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Inequality and morbid symptoms of a financialised system

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Introduction

Today as the world endures the crisis of a global pandemic, "an old order is ending in convulsions". So writes Rebecca Spang, historian of the French revolution in *The Atlantic* (Spang, 2020). In the 1790s, money, debt and the non-payment of taxes by France's rentiers, played a critical role in revolutionizing France. Today purveyors of money and debt – creditors, investors and speculators – both avoid taxes and prey on a global economy radically weakened by the Great Financial Crisis and the policy response to the events of 2007-9. As a result, and unsurprisingly, the international economic system is both unprepared for, and prone to increasingly frequent "convulsions". COVID19 is but the latest, and will cause long-lasting economic damage. Above all, and according to Case and Deaton, COVID19 is expected to widen the US's "already vast inequalities in health and income".[2]

The "pillars" of the global economic system are fabricated on shaky, "liberal" foundations (see Pettifor, 2006, 2017a). It is an international system specifically designed to expand markets for creditors and investors; and to protect, above all others, the interests of private creditors. The most important foundations of the system are capital mobility, the marketisation of interest rates and exchange rates. The system is largely maintained by the world's hegemon – the United States – which uses its role as issuer of the world's reserve currency to protect the interests of private finance, in particular Wall Street. US monetary power is backed in turn by military power, used to maintain control over access to, or the denial of access to markets worldwide.

A central tenet of the system is that wherever possible, the policy autonomy of governments (whether democratic or not) must be constrained and subordinated to governance by those active in capital, goods and labour markets. The global system – its regulations and laws - are thus largely governed by *private authority.*

Obscene levels of inequality are but one of the *outcomes* of the current global economic order or architecture. Addressing inequality is, therefore, not just about individual policy focus, it is about international system change.

Inequality is not the only outcome of the system. Other worldwide outcomes include: immense, and unaccountable corporate power; high levels of costly private and public debt; sky high levels of rent (wealth) extraction by the owners of both financial and physical assets; weak or non-existent public health infrastructure; low levels of investment; high levels of fraud, illiteracy, homelessness. Capital mobility facilitates drug dealing which in turn leads to escalating levels of addiction and mental illness. Globalised transport systems – aeroplanes and international travel - act as passports and vectors of disease and pandemics. These

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[2] Anne Case, Angus Deaton, Jun 15, 2020, Project Syndicate. *United States of Despair.*

expose systemic problems for the many who have functioned as global reserves of low-paid, insecure, non-unionised and unskilled workers.

In the United States these outcomes are worsened by a costly, exclusive private healthcare system, lavish levels of public spending on the military; and a privatised prison-industrial complex, accompanied by extensive surveillance and policing. With the constitution and democracy corrupted by corporate power, elites mimic their French predecessors. Like Norman noblemen, they appear largely unaware of the social and political stresses unleashed by the privatised economic system. While the rentier class have made extraordinary capital gains, many US workers in employment can only function by drawing on high levels of debt. In the bottom half of US income distribution, Americans have experienced essentially no income growth since the late 1970s after accounting for taxes, inflation, and cash benefits from the government. [3] Those that are unemployed and without healthcare, suffer what Case and Deaton dub "deaths of despair" (Case and Deaton, 2020). Their work reveals that:

> "[I]n the past two decades, deaths of despair from suicide, drug overdose, and alcoholism have risen dramatically, and now claim hundreds of thousands of American lives each year – and they're still rising."

Between just March 18 and April 10, 2020, over 22 million people lost their jobs in the USA as the unemployment rate surged toward 15 percent. Over the same three weeks, American billionaire wealth increased by $282 billion. This was an almost 10 percent *gain*, according to a US Institute for Policy Studies (IPS) report *Billionaire Bonanza* (Collins et al, 2020).[4] Market capitalizations may have become erratic, perhaps there will be losses to some, but the wealthy face a different world than the many. As the IPS report also states:

> "Billionaire wealth… tends to rebound from market meltdowns. In the immediate aftermath of the global economic crisis of 2008, the *Forbes* 400 saw their combined wealth decline $300 billion from $1.57 trillion in 2008 to $1.27 trillion in 2009. Within 30 months of the September 2008 crash, most of these fortunes recovered. By 2012, billionaire wealth had reached $1.7 trillion, exceeding pre-2008 levels. Between 2010 and 2020, the combined wealth of the U.S. billionaire class surged by a staggering 80.6 percent, from $1.631 trillion to $2.947 trillion in 2020 dollars" (Collins et al 2020: 10).

If we are to address "billionaire bonanzas" and reverse inequality and other morbid outcomes of the current system, then we must begin by transforming the international system which generates such inequality. Fundamental to such a transformation will be the removal of private authority over the globalised financial architecture and the restoration *of public* authority over financial regulation and economic policy (Pettifor, 2017a).[5]

[3] Matthew C. Klein and Michael Pettis, 2020, p. 177. *Trade Wars are Class Wars.*
[4] For example, in the case of Jeff Bezos: "The stock market crash initially left Bezos" net worth deeply damaged, down to a meager $105 billion on "Black Thursday" March 12, the stock market's lowest point. Bezos' wealth has been trending upward ever since, with no company better positioned to profit from the pandemic than Amazon. The closure of hundreds of thousands of small businesses is giving Amazon the opportunity to increase its market share, strengthen its place in the supply chain, and gain more pricing power over consumers. Despite Amazon's e-commerce dominance, Bezos has been unable to protect his workforce from Covid-19: workers in ten different Amazon warehouses tested positive for the disease in late March. Instead, in early April, Bezos announced a donation of $100 million of his $140 billion in wealth to Feeding America (Collins et al., 2020: 11).
[5] There are many other associated issues and policies, including a Green New Deal (see Pettifor, 2019).

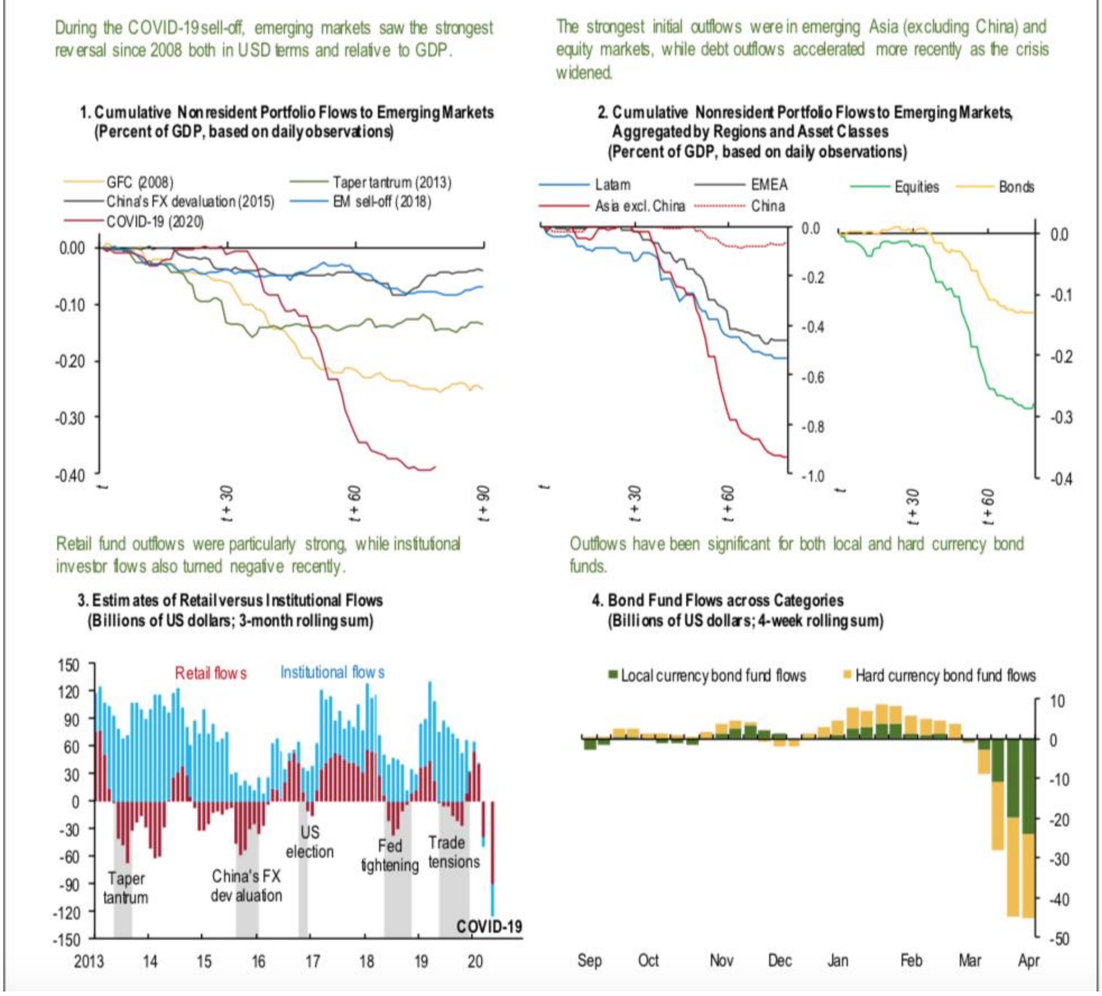
Inequality and the Global South

The rise of extreme levels of inequality within domestic economies is mirrored in the inequality that exists between the world's richest and poorest economies. The injustice of the inequality of power – not just over the international economy, but over domestic economies - was starkly exposed by the Coronavirus crisis. A shortage of US dollars worldwide, led the Federal Reserve and the IMF to lend dollars to certain governments, but denied this largesse to others. The Fed's "swap lines" covered fourteen central banks, but excluded Turkey, South Africa, Nigeria and Indonesia, despite their need for dollar finance to pay for vital imports, including oil; and despite the challenges posed to their health systems by a global pandemic.

The failure of the international financial system to provide quantities of the world's reserve currency to low income countries at a critical period, does not bode well for those countries most exposed to forthcoming shocks, including climate breakdown (for issues and alternatives see Pettifor, 2019).

To add to the stresses imposed by coronavirus, emerging and frontier markets experienced the sharpest portfolio flow reversal on record, according to the International Monetary Fund's recent *Global Financial Stability report* (IMF, 2020). Low-income countries faced a "perfect storm" and "big reversals", for example, on portfolio flows, see figure below (IMF, 2020: 13):

Figure 1.8. Portfolio Flows to Emerging Markets: A Big Reversal



One hundred billion dollars of capital stampeded out of emerging markets over the last few weeks of March and early April, 2020. These outflows, sparked by fickle and volatile investors and creditors, crushed the currencies of low-income countries, while simultaneously inflating the dollar's value. Because the US dollar alone is recognised by international markets for the payment of vital imports, including oil, the cost of dollar-denominated imports rose. This in turn led to trade and capital account imbalances, which then prompted the ghouls of the global economy – western-based rating agencies – to downgrade countries that were victims of capital flight. Downgrades in turn raised borrowing costs and tightened credit availability at a time when global markets for poor country commodity exports were already weak, and prices falling, cutting their income. Simultaneously weakened currencies raised the cost of purchasing vital equipment and pharmaceuticals from abroad.

As they faced the challenges of a pandemic, impoverished countries were effectively sacrificed on the cross of the US dollar and the international order.

Capital flight on the whim of investors, coupled with the subsequent strengthening of the US dollar, are not accidental nor inevitable consequences of the pandemic. The virus, after all, portends greater economic failure in the United States than in many emerging markets. Nor can it be explained directly by sudden changes in the economic circumstances of the countries trampled down by investors' rush for the exit. Instead, it is a consequence of the international system's *design* – an architecture purposed to accommodate the whims, no matter how irrational, of investors, and to protect the interests of creditors.

What has to be done?

Taking action to transform the current highly unbalanced system requires, in the first place, a fuller understanding of how and why the international financial architecture was constructed.

Ken-Hou Lin and Donald Tomaskovic-Devey argue in their important paper "Financialization and U.S. Income Inequality, 1970–2008" (Lin and Tomaskovic-Devey, 2013) that the rise in inequality is undoubtedly the consequence of the deliberate financialisation of the global economy in the late 1960s and early 1970s.

Financialisation has permitted the almost effortless making of extraordinary capital gains by those that derive income from the possession of financial assets that generate interest, or from scarce assets or assets made artificially scarce (like patents and intellectual property). Rental income from land, property, minerals or financial investments, are the best-known forms of rentier capitalism. And as Guy Standing has argued:

> "[T]hey include the income lenders gain from… capital gains on investments; 'above normal' company profits (when a firm has a dominant position); income from subsidies; and income of financial intermediaries derived from third-party transactions" (Standing, 2017).

Tackling rentierism and its consequences by restoring public authority over the system at the level of the domestic economy, is the internationally coordinated policy action required.

Conclusion

As I explained in a 2012 article for *Real-World Economics Review*, on the causes and consequences of President Donald Trump, the collapse of the Bretton Woods system in 1971 represents a decisive episode in the process of financial globalisation, and with it the corresponding weakening of regulatory democracy. The OECD recognises that:

> "[T]he easing of capital controls, and the international branching of business firms or establishment of their finance companies, made domestic regulations easier to circumvent by conducting financial transactions outside national boundaries" (Pettifor, 2017b).

Up until the early 1970s, financial systems in most western economies were governed by the regulation of market forces, enacted within the policy-making boundaries of democratic nation states. These constraints included: interest rate controls; securities market regulations; quantitative investment restrictions on financial institutions; line-of-business regulations and regulations on ownership linkages among financial institutions; restrictions on entry of foreign financial institutions; and controls on international capital movements and foreign exchange transactions. The reason for constraint is based on common sense. The nature of money-creation as a largely effortless *social* construct or technology, requires social, or society-wide regulation of the public good that is the monetary system in order to prevent the capture of this public good by a small elite. As John Maynard Keynes understood better than many of his peers:

> "Interest today rewards no genuine sacrifice, any more than does the rent of land. The owner of capital can obtain interest because capital is scarce, just as the owner of land can obtain rent because land is scarce. But whilst there may be intrinsic reasons for the scarcity of land, there are no intrinsic reasons for the scarcity of capital..." (Keynes, 1936).

From the perspective of Keynes, the consequences of markets governed effectively by rentiers were entirely predictable: rising and even obscene levels of inequality, political instability and recurring financial crises. Such inequality and financial instability is particularly problematic as societies struggle to meet threats posed by present and future climate and health shocks.

We need a different international financial system, one governed by public authority, if inequality and its harms are to be addressed. To paraphrase Karl Marx: political economists have only interpreted the world, in various ways. The point, however, is to *change* the current global financial architecture. An understanding of the systemic and international causes of inequality enables us to claim this moment of crisis as a revolution. To do so, is to claim it for human action, as Rebecca Spang argues.

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