

INET Plenary Conference

October 21-23, 2017, Edinburgh Scotland

Reawakening: From the Origins of Economic Ideas to the Challenges of Our Time

***Saturday Lunch Session: Adam Smith and the Scottish
Enlightenment***

**The Road to a Decent Society in the age of Financial
Mercantilism; warnings from Classical Political Economy**

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3 Steps

- 1. Use values and a decent society**
- 2. Classical Political Economy: physical reproduction and the limits of markets**
- 3. Exchange values and the age of Financial Mercantilism**

1. Use values and a decent society

The modern use values: UN September 25, 2015

Agenda 2030 and 17 Sustainable Development Goals

-169 targets -241 indicators (march 2016)



The ultimate goals: People and Planet

3 dimensions of sustainability	5 areas of critical importance
Social	People
Environmental	Planet
Economic	Prosperity
	Peace
	Partnership

The 'structural' goals

- Goal 8** Inclusive growth, **full employment, decent work**
- Goal 9** Resilient infrastructures and sustainable industrialization
- Goal 10** Reduce **inequality** within and among countries
- Goal 12** **Sustainable consumption and production patterns**

2. Classical Political Economy: physical reproduction and the limits of markets

Mercantilism: wealth and power through trade

Mun 1623. Nations' wealth and the surplus in balance of trade. Protectionism. Trade is a zero sum game

- **Profit upon alienation, a difference: 'buying cheap and selling dear'**
- **The alliance between big merchants and the state. The East India Companies.**

Physical reproduction and the necessities of life

➤ Petty 1662, agricultural surplus

‘That **Labour** is the Father and active principle of Wealth, as **Lands** are the Mother’ (Petty 1662)

➤ Quesnay 1758, the net product and the modernisation of French agriculture, Agrarian capitalism? *Laissez faire?*

The realm of use values; the physical features of commodities dominate the analysis

Montesquieu and the separation of powers

- “**In order to avoid that someone abuses of power, it is necessary that, in the state of things, power obstructs power**” (Montesquieu 1748 vol. 1 pp. 162-3)
- checks and balances are necessary **without the separation of powers there is no freedom**(see Montesquieu, 1748 vol. 1:164)
- “**the natural consequence of trade is to bring peace**”(Montesquieu 1748, vol. 2, p. 8); ***doux commerce***, **sweet trade as a formidable argument for capitalism**(see Hirschman 1977, p. 60)

Smith and a decent society:

The market is not enough

The rise and fall of nations

- Progressive
- Regressive
- Stagnating societies

The **natural order of investments**: agriculture, manufacturing, domestic trade, foreign trade
(*WN. Book II ch. V Of the different employments of capital*)

Merchants try to subvert it

A harmful alliance

‘Commerce, which ought naturally to be, among nations, as among individuals, **a bond of union and friendship, [sweet trade]** has become the most fertile **source of discord and animosity [sour trade]**’. (*WN*. IV.iii.c.8).

This is the outcome of the **alliance between the merchants and the nation state**: ‘The sneaking arts of underling tradesmen’ (*WN*. IV.iii.c.8).

The labour market: not much harmony

“what are the common wages of labour depends every where upon the contract usually made between those **two parties, whose interests are by no means the same**” (*WN*. I.viii.11). .

Uneven powers and the labouring poor

- Masters being “**fewer in number**, can combine much more easily; and the law, besides, authorises, or at least does not prohibit their combinations, while it prohibits those of the workmen. ...”(WN. I.viii.12)
- masters are always and every where in a sort of **tacit**, but constant and uniform **combination, not to raise the wages of labour** We seldom, indeed, hear of this combination,These are always conducted with the **utmost silence** and **secrecy**,..... (WN. I.viii.13).

Uneven powers and the labouring poor

- masters are **too much wealthier** than workers;
- they are **less in number** which make it easy to join forces in order to support their interests;
- **lack of transparency**;
- they are **connected to political powers** and can influence the governors and the law makers.

Redressing imbalances

‘this alliance could perpetuate and even enlarge the differences between the different market players, **thus increasing imbalances instead of reducing them**’ (*WN*. IV,iii.c.9-10).

‘But the mean rapacity, **the monopolizing spirit of merchants and manufacturers**, who neither are, **nor ought to be the rulers of mankind**, though it cannot perhaps be corrected, **may very easily (sic) be prevented**’ (*WN*. IV.iii.c.9).

Exchange values and the falling rate of profit

- **Ricardo** on the distinction between **value** and **riches** (see Ricardo 1817 *Principles*: 273).

The **privatization of water**: ‘water which had no price will now have a **positive exchange value**, not because of its scarcity but because of the monopoly’ (*ibid.*: 276-277).

Ricardo’s *Principles* opens with a chapter on **‘On value’**

- **Marx**’ *Capital* opens with a chapter on **‘The commodity’**

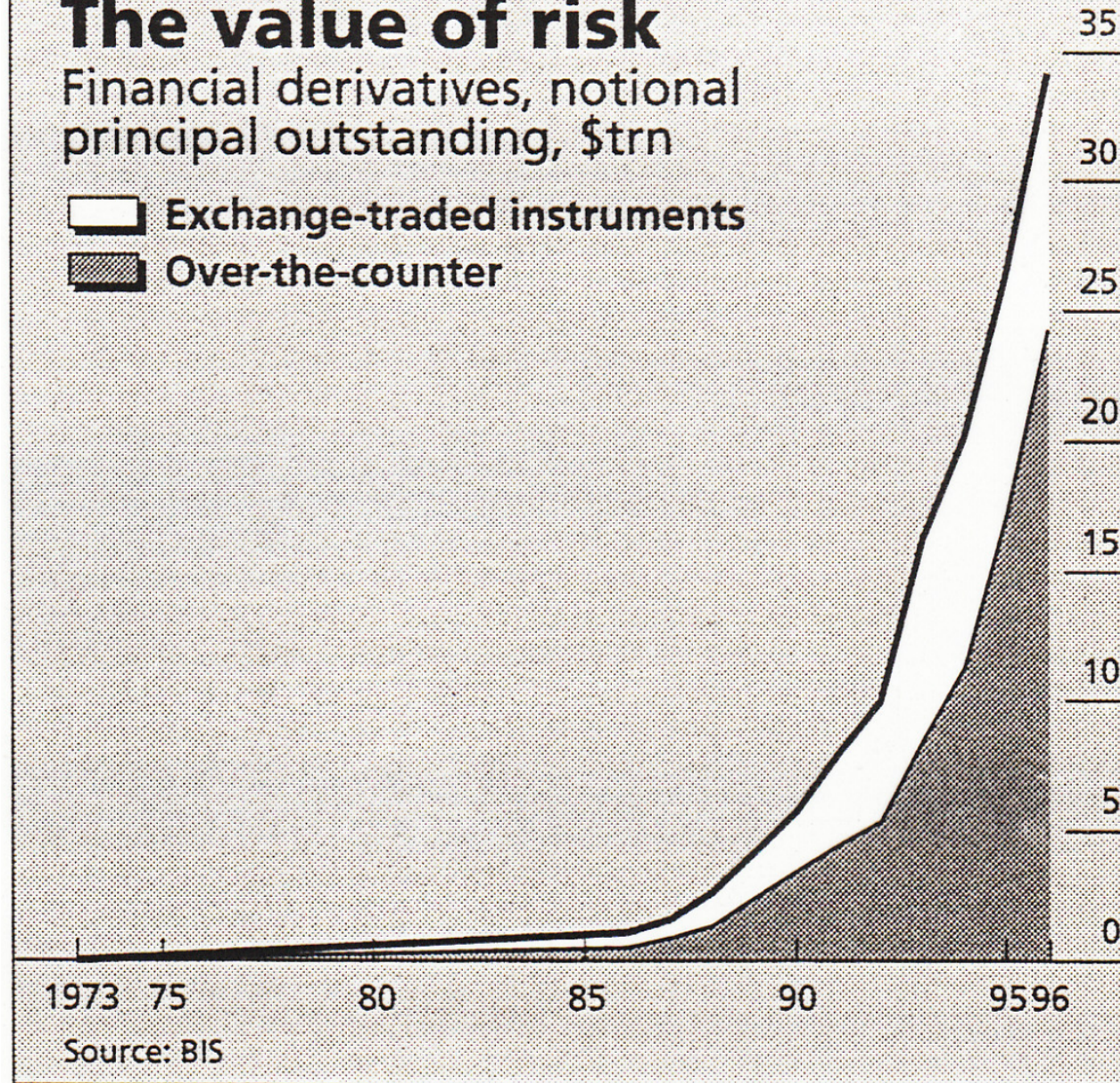
**From use to exchange values
which depend on social relationships**

3. The age of Financial Mercantilism

The value of risk

Financial derivatives, notional principal outstanding, \$trn

- Exchange-traded instruments
- Over-the-counter



Source: BIS

The second 'neoclassical' revolution

- **Solow 1956.** Convergence and catching up
- **Lucas 1976.** Rational expectations. The Micro-foundations of macroeconomics.
- **Bacon and Eltis 1976.** *Britain's economic problem: too few producers.* **Market = productive/State unproductive**

Efficient market hypothesis. Well informed agents and **competitive markets** are enough to achieve the best possible economic combination of **production, distribution** and **growth.** **Deregulation**

New Mercantilism

- The **'alliance'** between big international and financial companies and the state

Not always in view of **state intervention**, may well be in view of the **state staying out**.

The market is enough

Narrative: 'trickle down growth'. The funds will flow where it yields higher returns and it is more needed

- Neo-Mercantilism is not necessarily characterized by lack of competition but by **competition among giants**

Financial Mercantilism

Capital gains: *buying cheap and selling dear*

but no need for **production, transportation**
and **storage**

$$M - [?] - M', \text{ with } M' > M$$

- **Zero-sum game, but bubbles**
- **Systemic risk, 'Minsky moment'**
- **Short-termism, even for long-term assets(bonds)**

Which impact on investments and growth?

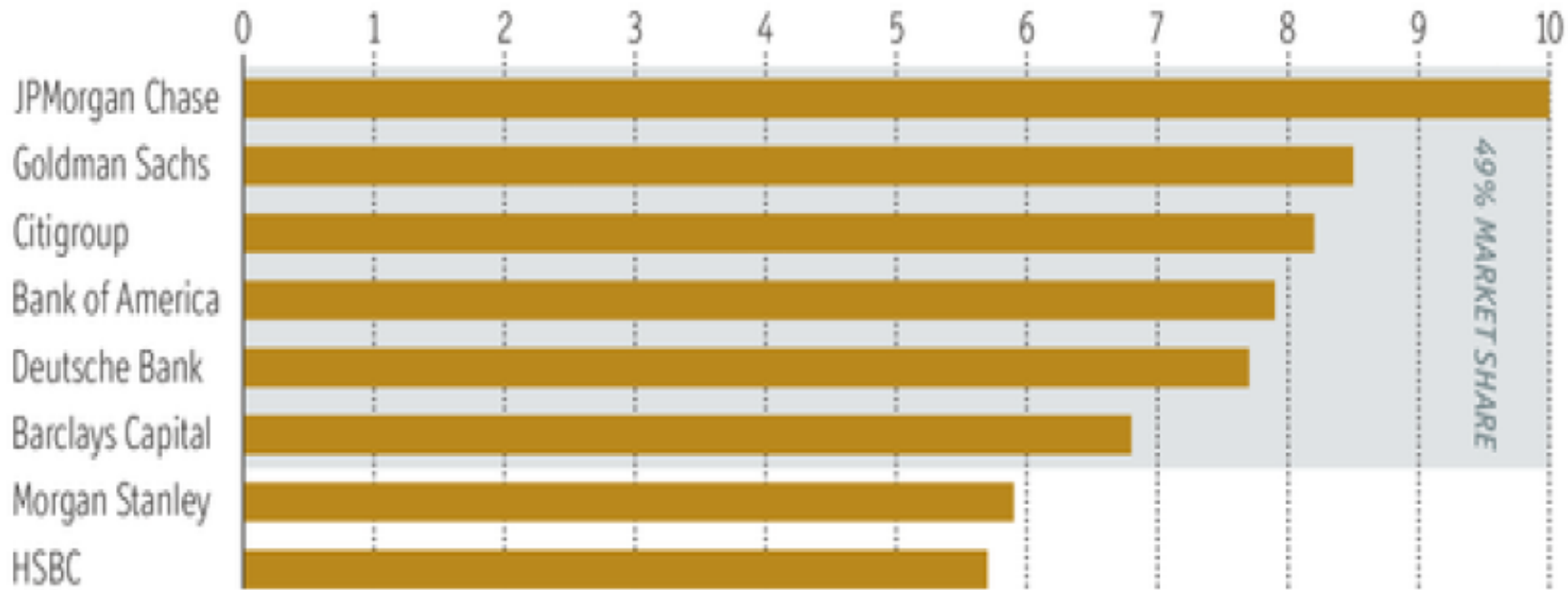
Strange? Two paradoxes

Secular stagnation and the savings glut

1. In Harrod's model **a higher saving ratio** leads to a higher warranted growth rate and in the neoclassical version, with $S=I$, to **a higher income per capita in the steady state**
2. In **East-Asia** capital accumulation based on **domestic savings**, **reinvested profits have by-passed international financial markets.**

Financial giants; an uneven game

Investment banks' global market share by revenue*, 2014 forecast, %



Source: JPMorgan

*FICC, equities and investment-banking division

Re-balancing

Financial Mercantilism is a variation of the capitalist system

- **Financial markets tend to perpetuate and to increase the gaps among the individual in society(Piketty 2013).**

The search for a decent society requires the re-balancing of the economic powers

- These can be done with **policy space** both in rich and in poor countries. Policies: re-distributive, **fiscal, industrial, investment, trade, employment, social protection systems.**

Last but not least: Goal 17 on global partnership and its target. Dealing with:

- **Finance**
- **Technology**
- **Capacity building**
- **Trade**
- **Systemic issues**
 - **Policy and institutional coherence**
 - **Multi-stakeholder partnership**
 - **Data monitoring and accountability**

Back to Montesquieu? **The separation of banking, commercial and investment**

➤ **US** Glass-Steagall Act 1932-33, repealed 1999

Dodd–Frank 2010, Wall Street Reform and Consumer Protection Act

➤ **EU** MIFID-1 2007 **Markets in Financial Derivatives Instruments Directive**
MIFID-2 Transparency

An uneven game; *pacta sunt servanda*

“On July 2014 a ‘vulture’ fund Themis Capital and Des Moines won a case against the Democratic Republic of Congo which should now repay **18 million dollars of an original debt** plus **70 million as interest**” (*The Financial Times*, November 27th, 2014)

- Themis Capital was **not an original creditor**, it bought Congo’s debt years later at **huge discount on face value**
- DRC has an **income per capita of 430 dollar**, **71.3%** of the population is **below the poverty line**
- The debt was contracted by **Mobutu Sese-Seko** in the **mid-80s when** **most people of Congo were not yet born**

Smart monkeys: **“How different mankind is”**

