

# Manias, Panics and Crashes

Examine the record of history, recollect what has happened within the circle of your own experience, consider with attention what has been the conduct of almost all the great unfortunate, either in private or public life, whom you may have either read of, or heard of, or remember; and you will find that the misfortunes of by far the greater part of them have arisen from their not knowing when they were well, when it was proper for them to sit still and be contented.

—Adam Smith  
*The Theory of Moral Sentiments*

Much has been written about panics and manias, much more than with the most outstretched intellect we are able to follow or conceive; but one thing is certain, that at particular times a great deal of stupid people have a great deal of stupid money. ... At intervals, from causes which are not to the present purpose, the money of these people – the blind capital, as we call it, of the country – is particularly large and craving; it seeks for someone to devour it, and there is a ‘plethora’; it finds someone, and there is ‘speculation’; it is devoured, and there is ‘panic.’

—Walter Bagehot  
‘Essay on Edward Gibbon’

I permit myself to note in this connection the words said to me by a very high personage of the Republic: ‘I know my country well. It is capable of supporting anything with calm except a financial crisis.’

—Raymond Philippe  
*Un point d'histoire: Le drame financier de 1924–28*

I can feel it coming, S.E.C. or not, a whole new round of disastrous speculation, with all the familiar stages in order – blue-chip boom, then a fad for secondary issues, then an over-the-counter play, then another garbage market in new issues, and finally the inevitable crash. I don’t know when it will come, but I can feel it coming, and damn it, I don’t know what to do about it.

—Bernard J. Lasker  
Chairman of the New York Stock Exchange in 1970,  
quoted in 1972 in John Brooks, *The Go-Go Years*

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## A History of Financial Crises

Fifth Edition

Charles P. Kindleberger

and

Robert Z. Aliber



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Foreword © Robert M. Solow 2005

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# Foreword

Charlie Kindleberger (CPK from now on) was a delightful colleague: perceptive, responsive, curious about everything, full of character, and, above all, lively. Those same qualities are everywhere evident in *Manias, Panics and Crashes*.

I think that CPK began to work on the book in the spirit of writing a natural history, rather as Darwin must have done at the stage of the *Beagle* – collecting, examining and classifying interesting specimens. Manias, panics and crashes had the advantage over rodents, birds and beetles that they were accompanied by the rhetoric of contemporaries, sometimes with insight, sometimes just blather. It was CPK's style as an economic historian to hunt for interesting things to learn, not to pursue a systematic agenda.

Of course, he was an economist by training and experience, and he soon found patterns and regularities, and causes and effects. What caught his eye especially were the irrationalities that seemed so often to enmesh those directly or indirectly enmeshed in the events themselves. By itself that would have been merely entertaining. The story got interesting for CPK with the interaction of behavior and institutions. The occurrence of manias, panics and crashes, and their ultimate scope, also depended very much on the monetary and capital-market institutions of the time.

CPK could not have known at the start just how hardy a perennial financial crises would turn out to be. The quarter-century *after* the publication of the first edition featured a whole new level of turbulence in national banking systems, exchange-rate volatility and asset-price bubbles. There was always new material to be digested in successive editions. This history cannot have been merely the result of increasing human irrationality, though CPK would have been charmed by what a German friend of ours called 'Das Gesetz der Verschlechterung aller Dinge' (the Law of the Deterioration of Everything). Increasing wealth, faster and cheaper communication, and the evolution of national and international financial systems also played an indispensable role, as sketched in Chapter 13, added to this edition by Robert Aliber. CPK's effort at economic history found a subject that does not appear to be going out of style.

The shape of a 'new financial architecture' and the possible utility of a lender of last resort – national and/or international – along with the guidelines that ought to govern it were also among CPK's preoccupations. Those who are engaged in reforming (or at least changing) the system would do well to ponder the lessons that emerge from this book.

One of those lessons is very general, and is most applicable in contexts where irrationality may trump sober calculation. CPK was a skeptic by nature, just the

opposite of doctrinaire. He mistrusted iron-clad intellectual systems, whether their proponents were free marketeers or social engineers. In fact, he considered clinging to rigid beliefs in the face of disconcerting evidence to be one of the more dangerous forms of irrationality, especially when it is practiced by those in charge. The international economy would be a safer place if CPK's tolerant skepticism were more common among the powers that be. I am thinking, in particular, about current discussions of the so-called 'Washington consensus', and the pros and cons of both freely floating exchange rates and unfettered capital markets.

Any reader of this book will come away with the distinct notion that large quantities of liquid capital sloshing around the world should raise the possibility that they will overflow the container. One issue omitted in the book – because it is well outside its scope – is the other side of the ledger: What are the social benefits of free capital flow in its various forms, the analogue of gains from trade? CPK, whose specialties as an economist included international trade, international finance and economic development, would have been sensitive to the need for some pragmatic balancing of risks and benefits. One can only hope that the continued, up-to-date availability of this book will help to spread his open-minded habit of thought.

It seems to me that the Aliber version preserves this basic Kindleberger orientation but imposes a little more order on CPK's occasionally wayward path through his specimen cabinets. More manias, panics and crashes may plague us, but readers of this book will at least have been inoculated.

ROBERT M. SOLOW