Capitalism in India

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Abstract

We work with the tradition in Marxian scholarship that develops Hegel's Logic in Marx's political economy. Accordingly, exchange, through the circulation of money, is accorded pride of place. The modern phenomenon of 'financialization' can be analysed as short circuiting the monetary circuit. We appraise Indian capitalism in this light through a polemic against the so-called Raghuram Rajan Committee Report on Financial Sector Reforms, 2008.

The virtuous circuit

Scholarship on dialectical materialism is vibrant with books and a dedicated journal. For ease of exposition and, we believe, no loss of generality we work with a classic by Chris Arthur, 2013. A general characterisation of systematic dialectic would not be different from an open systems perspective in philosophy. It signifies a modus of working with categories that keeps them open-ended, yet structurally connected (Arthur, 2013, p. 5). In practice, concepts emerge in sequence. However, the ordering is not linear because neither are the initial nor the terminal conditions given. Epistemologically, it champions the reflexivity of the subject-object connection (Smith, 2009). Where only the former is present, there might be causal relations but no dialectical relations. With Ricardo, in contrast, value was material. Human labour was a commodity. Classical economics was a theory of natural prices. Subjectivity was recognised but regarded as irrelevant. It consisted of the decisions of capitalists or managers with reference to investment or the labour process. Georg Simmel described money as a "claim on society" (Dodd, 2015). The cement is trust, not just between individuals but across society. Society is sociation or association through the medium of money. Ontologically, it engages with the connections between parts and wholes which are different from particular historical marks.

The pure logic of the movement of value takes place in the realm of circulation. It resides in the transformations of commodity and money (Arthur, 2013, pp 10-11). Capital is a monetary form. Money generates money. It is also the case that money mediates commodity exchange (Arthur, 2013, p 30). The turning point in Marx's *Capital* is when the general formula of capital includes the concept money but where the source of circulation is not theorised. We then move from circulation to production. Capital must transform use-values and, to that end, it requires labour. Money may be immaterial like dots and dashes on a computer (Arthur, 2013, p 12). The abstraction of value from commodity relations must be grounded in something concrete representing it (Arthur, 2013, p 31). Through a dialectical development, the money form generates surplus value as the aim of exchange in the capital form. The final move from circulation to production is necessitated, then, by need to explicate the production of surplus value (Arthur, 2013, p 32). The answer lies in the purchase and consumption of value-producing labour power. In short, money is the measure of value. Labour is its source.

The vicious short circuit

With money as a store of value, there can be at most a temporary break in circulation, the steps being resumed later (Arthur, 2013, p 102). When we start with money, we write the famous M-C-M´. The circulation between money and commodities offers a greater scale of self-reproduction than C-M-C´. With the form of *capital*, value becomes an end in itself rather than the link in other relations. Capital is self-valorising value. However, its self-realisation depends upon external sources (Arthur, 2013, p 104). Exchange could evaporate. Commodities as use values are required to generate capital but are not assured to do so. In order to ensure its existence, capital must produce these commodities. For the purpose of self-grounding, capital must undertake the production of commodities itself and reduce them to moments in its own circuit. Production involves the activity of labour. Only thereby can capital effect a surplus.

Financialisation is a permanent break in the circuit. The connection between use values and exchange value is snapped, that between money and commodities rent asunder. It is a perverse, and ultimately self-defeating, moment in the monetary circuit (Michell, 2016). In all non neoclassical accounts, money is the manifestation of production. It circulates through the economy and is destroyed when workers spend their wages on Basics or buy securities. Capitalists, thereby, repay their loans to banks closing the circuit. In the epoch of shadow banking, money and credit claims are originated by banks lending to households. The spent money ends up in the possession of the rich or with corporations. These entities proceed to purchase the liabilities of money market funds or other financial corporations. Money passes through links of a chain until it is used simultaneously to extinguish a loan and a deposit from the balance sheet of a bank. This circuit escapes the dynamics of commodity production. Capital fetishism is the notion that finance can generate surplus without the exploitation of labour (Roberts & Joseph, 2015). It appears that money can produce more money by itself even in the face of the increasing inability of industrial capital to earn profits.

The fascism of financialisation in India

The tributary mode of production is defined as a "mode of production where the state controls both the means of production and the ruling class and has unlimited disposal over the total surplus labour of the population." (Banaji, 2013: 23). Under advanced capitalism, money takes the form of Central Bank money assuming the convertibility of private monies (Blanc et al). There is, though, a conflicting logic at work. One is the impulse towards

centralisation ensuring the convertibility of debt commitments, the other the splitting of the convertibility in financial markets. The Central Bank can favour debtors in the former case by offering refinancing facilities or creditors by permitting them direct control over the management of debt. The nature of the Federal Reserve was defined as a tension between centralising and atomising forces (Brown, 2015). The former element consisted in being absorbed as an organ of the American government. The second force consisted of control by the market in the form of Wall Street. The conflict has been resolved in the nexus between the Fed and Wall Street (Broz, 2015; Goodhart & Schoenmaker, 2016). In the realm of finance, it is now easy for Congress to pass laws like Sarbanes-Oxley that intrude into the space of other countries. In the case of SWIFT, Cuba, Iran, US banks and corporates were obeying orders from Washington DC. The Fed actively intervened in support in countries in which US money center banks has high loan exposures. An "Audit the Fed" proposal that would end the Fed's confidentiality about this activity is doing the rounds of the House of Representatives. The campaign contributions from the banks to Congress clearly suggest that the Bill will not see the light of day. The Fed flooded foreign banks and Central Banks with liquidity thereby softening somewhat the severity of the financial crisis. In short, the Federal Reserve has become the lender of last resort to the world's most international private banks.

It is not difficult to record the imperialism of this model on other countries of the world. The agenda for heightening the financial circulation in India is sanctified in a manual authored by a reputed scholar of finance who occupied a senior research position at the IMF and is now the Governor of the Reserve Bank of India, Raghuram Rajan. The Report is available on the Net. It is labelled 'A Hundred Small Steps'. The slogan is a signal that not even the outline of a path need be sketched. Instead, subliminal messages are sent out. Who would question the homely scold, 'walk before you run'? Infant social scientists today are weaned on a diet of incentives and regulation. For a developing country there is a nod in the direction of the poor through the pitch of inclusion. A model is required to give point and purpose, to indicate spheres to be locked in, and activities to be locked out. We would have expected a high-powered crew to dig into the dishes, cutting and chopping here, filling out there. In the absence of a serious engagement with concepts, we have an everyday menu: less control is better than more; regulation must not be too hot, nor too cold, but just right for proper incentives; the poor must not be forgotten, and so on. Our alternative perspective is grounded in structure and history. The path to long-run growth was engineered at points of time and space in the history of nations by organs of the State collating massive resources and

directing them into particular sectors. These sectors were identified because of their potential multiplier effects, their ability to generate virtuous cycles. To that end, monopolies were created including, notably, the monopoly of note issue.

There is an established literature about how finance and the real might connect. From the latter cajoling innovations in the former to the revolutionary thesis that monetary-financial mechanisms must be installed *before* industrial revolutions take off, econometricians and historians have been hard at work. One lesson that has been learnt is that there are important threshold effects; that is, real development must be sufficiently advanced before finance can impact and, as well, there are often nonlinearities in the relationship between the two. A status report is that the impact of finance on growth is, at best, weakening, at worst turning parasitic (Demetriades & Rousseau, 2015). Some financial reforms have large growth effects but the sign of the latter is ambiguous.

The financial and the real are separated in the Report. Even more, the real is to be manipulated to conform to the textbooks in Chicago-school fashion. Thus, on page 6, financial sector reforms are supposed to "piggyback on real sector reforms". The list of aberrations in the real world that must be abolished before finance floats in is comprehensive on page 63: "levels of risk may be brought down *first* through physical methods (my emphasis)". These include soil and water conservation for reducing drought risk in the case of crop insurance and preventive health care, safe drinking water and sanitation in the case of health insurance. A chicken-or-egg question might be posed here. Is not finance for the purpose of the production and consumption of goods and services? If the ends of economic activity must be achieved by nothing short of a 'real' revolution in India, what need of the means of finance? Agriculture is dismissed in a line or two on page 32. We could add a footnote; finance cannot have any bearing on the food crisis.

Among the errors committed are the following: that price fluctuations are stabilizing (page 106). The reference seems to be to real markets where the claim is false. The conditions for stability in interacting markets are stringent and unlikely to be met in practice. As wrong is the offering that news is about fundamentals. We may or may not get *information* about fundamentals. Besides, given information sets, the next round of Nobel prizes will be awarded to those who propose models showing that, with full rationality, people choose to ignore information that leads them to complex behavioural routes. News might move in a direction orthogonal to the fundamentals. At academic campfires, riveting tales have long

been told of informational cascades, fads and fashions, mass behaviour driven by news variables. Financial history, best exemplified by the scholarship of Charles Kindleberger, is replete with equilibria punctuated by manias and panics. Many of the financial crises that have bedevilled countries have been the outcome of mood swings even when the basic macroeconomic identities were in place. For instance, often banks were both solvent and liquid in meltdowns that reduced them to naught. If financial-real couplings were at the back of the framers' minds, and they should have been, a well-established literature has developed around positive feedbacks like financial-real accelerator models. Efficiency and liquidity are touted as "outcomes" measures on page 110. The former criterion, any student of economics knows, appears in two places. It is part of the grand finale of general equilibrium theory. Also, it is a benchmark in Financial Economics in the assumption of efficient markets. There it is a joint hypothesis and, like most theorems in financial economics, is more famous for its violation in applications. Liquidity is a characteristic of a portfolio that might, optimally, consist of illiquid assets as well. The message is invidious. Illiquidity is "represented by rules and regulations like the banning of futures and options" on the same page. Properly, farms, factories, irrigation projects and the like are illiquid assets. In a few sentences and in the face of the crisis that was brewing beknownst to the members (in a remarkable aside, the authors claim to have seen signs of recovery in America at the time of writing in 2008!) the suggestion is that illiquid assets be securitized, dicing and slicing them with other assets, so that all assets can be marketed. The logic is pursued inexorably. Even priority sector lending is to be marketed. The recommendation is to create certificates so that the forces of inter temporal demand and supply might equilibrate that market. Naturally, we would expect priority sector certificates to be standardized and combined with other assets in saleable bundles. The fundamental characteristic of local environments which is the domain of priority sector lending and long-lived assets which are illiquid, however, is that they are information-intensive. Finally, one of the beautiful constructions of the general equilibrium structure to deal with the unknown is the device of markets for all future dates and states of the world. The problem is that some date-state exchanges might not be available. Markets might be missing. Kenneth Arrow and Gerard Debreu would shudder at the suggestion that the implication is to go out and "complete markets" (page 116). The advice is senseless but this is digging beneath the written word. No more than a hanger is required for the dictum to open markets for all financial assets.

Somewhere the authors claim that the rich-poor divide has supplanted the rural-urban divide in India. If true, this Report is geared towards cementing the wall. It is all about smoothening the financial circulation of the rich.

What can be done?

We propose an alternative rigor, the discipline of National Income Accounting. The actual working of economies can be tracked, thereby. Using the accounts as an alternative to financial statements, for example, studies show that during the Great Depression, while the non-bank financial sector went into a tailspin, banks booked positive profits (Cinzia & Gros, 2009). National Income statistics are not marked to market. The supposition is that there is an internal logic to the working of societies as a whole that is not reducible to the strivings of individuals. An economy is a set of interrelated balance sheets. At the heart of the system are households that hold the liabilities of corporations in order to make payments and accumulate wealth and business firms which issue liabilities to acquire productive capital stock and provide income and employment to households. In that case, the measure of a well-oiled capitalist economy is the provision of safe and secure means of payment and a reliable store of value that ensures financing of a level of capital investment sufficient to provide employment to all. A critical stratum here is banks and the leader of the club of banks, the Central Bank, because it and only it can create liquidity. A financial system can be said to be stable when the overarching fabric is such that cash commitments can always be met. The US arose like a phoenix of what Minsky called a robust financial system from the ashes of the Second World War with private balance sheets full of safe government debt. High government debt ratios and slowly-moving private debt ratios accounted for the early postwar success and high level of liquidity. Investment goods are not putty and require complex financial arrangements. Consequently, increasing investment will result in growing private debt ratios and, thereby, increasing financial fragility. Increasing government spending, in that case, is stabilizing because it permits private spending to grow as a function of income, not debt. In sum, what Randall Wray, 2009, has called ratchet government spending is called for. That is to say, government spending is called for in a recession to revive effective demand but continued fiscal stimulus is called for to operate the plant and new machinery that has been supplied. Budgets are balanced, we cannot underline enough, and there is solid crowding in. A model with deficits could be written but we deviate minimally from the philosophy of the Report.

The Report deals with the poor in Marie Antoinette fashion with a 'let them have deposit accounts' order on page 6. Where is this money supposed to come from? Where will it go? In any respectable booklet, it is not helpful to be presented with only one side of an equation. Of course, the spirit is neoclassical; take care of supply, demand will wind its way accordingly. In order to work this airy wave into a coherent scheme we welcome the advice to push cash transfers via bank accounts courtesy the National Employment Guarantee Scheme on page 69. Also interesting is the recommendation of a holding company structure (Proposal 12 on page 11) where the holding company would not engage in any operating activity (page 97). Keynesians have been fleshing out this blueprint according to which banks would be broken down into a variety of smaller units catering to different tastes under the umbrella of a holding company (Kregel & Papadimitriou, 2012). Adding this up leads to the institution of deposit-creating institutions for poor countries suggested by Biagio Bossone (see, for instance, Bossone & Sarr, 2004). The idea is to construct a firewall between the lending and the deposit-creating functions of banks. Deposit-Creating Institutions (DCIs) would collect non-interest-bearing deposits and would distribute money on a non-lending basis, that is, with no condition to restitution. Their liabilities would be backed by Central Bank money. Every deposit balance would be augmented by a proportion of the depositor's own holdings calculated over a reference period. DCIs would not extend credit but would earn revenue from fees charged for payments services. They would not be permitted to distribute their liquidity to capitalists or non DCI intermediaries. The latter would fund their assets exclusively with non-debt instruments. A holding company structure could connect them. What the consistent accounting framework provides is clear dos and don'ts. In contrast, the recommendation of the architects of the Report that all banks be universal banks, small banks being no exception, (page 60-61), is ungrounded. The Bossone-Sarr formulation bears a family resemblance to narrow banking which is being entertained in the aftermath of the financial crisis in America. However, the latter is concerned with deposit acceptance. At the same time, the meeting ground is failure-proof banking. Secondly, the objective is to ensure the complete integrity of the money supply process and both innovations involve a firewall. Non-DCIs would operate under securities firm regulation on which the Report is rich. Their innovative impulses would not be impaired. Their non-monetary financial activities would be backed by non-guaranteed funds and they would be allowed to fail.

All sophisticated accounts of competition speak of it as a process. The outcomes might be surprising and often are unfortunate. In the old tirades against planning, measures of

the quality of output were looked at askance as the implication was that society could decide on goals and, thereafter, mechanisms that could deliver would be grafted. In the Report, principles are intended to supplant rules, "so as to determine quality of output". In all fairness, since goods and services is not the domain of this study the expression must apply to the realm of financial reform but then the admonition is empty. So we twist this precept around with our sine qua non in mind, restoring the connection between money and commodities.

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