The Economic Crisis and Contemporary Capitalism

Prabhat Patnaik

The current economic crisis, which originated in the United States, is commonly explained as resulting from financial deregulation in the U.S., in particular the repeal of the Glass-Steagall Act that had erected a Chinese wall between ordinary banking and investment banking. Deregulation, it is argued, allowed, not just investment banks, but even ordinary banks to pick up assets that could rapidly become worthless, as has actually happened: the losses in the value of assets of the U.S. banks today exceed their net worth, which means that the entire banking system has become insolvent, with the scale of the bail-out packages for banks presented till now being utterly inadequate for restoring solvency.

There are however two obvious problems with this explanation. First, since deregulation can play only a permissive role it does not really amount to an explanation. This explanation is analogous to an explanation of theft in society in terms of the laxity of anti-theft laws. Secondly, if the impact of the absence of deregulation, i.e. of tighter regulation, would have been exclusively to prevent the crisis, then there would still be some point in remaining satisfied with deregulation as the proximate explanation, and not delving too deeply into more basic explanations. This however is not the case. Tighter regulation, even if we accept that it would have lessened the crisis, would almost certainly have truncated the boom as well. In other words we have to see deregulation not as something which is superimposed on an otherwise well-functioning system with the sole consequence of producing a crisis, but in the context of the totality of the logic of the deregulated system. And when we do so, the crisis, of the sort being experienced, appears not as an aberration of the system but as part of its very *modus operandi. It represents not the failure of the system but the system itself.*

Keynes had recognized this, which is why he had wanted a different capitalist system, with "socialization of investment" and "euthanasia of the rentier". Under "free market" or deregulated capitalism, asset markets, especially those for financial assets, which have negligible carrying costs, get dominated by speculators who buy the assets not for the yield they give but for selling at a higher price. They have little interest in the asset as such since they are not interested in holding it for "keeps"; their only interest is the capital gains they can get on it in a day's, or a week's or a month's time. And this according to Keynes was not just a source of great instability but made crucial social variables like employment dependent on the caprices of a bunch of speculators.

Monetarist economists by contrast see speculation as essentially price stabilizing. Since the expected price of the asset must be linked to its "fundamentals", any deviation of the current price from its expected price would call forth according to them speculative behaviour that counteracts such deviation; and it is this which makes speculation price-stabilizing. But this is an untenable assertion. Even assuming a world where everybody expects that "ultimately" the price of an asset must get back to what reflects the "fundamentals", as long as this is not expected to happen *immediately* this faith in the "ultimate" return to a price that reflects "fundamentals" becomes irrelevant for preventing instability, even massive instability.

Speculation, Keynes argued, produces bouts of euphoria, or "speculative excitement" as he called it. An initial rise in asset prices gives rise to expectations of a further rise, which makes wealth-holders demand more of the asset and hence causes an actual further increase. And so the process goes on creating a speculative bubble. Of course the decision to demand more of an asset depends not only upon its expected price appreciation, but also upon the evaluation of the risk associated with holding more of it. But the same euphoria that makes wealth-holders expect a continuation of asset price increases, also gives rise to an underestimation of risk. And it is this phenomenon of euphoric expectation of capital gains net of risk premium that makes for bubbles.

A rise in asset prices caused by such a bubble, however, has important consequences for the real economy. The rise in asset prices improves the wealth position of the asset holders which increases their consumption expenditure. In the case of financial assets, since it makes raising finance easier, it enlarges investment expenditure. In the case of all producible assets, such as houses for instance, since the rise in asset price makes it exceed the cost of production, there is larger demand for newly-constructed assets and hence larger production of them. Thus the asset price bubble raises aggregate demand, and hence output and employment, well beyond what it would have been in the absence of such a bubble.

During the boom therefore the asset price bubble acts as a "super multiplier" to use Hicks' term (or "compound multiplier" to use Oskar Lange's term), i.e. an initial rise in the demand for an asset and hence in its price, which gives rise to an initial increase in its output, and hence in employment in the economy, is followed by a much larger increase in output and employment because of the asset price bubble which it generates. There would of course be, in all such cases, "super-multiplier effects" *through other channels as well*, e.g. the larger investment caused by the increase in output via the acceleration principle, which are well-known (in fact both Hicks and Lange coined their respective concepts to describe *these* effects). But in addition to all of them, there is also the super-multiplier effect operating through asset price bubbles which curiously has not received the attention it deserves (reflecting perhaps the fact that the influence of Kalecki who did not incorporate speculation into his argument about business cycles has been greater than of Keynes who did, though Keynes' manner of doing so, as we shall see, was not altogether satisfactory).

If for some reason however the rise in asset prices comes to an end, then speculators start deserting the asset like a sinking ship. The reverse mechanism sets in, with expenditure shrinking for two analytically distinct reasons: the first is simply the negative wealth effect, the operation in the opposite direction of the very forces mentioned earlier that served to accentuate the boom. The second is through the credit system. As asset prices fall, economic agents who have borrowed from banks, find themselves becoming insolvent, which in turn makes the banks insolvent. Credit therefore dries up, and in extreme cases, as during the Great Depression of the 1930s (or as is happening in the Ukraine at present), even depositors become chary of keeping their deposits with an insolvent banking system. Putting it differently there is a marked increase in liquidity preference, associated with a marked increase in the estimation of risk because of the perceived insolvency of borrowers. The pervasive desire, down the line, is to hold cash rather than private debt, and in extreme cases the preference is for *currency* and not even *bank deposits*. All through however increased liquidity preference is associated with an increased preference for *government debt*, in which wealth-holders' confidence remains unshaken.

These are two very different channels: the first would operate in principle even in a world where there was no debt; the second operates in a world where there is debt. One refers to the wealth loss on account of the asset price crash; the other refers to its fall out, associated with the *distribution of this loss across different groups of wealth-holders*.

Two obvious questions arise here. The first is: what triggers the initial increase in asset prices? This can happen for a variety of reasons, including the introduction of innovations, which has been given the pride of place by many in explaining business cycles. In short even if we take conventional "non-Keynesian" views of business cycles, like those for instance which focus on innovations as the key element in the cycle, this "Keynesian" factor of "speculative excitement" will still operate, superimposed upon this (or any other) key element.

The second question is: why does the boom collapse? It can happen for a variety of reasons, from tightness of money (Minsky), to a sudden waking up to the risks associated with the bubble (an almost reverse L-shaped risk premium curve, as a function of the level of asset prices), to the actual addition to the supply of the asset through larger production (which was the mechanism in Kalecki's theory of business cycles) which, in the present context, starts pulling expectations of capital gains downwards.

It is obvious however that such a speculation-sustained boom cannot be kept going indefinitely. To the extent that the latter set of factors, i.e. a suddenly increased perception of risk or the larger production of assets, operates to bring about a collapse of the boom, an easing of monetary policy at the height of the boom to keep it going, while it may postpone the collapse of the bubble, can not do so indefinitely. A camouflaging of the risks associated with the asset price bubble, such as for instance what the innovation of the "derivatives market" achieves, can also likewise postpone at best the collapse of the boom; and when the collapse comes it will be all the more severe for having been postponed, as we are witnessing at present.

A comment each on Keynes' theory of crisis and on Irving Fisher's (1933) theory of "debt-deflation" may be in order here, especially because of the strong influence that Fisher's theory seems to exercise on thinking on the American Left (via Minsky and the *Monthly Review*). While Keynes, as mentioned earlier, emphasized the role of "speculative excitement" during the boom, and recognized that the business cycle is associated with *a "crisis"* as the boom collapses, as distinct from *a mere cyclical downturn*, he saw this "crisis" as following from a collapse of the marginal efficiency of capital. Now a collapse in the speculative bubble has the same effect as a collapse in the marginal efficiency of capital, and may actually lead to the latter; but the two are not the same thing. By the very definition of the marginal efficiency of capital, if the expected yield from the asset remains unchanged (and there is no reason to believe that a change in the expected *capital gain* which is associated with the collapse of the bubble should *ipso facto* cause a change in the expected stream of yields), and if the cost of production of the asset remains unchanged, then the marginal efficiency of capital must also remain unchanged. A collapse in the inducement to invest because of the collapse in the asset price bubble therefore is not mediated through the marginal efficiency of capital (which

is an additional weakness of Keynes' theory of investment, apart from the well-known ones discussed by Kalecki[1]). By emphasizing the collapse of the marginal efficiency of capital, therefore, Keynes missed out on crucial aspects of the collapse of the bubble which his own theory was pointing towards.

Irving Fisher, as is well-known, emphasized "over-indebtedness" during the boom as the basic factor underlying the depression, since all efforts to reduce debt cause only price deflation, and with it unemployment and output loss, but no reduction in real debt. What is not clear from Fisher's analysis is: "over-indebtedness" relative to what; and why should there be such "over-indebtedness"? If we are talking about the introduction of innovations, as Fisher appears to be doing, there is no obvious reason why such introduction should not occur in a smooth manner, financed by debt that is growing steadily; the question of "over-indebtedness" does not necessarily arise. In fact the only reason why people should at all have debt levels that are unsustainable, and hence get "over-indebted" in this sense, is when the assets against which debt is incurred fall in value. In fact Fisher's theory really comes into its own in the context of asset price bubbles, though he himself does not appear to have linked it to such bubbles.

To miss this aspect of the bubble and to concentrate only on the size of the debt in explaining the crisis, as many on the American Left appear to do, is unpersuasive. It becomes logically untenable as well when *both public and private debt are lumped together to show the fragility of the system*, when quite clearly each of the two stands on an entirely different footing from the other: public debt becomes a prized asset to hold in a crisis while private debt is what all wealth-holders wish to substitute by money. The position that lumps together all debt and sees "over-indebtedness" as the cause of the crisis, should then frown on any fiscal deficit-financed government spending as aggravating the crisis rather than alleviating it. Now, there may be important political economy reasons why a deficit-financed government spending in a crisis would either not happen, or have other adverse consequences even as it alleviates the crisis in an immediate sense. But surely the argument that it would not alleviate the crisis but constitute instead an aggravation of the crisis, which the portmanteau "over-indebtedness" view would suggest, makes little sense.

To come back to the main argument then, in contemporary capitalism, with its developed financial markets, speculation which is necessarily rampant, plays as important a role in accentuating the boom as it does in precipitating a crisis. Booms in contemporary "free market" capitalism are necessarily speculation-driven. To truncate its effects, through financial regulation to prevent the crisis, also entails truncating the boom, i.e. causing unemployment even earlier (though perhaps to a lesser extent).

Interestingly, the case for such a truncation of the boom had been advanced by Dennis Robertson in the 1930s, and had been stoutly opposed by Keynes. In Robertson's view, full employment was an impractical objective. But stabilizing the economy at a certain level of employment below full employment was both wise and practical. Hence he argued that whenever the employment rate in the economy tended to exceed the average of say the previous ten years, the interest rate should be raised to truncate the boom; and likewise

[1] Kalecki's logical critique of Keynes' theory of investment was contained in his article on the business cycle published in the late1930s in *Economie Appliquee*. This critique is summarized in Joan Robinson (1965).

whenever the employment level tended to fall below such an average, the interest rate should be lowered to prevent such a slide into recession. By truncating booms and slumps in this manner, the economy, he thought, could be stabilized at an employment rate which was higher than the average that would emerge through booms and slumps.

Keynes was skeptical about this last claim; indeed he thought that the opposite was more likely to be the case. But in addition he also felt that Robertson's suggestion was "dangerously and unnecessarily defeatist. It recommends, or at least assumes, for permanent acceptance too much that is defective in our existing economic scheme" (1949, 327). He recommended, in contrast to Robertson, not a raising of the interest rate to truncate the boom, as a means of preventing the ensuing crisis, but a lowering of the interest rate to perpetuate the boom whenever it appeared to be running out of steam. "Thus the remedy for the boom", he wrote, "is not a higher rate of interest but a lower rate of interest! For that may enable the so-called boom to last. The right remedy for the trade cycle is not to be found in abolishing booms and keeping us permanently in a semi-slump; but in abolishing slumps and thus keeping us permanently in a quasi-boom" (1949, 322).

But, above all, taking the economy close to full employment and keeping it there was not a task exclusively of monetary policy; fiscal policy had to be used in addition, with the State playing a pro-active role in demand management. Keynes in short wanted the regime of "bubbles-sustained growth" such as characterized so-called "laissez-faire capitalism" in the era of finance, to be replaced by a regime of State-led growth, or more accurately, fiscally-stimulated and fiscally-sustained growth[2].

The Keynesian remedy was not accepted during the 1930s, because of the stout resistance of finance capital, which is invariably opposed to all State activism, except that directed towards the promotion of its own interests. Even Roosevelt's New Deal, after its initial success in bringing down the unemployment rate, once again gave way, under pressure from financial interests, to fiscal conservatism that precipitated the 1937 crisis. Ultimately it was only war preparation that got capitalism out of the Depression. Japan was the first country to come out of the Depression because of the armament drive of the military-fascist regime, followed by Germany after the Nazi take-over. The liberal capitalist economies started their war preparations only in the late 1930s to meet the growing fascist threat, and it is only then that they started overcoming the Depression.

The institutionalization of Keynesian demand management as a characteristic feature of a restructured capitalism had to wait for the post-war period when there was a changed correlation of class forces brought about by the war itself. The hegemony of finance capital was greatly weakened by the war; and the working class, which had made great sacrifices during the war, was not only unwilling to go back to the days of Depression and unemployment, but also became far more assertive politically (as witnessed for instance in the defeat of Winston Churchill's Conservative Party in the post-war British elections and in the enormous increase in the strength and popularity of the French and Italian Communist

[2] In drawing this contrast I do not mean that the "bubbles" are not themselves fiscally-aided. The dotcom and the housing bubbles in the U.S. for instance were aided by significant tax concessions by the government. But there is a difference between fiscal aid for a "bubble" and fiscally-sustained growth, which typically involves the erection of a regime that tries to restrict the formation of bubbles through regulatory measures.

Parties which had been active in the Resistance). This, ironically, was in sharp contrast to Keynes' own belief that the world was ruled by "little else" but the power of ideas: the choice of which ideas were to rule was, on the contrary, determined by the correlation of class forces.

The contradictions of the "Keynesian demand management" regime need not detain us here. Keynesian demand management produced, in the advanced capitalist countries, remarkably low unemployment rates, high levels of capacity utilization, and hence strong inducement to invest, resulting in high output growth, and, correspondingly, high labour productivity growth. High labour productivity growth in turn led to high wage increases because of the strong bargaining power of the workers in the new situation of low unemployment rates. This, together with the high social wages under the new regime, resulted in a distinct improvement in the living conditions of the workers, so much so that the period has been called by many "the Golden Age of Capitalism". At the same time however, the process of "centralization of capital" that Marx had highlighted led to the formation of ever greater concentrations of finance, during the Keynesian period itself, which ultimately overthrew one of the basic premises of the Keynesian regime, namely *national control over cross-border capital flows*. With "globalization" of finance, the capacity of the nation-State to pursue Keynesian demand management policies was undermined. The U.S. whose currency was generally deemed by wealth-holders to be "as good as gold", *de jure* during the Bretton Woods regime and *de facto* thereafter, could enjoy no doubt a degree of leeway in this respect, but this did not mean that it shunned "deregulation". The capitalist world economy in short entered its neo-liberal phase that was reminiscent in crucial respects of the pre-war period. Not surprisingly, financial crises which had disappeared during the Keynesian period began to reappear, the first major post-war financial crisis occurring in 1973. And the regime of "bubbles-sustained growth" that had characterized pre-war capitalism, also made its appearance, with its inevitable sequel, the crisis that we see now.

II

It follows then that the need today is not just to come out of the crisis, but to do so as part of a set of steps that simultaneously prevent the recurrence of such crises. And for the latter it is not enough to have "regulation" of the financial system; what is needed is the institutionalization of a regime, alternative to the current regime of "neo-liberal" capitalism, where the maintenance of near-full employment is no longer dependent upon the formation of "bubbles" in asset markets.

International finance capital, needless to say, will not countenance any regime change away from neo-liberalism; and even its panacea for coming out of the current crisis is that the capitalist States should merely "bail out" the "financial oligarchs" by providing the financial system with tax payers' money, *without effecting any change in this system's ownership*, and then simply wait for the next "bubble" to come up. But the pertinent question that arises is: what can be a minimal alternative democratic programme as against this? Let us start first by looking only at possible revival measures.

The fact that any recapitalization of the financial system using tax payers' money *must be accompanied by a nationalization of the system,* in the sense not just of the State acquiring ownership, but of doing so while giving *zero compensation to the existing owners and even to a whole*

category of creditors, is by now fairly widely accepted. What is equally widely accepted is the additional need for a fiscal stimulus, not in the form of tax cuts, which in the present context would have little demand-generating impact, but in the form of larger government spending; and if such spending is to have public sanction then it must be in areas that directly benefit the people, e.g. education, healthcare and the provisioning of essential collective consumption.

There is a tendency, especially in India where the official retreat from neo-liberalism is less marked than elsewhere, to argue that the fiscal stimulus should promote "infrastructure development" and that this should happen through "public-private partnerships", which essentially means that the government should hand over even larger amounts of money to private capitalists, to undertake mega-projects for the rich as a way out of the crisis. Since this is what the government was doing under the neo-liberal dispensation anyway, it amounts to using the crisis, caused by neo-liberal capitalism, as a means of further buttressing neo-liberal capitalism. This strategy's only departure from the strict neo-liberal programme is its acceptance of the need for a larger fiscal deficit; in every other respect it conforms to the neo-liberal programme, which makes it not just futile in the present context (when the inducement to invest is so low that even larger government munificence is unlikely to help in inducing larger private investment), but also undemocratic in a double sense: first, the choice of projects promoted invariably ignores people's priorities; and secondly, the expenditure of tax payers' money is better done directly through a government accountable to them than through transfers of questionable necessity to private capitalists.

But even assuming that the right fiscal stimulus is adopted by the State in each country, there is a further problem. Any single country adopting a fiscal stimulus package would find a part of the stimulus leaking away to other countries through imports. To prevent a situation where the increased debt of its own State goes to create employment elsewhere (and in countries like the U.S. this "leakage" would be quite substantial), the country in question will be inevitably tempted to adopt protectionist measures (of the sort that President Obama is already moving towards). Any such measures however would provoke other countries to have their own protectionist measures even as they too adopt fiscal stimulus packages. But such a scenario of sequential, uncoordinated stimulus packages supported by protectionism cannot be a particularly desirable one from the point of view of the world economy.

The reason is obvious. While protection to defend the prices obtained by peasants and other petty primary commodity producers, who, in Kalecki's terminology, are faced with demand-determined, as opposed to cost-determined, prices, is necessary and justified, protection of the "beggar-my-neighbour" sort will be counterproductive. True, since such "beggar-my-neighbour" policies would be sought to be enacted *together with fiscal stimuli* in each country, any facile comparisons with the 1930s period and conclusions drawn on the basis of such comparisons about all countries ending up with worse slumps as a result of such protectionist policies than they otherwise would have had, are unwarranted. Nonetheless, protectionism of this sort will be undesirable since such generalized protection would entail a lower vector of real wages for any given vector of money wages across countries. This, *apart from being undesirable in itself,* would also *ceteris paribus* have a demand-compressing effect, so that for any given magnitude of fiscal stimuli across countries the additional levels of employment generated would be lower than would have been the case otherwise.

Sequential uncoordinated fiscal stimuli combined with protection therefore will be a distinctly inferior option compared to coordinated fiscal stimuli of identical magnitudes. Hence a democratic agenda for overcoming the crisis must include a *coordinated fiscal stimulus* across a set of major countries, which in turn would require the imposition of controls over cross-border financial flows (so that the nation-States can have the autonomy to pursue such expansionary fiscal policies without having to worry about the possible "flight" of finance capital), and an arrangement for taking care of the increased surpluses and deficits on the balance of payments. The following arrangement for taking care of the increased surpluses and deficits suggests itself for inclusion in a democratic agenda for overcoming the crisis.

III

As is well-known, a basic problem with any international financial system is that while adjustments should ideally be undertaken by the surplus countries, they are precisely the ones who are under no compulsion to adjust. True, if instead of maintaining balance of payments surpluses they expanded domestic demand instead, especially through enlarged workers' consumption, then all economies, both the surplus and the deficit ones, would be better off: the surplus ones would be better off since the people there would enjoy higher living standards; and the deficit ones would be better off since they would experience larger aggregate demand leading to larger output and employment. But whether out of excessive caution (warding off potential currency crises) or out of mercantilist ideas of "national power" (which the holding of claims upon other countries gives), surplus countries have always been loath to make adjustments. This was as true of Germany and Japan earlier as it is of China today. And even the Bretton Woods system devised by Keynes had failed to set up a mechanism to force surplus countries to adjust.

But even though this must remain the objective of any international arrangement, a beginning can be made by ensuring that *the increments in surplus*, starting from a given initial situation and arising as a result of a coordinated fiscal stimulus, are put to use. There is an obvious justification for this: in the absence of a *coordinated* fiscal stimulus, the surplus would not have arisen at all. In other words, if a habitually-surplus country simply enlarged its own government expenditure then the most it can hope for is no worsening of its balance of payments compared to the initial situation. If it gets an additional surplus over and above what it had to start with, then *that is entirely because of the fiscal stimulus undertaken in other countries*. Its enlarged surplus in short is a booty that lands on its lap because of the actions of other countries. If this surplus is taken away from it, *then its employment and output would still remain unchanged*, but it would simply have been divested of this booty. Of course it is free to use this booty for raising the consumption of its own working population, but in that case there would be no *ex post* surplus left. If there is a surplus then *ipso facto* it is holding on to the booty thrown on to its lap by the actions of other countries. A case exists for divesting it of this booty.

The obvious way of doing so is to make the countries with increased surpluses on account of the coordinated fiscal stimulus, give these additional surpluses as grants, either directly or through some new international financial institution, to the less developed (or least developed) countries. The latter in turn must not be allowed to keep these grants as mere accretions to reserves, but to spend them on imports. *In fact they can enlarge their own fiscal deficits until the point where they can use up the entire grant given to them,* which would mean of course

that the increase in fiscal deficit they can sustain on the basis of these grants would be several times these grants. For instance if their import-GDP ratio is 0.2 and private savings ratio is 0.2 (all ratios assumed to remain constant), then a grant of $100 can sustain an increased fiscal deficit of $200. The coordinated fiscal stimulus provided by a group of countries initially can thus be generalized to become a coordinated stimulus for all countries of the world by the institution of such a system of grants.

With these grants, say of $100, the demand for imports, now emanating from the less (or least) developing countries will increase. Now, no matter which countries this import demand is directed to, it will succeed in eliminating all increases in surpluses and deficits. If these $100 given as grants are used to buy goods from the countries whose deficits had increased (and they would have increased by exactly $100 from the initial situation since *ipso facto* all increased surplus is accruing as grant), then the increased deficit would have been simply wiped out. If on the other hand the grant of $100 is used to buy goods from the increased-surplus countries, then they would be redirecting their sales from the increased-deficit to the grant-receiving countries which again would wipe out the deficit of the increased-deficit countries. Whichever way we look at it therefore a system of such grants will not only raise world output and employment, but also *eliminate all increases in the net indebtedness of countries relative to the initial situation of recession.* The grant-receiving countries will not get into debt. What would otherwise have been increased-deficit countries on account of the coordinated fiscal stimulus will have this increased deficit wiped out; so *ipso facto* would the increased surplus countries.

These grants, and the larger fiscal deficits they can sustain in the recipient countries, can in turn be made the basis for promoting food security in these countries, and hence, by implication, food security in the world as a whole. The per capita cereal output in the world economy has declined in absolute terms over the last two decades or more, and this fact has been at the root of the growing world hunger. The recession, as long as it lasts, will entail a generalization of hunger among the world's population because of the generalized income deflation it gives rise to. But after the recession gets over, since the increase in employment will mean that the newly employed would have shaken off the income deflation to which they had been subject during the period of their unemployment, the rest of the world's population will feel the impact of hunger even more acutely. To prevent this from happening, there has to be an increase in the rate of growth of world food output, which alone can promote world food security. The very mode of overcoming the recession therefore should be such that in the process food security is promoted. The system of grants should be used for this purpose as far as possible.

Such a system of grants therefore can kill four birds with one stone: first, it can bring about an improvement in the conditions of the people in the less (or least) developed countries relative to what would have obtained without such grants, and hence reduce global inequalities; secondly, it would give rise to larger world output and employment *over and above what the coordinated fiscal stimulus alone would have achieved*; thirdly, it would do all this without causing any increase in the net indebtedness of any group of countries relative to the very initial situation, i.e. prior to the coordinated fiscal stimulus itself; and fourthly, it can be used to promote world food security. Hence a coordinated fiscal stimulus combined with such a system of grants must form the cornerstone of a democratic anti-recession agenda.

To sum up this part of the argument, a democratic agenda for coming out of the recession must have at least five elements: first, the nationalization of financial institutions in the leading capitalist countries where they have basically become insolvent; second, controls on cross border financial flows; third, protection introduced to defend peasants and other petty producers of primary commodities (ideally through agreements among producing countries) in the case of all commodities whose world prices are "demand-determined" (as opposed to "cost-determined"); fourth, a coordinated fiscal stimulus to the world economy provided by a group of leading countries; and fifth, a system of grants whereby the increased surpluses generated by such a stimulus are given as grants to the less (or least) developed countries on the condition that they do not merely add these to their reserves.

IV

The most powerful opposition to any revival attempt of this sort will come from international finance capital. Finance capital, as mentioned earlier, is always opposed to an activist State except when the activity is exclusively in its own interest. This opposition which was expressed against the 1929 Lloyd George plan for public works based on government borrowing, which was also expressed against the coordinated fiscal stimulus idea suggested by Keynes, Blanqui and a group of German trade unionists during the Great Depression, and which had even succeeded in rolling back after a brief period of implementation the only non-militarist fiscal attempt to overcome the Great Depression that occurred in the 1930s, namely Roosevelt's New Deal, is even more powerful today than ever before. The strategy that finance capital would prefer is one of protecting the financial system through the injection of public money *without in anyway impinging on the interests of the existing owners and large creditors,* and of waiting for a new bubble to emerge (and even of getting the State to help the process of formation of some new bubble). Any proactive role of the State that impinges on the interests of finance capital, both through nationalization of the bulk of the existing financial system and through curbs on cross-border flows, not to mention the abandonment of "sound finance" will naturally be anathema for it.

But the question here is not just of choosing between two alternative agendas or two alternative solutions to the crisis, one favoured by finance capital and the other with a democratic content. The one favoured by finance capital will not even overcome the crisis; it will only succeed in prolonging the crisis. And this is dangerous for at least three reasons: first, the crisis is painful for the ordinary working people, the workers, the peasants, the petty producers, and the agricultural labourers. Anything that prolongs that pain is abhorrent. Secondly, any such prolongation of the crisis runs the risk of causing a price deflation. Since the long-term interest rate cannot at present be reduced any further in nominal terms (a fact that has led some people to talk of economies being caught in a "liquidity trap", though the "liquidity trap" is a problematical concept[3]), any such price deflation will lead to an increase in the real interest rate which will be extremely difficult to control and which will aggravate the crisis and make it far more intractable. Thirdly, any prolongation of the crisis runs the

[3] The concept of the "liquidity trap" used in the current context differs from the one normally associated with Keynesian economics. Keynes was talking about private wealth holders having an infinitely elastic demand for money at a certain interest rate, while in the current contextthe infinitely elastic demand for money in the current context must refer to *both private wealth-holders and banks*. For a critique of the use of this concept see Patnaik (2009).

risk of producing fascist and other dangerously divisive movements that thrive on unemployment. This phenomenon can extract a heavy social cost, as we know from bitter past experience.

The struggle between the two agendas therefore is a matter of immediate practical importance. Even if not all the elements of the democratic agenda are sought to be implemented immediately and even if not all these elements get the same degree of support, some elements at least need to be put into immediate practice. For this a struggle has to be launched against the hegemony of international finance capital.

References

Fisher Irving (1933) "A Debt-Deflation Theory of Great Depressions", *Econometrica.*

Keynes J.M. (1949) *The General Theory of Employment, Interest and Money*, Macmillan, London.

Patnaik P. (2009) "Speculation and Growth under Contemporary Capitalism", Kale Memorial Lecture, Gokhale Institute of Politics and Economics, January, 2009.

Robinson J. (1965) "Kalecki and Keynes", *Collected Economic Papers,* Vol.3, Blackwells, London.