Global financial bubbles and capitalist crisis

CENTRE FOR CIVIL SOCIETY

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World Forum for Alternatives
and the Network of Artists and
Intellectuals in Defense of Humanity
Workshop on the Financial Crisis

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OUR OBJECTIVE IS TO ADVANCE SOCIO-ECONOMIC AND ENVIRONMENTAL JUSTICE BY DEVELOPING CRITICAL KNOWLEDGE ABOUT, FOR AND IN DIALOGUE WITH CIVIL SOCIETY THROUGH TEACHING, RESEARCH AND PUBLISHING.

CENTRE FOR CIVIL SOCIETY

South Africa's 'Social Movements United' march from Alexandra Township to the World Summit on Sustainable Development in Sandton, 31 August 2002

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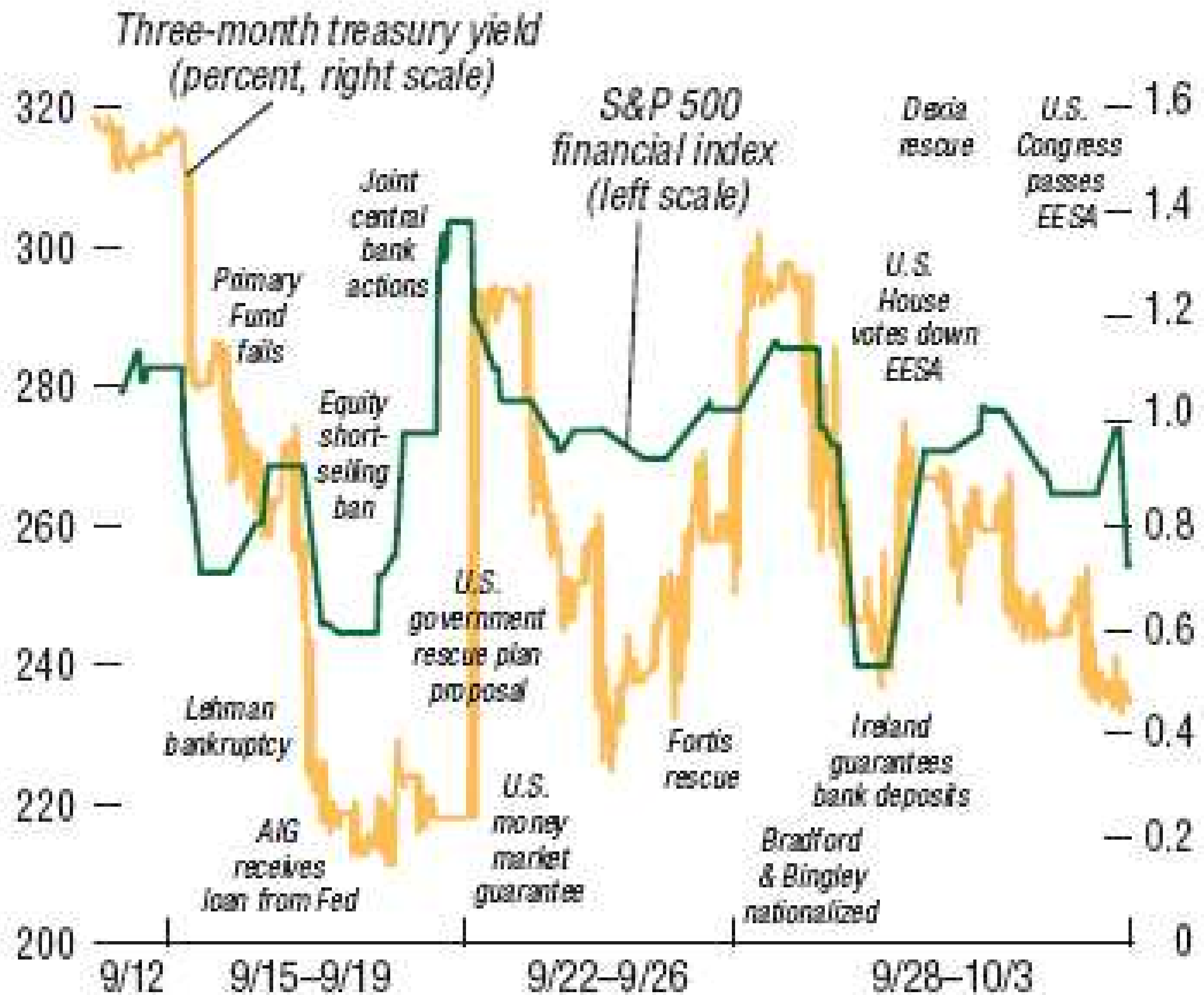
These slides cover new data:

1) Background: deep-rooted causes
2) Financial capital takes over
3) Real estate speculation
4) Financial market volatility
5) Stock market devaluations
6) Housing devaluations
7) Financial losses
8) Is inflation a way out?
9) Currency movements are a key variable

Regrets, no conclusions yet – just a review of recent IMF data, *with a few side remarks*



Sources: Bloomberg L.P.; and IMF staff estimates.
Note: EESA = Emergency Economic Stabilization Act.

Autopsy of financial meltdown, September 2008

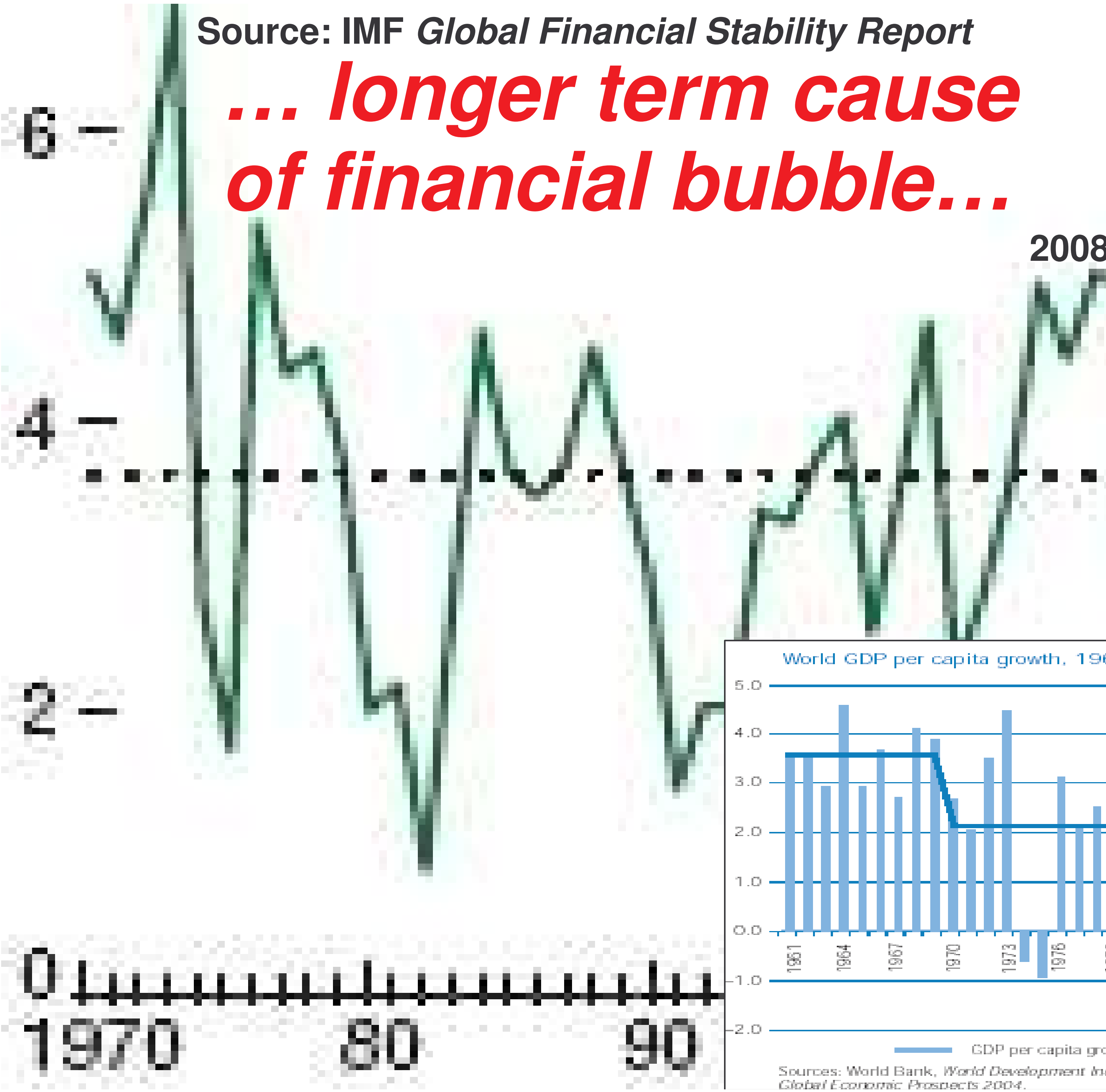
What lies deep below current financial bubble?…

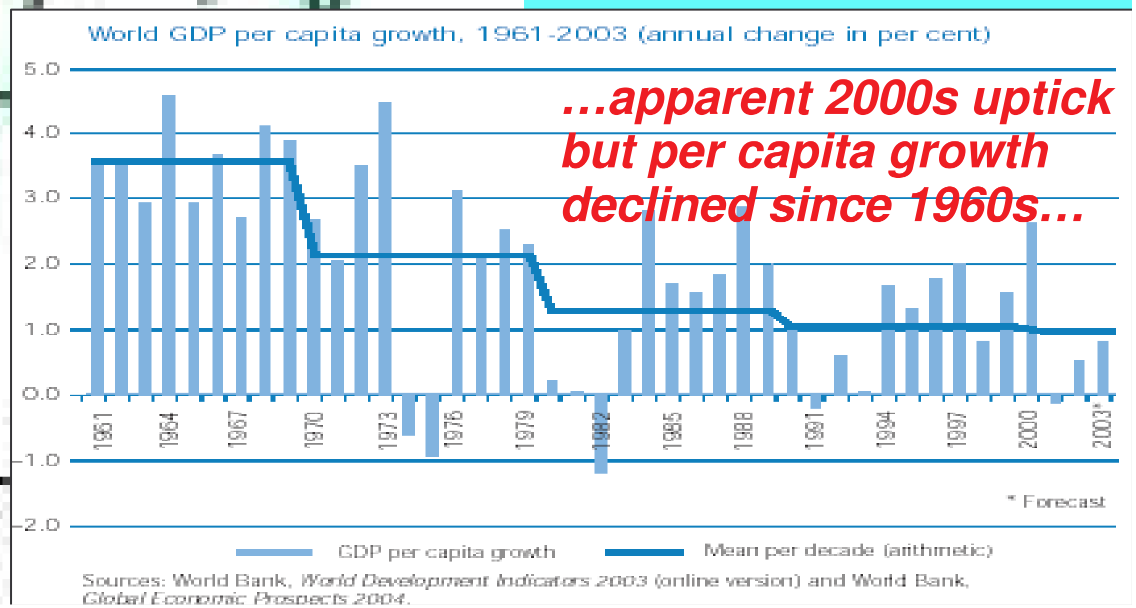
Source: IMF, *Global Financial Stability Report*

1) Background: Stagnant global real annual GDP growth, 1970-2008

Source: IMF *Global Financial Stability Report*

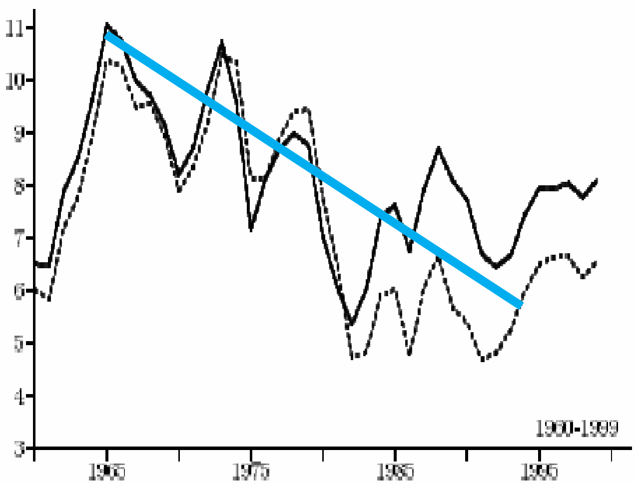
… longer term cause of financial bubble…



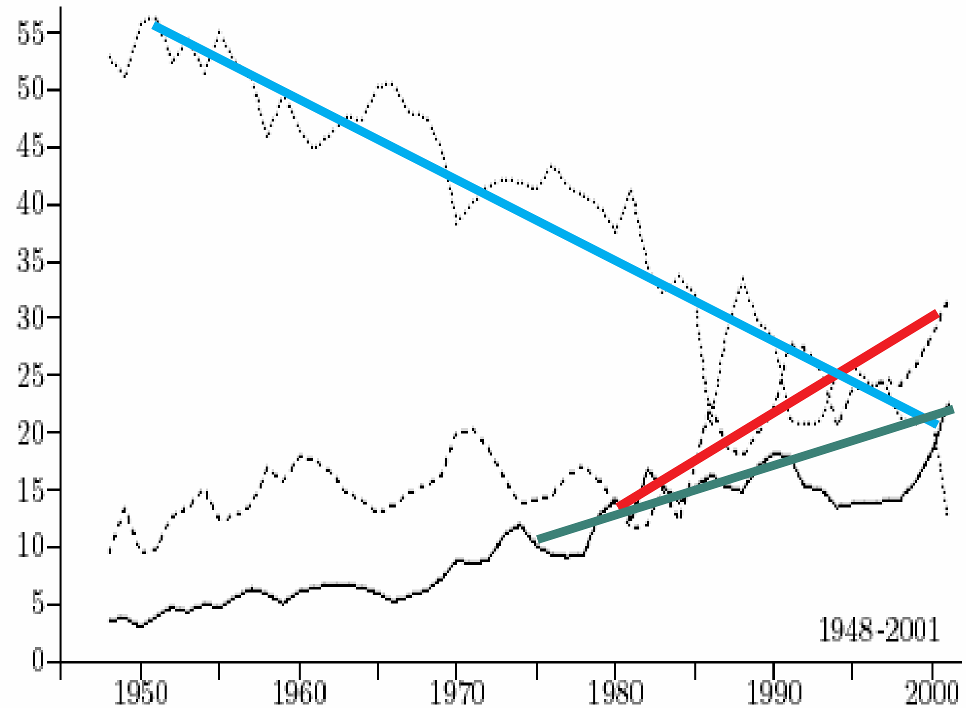


Root ‘overaccumulation’ process: source of declining US profits during globalisation/financialisation era

Figure 3 US, nonfinancial corporations: Profit rates prior to the payment of real interest (——) and after (-----), %



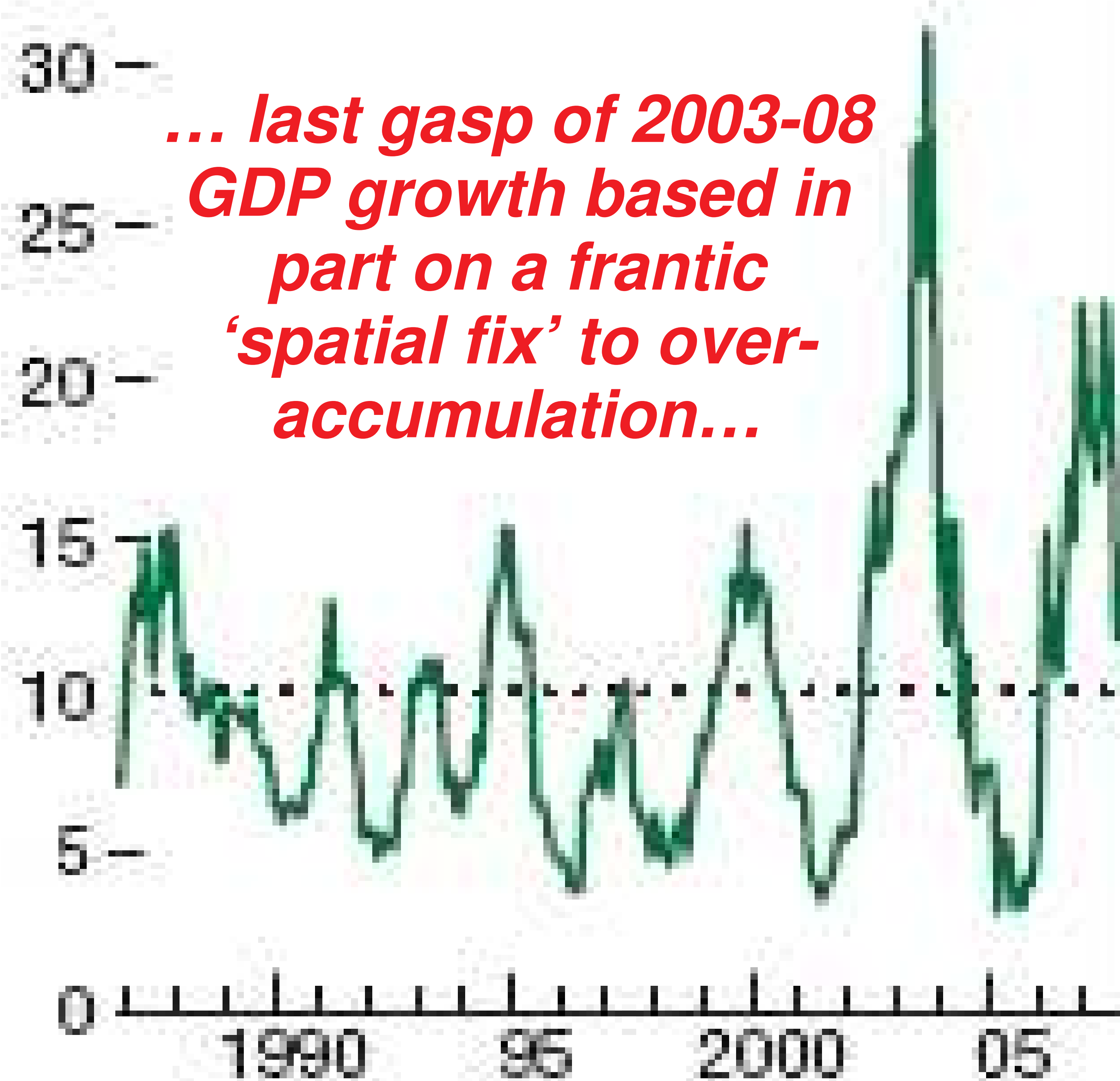
In the first series, profits are equal to the net product minus the cost of labor, and business and profit taxes. They are divided by the net worth (total assets minus debt). For the second series, real interest is subtracted from profits, *i.e.*, interest minus a correction for the depreciation of debt resulting from inflation.



Rest of the world: (——); Financial sector: (-----); Manufacturing: (·········)

Profits are measured before profit taxes. The *rest of the world* corresponds to the excess of profits made on US investments abroad over the profits made by the rest of the world on foreign direct investment in the US. (These profits may remain in the country where the investment is made.) Trade, Contruction, Public Utilities, Transportation and Communications, and services are not represented.
Source: NIPA (BEA).

US corporate profits derived much less from manufacturing products;
much greater sources of profits came from abroad;
profits also came more from returns on financial assets.
Source: Gerard Dumenil and Dominique Levy



Global real trade growth

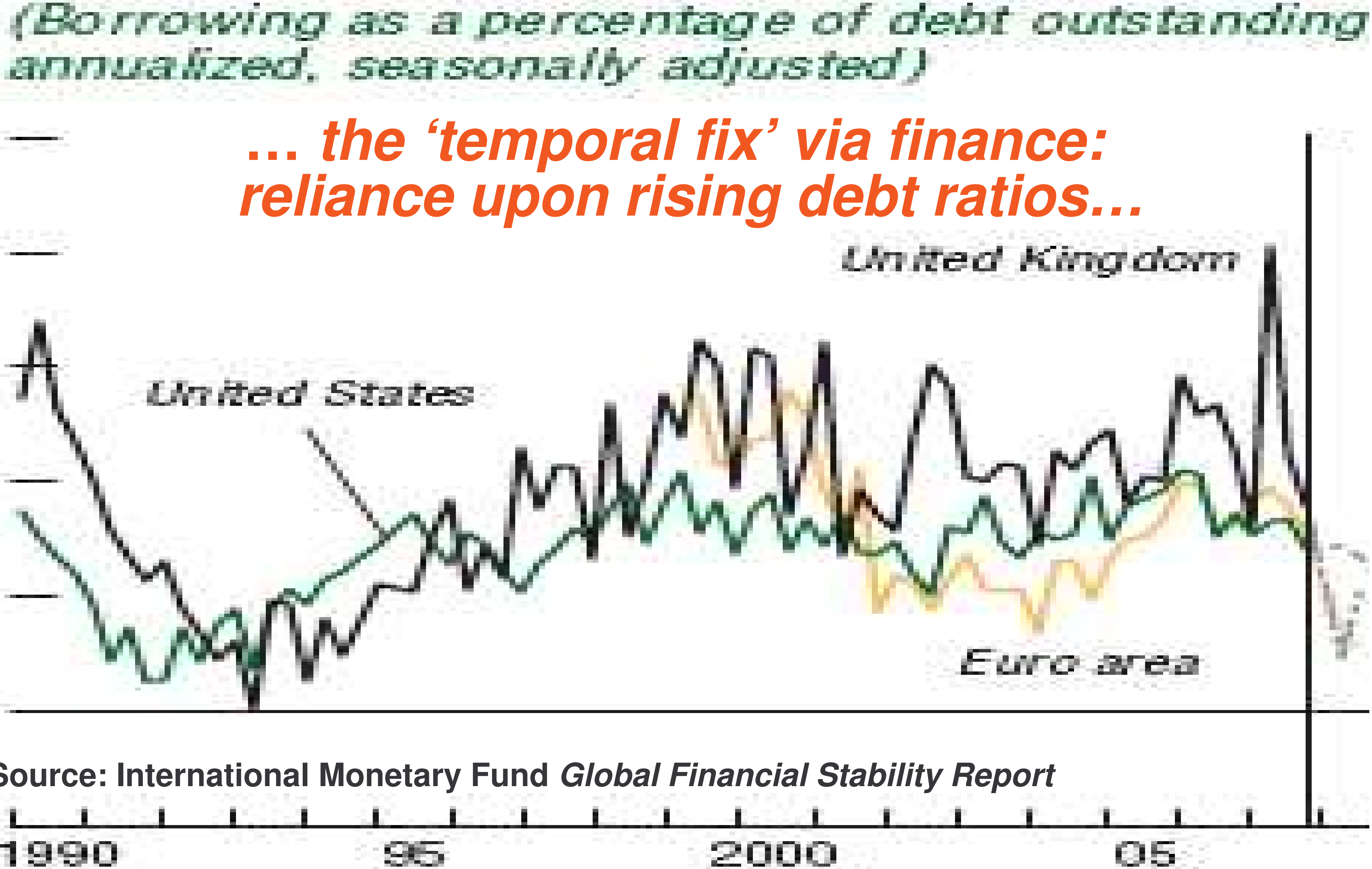
(% per year) 1985-2008

(especially driven from E.Asia)

Source: IMF *Global Financial Stability Report*

(as implied by Baltic Dry Index)

2) In the West, financial capital takes over

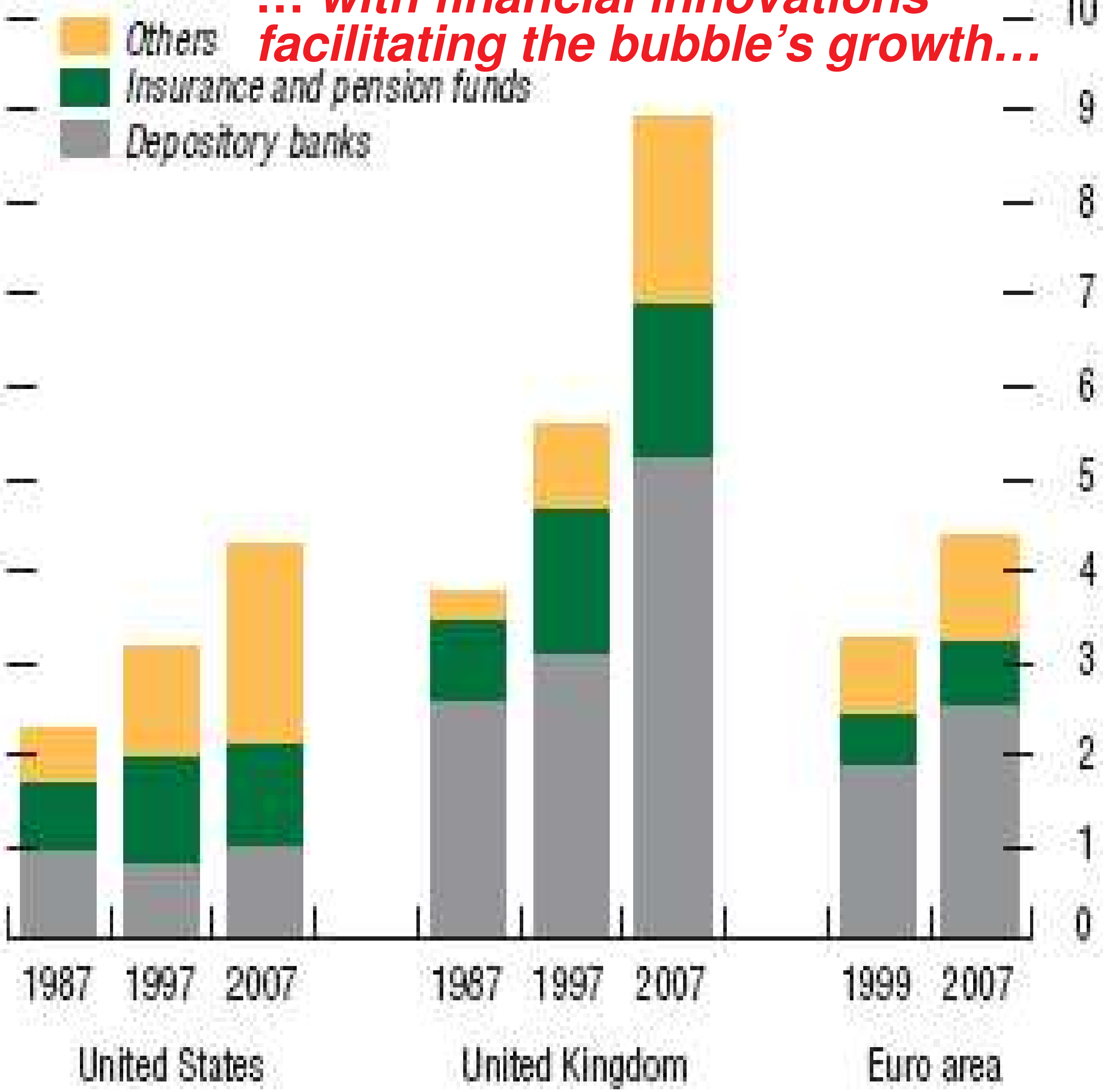


… the 'temporal fix' via finance: reliance upon rising debt ratios…

Source: International Monetary Fund *Global Financial Stability Report*

Financial bubbling in the US, UK and Euroland, 1987-2007: financial assets/GDP

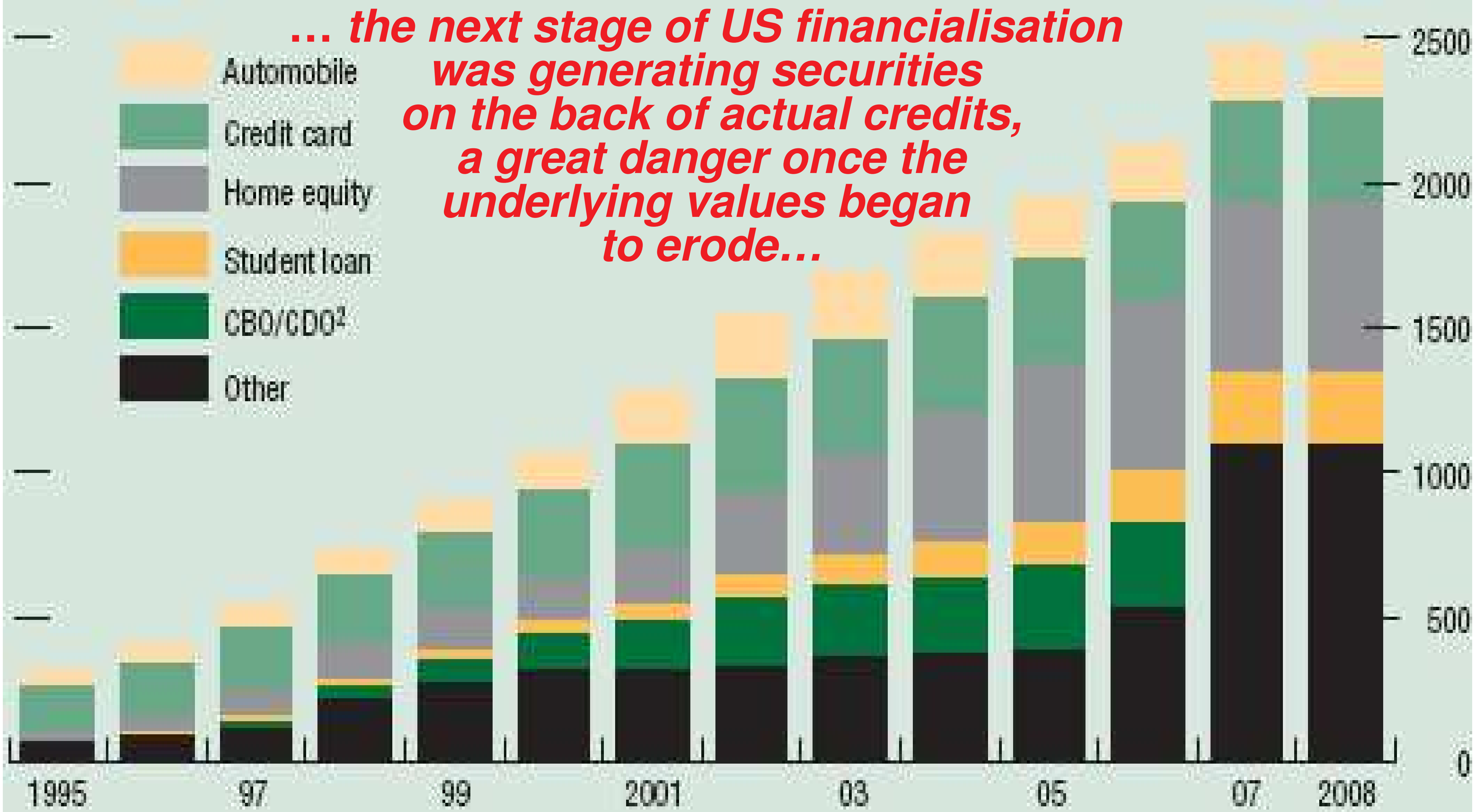
… with financial innovations facilitating the bubble's growth…



Source: IMF *Global Financial Stability Report*

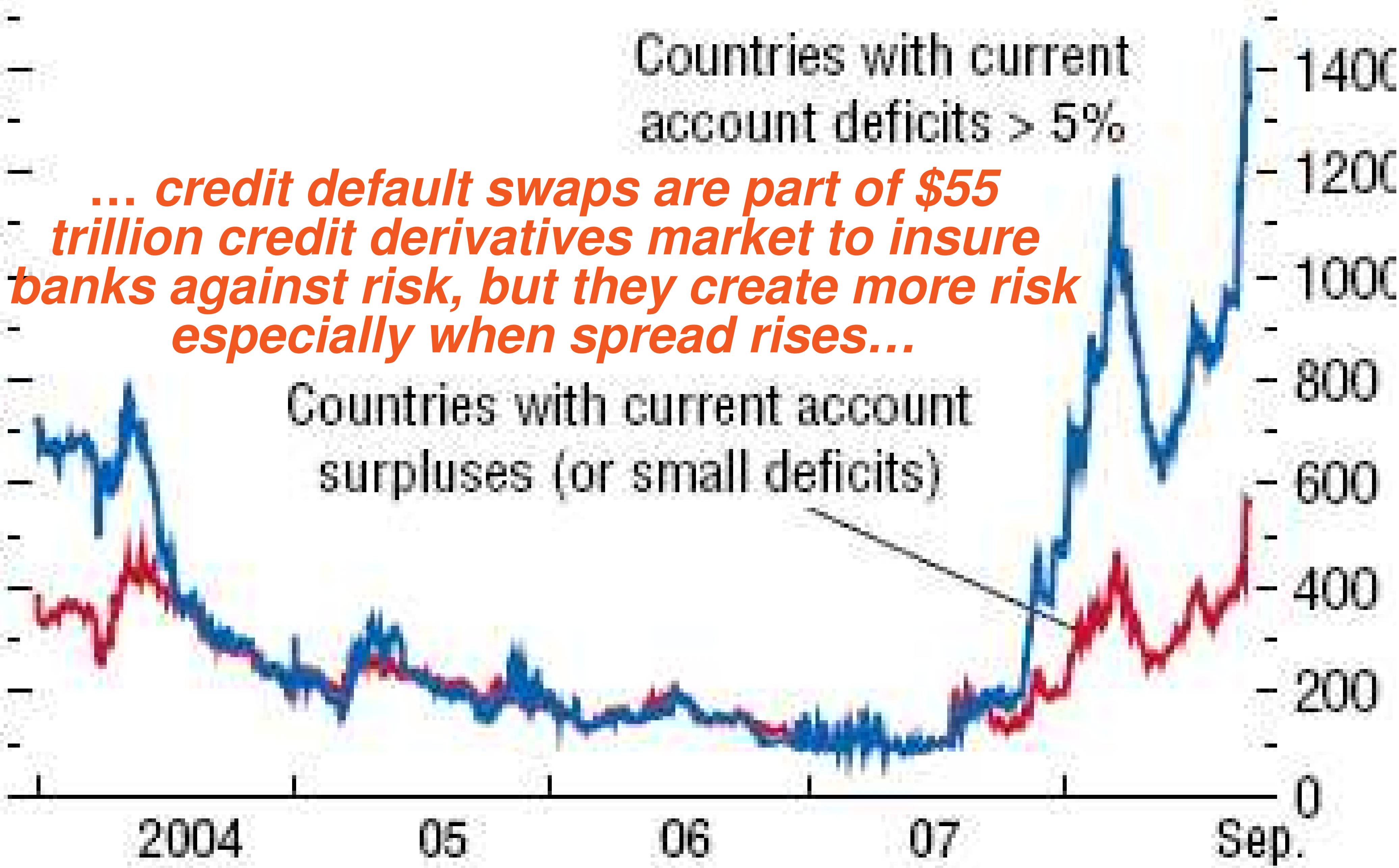
Debt underlying US asset-backed securities, US$ bn

Source: International Monetary Fund *Global Financial Stability Report*



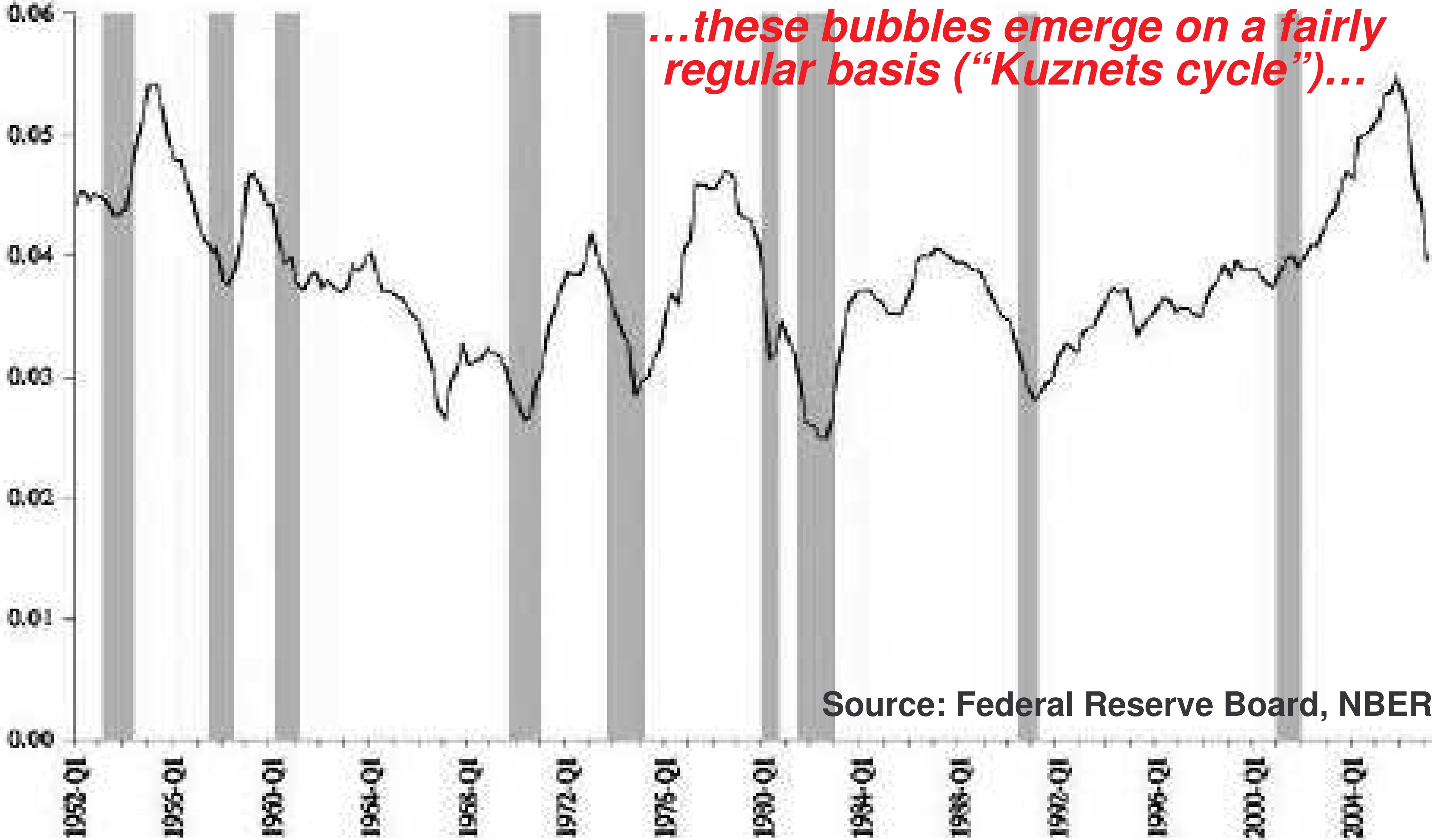
²Collateralized bond/debt obligations; for 2007 and 2008 Q1, CBO/CDO amount outstanding is included in Other.

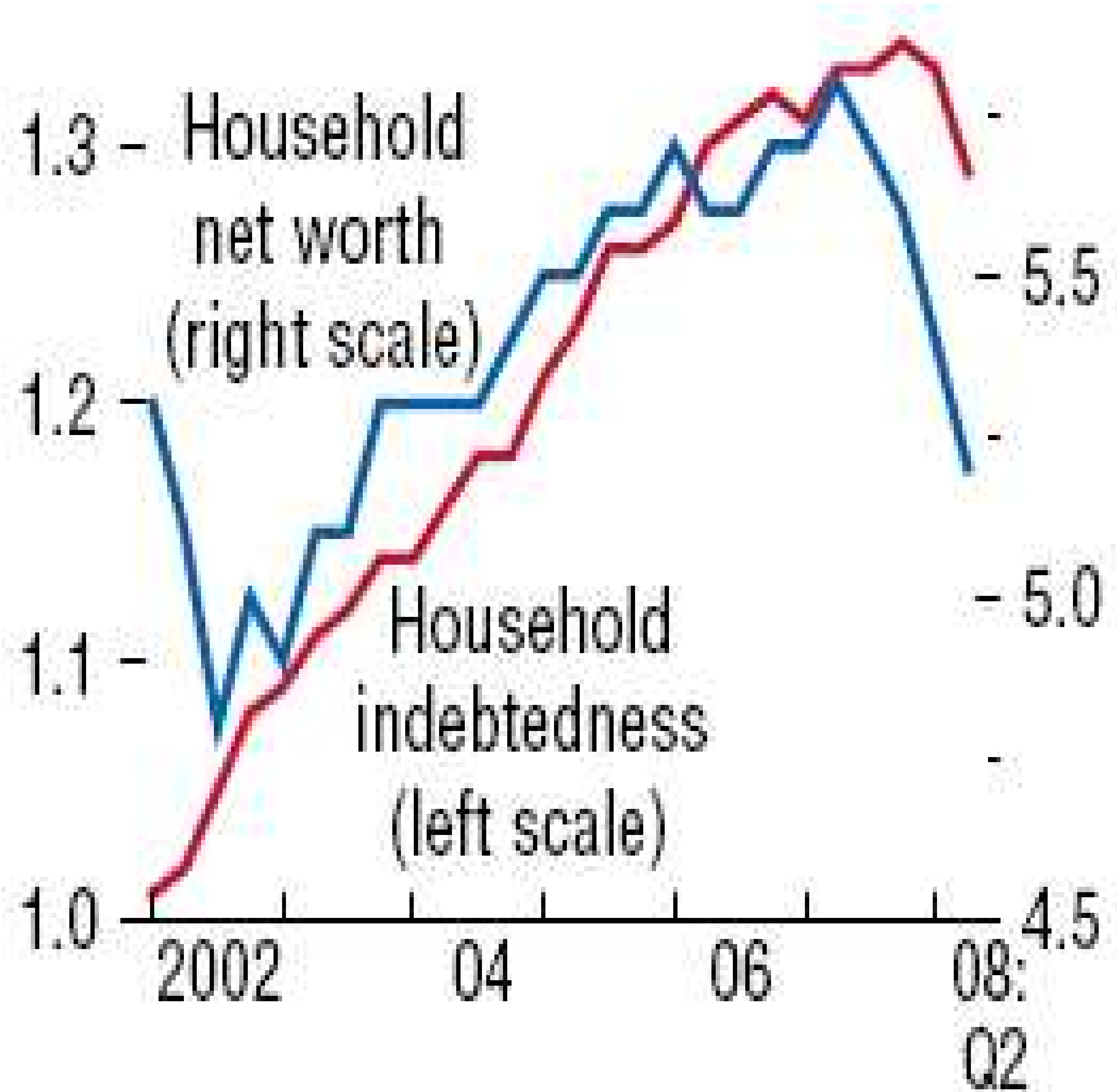
Worst threat: credit default swap spreads, 2004-08



Source: International Monetary Fund, *Global Economic Outlook*, October 2008

3) Real estate speculation: US housing investment as % of GDP, 1952-2007





Household net worth and debt in the US

…artificial housing bubble as US households built real estate empires on debt…

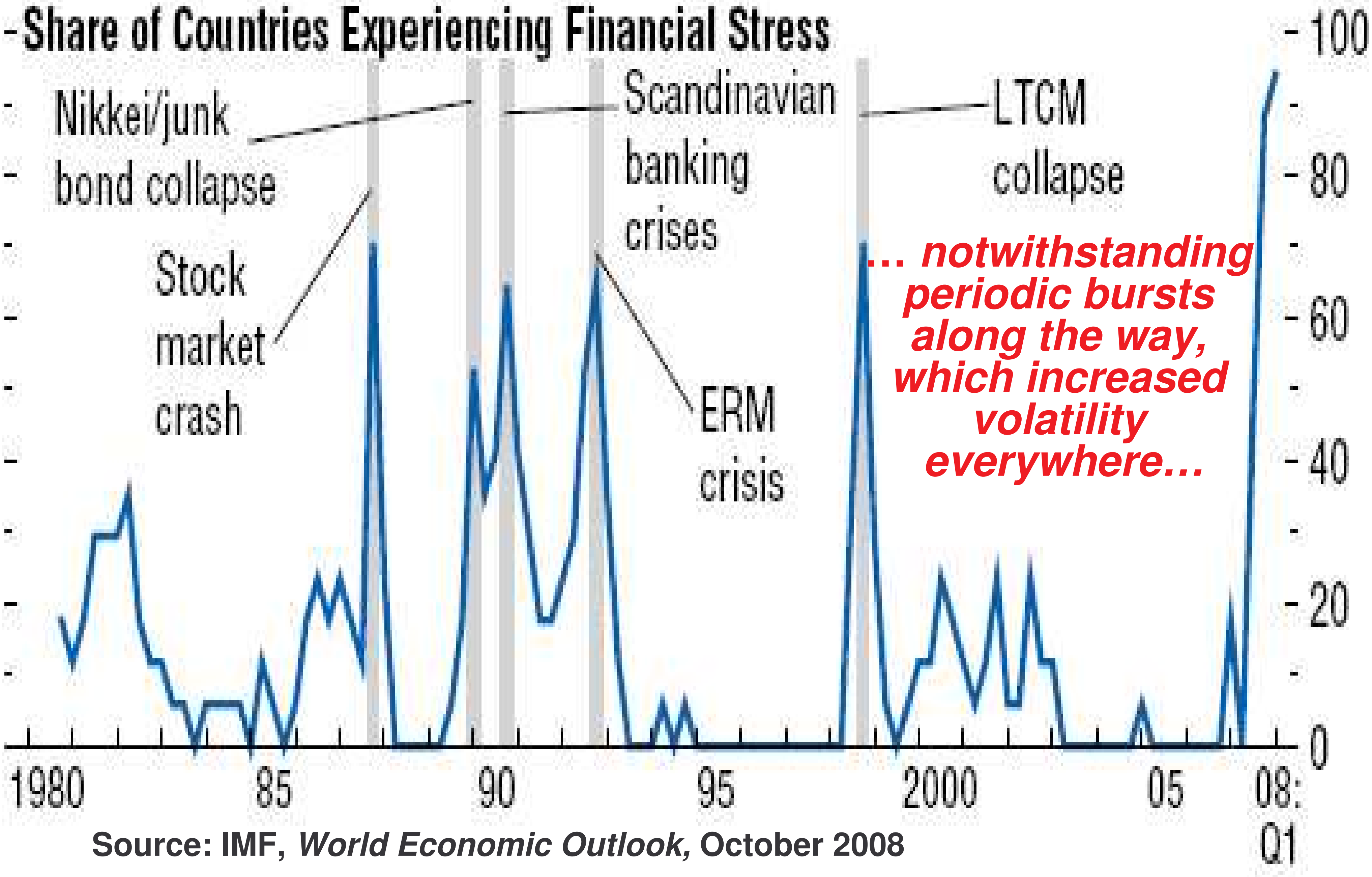
Source: IMF, *World Economic Outlook,* October 2008

US & other housing bubbles (2002-06 prices)

… but not only the US, most major economies witnessed real estate speculation…

Source: Federal Reserve Board, NBER

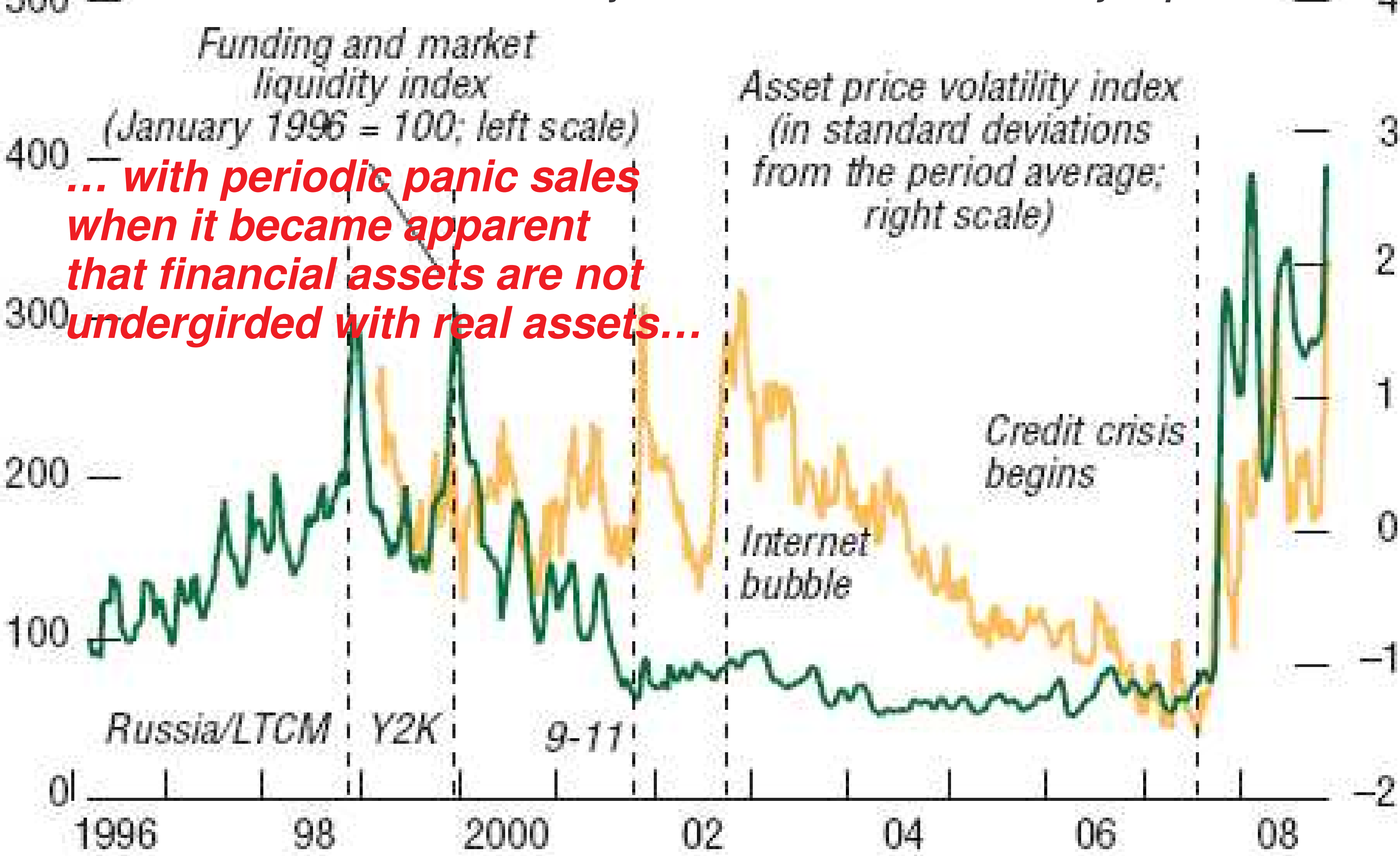
4) Financial market volatility and contagion



Source: IMF, *World Economic Outlook,* October 2008

Financial market volatility, 1996-2008

Source: International Monetary Fund *Global Financial Stability Report*



… with periodic panic sales when it became apparent that financial assets are not undergirded with real assets…

5) Stock market devaluations (since 1994)

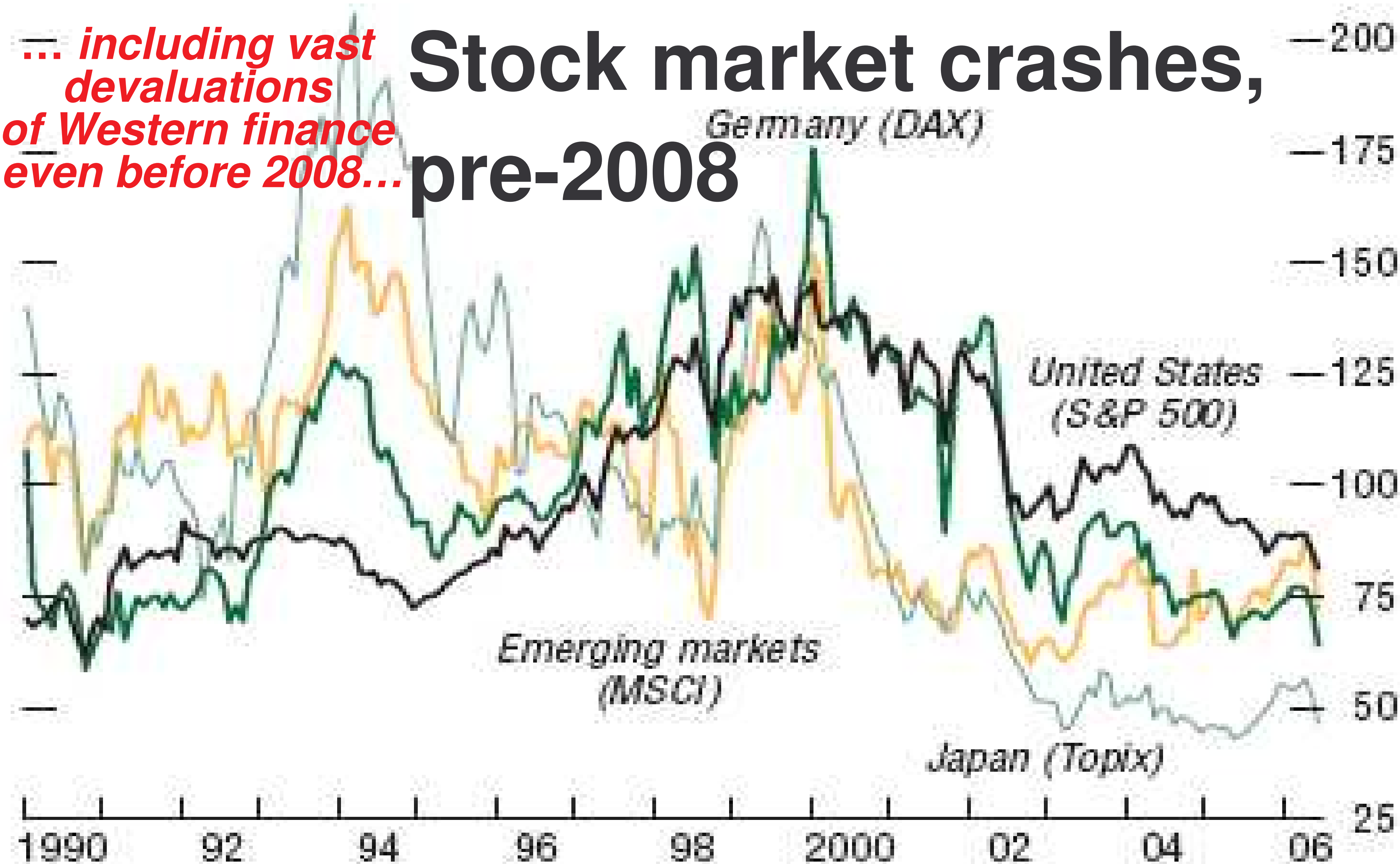
Source: International Monetary Fund *Global Financial Stability Report*

… huge losses especially in Third World stock markets, e.g. Thailand and Indonesia 90%+ crashes in 1998…

	Peak to trough	Equity Price Index (percent change)		Equity Market Capitalization/GDP		
		Rise to peak	Peak to trough	At peak	At trough	Difference
Emerging markets						
Argentina	Feb. 2000–June 2002	86	–85	23	13	10
Brazil	July 1997–Jan. 1999	134	–69	74	35	39
Hong Kong SAR	July 1997–Aug. 1998	99	–60	337	152	186
Indonesia	Jan. 1997–Sep. 1998	134	–92	42	10	32
Korea	Apr. 1996–Aug. 1998	100	–83	37	14	23
Mexico[1]	Nov. 1994–Feb. 1995	71	–64	28	25	3
South Africa	Jan. 1996–Aug. 1998	188	–64	214	106	109
Thailand	May 1996–Aug. 1998	174	–93	80	16	65
Memorandum item:						
Advanced economies						
Germany	Feb. 2000–Sep. 2002	74	–63	81	31	51
Japan[2]	Dec. 1989–July 1992	928	–52	140	55	85
United Kingdom	Dec. 1999–Mar. 2003	122	–47	200	88	112
United States	Aug. 2000–Sep. 2002	235	–46	180	98	82

Stock market crashes, pre-2008

… including vast devaluations of Western finance even before 2008…



Sources: Thomson Financial I/B/E/S; and IMF staff estimates.

Volatile $ flows into US stock market, 1990-2008

… but also in the North, e.g. $7 trillion devaluation in even New York, 2000-02…

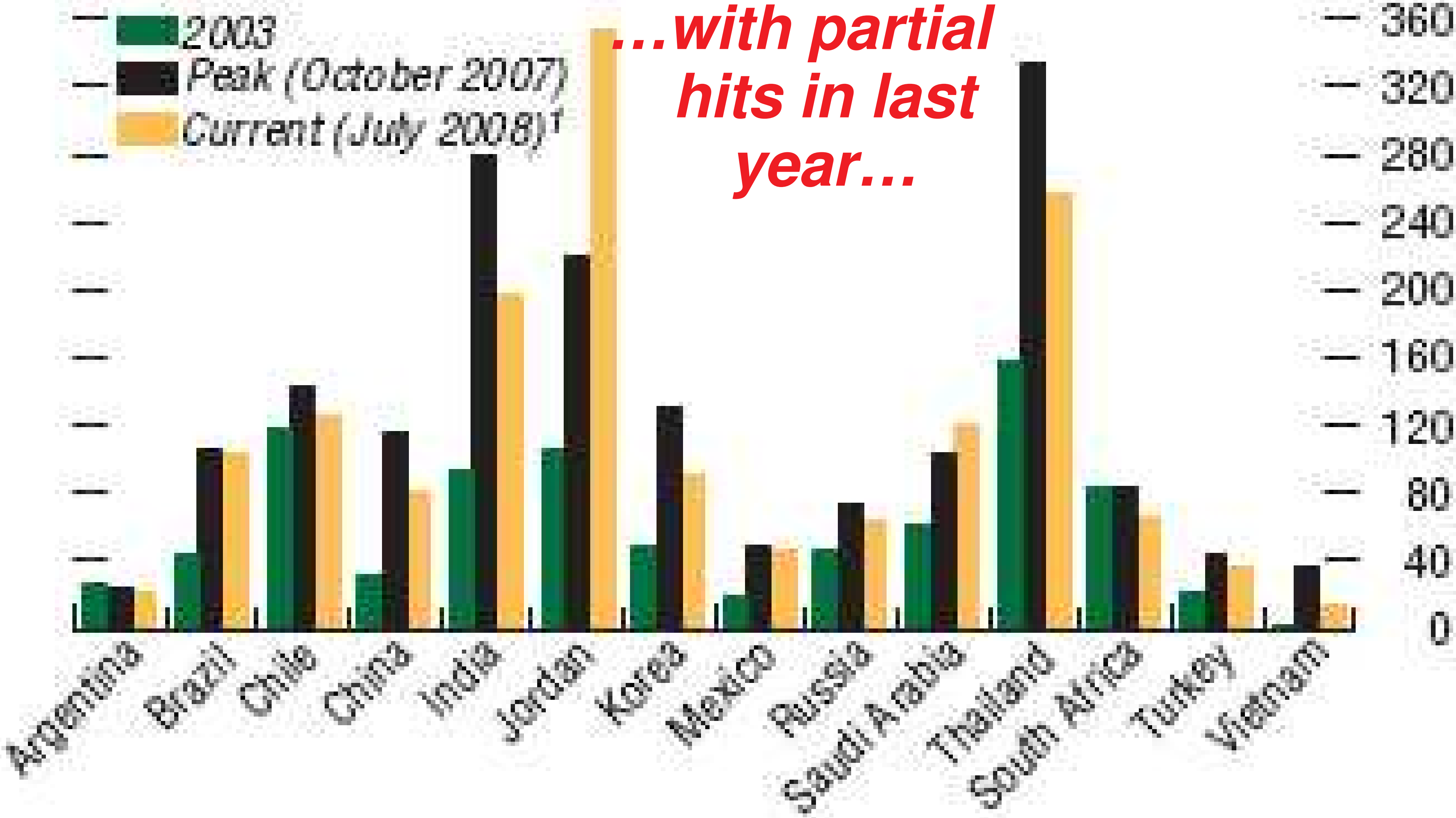
Source: International Monetary Fund *Global Financial Stability Report*

Stock market volatility: emerging markets

Source: International Monetary Fund *Global Financial Stability Report*

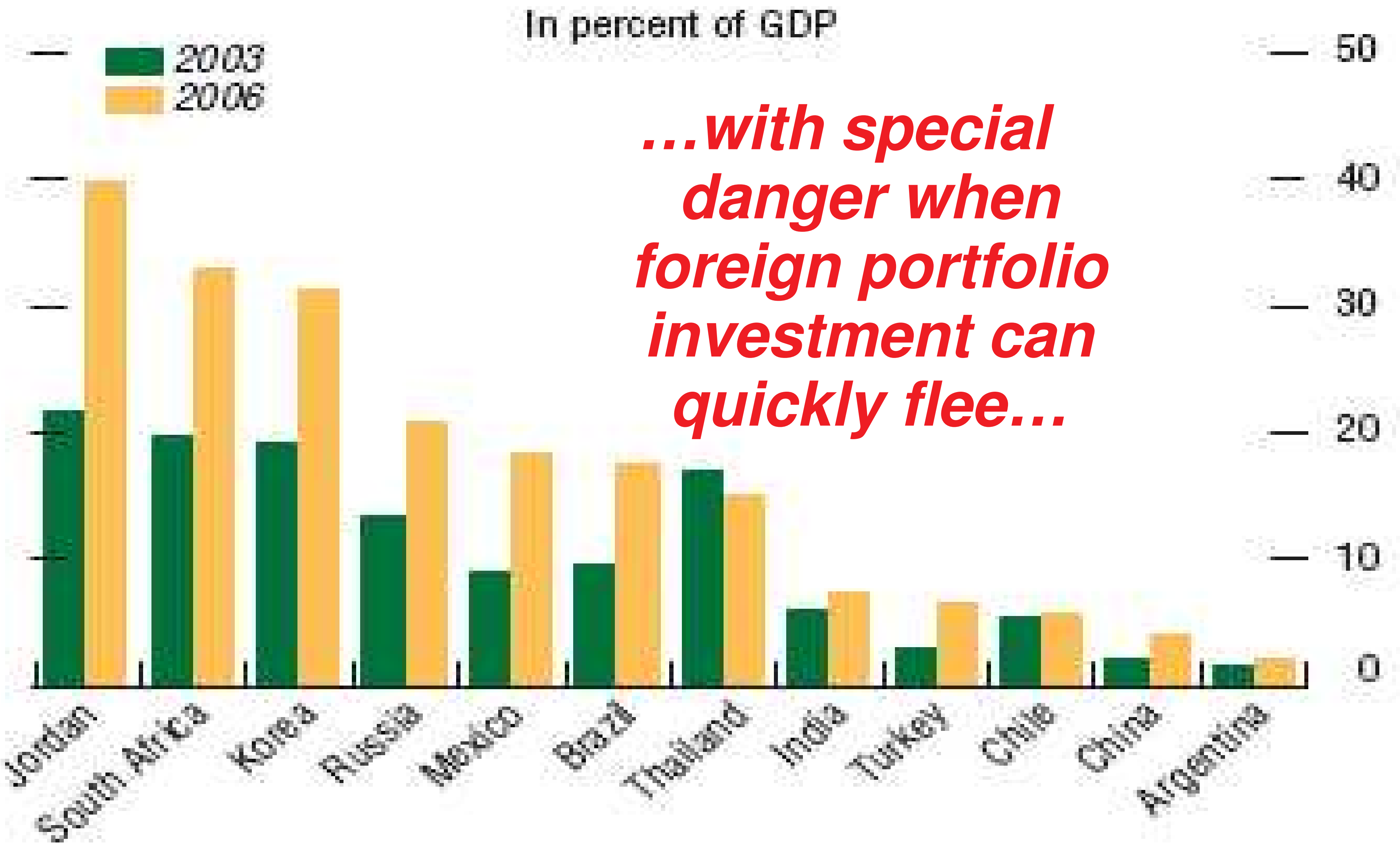
Emerging market share devaluation, 2007-08

Source: International Monetary Fund *Global Financial Stability Report*



Foreign holdings of equity, 2003, 2006

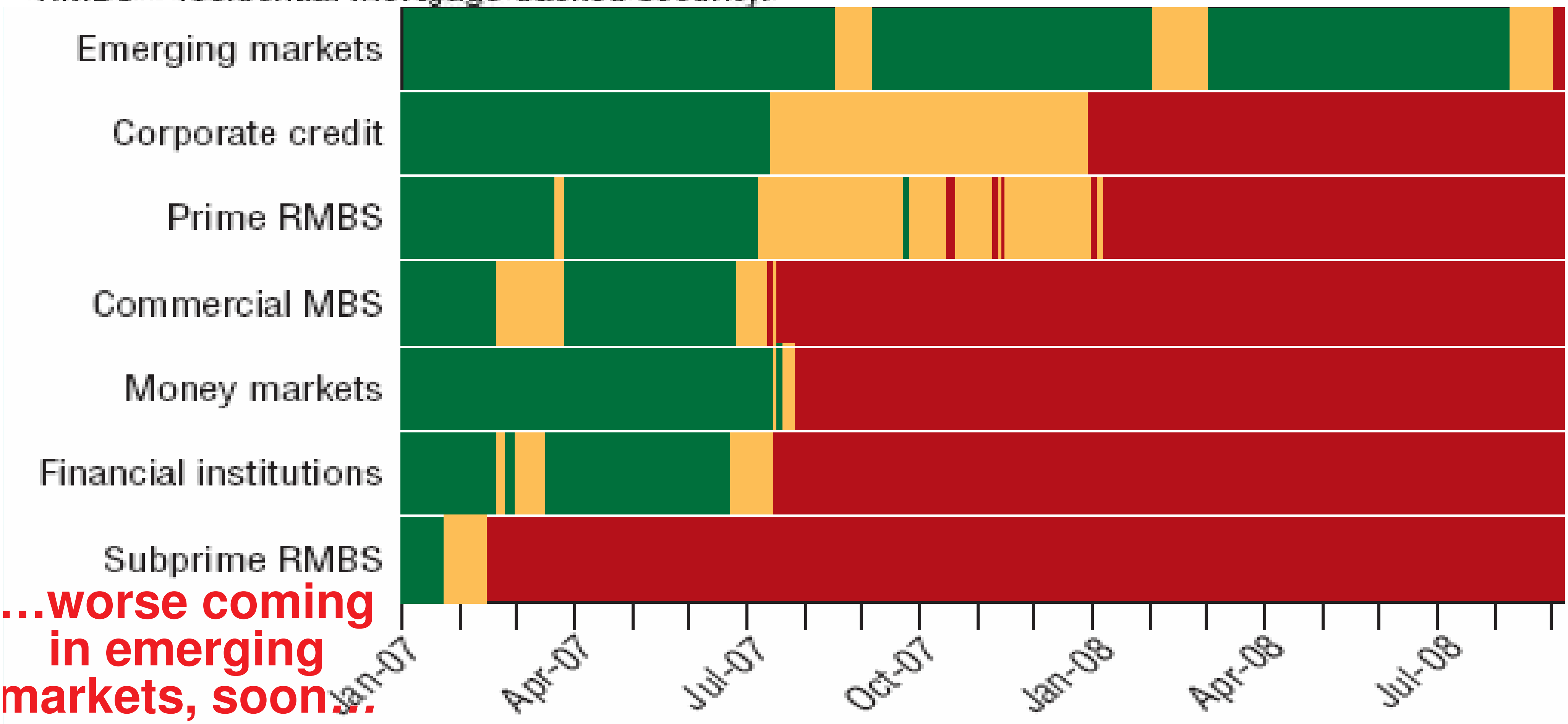
Source: International Monetary Fund *Global Financial Stability Report*



…with special danger when foreign portfolio investment can quickly flee…

Bursting the bubbles: IMF 'heat' indicator

Note: The heat map measures both the level and 1-month volatility of the spreads, prices, and total returns of each asset class relative to the average during 2004–06 (i.e., wider spreads, lower prices and total returns, and higher volatility). That deviation is expressed in terms of standard deviations. Green signifies a standard deviation under 1, yellow signifies 1 to 4 standard deviations, and red signifies greater than 4 standard deviations. MBS = mortgage-backed security; RMBS = residential mortgage-backed security.

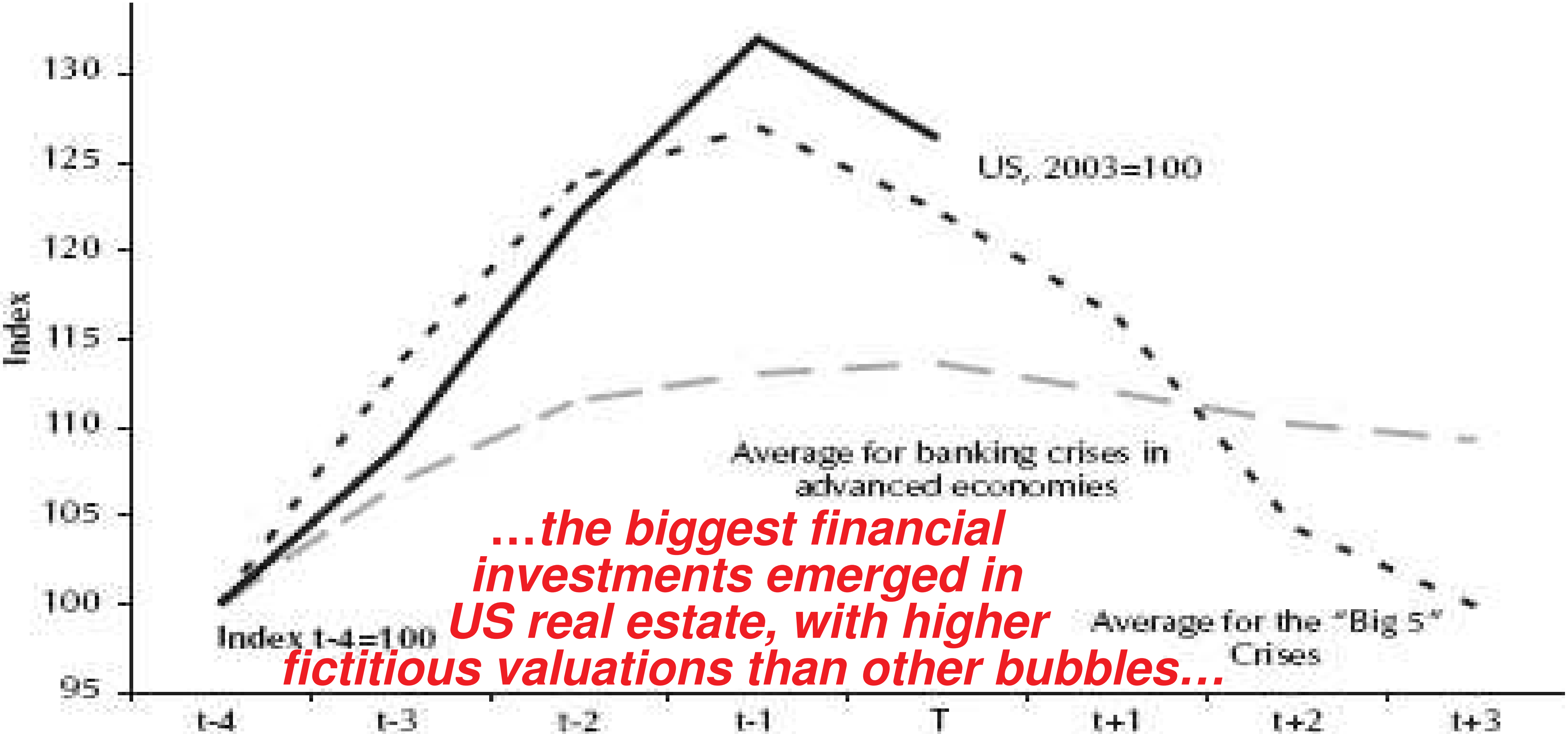


…worse coming in emerging markets, soon…

US financial devaluation

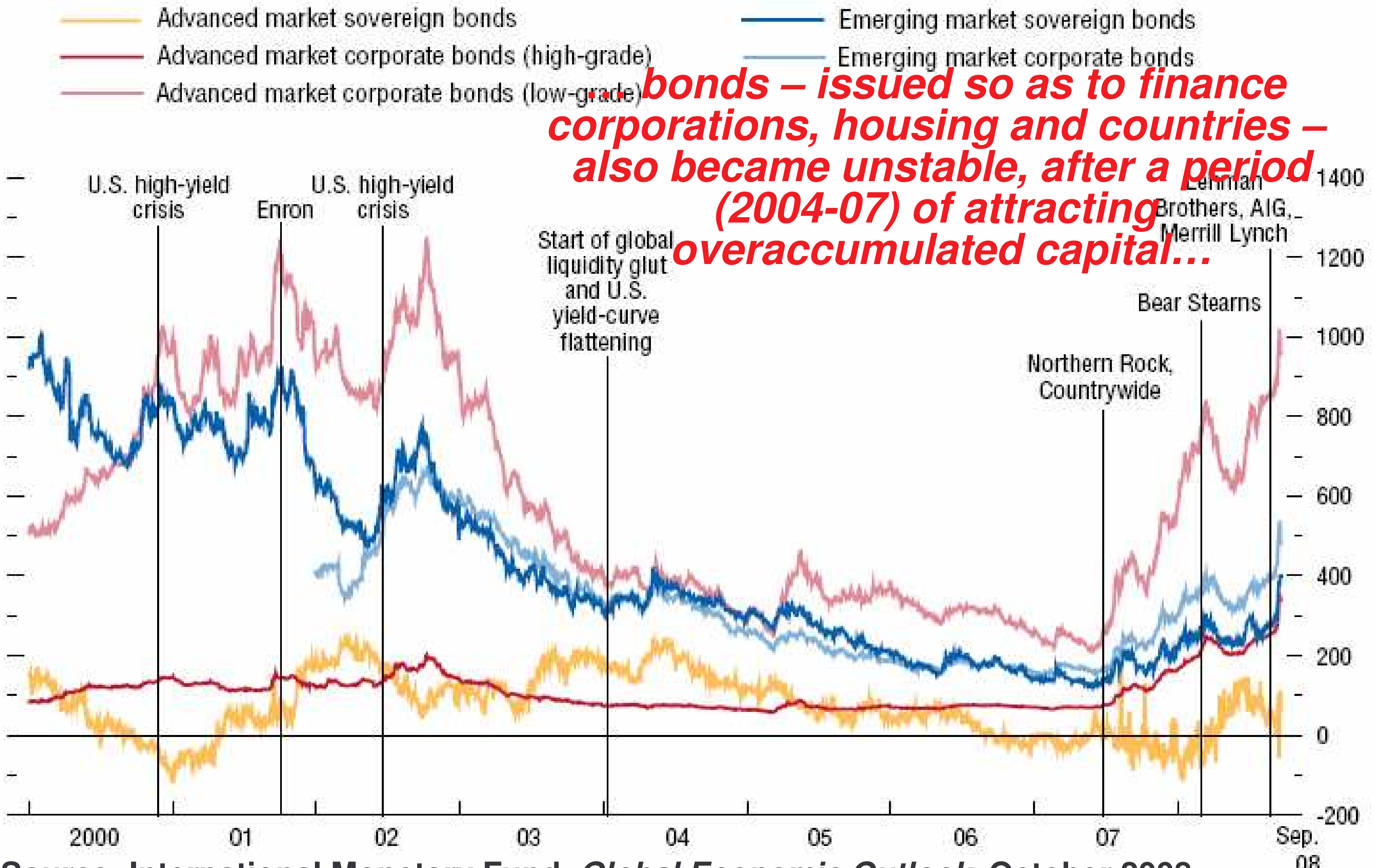
The five Big Five crises: Spain (1977), Norway (1987), Finland (1991), Sweden (1991) and Japan (1992) (starting year in parenthesis).

Other banking and financial crises: Australia (1989), Canada (1983), Denmark (1987), France (1994), Germany (1977), Greece (1991), Iceland (1985), Italy (1990), New Zealand (1987), United Kingdom (1974, 1991, 1995) and United States (1984).

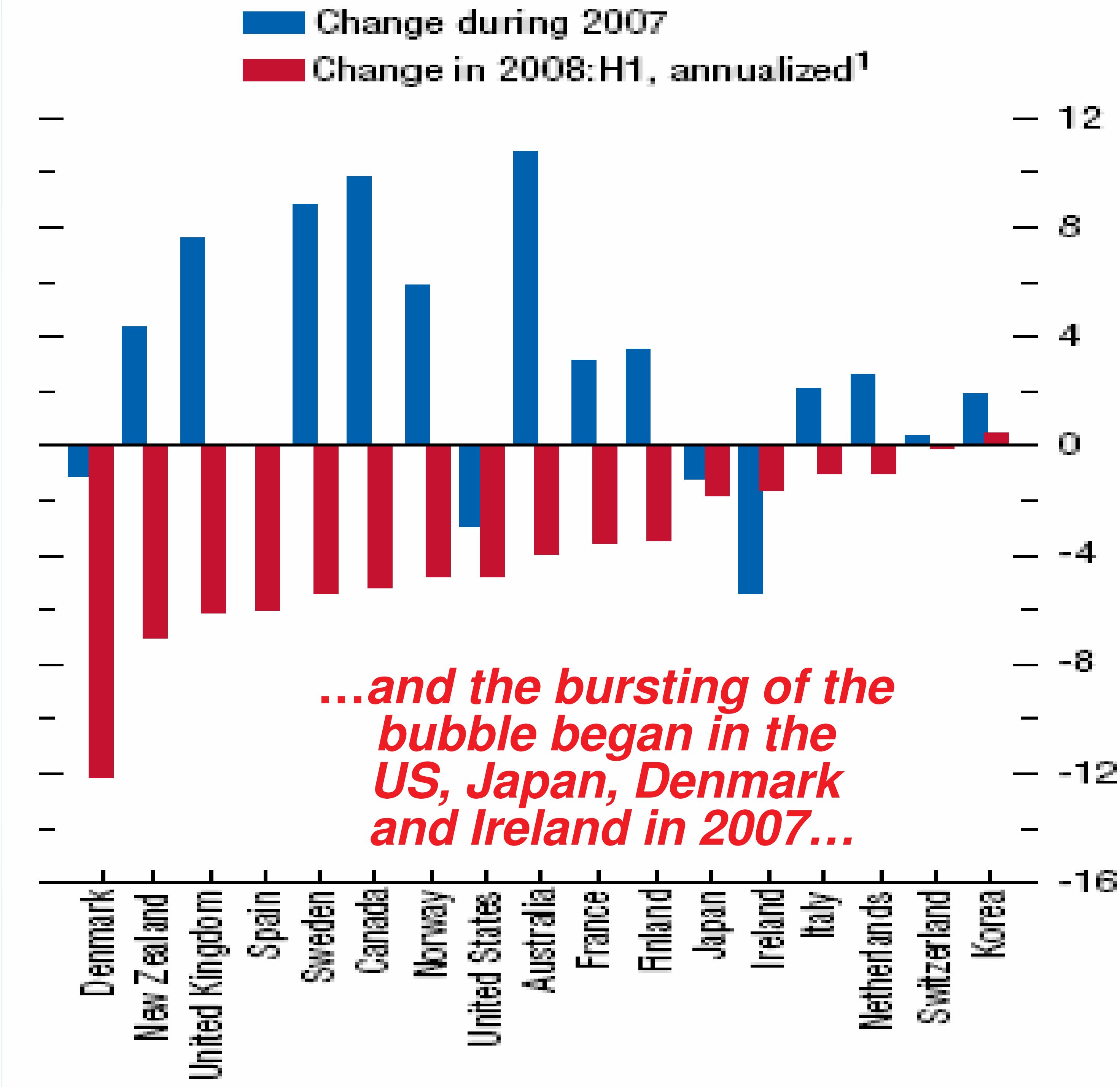


Sources: Reinhart and Rogoff (2008) and sources cited therein.

Bond market volatility, 2000-08



Source: International Monetary Fund, *Global Economic Outlook*, October 2008

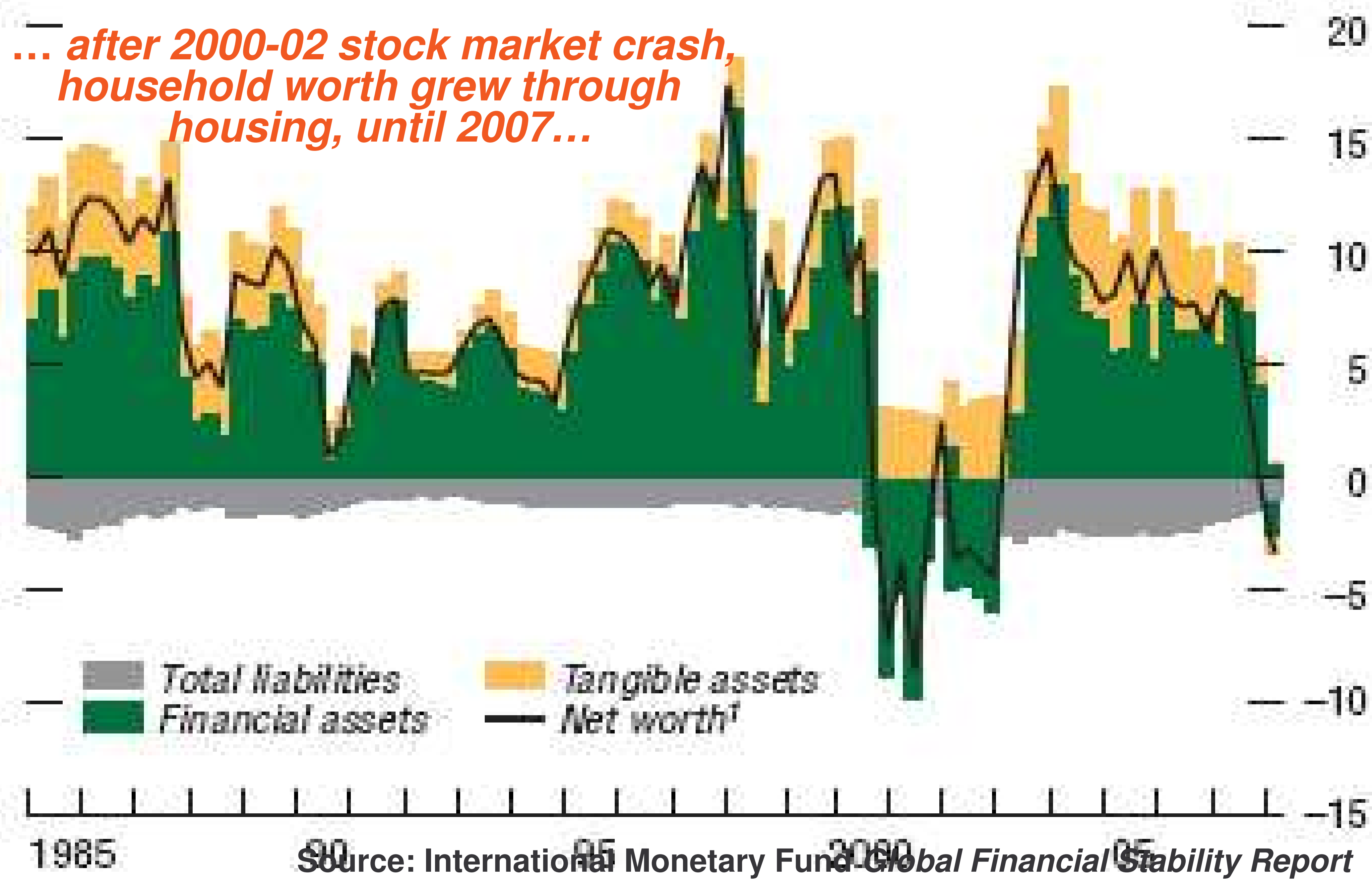


6) Housing devaluations:

Change in prices, Jan 2007- July 2008

Source: IMF, *World Economic Outlook*, October 2008

Writing off US household net worth (%/year)



Source: International Monetary Fund *Global Financial Stability Report*

7) Financial losses: IMF estimates of devalued US loans ($bn)

Source: IMF *Global Financial Stability Report*

	Outstanding	Estimated loss April 2008 GFSR	Estimated loss October 2008
Subprime residential	300	45	50
Alt-A residential	600	30	35
Prime residential	3,800	40	85
Commercial real estate	2,400	30	90
Consumer loans	1,400	20	45
Corporate loans	3,700	50	110
Leveraged loans	170	10	10
Total for loans	12,370	225	425

…has IMF correctly estimated size of devaluation? $425bn…

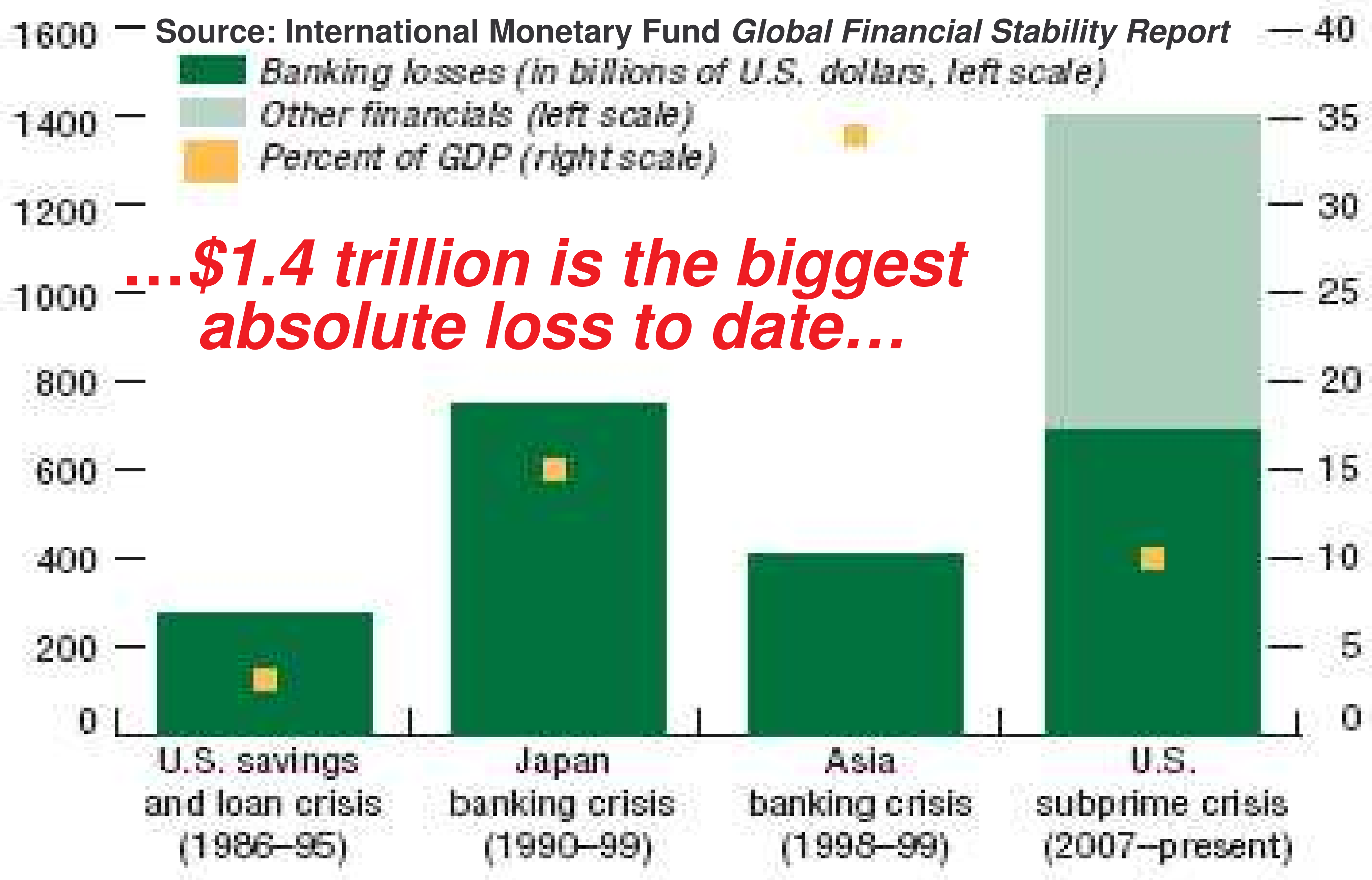
IMF estimates of devalued US financial assets: securities ($bn)

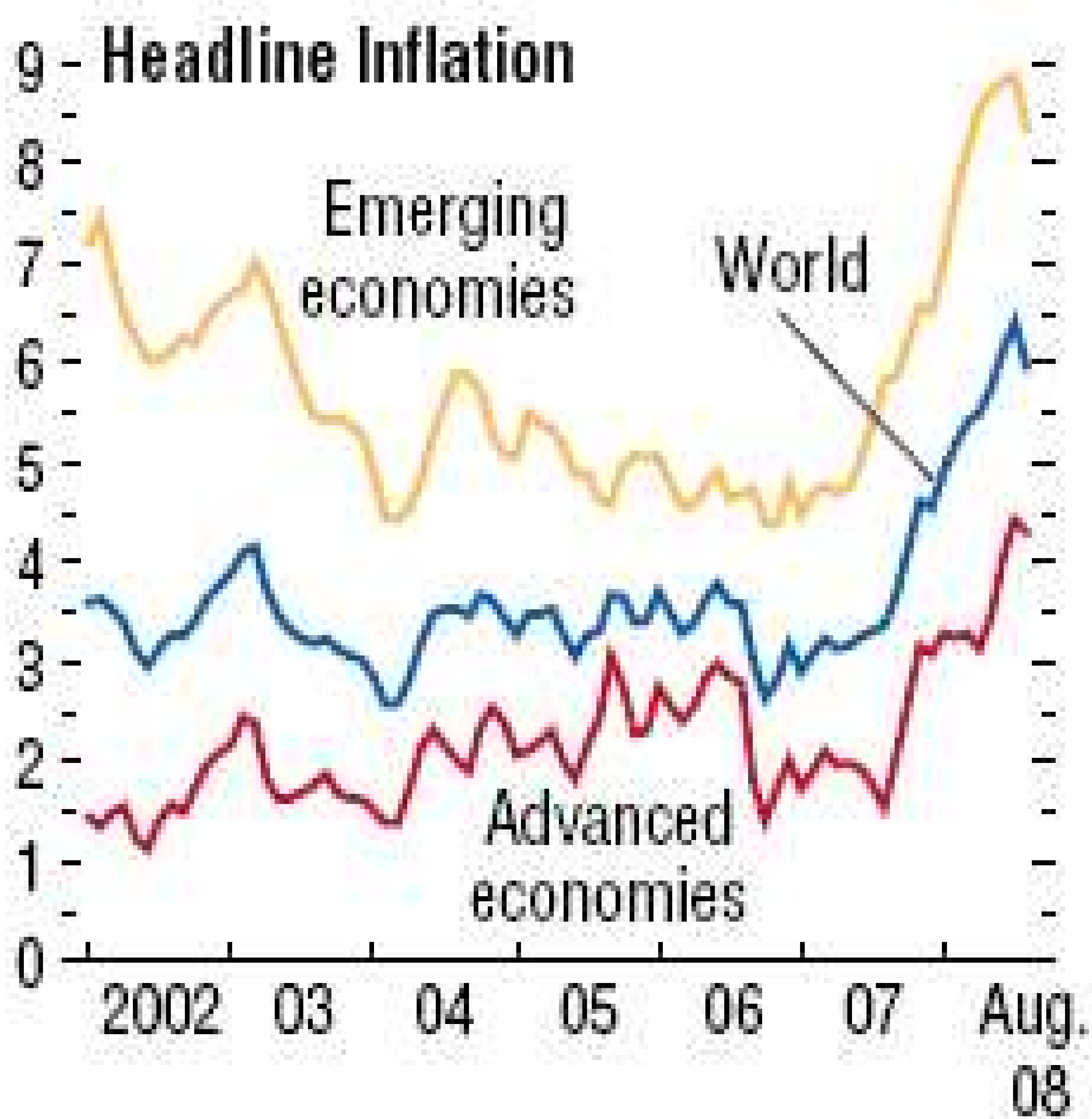
Source: IMF *Global Financial Stability Report*

	Outstanding	Estimated mark-to-market loss April 2008 GFSR	Estimated mark-to-market loss October 2008
ABS	1,100	210	210
ABS CDOs	400	240	290
Prime MBS	3,800	0	80
CMBS	940	210	160
Consumer ABS	650	0	0
High-grade corporate debt	3,000	0	130
High-yield corporate debt	600	30	80
CLOs	350	30	30
Total for securities	10,840	720	980
Total for loans and securities	23,210	945	1,405

Note: ABS = asset-backed securities; CDO = collateralized debt obligation; CLO = collateralized loan obligation; CMBS = commercial mortgage-backed security; MBS = mortgage-backed security.

Writing off overaccumulated finance





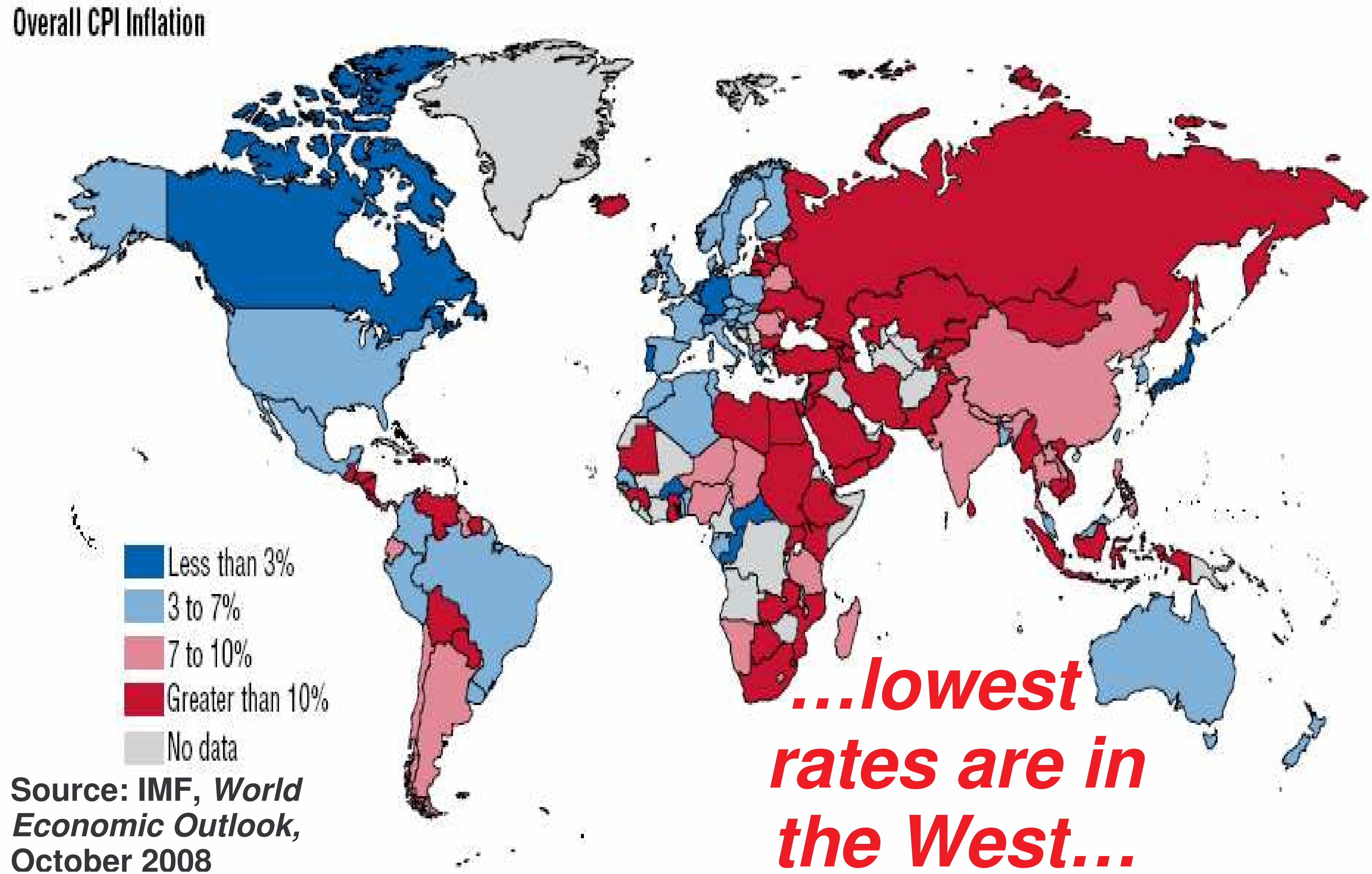
8) Is inflation a way out?

Devaluing financial assets through inflation

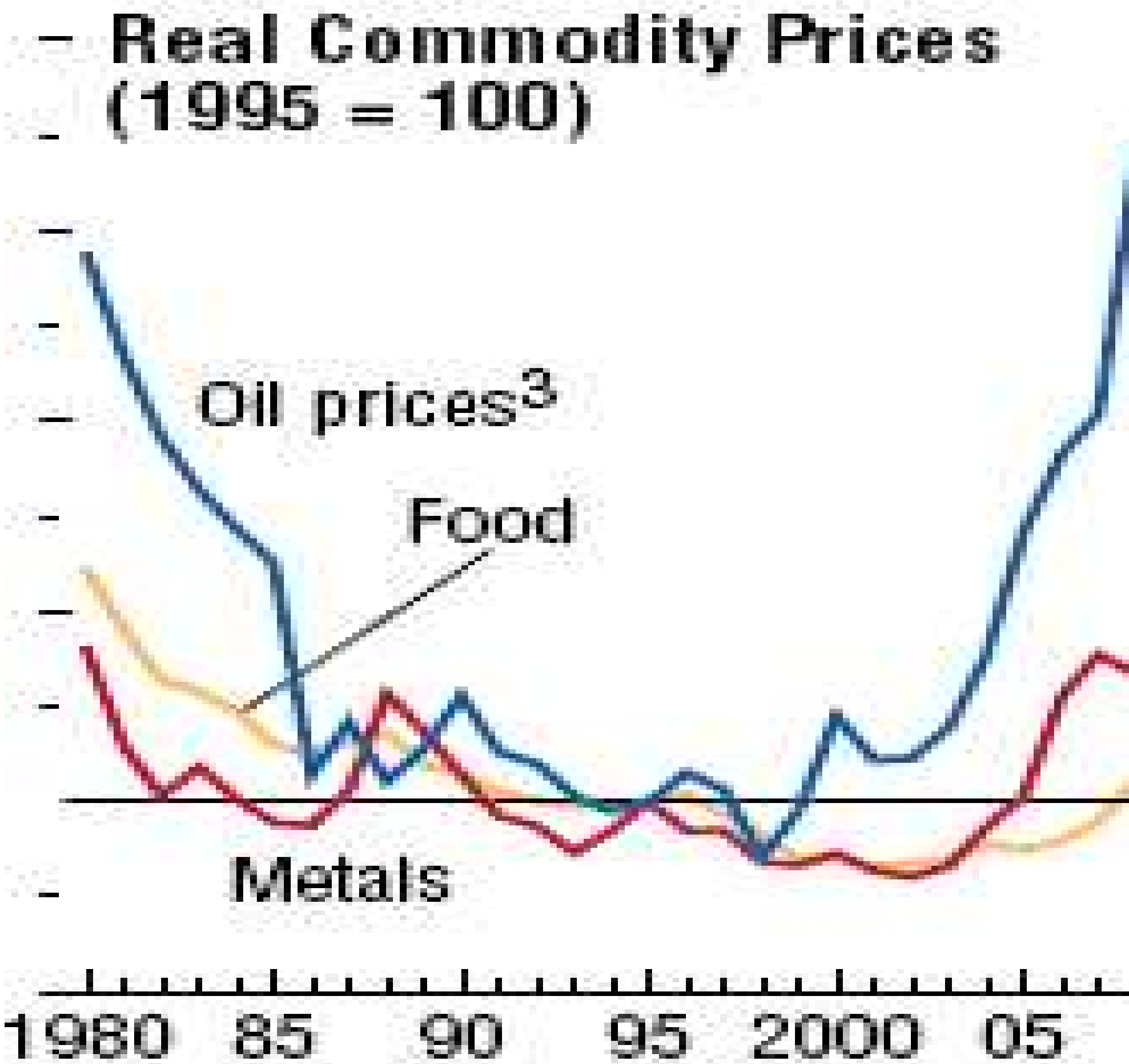
…a viable strategy for deflating debt?…

Source: IMF, *World Economic Outlook,* October 2008

Inflation rates



Source: IMF, *World Economic Outlook,* October 2008



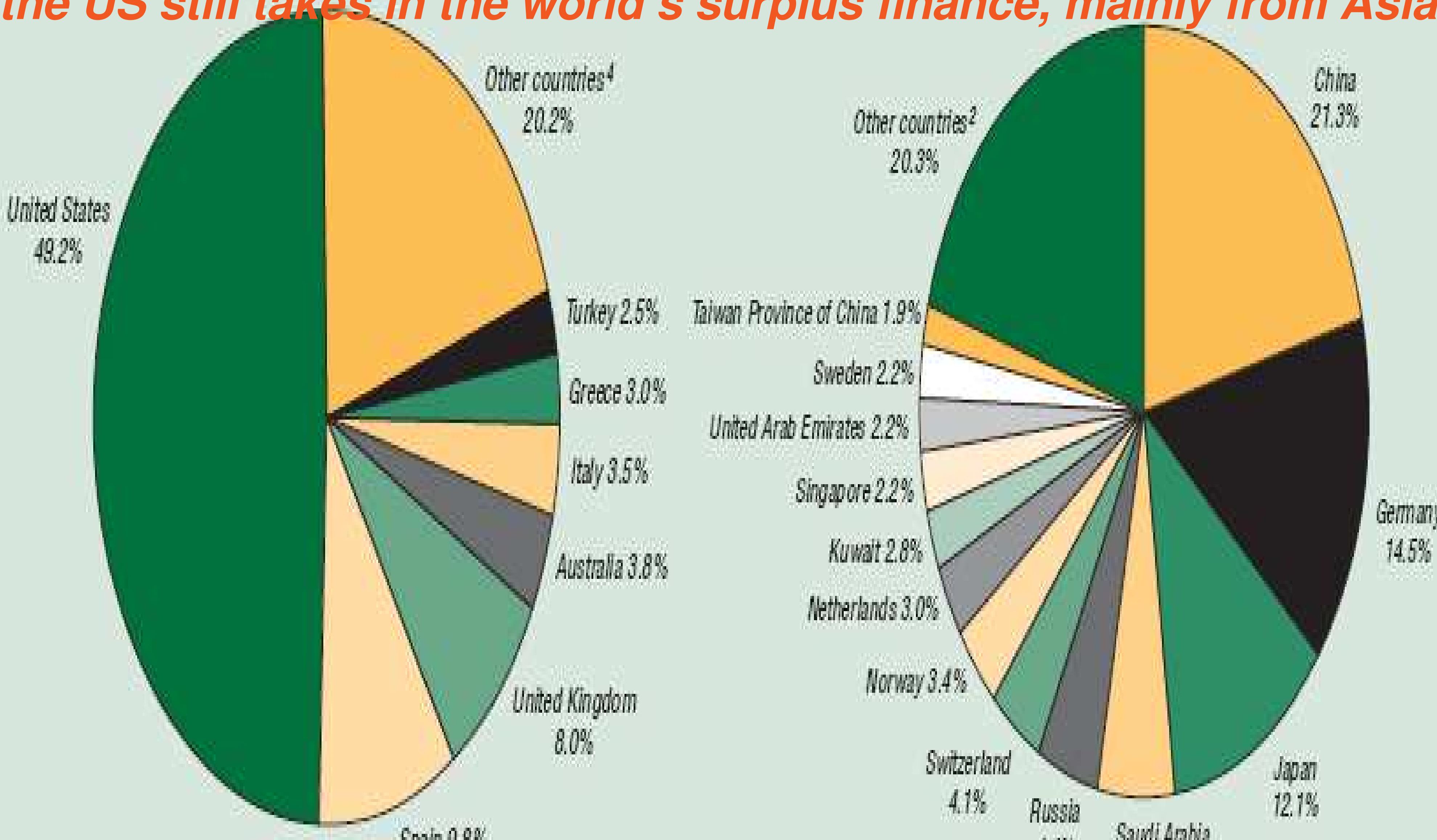
Price rises for oil, food, metals, 1980-2008

… and it appears oil price is due to specu-lation…

Source: IMF *Global Financial Stability Report*

9) Currency movements are a key variable: Importers and exporters of capital, 2007

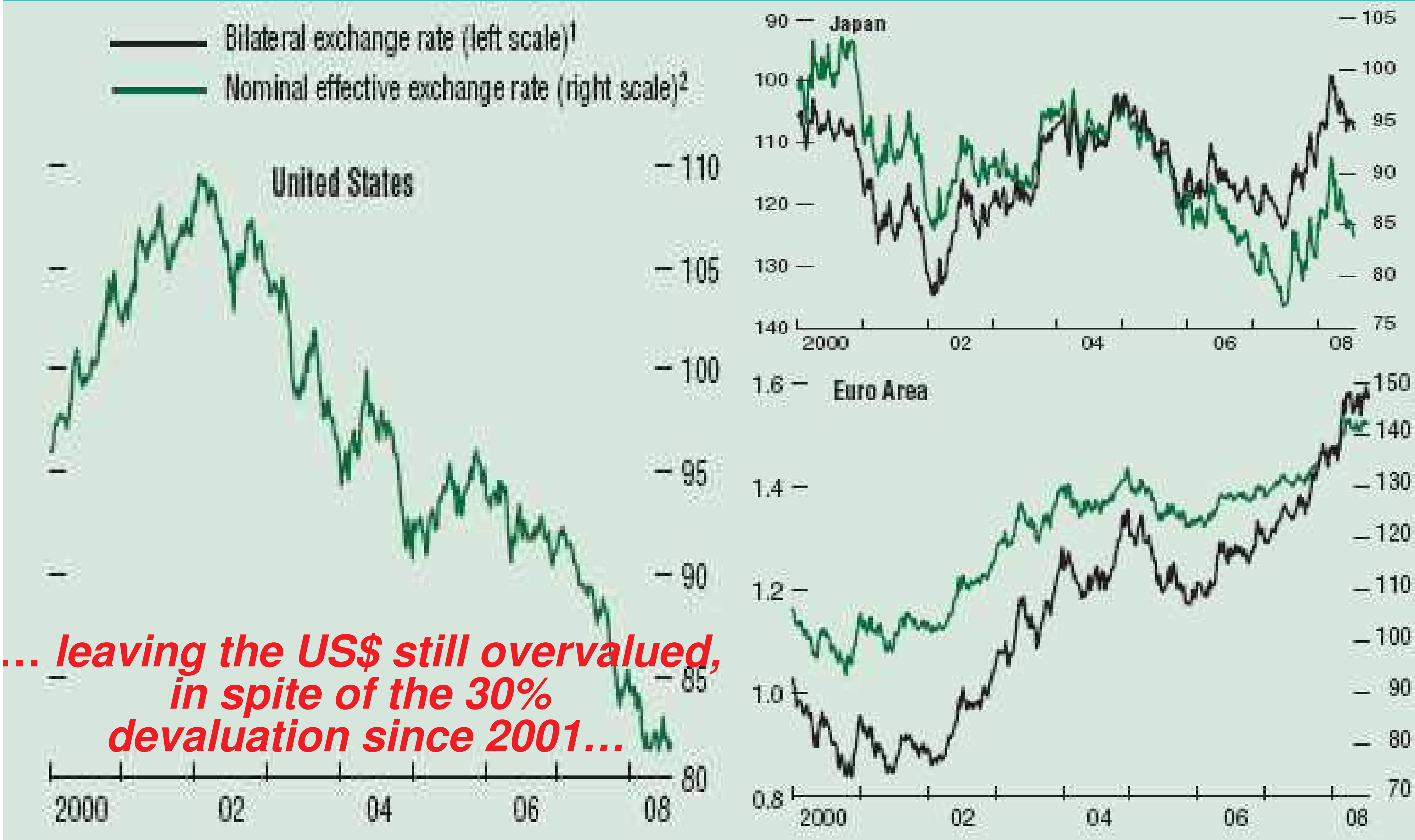
.. the US still takes in the world's surplus finance, mainly from Asia..



Source: International Monetary Fund *Global Financial Stability Report*

G3 currency value changes, 2000-08

Source: International Monetary Fund *Global Financial Stability Report*



… leaving the US$ still overvalued, in spite of the 30% devaluation since 2001…

G3 short term (real) interest rates

…compelling the US to raise rates from 2004-06, but can it continue?…

Source: IMF, *World Economic Outlook,* October 2008