

2001, OR THE GREAT CYCLICAL DOWNTURN*

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**Michel Husson, an economist and member of the Economics working group of the Revolutionary Communist League (LCR), French section of the Fourth International, has just published *Le grand bluff capitaliste* (La Dispute, Paris 2001, 15 Euros), which extends and deepens his previous studies : *Misère du capital* (Syros, Paris 1996), *Les ajustements de l'emploi* (Page 2, Lausanne 1999) and *Somme-nous trop ?* (Textuel, Paris 2000).

An analysis of the world economic situation is of course complicated by the attacks of last September 11. The discussion is necessarily a dual one: on the nature of the current downturn, and on the major features of the new period that opened in the wake of the 9-11 events. The analysis must alternate between the short term and a longer perspective, between fact and speculation.

If, for the moment, we ignore the September 11 shockwave, and if we review the recent debates, we encounter two questions that underscore the profoundly ambivalent nature of the period. In the wake of the 1997-98 financial crises, the debate was polarized around the question of whether this was the long-awaited collapse or just a downturn. In the end, we had neither, but instead a rebound in growth, the « upturn » of 1997-2001, that gave rise to a new question: was this an exceptionally vigorous high-tech cycle or the beginning of a new long wave of expansion ?

The suggested answers ranged far and wide, from catastrophism to critical support for the capitalist euphoria. The leading indicators of production illustrate the highly cyclical functioning of the European economies. They also confirm that the cyclical downturn preceded September 11, just as the recession of the early 1990s began prior to the Gulf War. This revelation justifies taking a step back to draw the lessons of the recent conjuncture, which serve to dispel a number of illusions.

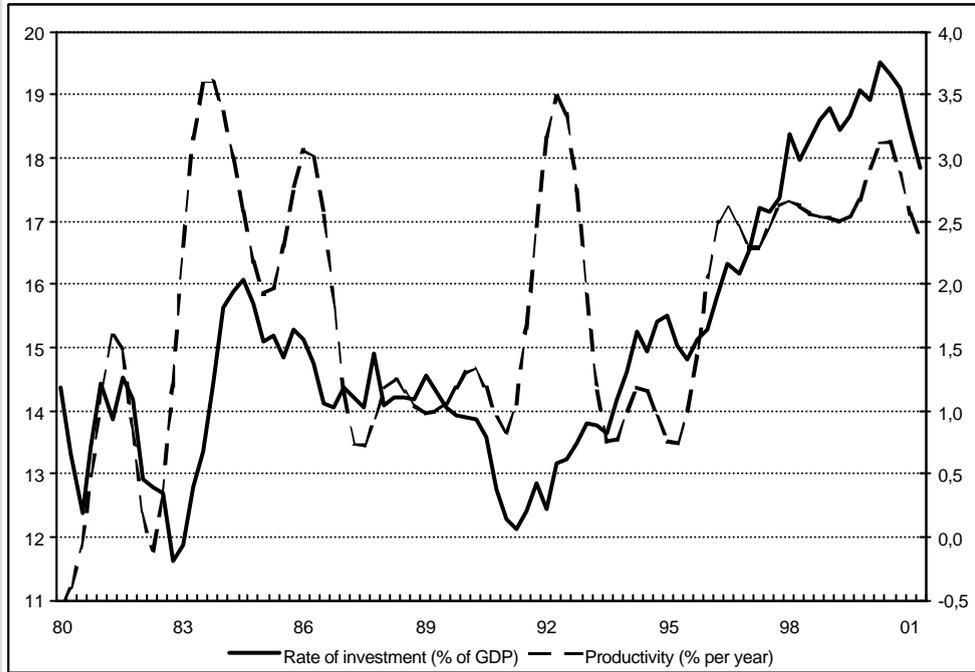
End of the « New Economy »

The economic cycle has clearly entered a downturn in the United States, and the major characteristics of this downturn illustrate the limits of the « New Economy » paradigm. These limits are of two kinds. Some are classical and reflect the underlying contradictions of capitalism, in particular the tendency to overaccumulation of capital. Others result from the concrete forms of the « New Economy » and are not yet fully evident. The expression « New Economy », used in relation to the United States, refers to a number of phenomena - among them, the stock market boom and the decline in inflation - but is based primarily on the acceleration of productivity increases linked to the new technologies. Such increases relax the constraints on the profitability of capital and are a precondition to higher and more stable growth. But they are not sufficient, as it is a known fact that there is no technological solution to the contradictions of capitalism.

The growth of the 1990s was, in fact, sustained in the United States by an investment boom, particularly between 1996 and 2001, that powered the productivity gains. Chart 1 illustrates this relationship between investment and productivity, and shows clearly that the recent productivity increases were obtained by dint of an unprecedented investment effort. This points the way to an objective answer to the question of whether it was a cycle or a new wave of growth. If it were a new growth phase, the increases in productivity would have to be maintained at a high level, with no let-up in the recent investment effort. But all the available data show that the situation has turned around: investment is falling and productivity is slowing. It seems possible, therefore, to put an end to the debate by saying that the « New Economy » was simply a « high tech » cycle. This observation in turn clarifies the nature of the recession in the United States, which has all the features of a classic crisis of overproduction. An examination of the comparative trends in the rate of profit and the rate of accumulation of capital suffices to demonstrate this. The rate of accumulation of capital steadily increased throughout the 1990s, only to decline during the year 2000. The rate of profit, while it kept pace with the accumulation of capital during the first two thirds of the decade,

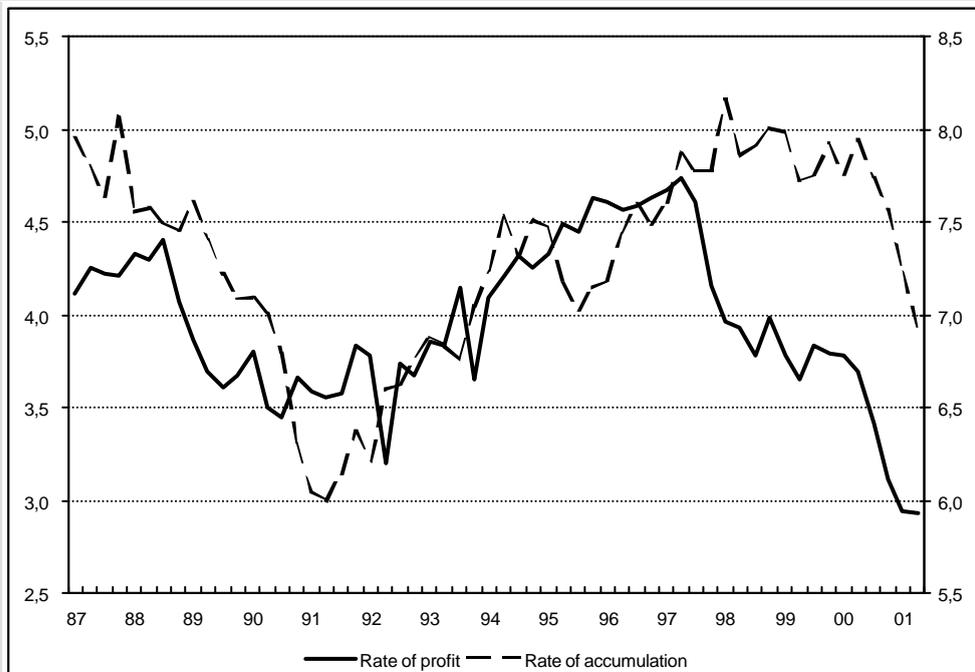
turned down much earlier, in mid-1997 (Chart 2). These observations necessitate some statistical explanation, in so far as we no longer have any official data (which must be reconstituted) on the capital stock. But the downturn in profitability can be directly observed in business profits, which declined from \$858 billion in the third quarter of 1997 to \$761 billion in the second quarter of 2001.

Chart 1. Investment and productivity in the United States



Source : Bureau of Economic Analysis

Chart 2 Profit and accumulation in the United States



Source : Bureau of Economic Analysis

The decline in the rate of profit results from two things in combination. First, the wage component is rising: private sector payrolls increased by 30% between 1997 and 2001, the GNP by 21.5%. A simultaneous increase in the organic composition of capital can be observed. The capital-output ratio accordingly increased by 17% in volume, but by 10% in value. In other words, the increase in capital and the decline in the rate of exploitation combined to bring about a fall in the rate of profit.

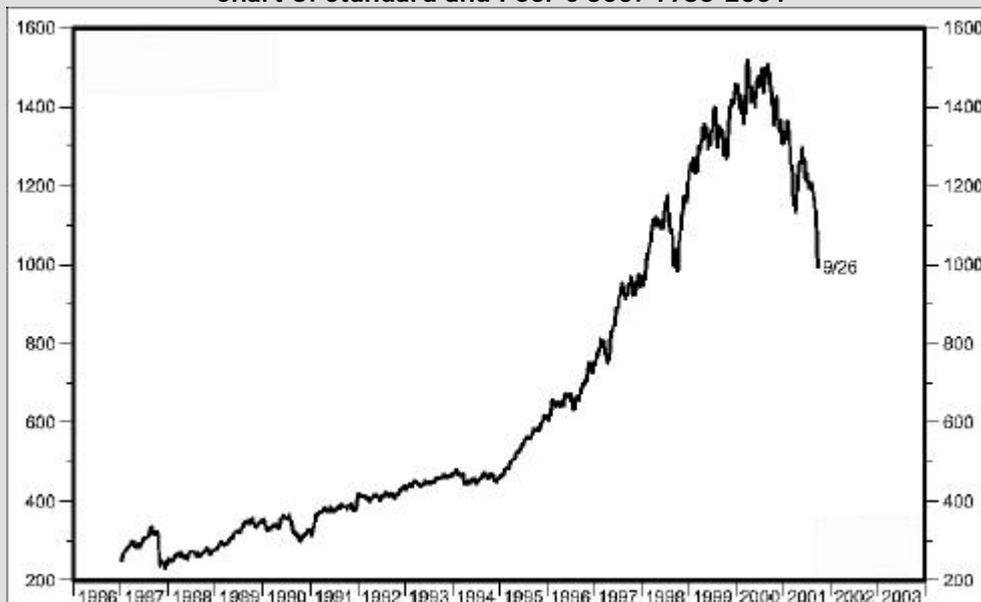
Since investment continued, meanwhile, it was only logical that overaccumulation would result, manifested in the development of excess capacity relative to the conditions of profitability. This surplus takes the form of a fall in the rate of utilization of production capacity: in August 2001, it was 76.2%, its lowest point since the 1982 recession. This drop particularly affected the high-technology industries, where capacity utilization dropped from 88% in 1995 to 63.4% in 2001. So it is the symbolic sectors of the « New Economy » that are most affected.

United States: the three major anomalies

Now that the classical contradictions have erupted into the open, the big question is how they will interrelate with the concrete contradictions resulting from the present configuration of the world economy, and with the consequences of the September 11 attacks. These concrete contradictions are expressed in the form of major economic imbalances involving stock markets, consumption and the external deficit.

The first major anomaly, the one that could exist between profits and stock market prices, is now fading thanks to a secular decline that at the very least suggests a « creeping crash » (chart 3). Here again, this movement must be interpreted as a call to order of the law of value. Shares represent, in effect, a claim on the surplus value that is created. In the medium term, the stock dividends and capital gains procured by these shares cannot indefinitely diverge from the actual profits they anticipate. One of the central affirmations of the « New Economy » was, on the contrary, to suggest that capital had freed itself from this law of value. Some people, Michel Aglietta for example¹, developed theories about this « patrimonial capitalism » on behalf of which workers were asked to be modern and accept financial products in place of their salaries.

Chart 3. Standard and Poor's 500. 1986-2001



¹ Michel Aglietta, *Le capitalisme de demain*, Note de la Fondation Saint-Simon, 1998.

This phantasmagoria dissipated into thin air with the stock market collapse, and the ideology of capitalism has suffered a serious blow whatever the evolution of the market indexes in the months to come. It will be very difficult, for example, to create or extend pension funds in Europe, for one of the major arguments in their favour has just disappeared. How can workers be asked to index their wages to the stock market now? The recession has already provided this first worthy lesson throughout the world: pay cheques are preferable to financial risk. The stock market correction began almost two years ago and thus has nothing to do with September 11. It operated in two stages. The year 2000 witnessed an interruption in the upward movement and the indexes marked time. The market analysts then devoted all their energy to explaining that this was a temporary stabilization that would soon be followed by a recovery. But the Coué method (« Every day in every way I am getting better and better ») failed to function, and the decline continued throughout 2001. This retreat takes the form of an impressive loss of substance of the Nasdaq index, which fell from 5000 to 2000 during the year 2000 and subsequently fell to 1700, overall a two-thirds decline. The new technologies index thus joins the « traditional » stock exchange indexes, perfectly symbolizing the end of the « New Economy ».

The second major anomaly has to do with private consumption. The United States is characterized by a completely exceptional situation; households have been devoting a growing portion of their incomes - now 100% - to consumption. This spending has been the main engine behind the much talked-about «new growth », but it is not sustainable. Some people consume a lot because they think the virtual capital gains achieved on stocks amount to some form of savings, while others go into debt in order to consume or to play the market. So the recent prosperity is based on a huge volume of private indebtedness. The downturn on Wall Street, which shows that these calculations had no foundation, should be expressed in a rise in the rate of savings (already a modest increase has been registered) and the ruin of some households, in short by a slower increase in consumption. The September 11 attacks, by accelerating the decline in euphoric expectations, should provide a further impulse in this direction. A catastrophic scenario is quite conceivable in which a wave of personal bankruptcies would lead to a drop in consumption and domestic demand.

The third and final major anomaly is expressed in a deficit in the current balance of foreign trade, which has now reached \$450 billion a year, or 4.5% of the GNP. This means that savings from the rest of the world are being substituted for domestic savings to finance growth in the United States. Up to now this might have been considered relatively « sound », since the surplus capital from Europe and Japan was being used to finance the boom in the « New Economy ». This influx of capital has been bolstered by the flight from the emerging markets and is sustained by a strong dollar and high profitability. But now things are changing. Investment has turned around, and the new money is going into consumption, which cannot continue for very long when profits are falling and a decline in the dollar becomes plausible.

The September 11 shock has just shaken this three-fold order in a variety of ways. It may well precipitate a downturn in consumption but at the same time indicate a way out for the dominant imperialism. The period now opening up will be marked by a reversal of fiscal policy. The surplus has already disappeared, but the program of subsidies to the most affected industries and the expenditure (military or otherwise) connected with the retaliation program will amount to a Keynesian recovery program that may, at least for a while, substitute for bogged-down consumption by workers. Already, it is reported that \$100 billion, or 1% of the GNP, has been earmarked. The need for external financing might then result in a deal between the United States and Europe based on the following arrangement: the United States will not try to balance its current account by resorting to an offensive lowering of the dollar (which would mean exporting its recession to Europe and Japan), in exchange for which the U.S. partners will undertake to guarantee the financing, now legitimized by the war against terrorism.

The road is a narrow one, obviously, and the imbalances appear to be so great that it is not hard to imagine a loss of control by the United States in a nightmare scenario where everything goes wrong at once: households stop spending and capital stops coming in. The adjustment is complicated, for it involves going along with the slowdown in domestic demand and even encouraging it by holding back any increase in wages, while at the same time jump-starting the economy through stimulating non-consumer goods industries. The success of the operation largely depends on the evolution of the political relationships between Europe and the United States and the United States' capacity to get the rest of the world to pay for its recovery.

The party's over in Europe

Things are certainly happening very quickly. Just 12 months ago, the European leaders were riding an upturn and singing the praises of Europe's success - this new world locomotive capable of taking back leadership from the United States. Today the same leaders are wondering how they can avoid implementing the disastrous European Stability Pact appended to the June 1997 Treaty of Amsterdam. For social liberalism, the party is over. Yet everything had been going well. Not only was the Euro launched without incident on January 1, 1999, but its birth was attended by a surge of investment in a favourable environment. Between 1996 and 2000, seven million jobs were created and the official unemployment rates fell by 3.5 million. It is absolutely necessary to analyze the nature of this recovery, for it helps us understand the cyclical downturn. In a few words, this recovery can be described as non-« neoliberal », in the sense that it was produced by a relaxation of the neoliberal dogmas, not their stricter application. This relaxation was only partially a deliberate choice and is explained primarily by some external factors.

The first external factor was the de facto devaluation of the European currencies against the dollar in mid-1997. Europe gained in competitiveness, its exports surged and a new mini-cycle began. The surge in exports was matched in 1998 by an increase in consumer buying power resulting from the unexpected slowing of inflation, rather than any increases in nominal wages. Consumption immediately rose - bourgeois economists expounded on the « confidence » of households - followed by a new takeoff in investment. The resumption of activity created jobs that in turn bolstered consumer spending. On the fiscal side, the growth increased government revenues and lowered deficits, to everyone's surprise in most cases.

These chain reactions, which could be characterized as Keynesian, amounted to an empirical critique of the neoliberal theology, a refutation of all its precepts. A strong currency was needed, we had been told, before we could have a single currency. In the name of this « law », a policy worthy of the structural adjustment plans was imposed on Europe, with the resulting loss of many jobs. But the great paradox is that the Euro proved, in the end, to be a weak currency. Without the life-saver offered by the 1997 rise in the dollar, the birth of the Euro would have encountered some serious problems.

The wage boost showed that an increase in salaries does not bring about any of the predicted disasters. Inflation remains low, and Europe is generally in a surplus position in relation to the rest of the world. While the share of wages in national income had been declining for more than 15 years, in accordance with neoliberal recommendations, it was when it stabilized that the economy took off again, thanks to the regained dynamism of the domestic market.

A similar refutation occurred in public finance. The neoliberal dogma postulated that the stabilization of public finance was a precondition to economic recovery, but it happened the other way around: it was the recovery that mechanically absorbed the deficit. The healthier economy we could observe during these years provides some indication of the time lost in pursuing the neoliberal policies that brought austerity and unemployment.

Social-Liberalism up against the wall

The time has come to abandon the naive posture of a literal adherence to the neoliberal discourse in the belief that the real purpose of this policy is to fight unemployment. In reality, the European Commission and its member governments are making no efforts to depart from the dogma. Instead of defining a standard for wage increases that guarantees some dynamism in wage claims, they have sought to return to their reference point, a wage freeze. But without this fuel, the recovery could only run out of steam and suffer the slowdown imported from the USA.

Basically, what we have now is the scenario that was most plausible in 1998, a gradual slowing down of all the engines of the world economy. Contrary to the optimists' forecasts, the U.S. slowdown was almost immediately transmitted to Europe. Now we are seeing the brutal effects of increased globalization reinforced by the fetters imposed on the expansion of domestic markets. The speed of this transmission is all the greater in that close to half of the world's trade is in capital goods, which faithfully reflect the sharp fluctuations in investment patterns. Social Democracy, then in government in most European countries, had signed up to the Treaty of Amsterdam in 1997. Lionel Jospin, the French prime minister who had just taken office, placed some conditions on his signature, among them the priority assigned to employment and the establishment of an « economic government ». This founding act of social liberalism

accurately summarised his underlying gamble: to make the liberal-monetarist course chosen for European construction compatible with an economic policy relatively focused on job creation. The upturn may have given the impression that Jospin had won his bet, but it was all an illusion originating in a largely unexpected recovery. This life-saver helped to get the Euro going and to shove the unresolved contradictions and questions to the background. Now, with the economic slowdown, they have come back.

There is a growing perception that the strict application of the Stability Pact will mean a super-recession for the European economy, but there is no institution other than the Central Bank to guide and coordinate business cycle policy. In short, European construction is shaky, truncated and distorted in the interests of finance. In every country the dilemma is appearing: how can taxes be reduced while lowering the fiscal deficit below one per cent of the GDP? That's what the much talked-about Stability Pact prescribes, but everyone is beginning to understand that it is simply not feasible. But the turn toward a less regressive policy is not guaranteed. To cite only one example, the European Commissioner responsible for employment and social affairs, Anna Diamantopoulou, stated recently: « EU labour markets are reforming, results have been positive so far, but government, business and unions must persist with the reform policies we have agreed on - regardless of any deterioration in the world business climate. Economic cool-off must not lead to policy cool-off. Our existing, long-term strategy is the only answer »². If we add to that the difficulty of changing policy in midstream, the absence of institutions capable of handling the necessary coordination of economic policies, and the limited conceptual horizon of the European Central Bank, we can only fear the worst - namely, some inadequate reactions to the cyclical downturn.

Challenge to an implacable globalization

On October 1, 2001 the World Bank published an alarming document that revised downward the anticipated growth rates for developing countries to only 2.8% in 2001 (from 5.5% in 2000) and predicted only a slow rise to 3.5% in 2002. The Bank's president, James Wolfensohn, stated flatly: « We estimate that tens of thousands more children will die worldwide and some ten million more people are likely to be living below the poverty line of \$1 a day because of the terrorist attacks »³.

This ominous forecast, worthy of an « antiglobalizer », sheds some light on the real regression that capitalist globalization represents, with its increased dependency. For many countries of the « South » and the « East », the economic situation is just a reflection that is a bit out of step in time with that of the imperialist countries. In other words, their capacity for autonomous development, based on the satisfaction of real needs, is virtually nil. The possibility of growth is completely subordinated to the fact that they occupy a « niche » in the world market. As for the countries dependent on raw materials prices, they will suffer a secular decline in their resources. Only the oil-producing countries can gain during the phases of price increases, but as a result their functioning is chaotic and unstable. Argentina⁴ provides an extreme example of these imbalances, but what about the situation of Japan, which has been stagnating for ten years, and of all those countries oscillating between dependency and increasing marginality vis-à-vis the major powers ?

This ominous situation is accompanied by a generalized questioning of capitalist globalization. We have cited the extremely pessimistic views of the World Bank. We could add to it the astonishing feature coverage in the September 29 issue of *The Economist*. This ultra-neoliberal magazine is not shy about its convictions, but its argument is extremely defensive. A good example is the title of one of the articles: « Anti-globalists see the 'Washington Consensus' as a conspiracy to enrich bankers. They are not entirely wrong. »

This loss of legitimacy is not, in itself, a product of September 11 alone. The list of countries hard hit by periodic crises is a long one, with a revolving sequence of chaotic economies: Mexico, Argentina, Korea, Thailand, Russia, and Argentina again. It is becoming clear that few countries are actually gaining from globalization, and Europe's relative interlude is now coming to an end. The Euro will become the common currency, but all the advertising campaigns in the world will not convince the workers in these countries

² *News release of the European Commission*, September 12, 2001.

³ « Poverty to Rise in Wake of Terrorist Attacks In US. », *News release of the World Bank*, October 1, 2001 <<http://Inweb18.worldbank.org/news/pressrelease.nsf/>>

⁴ See Eduardo Lucita, « Crisis and reorganization of the social movement. » *International Viewpoint* n°334, October 2001.

that they should expect anything positive from this. Germany, a model of monetary rigour, is crawling along and still absorbing the unification, its « victory over communism ».

As for the United States, the Eldorado of the New Economy and even of the « New Age », the recession was evident before the attacks. Even the immediate response to the attacks takes the form of a self-criticism. Domestically, it is spontaneously Keynesian, almost Rooseveltian, and puts paid to the goal of a budget surplus. Internationally, the United States is discovering, rather late, that excessive financial liberalization has eased the interpenetration between the real economy and the illegal economy. A few months earlier, the U.S. sabotaged the OECD meeting on this issue, and the current treasury secretary, Paul O'Neill, had warned against any restriction on the sovereignty of governments in the name of fighting money laundering and doubtful tax practices⁵.

Political features of the new phase

The most probable perspective is now one of decline in the world economy accompanied by major recessions at its weakest links, particularly in the South. Once again, this new phase was not created by September 11 but is consistent with the trends operating over the last decade. Its exact profile will depend, in the last analysis, on political variables that concern primarily Europe and the United States. Whether Europe will enter a recession or simply slow down depends on the degree of dogmatism in the policies applied.

But the key to the situation lies in the dominant power, the United States. September 11 raised a new possibility that the dominant imperialism may manage to avoid the full potential impact of the recession through military Keynesianism (similar in this regard to Reaganism), the viability of which will be based on the U.S. ability to force its global partners to fund these efforts out of geopolitical considerations (somewhat reminiscent of what happened during the Gulf War). Contrary to Tony Negri's theories about the global Empire⁶, this scenario implies a refocusing of the U.S. economy on the interests of its own capitalists and its own productive apparatus. The potential recovery will be targeted so as not to benefit the competition. Along similar lines, the experts of the World Bank rightly fear that the Bank's long-term loans will be cut back and assigned on a priority basis to countries that can serve as intermediaries in the reprisal operations undertaken by the Americans.

As a result, a whole series of countries will be placed in the situation of having to redefine their policies in an effort to achieve greater consistency between the interests of capitalism in general and those of their national capitalists. In this situation, governments can be expected to derive new rationales for economic intervention. It is not excluded that in Europe this delicate phase will boost increased coordination and stimulate the emergence of a European capitalism with a distinct conception of itself as such. But it may well be a difficult birth, for it will be occurring in a context that favours a resurgence of the contradictions between capitalist economies unevenly hit by the cyclical downturn. From this standpoint, German capitalism has now lost its pre-eminence, both monetarily and financially, while the United Kingdom will tend increasingly to strengthen its traditional close partnership with the United States.

At the same time, the new phase now opening up should accentuate the contradictory nature of the triumph of capitalism. In one sense capitalism has triumphed, since it has obtained virtually everything it wanted. Wage freeze, liberalization, privatization, and greater flexibility are the major trends operating through the world. Capital is restructuring without serious obstacles and racking up ever-greater profits. But this victory has its opposite side, for capitalism has no further excuses for its chaotic, regressive and uneven functioning. The decade of growth in the United States, like the recovery in recent years in Europe, has not led to a more equitable distribution of wealth or a diffusion of social progress - quite the contrary. These successes are consistently offset by the additional restrictions faced by the vast majority of working people throughout the world. After the crisis, there was a widespread perception that the economy had to be stabilized in order to be given a fresh start. This schema no longer operates: employees are confronted with a capitalism wholly convinced that all the concessions that have been made to it are now conquests to be built on in future. There's been no slaking of the thirst for profit in response to reduced wage demands!

⁵ See Babette Stern, « Paradis fiscaux: désaccord entre les États-Unis et l'OCDE. » *Le Monde*, May 16, 2001.

⁶ See Michael Hardt and Toni Negri, « La multitude contre l'Empire. » *ContreTemps* n°2, September 2001, Editions Textuel, Paris.

So the issue is no longer one of how long we must wait for the recovery to begin. It has begun, with no change in the fate of the majority. The lesson has been understood: any improvement in the workers' situation is a function of whatever pressure they can exert in support of their demands. It is conceivable, therefore, that it will be much harder to win acceptance for the counter-cyclical program. In France, the most recent social struggles have been informed by an almost moral rejection of layoffs in companies that are turning a profit. This majority sentiment suggests an alternative legitimacy to that of capital that can no longer be neutralized by an appeal for compromise. The exploited have learned, on a mass scale, that this capitalism is incapable of spontaneous redistribution and that they will get only what they can seize from it.

This exposure should facilitate the transition from reflexive actions in defence of past conquests to the assertion of new rights. The new awareness of the overt brutality of capitalism should lead to the formation of an international coalition in which the new social movements and actors come into play, regenerating the traditional workers' movement. This perspective is completely inherent in the possibilities opened up by this new phase of capitalism, even if the immediate consequences of September 11 blur it in the short term.

A new long wave?

That the cycle has turned is now beyond doubt. In so far as the subsequent evolution is concerned, the major possibilities as we see them can be summarized as follows. A major catastrophe in the form of a huge stock market crash followed by a world recession is unlikely, for two reasons.

First, the likelihood of a collapse in the stock market is diminished by the lack of alternatives for institutional investors, who have no choice but to purchase some stocks in place of others but have no inclination to withdraw completely from the market. This constitutes a floor below which prices should not fall. Moreover, prices have already gone a long way toward catching up with the « fundamentals ».

Second, in recent years the respective national bourgeoisies have demonstrated an ability to react in a coordinated way, not hesitating to use such tools as an injection of liquidity, exchange controls, etc., that in « ordinary » times they categorically denounce. Some re-regulation of markets cannot be excluded as a possibility, by the way, should crises follow in quick succession.

None of this constitutes a retreat from our anticapitalist positions, which are not fundamentally based on the expectation of a major crash. On the contrary, they are developed on the basis of a critique of the « normal » functioning of the capitalist system, and not its imminent downfall. Similarly, the present turn throws some doubt on the idea that we have entered a new expansive phase, a new long wave or a new Kondratiev cycle. Clearly, the current period is not one of strong and ongoing accumulation, of sustained growth in which productivity gains are being passed on to workers. Economic cycles, far from being cushioned, are more and more extensive and frequent. Yes, capitalism has an overall model that defines a new « productive order »⁷, but this is by nature regressive and based on an uneven redistribution of wealth.

This would be of no concern to capital, of course, were it not that this characteristic leads to instability in growth and undermines the ideological foundations of its domination to a degree that we should not underestimate.

What we ought to be convinced of, in any case, is that the present modus operandi of the capitalist system is by nature antisocial, and that its future successes will take place precisely in proportion to its capacity to impose a model based on increasing inequality. That should be sufficient reason to be anticapitalist.

⁷ See Henri Wilno, « A new productive order? » *International Viewpoint* n°325, November 2000.