

BOOKS

The Price of Time: The Real Story of Interest By Edward Chancellor

Liz Hecht, August 2023

“Usury is defined as the charging of excessive interest. But no word exists to describe too little interest.”

—From *The Price of Time*

During the terrible inflation that gripped Germany in the 1920s, my grandfather was a resident at the hospital in Heidelberg. Every payday, my grandmother would meet him at the gates of the hospital to collect his paycheck before rushing off to buy food because an hour later his paycheck would be worth much, much less.

In considering recent Fed moves to curb inflation with higher interest rates, I often try to remember this bit of family history. I have to keep reminding myself that rising interest rates—painful though they may be in many respects—are designed to keep inflation in check.¹

Because higher interest rates tend to put pressure on stock markets, recent interest rate hikes have become a subject of endless speculation and trepidation. In this environment, Edward Chancellor’s book, *The Price of Time: The Real Story of Interest*, provides invaluable perspective. The book documents the origins of interest and the unintended consequences of excessively low interest rates.



Chancellor defines interest as the time value of money or, simply, the price of time. Initially reviled as a form of theft (demanding back more than has been given), interest became an accepted way to transact across time. “Interest exists,” Chancellor writes early in the book, “because those in possession of capital need to be induced to lend, and because lending is a risky business. It exists because production takes place over time and human beings are naturally impatient.”

During a period when many are worried about excessively high interest rates, Mr. Chancellor’s book provides an encyclopedic, intensively researched, elegantly written history of all the economic woes that can result from excessively low rates. He specifically addresses the evils that can arise from the ultra-low, zero-bound (even negative in some countries) interest rate regime that held sway after the Great Financial Crisis. Here are but a few of the many ills caused by an excess of easy money:

Financial Recklessness. “When the cost of borrowing is low enough, even the most absurd investments can appear viable,” Mr. Chancellor writes. He documents the role of easy credit in diverting valuable resources away from sound investments to corporate zombies and profitless unicorns. “Interest rates set at 2 per cent or less fuel speculative manias, drive savers to make risky investments, encourage bad lending and weaken the financial system ... The large-scale misallocation of resources to loss-making businesses whose profits exist in NeverNever Land is a sign that the cost of capital is too low ... A tale not so much of creative destruction but of capital destruction on a grand scale.”

Reduced Competition and Productivity. “Low interest rates [after the Great Financial Crisis] fueled a takeover boom, reducing competitive pressures by creating monopolies and oligopolies. Since zombies, monopolies and financialized firms tend to invest less, collectively they lower an economy’s innate capacity for growth.” Mr. Chancellor describes how cheap borrowing costs facilitated share buybacks with U.S. firms spending more on buybacks in the post-crisis period than they invested in their operations.² By increasing market concentration, low interest rates may lead to slower growth by creating “barriers to entry which discourage the establishment of new firms and innovation ... a decline in workers’ bargaining power, and falling investment and R&D.”

Greater Income Inequality and the Rise of Populism. By disincentivizing and reducing savings, ultra-low interest rates can promote income inequality. In the U.S., growing pension deficits due to low rates caused some cities and towns to cut public services and fire workers. As the market recovered after 2008, the rich enjoyed most of the spoils while the middle class had most of its wealth tied up in the housing market. After their subprime losses, most American banks increased their interest charges to borrowers with poor credit scores, even as the Fed funds rate was slashed to zero. “Banks with busted credit,” Mr. Chancellor notes, “got bailed out while homeowners with busted credit got foreclosed.” For those who believe that political stability depends on the existence of a strong middle class, such trends are bad news. German Finance Minister Wolfgang Schäuble has blamed the rise of the German nationalist party AfD on the ECB’s negative interest rates.

Mr. Chancellor covers the bizarre topic of negative interest rates in a chapter entitled “Rusting Money.” At this farthest end of absurdity, homeowners in Europe and Japan were receiving rebates on their mortgages—a phenomenon the book describes as being “against human nature” and “possibly the stupidest and certainly the strangest innovation in the history of finance.” “Capital, like employees,” observes the author, “does not work productively without pay.”

A half-century after my grandmother rushed to cash my grandfather’s paycheck, I was trying to land my first job as a freshly minted college graduate. This was in 1980 when the Fed funds rate had climbed close to 19% with the goal of curbing inflation. Because of high interest rates, my job search was a vividly negative experience shared by many of my fellow graduates. I suppose I should have been happy that the Fed was putting the brakes on inflation with higher interest rates. But I was not happy.

Reading this book today begs an important question: Must we forever oscillate between the excesses born of easy money and the constraints of extreme monetary tightening? Endure the massive negatives associated with ultra-low interest rates or suffer through the keen miseries of ultra-high rates? Mr. Chancellor’s book suggests that Central Banks have been “slow to hike during booms but rush to ease during busts.” He also points to Iceland’s strong recovery (“The Icelandic Counterfactual”) after 2008 as being opposite to the U.S. approach in every respect. Iceland “swallowed the bitter medicine of austerity” by letting the banks fail, prosecuting miscreant bankers and sheltering domestic depositors and homeowners at the expense of other creditors.

I am profoundly grateful for a book that sheds light on the forces shaping my family’s experience and my own. *The Price of Time* enhances understanding of how interest rates—“the most important price in a market-based economy”—affect markets, companies and individuals.

1. Modern policymakers view interest as a lever to control the level of consumer prices and the impact of interest rates on inflation is a daily news event. But in the introduction to this book, Mr. Chancellor writes that “influencing the level of inflation is just one of the several functions of interest, and possibly the least important.” He organizes the book’s chapters around the various functions of interest, including “its influence on the *allocation* of capital, the *financing* of companies, the *capitalization* of wealth, the level of *savings*, the *distribution* of wealth, the measurement of *risk* and the regulation of *international capital flows*.”
2. Based on a November 2015 Reuters study of 1,900 listed companies showing that since 2010 aggregate dividends and buybacks amounted to 113 per cent of capital spending.



ALPHA PARTNERS LLC

1062 Oakridge Road South
Park City, UT 84098

www.alphainvestmentmarketing.com

LIZ HECHT

435.615.6862
435.901.1546 (cell)

liz@alphainvestmentmarketing.com