What is capitalism, exactly? And can we destroy it before it destroys us?

This text is based on a series of participatory workshops. It offers an introduction to economics, finance, and the theory of capitalism, for anti-capitalists. No previous exposure to economics necessary.

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Kaput

capitalism for anti-capitalists

volume 1: workshops 1-4

to love our country. We learn the histories of good and great rulers (as well as of a few “bad apples”). We learn that consumer goods make us happy, and work makes us free. (We will look more at these points in Workshop 6).

The figures on welfare spending above didn’t include one thing: spending on public education. Modern industrial states spend between 5-10% of GDP on education systems. Neoliberal policiticians often propose outsourcing education to private businesses. Or transferring education back to religious institutions, which often ran schools in the past. But no one would propose scrapping public education altogether. Modern workers, and modern citizens, need to be educated.

This text is based on a series of participatory workshops run over the last few years, and on materials gathered online at network23.org/kaput. It is work in progress.

Please get in touch (kaput@riseup.net) if you have any comments, suggestions, or questions. Or if you'd like someone to come and run a workshop. Or if you'd like to help illustrate, edit, or publish this in a more finished version. Or if you want to get involved in working on anti-capitalist economics education with us.

For updated versions, more info, further reading, workshop dates, go to: network23.org/kaput

Warning: we should note that much of the way the authors understand capitalism and resistance is still pretty ***European focused***. This reflects where we come from. It would be great if future versions of these workshops could have a more global understanding. We could also do with collaborators to help work on that.

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with "free trade agreements".

The military government of Augusto Pinochet in Chile was the first big "neoliberal experiment". Friedman flew out to give advice, and the economy ministry was run by his students – the "Chicago Boys". In 1979 Margaret Thatcher introduced a neoliberal programme in the UK. In 1981 "Reagonomics" took power in the US. Over the next two decades neoliberal policy became the new orthodoxy – they are all neoliberals now.

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Role 4: manufacturing consent.

A bit like fairies (only not so nice), capitalism and the state can only survive so long as people believe in them. Private property, markets and the rest are systems of rules and conventions which we have to learn and accept. Even the power of the state doesn't just come "out of the barrel of a gun": even the strongest and most brutal tyrannies can topple if people stop believing in their power.
If we grow up in capitalist societies, we learn most of the rules – how money works, how to buy and sell things, and so on – as children. We learn that the State protects and defends us. We learn

exchange rates until 1971; institutions like the World Bank and IMF acted as global economic police.

Twenty years after Keynes' death the system seemed solid. In 1965 Time magazine ran a famous cover story with the headline "We are all Keynesians now", celebrating unparalleled economic growth and confidence. The title was a (mis)quote from Milton Friedman, professor of economics at the University of Chicago. Two editions later Time published Friedman's letter complaining that he'd been quoted out of context. Within a decade, Keynesianism was dead and Friedman was the reigning prophet of the new, rightwing, "neoliberal" economics.

What happened was the end of the post-war "long boom", two decades of continued post-war growth. In 1971 the US, crippled by its debts from Vietnam, pulled the dollar out of Bretton Woods, breaking the worldwide currency system. In October 1973 the Organisation of Petroleum Exporting Countries (OPEC) quadrupled the price of oil – the first of the 70s "oil shocks". Stock markets collapsed, triggering recession. Through the late 70s Keynesian policies failed to pull developed economies out of "stagflation" – a combination of stagnant production and inflation. This failure opened the way for a new doctrine which fitted nicely with the interests of big business.

The handiest term is "neoliberalism". Basically, it meant turning the clock back to the 1920s. The state should defend property, but not regulate or intervene too much. Markets will run smoothly if they're left alone. But to get back to the ideal of "natural" competition, governments first have to get busy hacking away the "distortions" that hurt the economy. State-run services should be privatised; financial regulations scrapped; trade unions smashed; "protectionism" for third world industry scrapped and replaced

Workshop 1. Capitalism: an economic system.

What does "*capitalism*" mean?

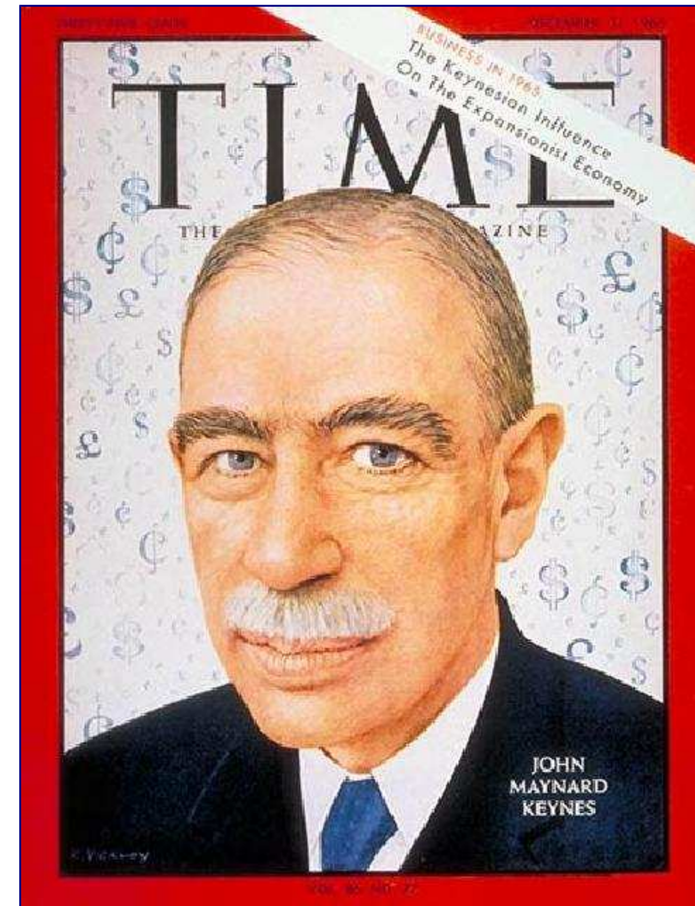
People use the word "capitalism" in many different ways. There is not just one "correct" definition. But we have to start somewhere. We will start by looking at capitalism as an *economic system*.

In schools and universities, economics is taught as if capitalism is "natural", or the only system possible. But in fact there have been, throughout history, many different ways of organising economies. Capitalism itself is quite a recent invention: it is sometimes traced back to 15th century Italy, or maybe 16th century Holland. In the last century or two it's taken over the whole world.

Klallam potlatch feast: a non-capitalist economic institution.

Some examples of other economic “systems” and institutions:

- Hunter-Gatherer economies
- Gift economies (e.g., pacific cultures)
- Slave-based economies (e.g., Roman empire, US Southern States in the 19th century)
- Feudal economies (e.g., Medieval Europe)
- Command economies (e.g., Soviet Union, Maoist China)
- “Market Socialism” (Yugoslavia under Tito)
- Syndicalism (“short summer of anarchy” in Barcelona 1936)
- Co-operative economies (e.g., co-operative movements in Europe 19th and 20th centuries)
- And history isn't over. There will be other economic systems in the future … maybe ones we can’t even imagine yet.



From keynesianism to neoliberalism.

After WW2 most capitalist economies were run along the lines of what became known as the “Keynesian consensus”, named after British liberal economist John Maynard Keynes. Governments regulated markets closely to keep them running smoothly. They used fiscal (i.e., tax and spending) policy to boost consumer demand. International capital flows were stabilised with a global financial architecture: the Bretton Woods system fixed currency

Bail-outs. The important role of the State in supporting capital when times get rough becomes very clear when we look at the recent crisis "bailouts". So far, since 2008, the US Government has spent about $3 trillion on "bailouts" to banks and companies hit by the economic crisis. That is about 20% of US GDP.

US Bailouts so far (money spent or loaned):

bailout	amount
AIG bailout	$127 bn
Economic Stimulus Act 2008	$168 bn
Recovery Act 2009 (2nd stimulus package)	$358 bn
Buying up mortgage securitisation bonds	$776 bn
Buying up government bonds	$295 bn
Support to car manufacturers	$78 bn
Bear Sterns bailout	$26.3 bn
Freddie Mac and Fannie Mae bailouts	$110.6 bn
Small bank takeovers	$45.4 bn

Organising production and distribution

We can think of an economic system as a way of organising what a society or group ***produces***, and how these products are ***distributed*** amongst different people in the group. Economic systems address questions like:

- Should we put our energy into making toys, or guns?
- How much time should we spend working, or playing?
- How should we use land, forests, oil, and other natural resources?
- Who makes these decisions?
- Who gets all the pies?

Example: Tahrir Square

When hundreds of thousands of people occupied Tahrir Square in Cairo in early 2011, they needed to create their own mini "economic system" to bring in and distribute food and other materials to everyone in the occupation. There were sleeping areas, collective kitchens and food distribution points, markets, toilets and waste disposal, assemblies to co-ordinate some of this, and lots more.

Example: Robinson Crusoe's Island

Economists often like to use the example of Robinson Crusoe, from the novel by Daniel Defoe, as a very simple economic system. Even all alone on his island, Crusoe had economic decisions to make, like how much fruit to eat now or how much to save to *"lay up a store, as well as of Grapes, as Limes and Lemons, to furnish myself for the wet Season, which I knew was approaching"*. Later, Crusoe met "Friday", and started a basic two-person class system.

What is "economics"?

So capitalism is an economic system. But how can you separate "the economy" from "everything else"? Economics is involved in everything from the food we eat to global politics to our most intimate relationships.

Actually, the question of how to define the economy is deeply political. The term economics comes from the Greek word **oikos***, a "household". Economics, in ancient Greece, meant household management. Only with the beginnings of capitalism, in late medieval Europe, did economics move from the "domestic" to the "public" sphere, and so get taken seriously by kings and philosophers.*

Adam Smith (1723-1790).

In 18th century England, as trade and industrial revolution took off, writers like Adam Smith and David Ricardo called their new science "Political Economy". I.e., the household management of the wealth of nations. These ***classical economists*** *defined the economy as a special area which politics should keep out of. In recent years, "neoliberal" economists have pushed things further. Theorists like Milton Friedman and Gary Becker argued that* **all** *aspects of human life should be seen in terms of markets. Neoliberal governments, from Pinochet in Chile to Blair in the UK, helped turn theory into reality.*

Breakdown of welfare spending in the UK, figures are % of GDP:

	2001	2009
state supported pensions	5.5%	5.4%
income support for working age people	4.6%	5.5%
healthcare	5.7%	6.9%
other services	3.5%	6.5%

Source for welfare spending: OECD SOCX database
http://www.oecd.org/document/9/0,3746,en_2649_34637_38141385_1_1_1_1,00.html
Source for military spending: SIPRI http://milexdata.sipri.org/

Outsourcing. Since the 1970s, "neoliberal" western governments have been trying to "shrink" the welfare state. The new "austerity measures" of the economic crisis are the latest move in this direction.

But in fact government welfare spending is not really shrinking. Just, more of that money is being redirected to private companies. With *outsourcing*, the State doesn't directly manage welfare services; instead it pays private *contractors* to run everything from prisons to pensions. Politicans and bureaucrats often have close links with the successful companies, such as holding well paid "advisory" or board positions.

Some examples: private prisons (G4S); private ("PFI") hospitals; private pension managers; corporations who run benefits systems, etc. Business is booming in the "security" and "anti-terrorist" industry. Some companies specialise in doing government outsourcing: like the UK's *Serco*, which runs everything from prisoner transport to school kitchens to the Docklands Light Railway.

Bismarck introduced the early pension and health insurance schemes in the 1880s. But these systems were massively expanded in the 1940s. Currently, most European countries spend at least a quarter of national income on state-organised welfare systems.

The welfare state can be seen as part of a "historic compromise" that ended open class war in rich countries. At the end World War One, millions of troops returned home to ruins and unemployment, but with modern military training. Revolutions broke out not just in Russia (1917) but in Germany and elsewhere. Western governments wouldn't let this happen again at the end of World War Two. Across mainland Europe, new welfare systems were largely funded by the US Marshall Plan. This massive US aid programme was designed explicitly to stop the spread of Communism.

Spending on welfare and warfare in developed countries – all figures as % GDP:

	Welfare spending 2001	Welfare spending 2009	Military Spending 2001	Military spending 2009
UK	19.4	24.3	2.4	2.7
US	15.3	19.5	3.1	4.7
France	27.7	30.7	2.5	2.5
Germany	26.7	27.6	1.4	1.4
Sweden	28.7	29.6	1.8	1.2
Greece	20.6	24.6	3.4	3.2

Tahrir Square 2011.

Example: Soviet Planning
In the Soviet Union, many economic decisions were made through a system of state planning. The central planning commission Gosplan, in Moscow, collected statistics about what resources were available in the economy, and then issued detailed plans for what was to be produced by different regions and sectors (mining, agriculture, manufacturing, etc.) One important decision was: how much work and resources should go into producing goods for consumption by Soviet citizens, and how much into producing machines and materials to build up industry?

Example: corporations.
Corporations compete with each other in markets. But internally a large corporation — and some are bigger, in terms of wealth and numbers of people, than small countries — are run much like socialist planned economies. Executives try to control the whole organisation from above.

Example: the financial system

As we'll see in more detail soon, *financial markets* (stock markets, bond markets, bank lending, and more) are central to the process of making production and distribution decisions in global capitalism. Companies buy raw materials and produce goods which they plan to sell at a profit. To buy those raw materials they often need to borrow money. Financial markets are where they meet investors, who lend them money in the hope of receiving interest (and share dividends) as those profits roll in. Investors decide who to lend to on the basis of ***returns*** (which investment offers the highest interest?) and ***risks*** (will the company go bust?) In today's highly complex financial markets, risk analysis is a dark mystery largely built on hype and confidence (what the economist J.M. Keynes called "animal spirits"). Then, sometimes, panic strikes, and investors pull out of everything but the "safest" assets. This hits production: companies don't get their raw materials, factories close, jobs are lost, recession – or depression – sets in.

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Systems aren't monoliths.

Even at its height, the Soviet planning system was never complete: the "commanding heights" of the economy were controlled tightly by the state; but workers were still largely paid in money wages. There were also "black" and "grey" markets. And people doing unpaid housework, working as domestic slaves … or sharing food, giving gifts to each other, or writing poems or volunteering on committees. Similarly, in capitalism not everything is controlled by markets. In any system, as the anarchist Kropotkin often pointed out, there are pockets of alternative ways of doing things – and seeds of resistance. (We will look at this point more in Workshop 7.)

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As we saw in workshop 2, though, major government military spending is nothing new. From the beginning of capitalism, leading powers have built up military might to defend their economic interests. At the same time, military spending "stimulates" the economy, encourages industrialisation, and has also been key in financial innovations such as early bond and share markets.

The new deal and war capitalism. Economist John Meynard Keynes argued that governments should attack unemployment directly by hiring unemployed workers on schemes such as road-building. "Keynesian" policies such as the New Deal in the US, or the massive industrialisation and infrastructure projects in Nazi Germany, were widely credited with ending the Great Depression. When financial markets collapsed and companies could no longer get finance to produce, the Government could step in. The wages paid out from government schemes would have a snowball effect, stimulating new demand for private industry also. Governments would have to borrow or raise taxes to run these schemes, but the long-run gain to the economy would outweigh the cost.

But was it roads and railways that saved the 1930s economy, or tanks and guns? According to the theory of "military Keynesianism", what really ended the Great Depression was government spending on arms. Whilst unemployment was killed off (all too literally) by mass recruitment.

The welfare state. After the Second World War, most developed capitalist countries developed "welfare states". Governments committed to providing a basic "social safety net" of minimum healthcare, housing, education, pensions, and benefits for unemployed people, etc. There had been some "social insurance" measures earlier on: the right-wing German government under

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Luddite uprising.

England, 1549. Kett's Rebellion. *A peasant army of up to 16,000 rebels uprooted enclosure hedges, defeated a government army, and captured Norwich. Their first demand was that "no man shall enclose any more". They were defeated, and 3500 massacred.*

Chiapas, Mexico, 1994. The Zapatista Uprising. *Around 3000 indigenous rebels launched an insurrection on 1 January, taking control of major towns in Chiapas and turning villages into self-governed "caracoles". Their programme included communal village land rights, as well as rejection of NAFTA, (North American Free Trade Agreement) which dramatically extended the reach of global capitalist markets in Mexico.*

There have been many rebellions against enclosure and commodification. What can we learn from them today?

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Modern Times.

In and out: production processes.

Imagine … a car factory. We can think of the factory's work as a *production process*. In at one end come *inputs*. Raw materials include steel, glass, plastics, etc., shipped in from steel mills, glass plants, etc. There are also some parts, electronic components, etc., which have already been assembled in other factories. These inputs are put together by workers — human beings — using machines, which need energy to run. Finally out comes a finished *output*, cars.

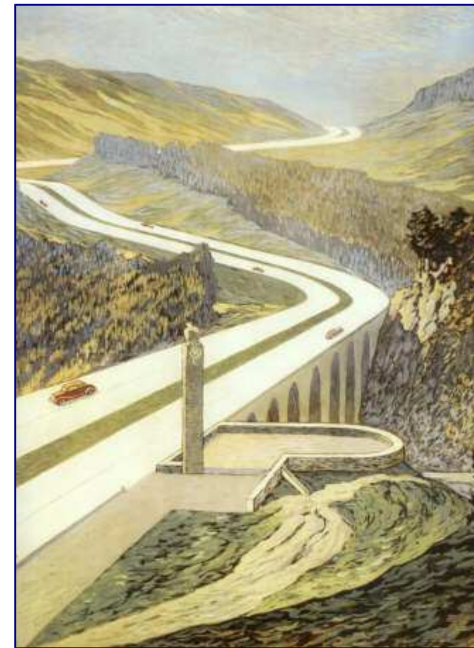
How many cars will the factory produce? It depends on how much of the inputs are put in. Though, if production gets really big, they might have to expand or build a whole new factory.

For example, here are some (completely made-up) figures for a factory producing at full capacity:

inputs	*outputs*
Raw Materials: 1000 tons steel, 100 tons glass, 10,000 mW electricity, ...	1000 cars
Machines	
Labour: 50,000 person/hours	

Complex economic systems generally involve *division of labour:* different workers specialise in different jobs, producing different parts of the process. They also involve *division of decision-making*. E.g., the factory has a manager whose job is to try and get as much output as possible. The hands-on job of squeezing the most hours labour out of workers is delegated to foremen. Workers get to decide things too: which way to turn the bolts … or whether to throw a spanner into the works when no one is looking.

But the decisions about inputs go beyond the factory. The same steel, or workers, could go to other car factories, or to make toys or guns instead, or more car-making machines. Or the iron ore could stay in the ground, and people could spend their time living life creatively instead of working in a factory. How are these decisions made?



Poster for German autobahn building programme.

Role 3: producer and consumer of last resort.

In classical liberal theory, the State is supposed to stay in the background, defining and protecting the rules and institutions on which capitalism relies. Private companies and individuals do the actual production and trading. In reality, it doesn't work like this: states are themselves major producers, consumers, and traders.

The military-industrial complex. In 1961 US President Eisenhower used the term "military industrial complex" (MIC), a combination of an "immense military establishment and a large arms industry". In 2009 the US Government spent $712 billion on "defence", about 5% of US GDP. World states altogether spent $1.531 trillion. (source: SIPRI).

The struggle continues.

Enclosure, colonisation, and other forms of commodification have continued apace through capitalist history. Very often the same pattern holds: local capitalists or landowners start asserting increased property rights; the dispossessed rebel; if property-owners aren't strong enough to smash resistance alone, or with hired thugs, they call in the State.

Shock Therapy. According to Naomi Klein in her book "*Shock Doctrine*", modern states use "shocks" to "re-engineer societies" whilst people are too confused to resist. It doesn't matter where the shock comes from. Some, like wars, are caused by States directly: after the invasion of Iraq, corporations like Halliburton and Blackwater, close to the Bush regime, moved in quickly to grab contracts for running new infrastructure, security apparatus, and privatised oil supply. But terrorist attacks like 9:11, or natural disasters like Hurricane Katrina will do just as well. Massive profits have been made from the security industry after 9:11, and from the "rebuilding" and gentrification of New Orleans.

The **economic crisis** is another example. Governments across Europe have been rushing through bank bail-outs, "austerity packages" and privatisations, claiming they are necessary to save us from economic collapse. These changes benefit the same corporations and banks who caused the crisis in the first place. In the "moment of vertigo" during a crisis, argues Klein, people often seem to accept any emergency "solution" offered by a government.

Markets

In the Soviet system, decisions about allocating steel to factories were made by planning commissions. In a "free market" capitalist system, many of these decisions involve ***markets***.

- The owner of the car factory tries to sell its products to consumers – in the *car market*.
- The car company, the toy business and the arms manufacturer all need to buy steel – in the *steel market.*
- They also need to hire workers – in the *labour market*.

Particular markets can work in very different ways – e.g., labour markets can involve internet job sites, government jobcentres and training schemes, regulations such as a minimum wage and employment tribunals, or cash-in-hand work and gangmasters, etc. But all markets have some basic points in common: sellers (***supply***); buyers (***demand***); and ***prices***.

Unlike a planning commission, "decisions" in markets are often **decentralised** (though not always – see below). Overall outcomes – what is produced, how products are distributed – are not made centrally, but are the result of many actions by many different individuals and groups, often acting independently. For example, there are lots of different car factory managers, and lots more car buyers. Each one can make an individual decision about what to produce, sell, or buy. The "total production" of cars in the economy is a result of all these separate decisions. And of many more decisions made in other interlocking markets.

This does not mean that some people and groups are not more powerful than others in markets. They certainly are. It just means that power relations are more complex, and can be hard to identify.

Santiago, Chile September 1973.

Markets and Power

A **monopoly** *is where there is only one seller in a market. (A monopsony is where there is only one buyer). For example, a company called De Beers has (or did until very recently) an almost total monopoly on the world's diamonds. Monopolists do not have to compete with other sellers who might* **undercut** *them, so they have considerable power to set the price on their products; and so to make high "monopoly profits".*

An **oligopoly** *is where there are a small number of sellers. These sellers may join to form a* **cartel** *which* **fixes prices** *by agreement. The OPEC cartel of oil producing states is an important example.*

According to orthodox economic theory, the more sellers there are, the more the price should be bid down by competition. In a "perfectly competitive market", with many sellers, the price would be forced down until it just covered costs, and there would be no profit at all. Orthodox economics often works with the theory that markets are perfectly competitive. But in reality, such markets don't exist outside textbooks. By controlling prices and

village field; and privatising and fencing the "commons", lands where villagers had collective rights to hunt, graze animals, gather fruits, etc. Enclosures were often the work of local landlords; but they were backed by the State with a series of "Enclosure Acts", new laws phased in from the 15th up until the 19th century. The peasants frequently rebelled, in local riots or major "peasant wars", and the State sent in the troops.

Colonisation. The biggest enclosure of all was the land grab in the colonies. The colonisation of Latin America led the way, directly enforced by armies sent by the kings of Spain and Portugal. In later colonisations, corporate and state power worked together. The British East India Company started out as a trading company, before gradually taking over state power from local rulers. In 1858 India became a direct colony of the British State, after it crushed the "Great Uprising" of 1857.

Enclosing our bodies. Enclosure threw hundreds of thousands off the land – they became fodder for the new factories and mills of the industrial revolution, or the mines and plantations of the colonies. Indigenous peoples of the colonies were enslaved *en masse*. Europeans became wage-workers, tied to the clock and subsistence wages. "This process required the transformation of the body into a work machine, and the subjugation of women to the reproduction of the work force" (Federici p63).

Again, resistance was met with force, as states sent armies to smash slaves' and workers' revolts. Federici argues that the Witch-Hunts of the 16th and 17th centuries were an attack on women and on their pre-capitalist roles in rural communities "to eradicate an entire mode of existence" which threatened economic and political power.

English countryside after enclosure. These fields, west of Sheffield in Yorkshire, were surveyed, fenced, and turned into sheep grazing land in 1789. http://sytimescapes.org.uk/zones/sheffield/S06

Role 2: Original Appropriation

Property rules are constantly changing. In the history of capitalism, the State hasn't just enforced existing property systems; it has also been involved in actively pushing the boundaries of property, helping create new markets and "commodities". Again, whenever necessary, force is used.

In the early stages of European capitalism, national armies were built up and used to enforce a number of important shifts in power relations which allowed capitalism to flourish:

Enclosure. Turning communal land into private property. In England this took two main forms: abolishing the "open-field" system in which peasants farmed strips of land in a non-hedged

production, big companies and cartels have power over distribution of commodities in markets. We can call this **market power**. *In general, an individual or company has more power in a market the more resources – capital, money, or other commodities – it has to trade.*
So, ultimately, market power comes down to owning stuff. But what does that mean? In many markets, ownership of resources is guaranteed by **property law**: *the state recognises what resources belong to you, and can send in the police to back up your claim. So market power does not exist unless it is guaranteed by other forms of power: the political and* **military power** *of the State, which enforces property laws with violence* (see workshop 4)*; and the* **cultural power** *of the* **norms** *and values that keep us believing in private property, and desiring more and more consumer goods* (see workshop 6).

Profit.

The car company needs to think about a number of markets. On the one hand, it aims to make as much money as possible in the car market. On the other hand, it wants to buy the inputs it needs as cheaply as possible.

Suppose its market researchers predict that they can sell 1000 new cars at £10,000 each. That will be a total **revenue** of £10 million. The table below also gives some (again, imaginary) costs for inputs. The money spent on machinery here includes maintenance of wear and tear, replacement parts, etc. – what economists call *depreciation*.

inputs	*outputs*
raw materials = £2.8m	1000 cars = £10m
machines (depreciation) = £500,000	
labour = £700,000	
Material Costs = £4m	Revenue = £10m

The thing is that, usually, the car company will only get the revenue from its car sales *after* the cars are produced. But it will need to pay for inputs in advance. So it will have to *borrow* money to fund its production.

This brings in another kind of market – *financial markets*. As we will see in workshop 2, there are various kinds of financial markets, including bank lending, stock markets, and bond markets. They work in different ways, but again we have the same basics. This time the commodity being bought and sold is finance

A witch riding a goat lets loose a rain of fire.

The bloody birth of capitalism – a hidden history.

"*The development of capitalism was not the only possible response to the crisis of feudal power. Throughout Europe, vast communalistic social movements and rebellions against feudalism had offered the promise of a new egalitarian society built on social equality and cooperation. However, by 1525 their most powerful expression, the "Peasant War" in Germany … was crushed. A hundred thousand rebels were massacred in retaliation. … With these defeats, compounded by the spreads of witch-hunts and the effects of colonial expansion, the revolutionary process in Europe came to an end. Military might was not sufficient, however, to avert the [economic] crisis of feudalism.*

… It was in response to this crisis that the European ruling class launched the global offensive that in the course of at least three centuries was to change the history of the planet, laying the foundations of a capitalist world-system, in the relentless attempt to appropriate new sources of wealth, expand its economic basis, and bring new workers under its command."

From: Silvia Federici, ***Caliban and the Witch.***

justified by a "social contract" between rulers and ruled. The government's role is to defend private property, and so prosperity; in return, the people obey its laws. But Locke and Rousseau argued that "the people" have a right to disobey and overthrow a "tyrannical" government that abuses its power.

*David Hume and Adam Smith, friends and leading thinkers of the "Scottish Enlightenment", argued that if individuals follow their economic "**self-interest**", this brings peace and prosperity for all. Earlier philosophy had praised aristocratic virtues of honour, courage, or noble self-sacrifice, and seen "self-interest" as "low" and undignified. Now, in liberal theory, it became the foundation of a good society.*

Many of the political struggles of 18th and 19th century Europe involved the rise of the new capitalist class – the "bourgeoisie". In the "Glorious Revolution" of 1688, English capitalists supported the replacement of Catholic King James II by the pro-market Dutch protestant William III. The new government was dominated by the "Whigs", identified with a new property regime against the old "Tory" "landed gentry".

In the French Revolution of 1789, and in the English reform struggles through the 19th century, the new class went further, overthrowing Aristocratic government altogether. In the new "Parliamentary Democracies", all property-owners could claim some share of state power.

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– money being lent. The "buyers" are the people and corporations trying to borrow money; the "sellers" are the lenders; the price the borrowers have to pay is the ***interest rate***.

For example, the car manufacturer needs to borrow £4m to pay for inputs. It agrees to pay back the money with 25% interest a year later, after the cars are sold. In the longer term, the car manufacturer probably also had to borrow to buy the machines and building for its factory. It will have to keep paying interest on these fixed costs, probably for many years.

costs	*revenues*
Material Costs = £4m	Sales = £10m
Total Finance Costs (long and short term) = £2m	
Total Costs = £6m	Total Revenue = £10m

Suppose the car manufacturer got it right and it can sell all its cars for £10,000 each. Then it makes a profit of £4 million (Profit = Revenues – Costs). Governments may take some of that in tax. Out of what is left, the car company owners now have a new decision: how much should they invest in expanding the business, buying more up-to-date machines, etc.? And how much should they keep for themselves to spend?

Things don't always go so smoothly. If the factory can only sell 500 cars, or has to sell them all at half price, then it makes a £1 million loss. The input costs and interest payments still have to be paid. If the company can't borrow more money to keep afloat, it will go bust.

From cattle to capital.

Historians usually trace capitalism back to the 15th or 16th centuries; but the word "capitalism" itself only goes back to the mid 19th century. The word "capital" is older. It comes from the Latin capita*, for "head". In the middle ages, "chattels" meant a wealthy person's movable wealth, especially animals or livestock – including, where slavery was legal, slaves. The term still survives in our modern English word "cattle". So, perhaps capital originally meant "heads" in the sense of the number of animals ("heads of cattle") belonging to an owner.*

18th century economists identified three "factors of production": land, labour, and capital. Capital now meant all other materials and machines involved in production. By the 19th century land was no longer a separate "factor", but considered just another form of capital. In the 20th century, with neoliberal theories of "human capital" ("intellectual capital", "social capital", etc.), some started to see human energy and skill as just another kind of capital too.

We can also distinguish between physical *and* financial *capital. Finance is not actual tangible stuff, but promises, agreements, IOUs, and contracts for using physical capital. (See Workshop 2.)*

the basis of mainstream "political philosophy" today. These writers developed theories to undermine the old medieval institutions of feudalism and supreme monarchy. At the same time, they also attacked the ideas of revolutionaries who wanted much more radical change: revolting peasants like the Dutch and German Anabaptists; the English Levellers, Diggers and Ranters; early urban rebels like the French Sans-Culottes.

Important tasks for liberal theory were: to develop new systems of ***private property****; to establish the power of the* **market***; and to fix the role of the* ***state****.*

Liberals supported strong and standardised property rights which benefited the rising merchant and capitalist classes. Property needed to be protected from kings and lords on the one hand; and from the "mob" (ordinary people) on the other. Liberals attacked old rules and institutions that limited the market: on the one hand, aristocratic corruption, feudal taxes and levies, and royal monopolies. On the other, traditional communal land rights, or the guilds of craftsmen and workers.

The English philosopher John Locke, who was also involved in the colonial administration in New England, developed a new theory of property. Land, and manufactured goods, belong initially to those who work or "mix their labour" with them. Only labour creates "value" – an idea later developed in the "labour theories of value" of David Ricardo and Karl Marx. As the "American Indians" left pastures and forests "wild", colonists had the right to take them and make them "productive". Labour and industry, together with enclosure ("commodification") and private ownership, bring wealth and prosperity.

Hobbes, Locke, and later Rousseau, argued that government was

and measures.

One important form of regulation is control over what can be used as money. For example, many states throughout the 19th century (re-)introduced monopolies on coining or printing money. The regulation of financial markets in particular is a particularly hot topic – we will look at it in the next workshop.

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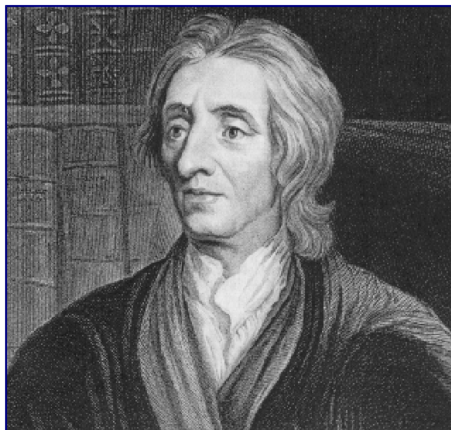

John Locke.

Liberalism.

Liberalism is a political philosophy that grew up together with capitalism. Of course, not all capitalism is "liberal". China is still officially Marxist. In Europe in the 1930s, many bankers and industrialists who had supported liberal democracy switched easily enough to fascism and nazism.

The arguments of early liberal thinkers such as Thomas Hobbes, John Locke, David Hume, or Jean-Jacques Rousseau still form

Capitalism – or capitalisms.

Maybe it's better to say that there is no one "capitalist system", but many systems and institutions which are more or less capitalist. Capitalist systems differ across space and time, and have been evolving for hundreds of years. Any capitalist system, though, will have some basic characteristics, for example:

Markets. Decisions are made through many complex interactions of buyers and sellers in markets.

Commodification. Can anything be bought and sold in a market? Fresh air, promises, love, ideas, principles? Things that are bought and sold in markets are called ***commodities***. Over the history of capitalism new kinds of resources have become ***commodified***. In 16th and 17th century England, and in the colonies, land held in common, and wild land, was "enclosed" and parcelled up amongst landlords. More recently "intellectual commons", or even the genetic codes of wild plants, are being trademarked and patented, and so "enclosed".

Property. The only people who can buy and sell in markets are those who have ownership rights over commodities. Thus behind every market is a background of property rules – laws, conventions, regulations about who owns what, and what they can do with their property.

The State. And behind property laws is the state – standing guard to enforce them with violence.

Profits. Capitalism is a system of production. Companies chase after ***profits*** wherever they can, and largely this means producing and selling new commodities. Investors finance companies for a share of the profits.

Capital. To make profits, whether by producing or investing, you need to own capital, whether "physical" or financial.

Labour. Human time and energy is also commodified, bought and

sold on “labour markets”. In particular, **wage labour** is important in capitalist systems – but we shouldn't forget that slave labour, and unpaid domestic labour, are also still prevalent today.

inherit: e.g., in “primogeniture” systems, the first son is entitled to most of a father’s property. Many states have introduced ***inheritance taxes*** to take a share of passed-on property.

Land rights: planning regulations. In many countries, the State has some control over the use of land: even if you are the owner of the land, you will have to apply for permission to use it for particular purposes, such as building houses or business property.

Crimes and Torts. The English legal system (and systems which descend from it, including the US) makes a distinction between *civil* and *criminal* law. For example, if you trespass on someone else’s land, this is not initially a criminal offence, but a disagreement between two “civil parties” – you and the owner – which has to be resolved in a civil court. The police are only supposed to get involved if the court rules against you. The UK government has recently (September 2012) changed occupying residential property into a criminal offence.

Intellectual Property. Intellectual property law governs rights in “intangible assets”: music or books, inventions, or designs and symbols such as corporate names and “trademarks”. The 1709 “Statute of Anne” in England is one of the world’s first laws for copyrighting written texts. The 1624 English Monopolies Act was an early *patent* law, granting rights to exclusively use a new invention. In 1980 the US Supreme Court upheld a patent on a genetically modified biological organism (case of Diamond v. Chakrabarty).

Regulating markets.

As well as guaranteeing property rights, States may actively ***regulate*** market transactions. States throughout history have policed markets by, for example, imposing laws on the quality of goods; on licensing for traders; or standardising the use of weights

- beatings with fists, shields, truncheons, batons, etc.
- tear gas, pepper spray and other chemical weapons
- horse charges, water cannons, tasers, plastic bullets, and other "less than lethal" weapons
- guns, tanks, bombs ("air strikes"), land mines, nerve gas, computer-controlled drones, etc.
- prison cells, hard labour, isolation cells, the death penalty (in some countries)
- tortures and "extraordinary rendition", cattle prods, sleep deprivation, water boarding, etc.

Changing property rights.
One role of the State is to ***define*** and then ***enforce*** who has rights over what. Property definitions, as well as enforcement techniques, are constantly changing. Here are just a few examples of how property rights can differ and change:

Slavery. Most ancient "civilisations" recognised *chattel slavery*: human beings could be owned as property, and traded on markets like other commodities. Property rights over slaves were formally abolished across the British Empire in 1833, and similar laws were enacted across the world over the 19th and 20th centuries. Some legal systems, however, still recognise forms of ***debt slavery***: you sign an enforceable contract to pay back debts with labour. Many democratic countries widely practice enforced ***prison labour***. In the US, and now also UK, selling rights to the use of prison workers to private contractors is a growing market.

Inheritance rights. Most property systems recognise inheritance: family members and others can pass on their property to others when they die. Inheritance helps maintain and build up concentrations of wealth. ***Inheritance law*** concerns who can

Workshop 2. The high seas of finance.

If the world economy were an ocean, finance would be the currents and swells shifting resources from one shore to another. Sometimes the flows are steady, the surface looks millpond smooth … but then, out of the blue, things start to get rough …

Recap of workshop 1: Capitalism is a complex system of many interdependent markets. For example, the car producer sells its products in the car market, and needs to buy inputs – raw materials, energy, labour – in lots of other markets. As a producer needs to buy inputs before making and selling its product, it often needs to get **finance** (also called: **finance capital**) from ***investors***. Later, it will pay them back out of its profit … if it makes one.

Equity and debt.

Basically, companies can raise finance capital in two ways: by selling shares; or by borrowing. Markets trading shares are called ***equity markets***. Markets trading loans and bonds, forms of borrowing, are called ***debt markets***. Nowadays things have got rather complex, and the distinction is not always so clear – but it is somewhere to start.

VOC trading ship.

rights to use and trade goods. It is part of the ***Legal System***: a system of rules which are defined and enforced by the State.

However, we should remember that as well as legal rules, there are also ***norms*** and ***conventions***, often unwritten, behind markets and property. For example, a market like the New York Stock Exchange has its own set of regulations which traders have to obey if they want to do business; these are not government laws, but the Exchange may exclude people who don't follow them. "Black" and "grey" or "informal" markets also have rules and conventions, though it will not usually be the State police who enforce them.

Theories of modern government often distinguish between three "branches" of state power. The ***legislature*** is where laws are made – e.g., parliaments, or presidential decrees. The ***judiciary*** means the court system (judges, lawyers, juries, inquiries, etc.) which rules on particular cases. Finally, the ***executive*** enforces the law.

The executive commands state forces like the ***police***, the ***army***, the ***prison service***, ***tax collectors***, ***border guards*** and ***customs officers***. These officers of the state do the hands-on work of ***enforcing*** the law. Alongside private sub-contractors: mercenaries, private prison companies, security guards, etc.

Law enforcement.

Enforcement means the threat, or actual use, of ***force*** against people who do not obey the legal rules. Perhaps this should be obvious. But liberal theorists and other state supporters do a lot of work to help us forget about the violence of the state, using euphemisms, selective reporting, etc. So, to be clear, some of the means used by the state to make sure that people do not take others' lawful property include:

Role 1: Defender of property and markets

In capitalist economic theory, a market is where people can come and make deals "freely" with each other. A market could be an actual physical place: like a town market, or an old-fashioned trading floor. Or it could be a virtual network of buyers and sellers spread around the world.

Any market needs a set of ***rules***. These could include: rules about *what* can be traded on the market; about *who* is allowed to trade on the market; about *how* deals are made, prices are decided, etc. In most capitalist markets, one very basic rule is: you can only trade a commodity if you have a legal ***property right*** to it. For example, if you ***own*** it as your own property; or you have borrowed it, with permission from the owner to trade it. If you don't have any property, you can't trade on a market.

Property Law is a system of rules which defines who has what

Equity markets.

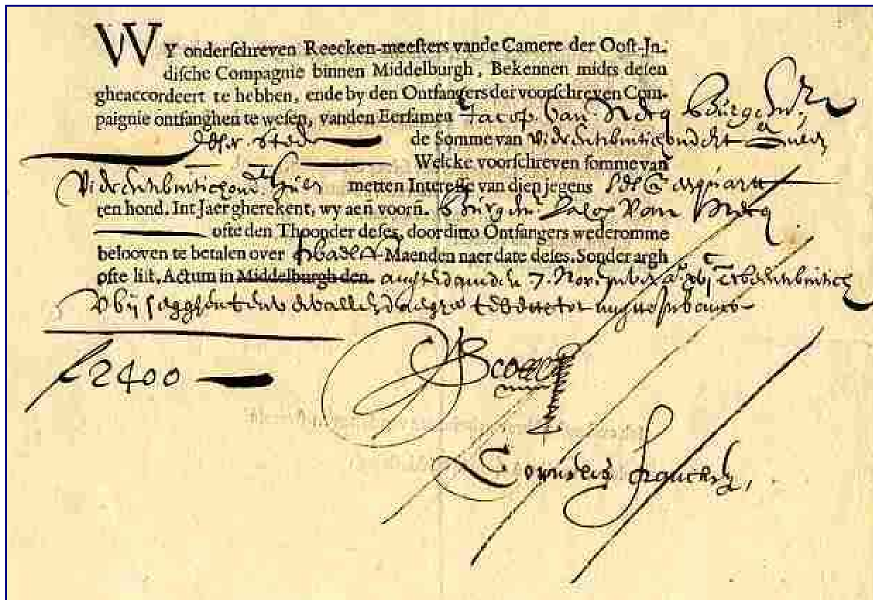
Equity markets trade ***shares*** in the ownership of companies. Company Law sets out different ownership structures for companies:

– Most UK law or accountancy firms are ***partnerships.*** All the partners share responsibility for the company's decisions. They share the profits; and also any losses and debts.

– A ***limited company*** is a special legal structure to ***limit the liabilities*** of the company's owners. ***Shareholders*** have a share in any profits; but if the company goes bust, they are only liable for its debts and losses up to the value of their shares.

– A ***public limited company*** (**PLC**) or ***listed company*** is a limited company whose shares are traded on an established stock market – e.g., the London or New York stock exchanges, the Paris Bourse. Anyone can buy and sell these companies' shares through a stock ***broker***. Only companies over a certain size can be listed, and they have to publish regular accounts. The first ever PLC was the Dutch East India Company (or: **Vereenigde Oost-Indische Compagnie**, **VOC)**. Its shares were traded on the Amsterdam exchange from 1602.

Stock exchanges, where the shares of big PLCs are traded, are just the most visible face of the equity market. Many shares are traded in private deals between individuals and companies. ***Private Equity*** funds are investors who specialise in doing equity deals away from the listed markets.



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VOC share certificate 1623.

The shareholders of a limited company are its legal owners. But a big corporation has millions of shares, and many thousands of “owners”. Only shareholders who own a sizeable percentage of the shares have any real control over the company’s actions. Often, the managers or ***executives*** of the company, who are technically employees, have much of the real power.

Shareholders are entitled to a share in the profits of the company. But if the company is going to keep on growing and competing with rivals, it will need to re-invest some of its profits back in the business. Managers and owners decide how much to invest in future production. What is left is then distributed amongst shareholders: this payment is called a ***dividend***. Big companies do not always pay out dividends, but shareholders can still make a profit by selling their shares – if the share price goes up.

What is a state?

Max Weber, one of the founding fathers of sociology, gave the classic definition. A state is an institution with a “***monopoly on the legitimate use of violence***” in a territory. The state uses violence through its armies, police, gaolers, and other armed functionaries. A *monopoly of violence* means that no one else in the territory is allowed to use force without the state’s permission: citizens should not “take the law into their own hands”.

What does “*legitimacy*” mean here? Perhaps that the state’s citizens or “subjects” agree that the state has the right to use force against them. Liberal political philosophy since the 17th century has endlessly discussed the “legitimate” limits of the state’s monopoly. The main point, maybe, is that no state really governs by force alone – as its troops are always outnumbered, it needs at least some level of “consent” from citizens.

In reality, Weber’s definition is an ideal that states aspire to: probably no state has ever been accepted as legitimate by everyone it tries to rule; or really held a complete monopoly of violence. (E.g., in the US, one of the world’s strongest states, citizens still have the legal right to own weapons.) Just as no economic system is monolithic, state power is never total.

their saviour from the communist threat. Massive state spending on arms and infrastructure gets Germany back to growth and full employment. Similar policies also work economic wonders in Japan, the US, the UK, and elsewhere, ending the *Great Depression*.

July 1945: The Labour Party comes to power in the UK, introducing the post-war *welfare state*: the National Health Service, national insurance and child benefit, and nationalisations of the Bank of England, railways, coal mines and more.

August 1953: The British government, working together with the CIA, organises a coup to topple the Iranian government headed by Mohammed Mossadegh, which had nationalised the *Anglo-Iranian Oil Company*. This company was then majority owned by the British government, and was a major contributor to the cost of the British Welfare State – but paid little back to Iran. It has since been privatised, and renamed BP.

September 1973: General Pinochet seizes power in Chile from the left-wing Allende government, which had nationalised US corporate property in the country. The "Chicago Boys", Chilean economists trained at Chicago University, are given control of economic policy. Their "*neoliberal*" programme of privatisation and deregulation will inspire Reagan and Thatcher.

November 2011: the leaders of two European democracies – Greek prime minister Papandreou, and the Italian Berlusconi – resign. Without elections, they are replaced by bureaucrat economists heading "technical governments". With one mission: to push through the "*austerity packages*" of cuts, privatisations and job losses demanded by Europe's bankers.

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Corporations.

The word **corporation** *comes from the Latin* **corpus**, *a body. In Roman and medieval law, States recognised certain institutions or associations as* **legal persons** *– "bodies" with legal rights and responsibilities of their own. For example, the* **Corporation of London**, *the governing body of the City of London, was granted its first royal* **charter** *in 1067. Many Lord Mayors and other individuals have been born and died since, but the corporation goes on with its own legal life and history.*

Some say that the oldest business corporation was Sweden's Stora Kopparberg mining corporation, chartered in 1347 and finally closed in 1992. Two important corporations in early capitalist history were the British and Dutch East India Companies (1600 and 1602), licensed by the British and Dutch states as monopolies to exploit the trade and colonisation of India.

Corporate law differs around the world, but everywhere it creates some form of legal separation between the corporation and the individuals who own and manage it. Corporations are usually **Limited Liability Companies**, *which protects individual owners from responsibility for the company's debts. But corporate law often goes further still, e.g., to protect individuals from legal responsibility for the company's criminal actions.*

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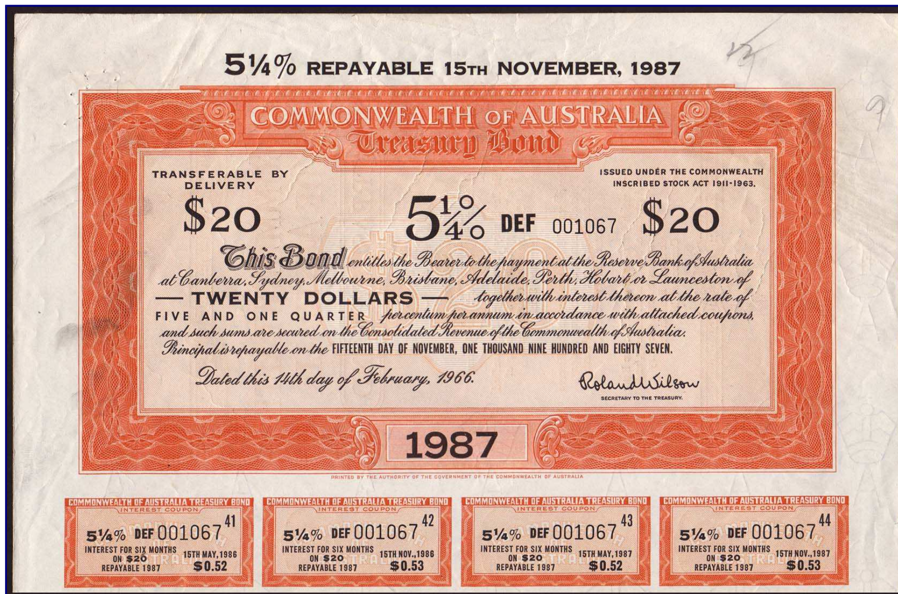

Australian treasury bond. Face value $20. Fixed interest rate 5.25%. Maturity 21 years.

Debt markets.

There are two main ways in which companies can borrow money: getting ***loans*** from banks; or issuing ***bonds***.

A corporate bank loan is basically the same as if an ordinary person gets a loan, only bigger. Any loan involves a ***contract***. The borrower and the lender agree: the ***term*** of the loan, or when it must be paid back (e.g., 3 months, or 3 years); the ***interest rate*** (e.g., 5%, paid each year); any ***collateral*** which the borrower forfeits if doesn't pay back the loan (e.g., in a *mortgage loan*, the collateral is a house). If the borrower doesn't pay back the loan, this is called a ***default***. Banks make loans to companies, individuals, and governments. They also make loans to each other. One important financial market is the ***interbank loan market***, where banks lend each other cash to balance their books in the short run. If banks stop trusting each other, this may be one of the

Workshop 4: the capitalist state

"*The military and the monetary get together whenever they think it's necessary*". Gil Scott Heron "Work for Peace" (http://www.youtube.com/watch?v=hPqpV9olIlw)

What role(s) does the state play in the market economy? One way to start thinking about that is to look at some moments in recent history:

August 1842: The governments of China and Britain sign the *Treaty of Nanking*, after China loses the first *Opium War*. China agrees to allow opium imports, to declare free trade in five port cities, and to give Hong Kong to Britain.

January 1933: Adolf Hitler is elected Chancellor of Germany, supported by the country's main industrialists and investors as

- 1960s: financial profits were 15-20% of all profits in the US;
- 2000s: they were 35-40% (source: Foster & Magdoff).

The other thing is the work people do. Here are some recent employment figures from the UK (sources: Graham Turner; Office for National Statistics):

	Manufacturing	Financial, business service, and insurance	Retail, hotels and restaurants
1997	4.2 million jobs	4.9m	4.9m
2007	2.9m	7.15m	7.1m

The famous “destruction of British manufacturing” which started under Thatcher continued apace under Labour. By 2007, over 7 million people were working in finance. Another 7 million people were making them cappuccinos.

Vendor financing.

The question: if US and UK industry has died or, at best, stagnated, what are these bloated financial markets actually financing?

The answer: **a massive consumer debt bubble**.

How does the first world pay for all those imported goods? By borrowing from the productive world. We will look more at these points in Workshop 5.

first markets to collapse: no one wants to lend (supply).

A ***bond*** is to a loan what a publicly listed share is to private equity. Basically, a bond is a tradeable ***IOU***, a loan contract that can be bought and sold by anybody in the bond markets. Originally, a bond was a piece of paper with something written on it like “I promise to pay you £100 on 1 January 2020”. When the date comes round, whoever owns the piece of paper can demand the money. Bonds also have a term, or ***maturity*** date. Bonds are usually longer term than loans, often 10 or 20 years. And they have an interest rate, or ***coupon.*** Fixed rate bonds have a standard set coupon, e.g., 5% per year; variable rate bonds (like mortgages), have a coupon which moves with a reference interest rate (e.g., Libor – the London inter-bank lending rate – plus 2%).

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A very brief history of banking and debt markets.

There are 4000 year old records of loans from Babylonian temples to merchants. Not only were money lenders based in temples, but the temple authorities often ran the business.

Modern banking is usually traced back to medieval Italy – the word **banca** *refers to the bench on which moneylenders would conduct business. The house of Medici opened in 1397. Italy's Banca Monte Paschei dei Siena, founded 1472, is still going.*

Medieval, like contemporary, banks could make money both from lending – to states, merchants, and the rich – and from taking deposits. Banks offered safe storage of gold, silver, and other valuables.

The basic idea is called **deposit banking***: savers deposit money in the bank; the bank can lend out the same money to borrowers, and charge interest. So long as too many savers don't come to withdraw their money at once (a "***bank run***"), the bank can "cover" loans with deposits.*

Early bank notes were simply receipts ("letters of credit") for the metal coins a saver deposited in the bank. As banking networks spread across Europe, a merchant could use the same receipt to withdraw coins from different branches of a banking house, in Antwerp or Venice.

From the beginning, European debt markets were associated with the financing of ***war****. Fortunes were made by the Venetian bankers who funded the crusades. The invention of bonds, or tradeable debt securities, goes back to the Dutch war of independence (from Spain) in the 16th century. The rebel Dutch state issued perhaps the first sovereign (i.e., government) bonds. The Netherlands was the leading capitalist economy of the time. Other Dutch*

capitalists are still at risk from the global depression – they need us to keep consuming their products.) Their products directly out-compete manufacturing in the old core, mainly due to much lower wage costs. So they do not need to rely on protectionist import tarriffs.

What does benefit them is to keep their own currencies low, making exports even cheaper. The *trade wars* rumbling between China and the US have been about currency "manipulation" not protectionism.

China has been winning these trade wars. The US now has neither the market power nor the *military power* to take on China. Like Britain 100 years eago, it has burnt out its economic and military resources maintaining a dying empire, getting caught in costly and pointless wars. All the old hegemon can do is grumble.

Once more, financialisation.

US economic independence from Britain also involved the development of financial markets in New York and Chicago to rival London. New financial centres – particulary Hong Kong, but also local markets elsewhere in Asia, and in Latin America – are developing.

But what's interesting is that the markets in London and New York have been growing even faster. "First world" GDP has been growing much slower than in the "emerging markets"; "first world" manufacturing is in decline; the only part of the first world economy that races ahead is finance.

A couple of things really show the shift towards finance in countries like the US and UK. One is where profits come from

Global shift.

We made a list above of some of the reasons why the US was able to successfully escape its "periphery" status and overpower British and hegemony. Now we can see how China, and also India and other former "third world" economies, fit the picture.

- *investment* capital – accumulated through high national savings, largely centralised and controlled by the State and mega-corps;
- *cheap labour*: millions of impoverished rural labourers flocking to the cities in search of work, in scenes reminiscent of the birth of Industry in Europe, only on a much bigger scale;
- *new technologies*: production line industry taken to a new scale.

There are also differences. China and India do not follow the import substitution model. Their manufacturing is mainly for export. Local consumer markets are developing, but not fast enough to keep up with production. (Which is why Chinese

innovations included the foundation of the Bank of Amsterdam in 1609, possibly the world's first ***central bank****, guaranteed by the City government. The Bank of Amsterdam began to expand on the old deposit banking model by (secretly) issuing overdrafts: letting depositors take out bank notes (receipts) for more than they had deposited. The Dutch East India Company was the world's first issuer of both listed shares and corporate bonds.*

By the 18th century England had taken over the role of leading capitalist state. The Bank of England was established in 1694, copying the Amsterdam model. It was set up by Scottish merchant William Patterson in a deal with the government, which used it for military financing. The first loan, for £1.2 million at 8% per annum, funded the re-building of the Royal Navy.

England also led the way in advancing bond "technology", issuing large standard issue "Treasury Bonds" that were widely traded in the coffee shops of London. From 1694 on the British state has been continually in debt, largely from war financing – its debt first rose over 100% of GDP in the 1750s, and stayed there for more than a 100 years.

The use of paper money took off in the 18th century. In 1844 the Bank of England was given an effective state monopoly (in London) on printing bank notes. Before then, any bank could issue as much "money" as it wanted – it was up to customers to decide if they trusted its reliability or not.

New Bank of England notes had to be backed 100% by reserves either of gold or of government bonds. I.e., the Bank had to keep the same value of either gold or Treasury bonds in its vaults to match the paper money it issued. The Bank became the "lender of last resort" to commercial banks: if they got into trouble, the central bank would lend them the money to cover any "bank run".

Similar "gold standard" models were adopted around the world

in the late 19th century. States either held their own gold and silver reserves, or pegged their currencies (fixed their exchange rate, and so limited the printing of new money) to Sterling or the US dollar. This system remained generally intact until the 1929 crash.

By the end of World War II the United States had clearly taken over from the UK as biggest capitalist power. The UK government was crippled by its war debts: 250% of GDP in 1945. In the Bretton Woods agreement of 1944, a new world monetary order was agreed which fixed most world currencies to the US Dollar. US Treasury Bonds became the ultimate "safe" asset against which risks and interest rates on all other debt was measured. And the World Bank and IMF, based in New York, were set up as "lenders of last resort" – and financial policemen – for the world economy.

In 1971, the US left the Bretton Woods agreement, unable any longer to support the world financial system, as its own debts — again, largely war debts, from Vietnam — massed up.

In the 1970s and 1980s, the US and other "advanced" capitalist countries followed neoliberal policies and "deregulated" their financial markets, allowing banks and brokers to develop whole new types of banking and financial markets involving **derivatives** *and* **securitisation**. *As manufacturing industry increasingly switched to the "developing world" (see Workshop 3), the finance "industry" became the leading edge of capitalism in the US and UK.*

For much more, see: **David Graeber – *Debt, the first 5000 years.***

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The share or percentage of income that is saved and invested is called the *savings rate*. There is a lot of discussion amongst economists about how people make "savings decisions". Generally speaking, the more income people have, the more they are likely to save. If your wages are near starvation level, you will spend everything you earn on food.

Here are some figures on national savings rates (as a percentage of GDP):

	1990	2000	2008
China	39.2	36.8	54.3
India	23	23.8	33.6
Mexico	23.6	23.8	25.5*
UK	16.4	15	15.6
US	15.3	17.7	12.1
Germany	25.3	20.2	26

(Source: Bank for International Settlements; *data for 2006.)

How does that add up? People in China and India are, on average, much poorer than people in the UK and Europe. And poor people usually consume a higher proportion. But, luckily for their rapid economic growth, Chinese and Indian "national incomes" are far from distributed equally amongst the population. Besides the "new rich", who do their best to spend at least some of it on luxury living, a lot of China's income is still controlled by the State and state-linked corporations, who pursue a planned policy of investment and growth. Not all strongly hierarchical and authoritarian economies are booming; but inequality and centralised control certainly can be key factors in rapid growth.

GDP is, effectively, the total *revenue* from all the production of a national economy. As we saw in workshop 1, some of the revenue of a capitalist production process goes to cover the costs: wages (labour costs); raw material costs; and finance costs (interest payments). The rest is the producer's profit. Out of the profit, the capitalist has to decide how much to re-invest in future production; and how much to "consume" herself.

We can do the same kind of breakdown on a bigger (national) scale. GDP is the (money) value of all stuff produced in a national economy. Some of that stuff will go to workers, as wages. Some will go to investors, as interest and dividends. Some will go abroad (exports). Some will go to the government, in taxes from workers and investors and on exports.

There are two things that workers, investors, and governments can do with their share of the national product. They can consume it, or save it.

What is consumption? Roughly: if a commodity is consumed, it is taken out of economic circulation. If I eat (consume) a chocolate bar, it leaves the economic system and enters my digestive system. It can no longer be traded, or used as raw material for a cake.

Alternatively, I can hide the chocolate bar under my bed for a rainy day. This is a form of *saving*. But, on the whole, most people with money don't save it by hiding it under the bed. They either deposit it in banks, who then lend it on; or invest it in shares, bonds, and other markets. These forms of saving thus involve re-investing capital, through financial markets, back into production. Thus a basic assumption of macroeconomic theory: *Savings = Investment.*

"Fotia stis trapezes" = Fire to the banks.

A snapshot of world financial markets.

The table below shows global assets: the amounts of the different kinds of securities in existence at that point. All figures are in trillions of US dollars (a trillion = a million million). Debt securities include bonds and short term *notes* – like bonds, but with maturities of a year or less. Private debt securities are bonds and notes from financial issuers (banks) and corporates.

	1990	2000	2007	2008
Total assets	**$48 tr**	**$112 tr**	**$194 tr**	**$178 tr**
equities	10	37	62	34
private debt secs.	10	24	48	51
govt. debt secs.	9	17	29	32
bank deposits	19	34	56	61
World GDP	21.2	37	56.8	60.7

The table shows how world financial markets grew massively in the 1990s and 2000s, up until the crash. This was the neoliberal boom period of "*financialisation*".

Both equity and debt markets shared in the boom. Government and private debt both boomed, but especially non-government debt. In earlier times, debt markets were mainly made up of government bonds, and only the very biggest companies issued bonds. Now it is common for corporates, and especially banks and other financial institutions, to borrow lots of money on the bond markets.

The next table breaks down the figures geographically:

Total financial assets ($ trillion)	2007	2008
US	60.4	54.9
Eurozone	43.6	42
Japan	28.7	26.3
China	14.4	12
UK	8	8.6
Latin America	4.1	3.9
"Emerging" Asia	4.2	3.8
Russia	1.9	1.1
India	2.6	2
Eastern Europe	4.3	1.5

Source: McKinsey Global Institute report.

Note how the most "developed" countries are far more "financialised". China in fact produces around 22% of the world's GDP – but less than 8% of financial assets are Chinese.

The price of our blood, sweat and tears.

GDP averages hide the vast inequalities within countries. And inequality in "third world" countries is typically more extreme than in "developed countries", where worker organisation has gained some concessions like higher wages and welfare services. Here are some figures on average hourly wages in manufacturing industry, as estimated by the US Bureau of Labor Statistics.

Germany	$26.90
US	$23.03
UK	$21.14
Greece	$10.38
Brazil	$4.45
Mexico	$3.93
Philippines	$1.13
China	$0.81

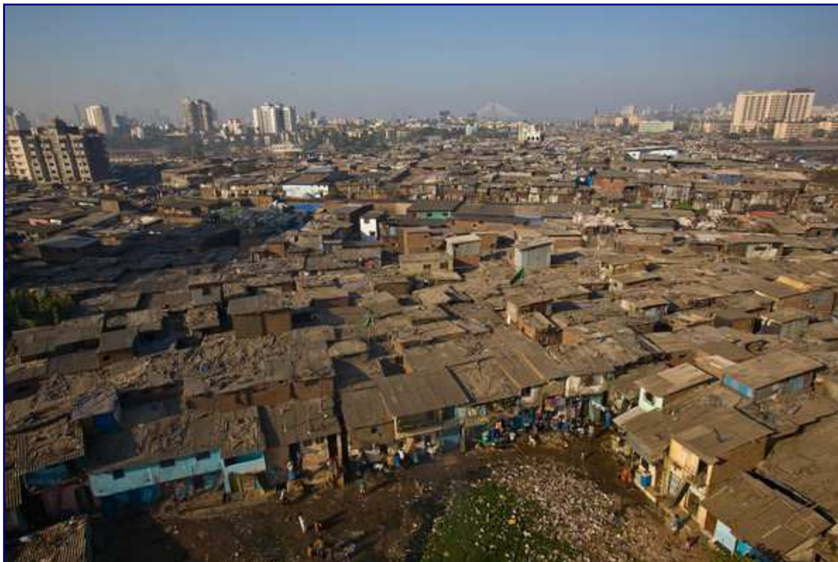
Note: data from 2010, except China from 2006.

Investment vs. consumption.

The table above shows that manufacturing wages in the US and Western Europe are more than 20 times higher than in China. The first table in this workshop showed that US GDP per head is 4 to 5 times higher than in China. So, most of China's high growth is not paid out as factory wages. Some of it goes into the pockets of China's "new rich". Most of it, though, is not consumed but *invested* back in production. I.e., spent on new capital: new factories, new machines, more raw materials and energy, to produce even more stuff.

goods. They used import tariffs and *state subsidies* to “nurture” “infant industries”.

ISI largely failed. These countries were not strong enough, economically or militarily, to take on the US. If they introduced import tariffs, core countries could retaliate with tariffs attacking their exports. Most of their income still came from exports, and local consumer markets could not fill the gap. The rich elites could afford to buy better quality imported luxuries. Most locals were just too poor to buy anything.



Dharavi slum, Mumbai. Rapid industrialisation means rapid urbanisation.

If these *trade wars* weren’t enough to keep third world states in their place, the US could resort to other means. Across Latin America in the 1970s, the US launched coups to impose governments that dropped ISI and kept to their place as raw material exporters. (See William Blum’s “*Killing Hope*” for a bloody history of US military interventions since 1945).

Meet the investors.

Who are these capitalists? Shareholders are, technically, the owners of companies and their capital. Bond investors and lenders (including bank depositors, who “lend” to banks) are the owners of “financial capital”, and get their share of the profits in the form of interest.

It is not so easy to get figures on capital ownership. The sums below are estimates by lobbying group “TheCityUK” of the size of global investment funds.

	$ Trillion
Private wealth	42.7
Pension Funds	29.9
Mutual Funds	24.7
Insurance Companies	24.6
Sovereign Wealth Funds	4.2
Private Equity	2.6
Hedge Funds	1.8

It's hard to know if those numbers are at all accurate. Note that they don't match up with the capital markets figures before – but then they miss out other major investors, which include banks and corporations. "Private wealth" means rich individuals and families, who do control a lot of the world's capital. But "institutional investors", put together, control more.

Institutional Investors manage the pensions, savings, and insurance premia of the world's middle classes and better off workers. As with share ownership, we should distinguish legal ownership from actual control. Technically, these assets may be owned by individual savers; in practice, they are controlled by executives, ***fund managers***. These companies decide where to invest the funds they manage, and take a percentage of the profits.

Some of these funds are bigger than large countries. Here are the top ten in the "Pensions & Investment" 500 (as of 2009). The amounts are their "assets under management" (AuM).

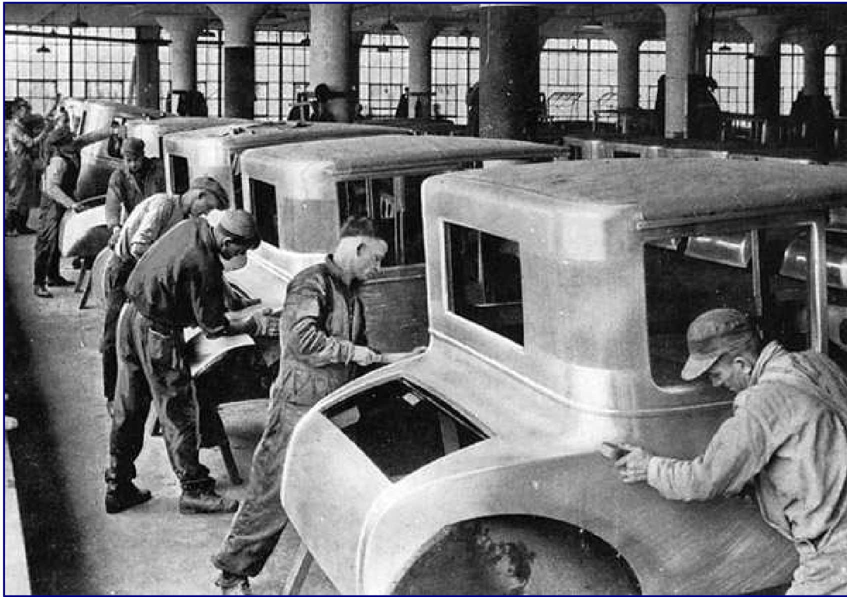
	$ trillion
BlackRock	3.35
State Street Global	1.91
Allianz Group	1.86
Fidlity Investments	1.7
Vanguard Group	1.51
AXA Group	1.45
BNP Paribas	1.33
Deutsche Bank	1.26
JP Morgan Chase	1.25
Capital Group	1.18

succeeded were:

- they had big enough capital reserves for the initial *investment*;
- new *technologies* – including "*Fordism*", the production line methods pioneered by Ford Motors — gave them an advantage;
- whereas Britain was stuck in old technologies – and with all their existing infrastructure in place, it was expensive for British capitalists to switch to copy the new American models;
- they had *cheap labour* from mass immigration, whilst British labour was getting more expensive, due to workers organising and fighting;
- alongside the development of manufacturing, the US state and capitalists built up *local financial markets*, so that industrialists didn't have to go to London to raise money;
- *protectionism* – the US government offered support to domestic industry by imposing high taxes (trade tariffs) on imported goods;
- but protectionism is only possible if existing core states allow it – the decline of British *military power* meant the empire was too weak to use force to defend "free" markets for its goods.

"Kicking away the ladder."

In the 1950s and 60s, "third world" states in Latin America and Asia tried to follow the US example and use protectionist policies to develop national manufacturing industries. This policy was known as "Import Substitution Industrialisation (*ISI*)" – building industry to substitute local products for imports of advanced



Ford assembly line in 1927.

"Development".

How can a country move from periphery to core? The problem is that advanced manufacturing production needs serious capital investment: factories, complex machines, energy plants, transport infrastructure, etc. These advanced goods are very profitable – but you need massive investment to get started. And that is assuming core producers allow access to advanced technologies and markets.

In the early 19th century the US was still a periphery country, producing grain and cotton for the British empire. But this was profitable business, and US capitalists were able to build up a surplus of finance capital for investment. They started to invest it in building up local manufacturing industry which could eventually compete with Britain. Some of the reasons they

Buy, sell … and in the middle.

In between borrowers and investors come a host of middlemen, including:

- *Stockbrokers* – middlemen who buy and sell shares for their investor clients
- *Traders* – who buy and sell bonds and other securities for clients
- *Underwriters* – bankers who buy bonds off a borrower when they are first issued, then sell them on to the market
- *Insurers* – e.g., offer insurance in case investments default
- *Structurers* – arrange complex securitisation bonds (see below)
- *Derivatives dealers* – see below
- *Lawyers* – lots of them
- *Analysts* – analyse securities to decide how risky they are, and what they should be worth
- … and more.

Arranging tricky financial deals is one of the best paid parts of banking. The fees are usually a tight secret. Traditionally, these roles were filled by brokers and specialist ***investment banks***. In 1933, following the financial crash, the US State passed the "Glass-Steagal" act to regulate and keep investment banking divisions separated from traditional deposit-based "commercial" banking. This law was repealed in 1999, and the same multinational banks now control both "commercial" and "investment" banking.

Risk and return.

The basic principle of pricing a security: the riskier it is, the more profit or *return* (i.e., interest) it should pay. Traditionally, US Treasury Bonds have been considered the ultimate "safe haven",

and so paid the lowest interest rates. The assumption is that the US government will never go bust, and will always honour its debts. The coupon (interest rate) on US Treasuries is used as a "benchmark" for pricing other debt.

The ***spread*** of a bond is the difference between its interest rate and the rate on another bond. For example, after the failure of the G20 meeting in November 2011, the spread on Italian over German 10 year bonds went to 459 basis points (4.59%, one basis point = 0.01%). I.e., markets demanded an extra 4.59% return to buy Italian instead of German bonds.

(***Note – slightly more technical***: When bonds are first issued they is usually sold, in large multiples, with a "face value" of 100 cents each. Suppose the coupon rate is 4%. Then each bond pays an annual interest of 4% of 100c = 4c. But if traders feel that the bond has become more risky, it will now be sold on at a discount – e.g., its ***price*** goes down to just 80c. It still pays 4c interest every year, so a new buyer is getting the same return for a lower investment. Bond traders say that the ***yield***, or return relative to price, has gone up to 4c/80c = 5%. Higher risk, higher return. Italy's yield in that example above was 6.66%. Of course, if the bond actually defaults, the investor gets nothing at all.)

Rating agencies.

The infamous ***rating agencies*** – the bug three are Moody's, Standard & Poors, and Fitch – are companies that specialise in assessing the risk of debt securities. They publish a rating from AAA (the highest) down to D (default) depending on how likely they believe a bond is to default. For many kinds of bond, they are paid on commission by the borrower issuing the bond. So, obviously, they are completely impartial.

and capital, market power was further increased by the sheer size of their resources.

The British state used its share of this accumulated wealth to create the world's most powerful military machine. Business and government worked together to "open" new markets and property systems with a mixture of trade and force. This did not always require direct colonisation: e.g., in the Opium Wars, and the smashing of the Boxer Rebellion, Britain and other capitalist states forced the Chinese government to allow the trade in opium and other goods.

Nor should we ignore ***cultural power***: missionaries, doctors, teachers, and other settlers, helped spread the new values, norms, and desires of the capitalist property system.

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Hegemony?

The greek word **hegemon** *(ruler, leader) is sometimes used for a state like Britain in the 19th century, or the US and USSR in the 20th, which dominates world politics and economics.*

But this concept shouldn't be over-used. In the 19th century, there were large areas of the world still uncolonised. For much of the 20th century there were two main rival powers. Even on its own home turf, a state or elite's power is never total: there are competing factions and interests within the elite; and free spaces and pockets of resistance where domination is much weaker.

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goods; the local countryside was their periphery. Colonialism mader core/periphery systems go global. In the 19th century, Britain was the biggest "core" of the global trade system. Its products involved skilled labour, for (relatively) high wages, and advanced technology. It was also the site of the financial markets.

The "periphery" of the empire produced the raw materials. The early economic role of the United States was largely as a mass grain producer for the Imperial market. India's own cotton maunfacturing industry was destroyed, and India became an intensive producer for raw cotton shipped to the mills of Lancashire. The ***Atlantic Slave Trade*** and ***Indentured Labour*** provided cheap (or free) labour for agriculture and raw materials production.

How did Britian become dominant? Britain's initial advantage came from new technologies: not only cotton mills and steam engines, and new weapons; but also new financial, legal, and cultural "technologies". Technology gave British industrialists a ***competitive advantage*** – they could produce better goods, more cheaply – and their manufactured products took over world markets.

Where capitalists in other countries could not compete with British manufacturing, their profit opportunities came from exploiting cheap labour and natural resources to produce raw materials. So the local capitalists – plantation and mine-owners, etc. – of periphery countries also gained in the core/periphery division.

Imperialism involved both ***market power*** and ***military power*** working together. Technological advantage gave the British capitalists their initial market power. As they accumulated wealth

Many funds base their investment decisions on rating agency reports. Market prices are often guided by ratings. Also, pension and some other big funds are restricted by regulation to only buy ***investment grade*** bonds, bonds with ratings of BBB and over.

The new finance 1: securitisation.

The great housing boom of the last 30 years was fuelled by a new kind of bond market. In the US, until the 1970s mortgage lending was largely done by small local lenders called the "Savings and Loans" or "Thrifts", the equivalent of UK building societies. This sector was deregulated in 1980 and 1981, and later many of the "S&L"s were hit by crisis and went bankrupt. Investment banks made this crisis into an opportunity. They bought up mortgages from the crashing S&Ls for cheap and moved into the mortgage industry. To help things along, the loans were guaranteed by US federal government agencies with cute names (Freddie Mac, Fannie Mae, etc.).

Unlike traditional mortgage lenders, investment banks didn't have deposits which they could use to make mortgage loans. Instead they invented a new technique called ***mortgage backed securitisation*** (MBS). They borrowed money by issuing bonds secured against the expected repayments on the mortgages.

This relied on a legal structure called a "special purpose vehicle" (SPV). The mortgage borrowers pay their repayments into the SPV over, say, the next 20 years. A bond is issued in the name of the SPV, and the SPV pays out bond interest to investors. The interest paid out to the bond investors is lower than the interest paid in by the mortgage borrowers. The investment bank sits in the middle and pockets the difference. At first the new idea was strange to analysts and investors. But the federal government guarantees meant the bonds got a AAA rating anyway. Then the markets got used to the idea. Car loans and credit card loans were the next targets for securitisation.

"***Shadow Banking***". Securitisation slashed away the old deposit banking model. Banks could lend out large sums to new hordes of

and a ***periphery***. The core is where high-technology, high-skilled, capital-intensive, production happens. These are usually the later stages in the production process. The periphery produces the raw materials which are shipped to the core. Some of the finished goods may then be shipped back to consumers in the periphery. The core is also where trading and organisation functions, such as financial markets, are based.

This division of labour makes the periphery dependent on the core: it cannot produce the finished goods on its own. Strictly speaking, core and periphery are dependent on each other. But the core has the advantage as its goods are more specialised, harder to produce, and more prestigious.

Imperial history.
In pre-capitalist civilisations, and in early capitalist Europe, commercial ***cities*** were cores, producing and trading the advanced

by women; or "black" work, like the work of illegal migrants. And, of course, GDP only measures commodities, things that can be bought and sold in markets. Using GDP as a measure of goodness or "quality of life" supposes, as economists do, that our well-being just involves accumulating and consuming commodities.

Why is economic growth the one great goal of democratic politics? Policies that chase growth certainly help capitalist profits. And they avoid questioning the **distribution** *of wealth: if everyone gets richer as the economy grows, we can all have more stuff without having to take it away from the rich. Questioning the distribution of wealth is labelled the "politics of envy". Questioning the very idea of commodification, of economic growth, or of what never-ending increased production means for our planet, is just crazy talk. (We will look at this issue again in Workshop 6).*

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What explains global income inequalities?

Neoliberal economists argue that it is all about the internal systems of countries. "Poor" countries (Latin America, India, Africa, etc.) have failed to keep up with world growth because of weak institutions: corruption, weak democracy, and above all a lack of strong property law. (The Peruvian economist Hernando de Soto is the master of this line – see his "*The Mystery of Capital*".) So is it just a coincidence that these "poor" economies used to be colonies of the successful capitalist nations?

Core and periphery.

According to the "***world systems theory***" of capitalist development, political-economic systems typically have a ***core***

customers, but without needing to get in any deposits. In the 90s and 2000s a new wave of "specialist finance companies" got in on the act, selling credit cards and mortgages from call centres, paper companies funded entirely by securitisation. This consumer credit boom spread from the US through UK and Europe. By 2000 the gobal investment banks were arranging securitisation deals from Mexico to Kazakhstan. In the US, the new frontier was "sub-prime": including mortgages to people with dubious credit ratings; funded by bonds sold to investors hungry for higher returns.

The new finance 2: derivatives.

The idea behind derivatives is not really new. The Greek philosopher Thales is said to have made a fortune on ***futures*** contracts. Predicting a great harvest, he placed orders with olive farmers for their whole autumn crop, agreeing a fixed price in advance. When the harvest came he got masses of olives cheap, and sold them on at a profit.

In general, a futures contract is an advance agreement to pay a set price for a good at a future date. When the future date comes around, if the market price for the good is higher, then the *buyer* of the futures contract makes a profit; if it is lower, then she loses the difference. The first standardised futures exchange began in Chicago in 1865, where farmers and traders could agree futures contracts for wheat harvests.

But the derivatives market really took off after the collapse of the Bretton Woods fixed currency exchange system in 1971. Fluctuations in international interest and exchange rates became crucial in financial deals. For example, a business looking to invest in a different country could use derivatives to fix the exchange rate it would pay in the future.

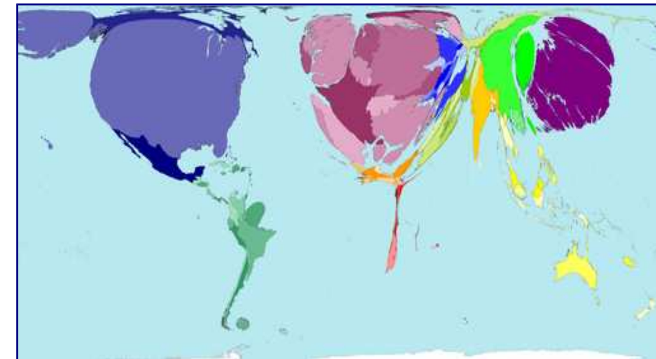
On the one hand, derivatives offer a form of insurance. If I buy a futures contract to change money next year at today's rate, then effectively I insure against the risk that the rate goes up and I have to pay more than the current price. However, I give up the chance to save money if the rate actually goes down. This use of derivatives is called ***hedging***.

On the other hand, derivatives can be seen as a form of gambling, or ***speculation***. The other party in the currency futures contract may gamble that the rate will go down, and so make them a profit. Derivatives markets look even more like gambling when neither of the parties has any involvement in the actual good (wheat, currency) except the hope of a speculative gain. Two parties could make a contract just because they are betting different ways about what will happen to a ***reference asset*** – whether it's an interest rate, a currency, the weather, or the chance of someone else paying their mortgage.

An ***option*** is a contract that gives a party the choice to buy an asset at a set price in the future – or not to buy. Other types of derivatives include ***swaps***, *swaptions*, and more. The biggest class of derivatives contracts today are interest rate derivatives. These are used to hedge against the risk of losing out on investments which pay a return linked to a major interest rate.

As the securitisation market took off, investment bankers invented *credit derivatives*. ***Credit default swaps*** (***CDS***) and ***Credit Default Obligations (CDOs)*** are insurance contracts – or, seen another way, gambles – about whether debts will default or not. There is now a major market in CDS contracts on sovereign bonds. CDS agreements also became routinely written in to mortgage securitisation deals, helping investors reduce their risk by hedging against defaults. A scandal broke, though, when it emerged that

seven times more (per person) than China. By 1970 it produced 20 times more. World income has doubled again since 1970. This includes the "developed world". But the most growth is in Asia: China has grown nine times richer, India four. Only Africa has been left out.



Map resizing countries by proportion of world GDP — from http://www.worldmapper.org/

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GDP?

GDP stands for "gross domestic product". Roughly, it means the value of all the marketable goods and services produced in a country. Economic **growth** *is the increase in a country's GDP over time.* **GDP per capita** *is the country's GDP divided by the number of people in the population: i.e., the average GDP.*

Economists use GDP as the standard measure of economic wealth and prosperity. And, often, as the measure of all goodness and "progress" in the world. But focusing on GDP hides many issues. Average GDP figures ignore the inequality of income distribution within a country. GDP statistics only reflect production that is known to the state, usually recorded in tax returns, and so ignore unpaid and unseen work: including domestic work, largely done

Global incomes.

The table below shows some of the global income statistics estimated (or “guesstimated”) by the economic historian Angus Maddison. They calculate income as GDP per person (annual income measured in 1990 dollars).

	1000	1500	1820	1900	1970	2008
W. Europe	427	771	1194	2885	10,169	21,672
US	400	400	1257	4,091	15,030	31,178
Ex USSR	400	499	688	1237	5,575	7,904
L. America	400	416	691	1,113	3,996	6,973
China	466	600	600	545	778	6,725
India	450	550	533	599	868	2,975
Africa	425	414	420	601	1,335	1,780
World Average	453	566	666	1,261	3,729	7,614

Of course, these figures are mostly just wild guesses, and ignore massive differences in economic systems. Including differences in what cultures consider as tradeable *commodities* at all. But they at least bring out some basic points. If we do measure prosperity in terms of the sheer quantity of tradeable stuff around, then the world has got much richer under capitalism. Average incomes around the world stayed pretty much the same in the centuries before the industrial revolution and capitalist take-off. China had more stuff that Europe in the millenium or so after the fall of Rome, but not dramatically more.

Then it all took off. In the early nineteenth century European and North American income was double the levels in the rest of the world. But this was just the beginning. By 1900 the US produced

investment bank Goldman Sachs had used CDS deals to gamble that sub-prime bonds it had issued itself were going to explode – the financial markets equivalent of match fixing.

Complex CDO contracts involving bets on packages of mortgage and other debt became another way to expand the securitisation industry. They spread the “exposure” to risk on sub-prime mortgages and other debts to wider ranges of investors. CDO investors never actually had to buy any mortgages or bonds, just bet about what would happen to debts other people were buying. Investments in these deals are usually confidential, and the sums complex. Whole new levels of complexity were reached with “***CDOs-squared***”, and even “***CDOs-cubed***” – bets about bets about bets on debt defaults.

Just who else will be in trouble if a mortgage in Wisconsin defaults? Has anyone kept track?

The hand of the market?

Workshop 3. The global division of labour.

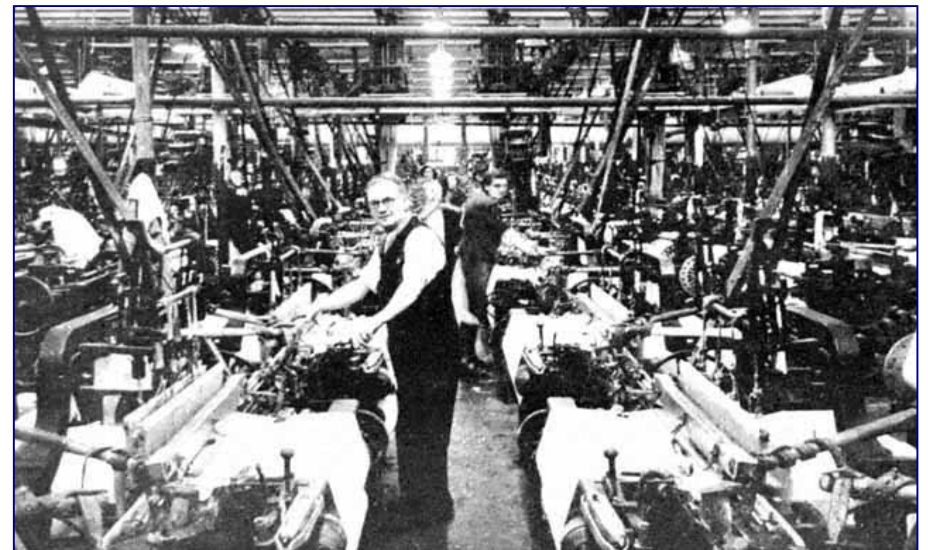
Textile mill in Xiaoxing, Zhejiang Province, China. 2004.

In 2011 China became the world's largest producer of manufactured goods, overtaking the United States, top producer for the last 110 years. China, India, and other Asian countries are now the "factories of the world", the main centres of production for most of the tangible things we buy and use, from cars to computers to crockery. Just as they were 200 years ago, before European capitalist expansion.

Other "developing countries" in Latin America, Africa, the Middle East, as well as Russia, provide most of the basic raw materials – fuel, metals, minerals, etc. – to run those factories. The "developing world" – or should we now call it "the productive world"? – also produces most of the world's food. But all this

wealth is still largely ***consumed*** in Europe and North America. How does that work? And how long can it carry on?

A recap. Capitalists chase profit. They can make profit "directly" by producing and selling commodities. Or "indirectly" by getting interest from investing finance capital; or by acting as middlemen, for a fee. Profit = revenues – costs. So to boost profits producers need to increase revenues, or reduce costs. To increase revenue they need to find higher demand for their products: more buyers; or buyers who will pay more. There are two main routes to reducing costs: more efficient production technologies; or cheaper inputs. New inventions and technological advances boost profits and production. So do finding new sources of cheap materials – or cheap labour. So the hunt for profits drives the ***expansion*** of capitalism in a number of ways, as capitalists try to find or create new markets. New consumer markets to buy their goods; new sources of raw materials; and new sources of cheap labour.



Textile mill in Blackburn, Lancashire, UK.