.

Debt and its complex politics of resentment represent a powerful force that can progressively erode contemporary globalization. Or, to go back to the Hamiltonian metaphor, instead of being a strong cement for a union, it has become a high-charge explosive.

There are once again proposals to channel debt through international institutions in order to systematize it and to make debt credible again. The coronavirus pandemic had an outsize impact on poor countries dependent on capital inflows (which came to an abrupt stop with the outbreak of the pandemic) and on exports of commodities and goods such as textiles, for which demand temporarily collapsed. Over a hundred countries went to the International Monetary Fund and explained that they required international financial support. The G-20 as an immediate response agreed to a temporary halt to bilateral loan repayments from a group of seventy-six of the poorest countries. One proposal then suggested that multilateral institutions such as the World Bank with other multilateral development banks should create a central credit facility, allowing those countries requesting temporary relief to deposit their stayed interest payments to official and private creditors for use in emergency funding to fight the pandemic. International institutions are supposed to take the poison out of debt relations in a way analogous to the classical era's sanctification of debt through the state.

Getting better terms for debt was a central spur to the process of creating political accountability, and even democracy.

The situation in which both sides, creditor and debtor, think that they are trapped looks like a variant of the famous Master and Slave dialectic in Hegel's *Phenomenology of Spirit* (1807). Both sides are trapped. The Slave is not recognized as fully human, or as an equal by the Master, and is not free. The Master is free, but does not find that he is recognized as a human by the Slave. He is constantly worried by the fragility of the relationship, and the fact that the Slave is building up an alternative universe of values in which the Master is not represented.

The dynamics of debt when combined with the forces of globalization produces a trap. Another way of seeing it is through the 1969 hit song by Mark James and Elvis Presley about the trap created by suspicion in a relationship: "We can't build our dreams on suspicious minds." Humans are always suspicious, especially when they think of foreigners. Debt, especially international debt, is the way that dreams of solidarity are changed into nightmares. ◆