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FİNANSALLAŞAN KAPİTALİZMİN BAŞARISIZLIĞI

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Özet

Küresel ekonomiler 1929 Büyük Bunalımından sonraki en şiddetli krizini yaşamaktalar. Bu çalışma, mevcut krizin, II. Dünya Savaşından sonraki uzun genişleme dönemini izleyen kâr oranlarındaki düşüşlerden kaynaklanan finansallaşma sürecinin bir yansıması olduğunu ileri sürmektedir. Finansallaşma yeni bir kapitalist birikim tarzı olarak görülmektedir. Bugün, finansal kriz olarak görülen olgunun aslında üretimde yaşanan bunalımın bir sonucu olduğu çalışmada yer almaktadır. Kapitalizme özgü bu bunalım içseldir ve depresyondan çıkışın şartı onu bütün sonuçları ile yaşamaktır.

Anahtar Kelimeler: *Düşen Kâr Oranı, Finansallaşma, Global Dengesizlikler*

Jel Sınıflaması:*E11, E44, F32*

THE FAILURE OF FINANCIALISED CAPITALISM

Abstract

The global economy has been living its worst crisis since the 1929 Great Depression. This paper argues that the current global crisis is the reflection of the financialization process which has been derived from the falling profit rates in the world economies following a long expansion period of capitalism after the Second World War. We see the financialization as a new capitalist accumulation process. Today, the phenomenon known as financial collapse is in fact a result of depression in production. The depression peculiar to capitalism is internal and the requirement of escaping from the depression is living it with all results.

Key words: *Falling Rate of Profit, Financialization, Global Imbalances*

Jel Codes: *E11, E44, F32*

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1. Introduction

The global economy has been living its worst and long crisis since the 1929 Great Depression. The build-up of exceptionally large global imbalances in the last few years was an early symptom of the growing risks faced by the global economy. These risks have now materialized. Their internal causes, such as insufficient savings and rising indebtedness in some advanced economies, excessive risk-taking and poor risk management, overly inflated financial markets, and the emergence of asset and real estate price bubbles, now appear obvious.

Some commentators argue that global imbalances are the main reason of the current crisis. Former U.S. Treasury Secretary Henry Paulson argues, for example, that the high savings of China, oil exporters, and other surplus countries depressed global real interest rates, leading investors to scramble for yield and underprice risk[1]. Similarly Bernanke emphasizes that it is impossible to understand the current crisis without reference to the global imbalances in trade and capital flows that began in the latter half of the 1990s[2].

It is true that the global imbalances and the financial crisis are intimately connected, but the current crisis peculiar to capitalism is internal and so it has to be analyzed inside the mechanism of capitalism. A concise say of Churchill, "*The farther backward you can look, the farther forward you are likely to see*", might lead us the way. Following this path, we analyze the last four decades of global economies. In this way, this paper makes the case that the current global breakdown is connected with the falling rate of profit in the past.

First of all, we believe that we have to catch what Marx means by the tendency of the rate of profit to fall. This law of capitalism pictures a tendency and it can appear in a certain stage of a long expansion process. The second section of the study presents when concrete conditions change opposed to rising labour productivity, the tendency to fall materializes. The falling profit rates in 1970s that the advanced economies had faced, have brought about a new capitalist accumulation process. Today, many Marxist economists call this phenomenon as financialization. In third section of the study, we denote financialization as a new capitalist accumulation process and its unfavourable contributions to human life. In fourth section of the study, we show that financialization also enlarges the global imbalances which aggravate the problem. Finally, the results are in concluding part of the paper.

2. The Tendency of the Rate of Profit to Fall

Marx manifests the basis of profitability[*] and the determinative components of its extent with labour process. During the labour process, workers use instruments

[1] Paulson, H., **Financial Times**, January 1, 2009

[2] Bernanke, B. ,"Financial Reform to Adress Systemic Risk", **Speech at the Council on Foreign Relations**, March, 10, 2009

[*]for a brillant analysis of the issue, see Shaikh, Anwar, "An Introduction to the History of Crisis Theories", **US Capitalism in Crisis**, 1978, pp.232-235

of labour (plant and equipment) to transform materials into finished products. The total labour-time required for the finished product is therefore composed of two parts: first, the labour-time implicit in the means of production used up; and the second, the current labour time expended by workers in the labour process itself. Marx calls the first element "constant capital" C, since it reappears in the final product, while he calls the second "value added by living labor", L. The total labor value of any final product is therefore C+L.

The value added by living labor L is composed of two parts, one of which corresponds to the labor-value of the workers' consumption requirements and also represents the necessary part of living labour, v. This is the necessary part because intimates the portion that worker has to take from the final product to come to the job following day. In this way, *v* shows the real wage indeed. The other part corresponds to the labor value of the surplus product *s* which is the basis of capital income under the term of profit. In other words, it is the difference between the value added by living labour L, and the necessary part of it v:

$s = L - v$.

Marx in Capital, calls the ratio s/v "the rate of surplus value" or "the rate of exploitation" and describes this as the hidden basis of capitalist society. Other things being equal, the greater the rate of surplus value the greater the amount of surplus value and hence the greater the profit[3].

Capitalists constantly try all methods of increasing the rate of surplus value, because, it is the unique state of capital accumulation and so being alive in competition circumstances. The rate of surplus value *s/v* can be increased in two ways: directly, by lengthening the working day L so that surplus labor time is directly increased; and indirectly, by lowering the necessary labor-time v so that more of a given working day is spent in surplus labor-time. This latter method of increasing *s/v* requires that either worker's real wages be reduced or that the productivity of their labor be raised so that it takes them less time to produce their means of consumption, or both. However, over time the growing strength of the working class has sharply restricted attempts to lengthen the working day and/or lower the real wage. Thus increasing the productivity of labor has come to be the principal means of raising the rate of surplus value. Finally, mechanization arises as the principle means of raising the productivity of labor and hence lowering unit costs. It is clear that lower unit costs increase the rate of surplus. In mechanization process capitalists seek to perfect the labor process by subdividing it into increasingly specialized and routinized tasks. With capitalist control of the labor process human productive activity is made increasingly mechanical, automatic.

According to Marx, the rising productivity of labor manifests itself in a falling profitability of capital. Marx explains the degree of profitability of capital with the rate of profit. It is clear that capitalists invest money in means of production C and in workers *v*, with the intention of making profit *s*. The amount of profit *s*

[3] Marx Karl, **Capital (1849)**,ElecBook Classics, Vol.3, Ch.3,1998, p.63

relative to their investment C+v is the capitalist measure of success. In other words, it is the rate of profit $s/(C+v)$ which regulates the accumulation of capital[4].

On the other hand, increasing mechanization gives rise to what Marx calls a rising technical composition of capital (C/v). Ever greater masses of means of production and materials are set into operation by a given number of workers. According to Marx, this in turn implies that out of the total labor value C+L of the final product, progressively more comes from the means of production used up and progressively less from living labor. In other words, the

rising technical composition is reflected in value terms as a rising ratio of "dead to living labor," of C to L, that is ($\frac{C}{L}$) $\uparrow$

The surplus value, as we have seen, is the difference between the value added by living labour L, and the necessary part of it v, that is $s = L - v$. Therefore, even if "workers lived on air" ($v = 0$), this means that $s = L$ and $s/(C+v)$ turns into s/C, which represents the ceiling to the rate of profit, while the floor is zero obviously. At the same time, s/C equals to L/C, when specially $s = L$ here. Now, if a rising technical composition does indeed reflect itself as a rising ratio C/L –hence a falling ratio L/C – then the actual rate of profit will be progressively squeezed between a descending ceiling and an unyielding floor, so that it must itself exhibit a downward tendency. This is what Marx means by the tendency of the rate of profit to fall.

In fact, if the real wage of workers were constant, the rising productivity of labor due to mechanization would continually raise s/v. The greater the productivity of labor, the less time it takes workers to produce a given bundle of consumer goods so that a greater portion of a given working day becomes surplus labor-time. Even when real wages do rise, as long as they rise less rapidly than productivity, the rate of surplus value will still rise. It is perfectly possible, therefore, to have both a rising real wage and a rising rate of surplus value[5].

Some economists reject the tendency of the rate of profit to fall by pointing out the tendency of capital-output ratio to be constant over long periods. Since C is the labor value of the means of production, and L is the value added by living labor, their money equivalents are K, the money value of the means of production, and Y, the money value added or net national product. On this basis the capital-output ratio K/Y is examined, and since official statistics indicate that it tends to be constant over long periods, this result is used for refusing the notion of a rising C/L. This is misleading, because economists have to know that the macro data set they use when they analyze the capitalist economy is based on Keynesian theory. Thus, the meaningless results something like above should not be attributed to the arguments of Marxist theory. In brief, Marx's thesis can be examined by tools of Marxist analysis[6].

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[4] Marx, **Ibid**, Vol.3, Ch.9

[5] Shaikh, Ibid, p.234

[6] Ahmet Tonak, "Krizi Anlarken", **Çalışma ve Toplum,** 1, 2009, p.31

Holding to tools of Marxist analysis, for instance Shaikh shows the capital intensity of the U.S. economy in the period of 1947-1985[7]. According to this study, the ratio of capital to production-real wages rises by 103 percent, while the capital-output ratio rises by 56 percent in this period. This augmentation of capital intensity can be explained by the capitalization of production which proves the mechanization process. On the other hand, Shaikh carries this analysis on the rates of profit. While his calculated profit rate is 12 percent for 1947, the number falls to 6 percent for the end of this period.

Mohun (2006) calculates the rates of profit in the US economy even if he uses a different methodology[8]. As seen in Figure 1, there is a visible fall in the rates of profit which reaches to 7,8 percent for the period of 1965-1982.

Figure 1: The pre-tax average rate of profit, USA, 1964–2001. Source: Mohun, 2005

3. A New Capitalist Accumulation Process, Financialization

The capitalist world had lived through the 1950-73 period with unprecedented rates of growth. The world economy had expanded at a rate of 2.9 % per annum over this period and so 1950-73 episode of capitalism is known as the "golden age". The valid international monetary system had a major role in this expansion. The US dollar was tied to the gold standard, and all major currencies were tied to the US dollar via fixed rates of exchange under the Bretton Woods system. The international currency system had been playing a kind of insurance role in international trade. On the other hand, the necessity of reconstruction of the broken down countries after the Second World War was a crucial factor at the appearance of these blinding years. In Keynesian terminology, it can be expressed

[7] Shaikh Anwar, "The Falling Rate of Profit and the Economic Crisis in the U.S.", **The Imperiled Economy, Book I**, **Union for Radical Political Economy**, Gle: Robert Cherry, et al.

[8] Mohun Simon, "Distributive Shares in the US Economy, 1964-2001", **Cambridge Journal of Economics**, September 2006, p.348

that the households' postponed demand during the war was turned into an effective demand by leadership of the governments[9].

By using the central role of governments on the demand side, it was impossible to keep going capital accumulation in the long run with Keynesian policies. It was true that Keynesian solutions lengthened the span of these happy years; however, these applications could not prevent the depression of 1970s. After reaching to the boundaries of purchasing power, increasing the demand artificially had only one result, inflation[10]. Thus, the capitalist world had the excessive production and also the inflation issues together.

As we see in Figure 2, a slowdown in the rate of global demand growth and an increasing intensity of competition in key product markets that caused a downturn in nonfinancial corporations' profit rates in 1970s[11] have brought about a major change on their behaviors. Nonfinancial corporations have started to substitute the financial profits for the real incomes. A new business-life has begun with the explosion of financial trading with a myriad of new financial instruments. This new phenomenon is defined as "financialization" that refers to a "pattern of accumulation in which profit making occurs increasingly through financial channels rather than through trade and commodity production[12]. On the other hand, Epstein describes the term financialization as, the increasing role of financial motives, financial markets, financial actors and financial institutions in the operation of domestic and international economies[13].

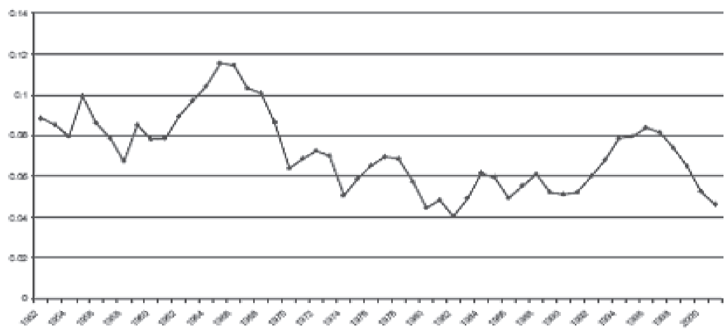

Figure 2:Nonfinancial Corporation Profits before Taxes as a Percentage of Net Worth in the US, 1952-2000, Source: Crotty, 2003

[9] Shut Harry**, The Trouble with Capitalism: An Enquiry into the Causes of Global Economic Failure** , Zed Books Ltd., UK, 1998, p.33

[10] Shut, **Ibid**, p.34

[11] Crotty, J. "The Neoliberal Paradox: The Impact of Destructive Product Market Competition and Impatient Finance on Nonfinancial Corporations in the Neoliberal Era", **Review of Radical Political Economics**, Volume 35, No.3, Summer 2003, p. 273

[12] Krippner Greta, "The Financialization of the American Economy", **Socio-Economic Review**, 3,2, May, 2005, p.174

[13] Epstein Gerald A., **Financialization and the World Economy"**, UK, Edward Elgar Publishing, 2005

Paul Sweezy underlines the financialization of the capital accumulation process as the main force lifting economic growth since the 1970s, in Monthly Review[14]. By using this view, Foster shows the transformation in the system that the new situation has brought about which reflected in the rapid growth on financial profits as a percent of total profits[15]. As seen in Figure 3, the financial profits have a bigger part in total profits especially since 1980s, year after year.

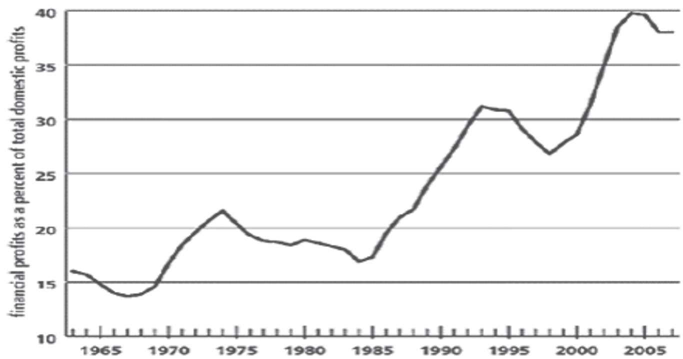

Figure 3: Financial Profits as a Percent of Total Profits in Advanced Economies
Source: Foster, 2008

In the meantime, the short termist and highly volatile expansionary nature of hot finance is vividly dominated with the advent of financialization. Banking and finance also have been transformed during the last three decades. Banks have turned their attention to individuals while becoming more distant from industrial and commercial capital. We have seen the increasing penetration of formal finance into the transactions of ordinary life: housing, pensions, insurance, consumption and so on. In addition, the crisis has revealed the extent to which contemporary finance relies on drawing profits directly from the personal income of working people and others across society. This is direct exploitation, a characteristic feature of financialized capitalism[16]. It is clear, while nonfinancial corporations move away real returns, they are obliged to get financial profits, and thus, firms are disappeared from the focus of banking sector.

We live in a world that every business contracts are purchased or sold. Thus, financialization has caused a hazardous thing, which is securitization of nearly everything related to business-life. Banks must hold significant amounts of own capital (partly due to Basle regulations) to support their loans (such as mortgages). On the other hand, holding own capital is expensive, and hence banks have a strong

[14] Sweezy Paul, "More (or Less) on Globalization", **Monthly Review,** Vol.49, No.4 September 1997 :3

[15] Foster, John.B. ,"The Financialization of Capital and the Crisis", **Monthly Review**, Vol.59, No 11, April 2008

[16] Lapavitsas, C. , "Financialised Capitalism: Direct Exploitation and Periodic Bubles", mimeo, University of London, May 2008

incentive to take loans off the balance sheet, sell them to others in the form of securities, and earn fees by using new methods of financial-engineering. In this way securitization has become a new source of systemic instability. As Stiglitz emphasizes, if the private incentives are not well aligned with social returns, the result can be excessive risk taking, excessively shortsighted behavior, and distorted innovation. For example, while the benefits of many of the financial-engineering innovations of recent years -options, swaps, swaptions, specialized investment vehicles, collateralized debt obligations, variable interest entities and so on- are hard to prove, let alone quantify, the costs associated with them -both economic and social- are apparent and enormous[17].

Moreover, we saw a number of tricks of some financial instutions such as Lehman Brothers in the current crisis. It was announced nearly two years after the bankruptcy that Lehman employed off-balance sheet devices, known within Lehman as "Repo 105" and "Repo 108" transactions, to temporarily remove securities inventory from its balance sheet, usually for a period of seven to ten days, and to create a materially misleading picture of the firm's financial condition in late 2007 and 2008. It is clear that the uncontrolled financial system allows this type of cunning.

Increasing financialization with stock, bond and derivatives markets is commonly misleading on pricing the financial instruments. Thus, there exists an increasing financial capital by itself. Karl Marx defines this capital which is not related with real production as "fictitious". *"With the development of interest-bearing capital and the credit system, all capital seems to double itself, and sometimes treble itself, by the various modes in which the same capital, or perhaps even the same claim on a debt, appears in different forms in different hands. The greater portion of this "money-capital" is purely "fictitious". All the deposits, with the exception of the reserve fund, are merely claims on the banker, which, however, never exist as deposits".*[18]

Central banks as the pre-eminent economic policy-making institutions unfortunately overlook this financial expansion. They have focused on inflation targeting for years, while casting a benign eye on the speculative excesses of finance. For instance, when the growth rates in Turkish economy were falling down distinctly before the global crisis, the Central Bank of the country insisted on the high interest rates for the sake of price stabilization. Therefore Turkish economy lived negative growth rates in the last quarter of 2008 and in the first half of 2009.

In addition to these, excessive risk taking has brought about a considerable rising on indebtedness. In debt markets, the outstanding stock of emerging market debt has grown to over $7 trillion, compared to under $2 trillion in the mid- to late 1990s[19].

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[17] Stiglitz Joseph, "Harsh Lessons We May Need to Learn Again", **in the China Daily**, December, 31, 2009

[18] Marx, Ibid, Vol.3, Ch.29, pp 631-632

[19] Peiris, J. Shanaka, "Foreign Participation in Emerging Markets' Local Currency Bond Markets", **IMF Working Paper** , No. 10/88, Washington, 2010

Eventually, financialization has also altered relations among countries in the world market. Expanding international flows of capital have forced developing countries to hold vast international reserves in recent years (see Table 1). The result has been net lending by the poor to the rich in the world economy, particularly to the USA. On the one hand, private capital has flown into developing countries, earning sizeable returns; on the other, even larger funds from developing countries have flown into the developed countries, earning little. Most of the benefits were drawn by the USA as issuer of the main form of international means of payment. Thus, financialization has increased the complexity of economic life[20].

Table 1: Reserve Accumulation $ bn

Reg/Year	2003	2004	2005	2006	2007	2008	2009	2010	2011
Developing Asia	670.3	934.6	1,156.1	1,489.6	2,128.9	2,534.1	3,077.9	3,669.1	4,380.5
Latin America and the Carib.	195.4	220.6	255.3	310.3	445.1	497.3	547.8	651.3	771.5
Russia	73.8	121.5	176.5	296.2	467.6	412.7	417.8	454.5	527.4
Mid. East and North Africa	230.3	293.8	434.1	595.5	836.9	999.5	1,001.2	1,104.0	1,249.0
Sub-Sah. Africa	39.1	60.7	80.9	114.0	144.8	155.4	156.4	159.4	193.2

Source: IMF, World Economic Outlook 2011, p.204

So far, we see that the falling rates of profit orientate the firms to substitute the financial profits for the real incomes and thus, this fact gives rise to financialization. The role of financialization on the creation of bubbles in financial markets and effects of these on the outbreak of the current crisis are clear. Moreover, global imbalances have increased since 1990s and this phenomenon has raised the risks on the global world by accompanying the extending financialization. Henceforth, our focus is on the global imbalances and their contribution on the current crisis and on its consequences.

4. The Significance of Global Imbalances on the Current Crisis

As Bernanke emphasizes, it is impossible to understand the current crisis without reference to the global imbalances in trade and capital flows that began in the latter half of the 1990s[21]. Global imbalances or, more precisely, global current account imbalances refer to the large current account deficits and surpluses that have emerged in the world economy during the last ten years. For the most part, the imbalances have been heavily concentrated among a small group of regions and countries, and until recently have displayed an unusually high degree of persistence. The imbalances have centered on the large current account deficits of the United States, which peaked at close to 6 percent of gross domestic product (GDP) in 2006,

[20] Lapavitsas, **Ibid**

[21] Bernanke, **Ibid**

and the corresponding surpluses in the rest of the world, in particular developing Asia, Middle East, and Russia. By definition, a current account deficit (surplus) is equal to negative (positive) net savings. Therefore, it is conceptually useful to view persistent global imbalances as the continuous financing of US consumption with the net savings of the surplus countries[22].

Table 2: Current Account Balances in Selected Countries/Regions

Selected Countries	2002	2003	2004	2005	2006	2007	2008	2009
United States	-459.1	-521.5	-631.1	-748.7	-803.5	-726.6	-706.1	-418
Euro area	47.9	42.9	116.9	45.3	47.6	47.3	-106	-43.8
Japan	112.6	136.2	172.1	165.7	170.4	211.0	157.1	141.7
Developing Asia	66.9	85.0	92.9	167.5	289.2	414.7	424.1	319.0

Source: IMF, World Economic Outlook 2010, p.172

Table 2 shows the large current account deficits of the US, increasing year by year and the large current account surpluses of developing Asia especially, rising consistently. On the other hand, Figure 4 pictures the rising negative net savings or bursting consumption expenditures of the US which financed by the current account surpluses of the developing world.

Figure 4: Personal Consumption Expenditures as a share of GDP in the US, Source: Economic Report of the President, 2010

As Jagannathan et al emphasizes, China's GDP, which was less than 12 percent of US GDP till 2000, more than doubled in relative size to 25 percent of US GDP by 2007 (see Figure 5). The growth in Chinese savings relative to US savings has been even more dramatic. As can be seen from the same figure, Chinese savings was less than a third of US savings till 2000 but grew to be 130 percent of US savings by 2007. These results indicate that the origin of global imbalances is mainly based on the current account and savings differences between these two large economies[23].

[22] Adams, C. and Park D. "Causes and Consequences of Global Imbalances: Perspective from Developing Asia", **Asian Development Review**, vol. 26, no. 1, 2009, p.19

[23] Jaganatthan Ravi. et al, **Why are we in a Recession? The Financial Crisis is the Symptom not the Disease**, NBER Working Paper, No:15404, October 2009

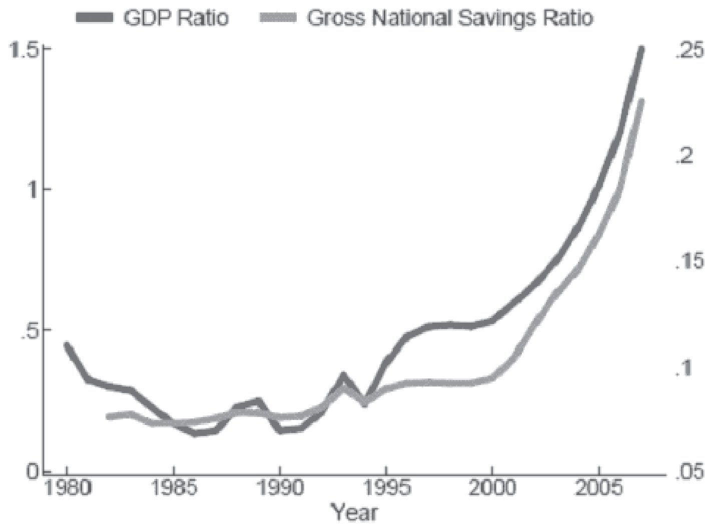

Figure 5: The Ratios of China and the US Gross National Savings (left scale) and Nominal GDP (right scale) Source: Jagannathan et al, 2009

According to balance of payments identity in macroeconomics, if you know that you can finance your current account deficit forever, you consume more just like the US to do. It is clear that the uncontrolled capital flows from the developing world invite the matter. In fact, the US' ability to finance macroeconomic imbalances through easy foreign borrowing allowed it to postpone tough policy choices. Foreign banks' appetite for assets that turned out to be toxic provided one ready source of external funding for the U.S. deficit. Inflated asset prices allowed financial actors to argue that their balance sheets were strong. Hence, the whirlpool enlarged and the asset bubble exploded as we know[24].

Now we think from the reverse side; when the country -the US- knows that it can not finance its external deficits, and then it is not able to attend to consume so much. In this manner, the country starts to save more. Similarly when the other country which is the main component of the global imbalances -China- knows that it is impossible to export the financial surpluses to the world at the same levels, it starts to consume more. Eventually, if the global world decides to apply capital controls, global imbalances will become less. Also, this will create a new state for reduction of financial risks. Otherwise, if the financialization degree of the world increases, this will carry with growing global imbalances.

As we see in the current crisis, theories advocating financial deregulation and opening markets have shown their ineffectiveness. Without adequate regulation, they are prone to excess. As Stiglitz mentioned, "we saw why Adam Smith's

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[24] Obstfeld, M. and K. Rogof, "Global Imbalances and the Financial Crisis: Products of Common Causes", **Federal Reserve Bank of San Francisco Asia Economic Policy Conference**, Santa Barbara, CA, October 18-20, 2009, p.36

invisible hand often appeared invisible: it was not there".[25] The crisis clearly demonstrates that the state has a role to play in financial markets for new regulations.

5. Conclusion

This paper argues that the current global crisis is the reflection of the financialization process which has been derived from the falling profit rates in the world economies following a long expansion period of capitalism after the Second World War. Financialization also enlarges the global imbalances. In a financialized world, it is misleading to see it feasible to finance the deficit forever. Hence, sustainability of the present international financial system is uncertain. Today, the phenomenon known as financial collapse is in fact a result of depression in production. It is due to capitalism and so it is internal. The requirement of escaping from the depression is living the depression with all results. This means, when the capital starts loosing its value, it is the time to leave. If capitalist economies prevent bankruptcies, we see that problems get more difficult. Monetary precautions could not solve the problems, only translate them to the future but make them harder this time.

As we see in the current crisis, theories advocating financial deregulation and opening markets show their ineffectiveness. Without adequate regulation, they are prone to excess. As we know, the newest threat to the financial system is growing sovereign risk especially in euro area. If anxious investors worry about long-run government solvency, a decline occurs on sovereign bond prices in advanced economies and so still-recovering banks, which are major investors in government debt, could face new hits to the value of assets on their balance sheets. Rising interest rates on public debt could also flow through to the private sector raising borrowing costs for businesses, consumers, and banks. At the end of a temporary recovery, it is possible to live another crash, because, so much financialization generates worse expectations.

[25] Stiglitz, Ibid

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