MARXISM AND THE ECONOMIC CRISIS

Rohini Hensman

A Theory of Crisis

The credit system was relatively undeveloped in Marx's time, and he would not have been familiar with hedge funds, mortgage-backed securities, collateralised debt obligations (CDOs), credit default swaps (CDSs), and all the other derivatives that are now part of the global financial system. However, he was familiar with generalized crises, and tried to explain financial turmoil in terms of what is now referred to as 'the real economy': i.e., a crisis in the accumulation of capital. In his view, such crises were inevitable in capitalism, because it is a system of production not for human need but for profit.

In Volume 1 of *Capital*, Marx divided capital into constant capital (machinery, raw materials, etc.) which transferred their value unchanged to the product, and variable capital, spent on labour-power. The latter, he argued, was the only creator of value greater than the value it possessed itself, i.e., of surplus value, and thus of profits. (He also referred to constant capital as 'dead labour' – objects that embodied past labour – and to variable capital as 'living labour,' embodied in living workers.) He called the ratio between constant and variable capital the 'organic composition of capital.' The competitive character of capitalism enhances the normal tendency in any society for the productivity of labour – i.e., the amount of means of production which one worker can handle – to grow, and under capitalism, this growth is reflected in an increase in the organic composition of capital. But the rate of profit – the ratio of surplus value to the total amount of capital, both constant and variable, required to produce it – would have a tendency to fall as the organic composition increases, because surplus value or profit is created only by living labour. Beyond a certain point, the amount of surplus value produced would be inadequate for profitable investment, and this, according to Marx in Volume 3 of *Capital*, was what resulted in crises. If this happened in all branches of production and not just one or two, people might be homeless while properties remained unsold, jobs would be lost while factories remained idle; businesses would go bankrupt and their assets would be taken over by others, leading to a centralization of capital.

In many ways, this resembles the scenario staring us in the face today, as more and more people recognize that this is not just a 'financial crisis' but also a crisis in the 'real economy.' In Marx's day, the crisis would end and the rate of profit would be restored only after a massive devaluation or destruction of capital, accompanied by a fall in wages, had taken place. Do we have to go through all this?

Counteracting Tendencies and Other Mechanisms

While Marx thought that the tendency for the rate of profit to fall was inevitable, he also identified counteracting tendencies which could slow down or even halt or reverse this fall temporarily. Chief among these was foreign trade, which, by cheapening the supply of raw materials (oil, cotton, iron, etc.), would counteract the fall; similarly, foreign investments in countries where capitalism was less developed, the organic composition of capital was lower and the rate of profit consequently higher would also boost the average rate of profit. Lenin took up this theme in his pamphlet on imperialism. Their argument suggests that globalization, which has vastly increased foreign trade as well as investment in developing countries, with their lower wage rates and lower overall organic composition of capital, should counteract a fall in the average rate of profit and prevent a crisis. Why has it not done so?

To answer this question, we have to look at possible causes of crisis that Marx examined less thoroughly than the tendency of the rate of profit to fall, or did not examine at all because they were not operative in his time. In Volume 2 of *Capital*, Marx draws up schemas for the social reproduction of capital, and they comprise only two departments of capital: one producing means of production, and the other producing means of consumption (goods and services) for workers. The products of both these departments re-enter production, either as infrastructure, machinery and raw materials, or as living labour working in production, and we could therefore refer to this as 'socially useful production.' Although Marx looks only at capitalist production, it is worth pointing out here that even if it is the state that invests in electricity and railways or healthcare and education, and no profit is made on these investments, capitalism still benefits from them, because they provide it with cheaper and higher quality inputs.

But what about luxury production of items consumed by capitalists? These do not re-enter the process of production, and Marx opined that if there were to be a disproportionate diversion of resources into articles of this sort, the process of accumulation would suffer. Looked at another way, the surplus value is obviously not all re-invested; some part of it is used for capitalists' consumption, and we could call the branch of capitalism producing these items Department III. The more surplus value is diverted into Department III, the less there will be for Departments I and II, resulting in a shortage of surplus value for accumulation.

Neoliberal policies result in this diversion. It has been pointed out by scholars like Jan Breman that it is a mistake to think that neoliberalism constitutes deregulation of the market; it is, rather, a regulation of the market in the interests of the owners of capital. The truth of this observation becomes obvious if we examine the issue of patents. From time immemorial, so-called 'intellectual property' was unregulated; the men and women who invented the wheel and agriculture made no money out of these inventions, despite the fact that all subsequent generations made use of them. It is only under capitalism that corporations rush to patent not only their own but also other people's inventions and discoveries, so that, for example, pharmaceutical companies can make obscene profits by selling life-saving drugs at prices that condemn most patients who need them to death. This is an example of regulation in the interest of capitalist profits.

In other cases, regulations protecting workers and the public are abolished. From the 1980s onwards, an orgy of such deregulation took place, above all in the US, proceeding apace under all regimes, including the Clinton administration. For example, the Glass-Steagall Act, which was passed in 1933 amid the collapse of the banking system to segregate commercial banking (taking deposits and lending) from the much more risky business of investment banking (underwriting and selling stocks and bonds), and helped to halt the run on banks, was repealed in 1999. Alan Greenspan had been arguing for its repeal from 1987, and pursued the 'securitization revolution' vigorously under the Bush administration. This, as William Engdahl argues, is at the heart of the present financial crisis. By allowing the non-transparent spreading of risk – rather like sending bird-flu patients back home without telling them have got the virus – it allowed contagion to spread from infected to formerly healthy banks. And by allowing financial institutions to gamble with the money of non-gamblers, keeping the bulk of their winnings when they won but leaving the public with the bulk of their losses when they lost, it led to a much greater concentration of wealth in the hands of non-productive capitalists than ever before.

This is brought out graphically by the Oversight Committee's hearings into the American International Group (AIG) bailout. In Chairman Waxman's words:

'There are obvious differences between Lehman and AIG. Lehman is an investment bank; AIG is an insurance company. Lehman fell because it placed highly leveraged bets in the subprime and real estate markets; AIG's problems originate in complex derivatives called credit default swaps. But their stories are fundamentally the same. In each case, the companies and their executives grew rich by taking on excessive risk. In each case, the companies collapsed when these risks turned bad. And in each case, their executives are walking away with millions of dollars while taxpayers are stuck with billions of dollars in costs…Last month, the taxpayers bought out AIG in an $85 billion bailout. This was a direct result of the mistakes made by Mr. Cassano. Yet even today, he remains on the company payroll, receiving $1 million a month. The federal bailout occurred on September 16. Less than one week later, AIG held a week-long retreat for company executives at the exclusive St. Regis Resort in Monarch Beach, California…Invoices provided to the Committee show that AIG paid the resort over $440,000, including nearly $200,000 for rooms, over $150,000 for meals, and $23,000 in spa charges. Average Americans are suffering economically. They are losing their jobs, their homes, and their health insurance. Yet less than one week after the taxpayers rescued AIG, company executives could be found wining and dining at one of the most exclusive resorts in the nation.'[3]

No doubt the AIG executives provide employment to the hotel workers at the resorts they patronize, but this is at the cost of tens of thousands of jobs lost in industries engaged in socially useful production.

The Impact of Militarism

While Marx considered war to be detrimental to the working class, he did not see it as having a negative impact on capital. This is probably because in his day, war and militarism were needed to secure and keep colonies, which contributed to keeping up the rate of profit. Today, when global trade and investment are better carried out through negotiation than through military occupation, militarism is no longer a necessity for capitalism.

Luxemburg came close to suggesting that military production belongs in a third department, since it constitutes the production of neither means of production nor consumption goods and services. It is clear that military products do not re-enter production, and we could therefore put it, along with luxury production, in Department III. Subsequently, there was a debate among Marxists as to whether a 'permanent arms economy' stabilized capitalism, while a more mainstream belief in the positive contribution of 'military Keynesianism' gained ground.

It is true that in the short run, the market for military production guaranteed by the state can boost employment in a downturn, thus smoothing over business cycles. Yet, like luxury production, it does this by diverting resources from the production of means of production and consumption; executives of military production units and private security contractors like Blackwater may be minting money, but this money constitutes a deduction from socially useful production. Seymour Melman concluded that excessive military spending by the US decimated its manufacturing base, slowed economic growth and reduced employment. In the words of Chalmers Johnson, 'Military industries crowd out the civilian economy and lead to severe economic weaknesses. Devotion to military Keynesianism is, in fact, a form of slow economic suicide.' This was reflected in the ballooning US national debt, more than $9 trillion by the end of 2007.

Large-scale military spending is a feature of many national budgets, but US expenditure on 'national security,' according to Chalmers Johnson, amounts to over a trillion dollars per year: more than all other national defence budgets combined. Needless to say, none of the products of this expenditure return to production, so it is a massive drain on the economy. Worse still, the role of the US dollar as a world reserve currency means that huge dollar reserves of other countries – especially Asian countries, with China and Japan in the lead – are also funnelled into US military expenditure. US 'national security,' in other words, has been acting as a black hole sucking in surplus value from the whole world. The crisis, consequently, is a global one.

How Do We Get Out of It?

Some socialists have opined that this is the end of capitalism, but the notion that the divided, confused and demoralized workers of the world are ready to take over and run the world economy sounds highly unrealistic. To adapt a metaphor used by Marx, that would be like performing a Caesarian section to deliver a 16-week-old foetus: it simply would not survive. And until it develops sufficiently to be able to do so, we have to ensure the health of its capitalist mother. Fortunately, doing so in the current crisis does not involve sacrificing the interests of workers, since this crisis is caused not by a fall in the rate of profit but by excessive syphoning of surplus value into wasteful expenditure. What measures can we fight for through our civil society organizations?

A common and understandable response to the crisis is the call for protectionism and deglobalization, but this would remove the only countervailing factor sustaining the rate of profit, and worsen the crisis. Instead, multilateral agreements (rather than bilateral ones, where a stronger partner can bully the weaker one) should concentrate on establishing equitable terms on which international trade and investment can be conducted. It is neither realistic nor even desirable to abolish finance capital either; as Hilferding pointed out, it enables even people with small amounts of money to invest, and Marx himself saw it as a step towards the socialization of production. Currently, pension funds built on the savings of wage and salary earners are among the most important financial institutions, and could use their clout to ensure better regulation of financial markets. This might include banning predatory practices, ensuring maximum transparency, and much stronger regulation and oversight by public institutions whose personnel do not overlap in any way with the personnel of the financial institutions they are supposed to monitor. Progressive taxation would redirect production from luxury resorts to socially useful products. In countries like Sri Lanka, the political elite consumes a large chunk of the surplus, extracting more and more from the public through runaway inflation, and their power to do so should be curbed.

At the same time, there should be campaigns for defence budgets to be slashed; this would need to be accompanied by signing international treaties to ban the production of certain weapons (nuclear, chemical and biological weapons, land mines, etc.), and nationalist ideologies would need to be combated. Thus in Sri Lanka, politicians espousing Sinhala and Tamil nationalism, who drive a war that has devastated the economy, should be rejected decisively. The US, being the biggest military spender by far, would need the most sustained campaign to end its wars, dismantle its foreign bases, wind up covert operations and shrink its military-industrial complex; and until it has done so, other countries should refrain from accumulating foreign exchange reserves in US dollars, because that simply contributes to the destruction of the surplus value produced by their own hard working people.

If these measures are taken, they would create massive funds for governments to invest in infrastructure (including water and energy conservation, flood prevention and renewable energy), and healthcare, education and child nutrition programmes, thus increasing overall productivity and creating employment. Workers cooperatives should also be encouraged and assisted by the state. All this would reverse the fall in incomes and consumer demand. Social housing could help to eliminate homelessness. Many countries already have programmes that could be expanded as well as adapted for other countries, such as the National Rural Employment Guarantee scheme in India, the *bolsa familia* in Brazil, the National Health Service in the UK and workers' cooperatives in several countries.

It is possible to get out of this recession without allowing it to become a depression if enough people press for decisive action along these lines. Eventually, another crisis will come along, of course: that is the nature of capitalism. But we can deal with that problem when we get to it!

Dr. Rohini Hensman is a free-lance writer living in Bombay.