

The “Great Financial Crisis”: A whole new kind of struggle is emerging

Interview with John Bellamy Foster

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MW: The financial crisis is quickly turning into a political crisis. Already governments in Iceland and Latvia have collapsed and the global slump is just beginning to accelerate. Riots and street violence have broken out in Greece, Latvia and Lithuania and worker-led protests have become commonplace throughout the EU. As unemployment skyrockets and economic activity stalls, countries are likely to experience greater social instability. How does one take deep-seated discontent and rage and shape it into a political movement for structural change?

JBF: The first thing to recognize is that we are suddenly in a different historical period. One of my favorite quotes comes from Gillo Pontecorvo's 1969 film *Burn!*, where the main character, William Walker (played by Marlon Brando) states: "Very often between one historical period and another, ten years suddenly might be enough to reveal the contradictions of an entire century." We are living in such a period; not only because of the Great Financial Crisis and what the IMF is now calling a depression in the advanced capitalist economies, but also because of the global ecological crisis that during the last decade has accelerated out of control under business as usual, and due to the reappearance of "naked imperialism." What made sense ten years ago is nonsense now. New dangers and new possibilities are opening up. A whole different kind of struggle is emerging.

The sudden fall of the governments in Iceland and Latvia as a result of protests against financial theft is remarkable, as are the widespread revolts in Greece and throughout the EU, with millions in the streets. The general strikes in Guadeloupe and Martinique, the French Antilles, and the support given to these movements by the French New Anti-Capitalist Party is a breakthrough. In fact much of the world is in ferment. Latin Americans are engaged in a full-scale revolt against neoliberalism, led by Venezuela's Bolivarian Revolution, and the aspiration of a new socialism for the 21st century (as envisioned also in Bolivia, Ecuador and Cuba). The Nepalese revolution has offered new hope in Asia. Social struggles on a major scale are occurring in emerging economies such as Brazil, Mexico, and India. China itself is experiencing unrest.

The one place in the world where this world historical ferment appears to not be having telling effect at present is the United States. This can be traced to two reasons. First, the United States as the center of a world empire is a fortress of conservatism. Second, the election of the Obama administration has confused progressive forces, leading to absurd notions that the Democrats under Obama are going to create a New New Deal without renewed pressure arising from a revolt from below. Meanwhile, under Obama's watch, and with the help of his chosen advisers, vast amounts of state funds are being infused into the

financial system to benefit private capital.

What is needed in the United States today, we argue in *The Great Financial Crisis*, is a renewal of the classic concept of political economy (with its class perspective), whereby it comes to be understood that the economy is subject to public control, and should be wrested from the domination of the ruling class. The bailing out of the system right now is going on with taxpayer funds but without the say of the public. A revolt to gain popular control of the political economy is therefore necessary.

It is possible to start with the demand for a New New Deal rooted in the best legacy of the Roosevelt administration in the 1930s, most notably the Works Progress Administration. But as Robert McChesney and I argued in “A New New Deal Under Obama?” in the February 2009 issue of *Monthly Review*, the struggle has to move quickly beyond that to an expansion of workers’ rights along socialist principles, breaking with the logic of capital. For this to occur there has to be a great revolt from below on at least the scale of the industrial unionization movement of the 1930s that created a new political force in the country (later destroyed in the McCarthy Era). The story of this struggle is told in David Milton’s classic account, *The Politics of U.S. Labor*, which also points out that the rising labor movement was led by socialists and radical syndicalists.

It is important, as István Mészáros explained in his *Beyond Capital*, that the radical politics opened up in this historical moment not be diverted into attempting to save the existing system, but be directed at transcending it. As Mészáros wrote: “To succeed in its original aim, radical politics must transfer at the height of the crisis its aspirations—in the form of effective powers of decision making at all levels and all areas, including the economy—to the social body itself from which subsequent material and political demands would emanate.”

In the United States a primary goal of any radical politics should be to cut military spending, which is the imperial iron heel holding down the entire world, while corrupting the U.S. body politic and diverting surplus from pressing social needs.

The obvious weak link of the whole political, ideological and economic structure in command in the United States today, is that the system has clearly failed to meet peoples’ real needs. Rather than addressing these pressing needs in the crisis, the emphasis of the economic overlords is to bailout private capital at virtually any cost. Between October 2008 and January 2009 the federal government provided about \$160 billion in capital and infusions and debt guarantees to the Bank of America, which had a total net worth in late January of only a small fraction of that amount. The rest had gone down the rat hole.

The robbing of public funds to bailout private capital is now on a scale probably never before seen. A politicized, organized working class capable of understanding and reacting to that theft, and choosing thereby to restructure society, to meet real social, egalitarian needs is what is now to be hoped for. The title of a recent cover story *Newsweek* declared: “We Are All Socialists Now.” As it turned out, *Newsweek*’s editors were simply referring to the increase in public spending now taking place—hardly an indication of socialism. But the fact that this is said at all in the mainstream media points to the fact that we are in a different historical moment in which radical forces have the possibility of moving forward.

MW: As the economy has become more dependent on financialization for growth, the gap between rich and poor has grown wider and wider. As you point out in your book, “In the

United States the top 1 percent of wealth holders in 2001 owned more than twice as much as the bottom 80 percent of the population. If this was simply measured in terms of financial wealth, the top 1 percent owned more than four times the bottom 80 percent.” (p 130). How have working class people managed to keep their heads above water with all this wealth being shifted to the rich?

JBF: The answer is fairly obvious. If people cannot maintain their standard of living on the basis of their income, they will borrow against income and against whatever wealth they have. The result—if their incomes don’t rise, or if the value of whatever assets they have do not increase—is that they will simply get deeper and deeper in debt in an attempt simply to stand still. I became concerned about the growth of working-class household debt in 2000 and carried out a study of The Survey of Consumer Finances, which is published every three years by the federal government with a three year lag in the data. This is the only major federal government data source that we have on household debt broken down into income groups so that we can determine the debt burden of different classes.

I published an article based on this research in the May 2000 issue of Monthly Review entitled “Working-Class Households and the Burden of Debt.” I then followed this up six years later with an article in the May 2006 Monthly Review on “The Household Debt Bubble,” which was to be incorporated into The Great Financial Crisis. There I wrote that “The housing bubble and the strength of consumption in the economy are connected to what might be termed the ‘household debt bubble,’ which could easily burst as a result of rising interest rates and the stagnation or decline of housing prices.” This is of course what happened, and the reason why this crisis has turned out to be so severe was the destruction over decades of the finances of working-class households, on the back of which financialization took place.

MW: Will you define “debt-deflation” and explain its potential danger to the economy? As credit continues to tighten and housing prices sink; aren’t we slipping into a reinforcing deflationary spiral? Do you think that fiscal policy will reverse this trend or is the stimulus package too small to stop real estate and equities from continuing to slide?

JBF: The term “debt-deflation” is associated particularly with the work of Irving Fisher during the Great Depression. Fisher wrote an article for the journal *Econometrica* in 1933 entitled “The Debt-Deflation Theory of Great Depressions.” Deflation as applied to the general economy is a drop in the general price level, something not seen in the United States since the Great Depression, and catastrophic in the economy of monopoly capital (and even more so under monopoly-finance capital). In the first place, deflation (or disinflation, i.e. the reduction of inflation to what the Federal Reserve calls “below optimal” levels) means that the profit margins of corporations are squeezed, even if the cost structure of production, and productivity remain the same. Under these circumstances price competition is reactivated with giant firms actually in a life and death struggle. This also generates pressure for heavy layoffs and wage reductions, creating all sorts of vicious cycles.

But the real fear of deflation has to do with the enormously bloated financial structure and the huge debt load of the economy. Under inflation, which is usually assumed to be built into the advanced capitalist economy, debts are paid back with smaller dollars (that is, worth less over time). In a deflationary economy, however, debt has to be paid back with bigger dollars (worth more over time). This then creates a debt-deflation spiral, enormously accelerating financial meltdown. As Fisher put it, “deflation caused by the debt reacts on the

debt. Each dollar of debt still unpaid becomes a bigger dollar, and if the over-indebtedness with which we started was great enough, the liquidation of debt cannot keep up with the fall of prices which it causes.” Stated differently, quoting from *The Great Financial Crisis* (p. 116), “prices fall as debtors sell assets to pay their debts, and as prices fall the remaining debts must be repaid in dollars more valuable than the ones borrowed, causing more defaults, leading to yet lower prices, and thus a deflationary spiral.” In order to check this deflationary tendency, the Federal Reserve and the Treasury have been trying to reflate the economy by printing money (euphemistically called “quantitative easing”). But they have not succeeded and deflationary forces are still very strong, causing President Obama to warn shortly after his election that “we now risk falling into a deflationary spiral that could increase our massive debt even further.”

It is also worth mentioning the effect that deflation has on investment. With capital faced with the fact that a few years down the line the price level could be lower than it is now, expected profits on investment in new productive capacity (given that this takes years to be built and has to be paid for in current prices) are depressed, creating a deeper stagnation of accumulation.

The stimulus package introduced by the Obama administration is far too small to pump up demand and reflate the economy under these circumstances. It is less than \$400 billion a year, forty percent of which is tax cuts, so that the increased governmental spending is minuscule compared to the size of the hole created by the drastic drop in consumption, investment, and state and local government spending. It is also dwarfed by the total federal government support programs, primarily to financial institutions, which now amount to more than \$9.7 trillion in the form of cash infusions, debt guarantees, swaps of Treasuries for financial toxic waste, etc.

MW: Karl Marx seems to have anticipated the financial meltdown we are now facing. In *Capital*, he said, “The superficiality of political economy shows itself in the fact that it views the expansion and contraction of credit as the cause of the periodic alterations of the industrial cycle, while it is a mere symptom of them.” Marx appears to agree with your theory that the real problem is deeper—economic stagnation which forces surplus capital to look for more profitable investments. While the monetarist theories of Milton Friedman are now under withering attack, Keynes and Marx seem to have held up rather well. What does Marx mean when he talks about “political economy”?

JBF: Marx was an acute analyst of financial crises in his time and described their main features. However, he saw financial expansions as occurring at the peak of a boom, not as a secular phenomenon. Financialization in the sense of a long-term shift in the center of gravity of the economy toward finance, with financial speculation building over decades, is a completely unprecedented situation.

Marx and Engels did place great emphasis on the growth of joint-stock companies/corporations and the appearance of a market for industrial securities that began to appear near the end of the nineteenth century. It was this creation of the modern market for industrial securities that was the real beginning of the emergence of finance as a relatively independent aspect of the monopoly capitalist economy. There are essentially two pricing structures to the economy: one in the real economy related to the production of goods and services, the other in the financial realm associated with the pricing of assets (paper claims to wealth). The two are interrelated but can be disassociated from each other for periods of time. Keynes in the 1930s singled-out the dangers of an economy that was

increasingly governed by the speculative pricing of financial assets. Marx was such an acute observer of capitalism, that even in his time he began to see the contradictions emerging between money (or fictitious) capital and real capital.

One thing that Marx did argue in this context is that surges in financial speculation were responses to stagnation and decline in the real economy, as capital desperately sought a way to maintain and expand its surplus. Thus he wrote that the “plethora of money capital” in such periods was due to “difficulties in employment, through a lack of spheres of investment, i.e. due to a surplus in the branches of production” and showed nothing so much as the immanent barriers to capitalist expansion (quoted in *The Great Financial Crisis*, p. 39).

Marx remains the strongest foundation for the critique of the capitalist economy, down to our day. But the real Keynes (not to be confused with the bastardized Keynesianism of today) is also important, since he emphasized what he called the “outstanding faults” of the capitalist economy: the tendency to high inequality and high unemployment. He also pointed to the dangers of a system geared to speculative finance.

MW: Is wage stagnation and income inequality a direct result of financialization?

JBF: I would put it the other way around. Wage stagnation and growing income and wealth inequality are components of the underlying stagnation tendency. Both have shown a tendency to worsen over time, resulting in deepening stagnation tendencies within the overall economy. Real wages in the United States peaked in 1971, when Richard Nixon was president, and by 2008 had fallen back to 1967 levels, when Lyndon Johnson was president. This is in spite of the enormous growth of productivity and expansion of wealth over the intervening decades. Hence, this is a marker of “the tendency of surplus to rise,” as Baran and Sweezy put it, or a rising rate of surplus value, in Marx’s own terms. This was accompanied by a massive growth of income and wealth at the top. As we stated in *The Great Financial Crisis* (p. 130), “From 1990 to 2002, for each added dollar made by those in the bottom 90 percent [of income] those in the uppermost 0.01 percent (today about 14,000 households) made an additional \$18,000.” By 2007 income/wealth inequality in the United States had reached 1929 proportions, i.e., the level reached just prior to the 1929 Stock Market Crash that led to the Great Depression.

I do think you are right, though, that financialization made income and wealth inequality worse, and contributed to the stagnation of wages. We can see neoliberalism as basically the ideology of monopoly-finance capital, introduced originally as the ruling class response to stagnation, and then increasingly geared to promoting the financialization of capital, itself a structural response to stagnation. Neoliberalism promoted incessant breaking of unions, forcing down wages, cutting state social welfare spending, deregulation, free mobility of capital, development of new financial architecture, etc.

One way to understand this is the enormous need for new cash infusions to feed a financial superstructure that was voracious in its demand for new money capital, which it needed to leverage still more piling up of debt and financial speculation. Insurance companies, real estate, and mutual funds all provided infusions into this financial superstructure, as did the state. All limits were removed. Under these circumstances workers were encouraged to use their houses like piggy banks to finance consumption, credit cards were handed out to teenagers, subprime loans were pushed on those with little ability to pay. Individual retirement packages were shifted toward IRAs that were tied into the speculative financial

system. This had all the signs of an addictive system. In these circumstances, too, the real economy, particularly production of goods and manufacturing, was decimated. In the introduction to *The Great Financial Crisis* we include a chart covering the period since 1960 showing production of goods as a percentage of GDP in a slow, long-term decline, while debt as a percentage of GDP is skyrocketing over the same period. All of this meant a massive redistribution away from working people to capital, and to those at the pinnacle of the financial pyramid.

MW: In your book *The Great Financial Crisis*, you are critical of Paulson's capital injections into the banks saying that "at most they buy the necessary time in which the vast mass of questionable loans can be liquidated in an orderly fashion, restoring solvency but at a far lower rate of economic activity—that of a serious recession or depression." On Friday, Timothy Geithner told CNBC that "We will preserve the system that is owned and managed by the private sector." This suggests that the Treasury Secretary might not liquidate the toxic assets at all, but try maintain the appearance that these underwater banks are solvent. What do you think will happen if Geithner refuses to nationalize the banks?

JBF: I would not interpret Geithner's statement that way. Rather we are experiencing one of the greatest robberies in history. I have written on the question of nationalization for the "Notes from the Editors" forthcoming in the March 2009 Monthly Review. All the attempts to rescue the financial system at this time go in the direction of nationalization. The federal government is providing more and more of the capital and assuming financial responsibility for the banks. However, they are doing everything they can to keep the banks in private hands, resulting in a kind of de facto nationalization with de jure private control. Whether the federal government is forced eventually toward full nationalization (that is, assuming direct control of the banks) is a big question. But even that is unlikely to change the nature of what is going on, which is a classic case of the socialization of losses of financial institutions while leaving untouched the massive gains still in the hands of those who most profited from the whole extreme period of financial speculation.

To get an idea of what is happening one has to understand that the federal government, as I have already indicated, has committed itself thus far in this crisis \$9.7 trillion in support programs primarily for financial institutions. The Federal Reserve (together with the Treasury) now has converted itself into what is called a "bad bank." It has been swapping Treasury certificates for toxic financial waste, such as collateralized debt obligations. As a result the Federal Reserve has become the banker of last resort for toxic waste with the share of Treasuries in the Fed's balance sheet dropping from about 90 percent to about 20 percent over the course of the crisis, with much of the rest now made up of financial toxic waste.

Obviously, full, straightforward nationalization would be more rational than this. But one has also to remember the system of power—both economic and political—that we are dealing with at present. The classic case of full bank nationalization was Italian corporatist capitalism of the 1920s and '30s, and was carried out by the fascist regime. Without suggesting that we are headed this way now it should be clear from this that nationalization of banks itself is no panacea.

The fact that Geithner, Obama's pick for Treasury Secretary, is overseeing the enormous robbery taking place, probably exceeding any theft in history, with the ordinary taxpayers picking up the tab, should certainly cause one to ask questions about the "progressive" nature of the new administration.

MW: Former Fed chief Alan Greenspan has dismissed criticism of his monetary policies saying that no one could have seen the humongous credit bubble developing in housing. In your book, however, you make this observation: “It was the reality of economic stagnation beginning in the 1970s...that led to the emergence of the ‘new financialized capitalist regime’s kind of ‘paradoxical financial Keynesianism’ whereby demand in the economy was stimulated primarily ‘thanks to asset bubbles.’” (p 129) The statement suggests that the Fed knew exactly what it was doing when it slashed rates and created a speculative frenzy. Debt-fueled asset bubbles are a way of shifting wealth from one class to another while avoiding the stagnation of the underlying economy. Can this problem be fixed through regulation and better oversight or is it something that is intrinsic to capitalism itself?

JBF: Greenspan is of course trying desperately to salvage his reputation and to remove any sense that he is culpable. I would agree that the Fed knew what it was doing up to a point, and deliberately promoted an asset bubble in housing—what Stephanie Pomboy called “The Great Bubble Transfer” following the bursting of the New Economy tech bubble in 2000. The view that no one saw the dangers of course is false. It reminds me of Paul Krugman’s face-saving claim in his *The Return of Depression Economics and the Crisis of 2008* that while some people thought that financial and economic problems of the 1930s might repeat themselves, these were not “sensible people.” According to Krugman, “sensible people” like himself (that is, those who expressed the consensus of those in power) knew that these things could never happen—but turned out to be wrong. It is true, as Greenspan says, no one could have foreseen precisely what really happened. And certainly there were a lot of blinders at the top. But there were lots of warnings and concerns. For example, I drafted an article (“The Great Fear”) for the April 2005 issue of *Monthly Review* that referred to “rising interest rates (threatening a bursting of the housing bubble supporting U.S. consumption)” as one of the key “perils of a stagnating economy.” Other close observers of the economy were saying the same thing.

The Federal Reserve Board, indeed, was internally debating in these years whether to adopt a policy of pricking the asset bubbles before they got further out of control. But Greenspan and Bernanke were both against such a dangerous operation, claiming that this could bring the whole rickety financial structure down. Since they didn’t know what to do about asset bubbles they simply sat on their hands and tried to talk the market up. The dominant view was that the Federal Reserve could stop a financial avalanche by putting a rock in the right place the moment there was a sign of trouble. So Bernanke went ahead, closed his eyes and prayed, raising interest rates to restrict inflation (an action demanded by the financial elite) and the rest is history.

At all times it was those at the commanding heights of the financial institutions that called the shots, and the Fed followed their wishes. Greenspan himself is no dummy. He wrote in *Challenge Magazine* in March-April 1988 of the dangers associated with housing bubbles. But as a Federal Reserve Board chairman he pursued financialization to the hilt, since there was no other option for the system. Needless to say, such financialization was associated with the growing disparities in wealth and income in the country. Debt itself is an instrument of power and those at the bottom were chained by it, while those at the top were using it to leverage rising fortunes. The total net worth of the Forbes 400 richest Americans (an increasing percentage of whom were based in finance) rose from \$91.8 billion in 1982 to \$1.2 trillion in 2006, while most people in the society were finding it harder and harder to make ends meet. None of this was an accident. It was all intrinsic to monopoly-finance capital.

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