

The nature of economic crises in the 21st century

Michael Roberts

Marx Memorial Library

October 2019

Why did we not see it coming?

- *“Your Majesty, the failure to foresee the timing, extent and severity of the crisis and to head it off, while it had many causes, was principally a failure of the collective imagination of many bright people, both in this country and internationally, to understand the risks to the system as a whole.”*

British Academy, “The Global Financial Crisis—Why Didn’t Anybody Notice”?, *British Academy Review* (July 2009)

Neoclassical economics

- The doyen of the neoclassical school, Robert Lucas, confidently claimed back in 2003, that “*the central problem of depression prevention has been solved*”.
- And leading Keynesian, Oliver Blanchard, soon chief economist at the IMF, told us as late as in 2008 that “*the state of macro is good*”!

Nobel prize winners!

- Eugene Fama: *“We don’t know what causes recessions. I’m not a macroeconomist so I don’t feel bad about that! We’ve never known. Debates go on to this day about what caused the Great Depression. Economics is not very good at explaining swings in economic activity. If I could have predicted the crisis, I would have. I don’t see it. I’d love to know more what causes business cycles.”*

What is the common element?

- In his farewell speech to the Association of American Economists, US Fed chair at the time of the Great Recession Ben Bernanke concluded:
- *“The task is complicated by the reality that every financial panic has its own unique features that depend on a particular historical context and the details of the institutional setting.”*
- What we need to do is to “strip away the idiosyncratic aspects of individual crises, and hope to reveal the common elements” of these ‘panics’. Then we can “identify and isolate the common factors of crises, thereby allowing us to prevent crises when possible and to respond effectively when not.”

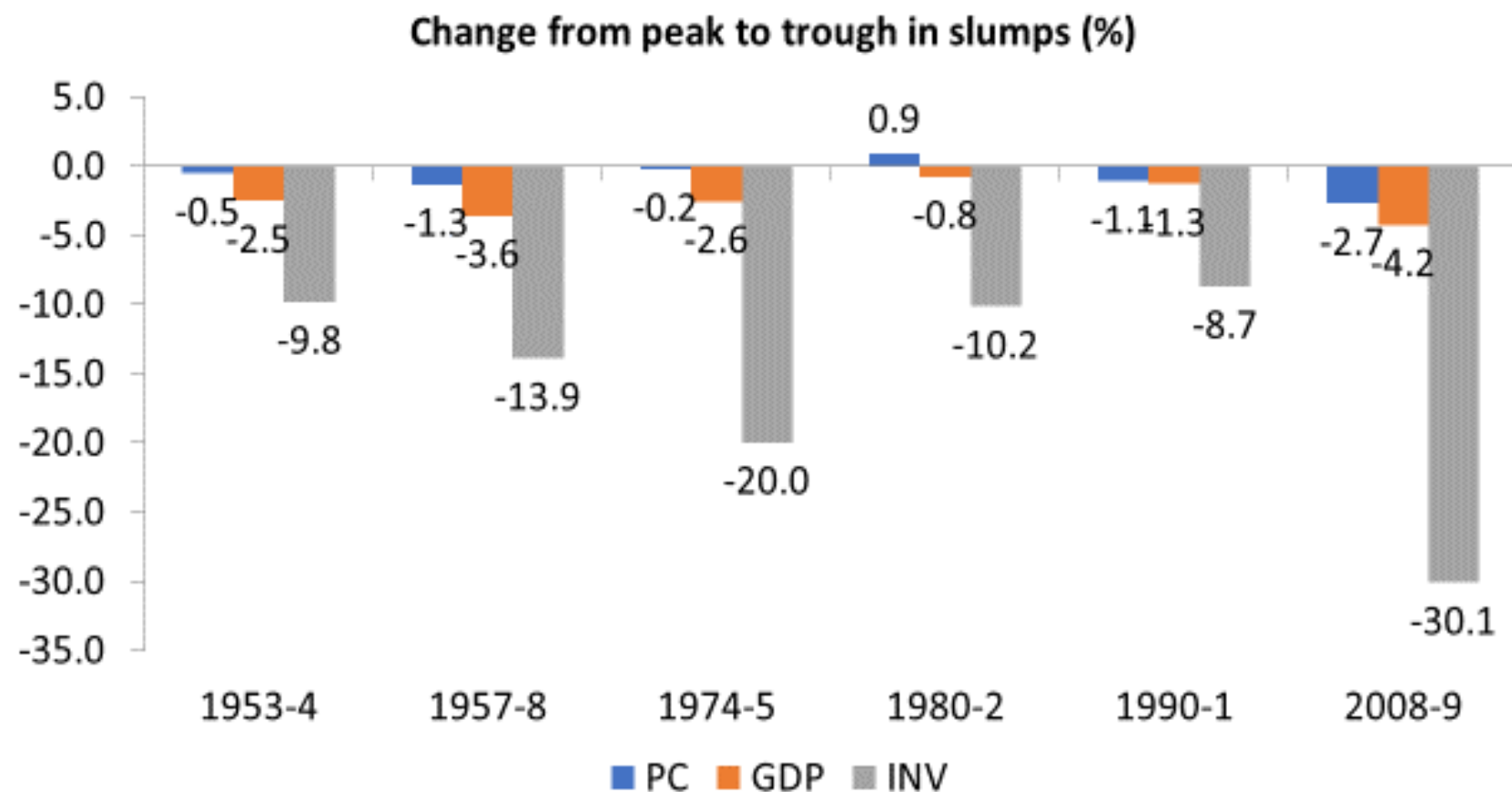
Crises: not random shocks

- In the case of crises, every slump in capitalist production may appear to have a different cause.
- The 1929 crash was caused by a stock market collapse; the 1974-5 global slump by oil price hikes; the 2008-9 Great Recession by a property crash.
- And yet, crises under capitalism occur regularly and repeatedly. That suggests that there are underlying general causes of crises to be discovered. Capitalist slumps are not just random events or shocks.

Keynes: a technical malfunction

- “Keynesian economics rests fundamentally on the proposition that.. depressions are essentially a technical malfunction....
- “As the Great Depression deepened, Keynes famously declared that “we have magneto trouble” —i.e., the economy’s troubles were like those of a car with a small but critical problem in its electrical system, and the job of the economist is to figure out how to repair that technical problem.”
- Paul Krugman,
<http://www.nybooks.com/articles/archives/2013/jun/06/how-case-austerity-has-crumbled>

But investment, not consumption, drives crises



Profits or investment?

Macro identities

- (NI) National income = (NE) national expenditure
- $NI (\text{Profits} + \text{Wages}) = NE (\text{Investment} + \text{Consumption})$
- So $\text{Profit} + \text{Wages} = \text{Investment} + \text{Consumption}$.
- Now if we assume that wages are all spent on consumption and not saved, then
- $\text{Profits} = \text{Investment}$

Which calls the tune?

Preposterous – back to front

- “Nothing can restore business profits that does not first restore the volume of investment” - Keynes
- “It is investment that calls the tune.” - Minsky
- Workers spend what they earn, while capitalists earn what they spend.” – Kalecki
- **No! Workers spend what they earn (wages)
capitalists spend what they exploit (profits)**

Back to Front

- Profits depend on investment - Keynesian
- Investment depends on profit - Marxist.
- And profit depends on the exploitation of labour power and its appropriation by capital.
- An objective causal analysis based on a specific form of class society (Marx) or individual behaviour (Keynes)

Denial of the role of profit

- What is wrong with all these explanations of crises is a denial of any role for profit in what is after all a profit economy where businesses are money-making machines – and where meeting some people's needs for goods and services is merely a necessary, but not sufficient, side-effect.
- If profit is not relevant to crises but only 'effective demand', a theory of crisis now depends on spending, particularly consumer spending, the largest segment of effective demand.

The law of profitability

- In Marx's view, "the most important law of political economy" was the tendency of the rate of profit to fall.
- The crisis of 2008-9 like other crises has an underlying cause based on the contradictions between accumulation of capital and the tendency of the rate of profit to fall under capitalism.
- That contradiction arises because the capitalist mode of production is production for value not for use. Profit is the aim, not production or consumption.
- The underlying contradiction between the accumulation of capital and falling rate of profit (and then a falling mass of profit) is resolved by crisis, which takes the form of collapse in value, both real and fictitious value.

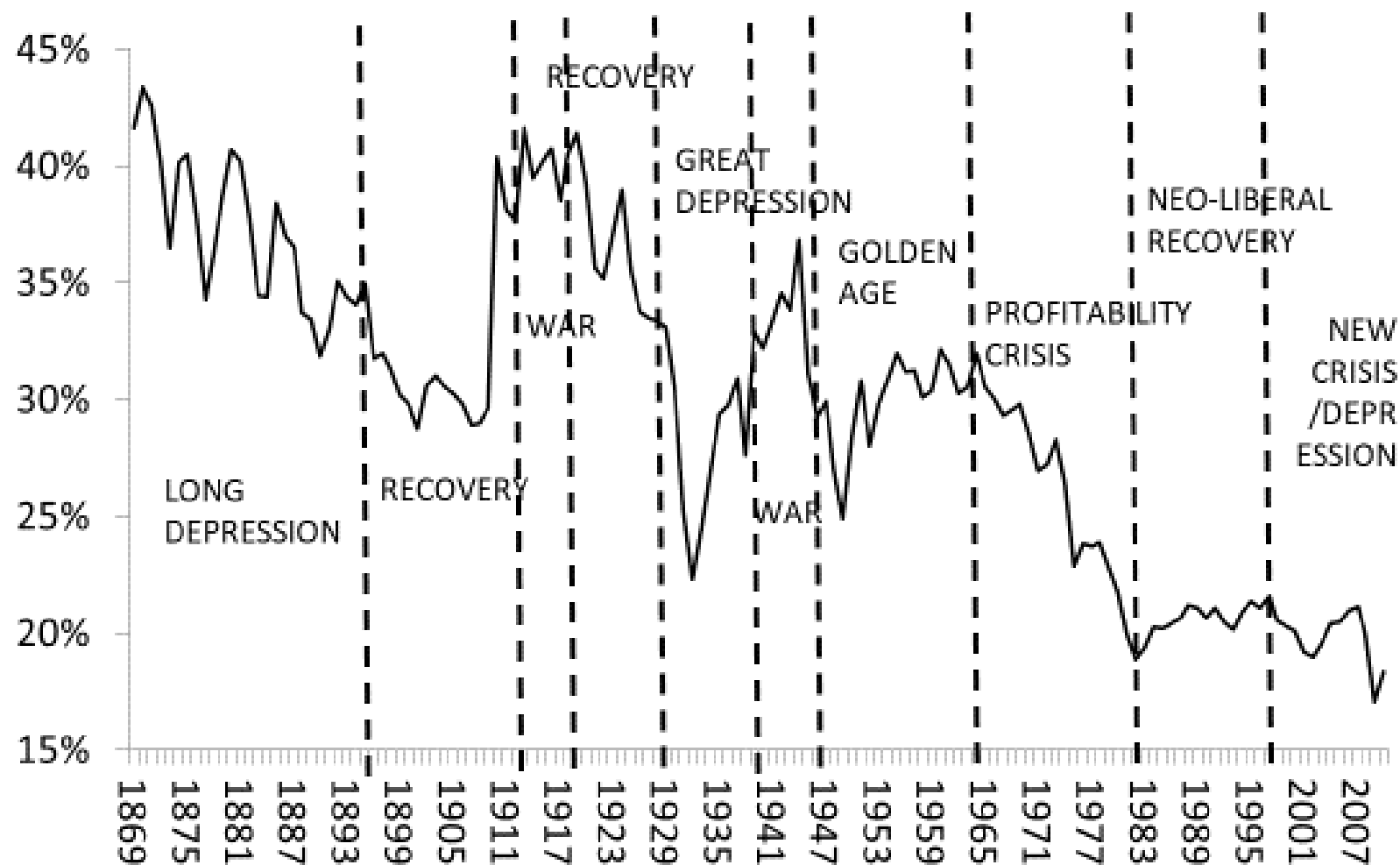
Tendency and countertendency

- The 'law as such' is a law of a tendency. There is a tendency for the rate of profit to fall over a long period of time and this tendency will overcome any counteracting factors eventually.
- But the law also says that, for a period, and especially after a major slump that devalues existing capital, counteracting factors can rule – namely
 - through a rising rate of surplus value,
 - higher profits from overseas
 - the cheapening of constant capital through new technology, among others.
- That was the experience of the so-called neo-liberal period from 1982 to the end of 20th century.

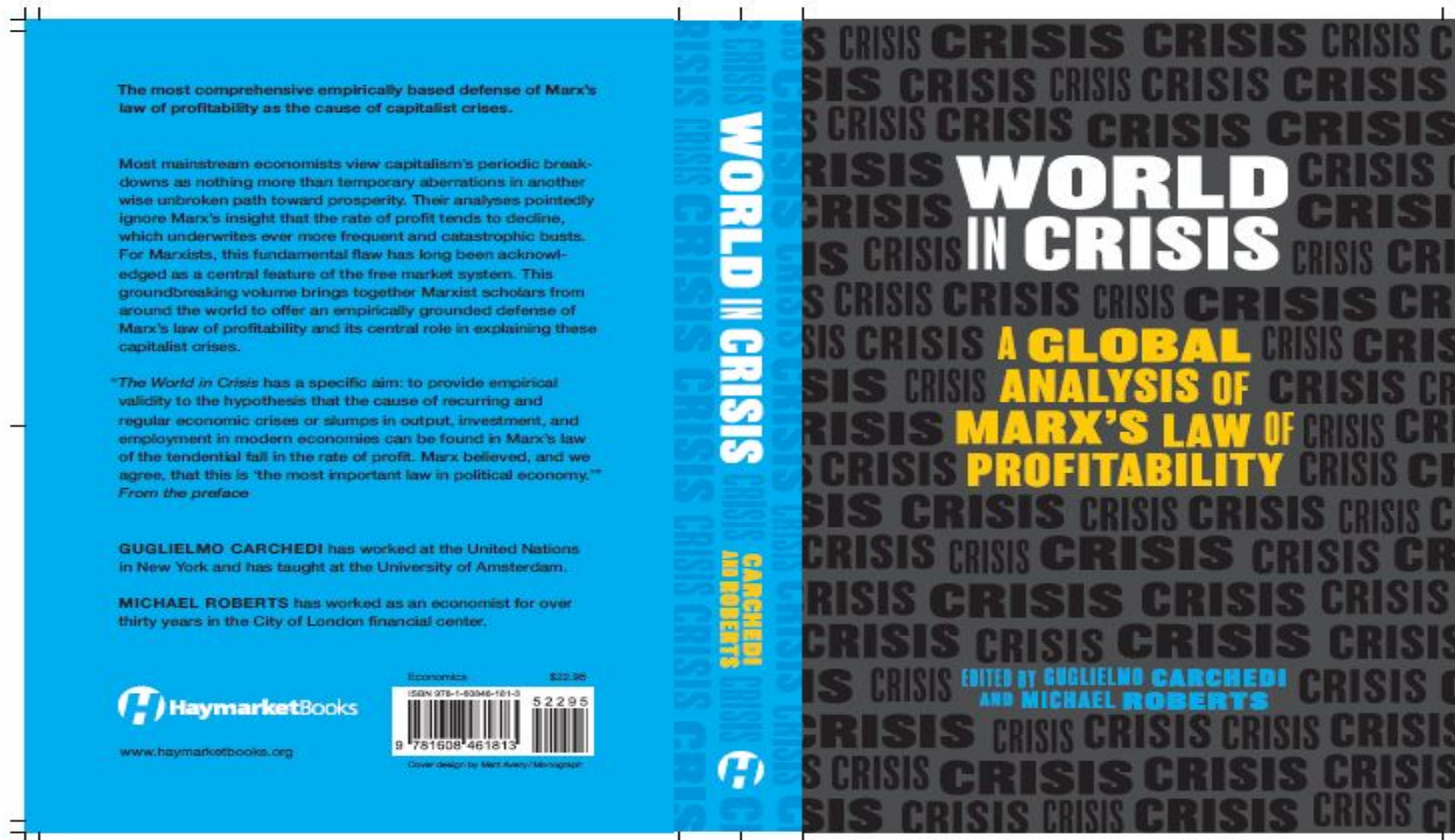
From the law of accumulation to the law of profitability

- 1) Displacing living labour from production depresses the average rate of profit, since only living, productive wage-labour creates surplus-value (the social substance of profit, rent and interest).
- 2) The tendency for the rate of profit to fall is offset by counteracting factors, but these factors cannot entirely negate 'the law as such'.
- 3) Economic crises create conditions for restoring profitability (up to a point), but also tend to become more acute over time. The secular trend of the rate of profit is downward, barring a massive 'slaughtering' of capital values.
- 4) The fundamental issue in capitalist economic crises is not a problematic 'distribution of income,' but insufficient production of surplus value.

A world rate of profit



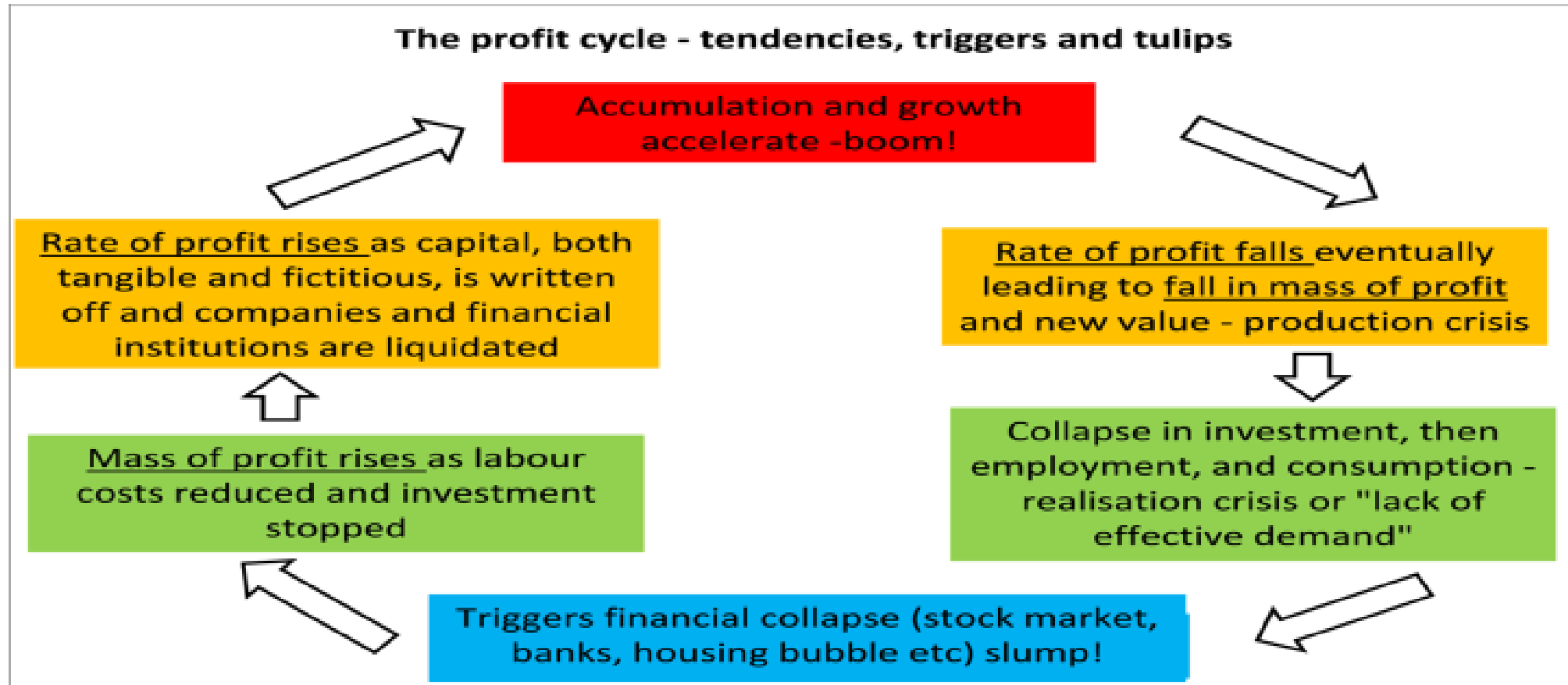
Global evidence



Secular or cyclical?

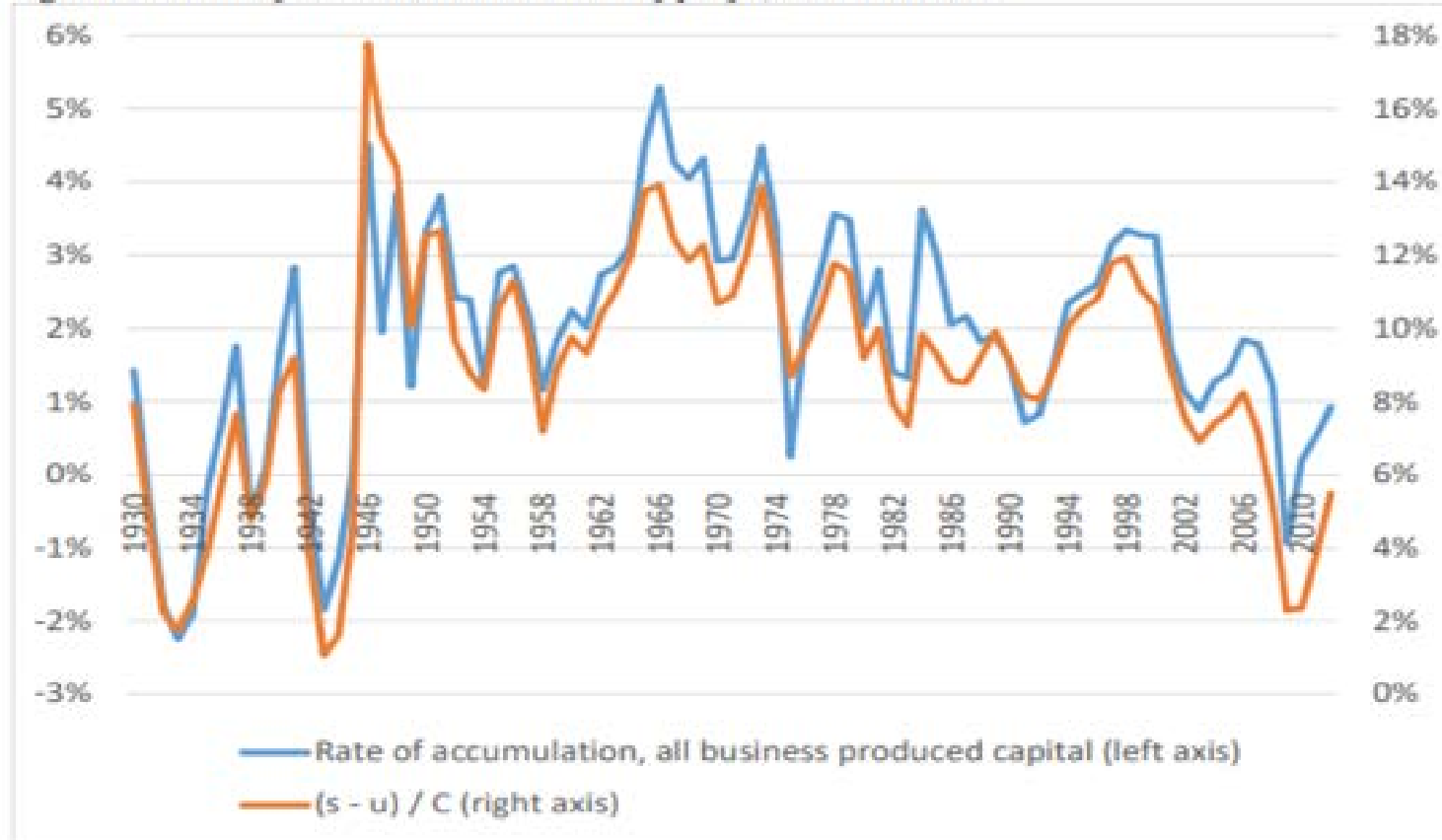
- Is the law of the tendency of the rate of profit to fall just a long-term secular tendency?
- Is the law of the tendency of the rate of profit to fall solely an explanation of crises and booms and slumps?
- IT IS BOTH

The profit cycle

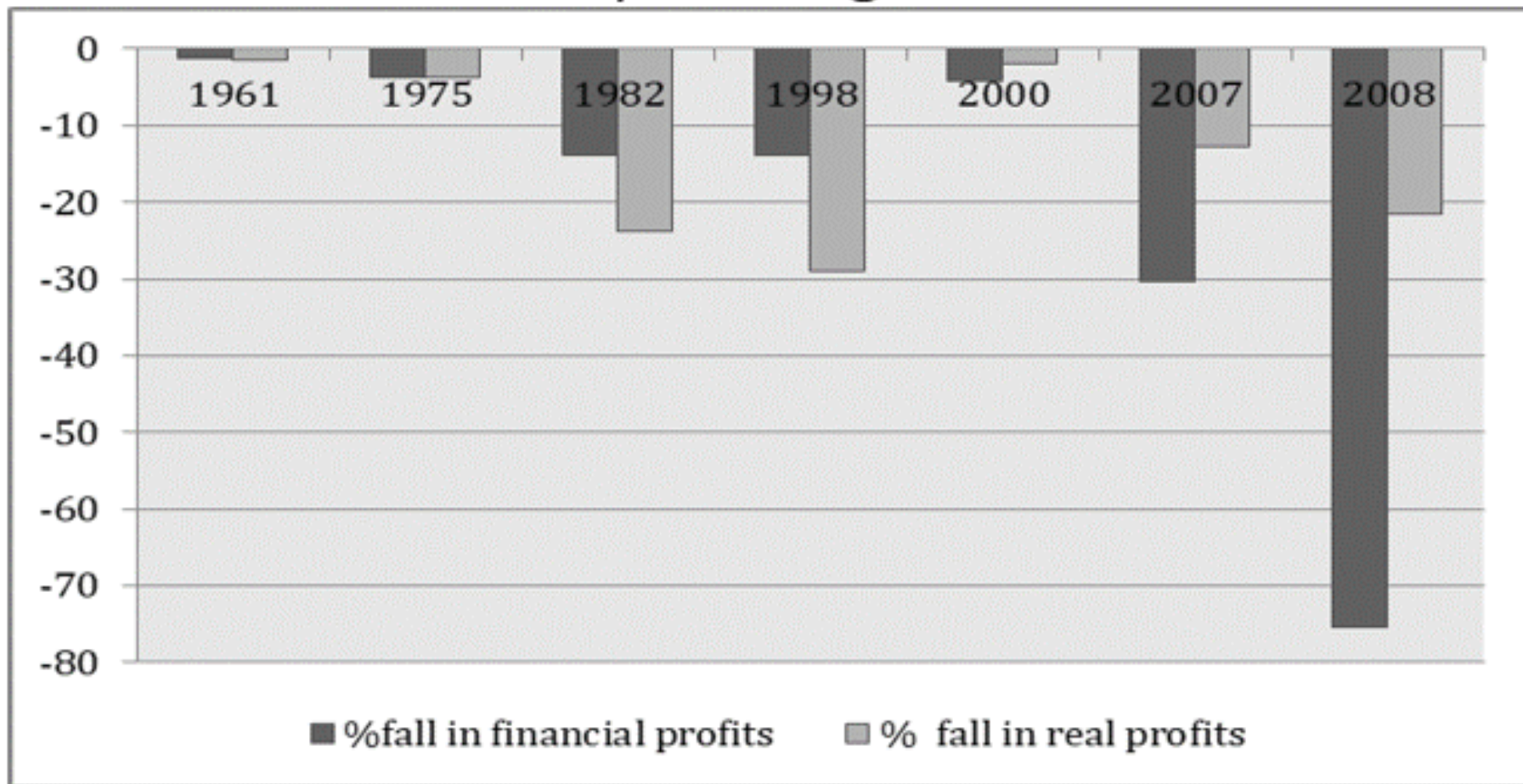


Close correlation: profit and investment

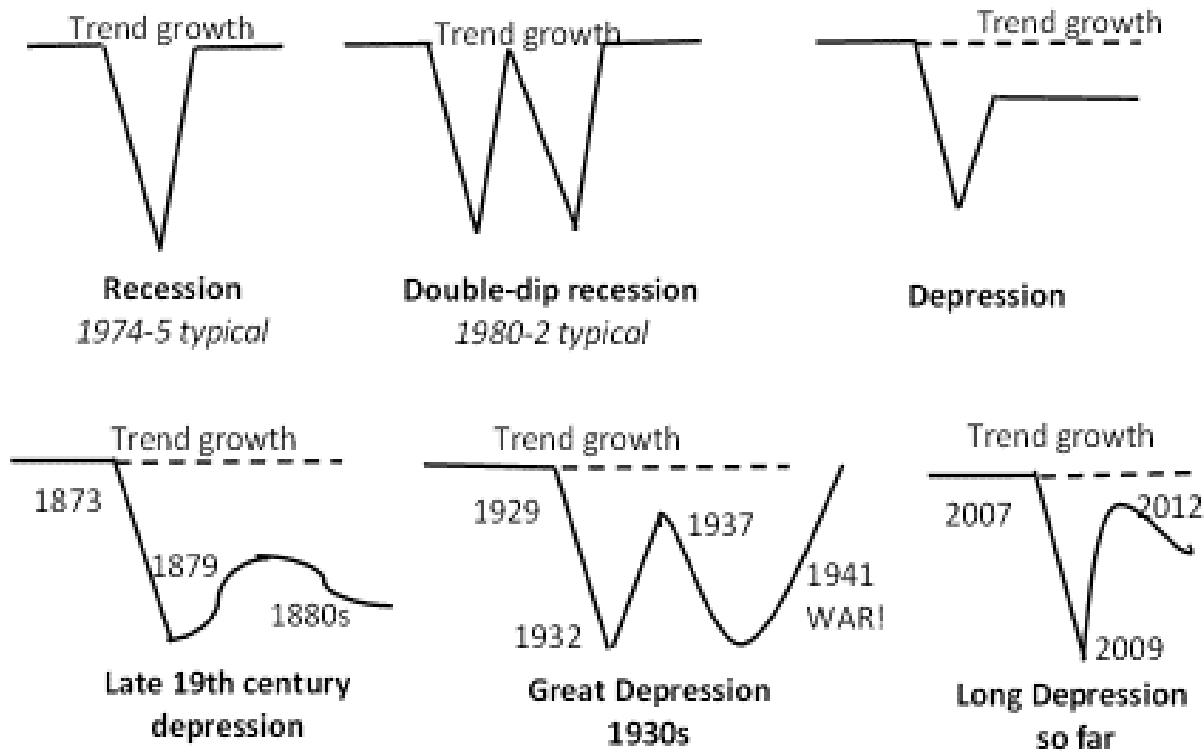
Figure 13: Rate of accumulation vs. rate of profit, all businesses



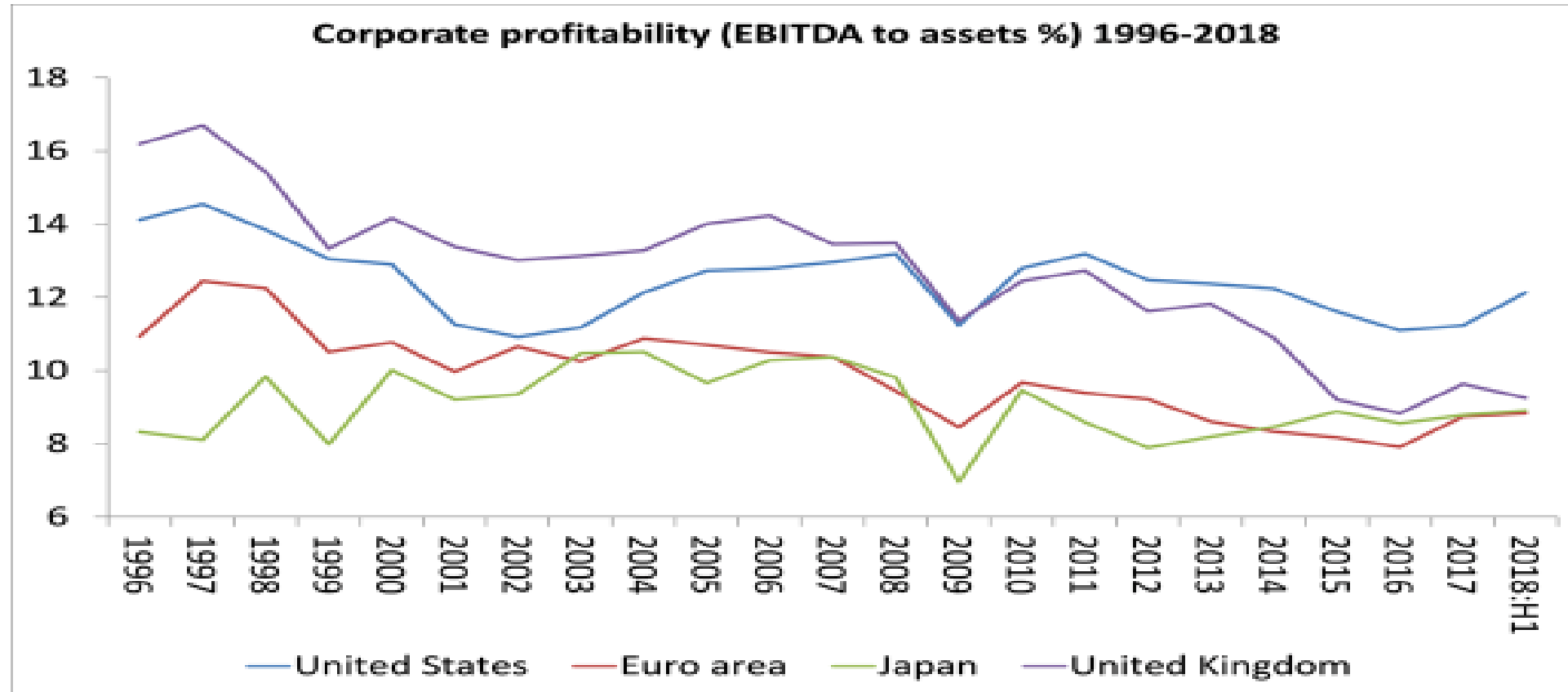
What are financial crises, what causes them and when do they emerge?



Depressions and recessions



Corporate profitability falls

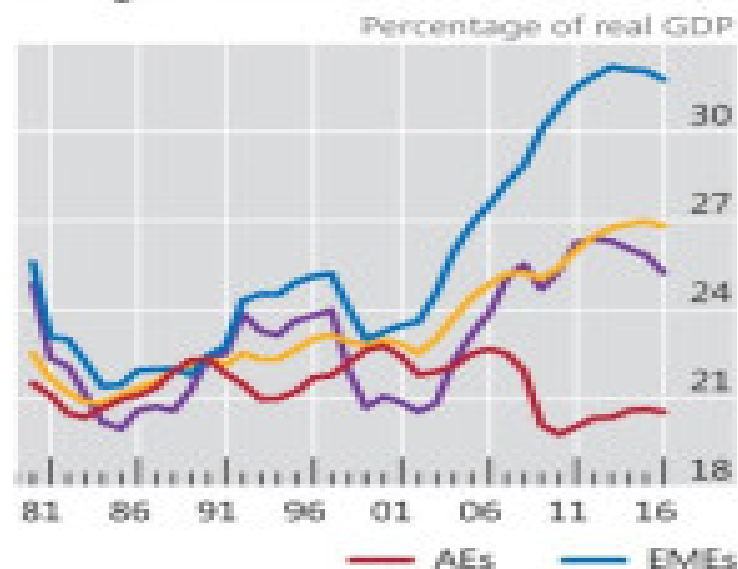


Zombie capital

Investment, productivity and resource misallocation

Graph III.8

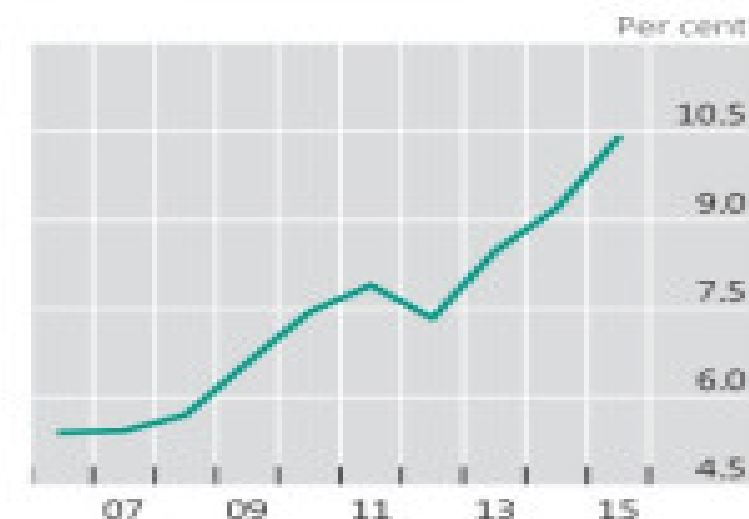
Real gross investment¹



Labour productivity growth^{1, 2}



Share of zombie firms³

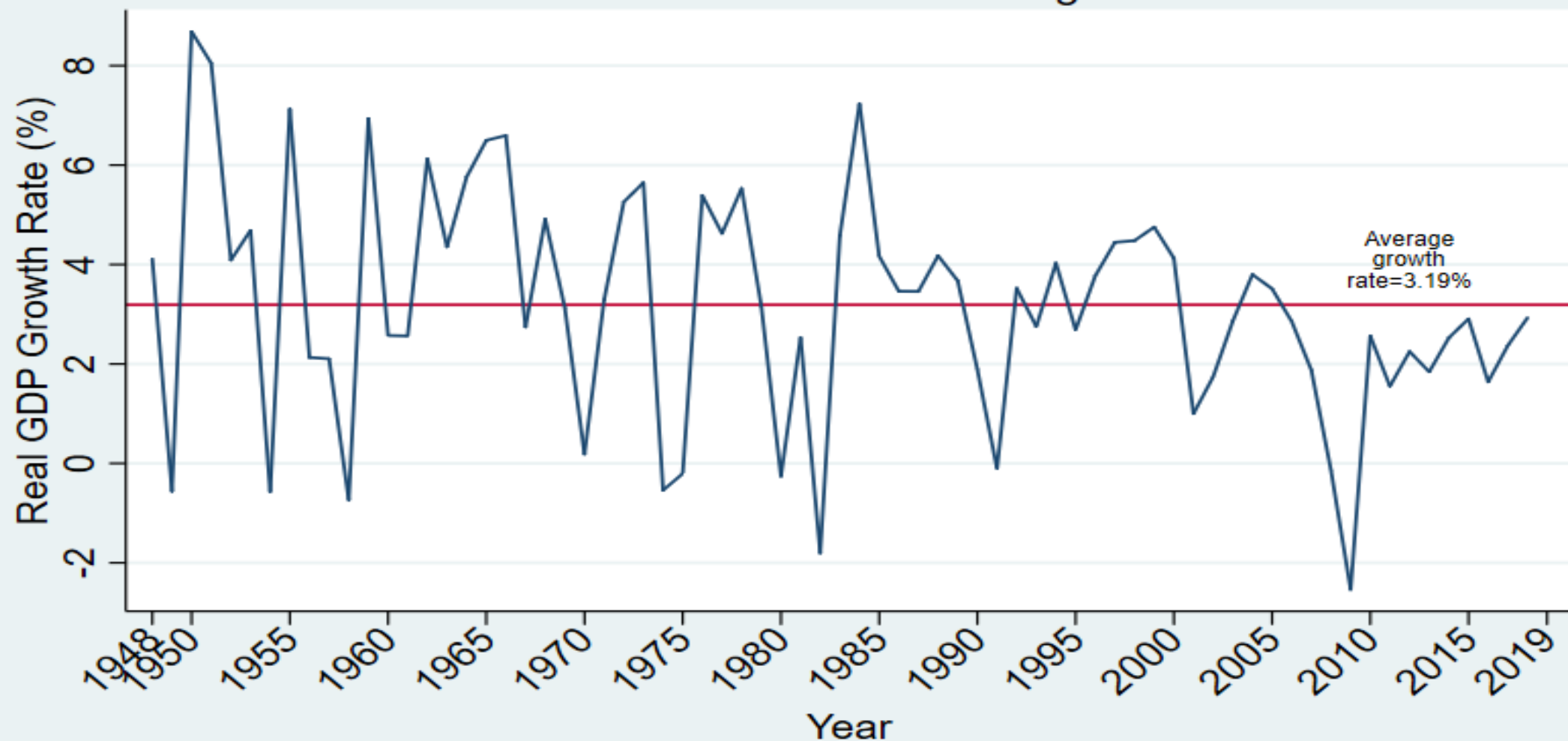


¹ Weighted averages based on rolling GDP and PPP exchange rates. ² Per person employed. ³ Zombie firms are defined as listed firms with a ratio of earnings before interest and taxes to interest expenses below one, with the firm aged 10 years or more. Shown is the median share across AU, BE, CA, CH, DE, DK, ES, FR, GB, IT, JP, NL, SE and US.

Sources: European Commission, AMECO database; IMF, *World Economic Outlook*; Datastream Worldscope; The Conference Board; BIS calculations.

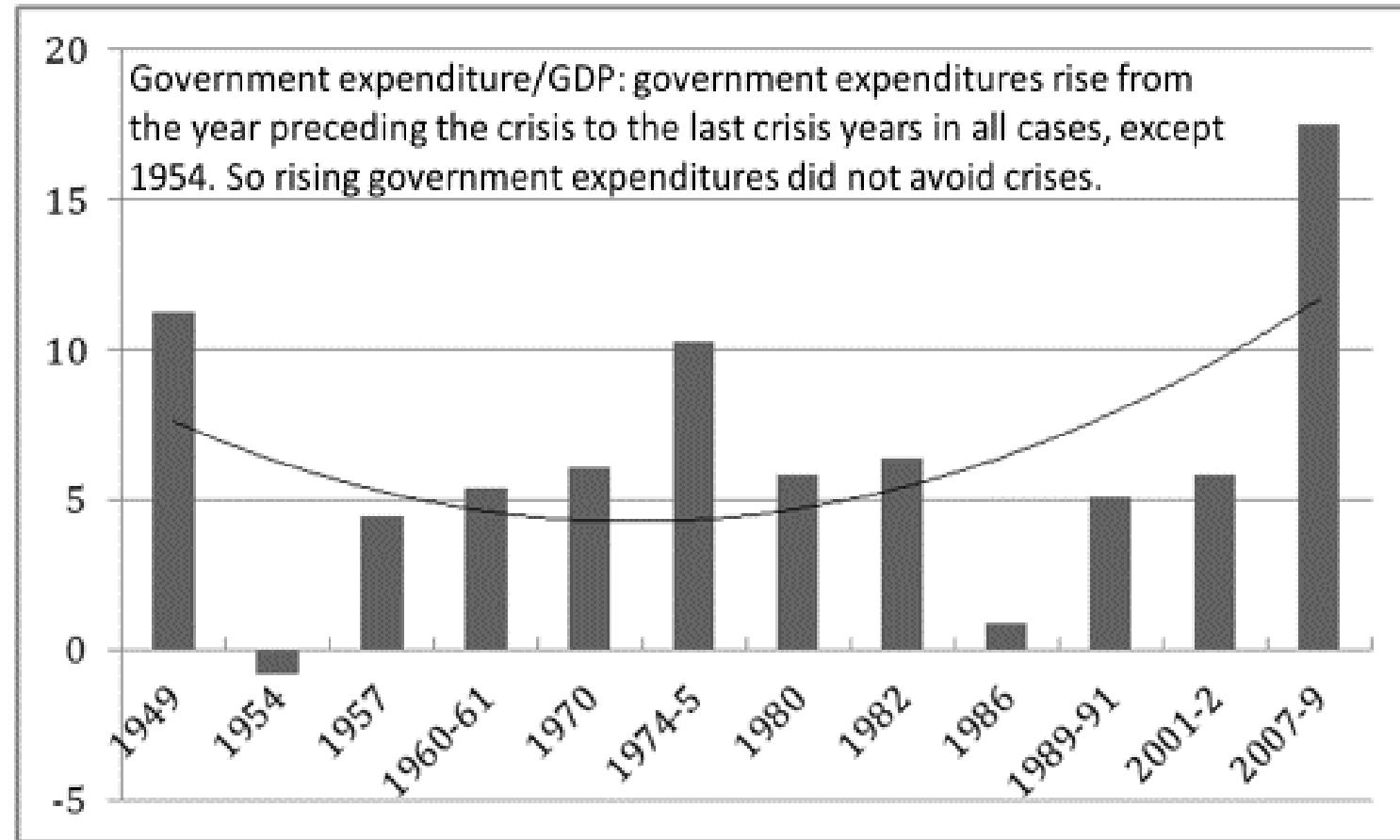
Average is Over

The US Hasn't Had a Year of Above Average Growth Since 2005

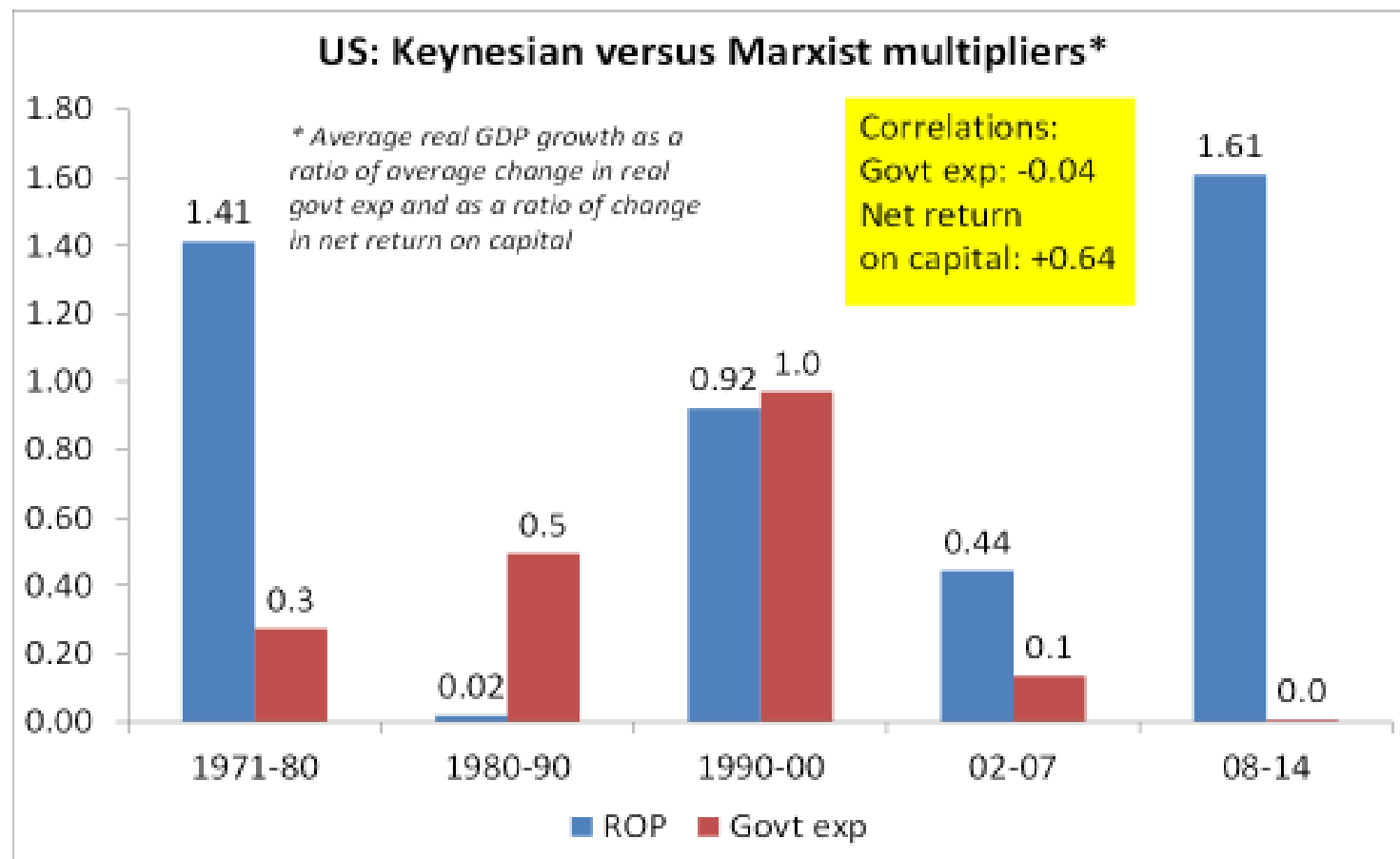


Source: Bureau of Economic Analysis
Alex Tabarrok

Government spending change before each recession



Which is compelling?

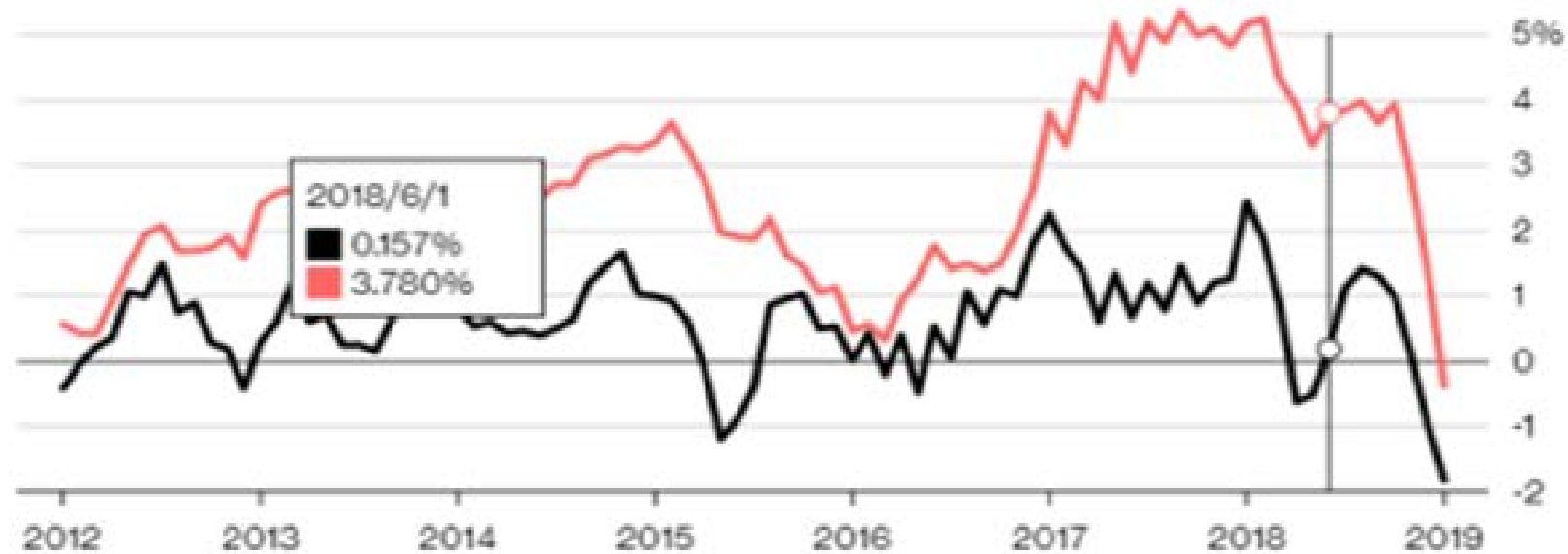


World trade diving

Highs and Lows

Global trade growth has seen a sharp downturn in recent months

Trade 3m/3m change 3m vs year earlier



Source: CPB World Trade Monitor

From manufacturing to whole economy

Global service and manufacturing PMIs



Source: CLSA, Markit

Investment too

Global capex, actual and nowcaster

%q/q saar. Last actual is 4Q18; 1Q19 is tracking. Nowcast through 2Q19.



Source: J.P. Morgan

Global profits weak



Another global slump is coming

- Profitability of capital is the driver of investment and economic growth under the capitalist mode of production, not consumption or needs.
- Profitability of capital tends to fall over time, leading to regular and recurring slumps in investment, and then production, employment and incomes.
- Slumps in investment and production are ways for capitalism to renew expansion and accumulation – but at the expense of people's livelihoods.
- This cycle cannot be ended without replacing the capitalist mode of production.
- The conditions for another slump over ten years since the last are appearing.