“Secular stagnation” and the contradictions of capitalism

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The surprise decision by Japan’s central bank at the end of last month to start charging for new deposits and enter the world of negative interest rates marks something of a turning point in the ongoing and deepening crisis of the global financial system.

With one quarter of the world’s gross domestic product now being produced in countries with a negative interest rate regime, and the failure of the quantitative easing policies pursued by the world’s major central banks to produce any turnaround in global economic growth, there are growing calls from bourgeois economists and institutions for a turn to other policies.

One sign of this shift was the report by the Organisation for Economic Cooperation and Development issued last week. Revising downward its previous forecasts for global growth, made just three months ago, the OECD for the first time since the onset of the financial crisis called for government spending measures to try to halt global recessionary trends.

This week, global economist Stephen Roach, a former manager of Morgan Stanley Asia who is now at Yale University, published a comment expressing the growing perplexity in economic circles over the failure of the policies of the last seven years, symbolised by the shift to a negative interest rate regime.

“In what could be a final act of desperation,” he wrote, “central banks are abdicating effective control of the economies they have been entrusted to manage. First came zero interest rates, then quantitative easing—one futile attempt begetting another. Just as the first two gambits failed to gain meaningful economic traction in chronically weak recoveries, the shift to negative interest rates will only compound the risks of financial instability and set the stage for the next crisis.”

According to Roach, the attempt to stimulate investment through interest rate reductions and now negative rates—in effect trying to push banks to make loans regardless of the demand for them—misses the essence of the crisis, which is centred on the demand rather than the supply side. Consequently, lowering the costs of borrowing only leads to an appreciation of financial assets and does nothing to jump-start aggregate demand.

Like many others, Roach points to the situation in Japan, where the supposedly powerful impetus of Abenomics—based on massive injections of finance—has failed to dislodge the economy from 24 years of low inflation and low growth. He notes that this is increasingly a global phenomenon.

Lawrence Summers, a former US treasury secretary, who at one point was considered a candidate for the chairmanship of the US Federal Reserve, has also re-entered the fray with the publication of an article in the latest issue of *Foreign Affairs*. In a blog published in the *Financial Times* last week, he wrote that he was “increasingly convinced” that the concept of “secular stagnation”, which he first advanced at the end of 2013, captured “what is going on in the industrialised world, and that the risks of long-term weakness on the current policy path are growing.”

He begins his *Foreign Affairs* article by noting: “Almost no one in 2009 imagined that US interest rates would stay near to zero for six years, that key interest rates in Europe would turn negative, and that central banks in the G-7 would collectively expand their balance sheets by more than $5 trillion. Had economists been told that such monetary policies lay ahead, moreover, they would have confidently predicted that inflation would become a serious problem—and would have been shocked to find that across the United States, Europe, and Japan, it has generally remained well below two percent.”

In other words, while Summers does not make the point explicitly, the economic institutions of global capitalism, with all the data provided to them, with massive computer facilities for analysis of that data, together with tens of thousands of bourgeois economists around the world, have no idea either of the dynamic of the capitalist economy over which they are supposed to preside or how to develop remedies to address its ills.

Turning to the concept of secular stagnation, first advanced by the American economist Alvin Hansen in the 1930s, Summers writes that it refers to a situation where industrialised economies “suffer from an imbalance resulting from an increasing propensity to save and a decreasing propensity to invest.”

As a result, excessive saving acts as a drag on demand, reducing growth and inflation, with the imbalance between savings and investment lowering interest rates. Where growth is achieved, such as in the US between 2003 and 2007, it comes from dangerous levels of borrowing that lead to the formation of bubbles, like that which developed in the American housing market in the lead-up to the 2008 financial crash.

Such an analysis, however, begs the most important question: what has caused the “propensity to invest” to fall so that there is an excess of savings supply over the demand for investment funds? Summers does not answer this question, but proceeds by pointing to the numerous and growing problems caused by the lack of investment demand.

When the desired levels of investment fall below desired levels of savings, this leads to “shortfalls in demand and stunted growth”, a situation, he notes, that accords with much of what has been seen in recent years. “Absent many good investment opportunities, savings have tended to flow into existing assets, causing price inflation,” he writes, in a reference to the escalation in share values and other financial assets.

The solution to the problem of secular stagnation, he maintains, “should rest with fiscal policy,” which can stimulate growth, particularly when pursued through increased public investment.

“A time of low real interest rates, low material prices, and high construction unemployment is the ideal moment for a large public investment program. It is tragic, therefore, that in the United States today, federal infrastructure investment, net of depreciation, is running close to zero, and net government investment is lower than at any time in nearly six decades,” he writes.

According to Summers, the main constraint on the industrial world’s economy is on the demand rather than the supply side. Consequently, measures should be undertaken to increase demand, as advocated by John

Maynard Keynes when facing a similar situation in the 1930s. If each of the countries were to adopt such measures, "the result would be very favourable for the global economy," Summers argues.

Taking his cue from Keynes, Summers likens the world economy to a car with a broken alternator that simply will not move, but it "takes only a simple repair to get it going."

"In much the same way," he writes, "secular stagnation does not reveal a profound or inherent flaw in capitalism. Raising demand is actually not that difficult, and it is much easier than raising capacity to produce. The crucial thing is for policymakers to diagnose the problem correctly and make the appropriate repairs."

The obvious question is: why, if it is not "that difficult" and would be "very favourable" for the global economy, has it not taken place?

There was, Summers states, a move in the right direction at the G-20 summit in London in April 2009, when common commitments were undertaken to engage in fiscal expansion, increased financial regulation, and a response to problems in emerging markets that were "effective in halting the collapse of the global economy." Unfortunately, he continues, subsequent G-20 summits returned to "traditional lethargy" and "preoccupation with fiscal austerity," and thereby ended up "missing opportunities to accelerate the recovery."

The turn came at the G-20 summit in June 2010, when the immediate prospect of a financial meltdown had passed. Abandoning references to the need for expansion, the summit communiqué insisted on the need for "fiscal consolidation", that is, the attacks on government spending and social services that have characterised the austerity drive of the past six years.

For Summers, this turn is not an outcome of processes within the capitalist economy itself, but is simply the product of mistaken ways of thinking on the part of those in charge of economic policy. Therefore, he argues, secular stagnation can be overcome if mindsets are changed.

The basic fallacy in this analysis is that it simply passes over the essential and most fundamental features of the capitalist economy and the profit system.

Take the crucial issue of the "propensity to invest" cited by Summers, but which he never explains. The driving force of the capitalist economy is not the creation of full employment, the pursuit of economic growth as such, the satisfaction of the needs of consumers, or the provision of decent living standards for the population. It is the drive for profit and the accumulation of capital. This is the key determinant of the level of investment.

New investment in productive activity—new construction, the expansion of industry etc.—will be undertaken to the extent that it can return a positive rate of profit, over and above what could be obtained by investing in financial assets.

If such investment does take place, then additional demand is created for firms that supply raw materials and machinery, providing wages for workers who are employed in these industries. The wages of these workers, in turn, finance increased consumption, which, in turn, increases the markets and profits for industries supplying these goods. In short, demand, which is sparked by increased investment in the anticipation of additional profits, grows, and the economy as a whole undergoes an expansion.

However, if the rate of profit turns down, then investment opportunities contract, overall economic growth declines, the economy stagnates or goes into recession, and firms increasingly use their cash surpluses not for productive activity but for financial speculation.

In short, the source of the stagnation is not deficient demand as such. That is only the appearance-form of a more fundamental problem—the fall in profit rates, which lowers the "propensity to invest". The would-be Keynesian managers of the capitalist economy maintain that this can be counteracted and economic activity stimulated if the government steps in and increases effective demand.

Insofar as such policies are not undertaken—as they clearly have not been since 2009—then, like Summers, bourgeois economists attribute this to some fault in the thinking or mindset of those in charge of economic policy, to their lethargy, preoccupation with dogmas or just downright stupidity in the face of problems that could be relatively easily resolved if only they had the wit and wisdom to do so.

However, an examination of the capitalist economy from the critical standpoint of profit accumulation—its essential driving force—reveals why the present policies are being pursued.

The source of all profit in the capitalist economy is the surplus value extracted from the working class. That surplus value does not flow directly to the capitalist firms immediately involved in its production, but rather is distributed among the various sections of capital. As Marx put it, through the operations of the market, the intervention of finance capital, the involvement of firms that provide advertising, retail services, legal services and so on, the different sections of capital, the property owners, divide up the available mass of surplus value among themselves.

There are also deductions made from what is available through the struggles of the working class to secure education, health care, social services, pensions and so on. All of these provisions represent a deduction from the surplus value available to capital in the form of profit. Consequently, if the rate of profit turns down, capital demands that such deductions be reduced. They can no longer be afforded.

Furthermore, expanded government spending on infrastructure and other forms of social investment also represent a deduction from the available surplus value. Either this spending is paid for via increased taxation, which impacts directly on profits, or via increased public debt, which must be financed in the long run out of the mass of surplus value.

In addition, there is the impact of increased government spending on the course of the class struggle. None of the would-be Keynesians such as Summers, who claim to have a solution up their sleeve, ever explain why the policies of demand management, which formed the conventional economic wisdom during the post-war boom, were cast aside by the end of the 1970s.

That was the outcome of the significant downturn in the rate of profit during the decade, to which the bourgeoisie responded with a continuous offensive on wages and conditions, in order to drive up the extraction of surplus value in an effort to restore profit rates.

One of the key features of the American economy, not to speak of other industrial economies, over the past four decades has been the continuous erosion of real wages and the share of wages in national income. In the US, it is calculated that real wages have not advanced since 1973. This drive against the social conditions of the working class is not a one-off policy, but is embedded in the very mechanics of profit accumulation.

And herein lies one of the fundamental reasons why there is no program of infrastructure spending or other forms of social investment to boost effective demand.

Would corporations across the US, for example, as well as in other countries, have been able to drive down wages if jobs had been available through government-funded investment and infrastructure projects? Would the Big Three auto companies in the US have been able to impose two- and three-tier wages systems if government-funded projects provided alternative employment? Would college and university graduates, some with masters and higher degrees, be working for minimum wages at Walmart, Amazon and other such corporations while trying to pay off tens of thousands of dollars in student debt?

As far as scientific content is concerned, Summers' *Foreign Affairs* piece and his prescriptions are worthless. But they have an important political significance.

They are aimed at trying to provide grist to the mill of the claims advanced by forces such as Bernie Sanders that the depredations of capitalism can be somehow controlled and regulated if only there is a return to some of the policies of the past. They aim further to prevent the understanding that there *is* a “profound and inherent flaw”, that is, irresolvable contradictions, within capitalism that can be overcome only through socialist revolution and the ending of the capitalist profit system.