

The World Economic Crisis: A Marxist Analysis

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The following is a lecture delivered by Nick Beams, national secretary of the Socialist Equality Party (Australia) and a member of the International Editorial Board of the World Socialist Web Site, to audiences in Perth, Melbourne and Sydney in November and December, 2008.

It is now clear that the greatest financial crisis since the Great Depression is on the verge of becoming the deepest global slump since the economic catastrophe of the 1930s. We could spend the entire time available for this lecture simply enumerating the myriad expressions of this crisis and examining their far-reaching implications. I propose here to deal only with some of the most significant.

On November 24, *Bloomberg News* reported that after the \$306 billion bailout of the US bank Citigroup, organised at midnight the previous day, the US government had now committed itself to providing more than \$7.76 trillion to the financial institutions and banks. This amount was the equivalent of half the American gross domestic product (GDP), or \$24,000 for every man, woman and child in the US.

Within 24 hours, however, the Bloomberg estimate was outdated after the Treasury announced that a further \$800 billion was being deployed to support mortgage companies Fannie Mae and Freddie Mac and launch a new initiative to provide credit to holders of student loans, auto loans and credit card loans.

One reads these figures and asks the question: who is going to bail out the United States?

Stock markets around the world have tumbled, with an estimated \$25-30 trillion wiped off the value of shares in the past six months. Around 38 percent of the value of major companies has been erased. General Motors, once the most powerful industrial concern in the world, teeters on the edge of bankruptcy.

According to official statistics, all the major areas of the world economy are now in recession: the United States, the eurozone, Britain and Japan.

The growth estimates for China and the so-called emerging markets, which, once upon a time—and I use the fairy-tale form advisedly—were supposed to provide a boost to the world economy, are now being revised downwards virtually on a daily basis.

Like the financial crisis that caused it, the economic slump is centred in the United States. The number of private sector jobs has fallen for the past 11 months straight. Some 533,000 jobs were lost in November—the worst monthly decline since December 1974—with predictions that losses in December will be even greater. At least one quarter of all US businesses plan to reduce employment next year. The mayor of Chicago, Richard Daley, recently warned of "huge" layoffs in the rest of the year, comparing today's "frightening economy" to that of the Depression years of the 1930s.

With unemployment rising and home prices continuing to slide—some 12 million homes in the US are said to be "under water", that is, worth less than the mortgages on them—consumer spending has dived.

US consumption spending, which comprises around 70 percent of gross domestic product, fell by 3 percent in the third quarter. According to a survey of economists conducted by Bloomberg, it will fall by a further 2.9 percent in the fourth quarter and 1.3 percent in the first quarter of 2009. Consumer spending has never declined for

three quarters in a row during the entire post-World War II period.

Consumer prices in October fell by 1 percent, the biggest monthly drop since 1947. But instead of lower inflation providing a boost to financial markets, it had the reverse effect. Wall Street took a dive on fears that deflation, which raises the real level of debt, could take hold.

The Detroit "Big Three"—Chrysler, Ford and General Motors—have been seeking a \$34 billion lifeline from the government in order to avoid bankruptcy. It is estimated that if one or more of the auto manufacturers were to collapse, around 3 million jobs could be wiped out across the US economy.

The statistics on the global economy are as bad, if not worse. According to the International Labour Organization (ILO), the financial crisis will lift world unemployment from 190 million in 2007 to 210 million next year. And the ILO has warned that the 20 million predicted increase could prove to be an underestimation "if the effects of the current economic deterioration are not quickly confronted."

Last week, in a desperate measure to try to combat the crisis, the Bank of England lowered its interest rate to 2 percent—equal to the lowest level since its founding in 1694.

In its latest global outlook report, the World Bank has forecast a growth rate in 2009 of just 1 percent for the world economy as a whole, and a contraction of 0.1 percent for the high-income countries. According to the Bank's chief economist, the world now faces "the worst recession since the Great Depression."

The OECD, which covers the world's major industrialised economies, has forecast contractions of 0.9 percent, 0.1 percent and 0.5 percent for the US, Japan and the eurozone respectively.

One of the most significant statistics concerns world trade. For 2009, the World Bank has forecast a decline of 2.5 percent in world trade volumes, compared with an increase of 5.8 percent this year and a rise of almost 10 percent in 2006. This will be the first time the actual volume of world trade will

have decreased since the deep recession of 1982.

On November 15, the leaders of the G20 group of countries, whose economies account for about 90 percent of global output, met in Washington to discuss proposals to meet the economic and financial crisis. It might have been better if they had not. The meeting demonstrated not only that the leaders of world capitalism are bereft of any program to deal with the situation, but the divisions among them are widening.

On the eve of the meeting, Bush, anxious to repulse calls for greater regulation, delivered a speech extolling the virtues of the "free enterprise" system. The summit, he insisted, had to be devoted, above all, to a reaffirmation that "free market principles offer the surest path to lasting prosperity". It was necessary to "move forward with the free-market principles that have delivered prosperity and hope to people all across the globe." One might have wondered whether the speech was actually being delivered by a satirist from "Saturday Night Live", following Tina Fey's success with Sarah Palin.

Three weeks before the summit, in a hearing before a US Congressional Committee, the high priest of the free market, Alan Greenspan, the former chairman of the Federal Reserve Board, had been forced to acknowledge the bankruptcy of the entire system he had been instrumental in building, and over which he had presided for almost two decades.

"Those of us who have looked to the self-interest of lending institutions to protect shareholder's equity, myself included, are in a state of shocked disbelief," he said. The risk management system, based on the use of financial derivatives, had not only got out of control but had helped exacerbate the crisis. "This modern risk-management paradigm held sway for decades. The whole intellectual edifice, however, collapsed in the summer of last year." The crisis had "turned out to be much broader than anything I could have imagined. It has morphed from one gripped by liquidity restraints to one in which fears of insolvency are now paramount."

Before the summit opened, the economics commentator of the *Financial Times*, Martin Wolf, explained why, in his view, preventing a global slump had to be the priority for governments and central banks. The idea that a quick recession could purge the world of past excesses was "ridiculous."

"The danger is, instead, a slump, as a mountain of debt—in the US, equal to three times GDP—topples over into mass bankruptcy. The downward spiral would begin with further decay of financial systems and proceed via pervasive mistrust, the vanishing of credit, closure of vast numbers of businesses, soaring unemployment, tumbling commodity prices, cascading declines in asset prices and soaring repossessions. Globalisation would spread the catastrophe everywhere. ... This would be a recipe not for a revival of 19th century *laissez-faire*, but for xenophobia, nationalism and revolution. As it is, such outcomes are conceivable. ... Everything possible must be done to prevent the inescapable recession from turning into something worse" [*Financial Times*, October 29, 2008].

In another pre-summit comment, the well-known international economist Barry Eichengreen warned it was far from clear that governments and central bankers were at all prepared for the difficulties that would follow as the crisis spread from Wall Street. "There is no agreement on what to do about the global economic downturn. Economically and financially there is a clear sense of things spiraling out of control again."

The problems confronting the leaders of the G20 and global economic and financial authorities are not simply of an intellectual character. The inability to reach agreement and the rise of economic conflicts and tensions among the major powers is, first and foremost, a product of objective contradictions rooted in the world capitalist system itself.

Take the question of regulation. Any analysis of the global financial system shows that some kind of international regulation is needed for the "efficient" operation of markets that are closely interconnected and integrated.

But to put such a system in place is impossible. The reasons lie in the very structure of the world capitalist economy. All markets are global in scope, but the world remains divided among capitalist powers—some greater, some lesser. Each section of capital is in a continuous struggle against its global rivals to maintain and advance its profit share. Those that fail to do so go under or are taken over by their more powerful rivals. In this struggle, each section of capital looks to its "own" national state as a political force through which it can advance its interests. There exists a conflict of each against all.

As the British magazine the *Economist* noted: "International finance cannot just be 'fixed', because the system is a tug-of-war between the global capital markets and national sovereignty. ... Governments broadly welcome the benefits of global finance, yet they are not prepared to set up either a global financial regulator, which would interfere deep inside their national markets, or a global lender of last resort." There is a fundamental dilemma, it concluded: "[I]nternational rules require enforcement, but nation-states demand sovereignty."

All the participants at the G20 summit, along with their numerous advisers and economists, agreed that the growth of protectionism would have disastrous consequences for the world economy. It is an intellectual given that the Smoot Hawley Act of June 1930, which raised tariff barriers in the US, played a decisive role in sparking the series of retaliatory measures that contributed to the disastrous two-thirds contraction in world trade from 1929 to 1933.

However, not only did the commitment, in the G20 summit communiqué, to eschew protectionist measures hang in the balance until the final hours, it was largely meaningless. This was made clear in a rather caustic comment by the foreign editor of the British *Daily Telegraph*.

"With no evident irony, the statement says; 'We underscore the critical importance of rejecting protectionism and not turning inward in times of financial uncertainty. In this regard, within the next 12 months, we will

refrain from raising new barriers to investment or trade in goods and services.'

"What complete nonsense. Leave aside the unilateral bailout of banks in nation after nation that left, among other things, European Union competition policy in tatters. They were said to be essential. Where does it stop?"

"General Motors, Chrysler and Ford are about to be given billions of dollars, presumably on the grounds that their failure would do as much damage to the American economy as a failure of financial institutions. If bailing them out is not a 'new barrier ... to trade in goods', I have absolutely no idea what is. Someone needs to tell the Americans that signing a communiqué with fingers crossed behind the back does not work outside the playground.

"And in case anyone thinks I am unfairly singling out the Americans, the coming rescue of Detroit is just a convenient and huge example. I can assure you the same arguments are being prepared to help, for example, Alitalia in Italy and other large companies elsewhere" [Comment by Adrian Michaels, foreign editor of the *Daily Telegraph*, published in the *Australian*, November 18, 2008].

The author of this comment may well consider that he has taken a stand on principle. However it is significant that his position reflects precisely that of British capital, which has little manufacturing industry left to protect, but which is concerned that the financial operations of the City of London should not be constricted in any way by the new regulatory mechanisms proposed by Monsieur Sarkozy, the representative of French capital and industry.

Disagreements abound, not only on the issue of finance and trade, but on government intervention. The European powers are deeply divided, as has been made clear by the very public conflict over the size of any European Union stimulus package.

Consider *Newsweek's* extraordinary interview with German finance minister Peer Steinbrück, published in its December 6 edition. Steinbrück was responding to criticisms from France and the EU

Commission that the German government should do more to try to stimulate its economy.

"We have a bidding war," he told *Newsweek*, "where everyone in politics believes they have to top up every spending program that's been put to discussion. I say we should be more honest to our citizens. Policies can take some of the sharpness out of it, but no matter how much any government does, the recession we are in now is unavoidable. When I look at the chaotic and volatile debate right now, both in Germany and around the world, my impression and concern is that the daily barrage of proposals and political statements is making markets and consumers even more nervous. Still, Brussels is pressing for a joint European approach. For a while the position in Brussels and a few other places has been 'We're now very much for setting up large-scale spending programs, but we're not really going to ask what the exact effects of those might be. And since the amounts are so high, well, let's get the Germans to pay because they can'."

**By Nick Beams
20 December 2008**

The following is the second part of a lecture delivered by Nick Beams, national secretary of the Socialist Equality Party (Australia) and a member of the International Editorial Board of the World Socialist Web Site, to audiences in Perth, Melbourne and Sydney in November and December, 2008. [Part 1](#) was posted yesterday and parts [3](#), [4](#) and [5](#) will be published next week.

The escalating antagonisms between the major capitalist powers are the result not of intellectual deficiencies, or an incorrect political program, or an inability to see the dangers ahead. They arise from contradictions within the capitalist order itself—contradictions that will intensify as the global slump deepens and which, at a certain point, will become the basis for political and military conflicts.

The questions we need to probe are the following: how has this financial crisis come about? How did problems involving \$34 billion

in US subprime mortgages, which emerged 18 months ago, morph into the catastrophe now engulfing the \$57 trillion US financial system and financial markets the world over?

And furthermore, how is it that the lives of hundreds, no, thousands of millions of people around the globe are threatened by a crisis arising from a financial system in which they are not involved, over which they have no control and about which they have little or no knowledge? How is it that highly complex financial operations involving things such as collateralised debt obligations, credit default swaps, and asset-backed securities can have such a far-reaching impact on their daily lives? Why has this financial crisis led to a breakdown in the global capitalist order, giving rise to the very real threat of depression and war? How has all this happened and, on the basis of our analysis, what must now be done? These are the issues with which we will be grappling in this lecture.

The ABCs of capitalism

In order to grasp the processes at work in the world of finance and their impact on the so-called real economy, we need to consider some of the ABCs of the capitalist mode of production.

The driving force of capitalism is not production for use or need, or even production for the market as such, but the accumulation of capital—the making of profit. In its simplest form, the process of accumulation begins with a mass of capital in the money form M , which is turned into a new and greater quantity of capital, M' , that is, the initial quantity of capital plus an increment, ΔM ("delta M ").

The source of this increment is the surplus value extracted from the working class in the process of production. Money, as capital, is used to purchase the means of production plus the labour power of workers. This labour power, or capacity to work, is a commodity available in the market, along with other commodities. The value of this commodity—the labour power that the worker sells to the capitalist in the wage contract—is determined by the value of the food, clothing,

housing and other necessities of life needed to sustain the worker and the workers' family. But the value of these necessities (the worker's wage) is not the same as the value added by the worker to the commodities supplied by the capitalist in the course of the production process. In other words, the worker's wage is less than the value he or she contributes in the production process. This difference is the source of surplus value. Labour power is consumed in the production process, but the commodities produced by it have additional, or surplus, value embodied in them. They are then sold on the market to realise M' , comprising the initial M plus an increment ΔM —the profit made by the capitalist out of the production process.

The capitalist mode of production sets in motion a vast accumulation of the forces of production. As Marx noted in the *Communist Manifesto*, in contrast to all previous modes, capitalism involves the continuous revolutionising of the means of production. This is inherent in the system itself. Accumulation depends on increasing the productivity of labour, and the key to increasing labour productivity is the development of the productive forces. The pressure of competition drives this process forward. Every section of capital must strive to develop the productivity of labour on pain of extinction.

This ever-increasing scale of the production process induces changes in the financial structure of the capitalist economy. It means that the capital now required to set in motion the process of accumulation—the initial amount, M —far outgrows the capacity of individual capitalists. It has to be drawn from the resources of society as a whole. Two great financial developments make this possible: the rise of the credit and banking system, and the formation of joint-stock or shareholding companies.

Credit, made available from the pool of money gathered up in the hands of the banks from all corners of society, provides the capitalist firm with resources on a scale far beyond the capacities of an individual or even a group of individuals. The functioning

capitalist, Marx explains, becomes a mere manager of other people's money. Without this money, Rupert Murdoch is an ordinary citizen. But with the resources of numerous banks placed at his disposal, he is a colossus, invited to deliver the Boyer lectures on ABC radio, explaining how we all should live.

In return for the provision of capital, the bank receives a portion of the surplus value extracted from the working class in the form of interest payments. The loan agreement with the bank, or the issuing of a bond by the company, entitles the creditor to regular interest payments. That is, the holder owns a title to income.

In the case of the joint stock company, established through the issuing of shares, the shareholders, in return for supplying money capital, receive a title to property. They do not have a right to a portion of the company. As a shareholder of a retail chain, you cannot go into a store and claim some of the merchandise, on the grounds that you are a part owner of it. The merchandise is the property of the incorporated person, the company. What you are entitled to is a portion of the profit, in the form of a dividend.

With the development of credit and shareholding we have the creation of new markets—financial markets—in which these titles to income, bonds and shares, are bought and sold. And as the prices of these financial assets rise and fall, so profits can be made by buying and selling them.

Here I want to emphasise that there are not two forms of capital. The money that was supplied, either as credit or through share subscription, has been deployed to purchase labour power and the means of production. It has become productive capital engaged in the process of extracting surplus value from the working class. It does not exist in the form of money as well. The shares and bonds are what Marx called "imaginary" capital, or fictitious capital. They are, in the final analysis, titles to income, to a share of the surplus value extracted by productive capital.

However, in the world of finance, of fictitious capital, it is possible to make great profits by buying and selling financial assets.

This is an enchanted world, a world of illusion, because here it is possible to make money simply through the manipulation of money. Money, through the payment of interest, seems to accumulate as a natural function of its existence. Money begets money as Nature herself nurtures the growth of plants and animals. How could labour possibly be the source of all profit when clever manipulations and trades by financial operators can result in the accumulation of vast wealth?

The enchanted world of finance not only engenders illusions in the minds of its inhabitants and those who profit from it, but also in the minds of those who would try and abolish it. From the very earliest days, financial markets have been denounced by those who would like to expunge or at least control them, but without overturning the capitalist economy as a whole.

"Regulate the bad side of capitalism!" is their catch-cry, so that the good—that is, capital in the productive form—might be able to grow and society advance. Insofar as finance capital is necessary, ensure it works for society as a whole! But, as Marx explained more than 150 years ago, such efforts are based on an illusion. The "good" cannot be separated from the "bad" and, in fact, it turns out that the "bad" is often the very driving force of historical development.

As the founder of scientific socialism noted in relation to the joint stock company: "The world would still be without railroads if it had to wait until accumulation had got a few individual capitals far enough to be adequate for the construction of a railroad. Centralisation, however, accomplished this in a twinkling of an eye, by means of joint-stock companies" [Marx, *Capital* Volume I, p. 780].

Fictitious capital and the growth of debt

In the light of these ABCs let us now probe the present financial crisis. Numerous statistics demonstrate the growth of the financial system over the past three decades. One of the most important indicators is the level of debt.

In 1981 it is estimated that the US credit market was 168 percent of GDP. By 2007 it

was 350 percent. Financial assets were five times larger than GDP in 1980, but over ten times as large in 2007. Moreover this debt has been increasingly used to finance operations in the financial markets themselves, rather than to expand productive capital. The debt taken on by banks and other financial institutions rose from 63.8 percent of US GDP in 1997 to 113.8 percent in 2007. Debt issued by US financial institutions nearly doubled between 2000 and 2007. And this debt has balanced, ever more precariously, on an ever-smaller capital base. In 2004, large investment banks had an asset to equity ratio (a measure of the extent of debt leveraging) of 23. By 2007 this had risen to 30.

Goldman Sachs, for example, used its \$40 billion of equity as the foundation for assets worth \$1.1 trillion. Merrill Lynch's \$1 trillion of assets rested on \$30 billion of equity.

The reason for such large leveraging ratios lay in the enhanced profit rates they provided. Consider the following simple scenario: If an asset purchased for \$100 million increases in value by 10 percent during a year (worth \$110 million at the end of the year), and if the purchase of this asset is financed by equity capital of \$10 million and borrowings of \$90 million, at an interest rate of 5 percent, then the profit at the end of the year, after interest of \$4.5 million (5 percent of \$90 million) has been paid, will be \$5.5 million. This means a profit of \$5.5 million has been made on an initial outlay of \$10 million, giving a rate of return of 55 percent.

The key to the process is the increase in asset values, fueled by cheap credit. If money is cheap it will pour into asset markets, bidding up prices, and providing large profits. The market may be in stocks and shares, or in commodities, or in housing.

Of course, it does not take any great intellectual capacity to see that such Ponzi schemes, involving the creation of asset bubbles, must eventually collapse. Why then did not at least some in financial circles call a halt? Why the herd mentality?

Involved here were not individual failings or a lack of intellect, but the very structure of the financial market itself. So long as credit is cheap and asset prices are rising, every financial institution is forced to participate. If, say, a particular fund manager sees the writing on the wall and decides to opt out, his institution will lose out in the competitive struggle for profits. His clients will simply go elsewhere, where bigger profits are on offer. It does not matter that he is right, and a collapse will eventually take place. So long as the collapse occurs across the market, no one involved loses their competitive position.

As the CEO of Citigroup Chuck Prince put it in July 2007, on the eve of the subprime crisis: "When the music stops, in terms of liquidity, things will be complicated. But as long as the music is playing, you've got to get up and dance. We're still dancing."

Now the music has stopped.

The subprime mortgage crisis was the trigger for the implosion that is now seeing the collapse of the mountain of debt accumulated not just over the previous few months, or even years, but for several decades.

To understand the mechanisms behind this implosion, take the following simple example. Suppose that an asset valued at \$100 million, which had an expected return of \$10 million, or 10 percent, now only returns \$5 million or 5 percent, then the value of that asset will drop to \$50 million. To put it another way, an investor seeking a rate of return of 10 percent would have been willing to pay \$100 million for the asset. Now he will only pay \$50 million. The value of the asset in the market has halved.

But suppose the asset has been purchased with borrowed funds, say \$90 million. Notwithstanding the fact that the market value of the asset has declined, the debt to the bank remains \$90 million. The asset, however, is now worth less than the debt incurred to purchase it. How will the bank be repaid? Other assets may have to be sold to obtain cash. But to the extent that this takes place across the board, the value of

those particular assets will fall and the crisis will worsen.

We said earlier that fictitious capital is a claim on income, the source of which, in the final analysis, is the surplus value extracted from the working class. But capital can grow far beyond the basis on which it ultimately rests. Financial market operations result in a massive growth in fictitious capital. At a certain point, however, this expansion comes to a halt and a crisis erupts.

The crisis is an expression of the reassertion of the fundamental laws of the capitalist economy. Its source lies in the fact that the claims of capital have vastly outgrown the available mass of surplus value. Capital must seek to overcome the imbalance. How is this accomplished? Through two interconnected processes: by intensifying the exploitation of the working class in order to expand the mass of surplus value and, above all, by bankrupting and eliminating whole sections of capital, thereby wiping out their claims to the available surplus value, and restoring the shares of those sections of capital that remain.

In a recent speech Kevin Warsh, a governor of the US Federal Reserve System, noted that the issues in the current financial crisis went far beyond subprime mortgages and pointed to the wider processes now unfolding.

"If the challenges to the economy were predominantly about the value of housing stock, my focus today," he told his audience, "would be narrower than the establishment of a new financial architecture. So, what diagnosis, beyond housing weakness, is consistent with the unprecedented levels of volatility and dramatic financial market and economic distress? I would advance the following: We are witnessing a fundamental reassessment of the value of virtually every asset everywhere in the world" [Kevin Warsh, *The Promise and Perils of the New Financial Architecture*].

This "reassessment", however, does not occur through some kind of accounting procedure. It takes place, as Marx drew out, through "violent and acute crises, sudden

forcible devaluations, an actual stagnation and disruption in the reproduction process, and hence to an actual decline in reproduction" [Marx, *Capital* Volume III, p. 363]. In short, it takes place through a violent economic contraction, whose severity depends on the extent of the initial over-accumulation of capital. In today's conditions, we are speaking of processes that have already led to the implosion of one economy, Iceland, with even bigger ones, Ireland and even the UK, to follow.

The violent economic contraction, to which Marx refers, was described in the infamous advice provided to US President Herbert Hoover in 1931 by his Treasury Secretary Andrew Mellon: "Liquidate labour, liquidate stocks, liquidate the farmers, liquidate real estate. Purge the rottenness out of the system. High costs of living and high living will come down. People will work harder, live a more moral life. Values will be adjusted, and enterprising people will pick up the wrecks from less competent people."

Insofar as they have a theory of financial and monetary policy, US financial authorities have acted on the belief that they could avert the outcome advocated by Mellon through the correct use of monetary policy.

Milton Friedman and Anna Schwartz in their book *A Monetary History of the United States* advanced the theory that the "great contraction" was caused by the incorrect policies of the US Federal Reserve. In the years following the book's release this theory has become "conventional wisdom."

A vociferous advocate of the capitalist "free market", Friedman was motivated by the desire to demonstrate that the 1930s Depression was not a consequence of its failings and contradictions but of contractionary monetary policies. Had they not been implemented, there would have been a recession, but not the economic disaster that actually occurred.

Acceptance of the Friedman hypothesis has meant that whereas Mellon's advocated liquidation in response to a financial crisis, the Fed's policy, under Alan Greenspan and now Ben Bernanke, has been monetisation.

This began in 1987, when Greenspan, shortly after his appointment, reacted to the October stock market crash by opening up the Fed's credit spigots. In every succeeding financial crisis—the Asian crisis of 1997-98, the Russian default of 1998, the collapse of Long Term Capital Management through to the collapse of the tech.com and share market bubble in 2000, and the subprime crisis of 2007—the same policy has been pursued. Interest rates have been cut and credit conditions eased.

Throughout his term, Greenspan insisted the Fed's task was not to try to prevent the formation of asset bubbles or to deflate them when they emerged, but to clean up after they collapsed. In practice, this meant that the collapse of one bubble would be countered by the creation of another through the provision of cheap credit.

Bernanke shares Greenspan's outlook. He defined his position in September 2004 thus: "For the Fed to interfere with security speculation is neither desirable nor feasible. ... [I]f a sudden correction in asset prices does occur, the Fed's first responsibility is ... to provide ample liquidity until the crisis has passed" [cited in Peter L. Bernstein, Introduction to Friedman and Schwartz, *The Great Contraction*, Princeton 2008].

For the 20-year period following the stock market collapse of 1987 this modus operandi appeared to be effective. Now it has broken down. In the 16 months since the current crisis first emerged, various attempts have been made to halt it through bailout operations. Unlike the experiences of the 1980s, the 1990s and the early years of the present decade, they have, however, failed.

In early October, the US Congress granted Treasury Secretary Henry Paulson \$700 billion in bailout funds under the Troubled Asset Relief Program (TARP).

The TARP's stated purpose was to buy up so-called "toxic assets" from the banks and major financial institutions. In effect this meant using the resources of the US Treasury to maintain fictional asset values across the board. But on November 12, barely a month after the passage of the

TARP, Paulson announced he was abandoning this plan. Asked to explain why, he replied: "The situation worsened, the facts changed."

Paulson was impaled on the horns of a dilemma. If the government paid the true value for these near worthless assets, the banks that held them would be forced to take massive losses. On the other hand, if the government paid the inflated values necessary to avoid these bank losses, the \$700 billion would be but a drop in the bucket.

In other words, Paulson's change of mind expressed his recognition that the crisis was so large that the previous 20-year policy of pumping up asset values could no longer be continued. Whole sections of capital were going to have to be liquidated. Thus the TARP funds are being used to recapitalise banks and other financial institutions—at least those deemed worthy of saving, or with the closest connections and ties to the administration—while others will be allowed to go to the wall.

In short, the attempt to evade the laws of the capitalist economy through the use of monetary policy has come to an end. Those laws are now asserting themselves as they did in the 1930s, in the same manner that, as Marx explained, the law of gravity asserts itself when a house collapses about our ears.

Two fundamental contradictions

Having pointed to the extent and consequences of the massive devalorisation of capital that has now begun, we now need to deal with the following questions. What are the origins of this crisis? How did it develop to the extent that it now threatens the world's people with the kind of economic, social and political disasters that characterised the 1930s?

Is this a crisis of policy, of inherent greed, a product of slack regulation by central bankers and governments? Are we perhaps all to blame, as one rather ignorant academic wrote in his column published in the *Australian* on Monday November 24, or does the crisis arise out of contradictions inherent in the foundations of the capitalist mode of production?

In order to provide answers, we need, once again, to consider some ABCs of Marxist political economy.

Capitalist society is marked by a profound contradiction: between the material development of the productive forces, which it promotes, and the social relations within which this development takes place.

If we study the economic history of the past 150 years this contradiction—between the material productive forces and the social relations of production—has emerged in two forms. The first is the contradiction between the global development of the productive forces under capitalism, and the nation-state system in which the political power of the bourgeoisie is grounded. That contradiction, as we discussed in relation to the recent G20 meeting, has once again assumed an acute form.

The second is the contradiction between the growth of the productive forces on the one hand and the social relations of capitalist production, based on the private ownership of the means of production and the exploitation of the working class through the system of wage labour, on the other. This contradiction manifests itself in the tendency of the rate of profit to fall and the crises produced by it.

The tendency of the rate of profit to fall arises from the fact that while labour is the sole source of surplus value, and therefore profit, expenditure on labour power comprises an ever smaller portion of the total capital outlaid by the capitalist. This is an expression of the continuing growth of the productive forces and increased productivity of labour. But what it means is that to expand the total capital at the same rate, the same amount of labour must produce an ever-increasing amount of surplus value.

Let us utilise these insights to assess the present crisis. The origins of the crisis lie in the crisis of capitalism that erupted at the beginning of the 1970s—the end of the post-war boom—and the way it was overcome.

The demise of the post-war boom was marked by two major developments: the collapse of the Bretton Woods Agreement of 1944, which had ushered in the system of

fixed currency exchange rates, and a sharp fall in the rate of profit in every major capitalist country. This profit decline led to a recession in 1974 followed by the onset of stagflation—high inflation combined with high unemployment—at the end of the decade.

The Bretton Woods Agreement was one of the pillars of the post-war economic order. It fixed the value of national currencies in terms of the US dollar, which, in turn, was tied to gold at the rate of \$35 per ounce. The agreement was put together after more than two years of sustained work in British and American government circles to ensure the resumption of world trade, the fear being that if this were not done and there was a return to depression, revolution would erupt.

The agreement did its work, resulting in an expansion of trade and then investment. However, this very expansion exposed the contradiction lying at the heart of the Bretton Woods system—between a global economic expansion and currency systems still grounded on the national state.

For a time, the overwhelming economic superiority of the United States was able to overcome this contradiction as the dollar, backed by gold, functioned, in effect, as world money. But by the end of the 1960s a crisis was developing. It took the form of a dollar overhang—the dollars outside the United States in world markets vastly exceeded the amount of gold held in Fort Knox that was supposed to be backing them.

Various figures indicate what was underway. By 1968 the volume of dollars circulating outside the United States had grown to \$38.5 billion, from just \$5 billion in 1951. This amounted to \$23 billion more than US gold reserves.

Moreover, the money circulating outside the US provided the basis for a new financial network, the so-called euro-dollar market. Banks found dollar resources were available that were outside the control of national authorities. Throughout the 1960s attempts were made by the Kennedy, Johnson and Nixon administrations as well as by British authorities to control the international movements of money and maintain the

stability of the Bretton Woods system. But their attempts were thwarted by the operations of the euro-dollar market.

With efforts to regulate being undermined at every turn, US President Nixon cut the Gordian knot and removed the gold backing from the US dollar on August 15, 1971. The alternatives, such as imposing a recession in the US to reduce the trade deficit, clamps on US foreign investment and a reduction in US global military activities at the height of the Vietnam War, aimed at reducing the outflow of dollars, were simply not viable.

After August 1971 attempts to maintain a regulated currency system rapidly collapsed and in 1973 the floating dollar regime began.

In the final analysis, Bretton Woods foundered because the very expansion of world trade and world investment to which it had given rise—a global expansion of capital—could not be contained within a system of national regulation. The contradiction between world economy and the nation-state system had reasserted itself.

We now need to trace the development of the other central contradiction.

Following the immediate post-war economic and political restabilisation, the ensuing boom seemed like a golden age, which would continue indefinitely. Now, it was claimed, the seemingly intractable problems that had beset world capitalism after the eruption of World War I in 1914 could be overcome, or at least kept at bay. This would be done through the judicious use of so-called Keynesian techniques of economic management, based on the regulation of global capital flows on the one hand and the use of demand-management techniques by national governments on the other.

However, the "golden age" lasted barely a generation. By the end of the 1960s the rate of profit was beginning to fall. This tendency had been temporarily overcome by the extension of the Fordist system of assembly-line production from the United States to the rest of the world. Assembly line production, through the enormous increases in productivity it effected, had increased the rate at which surplus value could be extracted

from the working class, so boosting profits. But after a quarter of a century, the process of catching up was coming to an end.

In 1974-75, after a period of rapid inflation, the world economy entered a recession. Recessions had developed during the boom, but they had given way to periods of even greater economic growth. The curve of capitalist development had continued to move up.

That was not what occurred after the recession of 1974-75. Pre-recession conditions were not restored and world capitalism entered a period of much slower growth, marked by rising unemployment and inflation—a phenomenon dubbed "stagflation". Keynesian measures, based on government spending to boost the economy, proved to be of no avail. In fact, they only worsened the situation by increasing the rate of inflation. Companies failed to respond to increases in effective demand by boosting production, as Keynesian theory suggested they should, but sought instead to lift their depressed profit rates by increasing prices while looking, at the same time, to cutting their workforce.

These great shifts in the economic base of society, starting from the mid-1960s, gave rise, as Marx had explained they would, to far-reaching political shifts. The period from 1968, beginning with the May-June events in France, to 1975, and the downfall of the right-wing Salazar dictatorship in Portugal, was one of immense revolutionary upheavals.

In every case, however, the struggles of the working class were betrayed by its social democratic and Stalinist leaderships, with the assistance of various radical tendencies. All of them promoted the illusion, in one way or another, that the bureaucratic apparatuses dominating the working class could be pressured to the left.

The betrayal of the revolutionary strivings of millions of workers around the world, and the resultant restabilisation of capitalist rule, did not signify that the economic contradictions lying at the base of this political turbulence had been overcome. How they were temporarily alleviated, and the way the measures that were adopted led to their

eruption once again, but in an even more explosive form, constitutes the history of the world economy and the global financial system from the 1970s to the present day.

The collapse of the Bretton Woods Agreement in 1971 marked the end of the dollar's role as a stable anchor of the world monetary system. More than that, it signified that no national currency could take on that role.

Many here will never have experienced fixed exchange rates. But when I was a boy, my grandfather would send me one British pound every year for Christmas, and I could exchange that pound, each year, for exactly 25 Australian shillings. The rate never changed. The same was true of every currency. But in 1971 this certainty came to an end.

In the early 1970s, in the absence of a firm foundation for the international monetary system, new mechanisms were developed to cover the risks arising from the new currency movements. Consider an Australian importer of a piece of machinery. A deal that would have seemed very good, and potentially highly profitable, when the machine was ordered from, say, the United States, could result in a major loss if the Australian dollar had lost ground against the US dollar by the time full payment became due, on delivery, six months later.

It is from this period that we can trace the rise of financial derivatives.

A derivative is defined as a financial contract or financial instrument, the value of which is derived from the value of something else.

Derivatives have existed for a long time. The most well known are futures contracts, in which a contract is made to deliver a certain quantity of a commodity at a certain price at a certain time. These contracts were developed in the markets for agricultural products to try to eliminate the effect of movements in price between the time when a crop was sown and when it was brought to market. If the price at which the crops were to be sold could be fixed in a futures contract, then some degree

of certainty could be brought into the production process.

Financial derivatives mark a new development. No longer do contracts relate to physical commodities, but to money and other financial assets. In 1972, the year after the demise of the Bretton Woods Agreement, a market in currency futures was launched on the Chicago Mercantile Exchange. This market enabled importers and exporters, as well as financial institutions, to hedge against currency fluctuations, under conditions where currency movements could effectively wipe out profits from business deals overnight.

The currency futures contract was only one of many new financial derivatives that were to develop in the next period.

In 1973 a major development occurred when two academics, Fischer Black and Myron Scholes, developed a formula for pricing options. While a futures contract locks in participants to buying or selling, an option is a kind of insurance. In return for the payment of a premium, it gives the buyer the right to buy or sell an asset at a certain price within a specified period. If prices do not move in the way that was anticipated, then the option has no value and the buyer loses only the premium. In 1973 the Chicago Options Exchange was established for trading, and in 1975 the Chicago Board of Trade introduced the first interest rates futures contract.

Options provided the means for making big profits, as we can see from the following numerical example. A purchaser buys an option to buy a share for \$50 in six months time. The cost of the option is \$5. The outlay for an option on 100 shares will therefore be \$500. Suppose that after six months the price of the share has risen to \$60. The purchaser then exercises the option and makes a profit of \$5 on each share: \$60 minus \$50 minus the \$5 per option. This brings a total profit of \$500 on an outlay of \$500, that is, a profit rate of 100 percent.

Consider what would have happened if the purchaser instead simply bought 100 shares for \$50 each and held them for six months. The profit in that case would be

\$1,000 (the \$10 increase in the share price multiplied by 100) on an outlay of \$5,000, that is, at a rate of 20 percent. The use of the option has yielded a much higher rate of profit.

By the same token, if the shares had fallen to say \$49, rather than risen to \$60, then the option purchaser would have lost \$500, a capital loss of 100 percent, whereas the share purchaser who held the shares for six months would have only lost \$100 or 2 percent of his or her original investment of \$5,000. Options offer greater rewards and also greater risks.

With increased trading in options after 1973, other types of derivatives were developed, including the currency swap, in which buyers could swap bonds issued in one currency with bonds in another, depending on their assessment of currency movements. Then came the interest rate swap, in which fixed interest rate payments could be swapped with variable rate payments and vice versa. In the last decade, the credit default swap has emerged, in which the holder can insure against the issuer of a bond defaulting on payment. These contracts can be made through an exchange, or, as has increasingly been the case, in arrangements between two parties in so-called over the counter (OTC) agreements.

While their origins lie in the attempt to protect against risk, derivatives become a source of speculation, in which vast profits can be made from correctly judging the movements of financial variables. Myriad statistics indicate the explosive growth of these financial instruments over the past three decades.

Foreign exchange transactions in the world economy increased from \$15 billion per day in 1973 to \$80 billion per day in 1980 and \$1.26 trillion by 1995. In 1973 world trade in goods and services constituted 15 percent of these transactions. In 1995 it constituted just 2 percent. This explosion in foreign currency dealings has been mainly the result of financial, not trade, transactions.

The growth of derivatives has been even more spectacular. According to the Bank for International Settlements, the notional

amount—the value of the underlying asset on which the derivative is based—for OTC contracts was \$683.7 trillion at the end of June 2008. This is an amount equivalent to more than ten times world output. Thirty-five years ago, in 1973, financial derivatives were virtually non-existent.

The daily turnover of global currency markets has increased 50-fold since 1980, and now stands at about \$1.9 trillion per day. Of this, two thirds is transacted in derivatives markets and three quarters of this derivative trade, that is, half the overall market, is foreign exchange swaps.

The financialisation of the American economy

As we have seen, one impetus for the rise of derivatives came from the uncertainty generated by the collapse of the Bretton Woods system and the increased risk posed by currency fluctuations.

There is another, even more powerful force at work. This arose from changes in the mode of accumulation over the past three decades, above all in the United States.

When Nixon removed the gold backing from the US dollar in 1971 his intention was to maintain the financial dominance of American capitalism. But by the end of the 1970s, that was far from assured. The value of the dollar fell sharply, profits were declining, the stock market was down and the US economy was in the grip of stagflation.

In October 1979 Paul Volcker—who has recently been selected by President-elect Obama to be one of his key economic advisers—was appointed to the position of chairman of the US Federal Reserve Board. Volcker embarked on a program of interest rate hikes under the banner of anti-inflation.

The "Volcker shock," as it became known, sent interest rates to record highs and led to the deepest recession since the 1930s. It was accompanied by an offensive against the working class, starting with the Chrysler bailout in 1979 and the smashing of the air traffic controllers strike in 1981 and continuing right through the 1980s. Millions of jobs were destroyed and whole sections of industry wiped out.

The result was a transformation in the structure of American capitalism. From the end of the Civil War in 1865, American capitalism's rise to power had been based on its industrial prowess. American methods of production had proven to be the most efficient and the most profitable in the world.

That was no longer the case. Thus the essence of the Volcker measures was to put in place a new regime of accumulation based on the expansion of finance capital.

The road to this new mode of accumulation was by no means smooth. The recession of 1981-82 was followed by a slow recovery, and while the stock market started to rise from 1982 onwards, it crashed in October 1987. The decade finished with a crisis of the savings and loans banks, requiring a bailout of between \$150 and \$200 billion, and the onset of another recession.

The liquidation of the Soviet Union in 1991-92 and the decision by the Chinese Stalinist regime to open the way for the integration of the Chinese economy, and above all the multi-millioned Chinese working class, into the circuit of global capital, marked a major turning point. It was these events that made possible a mode of accumulation based on finance capital.

The opening up of China, with labour costs one thirtieth of those in the US and other major capitalist countries, provided the basis for an expansion in the mass of surplus value extracted by capital from the working class. In a recent speech hailing the virtues of globalisation, European Commissioner Peter Mandelson noted that a Chinese manufacturing firm producing an iPod receives only \$4 for a device that retails for \$290 in the US.

Mandelson was pointing to a process in which surplus value extracted in China is then distributed to other sections of capital in the form of license fees, rents on shopping centres, and interest to banks and financial institutions.

This relationship with China formed a kind of virtuous economic circle. Cheap manufactured goods kept down the rate of inflation, allowing the Fed to lower interest

rates in the US without worrying about inflation.

Cheaper credit fueled various asset bubbles—the share market bubble, the dot.com bubble and the housing bubble—that financed the debt, while helping to sustain US consumption levels in the absence of real wage increases. At the same time, Chinese authorities invested their trade surpluses in US financial assets, in order to keep down the value of the yuan against the dollar and ensure the maintenance of export markets. This also helped keep US interest rates low and sustain the supply of cheap credit, which, in turn, sustained the asset bubbles.

In 1982 the profits of finance companies amounted to 5 percent of total corporate profits after tax. By 2007 their share had risen to 41 percent. This transformation—the financialisation of the American economy—has had vast implications for the process of capital accumulation and the growth of debt in the US economy.

In previous periods, debt was incurred by industry in order to finance its expansion. But with the growing importance of the finance sector, debt has been increasingly incurred to finance further financial activity.

The buying and selling of securities based on assets became the new road to wealth accumulation. In 1995 the dollar value of asset-backed securities stood at \$108 billion. By the year 2000, at the height of the share market bubble, it was \$1.07 trillion. It reached \$1.1 trillion in 2005 and \$1.23 trillion in 2006. In other words, in the space of a decade, the value of these securities had increased ten-fold.

In other words, the financialisation of the economy, that is, the appropriation of surplus value rather than its extraction in the production process, became the other key factor in the explosive growth of derivatives.

In their valuable study *Capitalism and Derivatives*, the authors, Dick Bryan and Michael Rafferty from the University of Sydney, point to two essential functions performed by derivatives.

First, there is what they call a "binding" function, in which a derivative links assets in

the present to assets in the future. The rise of these derivatives was bound up with the increased uncertainty and risk generated by the demise of the fixed currency regime. Under Bretton Woods, the national state kept its currency fixed, providing stability for capital involved in international financial transactions. When that was no longer the case, new mechanisms had to be developed to provide certainty and overcome risks.

Derivatives also have what these authors call a "blending" function. That is, they make possible the commensuration of different types of financial assets. For example, a contract may involve the swapping of shares for a company bond, or vice versa. This may or may not be exercised, depending on the relative movement of interest rates in the bond market and of the dividend paid in shares. Shares and debt both represent claims on future earnings, but interest and dividends may move in different directions and, depending on that movement, the holder of one or other asset may be disadvantaged. That risk can be countered by using derivatives.

The blending function of derivatives enables the holder of a financial asset to hedge against adverse movements in one or another financial variable, or to take advantage of such movements. The risk to finance capital is that once money is invested in a particular form of financial asset, any adverse movement in financial markets can see this asset receive a lesser rate of return than other financial assets, or even suffer a loss.

The use of derivatives has the effect of giving one asset the characteristics of another. In other words, finance capital is not tied to any particular form, but can develop a more universal character. And this becomes vitally important in conditions where the appropriation of profit—the basis for the accumulation of capital—is increasingly dependent on financial market operations.

Our examination of the rise of derivatives should dispel the notion that they were somehow developed purely as a vehicle for speculation, and that if only they were done

away with, or somehow curbed, then economic and financial stability could be restored.

Of course, like every other financial asset, derivatives have certainly become a vehicle for speculation, with disastrous consequences. But simply to focus on this is to ignore the fact that they arose as a means to try to overcome objective contradictions in the capitalist economy, caused by the breakdown of the previous system of regulation—to which the would-be reformers of the capitalist system would now like to return.

The history of derivatives recalls comments made by Marx on the growth of credit, which likewise arose as an attempt to overcome objective contradictions within the capitalist economy, but whose development served to impart to these contradictions an even more explosive form.

"In its first stages," Marx wrote, "this system [credit] furtively creeps in as the humble assistant of accumulation ... but it soon becomes a new and terrible weapon in the battle of competition and is finally transformed into an enormous social mechanism for the centralisation of capitals" [Marx, *Capital* Volume I pp. 777-778].

If we were to adapt Marx's comments to the present day, we could say that derivatives first entered the scene as the humble servant of finance capital, offering to protect it against risk, but ended up creating the risk of the greatest financial disaster in history.

A turning point in the curve of capitalist development

There is another process we must examine to round out our review of financialisation. That is the phenomenon of securitisation, which has played such a crucial role in the mortgage crisis.

In the days of national regulation, US banks operated according to the so-called "3-6-3 model". Money borrowed at 3 percent was lent out at 6 percent, whereupon the bank manager could go to the golf course at 3 o'clock.

This model broke down under the impact of the rapid interest rate hikes at the

beginning of the 1980s and the financialisation of the economy that followed. Banks now had to compete with other financial institutions for funds. But that was not possible on the basis of the old model, where loans were originated and then held by the bank, which then recouped the interest payments. The originate-and-hold model meant that large amounts of capital were tied up for long periods of time. Banks and other financial institutions could increase their profits and remain competitive only to the extent that they could turn over their capital at a faster rate.

The way forward lay in transforming the financial assets they held into bonds, and selling them off. This, though, presented another problem because, unlike the bonds issued by a company such as IBM or General Motors, the underlying asset, in this case mortgages, are not uniform. How then could the bank convert a pool of differentiated mortgages into a security that could be traded like a bond, so that investors would only have to examine the interest rate and the maturity date, without being concerned with the security of the underlying asset?

The solution was to create a pool of mortgages and then issue a series of bonds on which interest was paid out of the money coming in from mortgage repayments. The pool was divided up in a series of tranches, with interest rates paid according to the level of risk of each tranche, the least secure paying the highest rates. Credit rating agencies supplied the risk assessment. These agencies developed various models of risk, on which they based the ratings. In many cases the investment banks issuing the bonds worked closely with the agencies to ensure that the bonds were structured in such a way as to receive the best rating. And investment banks like Lehman Brothers could, and did, sell these bonds around the world to German banks, British banks, or to Australian local councils seeking to boost their funds.

The process of securitisation replaced the "originate-and-hold" model with "originate-and-distribute". The originators had no need to undertake a risk assessment, because as

soon as the mortgage was finalised it would be sold off as part of a securitised package. The bank would receive income in fees from the sale, enabling it to finance new mortgages and repeat the process. Capital could be turned over many times faster than before, with a resultant rise in profits.

Mortgages were increasingly financed without regard to capacity to pay, because the general assumption was that house prices would continue to rise—not since the 1930s had there been a uniform fall in home prices across the United States—so that mortgages could always be refinanced or, failing that, the house could be sold for a profit.

We have now examined the various components of this crisis. What then are its historical implications? The first point is that it is not merely a product of massive losses. That would be one thing. But here we have the collapse of a whole regime of accumulation, a regime that developed in response to the last crisis of accumulation in the 1970s.

The banks and financial institutions can no longer continue on the basis of the originate-and-distribute model. Nor can they return to the previous model.

We have arrived at a turning point in what Leon Trotsky called the "curve of capitalist development". Following the crisis of the 1970s and the downswing of the 1980s, a new upswing began in the 1990s, based on the integration of ultra-cheap labour into the global circuits of capital. This facilitated a new mode of accumulation—highly unstable as the financial crises of the past 20 years reveal—but an upswing, nonetheless. It has now come to a shattering end.

The vast changes that occurred in the global capitalist economy in the past three decades failed to resolve the fundamental contradictions that had erupted in the late 1960s and early 1970s. These contradictions were temporarily suppressed, only to re-emerge in an even more explosive form.

To return to the ABCs of Marxism: the material productive forces have once again come into conflict with the social relations of

production, giving rise to a new period of social revolution, in which the fate of the working class, and humanity as a whole, will be decided. It is for precisely such a period that we must now prepare.

Above all, this requires the development of a program and perspective—the program of international socialism—on which the working class must advance its own independent interests. It can only be established and, most importantly, fought for, through a clear differentiation from the policies advanced by the various "left" reformers and radical tendencies.

All of them, in one way or another, maintain a profound faith in the permanence of the capitalist order, seeking to block the political development of the working class. They do this either by downplaying the extent and significance of the global crisis, or by insisting it can be overcome through a series of reforms. Let us examine the positions of some of them.

For would-be Keynesians, such as the writer Naomi Klein, the source of the crisis is political. It lies in the decisions made to abolish the regulatory regime that operated in the post-war period. Any analysis that goes further, that recognises that the collapse of the post-war system of regulation was not a product of ideology, but of deep-seated contradictions within the capitalist system itself, is dismissed by Ms Klein as "fundamentalism," on a par with the fundamentalism of free market ideology or of Stalinism.

No doubt Klein genuinely holds such views. But they serve very definite political and class interests. Their role is to divert those people who are being radicalised by this crisis, especially young people, from seeking a genuine revolutionary socialist perspective.

According to Klein, tougher regulations should be put in place and all will be well. This is the theme of her article published in the December 1 edition of the *Nation* entitled, "In Praise of a Rocky Transition"—in contrast with the incoming Obama administration's call for a "seamless" transition.

After denouncing the stock market for having the "temperament of an overindulged 2-year-old", Klein writes: "One thing we know for certain is that the market will react violently to any signal that there is a new sheriff in town who will impose serious regulation, invest in people and cut off the free money for corporations. In short, the markets can be relied on to vote in precisely the opposite way that Americans have just voted. ... There is no way to reconcile the public's vote for change with the market's foot-stomping for more of the same. Any and all moves to change course will be met with short-term market shocks. The good news is that once it is clear that the new rules will be applied across the board and with fairness, the market will stabilize."

Not surprisingly, this call to put a bit of regulatory stick about the place is coupled with friendly advice to the incoming president. Klein politely raises that the shocks of the past three months provide him with the opportunity to honour the wishes of the electorate and "do the hard stuff first".

A common characteristic of many would-be "left" reformers is their refusal to draw any lessons from history or to critically examine the logic of their political perspectives.

The British anti-debt campaigner Ann Pettifor, writing in the *Guardian* of October 21, calls for a "great transformation" to reverse the most pernicious elements of the failed "globalisation" experiment.

The financial markets, she insists, must be "tamed", the national state "upsized" so that governments can make effective decisions, and the single global market "downsized" and replaced with an international trading system based on the concept of "appropriate scale".

Ms Pettifor's prescriptions recall nothing so clearly as the "left" policies of the right-wing and fascist movements of the 1930s, including that led by Oswald Mosley in Britain, who spent an early part of his career as a Labour Party "left". Those movements likewise denounced the world market in favour of the national state and gave vent to

their hostility toward "globalisation," or "cosmopolitanism" as it was then called.

Pettifor's call for the power of national governments to be strengthened may well take place as the logic of the bailout process begins to unfold. The banking crisis has already led to deep splits among the European governments, with each of them stepping forward to defend their "own" institutions. And if the US administration does bail out the auto companies, there could well be similar moves by other governments to defend their own "national champions".

In other words, while all national governments proclaim their opposition to the erection of the kind of tariff barriers that caused such devastation in the 1930s, an equally destructive form of protectionism may develop as they each assume increased powers to defend their "own" industries. And Pettifor's call for an "appropriate scale" in international trading is reminiscent of the trading blocs that formed in the wake of the collapse of the global market in the 1930s--a development that culminated in war.

The Keynesian "lefts" support the implementation of an economic stimulus package and anxiously await the coming to power of the Obama administration on January 20.

However, the accelerating economic crisis is developing well beyond the scope of the president-elect's proposed measures. On November 22, Obama announced an economic plan to create 2.5 million jobs in 2009 and 2010. But it has already been rendered a dead letter by a statement issued on November 7 from the Bureau of Labor Statistics.

According to the BLS: "Employment has fallen by 1.2 million in the first 10 months of 2008, over half of the decrease has occurred in the past 3 months... Over the past 12 months, the number of unemployed persons has increased by 2.8 million, and the unemployment rate has risen by 1.7 percentage points."

The would-be reformers continually attempt to portray what they call the "neoliberal" regime of the past 30 years as

some kind of economic "model," which most now be exchanged for a new one.

In its statement on the economic crisis, the French-based organisation ATTAC, well known for advocating a turnover tax on all international financial transactions, called for a new paradigm "where finance has to contribute to social justice, economic stability and sustainable development." The present "model" had been completely discredited and clear consequences had to be drawn so that "political and economic decision-makers fully turn around this unsustainable and unequitable financial system towards the needs of people, equity and sustainability".

In recent years, organisations such as ATTAC that were involved in the so-called anti-globalisation movements advanced the slogan "Another world is possible," creating the illusion that, in some way, they might be for the ending of the capitalist system. In its latest statement ATTAC has refurbished the slogan to read "Another finance system is possible: Stability and solidarity before profits."

Its call for the setting up of an institution under the auspices of the United Nations to "strictly regulate and re-orient the financial system" will prove no more successful than the attempts in the UN to prevent the United States from launching its criminal invasion of Iraq in 2003.

One of the most prominent intellectuals of the Communist Party of India (Marxist), Prabhat Patnaik, gives a "left" slant to the Keynesian program of increased government spending. In a "Perspective on the Crisis" published on October 13 he writes that the need of the hour is not just the injection of liquidity into the world economy, but the injection of demand through increased spending.

Moreover, he continues, "the general objective of such spending must be the reversal of the squeeze on the living standards of the ordinary people everywhere in the world that has been a feature of the world economy in the last several years". The "new growth stimulus" must come not from some new speculative bubble but from

"enlarged government expenditure that directly improves the livelihoods of the people, both in the advanced and in the developing countries".

To advance the notion that governments can somehow be pressured into lifting living standards and that this would alleviate the crisis of the capitalist economy is to blind the working class and the oppressed masses as to the real situation they confront.

At the heart of the crisis is the over-accumulation of fictitious capital in relation to the surplus value extracted from the world working class. This means that any improvement in living standards will exacerbate the crisis of profitability. That is why governments around the world, while handing out billions to the banks and financial institutions, will seek to drive down further the living standards of the working class, as the negotiations in the United States over the proposed bailout for the major car producers clearly demonstrate.

The perspective offered by the various radical tendencies is no different from that of the left Keynesians. In Australia, the Socialist Alliance is so confident of the capacity of the state to deal with the global final crisis that a perspectives document prepared for its recent sixth national conference made no reference to it, until the omission was noted in a letter to the group's national executive.

The Socialist Workers Party in Britain, which tries to project itself as a "Marxist" organisation, rejects any prospect of building an independent revolutionary party of the working class. According to a statement issued by the International Socialist Tendency, to which the British SWP is affiliated, the task is to develop "a broader radical left that can begin to present a credible and principled alternative to capitalism".

Such an alliance will undoubtedly contain Keynesian "lefts" and adherents of groups such as ATTAC, all of whom are deeply hostile to socialism. In any case, there is no great urgency since, according to SWP leader Chris Harman, the crisis will not

develop on the scale of the 1930s because "the state will intervene".

At an SWP-organised conference on "Marxism and the Economic Crisis" last month, long-time radical Robin Blackburn insisted that all that was possible was a series of reforms of a "state capitalist nature".

The scepticism and outright cynicism marking the outlook of the middle class radical milieu was articulated most clearly in a comment, entitled "Marxism and the Economic Crisis," by Rohini Hensman, posted on the website, Countercurrents.Org, on October 30.

"Some socialists," she wrote, "have suggested that this is the end of capitalism, but the notion that the divided, confused and demoralised 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 the capitalist mother."

Ms Hensman is only summing up more clearly and more openly the position of all the radicals: the working class is simply not capable of being won to, and advancing, the fight for socialism. In the 19th century, Marx developed his scientific socialist outlook in constant struggle against the various forms of utopian socialism that emerged at the dawn of capitalist development. Today, as the profit system enters its death agony, the radicals step forward with what can only be described as a program of "utopian capitalism" to try to block the development of a mass socialist movement.

The perspective of the International Committee of the Fourth International

I have spent some time making a critique of these positions because it helps illuminate more clearly the perspective on which our movement, the International Committee of the Fourth International, bases its struggle.

How is this crisis going to develop? This question quite naturally springs to mind at the conclusion of a lecture such as this. In

considering it, I am reminded of a letter sent by Marx to his lifelong collaborator Frederick Engels in which he outlined to Engels the third volume of his monumental work, *Capital*. At the end of the letter, after he had discussed the rate of profit, the equalisation of profit, credit, interest, merchants' capital and the rate of surplus value, among other things, Marx wrote: "[W]e have the *class struggle*, as the conclusion in which the movement and disintegration of the whole shit resolves itself."

I raise this rather blunt assessment in order to emphasise a very important point. We have reached a point in history where once again the material forces of production have come into violent conflict with the social relations of capitalism within which they have hitherto developed. Now begins an era of social revolution in which men become conscious of this conflict and fight it out. That is the significance of the recent occupation of Republic Doors and Windows by workers in Chicago and the mass demonstrations in Iceland.

How, then, do we proceed? Do we have some crystal ball that will tell us exactly what will happen and when? Of course not. And in any case, the situation will not be determined simply by the relationship of abstract economic categories. These categories are themselves only the expression of the movement of social classes. The class struggle, for so long hidden and concealed, is going to assume more open forms.

We begin our work, not from the present level of consciousness of the working class, but from the objective situation and the tasks that it poses.

Trotsky emphasised the importance of this approach in preparing for the founding of the Fourth International in 1938: "The program must express the objective tasks of the working class rather than the backwardness of the workers. It must reflect society as it is, and not the backwardness of the working class. It is an instrument to overcome and vanquish the backwardness. That is why we must express in our program the whole acuteness of the social crises of

capitalist society, including in the first line the United States. We cannot postpone or modify objective conditions which don't depend on us. We cannot guarantee that the masses will solve the crisis; but we must express the situation as it is, and that is the task of the program."

There is no question that there is great political confusion in the working class. How could there not be? For decades the working class has been dominated by the social democratic, Stalinist and trade union bureaucracies, all of which have waged a continuous war, ideological and physical, against socialism.

Yes there is great confusion. But there is a much more powerful factor: the greatest financial crisis since the Great Depression, which is creating the material conditions to overcome that confusion. Our movement, and the program for which it fights, can and must become a decisive factor in this process. That is our starting point.

The task of the revolutionist, Trotsky once wrote, is to extract from every given historical situation "the maximum that it is capable of rendering toward the advancement of the revolutionary class". Any outlook that begins, not from the present objective situation, but rather from the confusions built up over previous decades, necessarily becomes, in this period, a source of further confusion and a political prop for the crumbling capitalist order.

Our perspective is grounded on an objective assessment of the historical crisis of capitalism. In the first place, therefore, it seeks to rearm the working class with the understanding that its task is the world socialist revolution and that only on this basis can the interests of humanity as a whole be advanced.

It is painfully clear that there is no way out of this crisis on a national basis. The notion that some areas of the world could "decouple" from its effects lasted about five minutes once it began to gather pace. The global financial and economic crisis can only be resolved on an international scale. And the

material and social forces to accomplish this have already been forged by capitalism itself.

Globalised production has created a global working class whose material interests are determined by the struggle against global capital. There is no road forward for the American, Australian and European working class outside its unification with the struggles of the working class in China, India, Asia and Africa. Likewise, there is no way forward in these regions on the basis of any kind of national development.

The program for the unification of the working class is the world socialist revolution: that is, the overthrow of the capitalist ruling class and the development of a planned world economy based on the democratic decision-making of the world's producers. No longer will millions of people have their lives turned upside down, and the future of their children destroyed, by the blind workings of the capitalist market and the drive for profit. They themselves will take part in the organisation of economic life.

The fulfilment of this perspective does not mean that the working class has to come to power all at once and everywhere. What it does mean is that the political struggle of the working class in every country—the fight for a workers' government and the establishment of an economy in which the banks, major financial institutions and key industries are publicly owned and democratically controlled—must be grounded on this global perspective.

An international economy in which the market is replaced by the democratic decision-making of the world's people? How is that possible? What kind of complex infrastructure would have to be set in place to realise such a goal? In fact, it has already been established.

One hundred and fifty years ago, Marx explained that as the market became increasingly autonomous, standing like an alien force over every individual, efforts inevitably emerged to overcome that autonomy.

"[I]nstitutions emerge whereby each individual can acquire information about the activity of all others and attempt to adjust his

own accordingly, e.g. lists of current prices, rates of exchange, interconnections between those active in commerce through the mails, telegraphs etc. (the means of communication must grow at the same time.) This means that, although the total supply and demand are independent of the actions of each individual, everyone attempts to inform himself about them, and this knowledge then reacts back in practice on the total supply and demand. Although on the given standpoint, alienation is not overcome by these means, nevertheless relations and connections are introduced thereby which include the possibility of suspending the old standpoint."

Look through Marx's somewhat Hegelian language and you can see that he is referring to precisely the kind of developments that have now taken place, and pointing to their role in establishing the conditions for a socialist economy.

The widening and deepening of international financial markets, the result not least of derivatives trading, has created a system that provides virtually instantaneous information about global developments, which then are factored into credit evaluations and funding decisions.

At the same time transnational corporations, responsible for an ever-increasing share of global production, plan their operations across continents and time zones. And these vast operations are co-ordinated and organised by workers with all manner of skills and capacities. The problem is not one of technology or information. It is political. These vast productive forces, created and sustained by the physical and intellectual labour of the world working class, are subordinated to the irrational and destructive drives of the outmoded capitalist profit system. They must be liberated so that mankind can resume its historical progress. That is the historical significance of this global economic crisis and of the international program advanced by our movement to resolve it.