Global Financial Power, Capitalist Crisis, and Uneven Development

An analysis of the impact of financial power upon the stability of the capitalist system, and economic development:

ABSTRACT

The ownership and/or control of financial resources has conferred (political) power to people, ever since the original development of money systems. However the nature and role of this power, relative to other power sources, has been difficult to determine. This paper attempts to construct a general theory of financial power, which indicates its function within capitalist mechanics and outlines money as the primary (but not exclusive) source of power that determines present outcomes and historical transition. Production power, for instance, is seen as a secondary source to financial power since the trajectory of production is determined by the vagaries of the capitalist economic order, whereas finance is not constrained in the same manner. The paper suggests, therefore, that the notion of *finance capital* is a false one since, although most of the time the interests of financial and productive powers converge, as a result of the wealth creation imperative, this is not always the case. In times of a conflict of interest financial power will gain supremacy when financial powers seek to retain relative proportions of power.

The paper further suggests that the nature of the capitalist economic system, and present forces of globalisation, hinder the use of financial power for the purposes of crisis prevention and even development. Redistribution and enhanced multilateral regulatory capacity, in substantial form, are seen as essential although it recognises that there is neither the political will or necessary consensus. It also ironically suggests that, at present rates of credit accumulation, debt could ultimately be replaced by redistribution as the only means of sustaining the interests of global capital and neo-liberalism. Much depends upon the agendas of the presiding financial powers.

Simon Mouatt
Senior Lecturer in Political Economy
Southampton Business School
East Park Terrace SO14 ORH
simon.mouatt@solent.ac.uk
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Introduction

Power can be described as the ability to get someone (or an entity) to do that which they would otherwise choose not to do. Using this definition we could then observe the historical exercise of power, in the capitalist economic order, and surmise on the sources of this power. This paper argues that money and finance have constituted the primary (but not exclusive) source of this power and therefore needs to be the central mode of analysis. A corollary of this proposition is that the *control* of financial resources, has largely determined power relations within world order, or that shifting power relations (originating from other power sources) are manifested through the medium of the *control* of financial resources. In order to accomplish this, the paper develops a general theory of financial power, and suggests its probable impact upon the capitalist economic order and development at a global, national, and local level. This raises several questions that this paper seeks to contribute to the contemporary discourse. For instance, what are the various agendas of the main political actors who wield substantial amounts of financial power? Are they constrained by the mechanisms of the economic system? What is the nature of the power relation between financial and structural (and other) power? An analysis of such issues should reveal significant findings concerning the nature and role of finance, as well as the trajectory of global development, and the prevention of crisis. It is hoped that the theoretical construct presented in this paper contributes to explanations of historical transition and stresses the need for effective multilateral regulation and redistribution. Firstly, some terms.

Uneven Development

Development, of course, is a problematic concept. In common usage, the term refers to a general improvement in any of a range of political, economic, social, and other criteria. It is also implicit that the development is established on a sustainable basis. In this sense, development is a desirable objective for most observers, and can be evaluated using a range of qualitative and quantitative data. Conversely, *economic development* has been traditionally measured by an increase in GDP per capita figures. The primary development concern, which underlies this paper, is the increasing disparities of income and wealth between north and south, and the internal distribution of financial resources within states. This, of course, is the notion of 'uneven development'. After about five centuries of capitalism these inequalities have never been so extreme. In a monetary economy financial power has had a clear role in these processes, but assuming the necessary political will, what are the solutions? The general equilibrium model, promulgated by neo-liberalism, would advocate policies to remove the market imperfections and rigidities in order to facilitate development. This paper questions this proposition and suggests instead that scale-economies, technology monopolies, structural power and resource control that are ever present in the latter stage of capitalism mitigate the fair and balanced competitive process that is indispensable for even development. Furthermore the political interests of the wielders of substantial financial resources could

also preclude the possibility of fair competition since they are perhaps reluctant to have their privilege, in terms of relative proportions of financial power, undermined.

The Capitalist Mode of Production and Capitalist Crisis

Historically the ideological rhetoric of the mainstream economists has presented the capitalist mode of production as based upon three fundamental principles. Firstly, the right to privately-owned business. Private individuals are able to own and control the means of production, and manage and allocate resources with a relative degree of autonomy. Secondly, the promulgation of 'free' markets. As products are exchanged, according to the vagaries of the price mechanism, all agents in the market are able to operate with the minimum of restraints. Thirdly, the facilitation of a competitive process between firms that produce similar produce. In time, it is assumed, this leads to technical efficiency and maximised utility from the available resources since the firms that do not meet the needs of consumers are eliminated from the market. This 'economic Darwinism' generates a wealth accumulating dynamic and, it is claimed, the 'trickle-down' effect ensures that the spoils gradually filter down towards the more marginalised of society.

Capitalist firms then depend for their survival upon the sustained sales of their goods and services. A failure to meet consumer need would result in liquidation and a reallocation of resources. The whole of this system is then regulated within a legal framework and various institutions, such as a stock market, that facilitate its functioning. So what goes wrong? The answer to this question lies in the need to generate sustainable sales of products, in order to function. This leads to periodic crises when goods and services do not sell in sufficient quantities. Constant sales require *inter alia* money (or credit), which is the exchange function of money, and subsequently financial resources are one of the key factors contributing to crisis. The trade cycle then booms and slumps, according to these sales fluctuations. A severe recession could be termed a crisis where, as output and investment fall, general resource unemployment (and strife) increases.

This reliance on the need for constant sales, as the primary motor of an economic system, is a fundamental weakness. Keynes and Marx had observed that 'Say's law' (supply creates its own demand) fails to work when money is hoarded and Keynes had advocated the fiscal management of aggregate demand. Those of a Marxist persuasion, conversely, have explained that crises stem from a falling profit rate, suggesting that the capitalist order fails to meet sustainable investment need, is inherently instable and possesses internal contradictions between capital and labour that will eventually transform it. Even those of a non-ideological disposition are concerned with issues such as an excessive materialistic culture, inequalities, environmental effects, and the relentless depletion of natural resources. Subsequently, there are many who advocate stronger state regulation of the economic system in order to tame its excesses and failures.

There are, of course, other forms of capitalist crisis such as sudden and sharp devaluations in exchange rates or the build-up and/or default of debt that threatens the

stable macroeconomic management of national economies or even the stability of the financial system itself. Present forces of globalization make the global financial system more vulnerable than ever to external shocks such as these. The impact is felt in the real economy and the lives of ordinary people are affected. It is clear that wielders of substantial financial resources are instrumental in such occurrences and therefore it will be useful to examine both the nature and the control of money and credit in more detail.

Money, Financial Resources and Financial Power

Money performs certain functions in the social economy, such as a means of account, store of value, enabler of exchange and a means of deferred payment (the creation of credit). Yet to function as money, an entity needs certain characteristics, such as divisibility, durability, homogeneity, portability and (most importantly) sustained acceptability. Social acceptability, in turn, requires a degree of scarcity, legitimisation and the maintenance of low inflation. It is, therefore, the primary responsibility of the (state) monetary authorities, to instigate and maintain the properties of money and the domestic financial system. In Britain these are conducted by the combined efforts of the Treasury, Bank of England and the Financial Services Authority. Whenever this fails, for instance in Germany in 1923, great political and socio-economic upheavals can result.

Historically money has also served to liberate economies from the inefficiencies of barter. This, in turn, has facilitated sustainable growth and industrial development in all known epochs. Furthermore, the technical development of the financial system directly correlates to the level of economic advancement. This suggests that, in conjunction with other factors, the evolution of money and finance has been indispensable for the substantial and sustainable growth of the modern era (Strange, 1986). An advanced financial system, managed in a stable fashion, is therefore a pre-requisite for modern economic civilisation itself. Without money and credit, capitalism in its present form would cease to exist. Furthermore, it is probably within the capability of the wielders of substantial financial power to bring the global economy to a standstill.

The creation and proliferation of credit, as a means of deferred payment, has also enabled economic systems to evolve more efficiently. This is because it can provide liquidity when it would be otherwise absent, and therefore it performs a useful enabling function. In addition, in the absence of redistribution, credit creation enables the utilisation of any money surpluses (and deficits) that occur in transaction needs, thereby enhancing efficiency. Credit is not new, the ancient Babylonians are alleged to have practised it, but the prolific scope and size of modern provision is. Present levels of internal debt, for instance, have reached record proportions in the United Kingdom and the United States. The global impact of high levels of international indebtedness became a particular concern at the time of the Mexican external debt crisis in 1982, since a threat to the stability of the global financial system (from bank failures) was perceived. Since then external debt has been politically managed and the immediate threat to the stability of the global financial system has disappeared, but it is perhaps myopic to assume that there

will be no difficulties arising from high external and internal debt levels in the future. The aggregate figures are huge and increasing. Furthermore, the actual ability to grant or decline credit itself is, of course, a source of financial power since the use of money is effectively controlled.

Financial power also manifests through the use of international money. The US dollar, as the main reserve currency, fulfils this role and US financial interests gain substantial *seniorage* as a result, notwithstanding occasional problems with this in practice.[1] International currency acceptability, in turn, is partly determined by the maintenance of value resulting from long-term balance of payments equilibria and prudent monetary management. The nature of *fiat money* is such that all currencies are ultimately valued, in foreign exchange markets, according to the relative strengths of the underlying fundamentals of the *real* economies they represent. Maintained currency value depends upon factors such as, the sustainability of the production (and sales) structure, monetary and fiscal policies, the expectations of future stability, and general regulatory capability. If any of these are found to be lacking, a currency will depreciate relative to others. This currency competition subsequently leads to a redistribution of financial power and so is therefore very significant for the future world order (Cohen, 1998).

Also monetary regimes such as Bretton Woods, as sets of political arrangements that define the structure of the international financial system and regulate the processes, can restrict the fungibility of money and financial power is subsequently curtailed. Exchange rate regimes, for instance, may seek to maintain currency stability amongst trading partners, which is useful for sustained trade or even attracting foreign direct investment but may necessitate capital controls.[2] Whilst state development agendas may be served financial powers are restricted. Conversely, during the neo-liberal order, exchange-rate flexibility has become increasingly pervasive and the volumes of private portfolio flows have experienced exponential growth. This enhances the capabilities of the owners of financial power as a determining factor in global order.

Neo-liberals claim that this present liberalization of finance can contribute towards an optimum macro-economic environment for effective development.[3] Critics disagree and point to uneven development concerns and systemic risk. Notwithstanding, all of the major financial markets are now global in nature and, in addition, several new financial instruments have been created. These have grown in volume and scope, particularly in the last ten years. One worrying feature of the new financial landscape is the sheer volume of capital flows, which now greatly exceed current account transactions. This has led some commentators to suggest that global finance has a momentum of its own, is

[1] The Triffin paradox points out that in order to ensure liquidity an international reserve currency needs be plentiful and the host currency needs to run a balance of payments deficit yet, conversely, in order to maintain stability and confidence in the international money a surplus (or at least sustained equilibria) needs to be obtained.

[2] In the modern era, governments are increasingly viewing these FDI flows as indispensable to future growth and prosperity.

[3] The liberalization of interest rates, for instance, will encourage positive interest rates and increase the financial resources that are available. It is argued that this will lead to a more efficient allocation of credit and, therefore, enhance the prospects for development (Pill and Pradham, 1997)

largely unregulated and is potentially destabilising, which can be viewed as altogether separate from the production structure (Strange, 1986). This paper argues that *fiat* money by definition cannot be separated from the *real* economy but that, private flows of money has increased the role of financial power and diminished state sovereignty as a result.

Globalisation and the Present Epoch

What kind of world do we live in? The general theme of the present globalisation discourse is that the world is becoming smaller, more standardized, interdependent and increasingly borderless. These developments have been manifested in the political and socio-economic dimensions. Most of the discussions, however, are centred on economic globalisation processes that have raised several concerns such as the threat of financial instability and its ramifications, or the erosion of state sovereignty. The modern global economy has been characterized by an acceleration of the general level of technological change, the growth of international trade, foreign direct investment activities, the increasing emergence of global markets and the removal of regulatory restrictions in the international financial system.

There is generally considered to be an earlier phase of globalisation, yet with essential differences to the present one, between 1870 and 1914. This period experienced goods, services, capital and persons freely crossing borders and the gold standard provided financial stability and minimal government intervention. However most trade was inter-sectoral, where primary products were exchanged for manufactures, and international finance was limited to bonds and trade. Conversely, modern international companies are more functionally integrated at all stages of production, and only 2% of financial transactions relate to trade. Perhaps the essential difference between the two eras is that the main issue today probably centres on the erosion of state sovereignty in key policy areas whereas the previous era experienced a stronger (albeit limited) state. This suggests that the financial power of private money has increased in relation to other sources of power or money controlled by the state.

Towards a Theory of Financial Power

The ownership and control of money, and the power to grant or receive credit, have been synonymous with political power in every epoch, through the empowerment that accrues in a variety of contexts and outcomes. Yet, when this financial power is considered relative to other sources of power, it becomes a problematic version of the ‘chicken and egg’ argument. When European monarchs initially raised taxes for instance, to finance military campaigns that changed the international balance of power, were the sovereign political structures or the financiers the main power source for this change? Clearly other factors, such as the production, state, security, or knowledge structure, are important

sources of power that would have contributed to the changes in world order.[4] Since these power sources are often interdependent, it is most probably a fruitless endeavour to attempt to ascertain their relative capabilities and significance. [5]

Susan Strange in her eighties work 'States and Markets' identifies primary and secondary sources of power. Her primary category includes power structures of knowledge, security, political entities, production and financial and she avoids too much discussion on their interdependence (Strange, 1986). For Strange, financial power is derived from the shaping of the structure of the money system and the ability to grant or decline credit that she attributes to the state and banks in varying proportions at different times. In recent years the exponential growth in the quantity of international financial transactions and private volumes have increasingly undermined state sovereignty and increasingly determined economic outcomes. Furthermore the banks (as businesses) are subject to the vagaries of financial markets and the executives constrained by the demands of the individual and institutional investors for safe and lucrative returns. They are, therefore, subject to the competitive pressures of the capitalist order. It is only the *owners and controllers* of the financial resources that have the effective ability to utilize money for their respective agendas that may differ from the usual demands of the capitalist order.

The central argument of this paper is that, in an advanced monetary economy, due to the unique *utility* of money (derived from its functions), power from all sources almost invariably needs to be exercised through the *medium* of money resources and, subsequently, the control of financial resources can be seen as the primary power source in historical world order and should be the central mode of analysis. Also the possession of money performs an *instigative* function, in that new production, research, military operations etc need to be financed and, furthermore, the actual control of financial resources *per se* can serve as a catalyst for outcomes. Thirdly, money contains the unique property of *fungibility* (the ability to change form) that increases its operational flexibility in relation to other assets or sources of power. There are, of course, different notions of the precise nature of money. For the purposes of the analysis it is not necessary to give a definitive account of what constitutes money and it is generally taken to refer to notes, coins and sight deposits (including near-liquid time deposits). Other assets are excluded.

Michael Mann, as a historical sociologist, sees societies as 'multiple overlapping and intersecting socio-spatial networks of power' (Mann, p.1-3) that are transnational in nature and therefore, do not exist within unitary bounded social systems. He identifies four sources of social power that interrelate, that of ideological, economic, military and political relations and further suggests that they are neither co-terminate or any one of them predominant in a permanent way. In his study of historical transformation he suggests that defining moments of structural change occur through these networks of interaction where, at any given point in time, the 'boundaries and capacities' of any of these sources of power may display greater capacities to organise and instigate than

[4] These are the categories that Strange identifies in *States and Markets* (Strange, 1987)
[5] Modern power theorists, such as Focault, have tended to view power as located anywhere and everywhere and essentially a social phenomenon. In addition there are different modes of power (such as persuasion and manipulation) and particularities associated with the *exercise and geography* of power (Allen, 2003).

others. As a result of this view Mann suggests that social relations and changes to world order cannot be reduced to some immutable systemic property such as the 'Marxian material relations of production' or a 'normative system' with an evolutionary process. Rather, he suggests that watershed historical changes have been instigated by either an empire consisting of military and political power combined with geopolitical hegemony, or by 'multi-power-actor civilisations' where diffuse powers in varied combinations were the pre-dominant reorganizing force (Mann, p 518-534).

With this approach it is difficult to present one source of power as preeminent since the networks 'overlap and intersect'. Yet, as previously stated, power almost invariably needs to be exercised through the control of money. With Mann's ideological power networks for instance, based on normative systems, the mobilisation of activities requires financing and it is difficult to conceive of substantial structural change occurring without the support (or control) of presiding financial interests. Whilst in Mann's work this is probably implicit, financial resources are not placed as the central mode of analysis. Also the financial needs of the military-industrial complex (Mann's military network) both for production and operations are colossal. In Niall Fergusson's work *The Cash Nexus*, for instance, Fergusson outlines the historical connections between money and war-making capabilities that illustrate financial interests as instrumental in world history (Fergusson, 2001). The state, as political power in Mann's analysis, has also been historically reliant on the relevant financial powers and remains indebted to the financial system. Notwithstanding the growth of the state in the immediate post-war era, the state control of financial resources, in relation to private financial capabilities, has declined. The recent liberalization of finance has further eroded state sovereignty whereby private capital flows determine exchange rates, open market operations are virtually ineffectual and state policy agendas are restricted as macroeconomic policies are forced to serve the interests of private capital.

In Mann's view of the economic networks of power, which consist of the control of resources, wealth generation and commerce, money is seen as merely serving the interests of the production process. Yet, the control of money functions as an instigator of new economic activities and, furthermore the production structure has substantial financing needs, which leaves it partially subject to the interests of privately owned capital.

A Contribution to Marxian Political Economy

According to the notion of dialectical materialism, historical transition of the capitalist order depends upon the contradictions and tensions between different social groups (determined by their relationship to production) that eventually lead to transformation. The state is seen as merely an extension of the powerful vested interests of the property owning class. In the Marxist analysis of material productive relations, a key distinction between the bourgeoisie and proletariat categories is the ability of the *bourgeoisie* (owners of the means of production) to initiate or withhold economic activity whilst the

proletariat remains dependent on selling their labour (Marx, 1848). Yet, in the modern era firms are run by managers who have to satisfy the demands of (separate) investors and are therefore subject to competitive markets and the governance constraints of the capitalist order. The trajectory of the firm then depends upon the market conditions and the *bourgeois* state. Conversely, *rentiers* who derive income from the possession of money are able to instigate economic (and other) activities, bankroll human warfare and wield financial power in a myriad of other ways yet are not subject to the same market or state constraints. They therefore can (arguably) be seen as the *bourgeoisie* of the modern era. Financial control can therefore be seen as a primary source of power whereas productive power, whilst significant, can be seen as a secondary source. Marx, of course, identified that money capital is advanced and then involves an expansion of value during the circuit of capital but did not fully develop the significant (social) implications of differentiating between those that provide the financial resources and those that manage the productive process (Capital, Vol 1, Part 2, Ch Four). He had identified a growing class of money-lending capitalists, who extracted a proportion of profit from the economy as a whole, but did not attribute to them as important a role as the productive capitalists (Capital, Vol 3, Part 4, Ch 31). In the modern era there has been exponential growth in the money, capital, bond, foreign exchange and derivative markets from which financial investors extract a substantial surplus. In addition the rentiers are also presently experiencing an accumulation dynamic that redistributes the proportions of financial power.

There are many overlaps with the productive structure, however, and the main political actors in the financial structure have much in common with the transnational group of business elites. This generic coupling has historically been dubbed 'finance capital' since both groups share similar interests and objectives and, in the latter stage of monopoly capitalism, these have become embedded in strong social relations (Hilferding, 1910). These presently reflect, almost invariably, the economic values (and political agendas) of the Washington consensus and elites in the developing world. This paper introduces a caveat, however, that there are times when the interests of financial power diverge from (and gain supremacy over) those associated with production power. In the vast majority of situations financial interests are in support of a successful productive structure since wealth accumulation enhances total social wealth for which *fiat* money is a claim. The value of money is subsequently increased. Yet financial interests, this paper contends, have a vested interest in maintaining their *relative* proportions of financial power in addition to increasing the *real* worth of their money holdings and there are times when the former objective has priority. After the *golden age*, for instance, it could be argued that the slow growth and deflationary period that ensued served the interests of historic financial powers through the mitigation of redistributive forces and the maintenance of monetary value. This further suggests that the control of financial resources is the primary source of power and that productive sources of power (amongst others) are secondary. The growth of the joint-stock company since the 1860's also underlines the point. Rentiers have facilitated the growth of the large firm through the provision of capital resources and are in receipt of a continual income from dividends and compounded interest.[6]

[6] It is worth noting that the rentiers have also financed the growth of the state in the modern era.

With current levels of credit accumulation in the global economy it is perhaps likely that redistribution will be necessary in order to maintain the sales of the productive economy if the logistics of debt service were to become unsustainable. This, of course, all depends upon the agendas of the financial powers towards the evolving capitalist order.

The Determination of Financial Power Capabilities

The term 'total social wealth' is used here to incorporate all use-value (utility presently being produced and all accumulated) in a given society and so money, in an abstract sense, is a claim to total social wealth in a monetary economy. This is the direct link to the 'real' economy and, more specifically, to the traded economy (a changing proportion of total social wealth) that it represents. There are, of course, assets that contain use-value yet are not traded (or not produced) and for the purposes of this paper these are excluded from total social wealth. In addition certain goods and services are produced within alternative economic (non-monetary) sub-systems and these are also excluded from the analysis as well. [7]

In the modern era, the physical attributes of money forms have little intrinsic value, since they exist in the form of paper, base metals and digits on computer software. Yet, fiat money is reflective of the material reality of the economy that it represents, and money derives its value from tangible production and traded activity. However, as stated earlier, money is not neutral, as in the Ricardian sense whereby money simply enables the economy to operate, since holders of money are able to determine outcomes and initiate economic activities. Furthermore, the unique quality of fungibility (the ability to change form) means that money can be seen as possessing commodity qualities in itself. It functions to enable trade, store value, enable accounting, facilitate credit and instigate new production. Indeed it is indispensable to the exercise of virtually *all* power. The owners and controllers of money resources therefore have financial power that directly derives from these mediator functions. Those that hold 'value' in other forms simply do not possess the same abilities. In order to exercise financial power, owners of alternative forms of wealth need to *materialise* this by transferring their assets into a money form. Similarly, those that possess powers derived from other sources are limited in scope, without access to financial resources, and therefore need to obtain them. It is these characteristics of money that set it apart as a primary source of power. Furthermore we can assume that the relative proportions of (claims to) social wealth, expressed in financial terms, constitute the relative capabilities of financial power. It is necessary, therefore, to outline the nexus between money and the real economy in closer detail.

During any specific period there will be a certain money supply that will vary according to the amount produced (or removed) by the financial authorities, the amount of credit creation and the quantity removed (either destroyed or held in the form of idle balances)

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[7] Adam Smith had famously mused on the difference in value between diamonds and water. Clearly water when freely available has a use-value but no exchange value. Such entities are superfluous to the study.

and/or added to circulation by private agents. Yet, at any particular point in time there will be a certain quantity of money (all owned), which will be termed a static money stock. According to the classical equation of exchange (see Figure1) the static (utilised) money supply (M), in a given period, multiplied by the velocity of circulation (V) will be equal with the price level (PT) (the average price times the number of transactions).

MV =PT

(Figure 1)

If the money supply is increased *ceteris paribus* then this will lead to an increase in the price level, namely inflation. Money supply can change and also the number of transactions in the traded economy (the level of economic activity) can also vary. This can result from new production, or part of the non-traded economy (accumulated wealth) being entered in the traded economy (obsolescence and depreciation will reduce the aggregate value of accumulated wealth). Figure 2 demonstrates these potential changes from a previous equilibrium period in an amended quantity theorem.[8]

(MS+FA+CC+IB) V = P (TE+NP+NT)

MS The present (utilised) money stock
FA The net balance of money stock change by the authorities
CC The net utilisation of any deposits as credit creation
IB The net introduction of any idle balances by private agents
TE The traded economy
NP New production traded minus any obsolescence, destruction or depreciation
NT Net economic activity deriving from the relative proportions of the traded and non-traded value changing

(Figure 2)

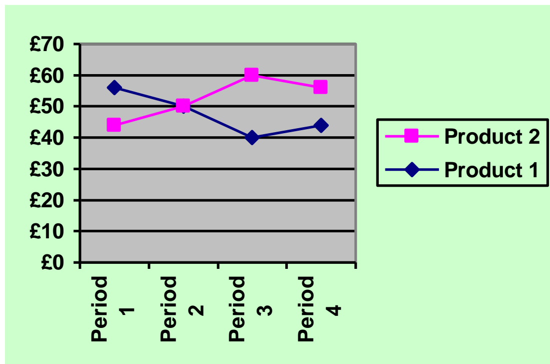
As stated earlier, our static money stock at any given point in time, as a claim to total social wealth, will not need to be of sufficient quantity to reflect the total utility. This is because much of the accumulated wealth is not subject to trade, in any particular time period.[9] Yet in a monetary economy, due to the unique qualities of financial resources, money can be the only real depository of value in terms of the (efficient) ability to obtain *produced* utility. We can conclude, therefore, that the money stock, at any given point in time, *reflects* total social wealth. If the non-traded sector were to be traded in full, the money supply could increase proportionately (given a stable velocity of circulation)

[8] This amended version of the quantity theory takes account of the Marxist and Keynesian traditions towards the demand and supply of money. Keynes had identified the precautionary and speculative uses of money and Marx was keen to emphasise the tendency for holders of money to hoard, both thereby refuting Say's Law (Itoh and Lapavitsas, 1999)

[9] In this theoretical context the static money stock, as fixed, can represent a given proportion of total social wealth whereas in a trading period the money stock (as indeed the trading economic activity) may vary.

without an increased price level.[10] A caveat to introduced here is that part of accumulated wealth held in non-money form would not be (or need to be) traded yet could still be a source of power. For the purposes of analysis these entities are considered to be a negligible proportion of total use-value.

So far we have considered the money supply/stock and total social wealth without considering the relative (and changing) prices that exist, in a given time period, and the concept of monetary equilibrium. In a hypothetical economy, the total exchange value of the traded economic activity will be expressed by the aggregation of the market prices, that will in turn equal the fully utilized money stock multiplied by the velocity of circulation. We consider three separate scenarios. First, if we assume Say's law, which states that supply creates its own demand, and assume that a fixed number of products are consumed in a given time period and the money stock is fully utilised, a fall in the price of one product will adjust the relative price ratios of all the products and one (or more) price(s) will rise accordingly (Figure Three). The aggregate money stock, with a stable velocity of circulation, will remain the same.[11] The principle of monetary equilibrium presupposes that there is a price ratio established between two goods and, therefore, between all goods. The demand for money and the supply of money will be in equilibrium and that, given certain assumptions, money supply and money income move together over different time periods (Congdon, 1989).[12] However the distribution of money income, and hence the relative proportions of financial power, will change accordingly.

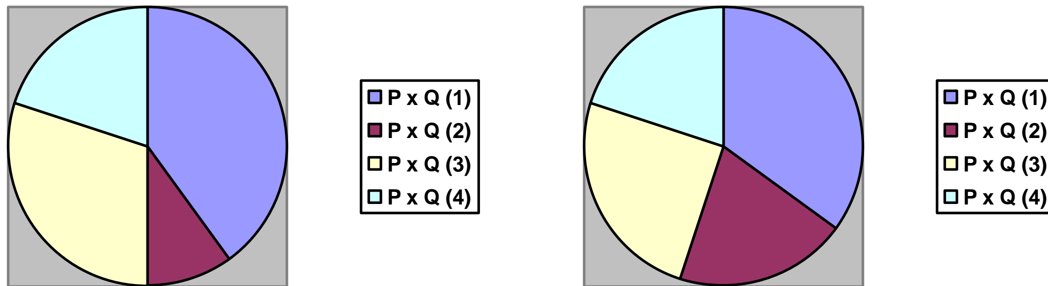


(Figure 3)

In a basic two-product economy the price ratios will simply adjust, during a given time (split in to 4 periods), with a fixed amount of transactions and (a fully utilised) money stock. The distribution of financial resources will change.

[10] This is, of course, the monetarist notion that the money supply growth needs to keep in step with long terms growth, *ceteris paribus*, in order to avoid inflation.
[11] With the classical view of a closed economy, with no government intervention, savings and investment are in equilibrium through an appropriate rate of interest.
[12] The assumption is that the payments technology, rate of interest and expected inflation rate remain constant (Congdon, 1989).

However, given the continual fluctuations in the conditions of supply and demand (in the goods market) present in the real world, in scenario two the *quantities* as well as the prices will be subject to change in a given time period. If the price of tomatoes falls following a shift in demand, for instance, the income and substitution effects will lead to different quantities of tomatoes (and other products) that are now produced and traded. However a fixed money stock (with a stable velocity) will still represent the (now) changed proportion of total social wealth, which is manifested in the traded economy as the aggregate of all exchange values. The price ratios of these products and services concerned will be altered in accordance with the relative market forces, resources and elasticities that exist in the various markets. Figure four illustrates the point



(Figure 4)

In a basic four-product economy, the relative proportions of the aggregated money stock (revenues generated), for each product (1, 2, 3 or 4), have changed. Yet at the same time, the price ratios of all products and the quantities produced have also changed.

Alternatively, we can consider a third scenario, where the utilized money supply expands or contracts, with changing prices and quantities, during a given time period. In all of these instances, however, it is still the aggregate exchange value, which equals the money supply times the velocity, that is relevant and this determines the distribution of income (and therefore financial power) during the last trading period. This, in conjunction with accumulated money stocks, determines overall financial power derived from a static money stock at any given point in time. In addition, changing market forces, *inter alia,* will determine price ratios in the next trading period and any subsequent alterations to financial power relations.[13]

So what factors determine the price changes? Traditional economic theory tends to ignore price rigidities, and other market imperfections, and assumes that each individual price is determined during a given time period by the forces of supply and demand. This then determines the exchange value of the product or service. The utility or use-value gained by the consumer may, of course, be different to this nominal value. Consumer surplus, for instance, will accrue to those consumers who have purchased their products at a price less

[13] It is worth noting that empirical studies from monetarists seem to suggest that there is also a clear historical link between long run prices and the money supply (Capie, 1998) whilst the methodology has been criticized by the likes of Tobin and Desai (p.220, Itoh and Lapavitsas, 1999).

than they would have been initially prepared to pay for it.[14] Yet, demand is determined by the present *perception* of use value rather than the underlying *actual* use value that the good/service contains. As more information becomes available (informational efficiency) we can assume that demand (and supply) gravitates towards the underlying real value over time that is reflected in a new equilibrium.

However, in terms of the present distribution of financial power, we are only interested in *actual* transactions that take place, determined by the aggregate *exchange* values of a trading period. Yet, if we are attempting to assess the relative ratios of financial power established in the next trading period, it can be very useful. It would also be useful for the business community to be able to assess their sales forecasts more accurately.

So what about the hard and soft currencies and the relative distribution of financial power between currency areas? At any given point in time there will be a certain money stock of all of the currencies in the world and these will, in turn, have relative values according to the prevailing exchange rates. If these values are expressed in a common currency, such as the dollar, the relative distribution of financial power can be determined. Figure 5 (a) examines a global stock of currencies whereby the proportion of global financial power (expressed in dollars), for each currency area, is determined by the money stock times the dollar exchange rate.[15] If we assume that the aggregate money stocks remain the same then the relative proportions of financial power will adjust with every exchange rate fluctuation (see Figure 5 b).

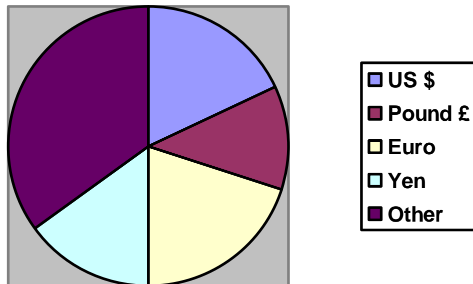


Figure 6 (a)

[14] Firms may, of course, use price discrimination in order to capitalize on this surplus.

[15] The proportion of financial power, represented by the dollar currency area, is simply determined by the nominal quantity of dollars. We also assume that all of the currencies have the same velocity of circulation.

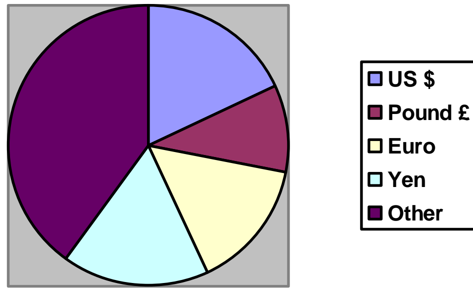


Figure 6 (b)

So what determines the exchange rate movements? Essentially it is the demand (and supply) for a currency that determines its value relative to others and this depends, in turn, on the strength of the *real* economy that it represents. Chartists and fundamentalists, working for financial institutions, will make rate forecasts that depend upon historical data and the underlying macroeconomic fundamentals respectively. However, it is the actual transactions that occur in the foreign exchange market that count. Traditionally, the purchasing power parity approach to exchange rates suggests that, over a period of time, exchange rates adjust in synchronization with the changes to purchasing power.[16]

In addition, any changes to trade patterns would affect the exchange rate value through the current account. However, in the modern era only 3% of foreign exchange transactions relate to trade. Subsequently, the vast volume of capital account transactions constitutes a clearer indicator of future exchange rate changes. Whilst purchasing power and the state of the current account are still significant determinants of agent behaviour in the foreign exchange market, the agents making capital account transactions, such as international lending, portfolio investments, speculation and foreign direct investments, are influenced by other factors as well.[17]

So the distribution of financial power can be determined and this reveals, as we would expect, that the bulk of these financial resources are located in the hard currency areas of the west. The holders of a currency, of course, are increasingly transnational in nature in the modern era. Benjamin Cohen, in a recent text, has outlined that the traditional state-centric notion of currency space is unhelpful. This approach inaccurately benefits the state government in creating an image of a certain structure of power in global currency relations. A more realistic perspective, of the geography of money, is that the vast bulk of currencies are privately held volumes that are now ‘deterritorialised’. He advises that policy-makers be more alert to these conditions (Cohen, 1998). He also suggests that there is a hierarchical ordering of currencies, subject to a measure of political maneuvering that serves to bring relative benefits to the relevant countries. This *currency competition* is particularly relevant when we consider the role of the dollar as the main

[16] A country with a higher inflation levels will experience currency depreciation over time

[17] The portfolio balance model suggests that, in the modern era, capital movements (and hence exchange rates) are determined by a variety of investment conditions as well as the traditional factors affecting market actors. This could include the expectation of inflation, asset prices, socio-economic factors, political factors and exchange rate stability (Valdez, 2003, p 202)

reserve and vehicle currency in the global economy. Seniorage brings substantial efficiencies to the US economy and financial powers are reluctant to relinquish these. In the modern era the reserve role of the dollar is unlikely to be replaced in the immediate future since, *inter alia,* virtually all foreign exchange transactions take place through the dollar and oil, the largest component of international trade, is still denominated in dollars even though there are those that speculate that this may change.

In this analysis of financial power distribution it has not been necessary to consider whether money is endogenously or exogenously determined (or some combination of both) or to be overly concerned with price ratio changes over time since we are merely concerned with a static stock and relative proportions of ownership. In the next trading period there will be changes according to the various factors mentioned above and this will give some indication of changing power relations

Gold and Credit

It would be helpful at this stage to discuss the significance of gold in monetary relations, and the existence of credit markets in the global economy.

Central banks keep a significant amount of their reserves in the form of gold and in times of financial crisis (or expected instability) investors often prefer to hold their wealth in the form of gold. However, in spite of the common acceptability of gold, it does not possess all of the necessary characteristics of money that derive from the modern fiduciary issue and advanced financial technologies. Since it does not possess the same fungibility and does not function as efficiently as money in a monetary economy, it wields (the most) financial power when converted to monetary resources, despite it probably being the closest substitute. Yet, there have been times when gold commodity money has formed the common currency. In this instance, of course, gold can be considered the full depository of financial power. In the modern era, and for the purposes of this paper, holders of gold will be considered to possess financial power but to a lesser extent than holders of financial resources. As Clower has noted money is set apart as the only real depository of value (Itoh and Lapavitsas, p.227).

Credit plays an interesting role in a monetary economy. States, firms and individuals all use credit and, as a result, money is thereby circulated from surplus to deficit agents. This, in turn, enables a more efficient functioning of the capitalist economy. Modern advanced economies now depend upon credit for their very existence. Yet, what is the impact of credit creation on financial power? Firstly, the capability to grant or decline credit will affect the distribution of financial power in the next period. Second, the creation of credit actually expands the money supply, since idle balances are being brought into circulation.[18] Third, in the next trading period, a certain amount of principal and interest will need to be repaid and this amounts to a redistribution of financial power in favour of the creditors. Aggregate levels of debt will give an indication of this future

[18] The money supply will also expand further as a result of the credit multiplier.

realignment. Overall, debt is not a serious problem as long as debt service is sustainable throughout the duration of the loan term. If, however, there is a threat of default then creditors will have substantial political leverage over debtors. Even without the threat of default the rentier financial powers enhance their capabilities as credit accumulates.

The Financial Powers

So who has all the money? For the purposes of this discussion the paper has adopted six key generic groupings that include, in order of significance, individual 'rentiers', corporations (inclusive of investment and commercial banks), the state, 'mafiosi', multilateral institutions, and the general population. These will be considered in turn.

The term *rentier* will be used to describe those wealthy individuals, families or organisations (other than those mentioned above) that own and control substantial financial resources. Subsequently they do not depend (directly) upon any productive resource for their income since they are in receipt of property or investment income. Many of these people are members of the elite from different societies, and have exercised historical financial power, whilst some are the 'nouveau riche' such as George Soros or Bill Gates that have gained their wealth from various economic activities in the modern world. The wealthy family groups could include historical banking families such as the Rothschilds', Rockefellers' or Warburgs', religious groups such as the Roman Catholic Church, or aristocrats like the UK royal family. The *rentiers* are set apart from other generic groupings by their substantial volumes of private financial resources and their subsequent ability to exercise financial power.

Corporations could be considered as the next most significant grouping of entities that own and control financial resources in the modern global economy, particularly the multi-national firms. It has become increasing practice, for instance, for multinationals to finance their future investment from retained profits rather than depend upon corporate bonds or equity finance thus demonstrating their autonomous financial abilities. However, despite being an important source for the generation of financial resources, and constituting accumulated wealth in the form of corporate assets, most monies that are controlled (and sometimes owned) by executives are earmarked for future production and trading activities. Furthermore, the business assets are owned by the securities investors and can, in normal circumstances, be readily exchanged for money forms and therefore are an indirect source of financial power, of a secondary nature to real money. In this sense share capital can be viewed as similar to the gold stock in the modern era. The financial businesses such as commercial and investment banks, and other financial institutions such as pension funds, insurance and mutual fund managers, whilst exercising a measure of financial power are still the stewards of financial resources that are owned by many individual (and largely separate) investors.

The state is the next most significant category of financial powers yet, as previously noted, the erosion of sovereignty that derives from the liberalization of finance has

diminished this. The state has found in recent years that its ability to impact exchange rates through the conduct of open market operations is futile and fiscal maneuvering is restricted since most monies are perennially earmarked.[19] Also the growth of the state in the modern era has coincided with (and been facilitated by) its increasing indebtedness to the financial powers in the private financial system.

Organised criminal groups are the next category worthy of consideration. They include, *inter alia,* cocaine drug cartels and the complex web of money laundering operations and groups such as the VAT fraud gangs or Mafiosi that operate in the European Union. Since these groups wield substantial private volumes of money they can be considered as a significant source of (political) power. The multilateral institutions such as the IMF and IBRD can also be considered to be organizations that wield a certain amount of financial power and this is the next category. This group, however, is constrained by the underlying financial interests that provide their legitimacy, resources and *modus operandi.*

Finally, there is the category of the general population and their collective financial resources. This group has had substantial influence in shaping the markets and the subsequent allocation of resources and are, therefore, a major factor in determining the trajectory of the capitalist order. Yet, since this paper argues that the key structures of the capitalist system are pre-determined by the historic financial powers, these abilities are substantially limited and the *individual* money holder is virtually powerless since their relative proportion of money holdings are minimal. All of these categories mentioned above are, of course, not mutually exclusive but intended to give a broad overview of the hierarchy of groupings that this paper implies exist.

The Manifestations of Financial Power

Financial power is manifested in the global economy through various transmission mechanisms such as markets, debt management, capital flows and the instigative function of money**.** In free markets, where consumers are able to choose the products and services that they wish to consume, within the boundaries of the rule of law, financial power will then determine the future redistribution of income and the allocation of resources. In terms of external debt management, ever since the Mexican default in 1982 the financial powers located primarily in the North have been able to subjugate the debtor nations in the developing world to structural adjustment policies that ensure the world is conformed to the whims of the neo-liberal agenda. Debtors struggling to sustain principal and interest payments become increasingly unable to pursue independent policies as a result of the monetary system that pervades the global economy.

[19] The Exchange Rate Mechanism crisis in the UK in 1992 illustrated the inability of the fourth largest economy in the world to influence its own exchange rate in the face of substantial private speculative flows.

In terms of the present huge volumes of private capital flows that circulate through the financial markets the pressures of exchange rate risk enforce a monetary discipline on those states that are able to manipulate macroeconomic variables to further their economic interests. Those states that are not as endowed find that currency devaluations lead to repressive adjustment policies and an enforced opening to foreign direct investment that enables multinationals to purchase assets on the cheap.[20] Finally, the *instigative* function of money that empowers controllers of financial resources to decide which military (or economic) operations are financed and the ones that are not gives substantial scope for influence. The mere ownership of financial resources *per se* can be the factor that leads to a variety of outcomes, purely as a result of the *abilities* that accrue to the owner. In short, money can be seen as *the* primary source of power.

Conclusion

This paper has argued that the *control* of financial resources is the primary (but not exclusive) source of social power and that financial interests largely determine, *inter alia,* the trajectory of capitalist order, crisis and the nature of economic development. It is for this reason that the paper concludes that financial power, determined by the relative proportions of a static stock, should be the central mode of analysis. It is further argued that by examining the prospects for the next trading period in sequence, the changing nature of power relations can be determined by looking at the likely redistribution of financial power. Given these conditions it would seem that the most appropriate policy response would be the strengthening of (multilateral) state regulation of the global financial system through a concerted effort to build consensus. In addition it seems that the redistribution of income and wealth is needed. This could perhaps be facilitated through the spread of ownership of productive capital - a binary economics approach.

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[20] The Asian crisis of 1997 was an example of such a currency crisis.

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