Editor’s Note

Volume XIV of Oeconomicus for 2014-15 has been a fun experience, made all the better by the increase in submissions seen this year. It was good to see the amount of submissions not only rise from previous years but also to see the people and places those submissions came from become more diverse.

But this also meant that more papers than previous years had to be rejected. It was a pleasure to read all the papers submitted this year and even if your papers weren’t published your hard work and enthusiasm is still appreciated and helped make this journal as good as it came out to be.

I’d like to call out a few of the individuals who helped make this year’s journal possible, namely Brian Hartley and Matthew Berg for assisting me in looking at submissions. Also this would not have been possible without the Guidance of Avi Baranes and Sudeep Regmi who helped me along nearly every step of this publication. Finally, a thank you to Dr. Ben Young for giving me this opportunity and advising me along the way.

Steve Bodenheimer

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Veblen’s Machine Process and Higher Education in the U.S.A.

By: Lorraine Hutton

Abstract: This inquiry seeks to establish that a comparison can be drawn between the United States of American’s higher learning process and the machine process advanced by Veblen in The Theory of Business Enterprise. Whereas the machine process conformed human labor and material inputs to standardized measures for cost and process efficiency, the educational process standardized human academic labor and knowledge inputs and student performance outputs to suit the market. Both processes venerate the businessman who, though disconnected from the process and its workers, propels a Tayloristic efficiency for the sole purpose of pecuniary gain. (words: 94)

Introduction

This inquiry seeks to establish that what Thorstein Veblen advances as a machine process, can be applied to offer insights into higher education in the United States of America. After first considering Veblen’s concept of the machine process, a comparison will be drawn regarding the United States of America’s higher education system. Veblen’s opinions from The Higher Learning in America, [1918] will punctuate my efforts to illustrate the higher learning’s move away from esoteric knowledge-sharing to “matter-of-fact” learning and its effects. My inquiry will proffer conjecture regarding the United States of America’s higher educational system and its underlying
motivation for pecuniary gain that is driven by the businessman who, like the factory businessman, deems profit the priority of industry or education.

**Veblen’s Machine Process**

We might be inclined to think of the machine process as merely the functioning of machines within an industry. However, Thorstein Veblen ([1904] 1978, 5-9) informs us that the machine process involves a concatenation of industrial processes, interstitial sub-processes, raw materials, resources and labor. The nature of the machine process need not be complex or comprehensive but its hallmark is that of a reasoned procedure of efficiency and standardization---a concerted operation of a multiplicity of machines working in interlocking tandem not self-sufficing. Veblen (1978, 17) suggests that the successful coordination of the concatenations increases solidarity and hence efficiency of the entire process.

The factory process evolved from a modest beginning in England. Instincts of Idle curiosity and workmanship contributed to increased technological knowledge which in turn was integrated into the cotton and wool production industry---propelling it into industrialism. What had been a one-man or family centered operation of non-uniform measures, creativity, and workman’s pride for the purpose of earned income was now an operation of human expediency, standardization, efficiency and pecuniary gain.

Veblen (1978, 8-13) notes that as operational complexity of the factory process increased, standardization became essential to the factory’s quantitative precision and uninterrupted flow. Precision necessitated the standardization of tools, materials and components regarding their size, shape and gauge. Similarly, labor did not escape the businessman’s Tayloristic efficiency measures. Veblen (1978, 13) purports that the worker’s day was pressed into conformity according
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to the schedule put upon him by the machine process; his own amusements taking second place to
industrial precision. In essence the community fell into the rhythm of what Veblen (1978, 14)
coined “super-induced mechanical regularity” of time, speed and intensity.

Standardization increased productive celerity and brought the factory manager’s
accounting and planning process to a new level of accuracy and efficiency which called for greater
employee specialization and expertise. Critical to uninterrupted production, Veblen (1978, 16)
emphasized the factory’s necessity of coordination at every level of operation; from resource
management to labor inputs and uniform outputs. The slightest operational problem would ripple
through every interstitial relationship and include inadvertent interference on the exigencies of life
pertaining to the community. Failure is rarely contained to a single entity or portion of the
community.

Veblen (1978, 24) portends that the transition from craftsmanship and making a living, to
business enterprise was driven by the businessman, historically the factory owner. In the past his
attention was almost entirely consumed by the intricacies of the factory process. With time, the
business of doing business and advancing the factory enterprise became the businessman’s
endeavor of opportunistic pecuniary gain. While his habitual cogitations tended to be pecuniary,
Veblen (1978, 317) believes that the businessman’s thoughts never abandoned the mechanical
process completely. However, Veblen (1978, 317) suggests that the businessman’s exemption
from the industrial process, due to his primary interest of pecuniary gain, propagated a
disconnection between the industry workers and himself. Veblen (1978, 317-318) speculates that
the vastly different engagements in the machine process induced variant habits of thought by the
two classes, to the extent that they no longer appreciated or understood each other easily. I might
add that worker’s socialistic animus or disaffection, noted as class hatred and envy by Veblen
Tradition and science are two very different habits of thought and Veblen (1978, 318) contends that the businessman is the conventionalist; finding validity in tradition, whereas the process worker or engineer concerns himself with scientific mechanical sequence and causation. Veblen (1978, 348) teaches that habits of thought are influenced by the work we do and the habits of our life. Material accumulations, or legal ownership of goods has little bearing on our habits of thought, however, Veblen (1978, 348) finds there may be a relationship between “legal relations” (such as ownership) and class animus that presents as socialist habit of thought. Veblen (1978, 349) notes that these socialist tendencies are more prevalent in industrial towns and amongst material scientists. These men, Veblen (1978, 352-353) insists, have an “ineptitude for an uncritical acceptance of institutional truths”, however, he further contends that the machine industry neither inculcates socialist tendencies nor shapes a socialist mindset. The machine process (industrial system) attracts the kinds of minds that have these socialist, matter-of-fact tendencies.

A further criticism of the machine process is its influence on culture and mental training. Veblen (1978, 323), regards the decline in mental training; both spiritual and intellectual as the result of the discipline of the machine process on men. Veblen (1978, 310) suggests that the mechanical process trains the mind and thinking of a man in impersonal “opacity” of cause and effect. The workman gives no thought to what is right or wrong or what is meaningful to man. Veblen (1978, 323) insists that the machine process inculcates skepticism and weakens the capabilities of the population to tend to their own pecuniary interests. Veblen (1978, 325) indicates that the workman and the engineer are inept at pecuniary responsibility and consider conspicuous
consumption evidence of good repute. Savings and bank accounts, investment in real property and living thriftily are not encouraged by the machine process.

Veblen (1978, 326) criticizes the machine process as an exploitive system, insisting that it utilizes labor as it does material inputs; requiring that it be distributable, interchangeable and mobile. It is not advantageous for the workman to own his own home and Veblen (1978, 327) attributes a decline in the appeal of ownership to the moral decline imposed through the effect of the machine process.

Lastly, Veblen (1978, 358-359) protests the turning away from religion, patriotism and everything “respectable, noble and dignified in human intercourse and ideals”. Man is no longer concerned with what his end means or the fact that he may be guilty of sin. The machine process Veblen (1978, 358) insists, is a leveler and a “vulgarizer” of man. Veblen (1978, 68-70) writes that behavior and business of ancient times was of a sentimental nature, conventional, “clean”, divine and built on foundations of clan relationships, allegiance and nationality. He bemoans the fact that the machine process has greatly weakened man’s power of restraint and proffers that ancient norms no longer hold man to the same convictions. Veblen (1978, 70) notes that the number of pecuniary relationships and pecuniary “settlements” are far greater than the past and pecuniary relationships now include the church and blood-relations. Pecuniary gain is the hallmark of the modern day machine process’s motivation. Doing business no longer merely fulfills the need to make a living. It is driven by the businessman who seeks profit in every business connection and will utilize any means necessary. Veblen had an apparent dislike of the machine process, its impact on the habit of thought and its promotion of the businessman above all. It was unsettling and apparent to Veblen (1978, 373) that the machine process would continue to infiltrate the population at an increasing
rate, with traditional conventions weakening with time and its “disintegrating” reach spreading uninhibited.

**Higher Education as a Machine Process**

The higher education machine process is entirely like the mechanical machine process in that it maintains interstitial relationships necessarily coordinated, supervised and tended by technicians, experts and the businessman; the University President. The University is every bit as complex as an industrial complex; having inputs (minimally educated students) equivalent to raw materials, a process of change (the learning process) and an output of standardized products—namely the “educated” student who is prepared for civil life or the academy.

Not unlike the English factory system or machine process, higher education began in a craftsman-like manner. Veblen ([1918] 2009, 6-10) teaches us that the church and the elder as well as “nobler virtues” shared esoteric knowledge in drawing rooms and courts and he bemoans the fact that modern civilization has moved away from old institutions and placed full value and acceptance on the modern University system. He decries the matter-of-fact knowledge and the fact that modern society sees this matter-of-fact knowledge as its most valuable spiritual asset. There are other schools who claim to be Universities, writes Veblen (2009, 10) and he disparagingly protests the validity of the quality of education they offer. Undergraduates are offered professional training, extension classes and “correspondence” for amateurs he writes. Veblen (2009, 15) sees the multiple learning options as attempts to enroll as many students as possible and to mass produce trained workers for professions in civil life or merely to conclude the college education of young men with no interest in high quality higher learning.
Veblen (1978, 8-13) noted that with complexity of the factory process and its many divisions of labor it required precision and standardization. Likewise, the multitude of University course offerings demanded standardization of time in units or credits hours. It became a matter of accountancy and surveillance wrote Veblen (2009, 16) and it was passed off in terms of efficiency. In actual fact, it undermined the co-operation between the student and teacher with its rigidity of routine and diminished graduate study to virtually an undergraduate extension. Undergraduate work he claimed, is merely “task work” and amenable to standardization and assembly line practices. Just as creativity and satisfaction, was robbed from the craftsman as he was forced into a monotonous, virtually thoughtless process, so is the student robbed of his enthusiasm for learning. Teaching to standards and rubrics for efficient grading has curtailed the deeper thought processes necessary to create scholars and scientists. The student learns to perform like a Skinner box animal. Grade point average is more important than the act of learning and absorbing knowledge.

Veblen (2009, 16) accuses the University offering a set curriculum of being nothing more than a college with little else to offer. He insists that the true University should have no set curriculum and allow the scientist to pursue knowledge at his will. The current experience is that the professor must teach undergraduate and graduate courses but also research and produce papers that bring either prestige or profits; by all accounts---both. Veblen (2009, 12) claims that the man of science (the professor) in reality has little autonomy and is obligated to be the taskmaster and vehicle of indoctrination which detracts from his own discovery.

Accordingly, the student has the right to a legitimate education and to make a scholar of himself if he is so inclined. Veblen (2009, 13) asserts that the lower schools, which may include all public Universities today, have the sole goal of preparing a student for civil life, what we might
call a standardized output or product. Many members of the community argue that the University is actually failing to provide an education that fully prepares a student for the prevailing market and civil life. With the Universities effort to “round out” the college student’s learning, curriculum of dubious content has been edged into circulation and offers no relevance to the real world nor can it justly be called esoteric knowledge. A fine line exists between entertainment (theater studies) and education with on-the-job training (internships) and instruction in “commerce” being taught by businessmen instead of academicians. Veblen (2009, 141) contends that the teachers of commerce have diverged increasingly from scientific inquiry to a point very distant from authentic higher learning. Just as the factory process diminishes the need for critical thinking, so does the watering-down of education and curriculum under the guise of higher learning.

Veblen (1978, 323) proposes that the machine process weakens the pecuniary dexterity of the workman, whom he suggests is incapable of thrift and instead spends his earnings on conspicuous consumption. The machine process has created a mobile workman with no interest in real estate investment. The modern student likewise has no regard for living a thrifty life and although the cost of tuition is extremely high compared to future incomes and the cost of schooling in foreign countries, the culture of consumption with credit is rampant. Veblen (1978, 325) believes that preaching of thrift has had no effect on spending behavior and he argues that the exemption from pecuniary training is only partly responsible. The balance of the cause is the fact that consumption is promoted as modern and good. Thomas Princen ([1951] 2005, 63) suggests that the ultimate consumer was created out of the factory system. He believes that subordination in the workplace could be accepted if one was able to have “mastery” elsewhere. As a consumer, one has control or purchasing power. Higher wages, less expensive products and consumption were the hallmark of the Ford era and the consumer sentiment has held over. The student who
perceives himself as having little autonomy in the efficient, higher learning system, fancies to look good and sometimes generous for his/her peers.

Adding to their acceptance of calamitous debt, is the societal notion that a student should rid him or herself of parental oversight and leave home. The University promotes this action in terms of independence and the ability for the student to have a “complete campus experience”. The skeptic might question the actual value of campus living and consider the pecuniary interest of the University. Veblen (1978, 20) reminds us that the pecuniary gain through purchase and sale is the motivation of every businessman. The University is a machine process and a business. The President is a businessman.

Higher Education and Pecuniary Gain

Thorstein Veblen (2009, 39) insists that the University’s main purpose was historically to diffuse knowledge without turning a profit, but as with any machine process or business, the goal is always to turn a profit.

While some argue that a well rounded education makes a complete scholar, one might also argue that this concept has been taken too far. Most public colleges and Universities require that a core curriculum be completed as part of the undergraduate and graduate degree qualifications, but personal experience has shown that Portland State University, while repeatedly praising its own University Studies program, fails to notice the complete dismay of the freshman student. Courses such as these are unique and non-transferable to most other Universities. A portion of the freshman inquiry course credit time is “taught” by low-paid undergraduate students. It is a cost saver for the University but a disservice to the student. The investment or “buy in” of the professors in the
program is bleak and disheartening and few are tenured. It can be likened to the cost cutting measures of the factory system that might include the use of inferior, material inputs.

Repackaging can be seen in the renumbering of courses. From time to time, departmental heads reformulate the course requirements for a baccalaureate degree. Students find that they will be required to fulfill as much as an extra term to satisfy the degree requirements. The critic might argue that it diffuses no extra knowledge but may in fact be an attempt to break one course into two separately priced courses. Many courses required in sequence are highly repetitive and one wonders at the intentionality of that fact.

In order to fool a consumer into believing he is getting a better “deal” the producer or businessman may repackage an item differently. This is a tactic the higher education factory employs. Educational fees are accepted by students as a matter-of-fact. They are rarely inclined to notice how much of their “tuition” is actually fee charges. Online learning, the kind of education Veblen despises, has added fees of up to three hundred dollars per term but often this fact is overlooked due to complicated appearance of the account tabulation. Students are not equipped to understand their own finances and the added online costs are never made obvious.

Veblen (2009, 10) criticized learning by correspondence as learning performed by amateurs. Personal experience has shown that learning from the online platform is as equally flat as the old fashioned “correspondence course” and lacks social reinforcement as well as the connection with the faculty member. Online learning may be seen as a repackaging of an old product with an added charge for the student and a potential cost saving for the University.

Of pertinent note, Portland State University has a current shortfall in revenue yet the President recently awarded himself and fellow administrators pay raises. While the craftsman charged for his goods and services to feed his family and the early businessman, spurred by the
increase of technology, sought to produce more goods, the machine process has produced a new kind of businessman; the Chief Executive Officer (CEO). The lust for profit or pecuniary gain, enabled by the efficiency of the machine process has created the CEO who will employ any means to extract profit from the enterprise. He rewards himself first, then his investors and last of all, the enterprise.

**Conclusion**

This inquiry has sought to establish that what Thorstein Veblen advances as a machine process can indeed be applied to offer insights into higher education in the United States of America.

Both the machine process and higher learning began in humble places with the intent of creating the finest products, molding individuality and innovation in a creative and fluid process. Both processes have tightened the reins on the individual “thinker” or workman and have conformed his thoughts and days to a schedule that organizes him in impersonal standardized units, inputting and outputting for the purpose of pecuniary gain.

**References.**


The Marxian Social Theory and Capitalist Crisis

By: Ruchira Sen

Abstract: This paper provides a brief explication of Marxian social theory. It examines the Marxian view of the development of capitalism and the contradictions that make capitalist crisis inherent in the system. In this regard, this paper argues that the Marxian explanation for crisis in capitalism is superior to the neoclassical consensus approach which simply assumes crisis away. This paper also tries to look at Marxian social theory from a contemporary lens, revisiting the structure-agency debates about revolutionary political praxis in the Second International and taking lessons from them with regard to the further development of Marxian social theory to address the questions of economic instability at the core of capitalist development and indecent labour conditions at the periphery today.

Introduction

Over the last five years, the world watched while the financial crisis in the USA deepened into a very real recession. In the European Union governments plunged their people into destitution and unemployment to pay off their debts. The repercussions of the crisis in the advanced capitalist core spread to developing countries who, already saddled with unimaginably poor and rapidly deteriorating living and working conditions, also faced the brunt of macroeconomic instability.

It is no wonder that the dominant ideas of the pre crisis period fell into disrepute. These were the ideas of the neoclassical consensus. According to the social ontology of this view, human
nature is innately rational and that while atomistic, rational individual agents make decisions intended to maximize their own benefits, an ‘invisible hand’ coordinates these decisions in such a way that social welfare is maximized. Clearly, in a system like this, there can be no systemic breakdown – there is no possibility of crisis. Any unemployment is the result of some rigidity in wages and that the self-equilibrating mechanism of the invisible hand would sweep such unemployment away. However, it became clear that nothing like this would happen.

As young people around the world searched for alternative ways to understand what was happening around them, ideas of radical political praxis became popular. The Occupy Wall Street movement identified finance capital as a dominant ‘class’ and rose to speak truth to power. Anti-austerity protests in Europe echoed this sentiment. All over the world, there was a resurgence of radicalism and a development of class consciousness. With the rise of such ideas, there was a renewed interest in Marxian social theory.

Section 1 of this paper is aimed at briefly outlining the main ideas of Marxian social theory – these are i) alienation, commodity fetishism and surplus value, ii) the process of historical development in capitalism or historical materialism and iii) the ‘reserve army of labor’ and capitalist crisis. In Section 2, I will explicate the Marxian Social Theory according to Global Social Theory (Bowles, 2013)\(^1\) which provides a useful set of criteria to compare and evaluate the various interdisciplinary social theories. Through this I aim to draw out how very different the Marxian social theory is from the neoclassical consensus approach and why it provides a superior analysis of capitalist crisis. In Section 3, I argue that Marxian social theory is more than just a way of observing the world. Instead, Marxism takes theory away from the ivory tower and into the streets – Marxian social theory is a theory of praxis. As Marx is known to have said, “Philosophers have interpreted the world in several ways: the point however, is to change it” (Marx, 1888).\(^2\) Marxian social theory is also a theory of development – everyday new social relations are developed, everyday capitalism evolves – praxis must also evolve to speak out against newer forms of exploitation. Similarly theory must also evolve to understand the newer contradictions within the capitalist system and to map out future political praxis. Therefore, Marxian social theory is a product of history. It is not possible to go back to reading Marx’s writings to discover a pure form


\(^{2}\) Marx Karl (1888), Theses on Feuerbach.
of his ideas (Joseph, 2006). Instead, the theory must evolve and resolve the conflicts within itself to address the contradictions in the economic system. In this light, I revisit the old debates of the Second International and draw from the ideas of different Marxian scholars to think of new ways to understand the current crisis in capitalism and what it means for revolutionary political praxis.

I

When Marx was a young man writing his doctoral dissertation at the University of Berlin, he was an active member of the ‘Young Hegelians’ – a club of young students who were interested in the ideas of Hegel (Giddens, 1971). Marx was drawn into this circle as he admired Hegel’s view of development as a historical process through a conflict of ideas – a process of thesis and antithesis – that converge to form a synthesis. About the time Marx submitted his dissertation, Feuerbach published his ‘The Essence of Christianity’. This work was received by the Young Hegelians with great enthusiasm. As Engels was to write “The spell was broken: the ‘system’ was shattered and thrown aside... Enthusiasm was general: we all became at once “Feuerbachians”” (Marx and Engels, 1958).

Marx was impressed with Feuerbach’s materialism. Unlike Hegel, Feuerbach did not see the ‘real man’ as emanating from the ‘divine’. Instead, he argued that the divine is an illusory product of the real (Giddens, 1971). For Feuerbach, God can only exist as long as man is ‘divided against himself’ or ‘alienated’ from himself. God is simply a fantasized being on whom man has projected his own highest powers and faculties and is thus seen as perfect and all-powerful and in contrast to whom man appears limited and imperfect. Feuerbach asserted the primacy of the material world arguing that the love formerly directed towards God must be directed towards man, replacing religion with humanism. While the old Hegelian idealist philosophy assumed that thought precedes existence, the new Feuerbachian philosophy argued that existence precedes thought.

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7 Giddens Anthony, (1971) ibid
Since Marx was primarily interested in philosophy as a guide to political praxis or the guide to a better world,\textsuperscript{8} he was attracted to materialism as it made human beings into the agents of change. However, Marx felt that Feuerbach’s approach was ahistorical – Feuerbach conceived an idea of the ‘abstract man’ who existed prior to the existence of society and reduced man to the ‘religious man’ without recognizing that religious feeling is itself a social product and that the abstract individual he analyses belongs to a particular form of society. Therefore, Marx did not see Feuerbachian materialism as an alternative to the Hegelian dialectical process. Instead, he sought to juxtapose materialism to the Hegelian dialectical process to create the theory of historical materialism in which human history is created not from a conflict of ideas but from contradictions between material processes and social relations between human beings.

Marxian social theory has often been accused of economism – of privileging the economic sphere or the sphere of production and exchange over any other. However, this was also a product of philosophical debates in Marx’s time as the prevalent ideas of socialism or communism were ‘Utopian’ in nature – Marx and Engels were of the view that they were not grounded in the material developments of the time – and therefore, irrelevant for praxis and social change. This is why Marx thought it most important to begin Capital with an analysis of commodities and the relations of production and exchange.

\textbf{i) Alienation, Commodity Fetishism and Surplus Value}

Marx identified the capitalist production process as a system based on commodity production. A commodity is not merely something produced for its ‘use value’\textsuperscript{9} or its ‘value in use’ but for sale

\textsuperscript{8} When asked to write an essay on the reflections of a young man when choosing a career in his final school examinations, Marx wrote that the choice of a career must be guided by two principles – the welfare of humanity and one’s own excellence. According to Marx, there can be no conflict between the development of one’s own capabilities and the welfare of humanity. Instead, young people can find their own personal development only when working towards the welfare of humanity (Giddens, 1971, ibid).

\textsuperscript{9} Use value derives from the consumption of a commodity. The use value of a chair draws from the fact that one can sit on it. It is possible for non-commodities to have use value for instance oxygen has use value in that one can breathe it in. However, oxygen is not a ‘commodity’ unless it is put into a cylinder and sold in the
in the market. Capitalism is associated with the creation of large, national and even international markets for goods. When a commodity is sold in the market, it assumes a kind of value other than value in use. This is the value in exchange – the value at which one commodity can be exchanged for another. However, what is the basis for exchange i.e. what is the philosophical rationale for equating say, a desk to three pumpkins? What does the desk have in common with the pumpkin? Certainly not ‘use value’ – as a desk and a pumpkin are used for different purposes.

To explain this, Marx drew upon an idea of abstract value. Commodities acquire abstract value as they are products of human labour. The value of a commodity is the expenditure of human labour in its production – whether or not they are commodities, all goods possess value as they are products of human labour. This value must not, however, be confused with price. Price in Marx, may be affected by demand conditions. Abstract value however, is not. Returning to the example of the relationship between a desk and a pumpkin – they are both products of labour. A carpenter has spent a certain number of hours producing the desk and a farmer has spent a certain number of hours growing pumpkins. The relationship between the desk and the pumpkin is actually a relation of exchange between the carpenter and the farmer. However, it takes the form of a relationship between things as opposed to a relationship between people. This is called ‘commodity fetishism’ – it alienates people from the products of their labour and human relations take the form of relationships between commodities. Commodity fetishism is exacerbated by the use of money which works as a unit of account for measuring the value of commodities, thus obfuscating the fact that when we say that a desk is worth $30, it is a product of a certain number of hours of human labour.10

However, if the value of any commodity is given by the number of labour hours in its production, one is bound to ask this question: Is the product of a lazy worker who takes more time to produce a commodity more valuable than the product of an industrious worker who takes less time to produce it? Marx solved this dilemma by introducing the idea of ‘socially necessary labour’ – the number of labour hours required to produce a commodity on average (which can be interpreted as the market value of a commodity). In short, non-commodities can have use value but commodities have both, use value and exchange value.

10 It is not accurate to say that the desk is worth $30 equivalent in human labor hours as value must not be confused with price. However, in the aggregate, the national output (denominated in dollars) can be thought in its equivalent of human labor expenditure (Giddens, 1971, ibid.)
empirically calculated). He further brought out the idea of ‘alienation’ – workers are not only alienated from the products of their labour as they lose control of the production process but they are also alienated from their own labour – their labour becomes a commodity like any other, its value in use being the actual kind of labour i.e. masonry, carpentry etc and its abstract value being the labour hours required to produce the means of subsistence required for workers to reproduce their own labour day by day. The minimum level of subsistence required for labour to reproduce itself is sociologically determined – it is the cultural notion of basic living standards, it is also a product of history – the claims of workers from developing countries or ex colonies who are historically accustomed to worse living standards may be more downward elastic than the claims of workers from developed countries. As labour is a commodity like any other, it becomes possible to think of average labour hours required to produce a particular commodity as the socially necessary labour required to produce it.

The concepts of value as abstract labour and labour as a commodity like any other also help us to examine another philosophical dimension – profit. Capitalism is driven by the eventual motive of accumulating capital. Suppose we think of capital as money capital. Then the process of production can be written as M-C-M’ i.e. money (M) is used to purchase commodities which are transformed by the process of production and sold for money (M’). No capitalist will go through the pain of purchasing commodities to be transformed via production unless the end result M’ is greater than the M that he put into production. But how does M’ become greater than M? Where is this surplus value created? Marx identified the ‘hidden realm of production’ as the source for the creation of surplus value. Commodities are transformed by the application of human labour and it is this human labour which is the source of surplus value. This can be understood by an example much like one of Marx’s own examples in Capital Volume 1 (Marx, 1887)\(^{11}\). Suppose the average workday is 12 hours. The average per-worker socially necessary labour hours required to produce the means of subsistence for workers as a whole is 5 hours. This means that on average, workers have expended 7 hours of labour over and above the minimum labour hours required for them to produce the means of subsistence necessary to reproduce their own labour. This extra 7 hours is called surplus labour or surplus value.

\(^{11}\) Marx Karl, (1887) ‘Capital Volume I’, Progress, Moscow.
The Theory of Surplus Value turned the political economy of Marx’s day on its head. The labour theory of value was nothing new—it was something the all political economists since Adam Smith agreed on. However, the Theory of Surplus Value expressed the idea that profit is by nature, a product of the exploitation of labour. It brought in a class consciousness into the study of political economy and thereby radicalised it.

Underlying Marx’s discussion on commodity fetishism and surplus value is the concept of alienation. Unlike in philosophical discussions of his time, Marx does not understand human alienation as alienation from the ‘essence’ of humanity. Instead, the Marxian view of alienation is to be understood in material terms and through material processes. Alienation implies the worker’s lack of control over the production process. The worker cannot take decisions with regard to the production, exchange and distribution of the products of her labour. With the mechanisation of the production process and the division of labour this facilitated, the worker has lesser and lesser emotional connection with or creative satisfaction from the production process. She could be doing no more than tightening a screw on an assembly line—for over eight hours a day! Under the capitalist production system, the ordinary worker cannot develop her mental and physical capabilities. Meanwhile, relations between people are reified as relations between things i.e. commodity fetishism and the human relations of production are forgotten.

The alienation of the worker in the capitalist economy is founded upon the disparity between the productive power of labour which increases with the expansion of capitalism and the lack of control which the worker is able to exert over the objects she produces (Giddens, 1971)\(^\text{12}\). As average productivity of labour increases, more commodities are produced—as more commodities are produced, they become cheaper and it takes lesser labour hours to produce the means of subsistence. The more workers produce, the lesser is the value of their labour.

\[\text{ii) The Process of Historical Development in Capitalism or Historical Materialism}\]

It may be recalled that the neoclassical consensus theory is based on an idea of ‘natural rights’—right to life, liberty and property. Marxian materialism posits a direct critique of such ideas. The main defect of idealism is that it attempts to analyse the properties of societies by

\[\text{\footnotesize\textsuperscript{12} Giddens Anthony (1971), ibid.}\]
inferring the dominant system of ideas (Giddens, 1971)\textsuperscript{13}. This neglects the fact that the dominant class is able to disseminate ideas which are a legitimisation of its position of dominance. The legal freedoms that are possible in bourgeois democratic systems legitimise contractual obligations in which property-less workers are heavily disadvantaged as compared to owners of capital. Therefore the right to liberty includes only freedom of speech, expression and ownership of property –not freedom from hunger or exploitation.

Nonetheless, Marxist materialism must also be seen in a historical sense –as driving the evolution of history. Contrary to the neoclassical consensus view, the ‘right to property’ or even the existence of property was not a ‘natural’ order of things. Instead, when one traces history back to primitive communism, property is communal –it is not co-operative in the sense that people pool in their property and share it; instead, people use natural resources in the same way that cattle graze upon the commons. Just as the ‘commons’ belong to everyone, similarly, there was no private property –land and other resources were simply held in common.

Marx theorised that the system of private property ownership first showed up in the Greco-Roman city-states\textsuperscript{14} in which only ‘citizens’ or property-holders had rights. The expansionist tendencies of these city-states came with an expansion in population which necessitated the conquest of more property –in the sense of land and slaves.

The best example of historical change through the dialectics of material processes can be seen in the transition from feudalism to capitalism. The most well known known case study as documented by Marx is that of the classic case of England in which a beleaguered nobility, impoverished by wars fought against each other, began disbanding its army of retainers and fencing off pasture-lands (a process partially accelerated by the increase in wool prices and the rise of the wool industry) to create a large pool of ‘free’ labour. By ‘free’ labour, it was meant that these disbanded workers were stripped of any property or any feudal obligations –in fact, they were stripped of everything but their labour power. This was the first necessary condition for the development of capitalism –the creation of a working class, a proletariat. Added to this was the

\textsuperscript{13} Giddens Anthony (1971), ibid.

\textsuperscript{14} In his early works, Marx wrongly assumed that there was no stratification based on property in Asiatic societies which were based on self-sufficient villages rather than cities. Perhaps Marx was not acquainted with the inhumane caste system in the Indian subcontinent and possessed a Eurocentric view that romanticized the Indian village system. However, this view may have been altered in his more mature works.
contribution of colonial expansion and international trade which brought in fresh imports of spices and muslin, causing the aristocracy to prefer holdings of money rather than land and retainers. The feudal system contained within itself, the seeds of its own destruction.

This is the essence of Marxian dialectics. Historical development is driven by contradictions between forces of production and production relations. As production relations change, it is found that the whole system of social and cultural ideas that once served to uphold production relations becomes oppressive to material change and the ‘economic base’ of production relations comes into conflict with the ‘superstructure’ of social and cultural relationships.

As expected, this view has been subject to interpretations and misinterpretations. One such interpretation is that of Marx as a technological determinist. Historical change is driven only by changes in technology or forces of production. Technological change comes in conflict with the system of production relations based on the old technology and drives a change in production relations. These in turn come in conflict with the social, cultural and religious relationships which legitimise the old relations of production and thus act as fetters upon the change in production relations and thus, these must also change. All societal change is driven by technological change. Technological determinists draw upon Marx’s famous quote in The Poverty of Philosophy for support, “The hand-mill gives you society with the feudal lord; the steam-mill society with the industrial capitalist (Marx, 1847).”

It is certainly true that Marx did consider technological change to be an important engine of social change. However, it is definitely inaccurate to say that Marx thought it was the only engine. As in Lukàcs’ critique of Bukharin, "Technique is a part, a moment, naturally of great importance, of the social productive forces, but it is neither simply identical with them, nor. . .the final or absolute moment of the changes in these forces” (Lukàcs, 1925).

Discussion of Marxian materialism also raises the question of the inevitability of the historical process –is every exploitative system based on class and property eventually doomed as every system contains within itself, the seeds of its own destruction? Is it inevitable that like feudalism, capitalism must also collapse? This question was one of the chief bones of contention in the Second International where Lenin and the Bolsheviks were of the view that the Bolsheviks

15 Marx Karl, (1847) 'The Poverty of Philosophy’, Paris & Brussels
16 Lukacs George (1925), "Technology and Social Relations,” New Left Review, no. 39
must seize political power in Russia and commence the process of building a socialist state on the principle of ‘the dictatorship of the proletariat’ while Kautsky, Luxemburg, Gramsci and several others felt that such a move would be premature and adventurist. (Joseph, 2006)\textsuperscript{17}. For most of these thinkers, it was assumed that even capitalism plays a historic role –that of developing the means of production.

This brings in the age-old question of structure and agency. Is there an ‘agency’ in Marxian social theory? A technological determinist may think otherwise as for her, all social change arises from technological change (even though this is a very ahistoric way of looking at technological change). Similarly, the supporters of the ‘inevitability’-of-capitalist-collapse view may lay emphasis on structure –capitalism would collapse when the forces of production had expanded, when labour was cheapened and when there would arise a very big contradiction between the development of capitalism and its own collapse.

However, one must recall that Marxian social theory is a theory of praxis. And the Marxian view of social stratification is based on class divisions. There are two principle classes in capitalist society –the bourgeoisie who own the means of production and the property-less free workers or the proletariat who have been historically dispossessed of everything but their labour power. In addition to these, there is also the free peasantry, the professional or the middle class and the lumpen proletariat –vagabonds, criminals etc. The existence of classes and the creation of class consciousness leads to a process of class struggle. If the workers are successful in organizing themselves and creating a ‘class consciousness’, they can struggle for living minimum wages, the famous eight hour work-day\textsuperscript{18}, decent work conditions and so on. This brings them into direct conflict with the capitalists as reducing the length of the workday or demanding minimum wages reduces the rate of surplus value. The agency of class can also express itself as it did during the Bolshevik or the Chinese revolutions –a well organized, disciplined movement of workers and peasants can help seize State power and commence the task of building socialism –even though capitalism has not yet been built and has thus not fulfilled any role, leave alone its historic role of developing the means of production. Lenin justified this contradiction by arguing that Russia was the ‘weakest link in the imperialist chain’ –it was a largely agrarian, feudal society but it had a

\textsuperscript{17} Joseph Jonathan, (2006) ibid.

\textsuperscript{18} “Eight Hours for Work, Eight Hours for Rest, Eight Hours for What We Will.”
highly disciplined industrial proletariat with an advanced sense of class consciousness while the national bourgeoisie was weak and disorganized and entirely dependent on international support which wasn’t always forthcoming. It was an opportune moment for the proletariat to seize power and create its own socialist development model (Lenin, 1921).

The structure-and-agency debate is still an important question for Marxist political praxis today especially for Marxist praxis in the periphery of economic development. In India, the Communist Party of India (Marxist) has come under valid criticism for appropriating land from the peasantry for the development of industry by big capital – no doubt a betrayal of the ‘toiling masses’ of Bengal. The Party justified this policy by drawing upon the idea of the inevitability of capitalist collapse – it saw its own task as the task of building capitalism and when capitalism would reach an advanced stage of development, it would self-destruct. Similarly, the Communist Party of China continues to follow a strategy of export-led development based on the suppression of wages in order to export cheaper and cheaper manufactures to the rest of the world. Chinese workers are known to work shifts of over thirteen hours a day (Hirway, 2010) and there have been reports that workers have been made to sign contracts promising not to commit suicide on account of the inhuman work conditions in the factories. The CCP however, sees no contradiction between its role of upholding the interests of the workers and the building of ‘market socialism’ – by the Stages of Capitalist Development approach, the CCP is only developing the forces of production and that one day market socialism would inevitably make way for communism.

iii) The ‘Reserve Army of Labour’ and Capitalist Crisis

Unlike the neoclassical consensus which has almost no explanation for chronic periods of unemployment, in Marxian social theory chronic unemployment is more of a norm than full

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20 Perhaps by the proletarianisation of the peasantry.
employment. This is because unemployment in capitalism pays a social purpose—it serves as a depressant on wages so that the rate of surplus value can be increased. Marx introduced the concept of the ‘Reserve Army of Labour’—a pool of chronically unemployed workers who can be drawn into the labour force when demand conditions are favourable, thus bringing about an increase in production without a corresponding rise in wages. As individual capitalists compete for profits, there is a tendency to opt for labour saving mechanisation which tends to displace workers and bring about an expansion of the reserve army of labour. This adds weight to Marx’s theory of immiserisation. ‘Value’ in capitalism is created by labour—which reproduces not only its own value (i.e. the number of labour hours required to produce the workers’ means of subsistence) but also ‘surplus value’ which is on aggregate, the profit that accrues to the capitalist class. The expansion of capitalism can occur as long as capitalists have the incentive to accumulate capital—which is as long as capitalists make profits. The reserve army of labour plays a role in suppressing wages to mere subsistence levels so as to allow for high surpluses and thus, the expansion of capitalism. As capitalists compete with themselves, they adopt labour saving mechanisation—which increases the ‘organic composition of capital’—this causes the displacement of labour and the expansion of the reserve army of labour—which further depresses wages. The more value that labour creates, the cheaper it becomes.

In the course of the development of the advanced countries however, Marx’s theory of immiserisation was said to be disproved as workers in advanced countries found that they would obtain wage increases and decent conditions of work and life through the success of their trade union struggles. However, Marxist scholars from Rosa Luxemburg and Lenin to Paul Baran, Andre Gunder Frank, Prabhat Patnaik and many others observed that the improved conditions of the working class in the advanced countries had followed upon the ‘export of unemployment’ to the developing countries where a ‘free proletariat’ had been created by a process of primitive accumulation driven by various colonial processes—taxation (Forstater, 2005)\textsuperscript{23}, forced contracts (Dutt, 1902)\textsuperscript{24} etc. The process of primitive accumulation had created a ‘reserve army of labour’


for global capitalism in the developing countries—simply exporting unemployment away from the advanced countries where improved conditions of work and life and thereby, a degree of political stability became possible. What workers in advanced countries did not foresee was that the reserve army of labour—even though it was stationed in the developing countries—would still serve as a depressant to wages in advanced countries. In the recent years, this has become more apparent with the shift of production processes away from advanced countries to developing countries—made easier perhaps by the technological improvement in communication facilities, fuelling the popular American fear of the shift of jobs to China.

Though the whole aim of the capitalist production process is to create profit, profit in capitalism has a tendency to decline. This is because the total profit in the economy depends on surplus value created within it. In fact the rate of profit is given by the ratio of surplus value to the value expended in total production i.e. constant and variable capital. Constant capital here, is the total labor hours that are expended in replacing the depreciation of plant, machinery and tools. Variable capital is the total labor hours expended in creating the means of subsistence required by the workers to reproduce themselves. In the economy as a whole, the ratio of constant to variable capital tends to rise as capitalists engage in labor saving mechanisation in competition with other capitalists for individual profits—this produces a new equilibrium in which every capitalist has a higher ratio of expenditure on constant capital than before, causing the rate of profit to decline.

There are of course, some countervailing tendencies to this downward tendency—the rise in the ratio of constant to variable capital also means a rise in productivity which may find expression as an increase in total surplus value as with increased productivity on average, workers can reproduce their own value in lesser time, thus producing more surplus value per working day. This can also be driven by an intensified exploitation of labour through an expansion of the working day.

Marxian social theory holds that capitalism is an anarchic system and there is no definite agency relating production to consumption. This is in sharp contrast to the neoclassical consensus theory which assumes that this definite agency exists in the form of an invisible hand. In Marxian social theory, capitalism is also an expanding system driven by a restless search for profit. As the profit motive is dominant, any state of affairs involving an imbalance between the volume of
commodities produced and their saleability at the average rate of profit constitutes a crisis for the system. If goods produced cannot be sold at the average rate of profit, then the average rate of profit must decline. This in turn dissuades capitalists from investing their capital in the production process, causing the engine to slow down and causing workers to be laid off. As workers are laid off, consumer purchasing power is diminished which causes another tendency for the rate of profit to decline.

II

To truly understand how the view of crisis in Marxian social theory is superior to the neoclassical consensus theory view, it is useful to compare the two theories according to a pan disciplinary set of criteria. The Global Social Theory Approach (Bowles, 2013)\textsuperscript{25} lays down a set of interactive criteria in a dynamic framework by which we can evaluate and compare the various ‘relatively adequate’ interdisciplinary theories. The criteria specified in the GST are as follows:

1. A conception of human nature as held by different theories.
2. An understanding of social stratification and structure and how group identities are constituted.
3. Individual or group agency or action
4. Material and social processes that may lead to certain goals –whether growth or development or some sort of end.
5. Philosophical foundations or meta-theoretical commitments:
   a. Ontological commitments –what does x theory assume to be real? Social Ontology is a theory of existence.
   b. Epistemological commitments –how does x theory claim knowledge of what it thinks is real. Is it based on a trust of observation (empiricism) or is it based on the inner thought processes of the human mind (rationalism)? Epistemology is a theory of knowledge.

\textsuperscript{25} Bowles Doug (2013), ibid.
c. Axiological commitments –what moral values does x theory uphold? What is its conception of the ‘good life’ or of ‘virtue’. Axiology is a theory of value.

These criteria are dynamic and interactive as shown in Figure 1.

Figure 1: GST as an Interactive, Dynamic System

As seen in Figure 1, the conception of human nature serves as an ontological commitment by which one may arrive at an understanding of the nature of human agency. Similarly, human agency may be confined and directed by social structures. Human agency sets in motion, the material and social processes of development which in turn, reproduce the social structure.

How can we think of Marxian social theory when set in the framework of GST criteria? Does Marxian social theory involve a conception of human nature? According to Norman Geras

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26 Bowles Doug, ibid.
(Geras, 1983)\textsuperscript{27} there is a vulgar view of Marx which holds that the individual is of no importance in Marxian social theory and that human nature is only a product of social structures. This view is derived from Marx’s ‘The Sixth Thesis of Feuerbach’ (Marx, 1888)\textsuperscript{28}

“Feuerbach resolves the religious essence into the human essence. But the human essence is no abstraction inherent in each single individual. In its reality it is the ensemble of the social relations”

-Marc, 1888.

Geras argues that it is incorrect to form a view of the conception of human nature in Marx on the basis of a single quote while the whole point of the transcendence of capitalism and the alienation inherent in capitalist division of labor is the full development of human potential and capabilities. The fully developed individual would not have to spend the entire day tightening a screw on an assembly line, for example. Instead, she should be able to fish in the morning, take part in production activities—all of which must give creative satisfaction and theorise in the evening.

Marx is of course, best known in classical sociology as one of the pioneers of the theory of social stratification. Social stratification in Marxian social theory is based on class and agency is expressed through the development of class consciousness and class struggle. The dialectics of change take place through the development of production relations and via class struggle, the working class is able to effect changes in the production process and in social, cultural and religious relationships that are defined to suit the needs of the bourgeoisie and to justify the exploitation of labour by capital. It is a matter of debate whether change in cultural and social relationships by the assertion of an identity (for example, by the feminist movement) is a revolutionary change or merely a superstructural change. In the recent years however, Marxist political activists have become more open to building coalitions—often called ‘rainbow coalitions’—of social and progressive movements like the indigenous movements in Bolivia and Ecuador or the feminist movements or movements against nuclear energy—to serve as agents of social change.

Through the agency of class struggle or by the dialectics of change driven through technology, material and social processes resolve their contradictions and create newer forms of

\textsuperscript{27} Geras Norman (1983) Marx and Human Nature: Refutation of a legend. Verso

\textsuperscript{28} Marx, Engels (1958) ‘Selected Works’, Volume 1, pg 13-15
capitalism. The Marxian social theory is a teleological view that anticipates some kind of end. For the Marxists, the end is communism. As the popular socialist saying goes, “Another world is possible”.

It is not difficult to see that this view is in sharp contrast to the neoclassical consensus theory. While the Marxian social theory has an ontological commitment to looking at every relationship or every force as a product of history, the neoclassical consensus view takes an ahistorical view of human beings as innately rational, atomistic individuals who take actions to maximize their own welfare and therefore, set off processes by which the welfare of society is maximized. Clearly, such a view is not only ahistoric but also not systemic. It does not understand deviations from situations of maximum social welfare as a part of the system. Instead, it makes false predictions, stating that the ‘disequilibrium’ will soon go away and that some institutional mechanism may be holding it up.

The Marxian view on the other hand, understands that every system has contradictions which are resolved as a part of a historical process to make way for newer forms of a social system or perhaps, a new social system altogether. The capitalist system has a tendency to cause the immiserisation of a large part of the global population in its relentless drive for profits—which may have to come to a halt as a very poor population cannot be a very good market for goods and services. Also, there is no definite agency by which all that is produced will be sold in the market—causing an inherent tendency towards overproduction and crisis.

Marxian social theory does not believe that every crisis will bring about the socialist revolution, however—contrary to popular perception. Quite often, a crisis may be successful in doing no more that suppressing wage claims to the level that restarting production may once again, become profitable (Giddens, ibid). The rise of Keynesian policies for stimulating activity presented a new social system in which institutions to keep economic activity at a desirable level were created. However, though this enabled the development of welfare and social security in advanced capitalist countries, the presence of the reserve army of labour in developing countries continued to depress wages. The challenge before Marxist political activists has remained that of identifying the contradictions in the rapidly developing capitalist system and arguing that the capitalist system, at each juncture, is based on creating great wealth at one end of the world and great poverty at another.
Marx is perhaps, one of the most interpreted, re-interpreted and misinterpreted figures in the philosophy of social science. Interpretations of Marx have ranged from positivist, heuristic, deterministic and humanist to critical realist. Nonetheless, there is no ‘pure’ form of Marxist theory and Marxian theory develops with Marxist political praxis –as a way to understand and address the challenges thrown by new developments –whether in technology or in institutions, whether in relationships based on class or identity.

The most heated debates in the history of Marxist political praxis were played out during the Second International –an international organization of socialist and labour parties formed in Paris on July 14, 1889. This was dissolved before the First World War as the different national parties could not form a united front against the war -which was a victory for the revisionist view championed by Bernstein who believed that the proletariat should support the war effort of their respective countries in the immediate and in the long term, win concessions from capital in the form of higher wages and better working conditions. Bernstein had given up hope that some crisis or some instability in capitalism would set off contradictions leading to its own downfall. Instead, he believed that through the system of credit and cartels, the capitalist system had largely stabilized and that the working class should direct its energies towards securing a better life in the capitalist system.

This view was sharply criticized by several voices in the Second International –the determinist voice of Kautsky, the orthodox “Pope” of Marxism and the revolutionary voice of Rosa Luxemburg’s Spartakist group. Kautsky could not stem the tide of revisionism in the Party and perhaps, his doctrinaire approach to dialectical materialism as drawn from the natural sciences remained unappreciated by Party members (Joseph, 2006)29. Rosa Luxemburg criticized Bernstein’s notion of capitalism as a stable system. By 1913, Luxemburg had published her own understanding of crisis –Accumulation of Capital (Luxemburg, 1913)30. She understood that there is no agency to induce capitalists to keep investing their capital in production –with the expansion of the reserve army of labour and the infinite suppression of wages it is unlikely that the expanded reproduction can go on forever –eventually a situation of overproduction is bound to manifest

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itself. She identified the colonial incursion into pre capitalist markets as a possible source of demand, thus relating the concepts of crisis and imperialism. Luxemburg was however, highly critical of V.I. Lenin’s argument for taking over political power in Russia –like Gramsci and many others, she felt it was premature. She was also critical of the rigid centralism in Bolshevik Party organization as it suppressed individual liberties and felt that seeing the Party as the revolutionary vanguard would distance the Party from the masses.

On his part however, V.I. Lenin answered Bernstein’s claims of the stability of capitalism through the provision of credit and the creation of cartels with his own theory of imperialism. Lenin argued that capital was getting increasingly concentrated in the advanced capital countries through the development of financial institutions. The First World War, for which Bernstein thought that the proletariat should rally behind their national bourgeoisie, was an imperialist war –a war of monopoly interests competing for markets and sources of raw material. Lenin felt that given the character of imperialism, the spark of the revolution would not come from the proletariat in the advanced countries as imagined by the Marxian orthodoxy but from a developing country. Lenin advanced the idea that Russia was the weakest link in the imperialist chain (Lenin, 1917)\textsuperscript{31}–its national bourgeoisie was weak, it was a largely agrarian society and it had a well developed industrial proletariat with an advanced sense of class consciousness –therefore, the Bolsheviks must seize political power. This was a view far removed from the deterministic view or the view of the inevitability of capitalist collapse on account of crisis. In fact, it was a rejection of the Marxian Stage Theory and an assertion of the agency of class through the actions of a Party-vanguard trained as revolutionaries through tight organizational discipline.

The debates of the Second International were centered on the question of crisis –would there be a day when capitalism would eventually collapse on account of a very large crisis? Bernstein rejected the idea and felt that political praxis should be confined to trade unionism. Luxemburg believed that one day, capitalism would run out of pre capitalist markets to make incursions into and the immiserisation of the global proletariat would bring about a state of overproduction –which is why political praxis should continue to be revolutionary rather than revisionist. Lenin did not concern himself with the question of inevitability. He was a man of action.

–or more appropriately, a man of praxis. He believed that given the concentration of monopoly capital under imperialism, the situation would be one of war as competing monopolists vied with each other for ‘spheres of influence’. In the interest of creating a world of peace, it would be best for communist revolutionaries to seize political power in relatively backward countries.

These competing views of crisis and imperialism maintain relevance for Marxist political praxis in today’s time. In the current period of capitalist crisis, should Left political parties aim to take political power or should they confine themselves to trade union struggles? When Left parties do take political power, should they aim to develop capitalism –even a more humane version of capitalism –or should they aim to form socialist states? What would be the nature of socialist states in the 21st century? Would they be based on democratic centralism like Lenin’s USSR or would they take a radicalized form of democracy where important political decisions are subject to referendum, where even the President will stand for election? What would be the nature of the production process –would it be organized by China where land is held by the State and leased to big business to set up large scale production units or would it be organized in a democratic way –owned and operated by workers? Many of such questions are recently under discussion with the founding of socialist states in Venezuela, Bolivia and Ecuador. Many orthodox Marxists tend to reject the idea of such states as socialist because these States allow individual freedoms and even allow the right to hold property to an extent but no one can deny that these States have posed to challenge to the capitalist system –that too, despite their geographical proximity to the USA, the largest and most potent imperialist force.

Conclusion

The idea of crisis is fundamental to the discussion of Marxian social theory. Not only is the Marxian social theory capable of explaining crisis, but it also shows how crisis is inherent to capitalism as a system. In this way, it is superior to the neoclassical consensus theory view of crisis which is that it is a temporary situation caused by institutional rigidities.

The Marxian theory view of crisis or the question of stability at the core is related to the question of the economic and political relations between advanced and developing countries by which underdevelopment is reproduced in the developing countries. Marxian social theory allows for the explication of the capitalist production process as an international system wherein the conditions faced by workers in developing countries affect those of workers in the advanced
countries as well. Most importantly, it supplies lessons for political praxis –the workers of the world must reach out to each other and develop an international class consciousness and work towards the building of a better world.

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The Other Transformation Problem in Marxian Political Economy

By: Sudeep Regmi

1. Introduction: Socialism and its “political cover”

On reading Marx when one finds him using the words “socialism” and “communism” interchangeably, one wonders what all the cacophony in the literature is about, for it is replete with different interpretations about what Marx had to say about when capitalism ends and socialism begins or when socialism ends and communism begins. A very common interpretation of Marx’s vision of the future is that the chronological order of post-capitalist transformation goes as follows: first there is today’s existing capitalism; following that there will be a transitional society, following which there will be socialism (which is nothing but the lower phase of communism) and then, lastly, the higher phase of communism. My argument in this paper is that this interpretation is erroneous in more than one way.

Firstly, nowhere in his writings does Marx ever posit a “transitional society” that follows capitalism; he specifically mentions a “political transition period” that is to be overseen by the rule of the majority. There is no mention anywhere of an economic transition period corresponding to this political transition period. This leads to a second point: the phrase “transitional society” or
“transitional economy” itself is meaningless. For, since every economy operates with a certain mode of production, and since this “transitional economy” is supposed to lie in between capitalism and socialism, what sort of mode of production is prevalent in this economy? An “in-between mode of production” hardly makes any sense. Thirdly, if Marx held that—as he indeed did—socialism is the same as communism, then one could as well speak of two phases of socialism as one does of two phases of communism. In this respect, socialism cannot be synonymous with “the lower phase of communism” that leads to “the higher phase.” Marx first made use of the distinction between lower and higher phases in his *Critique of the Gotha Program* while discussing how the society that emerges out of capitalism is “still stamped with the birth-marks of the old society.” Furthermore, if one were to note Marx calling socialism a “real movement which abolishes the present state of things” rather than a finished product, one could understand why he was not so keen to divide the future into distinct historical “phases” in chronological order but rather was interested in understanding the struggle against capitalist social relations as occupying a continuum of unresolved tension, the way out of which would involve both theory and praxis. Fourthly, there will be no “the higher phase” anyway; rather, there would be “a higher phase” because nowhere in his works does Marx seem to have been inclined to talk about the future in such deterministic ways.

Given that Marx had in mind something altogether different than what has been distorted in his name, recounting all this interpretive mess here seems a pointless task. What is more useful

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32 Kliman (2013).
33 See Chattopadhyay (2010) for an extensive criticism of this erroneous and forced distinction between socialism and phases of communism.
36 Hudis (2011).
and interesting, and is the focus of our inquiry here, is what Marx meant by socialism (or communism) and what sort of economy and political structure he thought would have to exist both for and after capitalism’s demise.

Throughout his life, Marx was consistent in holding that the transformation of capitalism to socialism involves a political rule of the majority, a regeneration of different kinds of men and social relations, and an economic transformation of the mode of production, with this last task being the gist of the issue. A problem appears when one tries to read the Marx of 1840s side-by-side with the Marx of the post-Paris Commune period. The impact that Paris Commune had on Marx’s thought has been well-documented and need not be elaborately discussed here, except that it is important to note that he seems to have taken a less dogmatic and more uncertain stance on quite a few issues after 1871 as compared to his work in the 1840s. Two issues relevant here for our purposes are: one, the primacy of political revolt over economic transformation; and two, the need for a workers’ state in a post-capitalist “political transition period.”

Writing in 1844, it appears to have been quite clear to Marx that economic transformation could not be achieved without a political revolt. He writes, “[G]enerally a revolution – overthrow of the existing power and the dissolution of the old relations – is a political act. Without revolution socialism cannot be viable. It needs this political act to the extent that it needs destruction and dissolution. However, where its organizing activity begins, where its aim and soul stand out, socialism throws away its political cover.” The Marxist theory of transformation of capitalism that followed seems to have taken this statement of Marx to mean that the political conquest of power, insofar as it is always prior to economic transformation, is more important than economic transformation itself. This very statement has also been the basis for the supposedly Marxian

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origins of Lenin’s focus on power and his quest for the “best organizational means to seize and conquer it.”

Questions can already be raised about whether or not the later Marx would still insist—as he did in 1844—on the absolute chronological priority of a political revolt over any sort of economic transformation, for Marx seems cognizant, even in 1844, that the “political act” is only a first step towards socialism and not socialism itself, and that “the aim and soul” of socialism is still an economic transformation. Guesswork aside, the contentious issue here is that this supposed priority in chronological order of a political revolt over an economic transformation has more often than not been interpreted as priority in order of necessity. In the Marxist theories of transformation of capitalism the focus has always been on political revolt and on the capture of the bourgeois state and its smashing. Consequently, economic transformation of the capitalist mode of production has received less attention. Moreover, since capitalism represents a fundamental separation of the producers from the means of production, the prioritizing of the political aspect of a revolution by making the subject of the revolution a political subject brings no fundamental change. In other words, neglecting economic transformation by prioritizing the political conquest of power seems to be a strategy that is anything but Marxian.

Textual evidence cited above certainly bears the claim that for Marx a revolution is a political act that will keep going on throughout the political transition period, all the while the period itself still suffers from class struggle and all the familiar ills that plague capitalism. At the same time, Marx also held that this political act in itself is not socialism. Rather, socialism begins only after the political act when material conditions for the new society are created. Marx opined

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38 Thomas (1994):131
so much, and the Marxist theory—if at all faithful to Marx (in theory if not in practice)—repeats this.

However, Marx also noted that once the economic organization begins, socialism throws away its political cover. Now, those who claim that the dictatorship of the proletariat means nothing other than a “workers’ state” interpret this as following: once capture of political power is successful and a workers’ state is installed, the taking off of the political cover of socialism means the same as the beginning of the withering away of the workers’ state. Such is the conception, for instance, in Lenin’s view of post-capitalist transformation: “Once we have overthrown the capitalists… and smashed the bureaucratic machine of the modern state, we shall have a splendidly equipped mechanism… which can very well be set going by the workers themselves, who will hire technicians, foremen, and accountants and pay them all workmen’s wags.”39 In part this is still in line with Marx (and Engels), but this was the Marx of 1847 who, writing the Communist Manifesto, thought that the proletariat “organized as a ruling class” would “use its political supremacy to wrest, by degrees, all capital from the bourgeoisie, to centralize all instruments of production in the hands of the State.”40 The origin of the idea that the future belongs to a state ruled by the working class evidently lies in this statement of Marx.

Throughout his work, beginning with his early overtly political writings down to his post-Paris Commune reflections, Marx also held that since capital “creates the subjective and objective conditions of its own negation and, simultaneously, the elements of the new society destined to supersede it”41 capitalism already in itself contains the antagonisms and contradictions that will bring about its own demise. Hence, capitalism itself is a transitional period on the way to socialism.

40 Marx, Manifesto of the Communist Party, in MECW 6:504.
The regeneration of new men and new social relations that is so crucial for a new society should begin in this transitional period, for it is no one but the self-emancipated people who are the “grave-diggers of capitalism.” It is a bad Marxist theory that interprets this set of grave-diggers as a revolutionarily conscious minority that has the license to rule and lead in the name of a majority and has the capability to oversee that much-awaited transformation of capitalism to socialism. In practice, as evident in the historical instance of the really (not)-existing socialism, there have consequently never existed Marx’s freely associated producers who have overcome the separation of men from the conditions of material wealth; all that was achieved was the nationalization of private property, and the people working for the state, still as wage laborers.

2. Marx after the Paris Commune

Marx lived long enough to experience the Paris Commune and noted that the Commune, without having a political party to its name, managed to seize for itself “the whole initiative hitherto exercised by the State” and in doing so forced the “old centralized government” to “give way to the self-government of the producers.”\(^4\)\(^2\) Hence, as opposed to previously existing governments that were repressive through and through, the Commune was “thoroughly expansive” and was “the political form at last discovered under which to work out the economical emancipation of labor.”\(^4\)\(^3\) As opposed to his own statements in the *Communist Manifesto*, Marx, in writing about the Commune notes that “the working class cannot simply lay hold of the ready-made State machinery and wield it for its own purposes”\(^4\)\(^4\) and that the purpose of the

Commune was not to perfect the State machinery but to eliminate the “deadening incubus”\textsuperscript{45} with the decentralized control of society by the regenerated new men who form the freely associated people. This, in the end, is nothing but the true example of “reabsorption of the State power by society”\textsuperscript{46} as opposed to being a new form of the state.

The Marx who once thought that the workers can capture and use the bourgeois state now had the opportunity to reflect on his previously envisioned future and thus no more mentions that the future belongs to a workers’ state. In fact, as noted above, since the aim of the Commune was to do away with the state altogether, Marx’s French edition of \textit{Capital} and his \textit{The Civil War in France} show his distrust that the “negation of the negation” can be done by a workers’ state. There certainly is, for Marx, a need for a proletarian dictatorship which is the rule of the majority. This much cannot be denied. But it is also clear that by a dictatorship of the proletariat he meant something other than the historical instance of the rule of a minority in the name of a majority.\textsuperscript{47} In fact, Marx never seems to have equated the Paris Commune itself to a dictatorship of the proletariat.\textsuperscript{48}

The point, however, stands that for Marx there is no state after smashing of the old state. If the Paris Commune is any guide—and Marx’s discussion of what the commune \textit{would have done} had it lasted longer than six weeks shows—it has to be a federation of communes. Marx is thus insistent that the commune is not a state. What follows from this discussion is that the conquest of political power does not imply a state: it implies a proletarian dictatorship, a rule of the majority, but it is not a centralized state. It just cannot be. It is one commune after another—or better put—

\textsuperscript{45} Marx, Drafts of \textit{The Civil War in France}, in MECW 22:484.
\textsuperscript{46} Marx, Drafts of \textit{The Civil War in France}, in MECW 22:487.
\textsuperscript{47} See Draper (1987) on the various possible meanings of the “dictatorship of the proletariat”.
\textsuperscript{48} Harding, quoted in Thomas 1994: 125.
a federation of communes together that will abolish the capitalist economy and dismantle its political structures.

3. Value production and political power

Putting aside for a moment the right or wrong guess about what Marx would—after the Paris Commune—have said about the Russian experience and the Soviet acceptance of his idea of a workers’ state, one can at the very least say that it was an extreme interpretation of Marx to hold that the conquest of political power from the bourgeoisie is always to be prioritized before an economic transformation is even attempted. In a letter to Friedrich Bolte written in 1871, Marx is at pains to emphasize that even though the conquest of political power is the final aim of political movements, the success of these political movements depends on “a previous organization of the working class, itself arising from their economic struggles.” To use Marx’s example, the struggle in each factory to force a shorter working day is a purely economic struggle. Struggles in every factory for shorter working day leads to a movement that pushes for a law, which is a political movement. In this sense, economic struggles begin before a general political revolt, and not the other way around. As Marx notes, “out of the separate economic movements of the workers there grows up everywhere a political movement, that is to say a movement of the class, with the object of achieving its interests in a general form, in a form possessing a general social force of compulsion” ⁴⁹ (original emphasis).

At another extreme, diametrically opposed to the power and state-fetishism and to the insistence that economic transformation comes only after a political revolt, is that economic transformation has not much to do with conquest of political power, and that the former can take

⁴⁹ Letter to Bolte, November 23, 1871.
place without the latter as a pre-condition. An example of this latter view is the concept of anti-power, put forward most famously by John Holloway in his *Change the World Without Taking Power* and later in his *Crack Capitalism*. Holloway’s general argument is that the power and state-fetishism evident in the experiences of the really (not)-existing socialism do nothing but reproduce the hierarchies that plague capitalism. In order to go beyond the same traps of the leader and the led and the owner and the owned that forms a capitalist economy, Holloway seeks to prioritize the importance of power-to against power-over. He is absolutely against even adopting the discourse of power, for if one does so then “the struggle against power is already lost.”

A broad conclusion, along this line of reasoning, is that we need to be “not just living despite capitalism but living in-against-and-beyond capitalism.” Revolution, defined this way, means working to build a new world, “a new commune-ism…in the interstices of and in opposition to capitalism.” To revolt would then mean to live like a misfit in the capitalist economy, to go the other way, and to seek to distance from everything that smells of capitalism.

But will such acts of defiance and dissent be sufficient to create a new world? Marx himself never failed to re-iterate that in order to create a new world, a different social relation, the workers themselves have to become “the grave-diggers of capitalism.” Would our everyday resistance against capitalism be enough to overcome the commodity fetishism that characterizes capitalism? Sure, if there is to be a new world, we need to behave in ways different from the ways behave when we form a part of the chain of capitalist production relations. But is there any way out of this capitalist mode of production except through negating capitalism by uprooting the value production that forms its backbone?

50 Holloway (2002).
51 Holloway (2005).
52 Ibid.
The gravity of the situation cannot be fully comprehended without understanding that the distinguishing feature of the capitalist mode of production is that labor exists as indirect social labor as opposed to labor being directly social. As opposed to pre-capitalism in which people are subject to personal dependence and where labor directly binds people, or as opposed to capitalism where people are bound “by the value form of mediation,” the new society that Marx envisioned is a society of freely associated producers where labor directly constitutes a part of total labor.

Thus, the only labor that features in value calculation in the capitalist mode of production is the labor that corresponds to the average socially necessary labor time needed to produce something. Since in this mode of production socially necessary labor time prevails over actual labor time, individual labor exists only “as a component part of the total labor” in capitalist production relations.

Value production, in this sense, is a cornerstone of the capitalist mode of production and hence will be present as long as there are no freely associated production relations that replace the capitalist mode. In such freely associated production relations, there is no distinction between concrete and abstract labor, i.e., the dual character of labor is eliminated. The abstract labor that forms the substance of value in the usual capitalist mode of production thus ceases to exist. In addition to this development, there will also no longer be exchange value which is the form of appearance of value in a capitalist mode of production.

With the disappearance of both abstract labor and exchange value, there will be no generalized commodity market in a post-capitalist economy: there will be no market in the sense that products of labor are not exchanged. There could be markets in another sense, just like there

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were markets before capitalism, but that is not the crucial point here: what is distinctive in a post-capitalist economy is that social provisioning is no longer defined or run by market transactions. Like Marx argued, Communism is the control of production by workers themselves, and, to this end, value production has to disappear if this Communism is “not to remain a sham and a snare.”

The question then is, to what extent does the establishment of the conditions of elimination of value production necessitate a prior conquest of political power by the working class? Will worker cooperatives, for instance, be sufficient to herald the new dawn? In conceiving of a post-capitalist/socialist/communist economy where producers are not haunted by an autonomous power existing from without, Marx writes favorably of worker cooperatives which, to him, represent a new production relation that overcomes the domination of labor in the hands of capital. However, for the workers to not “valorize their own labor” or to be reduced to “wanting capital without the capitalist” they cannot keep operating “as islands within a sea of value production” or continue to exist “in a context in which exchange value continues to govern the production and circulation of commodities.”

“Freedom” associated with the producers being in control of their products or with the escaping of the domination of capital over labor is not very emancipatory. The “freedom” associated with working as a wage-laborer for the state is less so. True freedom, for Marx, means being able to live a life that is not defined by labor. For him, this true freedom “really begins only when labor determined by necessity and external expediency ends” and lies in the “development of human powers as an end in itself.”

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57 Hudis (2011).
4. Conclusion

Marx himself was never in two minds about whether or not the state should necessarily persist until the new society is created. What seems unlikely, upon close reading of the post-Paris Commune writings of Marx, is that he was as enthusiastic about a workers’ state as he was when he wrote the *Communist Manifesto*. In his preface to the Russian edition of the Manifesto he insists on how the Russian communes cannot go directly from their then-present form to socialism without passing through a capitalist development phase. However, this only helps to strengthen the claim that Marx believed that the material advancement capitalism creates was needed and its own antagonisms it contains helpful in the struggle to overcome it and to herald a new society.

This fact, that capitalism itself is a transitional economy, is of prime importance. A better understanding of what Marx meant by this should have been sufficient to dispel any speculation, erroneous as they are, about the need for another transitional society that follows capitalism or about the need necessity for a proletarian dictatorship in the form of a workers’ state that would oversee the transformation, and bring about the regeneration of new men and new social relations, and uproot value production. The inquiry into two views about the transformation of capitalism into communism taken up in this paper has hinged on the understanding that reaffirming this insight of Marx can highlight the steps that need to be taken if that new society of his dreams are to be more than “a sham and a snare.”

Accordingly, what seems plausible, reading Marx and his views about post-capitalism, is that the neglect shown in both theory and practice when it comes to the issue of economic transformation of capitalism to socialism is due to not paying requisite attention to the later works of Marx, especially his revisions of Capital and his other works written after the Paris Commune.
At the same time, any insistence that resisting capitalism and trying to crack it by dissent and disengagement from capitalist social relations seem equally naïve. An economic transformation, and the uprooting of the mode of production and value production that it entails, cannot be done either purely through conquest of power and state control of the economy with the workers still stuck being wage-laborers, or purely by detaching ourselves from the struggle against capitalism by creating autonomous zones in the intricate network of capitalist social relations. A socialist theory and praxis should inform each other and political revolt and economic transformation need to be simultaneous, should begin during capitalism itself, and should take place both at the site of production and at distance from it. Additionally, since there is no science or revolutionary consciousness to be imported from without in a world where capital is spread throughout, the grave-diggers of capitalism can neither leave this capitalist town nor wait for a spade. The way out is to start digging, in whichever way possible, for the time to dig is now.

References


WTO: A Modern World Mafia?

By: Nicola Matthews

1. Introduction

The World Trade Organization's (WTO) website proclaims that it is a multifaceted organization which should be seen in a number of different ways, that is, it is an organization that liberalizes trade, it is a forum for governments to negotiate trade agreements, it is a place to settle disputes, it operates a system of trade rules, but, as the website reminds us, it is not superman and cannot solve, or for that matter cause all the world's problems! Quite the disclaimer. Evidently, the WTO feels it is necessary to recuse itself from targeted condemnation. Its defense is the claim of a large world; no international institution, given the size of the world, is capable of single handedly controlling it. Logically then, for those who see the WTO as a secretive but all powerful black box must simply be ignorant of its organization and policies (McGillivray, 2000, p.2).

59 See Understanding the WTO: Basics, What is the World Trade Organization, http://www.wto.org/english/thewto_e/whatis_e/tif_e/fact1_e.htm. It is interesting to note that the statement both professes to be the solution and the cause to world problems. Is this to be taken as a confession that the WTO does in fact, through it daily operations, cause harm in the world?
Now clearly no reasonable person would present such an argument—the world is large and is structured through hundreds of thousands of organizations. But just because this may be the case, it does not follow that a large international organization cannot be the cause of many problems throughout the world. This is made that more conspicuous when we take into account the dominance and prevalence of large multinational corporations. To argue that all one merely needs is a proper understanding of the WTO's operational framework is itself ill formed of human behavior and the structural characteristics of capitalism. The WTO, as will be shown, serves the interests of developed countries at the expense of developing ones. More specifically, it serves the interests of multinational corporations. From what begun as an agreement on trade has mutated into a global governance regime. Furthermore, it has been a silent coup over national government policies, over democracy and over civil interests as it requires that “each member shall ensure the conformity of its laws, regulations and administrative procedures with its obligations as provided in the annexed agreements” (Article XVI.4,).

The organization of this paper is as follows: section two will address the WTO's origin and structure, including its control mechanisms. Section three will discuss the role of the UN in relation to the WTO, some development theory, democracy and the implication it has on policy space. Finally, section four will contain the conclusion.

2. The WTO

Out of the aftermath of World War II, many countries entered into a series of negotiations to stabilize trade and international relations. The solution was to establish an International Trade Organization (ITO) capable of addressing multiple issues such as trade barriers, employment,
investment, restrictive business practices and commodity agreements. The ITO was to be incorporated into the United Nations (UN) and was the third pillar of the Bretton Woods system (the World Bank (WB) and International Monetary Fund (IMF) comprised the other two). However, the ITO treaty was not approved by a small number of countries including the United States. In its place and outside the purview of the UN, the General Agreement on Trade and Tariffs (GATT) was created. It would go into effect in 1948. Originally designed as a provisional agreement, the GATT would serve as the rules for international trade for the next 47 years. It would not be until the Uruguay Round (UR, 1986-1994) of Multilateral Trade Negotiations—launched in September 1986 at Punta del Este by a Declaration of Ministers—that a permanent set of rules were established. This round transformed the GATT into the World Trade Organization (WTO) becoming operational January 1, 1995.

The organization of the WTO is hierarchal with the Ministerial Conference (MC) its highest level body followed by the General Council (GC). The MC is required to meet every two years and represents the trade ministers of each member country. Day to day operations are run by the GC, which meets monthly in Geneva. Both the MC and the GC are comprised of member representatives. The GC however is tasked with two additional duties, one to monitor national trade policies under the Trade Policy Review Body (TPRB) and two, to meet under the Dispute Settlement Body (DSB) and administer the dispute process. Both TPRB and DSB were established in the Uruguay Round.

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61 See William Diebold (1952) for the dissolution of the ITO.
62 Reviews are done according to trade volume, the top four countries with the largest shares are reviewed every two years, the succeeding sixteen countries are reviewed every four years, while the remaining are reviewed every six years.
To date, since the new trade structure of the WTO went into effect, the MCs have met nine times. The two most significant meetings were the UR and its successor, the Doha Development Agenda round—currently still in negotiations. There were 18 major agreements to come out of the UR, yet generally they fell into handful of themes: (1) Privatize and commodify, (2) Deregulate, (3) Harmonize, (4) Liberalize investment, (5) Liberalize finance, (6) Managed trade (as opposed to free trade), (7) Create new property protections, and (8) Homogenize culture and consumer demands (Wallach, 2004, pp. 3-4). These new agreements would be the most expansionary set of rules in the history of the GATT. The WTO was no longer solely concerned with trade but with a whole new range of provisions. This expansive scope encompassed the service sectors, intellectual property rights (copyrights, trademarks, and patents) and international finance. In addition, it also produced a built-in agenda to be applied to the succeeding round that required further negotiations in agriculture as well as those listed above. Yet with the beginning of the Doha Round in 2001, the WTO would find itself in a storm of unanticipated disappointments and resentments on the part of developing nations. The gains that developing countries were guaranteed in the UR never came to fruition. The WTO today remains marred from this fallout as developing countries struggle for an equal voice within an international organization designed to benefit powerful nations and their corporations.

2.1 Mechanisms of Control

The existence of the WTO creates an international arena for corporations to bypass domestic laws and circumvent governments for their own gain. Technically, corporations do not

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63 More recently, the Ministerial Conference met in Bali, Indonesia from December 3 to December 7, 2013, where, for the first time, a trade facilitation agreement was reached. While this agreement reflects a move away from 18 years of contentious debate and an overall stalemate, it does little to address the most pressing issues that the UR and the Doha Development Agenda round have proposed.
have legal standing within the WTO yet there are countless corporate advisory bodies dispensing “expertise” to the delegates. “The delegates themselves are drawn from trade ministries and confer regularly with the corporate lobbyists and advisors who swarm the streets and offices of Geneva,” turning the WTO into what one Financial Times delegate called it: “a place where governments can collude against their citizens” (Frank, 2006, p. 106). Of course, those that stand to gain the most from such collusion are corporations. The general mechanism for which corporations achieve this, is the Dispute Settlement Body (DSB). In addition, solidification of corporate positions was further facilitated when the GATS, the TRIMS and the TRIPS (expanded upon below) were signed during the UR. In case after case, the WTO has consistently ruled that environmental, health and safety policies are illegal forms of trade barriers, i.e. bad for business. The weakening of the Clean Air Act and policies concerning the safety of dolphins are but two responses by the U.S. government to comply with WTO orders. In another case, the WTO would rule against the European Union ban on artificial hormones in beef, threatening human health. When the Bush Jr. administration blocked a WTO agreement that would have allowed least developed countries to import cheap, life saving drugs (under compulsory licenses), this was not done for the benefit of the U.S. citizens but for large pharmaceutical companies. The environment, human health and safety all play second fiddle to big business. In the WTO, big business found a mechanism to get around domestic laws for the purpose of expanding their bottom lines, that is, “global commerce takes precedence over everything—democracy, public health, equity, access to essential services, the environment, food safety and more” (Wallach, 64

WTO rules ban countries from differentiating products based on the tools and methods by which they were made. In the case of dolphin safety, the U.S.’s previous domestic laws banned the use drift-nets that ensnared dolphins and ultimately killed them. Threatened by Mexico to use the Dispute Settlement Body of the WTO, the U.S. government would lower their standards to conform to the international agreements.

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2004, p. 13). And as mentioned above, this has generally been accomplished through the DSB and the implementation of the GATS, the TRIMs and the TRIPS.

2.1.1 The Dispute Settlement Body—DSB

Advocates of the WTO portray the DSB as a mechanism for spreading democracy and assisting smaller countries in the face of larger state powers. The DSB’s own powers were greatly enhanced during the Uruguay Round in 1994 resulting in one of the most formidable enforcement procedures of any international agreement (Wallach, 2004a, p. 239). The grounds on which these new laws were created were to ensure more reliability and security for the global economic trading system. Thus, in order to avoid fluctuations in world trade, the “Dispute Settlement Understanding (DSU) discourages stalemate by not allowing parties to block decisions. It also establishes a standing Appellate Body, making the dispute settlement process more stable and predictable” (GAO, 2002, p. 45). However, major problems reside within the DSB, the most problematic is the role of sanctions as a method of penalty. Because there exists significant differences in trading volume between countries, asymmetries are prevalent among the large developed economies and the smaller developing ones. For instance, sanctions instituted by the U.S. or other large European countries against a small African nation would have a detrimental impact, on the other hand, if these sanctions were reversed it would have little if any effect on the larger trading nations. In addition, developing countries have encountered several other obstacles of working within the DSU: cost and access to the process, issues of implementation and compensation and the implementation of the provisions in regards to Special and Different Treatment in favor of developing countries (SouthCentre, 1999, p. 23).

Furthermore, after a tribunal rules on a case, a consensus is required to stop the sanction(s) from going forward (Wallach, 2004a, p. 240). If a consensus is not reached, no independent appeals
will be heard. There is no due process and no outside appeal. This binding enforcement dispute resolution places developing countries at a great disadvantage. And in contradistinction to its advocates, it in fact skirts democracy rather than promotes it by favoring developed nations.

2.1.2 GATS, TRIMs & TRIPS

Of all the agreements established in Marrakech, Morocco, as a result of the UR, three would go well beyond what was considered to be traditional trade. These three agreements, General Agreement on Trade and Services (GATS), the Trade Related Aspects of Intellectual Property Rights (TRIPS) and the Trade-Related Investment Measures (TRIMs), were perceived at the time of their implementation as highly contentious. They would expand the purview of trade to include almost all aspects of social life bringing them under the discipline of economic commerce. The GATS came into existence in 1995 to the chagrin of many developing countries and after vigorous lobbying by the U.S. (Madeley, 1993, pp. 71-72). The GATS is all encompassing and extends into regions not once recognized as trade policy. The GATS applies to most service sectors such as healthcare, postal services, education, water and sanitation as well as telecommunications, transport, insurance services and finance. For most critics, the contention resounds in the fact that many of these services, especially items like water, education, health care and security are seen as a global commons (Cavanagh, 2002, pp. 79-97). In other words, these services are a right and not a need. However, under the GATS agreement, services are rewritten in the converse language, i.e. as a need and not a right. What is more, there

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65 The then Director General of the WTO, Renato Ruggiero, would reference the impending controversies of the new GATS agreement: “[T]he GATS provides guarantees over a much wider field of regulation and law than the GATT; the right of establishment and the [obligations]...in all relevant areas of domestic regulation extend the reach of the Agreement into areas never before recognized as trade policy. I suspect that neither governments nor industries have yet appreciated the full scope of these guarantees or the full value of existing commitments” (Ruggiero, 1998).
are many rules that constrain governments from protecting these rights: (1) they are restrained
from setting limits on the number of service providers or the array of services in any one sector,
(2) there are restrictions on overall domestic regulation, (3) the regulations in place must have
the same impact on both domestic and foreign service providers, i.e. the conditions for
competition must be level and finally, (4) once a service sector has signed on to the GATS no
new government services or private not-for-profit monopolies may enter into operation without
reparation to other WTO members for abolishing competitive conditions (Wallach, 2004a, pp.
110-11).

The overall objective of the GATS has been to deregulate and privatize the service sector.
Although it does not specifically mandate this as such, it encourages it by locking in a countries'
path toward liberalization once they have become a member (Communications, 2001, para 8).
Signatory countries are under constant pressure to open services to multinational corporations
due to built-in negotiations; it is “by design, a formidable instrument to encourage and to
entrench privatization...[it] is, at root, hostile to public services. It treats them, at best, as missed
commercial opportunities and, at worst, as unfair competition or barriers to entry for foreign
services and suppliers” (Sinclair, 2002, p.75).

Like the GATS, the TRIPS would be just as contentious if not more so. Its passage as an
agreement in the WTO would be the end result of a massive push on the part of large
multinational pharmaceutical and information technology corporations (U.S. dominated) alleging
intellectual property theft (Jawara, 2004, p. 36). Needless to say, there is a wide-range of issues
associated with the TRIPS. These span from exorbitant pricing on medical supplies, the
promotion of biopiracy, barriers to technological transfers and the encouragement of monopolies
and anti-competitive practices—almost all of which are consequences of the 20-year patent term
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(Khor, 2002, para 9). Yet the more pressing and fundamental issue is “whether intellectual property, which is basically a device that enables monopoly and anti-competitive practices, should even be located within a trade organisation whose purpose is supposed to be the promotion of free trade and competitive practices; and if not, then what to do about it. Moreover whilst the WTO is supposed to be based on the principle of reciprocal benefits, TRIPS has proven to be inherently and in practice very imbalanced, as developed countries...have reaped the overwhelming share of benefits amounting to large values, whilst developing countries are carrying the heavy burden of costs” (Khor, 2002, para 9).

The development of the TRIMs was also promoted by the U.S. and its corporate interests as well as the interests of other developed countries. Initially, ministers from a handful of wealthy countries assembled in 1997 to form a Multilateral Agreement on Investment (MAI) for international investors but when this was met with stiff resistance, they would rely on the WTO to implement their agenda (Frank, 2006, p. 102). The TRIMS is designed to curb a countries’ ability to form their own domestic policies in regards to foreign investment and force governments into compensating corporations in the event that these policies change. Under this agreement, developing countries continue to face capital flight as well as competitive conditions for infant industries.

3. Repercussions for Developing Countries

3.1 The United Nations & Early Development Theory

The GATT and subsequently, the WTO, was not the only institution to be created from the aftermath of WWII. The United Nations (formally the League of Nations), the World Bank (formally the International Bank for Reconstruction and Development) and the International
Monetary Fund (IMF) were all created ostensibly to bring international peace and development to countries worldwide. The UN in particular originally intended for economic development to be at the center of its policies. As decreed by Article 55 of the UN charter, the UN was to promote full employment, higher standards of living and economic and social progress and development. The objective of the UN—international economic cooperation—was to be realized through a non-discriminatory and multilateral approach with all members on an equal footing (Toye, 2004, p. 27). Yet development theory and thus economic growth was still inchoate during this period and therefore theories of international commerce were resolved to rely upon the ideas underscored by orthodox Ricardian trade theory. This trade theory postulated that the promotion of unrestricted trade permits countries to specialize in the production of commodities for which they can produce at the lowest real cost relative to other countries and ergo allows all to benefit.  

This standard and conventional approach was to impose freer trade and enlist the fortune of comparative advantage. It was, and is a “one size fits all” theory for prosperity.

However, early development theorists, many of whom would work in the UN or the World Bank, would reject this form of monoeconomics and in fact would argue that free trade actually obstructs development. In 1943, Paul Rosenstein-Rodan, one such development theorist, would advocate for a governmental and finance led change in the overall institutional framework, known as the “big push” policy. To increase industrialization and to create employment for the excess agrarian population, resources and financing for industrial investment were to be employed on a large scale (Rosenstein-Rodan, 1943). Raul Prebisch, an Argentinean economist, formulated a model that partitioned the world economies into a center-periphery

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66 It must be noted that free trade theory requires some stringent assumptions such as full employment and equal access to the same technology. See Robinson (1979).
67 The term monoeconomics was originally coined in Essays in Trespassing by Albert Hirschman (1981).
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construct; the center economies, US and Europe, dominated the peripheral ones, Latin America, Africa and Asia (Marco, 1972, pp. 3-13). It was the very nature of the position of a peripheral country relative to a center country that was the determinant in the lack of progress (Peet and Hartwick, 1999, p. 42). The center-periphery theory maintains that it makes a difference if a center already exists when a peripheral country begins to develop. Prebisch would argue that technological advances accrued solely to the center countries; hence, impediments to development were structural in nature. Two of the more fundamental determinants that created these impediments and proliferated international inequality where inelastic demand for primary products (for which developing countries saw declining terms in trade), and monopolies in manufactured markets but competitive markets for primary products (Brid and Caldentey, 2010, p. 399). To counter these impediments, peripheral countries needed structural change—rather than emphasizing primary exports as an engine for industrialization, they should focus on import substitution strategies and capital accumulation. Free trade and the market was, to say the least, seen as highly deficient in respect to industrialization.

Gunnar Myrdal, would expand upon these concepts; development, as defined, should be comprehensive and include elements outside the narrow economic domain, that is, development is a “movement upward of the entire social system...[t]his social system encloses, besides the so-called economic factors, all noneconomic factors (1974, p. 729). Moreover, economies were not equilibrating but rather where in states of perpetual cumulative change—“economic development is a process of circular and cumulative causation which tends to award its favours to those who are already well endowed and even to thwart the efforts of those who happen to live in regions that are lagging behind” (Myrdal, 1964, p. 345). In other words, a “virtuous circle” of development existed as a structural property in the developed countries whereas a “vicious
circle” of poverty existed in the developing countries. Other early development economists, such as Albert Hirschman (1960) and Ragnar Nurkse (1958) would argue for unbalanced and balanced growth respectively. Nurkse, in particular would stress the role of demand or lack thereof in the developing countries. These countries were not resource nor savings nor foreign exchange constrained but were constrained by the inelasticity of demand at low real income levels. What these countries faced therefore was an employment constraint that could only be remedied through a national planning agency.

The UN, for its part, would convene a new Conference on Trade and Development (UNCTAD) in 1964 that would focus on issues of trade, finance and development. Within the UNCTAD, developing countries would call for a New International Economic Order (NIEO) that demanded more advantageous terms of trade for primary commodities. Yet, despite these measures and the work of the early development economists, the UN would effectively become marginalized on these matters by the beginning of the 1980s. This would be due in large part to a handful of phenomena—the Vietnam war and its repercussions, the eventual disintegration of the Bretton Woods system, the oil induced inflation and the sharp change in the political and ideological ethos of the developed countries (Toye, 2004, pp. 3-4). Most significant among them however was the shift in the political climate towards the conservative right that would drive OECD (Organization for Economic Co-operation and Development, i.e., developed nations) countries to pursue their own economic interests without recourse to the consequences of the developing ones. The UN would not be one of the institutions facilitating this change, instead

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68 Hirschman in particular would argue that the “big push” balanced growth model is in fact not a theory of development because “development presumably means the process of change of one type of economy into some other more advanced type. But such a process is given as hopeless by the balanced growth theory which finds it difficult to visualize how the “underdevelopment equilibrium” can be broken into at any one point (emphasis in the original) (1960, pp. 51-52).
the OECD countries, and in particular the U.S., would employ the IMF, the World Bank and the newly created WTO to obtain their ends. It is of little wonder why the U.S. and other OECD countries would turn away from the UN—they had lost control over its functioning as well as the moral authority as a guiding principle. As Prebisch (1971) would note, developing countries were gaining in both these spheres within the UN:

With regard to external factors that cramp development...controversy is already bearing fruit. Ideas which were considered inadmissible until only a short time ago are now infiltrating into circles where they used to be labeled unrealistic, if not flagrantly irresponsible. Such ideas...were crystallized in the [UNCTAD], and are now among the many important concepts and recommendations embodied in the Pearson Report. Thus they are endorsed by the moral authority and intellectual prestige of the Report's authors...(p.8).

This North-South dialog would be effectively broken in October 1981 when Margaret Thatcher insisted that the WB and the IMF not be underfoot of the UN (Toye, 2004, p. 257). And the WTO would come to play a monumental role in minimizing the UN and in spoiling early development nations as well as development theorists' plans to realign the economic powers. Through its hierarchal organization, its Green Rooms and through the strong-arm of developed countries, it would co-opt democracy and obstruct government sovereignty in the interest of expanding global corporate dominance.

3.2 Democracy at the WTO

*The WTO is no would-be tyrant. It is democratic to a fault and has few powers of its own—The Economist*

*September 27, 2001*
Technically, the WTO’s decision-making process is dependent upon all members, that is, it is determined by consensus. The reliance on consensus is a remnant from the GATT. Signatory countries therefore have, in principle, equal voting rights. However, in practice this is far from the reality. What is more, consensus was never fully defined, either in the GATT nor the WTO, thus in diplomatic practice, where there is extensive use of “Green Rooms,” it is considered as the “absence of dissent” which is quite distinct from a practice of unanimity (Jones, 2010, p. 86). Invitation only Green Rooms that make vital decisions and establish trade talk agendas are predominantly represented by the “Quad” or “Quartet”—U.S., Canada, the EU and Japan. Although developing countries will occasionally be invited to participate, contingent upon the relevant issues, they are regularly absent. And despite the fact that Green Rooms are informal arrangements, they manifest, in part, officialdom and credibility (Jones, 2010, p. 88). The Green Rooms effectively exclude developing nations from shaping the agenda, once the declaration is drafted, they are left with but two options, agree or block the already, predetermined set of proposals.

This structure effectively excludes the majority from influencing the international trade agenda. Throughout the negotiations and even within the Green Rooms itself, developing countries, due to their dependence upon international aid, unsurprisingly are reluctant to object to the declaration because they are more often than not beholden to the Quad and fearful of financial ramifications. The outcome of such institutional arrangements is the curtail of democracy and the undermining of developing nations.

3.3 Developing Countries, Policy Space & the WTO

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International trade agreements and policies are not just high-minded protocols but have real world effects, particularly on developing countries. In the bureaucratese and jargon of international trade we must always be reminded that there are actual livelihoods at stake. One agreement that affects this directly is the Agreement on Agriculture (AoA). The AoA was negotiated in the UR and accepted by many developing countries under the pretense that the developed countries would liberalize their agriculture and textile markets. Needless to say, OECD countries have found ways to sidestep these by creating loopholes that circumvent the liberalization of their agriculture and textile markets. Consequently, “OECD countries agricultural subsidies and dumping (the sale of products below the real cost of production) have been legitimized rather than legalized, and have increased rather than decreased, since the Uruguay Round” (Jawara, 2004, p. 27).

On the whole, the AoA puts developing countries at a disadvantage because they are forced to compete with large-scale industrialized agribusinesses of the North which can produce at cheaper costs due to its advanced technological abilities. The Indian wheat economy of is one example where livelihoods are threatened. The agribusiness corporations, such as Cargill and Archer Daniels Midland, have declared the wheat crop of India to be undeveloped and decentralized and hence in dire need of development. Though it was claimed in an industry report, entitled Faida, that such development by industrialized global corporations would bring five million jobs, it is well known that corporations with economies of scale and advanced technology in effect displace labor.69 The impact on the livelihoods of Indians if full-scale development is undertaken in the wheat economy alone could reach over one hundred million people once forward and backward linkages are taken into account (Shiva, 2000, p. 103).

69 The Faida (meaning plentiful or profitable) report was put out by CII & Company in 1998.
Developing countries have been adverse to the WTO trade agreements on many grounds; arguing against a “one size fits all” approach and underlining imbalances in competitive cultures, imbalances in institutional capacity and above all imbalances in technology and competitive conditions (Jawara, 2004, p. 241).

The WTO also inhibits countries abilities to enact development strategies. Much of the development theory that was advanced by economists and scholars in the UN and the World Bank, as well as those that would come after them, would be of little use if those strategies fell under the legal domain of the WTO. And not surprisingly, the three agreements listed above, the GATS, the TRIMs and the TRIPS all circumscribe a country's ability to pursue certain development strategies. If a country's strategy is to limit capital flows and create capital controls, they will have a difficult time pursuing this path do to these three agreements. “Indeed the very purpose of the GATS, TRIMs and TRIPS agreements was to protect U.S. investment overseas...” (Wallach, 2004a, p. 151). Yet again, developing countries hands are tied in the type of strategies they can undertake as a result of large multinational corporations and their governments.

Even still, there remains another considerable problem for both developing and developed countries alike—the diminishment of governmental policy space in the face of WTO agreements. When the U.S. congress passed the Uruguay Round Implementing Act in 1994, it was required to alter over one hundred pages in its effort to conform to the latest laws (Wallach, 2004a, p. 5). Domestic policy in many cases has become hostage to international trade agreements. For those least developed countries where food security can be disrupted by natural disasters it is a necessity, in this context, for their governments to have flexibility. If we re-evaluate and re-examine the role of WTO and the GATT before it, it becomes evident that it is
substantially a mechanism for multinational corporations. It “has never been an institution designed to bring about free trade. It has always been, for the leading industrial states at least, about protecting declining industries for as long as possible (the history of textiles and clothing and of agriculture in the GATT provide ample examples) while pressing for market openings in areas of growing economic strength—that is, it has always been a machinery for gaining trade advantages” (Wilkinson, 2012, p. 400). And those advantages accrue to multinational corporations not necessarily to individual countries in themselves. When Robert Lighthizer (2007), a trade lawyer and once deputy trade representative testified before Congress in 2007, albeit heavily biased towards U.S. interests, that “[r]ogue WTO panel and Appellate Body decisions have consistently undermined U.S. interests by inventing new legal requirements that were never agreed to by the United States...The result has been a loss of sovereignty for the United States in its ability to enact and enforce laws for the benefit of the American people and American businesses. The WTO has increasingly seen fit to sit in judgment of almost every kind of sovereign act, including U.S. tax policy, foreign policy, environmental measures, and public morals, to name a few,” he is identifying that government, citizens and varying business are not the institutional victors of the WTO process.

What is even more worrisome has been the WTO’s engagement in widening its authority over governments and citizens. To quote at length Ian Fletcher (2010):

The WTO's tendency is to expand over time on two separate tracks. Track one, for those powerless to resist its dictates (or foolish enough to actually believe in them), consists in ever-more-rigid rules, of ever greater scope, designed to usher in a borderless world economy, at least on paper. Its ultimate ambition has been described as `writing the constitution of a single global economy.' Track two, for nations shrewd enough to practice mercantilism while preaching free trade, is a puppet show designed to square these nations' policies with the legal framework that
props open their foreign markets. Since this puppet show furthers both the power of the bureaucrats and the profits of the corporations, neither has any reason to announce public what both know perfectly well: free trade is largely a charade, the real meaning of which is well understood by those in the know but differs markedly from the literal meaning of the phrase (p.175).

By and large, the WTO, for all intents and purposes, operates as a global financial governance regime. Moreover, it operates as the behest of multinational corporations to the detriment of governments and citizens.

4. Conclusion

In a December 2011 letter to Professor. de Schutter, the Director General of the WTO, Pascal Lamy roundly disagrees with the professor on whether more trade is in fact desirable for food security: “I fundamentally disagree with your assertion that countries need to limit reliance on international trade to achieve food security objectives.”70 Why does Mr. Lamy and many others of his ilk, believe more increases in trade will solve this problem when, arguably the world is more liberalized in trade today than it has ever been (with the possible exception of the late nineteenth century early twentieth) and our advances in technology have increased food yields around the world? Although a partial explanation can be found in his institutional commitments and identification with the WTO, another reason can be found in is his failure (or possibly a turning of a blind eye?), of a proper conception of the capitalist structure. Corporations undertake production, not for the sake of people but for profit. As history continues to informs us, corporations will go to almost any end to gain advantage over

competitors and to increase their profit margins. If people happen to be a casualty of this process, it is of little concern to the corporation. This is especially so when those people happen to be halfway around the world, with little resources and very little power. The WTO has thus far been a great boon for multinational corporations. And they have used it much like a weapon, that is, they “use the threat of the WTO to roll back, block or chill countless rules designed to benefit workers, consumers and the environment and to promote human rights and development in the world's poor countries” (Wallach, 2004, p. 13). Some have called the WTO a Trojan horse for economic planning to the impairment of developing countries and citizens around the world. In many ways this is an accurate metaphor but it is not complete because the WTO also appears to have many traits similar to that of a Mafia. Mafias are typically seen as a centralized juridical organization which believes itself to be the sole arbiter of all conflicts and imbued with a set of institutional symbols and codes. It is an industry of violence, criminality and economic enterprise. Their ends are personal gain at any expense. Clearly too many parallels to take lightly.

References


13 Bankers: The Wall Street Takeover and the Next Financial Meltdown

By: Joyce Medeiros

Introduction

Simon Johnson and James Kwak depict many untold realities of the American financial structure in their book 13 Bankers: The Wall Street Takeover and the Next Financial Meltdown. The authors' analysis is focused on the housing crisis of 2007-2008, which compelled the 13 most influential financial leaders to assemble at the White House in early 2009. Their conversation addressed the topic of crisis and a solution to bankruptcy. Since financial institutions are the powerhouses of the economy, their failure would lead to economic disruption of unprecedented and inestimable proportion. To prevent such a dimensional crisis, the government felt it was its duty to save the big banks at any costs. In a moment of high tension, Obama’s administration worked to maintain bankers in his favor. The opportunity to seize and reform the banking industry to prevent future crises was overlooked and nothing was done. Subsequently, the financial institutions that were “saved” reported more earnings than ever before and as a result became even more powerful. Johnson and Kwak emphasize the size of the financial sector in the U.S and its robust lobbying power, which has resulted in enormous political influence and created a quasi-oligarchy. Prior to 2008, the key leaders within the Federal Reserve and the government presented a certain bias in favor of large banks, as many were previously employed by those institutions. Johnson and Kwak characterize the financial
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system as pervasive and distorted and illustrate the manner in which the government has encouraged it to be involved in politics throughout the years. The financial system’s involvement in politics has compromised democracy and the rights of taxpayers. The financial crisis has proven to be a political economy crisis and exposed the fact that without immediate reform, the next financial crisis will be even more severe.

**Historical Analysis**

Banks have historically shared a conflicting position in the foundation of the U.S. Thomas Jefferson and Alexander Hamilton had opposing views on the economic groundwork of a democracy. Hamilton believed that without government to support economic development, the U.S would not achieve its potential of becoming a prosperous and highly entrepreneurial nation. Jefferson foreshadowed a different problem as he rejected the idea of a national bank. Jefferson feared that private institutions could gain disproportionate influence over the government by “creating and managing the supply of credit,” which “could give them both economic and political power.” (Johnson and Kwak, 2010; p 17) In the end, it was Hamilton’s view that prevailed and he established the first national bank to stabilize the financial system through severe business cycles. It was proven, however, to raise inequality as it benefitted investors at the expense of the majority of the citizens when the first economic panic occurred. Hamilton was correct that a national bank could make a nation more prosperous. It would take economic expansion and industrial growth in the U.S to illustrate an innovative economic strategy compared to England. President Jackson later acknowledged Jefferson’s rejection of a national bank by stating that the “enemies of today are the forces of privilege and greed within our own borders.” (Johnson and Kwak, 2010; p 34) Although throughout the 19th century the U.S developed a well-functioning financial system, Jefferson’s fears would soon become apparent.

Innovation was the dominant economic philosophy of 19th century America and as a decentralized financial system took hold, America became a great place for the expansion of business interests and the creation of wealth. Industrialization and new technologies allowed the U.S to reach new heights. J.P Morgan, the largest financial institution at the time, had a central role in the growth of the industrial sector due to it holding an extraordinary share of the money flowing in the American economy. In efforts to battle monopolization in the economy, the
government imposed new regulations to improve the supervision of large corporations. (Johnson and Kwak, 2010; p 25) The policies adapted in the 19th century, however, were blunted by the influence of the financial sector. It was also during the 19th century that the first economic crises occurred. The Federal Reserve (“the Fed”) was created in 1913 but it allowed banks to participate in risky lending and generate huge economic booms. (Federal Reserve Education) At the time, the Fed was still too small to bail out institutions and did not have any restrictions on banks. During the early 20th century, an unregulated stock market boomed throughout the “roaring 20’s” with the expectation of “permanent prosperity” and endless optimism. (The Crash of 1929) At the time, investment banks and firms loosely sold and traded securities in an unregulated market while a series of significant deregulation took place, making financial speculation exorbitant. The sharp crash of 1929, however, brought an important regulation: The Glass-Steagall Act of 1933, which separated commercial and investment banks to prevent possible damage caused by risky trading with the public’s money. As a result, J.P Morgan, the finance giant, was forced to create an investment division, which became Morgan Stanley. After The Glass-Steagall Act, banks gained government protection in exchange for strict regulation. The financial stability brought by this crucial regulation has brought peace of mind and steady growth to the U.S economy. That is, until very recently.

The U.S economy has indeed grown to become one of the most robust and confident in the world. The regulations of the 1930’s, prompted by the Great Depression, protected the economy from becoming too concentrated. Growth during the period of 1945 to 1973, commonly known as the Golden Age, was led by a combination of technology, productivity, and consumption. In addition, the highest capital investments were made at this time and they did not result in “massive debt-fueled booms ending in spectacular crashes.” (Johnson and Kwak, 2010; p 37) However, by the 1990’s, it had been as if all the lessons learned from the Great Depression had been forgotten. Economic leaders were fearful of conservative regulations and criticized them for being a potential threat that could eventually lead to emerging markets surpassing the U.S. economy. This new ideology led to strong beliefs in favor of proposing looser banking regulations. Economists and government officials at the time assumed the U.S was immune to the financial problems present in emerging markets and as a result thought it was time to deregulate in order to spur innovation.
Wall Street has become a mere tourist attraction, as big banks are now located throughout the country, exposing a ravishing craving to become the next dominate money machine. The growth of the financial sector in the last 30 years has been overwhelming when compared to any other sector. With its increasing size and value comes a concentration of power and ability to influence the political system. Through constant deregulation the financial sector has reached a frightening record size. Between 1978 and 2007, the financial sector grew 3.5 percent of the economy (measured by contribution to GDP) and the financial sector’s profits grew by 800%.. (Johnson and Kwak, 2010; p 60) In addition, the sizes of “assets held by commercial banks, securities firms, and the securitizations they created grew from 55% of GDP to 95%.”(Johnson and Kwak, 2010; p 85) The growth was even faster for larger banks that diversified portfolios by taking on risk and highly leveraging the company. In “1978, all commercial banks together held $1.2 trillion in assets, equivalent to 53% of U.S. GDP. By the end of 2007, the commercial banking sector had grown to $11.8 trillion in assets, or 84% of U.S. GDP.” (Johnson and Kwak, 2010; p 59) Not only have banks become larger but they also hold most of the debt issued in the economy, growing from “$2.9 trillion, or 125% of GDP, in 1978 to over $36 trillion, or 259% of GDP, in 2007.” (Johnson and Kwak, 2010; p 59) The divide is now no longer between commercial and investment banks, it is between banks and megabanks.

Alan Greenspan, the chairman of the Fed from 1987 to 2006, admired financial innovation during his term, particularly that which was successfully carried out without government intervention. Greenspan is a libertarian and conservative who believes in a “laissez-faire” market approach, a world without government regulation. He is still an influential economic leader and a keynote speaker for the deregulation of the banking industry. Under Greenspan, the Fed’s deregulation policy led to immeasurable growth within the financial sector. Through the 1990’s a complete dismantle of the regulatory system had taken place. First, The Riegle-Neal Act of 1994 eliminated restrictions on interstate banking, allowing banks to expand across state borders and participate in mergers and acquisitions. (Johnson and Kwak, 2010; p 84) The Gramm-Leach-Bailey Act of 1999 was the demise of The Glass-Steagall Act, and allowed holding companies to own subsidiaries operating commercial and investment banks and even insurance companies. (Johnson and Kwak, 2010; p 92) Such policies led to the growth and
Oeconomicus

expansion of the larger banks. The predominant economic theories of the time also supported Greenspan’s deregulation. The "Efficient Market Hypothesis" by Nobel Prize Laureate Eugene Fama acted as an endorsement to the non-intervention of the Fed. Fama and Greenspan believed prices to be a function led by market power and explained this through mathematical modeling. (Johnson and Kwak, 2010; p 102) Greenspan thus achieved the freedom that allowed financial institutions to grow and the innovations that followed led to greater economic gains.

The economy during Greenspan’s tenure was unstable but this was concealed by a period of technological innovation that led to heightened prosperity and commercial activity. Meanwhile, the stock market was heading towards the height of an economic bubble. The impact of this crisis would cause the demise of large corporations and expose the weaknesses of the financial sector. The first corporation considered “too big to fail” was the large financial institution Long Term Capital Management (LTCM), which became insolvent and illustrated the risks within the derivatives market. In response, the Fed bailed out LTCM to ease the impact of its bankruptcy on the market and derivatives continued unregulated. (Johnson and Kwak, 2010; p 148) Knowing that the government would bail out such “too big to fail” financial institutions placed investors and bankers in an optimistic position; which led to greater speculation and risk-taking.

The Financial Crisis

Financial innovation soon took shape as complex securities and derivatives. To government such addition appeared relatively attractive as it could help the low and middle class citizens achieve the American dream of homeownership. Economist Hyman Minksy, had explain in his essays that financial innovation was an enabler to increase the profits of the financial sector, however it would come simultaneously attached to the risk that could also destabilizes the economy. (Johnson and Kwak, 2010; p 108) The government under Bill Clinton’s administration supported homeownership and sought to increase its rate of 65%, which later peaked at 69% under George W. Bush’s administration. (Johnson and Kwak, 2010; p 112) In order to increase homeownership, the government mandated Fannie Mae and Freddie Mac to provide many additional mortgages, leading to a highly leveraged firm. As a result, larger banks saw an opportunity to profit and developed “subprime” mortgage lending. Sub-primers were the riskiest
loans based on the ability of the borrower to repay the debt, encompassing those with poor credit and a history of bankruptcy. Since the Fed kept interest rates historically low from 2001-2005, borrowing money was cheap and this was a great opportunity for consumers. Buying a home became more attainable which led to an increasing demand and also escalating prices. The misallocation of cheap loans provided by the Fed, speculated a new bubble..

In order to keep the risk off the balance sheet, banks created a system of packaging loans and selling them in the market as mortgage backed securities (MBS). Not only were the MBSs speculated, their actual risk was unknown since respectable credit rating agencies gave them the safest risk rating of AAA. “Housing was not only a bubble made possible by cheap money, aggressive risk-taking, and structured finance…there were able to use commercial mortgage-backed securities to unload large, risky loans they were making. There was a boom in takeovers of companies by private equity firms, again made possible by cheap loans advanced by banks and then syndicated group of investors or used as raw material for new structured products.” (Johnson and Kwak, 2010; p 129) The bubble eventually burst as many had predicted. Between 1998 and 2005, the number of subprime loans tripled, and the number that was securitized increased by 600%. (Johnson and Kwak, 2010; p 132) As any bubble, rising housing prices attracted its’ own momentum and therefore speculation occurred naturally. Minskyian theory explains the development of speculative finance transforming into a higher risk named Ponzi finance, which is always followed by the downfall of finance.

The lack of government regulation of derivatives was predicted to lead an irresponsible speculation of MBS. Brooksley Born, the chairperson of the Commodities Futures Trading Commission (CFTC), predicted the trouble ahead and advised the government to regulate the derivatives market. Born understood the nature of the hazard, however, Congress was persuaded to deregulate and would not consider pleas for the regulation of derivatives. (Johnson and Kwak, 2010; p 136) The existing regulations were flawed and allowed exploitation by the banks. Regulatory capital requirements were constantly distorted by financial innovations and arbitrage. Banks felt it was not necessary to follow the capital requirement and over-leveraged in risk taking. In addition, all risks were falsely labeled because there is an inherent conflict on interest within the system since banks are the customers of credit rating agencies. This of course provides credit rating agencies with little incentive to diligently rate securities. (Johnson and Kwak, 2010;
Some companies even went as far as modifying their models and firing those who questioned the arrangement of the derivatives.

Deregulation also left consumers unprotected from predatory loans and abusive lending practices. Low income and minority communities were specifically targeted for subprime mortgages. Congress also increased the demand for subprime loans by increasing Fannie Mae and Freddie Mac’s ability to borrow cheaply and abundantly. Fannie and Freddie created demand for the most aggressive subprime mortgages in the market, all of which were also rated AAA. (Johnson and Kwak, 2010; p 142) In late 2003, in the face of the expansion of mortgages, New Jersey, North Carolina and Georgia limited some of the sub-prime activity and abuse within their states. Any larger investigation and reform of the mortgage market was simply dismissed by Greenspan, who described it as “healthy financial innovation.” (Johnson and Kwak, 2010; p 142)

In early 2007, economic pressures caused homeowners to become unable to meet their mortgage payments. Without the continued ability to refinance, the mortgage bubble slowly started to deflate. Assets based on housing values soon began to lose value, depreciating enough to distress the entire global financial system. At the height of the crash, in late 2008, Treasury Secretary Henry Paulson met with the head of nine major Wall Street banks—Bank of America, BNY Mellon, Citigroup, Goldman Sachs, JPMorgan Chase, Merrill Lynch, Morgan Stanley, State Street and Wells Fargo to make a deal that was “too good to pass”. (Johnson and Kwak, 2010; p 153) On that day, a total of $125 billion from Obama’s Troubled Asset Relief Program (TARP) was used to buy toxic assets which projected to relieve the breakdown. However, this preliminary action would not be enough to contain the crisis or repair the behavior of Wall Street. Banks had become too big to fail and if they did not receive massive government aid the entire economy would be in desperate shock. The stock market had already taken a loss and there was near total freeze of the credit markets. Global markets had also partaken in the same financial activity and without other governments saving its banks a major crisis would not be contained. Each of the banks was told to sell shares to the government and allowed to borrow well below market value at a rate of 5 percent. The U.S. government did not set up any restrictions that would limit the use or direction of its loans to the big banks. Instead, the government would only intervene if the banks failed to pay its dividends six times, which allowed the government to select new directors. (Johnson and Kwak, 2010; p 154) Cheap money was essentially handed to the largest nine banks that had caused the financial crises through
immensely irresponsible risk taking. The financial crisis brought to fruition Thomas Jefferson’s fear of the concentration of power by financial institutions.

After the collapse of Lehman Brothers in 2008, it became evident the U.S could not support another failure of such dimension. The U.S chose to increase the capitalization margin of the banks in exchange for preferred shares. “Putting government money into some banks is standard practice in emerging market financial crises, but money typically comes with strict conditions in order to begin the reform process.” (Johnson and Kwak, 2010; p 168) The U.S government, however, did not impose any conditions fearing that banks would not participate. Instead, the government offered great rates that benefited shareholders but not tax payers. The government had considerable power to dictate the terms of bailout contracts but did not. When the Swedish economy was confronted with insolvent banks their government imposed nationalization of insolvent major financial institutions. Under the Swedish bailout all of the top management was replaced and the bank ran as a government institution until it was able to maintain itself. This was a policy the U.S highly recommended to emerging markets in the 1990s but it did not consider this policy during its own crisis. The financial system was allowed to operate in the same fashion and the financial institutions that survived thrived on the back of cheaply borrowed government money and a decrease in competition.

**Conclusion**

The U.S missed an opportunity to reign in the financial system once and for all. Even the biggest supporter of free markets, Alan Greenspan agreed that “If they’re too big to fail, they’re too big.” (Johnson and Kwak, 2010; p 189) The amount of collateral damage in each bank’s balance sheet created an obligation to other institutions, therefore deeming failure could mean all or none. In addition to being so interconnected, a global domino effect would spread and other separated industries would also suffer as they often rely on financial products for daily business procedures. The last few years have proven that our financial sector has had too much involvement in the political system, creating serious risks to the economic interests of the country. The liberties allowed the financial sector have caused irresponsible trade activity and giant market speculations. A middle ground could have been achieved during the bailout by firing the CEOs and top officers of the major banks and increasing regulations. Threats also
leaked to consumers, whom were not protected by any regulation in the market, therefore the impact of more banks becoming insolvent would negatively impact the lives of many more citizens. In addition, the U.S. government did not act in the interest of the taxpayers but of the wealthiest 1% of the population. After the crises, enormous growth has presided over the six largest financial institutions and this has directly corresponded with their increase in political power towards becoming a quasi-oligarchy. While regulations can impose some barriers to banks, a decreased political presence is also necessary. This reform starts by the government dismantling large financial institutions and creating smaller institutions. This creates more competition and less risk for the government. Just like Thomas Jefferson believed that American prosperity was not meant to be built by banks but by the people, government leaders must be strong and fight against the concentrated power of large financial institutions that threatens democracy and the rights of taxpayers.

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