Levy Economics Institute of Bard College

Policy Note

2012 / 3

RECONCEIVING CHANGE IN THE AGE OF PARASITIC CAPITALISM: WRITING DOWN DEBT, RETURNING TO DEMOCRATIC GOVERNANCE, AND SETTING UP ALTERNATIVE FINANCIAL SYSTEMS—NOW

C. J. POLYCHRONIOU

Overview

We live in highly uncertain and critical times. That much is admitted by almost everyone—economic analysts, political commentators, and investors alike. But we also live in dangerous times, and this is something that far fewer members of the chattering classes are willing to admit. The five-year-long crisis of Western finance capitalism (certainly not a new crisis, but one with a much deadlier twist than at any other time in the postwar era) is pushing advanced liberal societies to a breaking point. If governments continue to be proxies of finance capital and aspiring political leaders cheerleaders for their financial backers, a catastrophic economic scenario is not really as far-fetched as some might like to think. Governments, industries, and households are under debt bondage, with the result that revenues from every sector of the economy are being diverted toward

C. J. POLYCHRONIOU is a research associate and policy fellow at the Levy Economics Institute of Bard College.

 ISSN 2166-028X

interest payments and late fees for various loans taken out on largely exploitative and, in fact, fraudulent terms.

Sure, there was a mood prevailing not long ago that everyone could strike it rich simply by borrowing money or making highly speculative investments, but this in itself becomes a serious problem when financial scams and economic policymaking join hands to dictate the rules of the game and the structure and operation of a given economic environment. In the 15th century, people used their life savings to purchase tulip bulbs in the belief that they would become rich overnight; more recently, individuals, households, industries, localities, and even governments took part in various mysterious financial schemes and instruments with the aim of a better future, but instead wound up bankrupt simply because the financial system had been structured to operate in this manner. Wealth creation through heavy borrowing (by consumers and homeowners urged to take on more debt in order to maintain their living standards in an age of stagnant wages) and excessive debt leverage (which ended up destroying even great companies) was the way to go—even though the officials involved knew the game was rigged. But in a way, the financial institutions themselves were vulnerable to the very system they had created. Greece was able to borrow over $500 billion dollars prior to being shut out of international markets, and private lenders are now taking a 74 percent haircut on the debt. So the question needs to be asked: on the basis of what criteria was the international investment community lending such huge sums of money to a national economy that was highly uncompetitive, maintained huge debt-to-GDP ratios, faced deep-seated structural economic problems, and was notorious for its corrupt political culture?

Now, after years of building up a Ponzi financial regime, Western capitalism faces its ultimate test. Will it collapse, giving rise to long-term economic instability and authoritarian political regimes? Or will it find the strength and the wisdom to make a comeback like it did in the United States during the Great Depression? Entire societies are under severe duress today, either because their governments succumbed to neo-imperialist pressures by dominant foreign powers and the international banking sector to repay odious loans (with Greece and Portugal being the prototypes); or simply because governments are unwilling to take on the economy's most powerful and adopt measures to revive growth, employment, and an "economy of plenty."

Today, the economic environment in many parts of the Western world already resembles in crucial ways the socioeconomic (and, to some extent, even the political) setting that prevailed in the late 1920s and early 1930s. Back then, when industrial capitalism was still prevalent, the West was in the midst of a destructive economic depression and faced the rise of nationalist and extremist politico-ideological currents, as well as conservative trends in economic policymaking. Debt and bankruptcy prevailed then as much as they do today. Accordingly, politicians and bankers, just like today, were overwhelmingly concerned with price stability and much less so with unemployment and measures to write down debt and restore living standards. Indeed, what eventually happened in the United States in the 1930s was a rare exception—and, had Roosevelt not been who he was (a man of the aristocracy but with enough foresight and determination to realize that, unless he embarked on a far-reaching democratic economic revolution, the nation was at risk of falling apart), it is unlikely that Western capitalism and liberal democracies would have survived.

In today's political environment, with finance capitalism exercising a hegemonic role over all other factions of capital and exhibiting some rather self-destructive tendencies, we have no politicians with either the capacity to grasp what is really going on or the character, wisdom, and determination to lead. In Germany, Chancellor Merkel practices an outdated and highly dangerous form of national economic neoliberalism (though it is still true that in Germany industrial and financial interests remain highly integrated), while French President Sarkozy erased any doubts about his political and intellectual standing when he recently declared that the eurozone crisis was over because of the Greek debt-swap deal. As for the United States, President Obama's economic policies exhibit both uncertainty (over what needs to be done) and a form of paralysis (because of his government's close ties to the most dangerous and destructive sector of the economy). And if we were to extend our reflection to the 2012 GOP presidential candidates, then the unfolding reality could be far grimmer than anyone among us would dare to admit.

Yet our situation is unquestionably dire. Debt is shrinking economies and rapidly reducing living standards as austerity measures are in effect implemented in order to raise revenues for the repayment of loan interest. Being under financial stress, many governments are forced to implement decisions that lack democratic legitimacy and work against the interests of the working populations, setting the stage for the emergence of highly dangerous political currents that do not in fact operate on the basis of strict ideological ideals and principles (ours is, after all, the age of ideological incohesiveness) but make their claims on the basis of a perceived threat to a nation's national and cultural identity. Various forms of neofascism are on the rise throughout the Western world, with factions on the left also succumbing to an antiprogressive discourse, especially since lack of a platform for economic change continues to be the left's Achilles heel.

The main problem is the power that finance capitalism exerts over domestic society and the abuses that it inflicts. Finance capitalism is economically unproductive (it does not create true wealth), socially parasitic (it lives off the revenues produced by other sectors of the economy), and politically antidemocratic (it restricts the distribution of wealth, creates unparalleled inequality, and fights for exclusive privileges). At the turn of the 20th century, finance capitalism, which led to what V. I. Lenin called capitalism's highest stage of development—i.e., imperialism—was still seeking to bring industry under its control and exercised its brutal power largely on undemocratic societies overseas. By the late 1970s, it can safely be said that finance capitalism had subjugated industry at home and took control of government power in the same manner that the great industrialists of the 19th and 20th centuries were able to influence public policy. The difference is that finance capitalism has no vested interest in seeing the living standards of ordinary people improve, and regards any public intervention as an attack on its freedom to exploit society's economic and financial resources as it sees fit. Industrial capitalism was a progressive stage of economic development relative to agrarian capitalism and feudalism. This much was admitted by capitalism's most brilliant critic, Karl Marx. But the dominance of finance capitalism represents a setback for society as a whole.

State Power and High Finance

The 2008 financial crisis will go down in history as a combination of scandalous corporate greed and callousness, fraud, and government irresponsibility—although it probably has deeper and more structural causes. As for the historic bailouts in the United States and Europe, they will long be remembered, not as policies that brought back state intervention (as some commentators naively claimed a few years ago), but rather as shameless, undisguised top-down class warfare.

In contrast to Economics 101 and the prevailing ideology, capitalism has always thrived on the basis of government intervention, including the type of government interventions that shift market-driven domestic expansion overseas and the distribution of wealth from bottom to top. Under neoliberalism, the state functions as the exclusive domain of the superrich and powerful, which in our own age happens to be the crowd involved in high finance and in the financial world in general. In a way, the state has been converted into an appendage of high finance and the power elite. Thus, the banking bailout plans—socializing losses for the disastrous actions of greedy individuals and companies—were the elite's only natural response to the flaws inherent in an economic system that makes a virtue of unfettered greed and unlimited wealth (including virtual wealth!) while displaying contempt for labor, disdain for justice, and apathy for the future of a nation's economy. Indeed, numerous high-ranking government officials served in big investment firms prior to taking senior-level positions in government, and, once there, fought hard to promote the interests of the investment banks and other financial organizations.

The financial crisis of 2008 was a meltdown in the operations of a system that had been set up through a marriage of convenience between the political elite and the financial elite. The "masters of the universe" (a term originally used by novelist Tom Wolfe to describe the titans of Wall Street) could not have had free rein to pursue profits irrespective of the risks involved, to destroy industries and communities with their reckless practices, and to get a royal tax treatment without the appropriate setup for the running of the game. This last required political intervention; otherwise, the seemingly expanding universe of Wall Street—made possible, of course, through the creation of more and more complex financial instruments and networks (both in order to squeeze out more profits and postpone the eventuality of a crisis)—could not materialize. This is why there is no such thing as "economics" but only something called "the political economy." Wealth creation and economic development are simultaneously political and economic processes, and any attempt to delink the two leads to gross deformities of both an economic and a political nature.[1]

It is high time that this premise took its rightful place in contemporary economic and political discourse. For this is the only way Western liberal societies can possibly escape the mess they've gotten themselves in. Since the 1970s, the US government has sought to create an environment conducive to the needs and drives of high finance, ultimately sacrificing the healthier sectors of the economy and driving down the standard of living for the nation's working population. In Europe, governments provided a more balanced economic setting, but did not hesitate to rescue their banks and the financial sector when the crisis broke out—without even ensuring that they had the policies in place to force these institutions to make significant adjustments to the way they do business. This speaks volumes about the power exercised by high finance over the public policy realm throughout Western liberal societies.

Yet the future of Western liberal societies may very well rest on radical changes in government's approach to high finance, growth and development, and employment (Crouch 2011). State power should be reasserted for the advance of the general welfare and not be merely an arm for high finance. In order for this to happen, public discourse should be refocused and opened up to involve people and communities at all levels. Financial capitalism has inflicted a heavy blow not only to the economy but to the political culture as well; democracy is in decline, and exercising the "general will" has become an exclusive privilege of the ultrarich.

Massive Restructuring of Existing Debt as the First Step toward Recovery

From the outset of the financial crisis, "knee-jerk" is the only way to describe government attempts to deal with the biggest capitalist crisis to face the Western world since the Great Depression—a debt crisis that threatens economies with long-term stagnation and societies with political and social instability. Wiping out debt may sound like an odd, even preposterous idea to some, but it has been widely used as a practice to reestablish balance throughout history. More important, at this stage it may be the only way to avoid another meltdown and economic catastrophe. Most recently, we've had the write-down of Greece's sovereign debt for the amazing sum of 100 billion euros, but it won't make one iota of difference in the country's ability to avoid sinking like the *Titanic*. Its debt level remains unsustainable, and another major haircut, and possibly its exit from the eurozone, will definitely be needed in order for it to survive financially and eventually recover economically.

With virtually all Western capitalist economies carrying unsustainable levels of debt, and the interconnectedness of those economies, a massive restructuring of public (and private) debt is a policy option that needs to be taken seriously. The other available strategies—growth, inflation, and further deficit reductions—are weak and/or unrealistic options. It is simply impossible for Western economies to return to strong growth in the near term while carrying huge loads of debt, and wiping out debt via rapid inflation (as happened in the Weimar Republic in 1923) is simply dangerous. Cutting federal deficits further will only sink economies deeper into recession and possibly cause a global depression. This leaves massive debt restructuring as the only realistic option. It's the one strategy that can bring about the desired outcomes, solving once and for all the debt sustainability issue and returning economies to growth.

Introducing a massive debt-restructuring plan in both Europe and the United States would probably require some new institutional arrangements (especially if the method chosen were repudiation of sovereign debt) and large-scale coordination across central banks (particularly if the method chosen for reducing the level of debt were government stock repurchases). Wiping out today's debt could also involve state intervention via nationalization. The case of Sweden provides a fine example of resolution, whereby banks were brought under government control during the banking crisis of 1992. Governments could take over certain financial institutions and wipe out debt in this manner.

These methods may sound rather radical but we live in rather extreme economic times. Millions of people are unemployed because of the recession in Europe and the United States, the standard of living has taken a sharp drop (compounded, in Greece and elsewhere in the eurozone, by stringent austerity measures), pension funds are at risk of disappearing, infrastructure is either decaying or collapsing because of inadequate public funding, and poverty and crime are eating away at the dream of a fair and decent society. Advanced capitalism is in a deep structural economic crisis that may or may not be directly related to the financial crisis of 2008 (see Harvey 2011).

Giving Rise to Alternative Financial Systems

Finance capitalism, which is by nature parasitic, can no longer be the driving force in a democratic society. It needs to be contained and, in fact, sterilized to the largest possible extent. As such, an ambitious political project for redesigning the financial universe needs to be initiated, with the support of governments and other public institutions. This project would not be intended to do away with financial institutions driven by profit but should have as its principal aims the design and implementation of policies that would restrict highly destructive undertakings by financial institutions and encourage the development of alternative financial systems.

Individuals like Joseph E. Stiglitz and George Soros have made some important contributions to the public discourse insofar as the setup of a new global financial architecture is concerned (see Stiglitz 2010 and Soros 2012). I won't dwell on their schemes as I wish to extend the discussion beyond the overarching architecture and into the confines of the microeconomic. The redesign of finance capitalism is a huge project that may take many years, and possibly more crises before we even get to such a stage. Even the mere question of financial regulation poses severe challenges (see Gordon and Mayer 2011). We saw how quickly the masters of the universe returned from their luxury beach homes following the financial meltdown, and now they are as powerful as before (for an analysis of the impact of failures of the system of governance in financial regulations see Levine 2011). Breaking their power implies, first and foremost, carrying the struggle into the political arena. In this regard, the Occupy Wall Street demonstrations have served a useful purpose.

Let's start with the banks, the primary financial institutions in a capitalist economy. It should be obvious to all that the notion of "too big to fail" is both absurd and dangerous. Banks are by definition public institutions. Hence, they should return to doing what they were created to do in the first place: offer a safe environment for peoples' savings and provide capital to businesses for development purposes. Banks can certainly increase their profitability by betting with their own capital, but they were not designed for such a purpose. If they wish to be investment institutions, they should not be permitted to practice traditional banking. In a mature political and democratic culture this should be self-evident. However, since ideology has long distorted reality and undermined the common interest, a public dialogue on this very issue should be at the top of any public policy agenda.

While this is an even bigger taboo in today's "polite society," nationalizing some big, banking institutions that are insolvent may also be a necessary ingredient in the effort to refashion the financial universe of advanced capitalism. We have plenty of examples to show that nationalized banks have never caused the kind of havoc experienced by advanced capitalist economies as a result of the 2008 financial crisis. Rather, they have a history as well-functioning and highly profitable institutions. In fact, the symbiosis of the public and private sectors has been a general success story throughout capitalism's modern history. Free-market capitalism, in contrast, has been a complete disaster—and only those with ideological blinkers and vested interests in the existing system would launch serious objections to this claim.

In this context, alternative financial systems should occupy a major space on the agenda for redesigning the financial universe. Such systems are very much needed, particularly in an increasingly uncertain world where globalizing trends tend to have uniform impacts across various economic sectors and throughout different localities.

Social banks are one example of an alternative financial institution. There could be financial organizations, at the local and national level, where the public good, not profit taking, is the principal driver.

There should also be a place in capitalism's future for social businesses that would attract small investors whose focus is the longer term, and who might also care about the planet and the communities they live in. Here, international organizations that promote sustainability and receive public funding could turn out to be important allies, providing know-how and possibly initial funding to socially responsible startups.

Social banks and businesses should have key roles to play in the future of capitalism, assuming there is something to be learned from the wreckage of an unsustainable financial system like the one that caused the 2008 crisis.

Conclusion

Fallout from the 2008 financial crisis continues unabated. Massive economic damage has been caused and the human suffering is immense. Yet the implications of this crisis continue to elude us, largely because many people are in the grip of neoliberal orthodoxy and refuse to acknowledge the need for large-scale economic, social, and political change. Wiping out debt may be the first step toward economic and social recovery. Recapturing the democratic spirit of government is a must for the future of liberal societies, as is establishing alternative financial systems. The purpose of life in any advanced society should not be the mindless accumulation of wealth, gross inequality and exploitation, the destruction of community values, and pollution of the environment. This is why we need to work toward redesigning a system that has the capacity for generating not only great wealth but also causing tremendous damage.

Note

1. The previous section has appeared in a slightly revised version of an article of mine titled "The 'Masters of the Universe' Outsmart Themselves," *Economic and Political Weekly* 48, no. 43 (October 25, 2008): 14.

References

Crouch, C. 2011. *The Strange Non-Death of Neo-Liberalism.* Cambridge, UK: Polity Press.

Gordon, J., and C. Mayer. 2011. "The Micro, Macro and International Design of Financial Regulation." Paper presented at the conference "Corporate Governance after the Crisis," Saïd Business School, University of Oxford, England, January 13, 2012.

Harvey, D. 2011. *The Enigma of Capital and the Crises of Capitalism.* London: Profile Books.

Levine, R. 2011. "The Governance of Financial Regulation: Reform Lessons from the Recent Crisis." *International Review of Finance* 12, no. 1 (March).

Soros, G. 2012. *Financial Turmoil in Europe and the United States.* New York: PublicAffairs.

Stiglitz, J. E. 2010. *The Stiglitz Report: Reforming the International Monetary and Financial Systems in the Wake of the Global Crisis.* New York: The New Press.