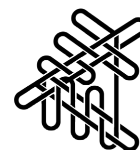

Book review

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Who can exercise the option of justice?

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Robert Meister, *Justice is an Option: A Democratic Theory of Finance for the 21st Century*, Chicago, IL, Chicago University Press, 2021, 304 pp., $30.00 (paper), ISBN 978-0-226-73448-4

Robert Meister's book is subtitled 'A democratic theory of finance for the 21st century'. At first glance, there are odd juxtapositions expressed in the title: justice and democracy on the one hand; finance and options contracts on the other. How can they be integrated? That is the challenge Meister sets.

My conclusion is that, in relation to whether Meister gives us a good analysis of a financially-driven politics of justice, I am unsure, and it's not my area of expertise. But as an explanation of contemporary finance, options theory, and the social meaning of liquidity, this is far and away the most elaborate and insightful thing I've ever read. Its significance as an engagement with social studies of finance, with Marxism, and with politics stands as a major contribution in its own right. It isn't an easy read – the richness of the analysis requires that it be digested carefully – but it will, for many people, change the way they understand the political meanings, and potentials, of financial analysis.

First, the justice proposition. As a development of his earlier book, *After Evil: A Politics of Human Rights* (2012), Meister holds the view that historical justice requires (at least) significant payouts to those who have suffered systemic injustice, who have had their wealth and life chances expropriated, perhaps across many generations, and where this expropriation forms the basis of the wealth (current as well as past) of the expropriators and their progenitors. Histories of colonial rule and racially-based indenture create the conspicuous, but not exclusive, expressions of historical injustice. But, says Meister, the argument in liberal states is always that it is never the right time for financial compensation: it is either too late (it's all in the past, and the state's welfare system addresses those currently suffering disadvantage) or it is too early (the financial conditions are not yet right to afford financial payout). So we instead live in a world of rituals: formal apologies from heads of state for past abuse, acknowledgments of traditional ownership, promises for the future, and so on. But nothing material really changes.

So how do you price something so big and unmeasurable as historical justice and where the consequences, should the struggle for justice be played out successfully, would be so

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disruptive of the financial conditions that would enable a payout? Meister contends that we can reframe payment for past injustice through finance options. Two features of options are critical here. First, an option is a financial exposure to the performance of an underlying asset, but without (necessarily) entailing ownership of the underlying asset itself. An option on justice is a financial exposure to a just future, but not necessarily ownership of that future justice. Second, through options, volatility – change, regardless of its direction – can be priced. This is the implied volatility derived from the Black Scholes formula for options pricing; a subject explored throughout this Special Issue. If market volatility can be priced and traded, so too could social and political volatility. Dissent and ferment expressed socially, including by and in support of those who have suffered injustice – regardless of whether it is successful in changing social practices on justice – opens a volatility spread, and where there's a spread, there's an opportunity to gain. Meister contends:

> … oppositional social movements, especially if they are militant, may or may not achieve their forward-looking goal of directional change, but … their efforts to do so will always take the path of raising uncertainty about the status-quo, and thus heightening financial volatility. An important political question will thus be whether they can benefit from the heightened volatility that results from any initial success they may have. (p. 43)

Volatility created by and on behalf of those suffering injustice may not generate access to full financial compensation (however that may be framed) but we should see them as holding an in-the-money *call option* on justice. The political strategy, within the financial capacities of the state in the present, is to focus on the price of the option; not the price of the underlier. The question then becomes: how much will it cost society (the state) to roll over the option on justice: to give a current payment that acknowledges the truth of past injustice and preserves the *right* to 'full' compensation (the price of the underlier), but keep pushing that full compensation into the future? And what are the social conditions that could enable financial liquidity in that option market? Framed in Marxist categories (for this is decidedly a proposition coming out of Meister's reading of the Marxist project), this is a proposal to harvest value from the injustices of the past.

This is a new and remarkably thoughtful framing of debates about distributional justice that engages capitalist development at its frontier (financialization and financial innovation). In highlighting the possibilities of harvesting volatility for political causes, Meister gives us a new window on political action in relation to finance. In 2011, Occupy Wall Street was a politics of grinding Wall Street to a halt. It could only ever have been a temporary intervention. In 2021, social media mobilized a crash of hedge funds short-selling GameStop (GME) shares, but ultimately at significant cost to participants. Both were profound activism in their context; neither sustainable. Meister is reframing long-term, sustainable political gains from the impact of political activism on option prices. He is opening a new political space.

But, to reiterate, the justice issue per se is not really what gets me excited about this book. It is the analysis of financial market liquidity and the financial conditions of building justice options that for me offers the richest insights. Meister explains that as options can price downside as well as upside risk, then downside risk can logically be sold off, leaving a 'risk-free' asset that can be pledged as collateral for lines of credit and provide an expanding liquid 'base' from which the risks of other assets may be effectively priced. Expressed dynamically, the expansion of 'safe' assets by means of derivative hedging has been the foundation for an even more rapid expansion of more risky assets. The spread of derivative positions on risk is the condition for the creation of the expansion of spending power, backed

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by assets once thought too risky to form collateral. This, for Meister, opens up new framings of the social conditions of the relation between volatility and stability, and hence the political opportunities of the resulting spread. There is so much to be said of the dimensions of this spread, and here is where this book offers page after page of lateral insight.

There is also extensive engagement with state financial/monetary policies. To give one instance, in an options-related analysis of state policy, Meister engages in some detail (at pp. 116-22) a paper in which Robert Merton et al. (2013) attempted to estimate the cost of state subsidies to capital markets in the 2007-2008 global financial crisis. At issue here is not just actual state expenditures, but the cost of the state's underwriting expressed as guarantees to bank deposits, financial market interventions to stabilize (or indeed increase) asset prices, and organized bank buyouts. Merton depicts the state's guarantees to financial institutions and markets as having the design attributes of financial options, essentially in the way insurance policies are options. He claimed that if the state had framed these guarantees as options, they could have been priced: logically, there would have been charges to the institutions holding the options (presumably significantly changing their collective risk profile, pricing, and appetite). These options would have also appeared on the books of the state as income on the sale of options, but as financial obligations of the state when the options get exercised. If this options framing were to be applied historically, the option price would have been low during the period from the mid 1980s to 2007 (what Ben Bernanke called the 'great moderation'), but in volatile conditions from 2007 onward, the option price would rise rapidly as risks of volatility rise. But these guarantees were given to financial markets and institutions with no charge. They were, in effect, freely-issued options. So, what if they had been priced 'realistically'? Merton et al. (2013) came up with a back-of-the envelope figure of $17 trillion in assets subject to free state underwriting. Others Meister cites, extending the Merton framing to include bank lending practices that assumed those guarantees and hence underpriced risk, put the figure much higher.

If we project Merton's options framing forward to the Covid years, the value of free state underwriting would/will be enormous: perhaps by a factor of 4, if the growth in central bank quantitative easing is used as a proxy measure. Meister's book was ready for publication before the Covid crisis hit financial markets. There is a less-than-three-page Afterword Meister penned in Spring 2020, pointing to the emerging significance of the financial market liquidity crisis as a result of the global pandemic. But the Afterword was too early in the pandemic for decisive statements and written before the US Federal Reserve led the world in massive asset purchases (i.e., new rounds of quantitative easing).

What can be said three years on from that Afterword is that Meister's analysis of liquidity predicts completely the way that states and central banks responded to the financial liquidity crisis, and the rapid growth of social and economic inequality that was associated with this. On the justice dimension, as Meister has said subsequently, financial market liquidity has emerged as the new 'public good' – surpassing expenditure on public welfare, education, housing, and health, with massive consequences for distributional inequality.

What does this have to do with Meister's arguments in *Justice is an Option*? If I frame this in rhetorical terms for brevity, we might depict financial institutions in the period 2020-2022 as financial terrorists, with sticks of illiquidity strapped to their chests, threatening to blow themselves up, and taking the rest of us with them, unless the state guaranteed market liquidity. And states gave those terrorists exactly what they wanted. The terrorist ransom payment is better known as Quantitative Easing, and because of it, the balance sheet of the Federal Reserve (to reference just one index) reached $8.9 trillion by mid 2022, up from $0.9 trillion in 2007, $2.3 trillion in December 2008, and $4.2 trillion in February 2020.

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Framed the financial options way, financial institutions have held (free) call options on state guarantees of market liquidity. They didn't settle for rolling them over; they exercised those options, triggering in the US $4.7 trillion in direct subsidy plus much more in implicit subsidies, and pushing up financial institution profits in the process. And a new set of options is spontaneously reissued. Imagine $4.7 trillion spent buying up bonds issued to provide social justice!

But here's the thing. Options, as Meister has posed them, could be a path to justice if the struggle for the rights to options can be achieved by oppressed people, and they then agree to roll over their options in return for a stream of payments. But options can also be a path to dramatic injustice when the rich and powerful are granted free options, and they exercise those options to generate massive increases in their incomes and growing wealth inequality. Justice may be an option, but so too is injustice.

Meister may or may not have delivered a reliable financial means of generating increased equality and justice, but his analytical path in getting there has remarkable clarity and insight, coming from incredible multidisciplinary grounding. Politically, he has presented the importance of a financial derivative framing of strategy; an approach that looks for the lethal combination of leverage and illiquidity as the condition of decisive action. As one application of this framing, when we write the financial history of how state policy under Covid led to massive increases in inequality and the financial practices consolidated by this policy implementation, Meister gives us exactly the conceptual framing we need. That's a mighty achievement.

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