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Financialisation and sustainability: a long-run perspective

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Introduction (1)

Fessud Research:

financialisation ↔ sustainability

Both concepts are controversial and ambiguous: different definitions and approaches

In the case of sustainable development there is at least a broad agreement that the concept may, or should, be rooted in the definition of the Bruntland Commission (1987)

In the case of financialisation it is difficult to find a common denominator to the different definitions and approaches

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Introduction (2)

the research team of Siena tried to {
- survey and discuss the main definitions/approaches from the point of view of sustainability
- suggesting a view general enough to accommodate some of them as special cases

The abstract part of this investigation has been summarized in the deliverable

D7.03 {
- 1° Part: long-run point of view from an evolutionary perspective
- 2° Part: applies this approach to the 2° financialisation (~1980-today)

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Three basic approaches

-specific historical episode

3 main options { -recurring phenomenon

-stage of a long-run process (or tendency)

In our opinion the three options do not exclude each other:

our suggested vision combines the three approaches within an evolutionary paradigm

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Preliminary definition

I start from a broad definition that may accommodate all the stages of the evolutionary process

Financialisation:

process of evolution of «money» (money/credit/finance) that increases its importance and thus the influence of financial markets, institutions and élites

While we analyse the processes of financialisation we should keep in mind the crucial

distinction {
- money as quantity that is created, multiplied, hoarded and utilized
- money as structure shaping the forms of exchange / accumulation

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Financialisation as a recurring phenomenon

significant analogies

recurring phenomenon in a broad sense {

significant differences

1st financialisation (about 1880-1929)

Since the industrial revolution {

2nd financialisation (about 1980-2014 → ?)

Under which conditions? Main answer: phase of long-term fluctuations:

long waves (e.g. Arrighi, 1994; Kevin Phillips, 2006)

within a theory of {

recurring technological upsurges (Perez, 2002)

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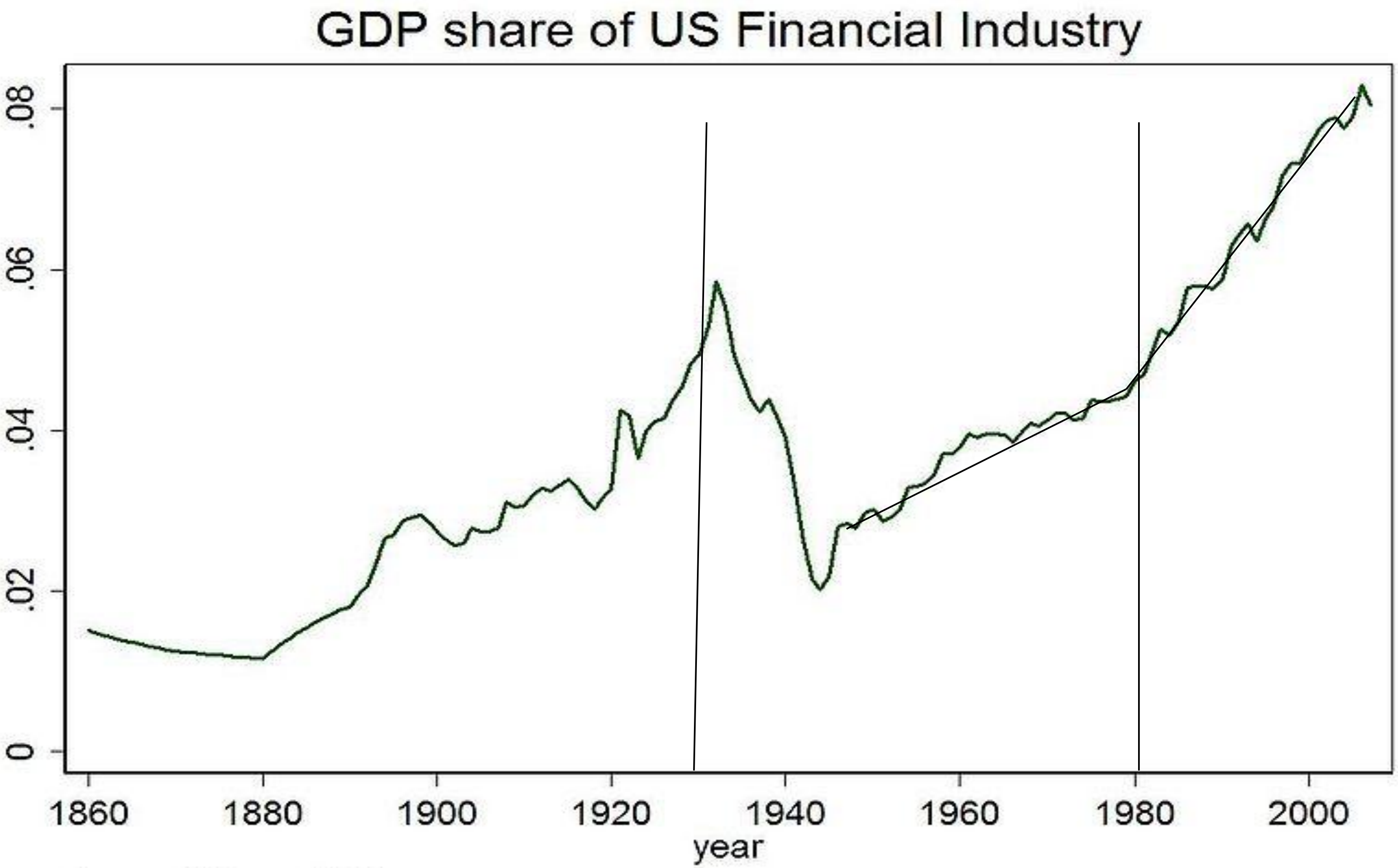
The first and the second financialisation



Source: Philippon, 2008

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Financialisation, globalisation, crises and technology

The long-run fluctuations of financialisation are correlated with:

-» long-run fluctuations of globalisation following phases of systematic liberalisation

-» technological trajectories: installation of a new technological paradigm (Perez, 2003) → financialisation provides the necessary structural flexibility

financialisation {
- **FIRST: trajectory based on oil, automobile, and mass production**
- **SECOND: ICT trajectory**

-» great crises: the excessive and unfettered flexibility leads to

great crises {
- **1° financialisation → Great Depression**
- **2° financialisation → Great Recession**

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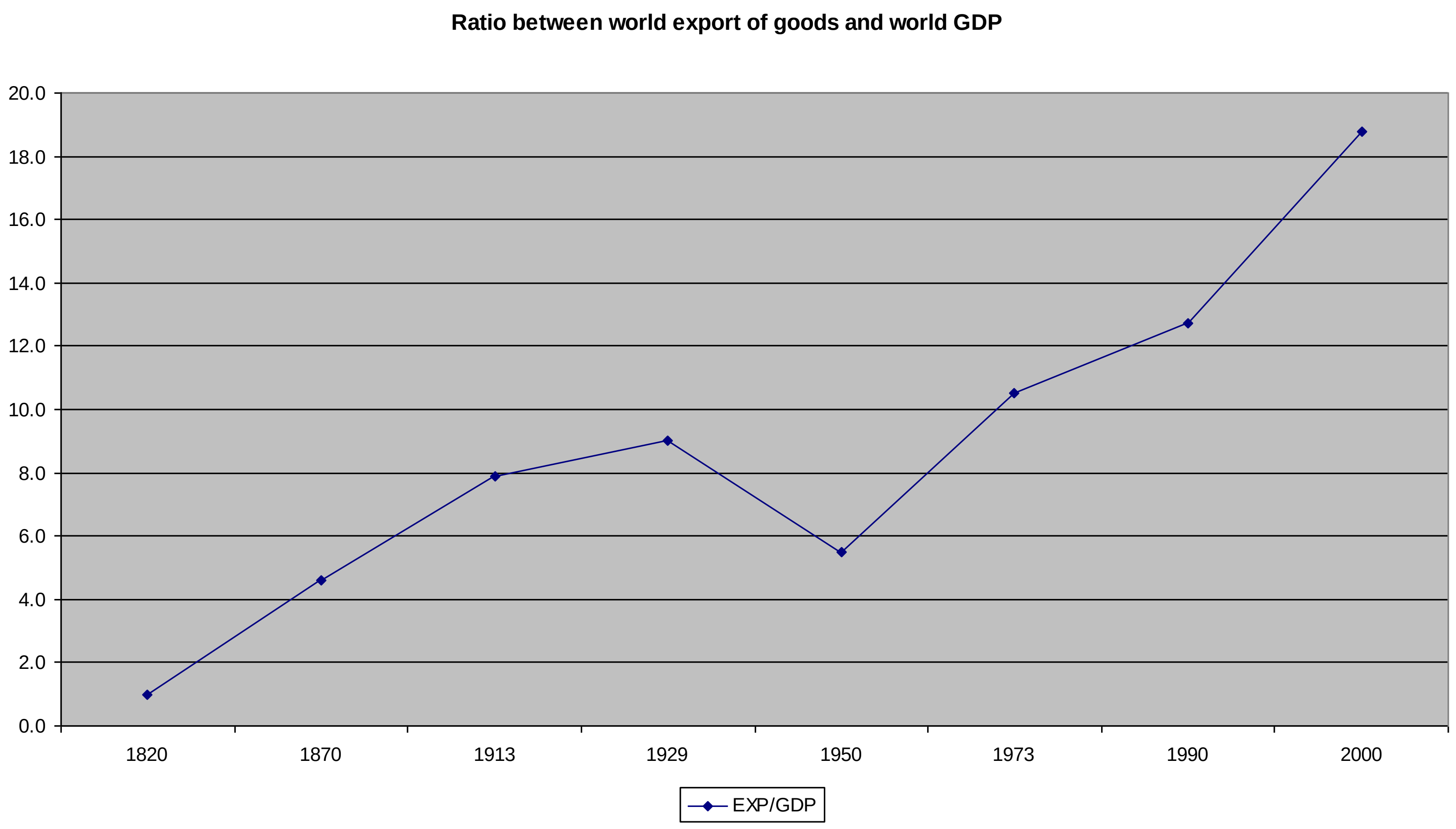
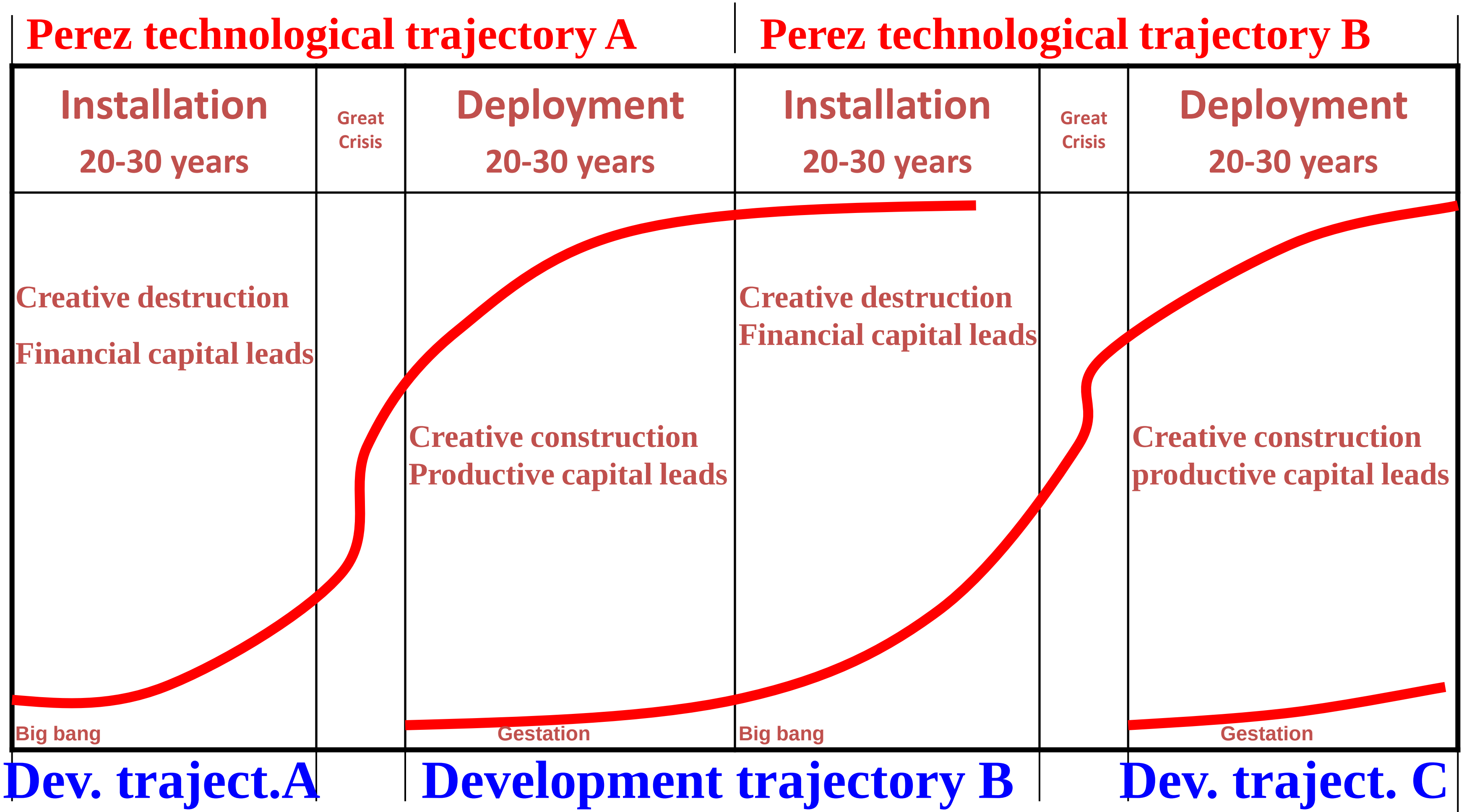
The first and the second globalisation



Technological trajectories and development trajectories



Source: Perez 2002 modified and integrated by the author (Vercelli, 2011)

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Secular tendency towards financialisation (1)

Long-term fluctuations of financialisation along a secular trend?

I claim that there is a secular tendency towards financialisation that is intrinsic in the development of market relations

This tendency progressed very slowly because, since the ancient civilizations, it was repressed for different reasons (religious, political, ethical, social protection) :

alternation {

- **deceleration (sometimes even decline) when the repression became tougher (e.g. in the Bretton Woods period)**
- **acceleration when repression was relaxed → phases of financialisation (neoliberal era: 1980s-today)**

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Financialisation after the Industrial Revolution

1st phase until about 1850: mercantilist financial repression slows down financialisation notwithstanding the progressive development of market relations

2nd phase since about 1850 accelerating since 1980: systematic introduction of free-trade policies progressively relaxing financial repression → 1st financialisation

3d phase since the Great Depression (1933: US banking act): new phase of financial repression slowing down financialisation

4th phase since about 1980: neo liberal policies → progressive relaxation of financial repression to an unprecedented level → 2nd financialisation

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Why a tendency towards financialisation? (1)

Why there is a secular tendency towards financialisation?

process driven by financial innovations introduced whenever at the micro level they are profitable and are not repressed

general tendency because financial innovations have something in common:

increase choice flexibility →↑ returns for the innovators

The increasing flexibility of the choice set is realized by increasing the liquidity and mobility of assets and capital:

-joint-stock companies (Keynes, 12th Chapter GT)

-securitisation (Minsky, 1987)

-shadow banking (Gorton, 2008 and 2009)

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Financialisation and sustainability

Flexibility-enhancing innovations very often have negative macro externalities

In particular a micro increase of efficiency is often accompanied by more systemic instability that may jeopardise systemic efficiency

→ trade-off between micro efficiency and systemic stability:

after a certain threshold systemic instability makes the system unsustainable

In what follows I try to substantiate my working hypothesis with the help of history of analysis

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Financialisation in (neo-)classical economics

In classical and neoclassical theory basic distinction {
- barter economy
- monetary economy

A monetary economy is believed to be much more efficient than a barter economy as it relaxes the strictures of "double coincidence of wants" →↑ flexibility

The trade-off between efficiency and stability (QTM) is "solved" by forcing a monetary economy to behave as a barter economy anchoring it to

- the gold standard
- and/or to an orthodox budget policy
- and/or to strict monetary policy rules

Serious problems{
- a barter economy never existed (Graeber, 2012)
- evolution of monetary economies disregarded

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Reaction to the 1st financialization

The process of financialisation that spread and intensified in the second half of the 19° century until WWI progressively changed the functioning of capitalism giving a growing importance to credit:

the increasingly endogenous process of money creation on the part of the banking system was inconsistent with the QTM but this passed unnoticed with most classical economists

We find significant exceptions only with a few perceptive neoclassical economists in the most heterodox part of their contributions who modified standard theory to take account of the role of credit:

Wicksell (cumulative process)
Fisher (debt-deflation)
Schumpeter (theory of economic development)

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Money and financialisation in Marx

Marx was the first to develop a radical critique of the QTM since it ignores the essence of circulation of goods in a monetary economy:

"The illusion that it is [...] prices which are determined by the quantity of circulating medium [...] has its roots in the absurd hypothesis...that commodities enter into the process of circulation without a price, and that money enter without a value..."

(Marx, 1976, pp.217-8)

This sharp criticism of the TQM also clarifies why many interpreters and followers of Marx reached the conclusion that money is not important

However, this conclusion does not take into account money as technological and institutional structure that plays a crucial role in capital circulation in identifying different forms and phases of capitalism characterized by different functioning rules

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Money as structure and financialisation: Marx

emblematic circulation forms (extremely simplified version: more details in Vercelli, 1973):

- U – U Immediate exchange of use values (occasional barter)
- C – C Immediate exchange of commodities
- C – M – C Simple circulation of commodities
- C — M — C’ Petty commodity production (“simple commodity production”)
- M — C — M’ Circulation of commercial capital
- C …. P …. C’ Circulation of commodities in industrial capitalism
- M — C …. P …. C’ — M’ Circulation of money capital

long-term tendency towards an increasing role of money as structure and institution encompassing production and any aspect of social life and culture

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Marx: long-term tendency towards financialisation

Money as structure plays a crucial role by enhancing the flexibility of exchanges that become increasingly independent of time, space and utility content

→ **higher degree of abstraction of exchange value**

from use value → { **↑ instability**
↑ fetishism
↑ alienation }

→ **increasing short-termism:**

a decision is taken if max the value of the portfolio whatever is the costs for society and nature (externalities not considered) → unsustainability

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Long-term financialisation in Keynes

Keynes in the GT resumes the traditional distinction between barter economy and monetary economy but shows that the second cannot be forced to work as a barter economy just through monetary means

In the GT {
- "barter economy" in the sense of C-M-C : money is not the end but the means
- the trouble with (neo)classical economics is that it assumes axioms fit for a barter economy (C-M-C) rather than for a monetary economy (M-C-M')

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Financialisation in Minsky

Minsky builds on Keynes, Kalecki and Fisher (debt deflation) to show that we have to distinguish different stages of a monetary economy:

his FIH refers not to a generic monetary economy but to a
"sophisticated monetary economy": a mature stage in the evolution of capitalism where credit and finance play a crucial role

even a "sophisticated monetary economy" undergoes an evolution:

the last stage examined by Minsky (1987) is the "money manager capitalism":
an economic system characterized by highly leveraged funds seeking maximum returns in an environment that systematically underestimates risk

→ money and finance play a more crucial role and become more uncontrollable

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The "irresistible" ascent of financialisation

In my view in the second financialisation the pathological aspects by far exceed the alleged advantages: systemic negative externalities much bigger than micro advantages

→ unprecedented concentration of wealth, income and power → vicious circle with a parallel concentration of power

that undermines sustainability {
- **economic (unemployment)**
- **social (poverty and inequality)**
- **environmental**

→ultimate cause of the recent crisis

In addition the recent process of financialisation, undermines democracy: without democracy we cannot hope that all the other problems may be solved

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Concluding remarks

We have to recover a democratic control of finance

To this end a very strict financial repression is necessary although this goal is very challenging taking into account the tough opposition of the very powerful financial lobby exposing the economy to increasing instability and unsustainability

we should thus not expect a significant progress in this direction in the near future; in the meantime we should try:

-to solicit a greater awareness of the nature and dimensions of the unsustainability of unfettered financialisation

-to advocate measures that try to restore the role of financialisation as support of the real economy in the direction of sustainable development

These issues will be discussed in the following presentation and in session 6

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Thank you for the attention