

## THE CENTRALITY OF FINANCE

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### ABSTRACT

*In the contemporary conjuncture financialization is driving a fundamental reorganization of American capitalism and increasingly that of other economies significantly impacting the trajectory of the world-system. This paper interrogates the nature and extent of financialization, the ways it is adding to systemic risk with attention to the future of the dollar, and implications for the relationship between US-based finance and new emerging centers of the world-system.*

### INTRODUCTION

This paper discusses the manner in which financialization is coming to dominate the US economy and the ways in which international financial institutions are influencing the trajectory of capitalist development. Ironically, for the dual nature of the new reality has not been widely grasped, it is the expansion of financialization which sets the terms on which US hegemony is being challenged and at the same time an important process through which it is being re-asserted. That is to say the territorial space of the United States productive economy is contracting relatively to global production while at the same time following the path of previous hegemonic powers which expanded the scope of their financial control to extract rentier income from rising centers of accumulation. From the perspective of geopolitical strategists the hope is to combine financial dominance with technological and military superiority. Such a claim is consistent with observations by world-systems theorists that previous great powers – Genoa, Holland, Great Britain – when no longer globally paramount in product markets moved decisively to financialization as their loss of leadership is accompanied by the geographic relocation of the centers of capital accumulation (Arrighi and Silver 1999). The speed with which this process is taking place and its multifaceted nature tend to be discussed in terms of the possible damage rapid financialization poses for system stability, a question which will be discussed here but in the context of the ways in which transformation is transforming contemporary American capitalism and its place in the world-system taking a longer look forward.

The first section of this paper defines and discusses the concept of financialization and details its rapid growth. A second part considers the ways in which it is changing the character of American capitalism and the American role in the international political economy. A third discusses the fragility resulting from aspects of financialization which are adding considerable risk and the extent to which speculative excesses are creating potential problems. The widely debated significance of the US current account imbalance and the future of the dollar are the topics of part four. In the concluding section the time frame of the discussion is extended and implications of these developments for the relationship of US-based finance to new emerging centers of the world-system are addressed.

## DIMENSIONS OF FINANCIALIZATION

Financialization refers to “the increasing importance of financial markets, financial motives, financial institutions, and financial elites in the operation of the economy and its governing institutions, both at the national and international levels.” (Epstein 2002:3) Finance capital, footloose and flexible, interposes itself whenever arbitrage opportunities present themselves. It represents the increased power of abstract capital as opposed to productive capital. On another level, financialization is a policy choice of governments in alliance with internationally oriented financial institutions. It is a tool of accumulation pushed powerfully by the American state and other money center governments.

Robin Blackburn has characterized financialization, this growing and systemic power of finance and financial engineering, as “grey capitalism” because relations of ownership and responsibility have become weakened or “blurred.” He writes “In the end the largest and most famous of corporations have only a precarious and provisional autonomy within the new world of business – ultimately they are playthings of the capital markets” (Blackburn 2006:42). While perhaps somewhat exaggerated in the sense that financial markets respond to and anticipate changes in the real values of assets including the credit worthiness of corporations, and CEOs have discretion over strategic decisions in meeting market demands, these financial pressures exercise a powerful influence over how success is to be measured at any point of time. Blackburn (2006:43) is right as well when he suggests that investors consider the corporation itself as simply “an accidental bundle of liabilities and assets that is there to be reorganized to maximize shareholder value.” Today’s investors are far from the patient capital of the earlier period. Given the pressure on institutional investors to maximize short term returns there is a constant churning of assets and so pressure on companies to maximize quarterly earnings. The incentive structure makes this rational behavior but can produce irrational results in terms of the longer run health of companies and the system.

The US financial market is the largest in the world with 37 percent of global financial stock, 45 percent of global equities, and 51 percent of private debt security stock (McKinsey and Company 2006). In 2005 foreigners held more than half of US Treasury securities (up from 20 percent in 1975), 14 percent of US equities (from 4 percent thirty years earlier), and 27 percent of US corporate bonds (compared to only 1 percent three decades previous). Surplus funds have been attracted to the US market for a variety of reasons ranging from the desire of governments to hold greater dollar reserves against the threat of financial crisis and to hold down the value of their own currency to promote exports to the desire of the investor class around the world for higher risk adjusted returns. Because of the dominant position of the dollar close to two-thirds of foreign exchange official reserves are held in the US currency and 89 percent of all foreign exchange trades are against the dollar. The United States has been the innovator in financial instruments, for example asset backed securities, primarily real estate but extending to a large variety of future earning streams from auto loans and leases, credit card receivables, small business loans and other categories now valued in the trillions of dollars.

Financialization has proceeded very fast in the opening years of the new millennium. Between 2001 and 2004 daily foreign exchange turnover increased by 57 percent and daily trading in derivatives was up by 74 percent. In 2006 private equity firms controlled \$800 billion in capital, 300 percent more than five years earlier and hedge funds managed a trillion dollars compared to half of that in 2001. Importantly debt creation, private and government debt securities, accounted for more than half of the overall growth in financial assets from 2000 to 2004. Taken as a whole the corporate profits of the financial sector of the US economy in 2004 were 300.6 billion dollars compared to 534.2 billion for all nonfinancial domestic industries, or about 40 percent of all domestic corporate profits. They had been less than two percent of total domestic corporate profits forty years earlier, a remarkable indication of the growth of financialization in the American economy (Council of Economic Advisors 2006).

## FINANCIALIZATION AS A SOCIAL STRUCTURE OF ACCUMULATION

A crucial difference between the era of national Keynesianism and that of global neoliberalism is in the priority given to growth by the managerial capitalism of the earlier regulatory regime under which top executives benefited from the growth in the size of the firms they managed. The triumph of stockholder capitalism in the era of global neoliberalism has meant firms are pressed to extract every bit of surplus they can from stakeholders. This produces a pattern of slower growth and upward redistribution. To align corporate leaders with the single-minded pursuit of stockholder value stock options became the dominant source of executive compensation in the new institutional setting (on managerial capitalism see Chandler 1977; on the new financial capitalists see Baker and Smith 1998; and on the new ideology of shareholder value see Lazonick and O'Sullivan 2000). In practice encouraging executives incentives to maximize short term profit invites manipulating earnings to coincide with cashing options and to a shift in the firm's objective function to a new chosen growth-profit combination which exhibits higher profit and lower growth. Firms under the new incentive structure could grow faster but choose not to because that would reduce profitability (Stockhammer 2000). This often involved the greater use of financial gimmicks, many illegal as was increasingly revealed (Mills 2003). Gatekeeper conflict of interest proved substantial as accountants, bankers, lawyers, stock analysts, and corporate boards cooperated with questionable and illegal practices (Coffee 2006).

Financialization is a central part of the social structure of accumulation we call global neoliberalism. Innovations in computer power and information processing has been the basis for an increased ability to parse and price risk in new, highly complex ways so that the future can be bought and sold by turning expected future income streams into negotiable securities and through a host of derivatives, financial instruments which allow taking positions on future outcomes to either minimize risk of unexpected events or to speculate on their occurrence. The possibility of gaining control of assets with borrowed money and using the underlying capital as collateral for extensive borrowing puts a steady pressure on corporate leaders to use any surplus cash for share buybacks, and to take on debt for this purpose so as to make their companies less likely to be takeover targets. This is changing the fundamental nature of the business enterprise. Indeed, it is our assertion here that financialization represents a new dominant regime of accumulation.

The moments of structure and agency which determine the trajectory of financialization are complex and multifaceted. The slowing of growth and decline in conventional investment opportunities relative to accumulation of surplus in the 1970s and 1980s led to a seeking of more speculative outlets in finance. At the same time the push to maximize stockholder value and the greater use of options as a form of executive compensation encouraged shorter time horizons by corporate leaders. Floating exchange rates following the demise of the Bretton Woods system invited hedging strategies to minimize exposure to currency risk (and invited counterparty speculation). Innovation in, and lower cost of, information technology and explosion in computer power allowed for advances in innovation of risk pricing and packaging at low cost which allowed for explosive growth in structured finance as future income streams were transformed into negotiable collateralized debt instruments.

As the sheer number of people making their livelihood from finance and linked sectors grew and the investor class expanded thanks in part to tax expenditures such as 401(k) and other programs attracting money to mutual funds, a larger constituency allied with the extremely wealthy to become part of what can be understood in Gramscian terms as a hegemonic bloc materially rooted in gains from financialization. As Wall Street as opposed to manufacturing came to more powerfully dominate US capitalism the political influence of financialization advocacy grew, its goals and strategies endorsed with greater urgency by major political parties. While always a central component of any hegemonic coalition, the increased political power of finance accompanies and enhances its economic centrality. This recursive process is evident in recent elections, their financing, and the policy priorities of officials once elected. It can be argued for example Bill Clinton owed his presidency to Robert Rubin and other Wall Street boosters. Through the Clinton Administration Congressional members of finance committees

were showered with contributions to facilitate deregulation and especially to repeal New Deal era banking legislation which had segmented the industry and imposed safeguards against excessive risk taking. The coalition which brought George W. Bush to power was Sunbelt-oil-military-contractor-based. However by the 2004 Bush campaign was the recipient of a huge infusion of cash from Wall Street which in 2003 was his biggest donor base. The leading figures were prominent executives from Merrill Lynch and Lehman Brothers. This influence was cemented toward the middle of his second term when Henry Paulson head of Goldman Sachs became Mr. Bush's third Secretary of the Treasury. Its power is further demonstrated in recent "reform" bankruptcy legislation.

Internationally, financial liberalization has both preceded, and allowed the rapid inflow of short term borrowing. It has set the stage for crisis when the cycle turns and then is the pretext for greater liberalization to solve the crisis. In the countries effected by serious debt and banking problems financial adjustment is typically accompanied by poor performance across various social indicators including health outcomes and education. There have been general impacts on economies globally even if not of crisis proportions. Tightening by a major central bank limits liquidity globally and impacts financial markets. For example a rise in interest rates by the Bank of Japan means hedge funds which had borrowed cheaply in yen and invested in high yield assets elsewhere leveraging their money. The popularity of such carry trade meant knock-on impacts to high yielding currencies from New Zealand to Iceland. Financial liberalization and the need to protect against severe dislocation has also produced an underconsumptionist bias to the global economy in the 1980s and 1990s as countries restrain domestic demand out of fear of inflation which might discourage investors and produce capital flight.

## FINANCIALIZATION AND FRAGILITY

Fear of serious asset valuation loss has led to a spectacular growth in credit derivatives which allow investors to buy protection against defaults and other downside risks. These are sold mostly by the giant banks. JP Morgan Chase is said to have held some 2.2 trillion of credit derivative exposure as of mid 2006. If another wave of Enrons and WorldComs were to occur in the presence of such exposure the global financial system could be seriously affected. The very existence of such contracts produces moral hazard, greater risk is undertaken because the investor is insured. Lenders do not worry because they believe themselves protected. As a result they may not as a result monitor closely, or at all. Neither may those who sell the derivatives which can be quite complex. For the issuers these instruments may prove highly risky especially when speculative activity is in remote markets and arcane products like credit default swaps and catastrophe bonds. These are highly illiquid and cannot easily be sold off as many of the earlier innovations in securitization allowed. While losses to individual investors and local issuers may not be a major policy concern for international regulators the scale of speculation has increased dramatically.

The fastest growing segment of the industry (until recently overtaken by the explosion in private equity finance) is hedge funds which follow high leveraged strategies and are another US contribution to the growth of financialization. The typical "2 and 20" compensation scheme (two percent fees go to managers plus twenty percent of the profits) encourage and generously reward risk taking with other people's money. The reward structure promotes excessive risk taking. Investment banks put larger amounts of capital at risk, leveraging their own funds by borrowing vast sums. The size and increasing numbers of such funds, which according to the SEC controlled \$2.4 trillion in assets, pursue essentially similar strategies and so have pushed down returns encouraging still riskier behavior as more money piles into these vehicles creating the potential (signaled by the near bankruptcy of Long Term Capital Management in 1998) for serious systemic risk. Hedge funds bet using lots of leverage and often unhedged credit derivatives. Because of the existence of deep financial markets there is a general belief that these positions can be sold if need be. But while speculators are believed by financial theorists to be exploiting market inefficiencies and anticipating market movements (Paredes 2006) the potential for herd

error is often ignored until a major widely shared misjudgment occurs. As successful hedge funds attract entry by less skilled, opportunistic players and their less sophisticated customers the potentially successful opportunities for high returns may not match the amounts being thrown onto the market. Sooner or later hedge financing turns into Ponzi financing (Minsky 1992) It is not only highly leveraged players who then face the prospect of serious losses.

Hedge fund borrowers have become an important source of bank revenues and, as Morris Goldstein (2005:8) writes, “In an environment where flows into hedge funds are strong, where banks face strong competition from other suppliers of services to hedge funds, and where hedge funds are very important clients to banks, how heavily we can count on a regulatory model where banks are the agents primarily responsible for exercising oversight over the risk-management practices of hedge funds?” Since these hedge funds follow similar investment strategies, position mistakes, say in emerging markets, can trigger a rush to the exit. With the growing amount of capital seeking investment opportunities market pricing reflect little provision for risk as the IMF has pointed out. It warns of the possibility of illiquid market conditions for some of the new and complex financial instruments which could act to amplify a market downturn (International Monetary Fund 2006)

The wreckage of the collapse of such leverage would be considerable and could be triggered not only by a change in market sentiment but by a failure to settle trades with knock-on effects in highly leveraged interdependent market (as the collapse of Long Term Capital Management threatened to do in 1998). The rapid rise of debt and high leverage raises serious questions for systemic stability despite the presumed more sophisticated risk management tools employed by major banks – as a reading of the increasingly agitated *Global Stability Report; A Report by the International Capital Markets Department on Market Developments and Issues* released twice a year by the International Monetary Fund – suggests. There appears as well to be a concentration of risk. The US Comptroller of the Currency (Office of the Comptroller of the Currency 2004) reveals that five commercial banks account for 96 percent of the total notional amount of derivatives and for four of these five exposure equaled 230 percent or more of their risk-based capital. For banks and hedge funds higher leverage has become the general rule and are worrying (Geithner 2006). Whatever the systemic risk, there is just too much money to be made to turn cautious too soon. Even in the face of widespread loss after a period of caution the game is likely to resume. The question which remains to be answered by history is whether financialization is now so much the economy’s driving force means the amounts involved in a meltdown will bring the era of global neoliberalism itself to an end.

Amidst the thrust and counter thrust of those worried about such a prospect and those resolutely unconcerned, what needs to be added to the discussion is proper appreciation of the success US-based financial institutions have had and are likely to continue to generate from global financialization. There is need to analyze the prospects for such firms separately from the territorially-based productive economy of the United States. While I would not want to bet against a hubristic overreaching by unilateralist, militarist nationalism and the capacities of those fractions of the US ruling class which have led to adventurist and costly undertakings to adversely effect the future of the dollar, it is my judgment that the financial sector will continue to be strengthened by the likely trajectory of globalization. The issues of the US foreign debt and balance of payments receives attention, but from a longer term perspective of how economic power will be exercised and which interests will appropriate the lion’s share of future growth, it is the expansion of financialization and the role of US-based and US-controlled financial institutions which is important. In the next section of the paper the two dominant positions on US foreign debt are discussed. The position I take is at something of an angle to these more narrowly economic perspectives; it is that the future of the dollar depends on three things. The first two are surely familiar terrain. They are dependence on the political-military strength of the United States and its effectiveness in deploying its power and on willingness and capacity to reign in borrowing and keep debt creation within margins of safety. The third is the comparative advantage of US-based finance vis-à-vis other firms with which they compete. If US-based investment banks, private equity, hedge funds and the rest are able to keep innovating, earning economic rents from bold moves successfully executed and retain

their leadership as they operate around the world, they can perpetuate and expand capacity to restructure global financial markets and earn continued impressive economic rents along the lines pioneered by earlier money center hegemony.

## THE DOLLAR

The financial liberalization the United States has pursued has favored both the US as a debtor nation living well beyond its means and financial institutions irregardless of the price of a build up of serious global imbalances. From 1996 to 2004 the US current account deficit grew to \$666 billion from \$120 billion, requiring external financing of \$546 billion. These funds allowed the country's economy to grow rapidly without inflation but raised the issue of how much longer this could go on. In 2006 the US current account deficit was close to seven percent of GDP leading to fears that adjustment would come through a dramatic drop in the value of the dollar (Roubini and Setser 2004; Blanchard, Giavazzi and Sa 2005). Estimates of an unwinding of the dollar's current account deficit, financed by three-quarters of the combined current account surpluses of all of the world's surplus countries, suggest a potential collapse of the dollar by as much as thirty percent or more (Obstfeld and Rogoff 2005). Many economists and financiers, as George Soros (1998:26) has said, see "an acute financial and political crisis" which "if left unchecked will lead to the disintegration of the global capitalist system" and it is true that if one extrapolates trends the United States in a not distant future would absorb all the world's savings and then some having to make interest payments exceeding its own GDP, but like all simple minded trend projections this will not happen. Such a linear extrapolation does however suggest the seriousness of the growing imbalance.

Adjustment however wrenching does not, contra Cassandra-like predictions from George Soros and others, necessarily mean the disintegration of the global capitalist system despite the pain of the expected adjustment process which would bring a decline in US living standards. An increasingly financialized system will write down assets, reassign ownership claims, and reterritorialize accumulation away from the traditional industrial core. This all becomes clearer when one disentangles the significance of trade and capital movements. The official position, that of the Treasury and the Fed, is that the United States because of the strength of its economy attracts surplus savings from countries where savings exceed domestic investment opportunities. The alternative story has a number of elements. The first is that in a world of floating exchange rates, uneven growth, and the impact of interest rate policies (above all of the United States), lead to rapid movement of funds into and out of smaller economies often to devastating effect. To protect their economies countries have substantially built up reserves, holding U.S. Treasury securities and other dollar assets. Wealthy individuals fearing currency weakness have done likewise. Such developments produce large capital inflows for the United States since the dollar remains the dominant international reserve currency and the US the market of preference for global south exporters. The foreign savings in this telling are not really voluntary but driven by export competitiveness imperatives and the need to build dollar foreign exchange reserves. There is of course pressure everywhere to hold down the value of currencies and so enhance their international competitiveness, to squeeze unit labor costs, and stimulate growth; but export expansion at the expense of wage increases and currency appreciation leads to low domestic demand.

The official story can further be questioned by pointing out that the seeming high savings of the Japanese, Germans, and Chinese are not quite what they seem. It may be that Japan as an aging society needs to save more (as is argued by among others Bernanke 2005), but this does not explain the capital account surplus. Japan's current savings surpluses come from the business sector and are not explained by an autonomous expansion of national savings. Japanese firms with surplus capital, insurance companies and banks, find it difficult to lend internationally in yen and so are big buyers of dollars. The driver is the continued position of the dollar as the key currency. Ironically this means that appreciation of the yen could bankrupt some of these same firms if the yen value of their dollar holdings dropped

significantly. In Germany, another current account surplus country there has been wage disinflation in recent years producing greater export competitiveness (for the numbers see UNCTAD 2006). Even China where money wages in manufacturing are growing substantially (12-16 percent annually in recent years in industrial centers) is experiencing declining unit labor costs in manufacturing as labor productivity is rising at close to twenty percent a year (UNDP 2006); and of course the renminbi is being held down by government fiat. Chinese net saving is not particularly high compared to its forty percent annual investment rate.

The Treasury and Fed claim that there is 'a worldwide savings glut' (Miller 2005) can therefore be contrasted with a competitiveness interpretation. While high tech sectors in the US are doing well, industrial production is growing slowly (overall by five percent between 2000 and 2005), while consumption of durable goods increased by more than thirty percent in this period. It has been the hegemonic position of the United States that has permitted and encouraged this capacity to transfer purchasing power to the United States. I would further argue that the United States has been put in a considerably better position since the end of the Bretton Woods fixed exchange rate system. Not only does the world need more dollars for reasons already discussed, but the United States is freed of any obligation to make good dollar claims in gold, a requirement under Bretton Woods which limited the creation of dollars at the whim of Washington policy makers. It is for this reason that the rest of the world would benefit from a new global financial architecture. It is also the reason the United States resists a more balanced and so potentially more stable system.

These are two separate but conjuncturally connected aspects of the US financial position. The first is the debate over what is widely viewed as the irresponsible behavior of the US government manifest in the impacts of large and continuing budget deficits. There is reason, noted above, to think that the fiscal policies of the United States are not sustainable and that financial markets may come to heavily discount federal debt instruments and there is the retort that the successful achievement of US-based financial institutions and transnational corporations in venues outside the nation's borders which draw capital from investors globally can grow without creating major difficulties. As to the more optimistic position, while US-based capital has been exceedingly successful, the country has become dangerously indebted.

The usual either/or, it is a problem or it is not, policy discussion proceeds innocent of any awareness of the importance of the stakes to finance sector participants and indeed to the gains from such policies to the country at large. Use of the dollar as the international medium of exchange favors US banks and financial interests more broadly and makes the US antagonistic to multilateral arrangements such as increasing global liquidity through expansion of Special Drawing Rights. The United States opposes European proposals for currency management including those for a target zone regime. In Asia, Washington has opposed a regional lender of last resort facility. For Washington policy makers the cost of addressing global imbalances is paid in a loss of US hegemony and the economic gains continued imbalances bring. It would take a major crisis to force the US to give up what in Charles De Gaulle's phrase is its "exorbitant privilege" and to accept something like Keynes' proposed bancor world currency and other symmetrical adjustment mechanisms. The appeal of continued growth of financialization, of more debt and leverage, speculation and hedging in the face of potential volatility to American capital is thus powerful. Whether the world-system comes to be centered in Asia only time will tell but the signs are there. In such a transition the allure of maintaining the position of US capital by relying on finance is evident.

A decline in the value of the dollar increases rest of the world exports to the United States. This creates American jobs and helps domestic producers increase their exports. It also makes US assets cheaper for foreign investors in their own currencies and encourages tourism and shopping sprees in the United States all of which helps the US reduce its balance of payments deficit. Likewise there is increased pressure on exports to the US. Since American liabilities are denominated in dollars and its foreign assets are not as heavily in its own currency, devaluation improves its position. The United States also benefits from its special privilege in terms of seigniorage rents. Well over half of all US coins and

currency circulates outside the United States. World trade is invoiced in dollars as are almost all commodity markets. The rest of the world exchanges real goods and services for this token money. American financial markets draw in capital from the rest of the world, the dollars generated by the world's need for dollar reserves and export oriented economies governments desire to hold down the value of their domestic currencies. If the dollar holds steady or declines in a controlled manner the US benefits. If there is fear of, or the actuality of, a serious drop and a flight from the dollar this would be a very different matter. Already the dollar price rise of oil has not brought a commensurate increase in income to producers who spend their money outside the dollar zone. OPEC now calculates the modified Geneva+1 basket. Were it to insist on payment in such a currency basket (which is weighted by its collective merchandise imports) this would lead to a further significant decline in the value of the dollar.

### **Financialization and the World-System**

That there is potential for systemic crisis present in a world in which leverage and risk may be expanding beyond tolerable bounds is widely recognized. Whether such crisis will occur from any other flash points discussed in this paper is unknowable. Regulators are active consolidating protective measures for a borderless world even as market players move the frontiers of financial market innovation (Geithner, McCarthy and Nazareth 2006). The growth of financialization continues basically unimpeded apace. Given existing constraints and incentives, foreigners are investing globally through the agency of US-based financial institutions and transnational corporations and earning good returns for doing so. The amount of capital coming into the country is two times the current account deficit of the United States. The rest is going out again. The continuation of such flows rests on U.S. structural power in the international political economy, confidence in the value of the US dollar, and the capacity of the debt-driven US economy to continue to be a motor of a global economy. Along such lines some economists embrace what has come to be known as the Bretton Woods II perspective which asserts that both debtors and creditors have a vested interest in preventing the dollar from losing value. American demand for goods and services paid for with borrowed funds coincides with the interests of exporters and investors. The US thus absorbs savings generated elsewhere, provides markets for other countries, and channels global investments through the mediating role of American financial institutions and transnational corporations. In such a view imbalances are likely to persist for some time and will be resolved with a smooth adjustment in interest and exchange rates (Dooley, Folkerts-Landau and Garber 2006).

While one would hope for such a benign outcome most analysts see a dangerous high stakes game being played. Assuming it can be sustained, the US will continue to benefit from the overvalued dollar and its stunning capital account surplus. The costs of addressing this imbalance would be great for other countries. It is this which gives those who hold to the Bretton Woods II perspective the sense that the current situation can be prolonged into the middle term. But the strains are showing and systemic breakdown is feared by others. Failure to develop a coordinated strategy to deal with the problem as Charles Dallara, managing director of the influential Institute for International Economics suggests, is to "roll the dice and to leave it to the markets to reduce global imbalances" (Guha 2006:4). The manner in which markets might do this could prove harsh. While such dangers are widely recognized, and surely appreciated in Washington and on Wall Street, the huge returns to US financial power, and continued political power, from the growth of a dollar-based globalized financialization are of unquestionable benefit despite any and all stability risk and goes unquestioned despite the stagnation of real wages and the growing insecurity it imposes on the majority of Americans. If the dollar loses its safe haven function and its status as a reserve currency to any significant degree, both unthinkable even a short while ago the dollar would decline precipitously and this cannot be ruled out. The only response the U.S. could make would be to raise interest rates. This would help the dollar but hurt domestic growth. It is the choice once Great Britain made to help its financial sector at the expense of its industrial competitiveness.

From this examination of financialization in the contemporary period that the United States it does appear to be on the historical trajectory of previous great powers. As described by Arrighi

(2004:536):

“...one kind or another of financialization has always been the predominant response to the overaccumulation problem of the established organizing centers of the system of accumulation. Thanks to their continuing centrality in networks of high finance, these centers have been best positioned to turn the intensifying competition for mobile capital to their advantage and thereby reflate their profits and power at the expense of the rest of the system. Over time, however, financial expansions have promoted the geographic relocation of the centers of capital accumulation by rerouting surplus capital to states and regions capable of ensuring a more secure and profitable spatial-temporal fix to the overaccumulation crisis. Previously dominant centers have thus been faced with the Sisyphean task of containing forces that keep rolling forth with ever renewed strength.”

A study by PriceWaterhouseCoopers (2006) forecasts that in the year 2050 the Chinese economy will be almost as large as that of the United States in dollar terms with India which has been the fastest growing in economy in recent years the third largest. They predict Brazil's economy in 2050 to be as large as Japan's, the Indonesian and Mexican economies to be larger than those of the UK and Germany, and expect the 'E7' (Brazil, China, India, Indonesia, Mexico, Russia and Turkey) to be around 25 percent larger than the current G7 – and to be driving the growth of the global economy. Whatever one may think of the details of such projections there is little doubt that momentous changes in relative nation state economic standing are in the offing. The questions of ownership claims and financial assets at mid century are another question. Looking at today's outsized rentier claims of Dutch and British capital (Epstein and Jayadev 2005) one suspects that the position of large asset holders domiciled in the United States in mid century may be impressive. The relative decline of the territorial United States economy is likely to be accompanied by the continued prosperity of the top ten percent of the US income distribution, and within that the top one-tenth of one percent of the population which has in recent years already increased its lead over the rest of the country to record levels (Piketty and Saez 2006).

Disappointing social progress during the decades of rapid globalization strongly support the view that the two decades 1960-1980 during which national Keynesianism reigned was a far more successful time overall for global development than the quarter century and counting of global neoliberalism during which economic growth and social progress for the vast majority countries has been significantly slower (Weisbrot, Baker, and Rosnick 2005). Real global growth averaged 4.9 percent a year during the Golden Age of national Keynesianism (1950-1973). It was 3.4 percent between 1974 and 1979; 3.3 percent in the 1980s; and only 2.3 percent in the 1990s, the decade with the slowest growth since World War II (Maddison 2001). The slowing of the real economy led investors to seek higher returns in financial speculation and the inventiveness of the financial sector in developing new products to meet the needs of those wishing to protect against the risks inherent in a globalized economy in which foreign exchange and interest rate risk had increased, permitted and encouraged by the greater capacity and lower information costs computerization and new technologies provided, allowed for an unbundling of risk and the ability to find willing buyers for different sorts of risk instruments of the sort discussed earlier. The increased liquidity and lower costs of borrowing encouraged in turn further expansion of finance. The coincident trends of growing inequality and insecurity on the one hand and the spreading power of rapid financialization do not suggest a smooth continued expansion path for a society based on increased debt and growing leverage.

Dissatisfaction with low dollar returns on their foreign reserves has lead an increasing number of countries from Brunei, Qatar and Kuwait to Russia, China and Korea to Norway, Australia and Canada to set up sovereign wealth funds to invest government reserves in higher risk-high return investments instead of simply holding their money in US Treasuries and other lower yield securities. Together these funds are larger than the largest pension funds and private equity funds. They are buying into among other investments the more successful US-based financial players. Wisely they are giving up voting

rights when they do so as Abu Dhabi did when it bought 7.5 percent ownership in Carlyle and China did when it purchased 9.9 percent of the Blackstone Group. These funds are growing rapidly in size and will increase their influence as they learn to manage their money. They may increase their stakes in US-based financial institutions as the US did in taking over the older houses in London, strike out on their own, or both. The 2007 Industrial and Commercial Bank of China's \$5.5 billion purchase of twenty percent of Standard Bank of South Africa, the largest overseas investment by the Chinese and the largest foreign direct investment in Africa may be indicative.

Such considerations do suggest that it is useful to examine the changes in the mode of regulation of capitalism in the contemporary period in the context of an appreciation of the relevance of historical precedents in the world-system of a seemingly natural trajectory in which great powers, that at one time dominate the world economy, come to lose their position of leadership and as a result turn to a dependence on financial skills and institutions build during the earlier period of hegemony. It also suggests stepping back from grand theorizing to consider working class responses to the contradiction of the distribution of the costs and benefits of further financialization.

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