Crises, Restructuring and The Legitimacy of Capitalism

C. P. CHANDRASEKHAR*
Jayati GHOSH**

Abstract: In this paper we dwell on the post-2009 crisis episode of the global economy and discuss how the legitemacy of global capitalism had been undermined. We argue that the crisis had questioned the solvency of many financial institutions including some banks, necessitating a massive bail-out, which included bank recapitalization financed with tax payer's money. Yet, this focus on the financial sector's survival did little to address the massive slowdown in the retail market, the services sector and real estate in the financial centres of the world. This brings us to confront the questions of systemic legitimacy.

Key Words: Crises, restructuring and the legitimacy of capitalism
Öz: Bu makalede 2009 sonrası küresel ekonominin içine sürüklendiği kriz ortamında küresel kapitalizmin içine sürüklendiği meşruiyet bunalımı tartışılmaktadır. Kriz bir çok finans kuruluşunun bilanço dengelerini sarsmış; ancak bunların kurtarma operasyonları dahilinde kullandıkları kaynaklar emlak ve finans piyasalarında gerilemenin önüne geçememiştir. Bu doğrultuda yapılan müdahaleler ise sistemin meşruiyetini sorgulamamıza yol açmaktadır.
Key words: Krizler, Kapitalizmin Yeniden İnşası ve Meşruluğu

Introduction

It is more than a decade since the onset of the Great Financial Crisis and the Great Recession that followed. Fearing that the advanced countries could experience a crisis comparable in intensity with the Great Depression of the 1930s, governments and central banks in the advanced countries intervened on multiple fronts to stall the downturn and trigger a recovery. By all accounts, the immediate post-crisis rhetoric seemed to suggest that, learning from the crisis advanced country governments were committed to adopting policies that would restructure capitalism in ways that would substantially reduce the probability of a similar crisis.

* Jawaharlal Nehru University, New Delhi
** Jawaharlal Nehru University, New Delhi

That rhetoric seemed plausible for two reasons. First, comparisons with the intensity of the Great Depression suggested that the response would be similar in scope. To recall, there were two overarching elements that characterized the New Deal, or the state's response to the Great Depression in the US. First, to address the banking and financial crisis that heralded the depression, President Roosevelt pushed through legislation, famously in the form of the Glass-Steagall Act, to rein in finance, by limiting competition and forbidding banks from engaging in the securities business, so as to prevent use of depositors' money for speculative purposes. This, together with other measures of financial regulation adopted subsequently made the United States financial system one of the most stringently regulated systems, from the mid-1930s till the beginnings of financial liberalization in the 1970s. Second, in a departure from the then prevalent conservative fiscal stance, Roosevelt opted for proactive fiscal policies to stall the downturn and trigger recovery with some success, though the final exit from the Depression was provided by expenditures on World War II. Before that, a temporary return to fiscal conservatism threatened even the limited recovery, encouraging a restoration of the fiscal stimulus. After the war this led to the construction of the welfare state, with its expenditures serving as automatic stabilizers till inflation challenged the system at the end of the 1960s. In the interim, between the end of the Second World War and the 1970s, the US experienced a Golden Age, with reasonable growth, low inflation and near full employment.

The Obama Moment

The second reason was the election of Barack Obama as President of the United States just as the crisis was unfolding. Barack Obama's victory speech inspired confidence and raised expectations. His victory was historic not just because it had brought a coloured man to the White House for the first time in US history. It also signaled that the more than three-decade old neo-conservative turn in economic policy making in the US was discredited and challenged. In more ways than one, Obama's later campaign had suggested that a change from that policy was required raising expectations that the President-elect will seek to redirect capitalism in new directions. The question on everyone's mind, at home and abroad, was: Will Obama ensure that the Golden Age of 20th century capitalism, the high growth, welfare-statist years of the 1950s and 1960s is not the exception that it seemed to be, by launching a new era of creditable growth, higher employment and lower inequality?

As has been repeatedly noted, the political tide turned decisively in Obama's favour because of the financial crisis and the popular anger against a private sector that engineered the crisis and an administration that supported and rewarded these private sector entities and individuals. The victims of that anger directed against the Bush administration were the Republicans and McCain. Obama did not fail to use the evidence that the Bush administration had helped precipitate this crisis through partisan policies, which favoured Wall Street vis-à-vis Main Street, the rich as opposed to the poor and middle classes and the banks and financial firms rather than homeowners facing foreclosure. Not surprisingly, economic circumstances and that campaign increased expectations that he would turn the economy around rather quickly.

The contours of the crisis till then had lessons to offer. The crisis had questioned the solvency of many financial institutions including some banks, necessitating a $700 billion-plus bail-out, which includes a bank recapitalization financed with tax payer's money. This focus on the financial sector's survival did little to address the massive slowdown in the retail market, the services sector and real estate in the financial centres of the world. The financial crisis had led to a contraction of credit, not because of a lack of liquidity which the Federal Reserve was injecting into the system, but because of uncertainties surrounding the ability of counterparties to meet future commitments on any credit provided. A consequence was the curtailment of debt-financed consumption and investment, which were already affected adversely by the wealth-erosion ensured by the collapse of house and stock prices. The resulting recession had taken the unemployment rate to 6.5 per cent.

The implication of all this seemed obvious. Support for the private sector through lower interest rates, financial bail outs and the like are unlikely to stop the downward spiral, because of insolvency and the collapse of business confidence. Nor would tax cuts spur demand, because they may be used to bolster savings and compensate for the erosion of paper wealth and home equity. It was necessary for the government to also intervene with expenditures in forms varying from an unemployment dole and prevention of housing foreclosures to large scale infrastructural investments. These circumstances had encouraged comparison with the situation when Franklin Roosevelt took office in 1932 in the middle of the Great Depression.

A decade later it is clear that the Obama promise was belied, excepting for the limited claim that things could have been worse if he had not been there. The message from the October 2018 meetings of the International Monetary Fund and the World Bank, which normally exude optimism, is glum. In January this year the IMF had noted that "the cyclical upswing underway since mid-2016" was growing stronger, contributing to "the broadest synchronized global growth upsurge since 2010". It now feels that while "the global economic expansion remains strong", it has "become less balanced and with more downside risks." This does not just mean that one more sighting of the 'green shoots of recovery' is proving to be premature. Given the IMF's predilection for underplaying the bad news it suggests that a return to recession is a real possibility.

While there have been periodic references of the end of the recession, the recovery itself has been limited and halting, on the one hand, and uneven on the other. In the OECD group the recovery between the third quarter of 2016 and the third quarter of 2017 merely replicated previous post-crisis trends that had been reversed. Thus, the growth rate in fact declined in the last quarter of 2017 and first quarter of 2018. And the third quarter figure was not very much higher than that in the second quarter of 2015, and much lower than the peak recorded at the end of the immediate post-crisis recovery in the third quarter of 2010. These trends were replicated with even less robust recovery in the G7, despite the fact that the US which is supposed to be the focus of the recovery has a much higher weight here. In fact, in the US, the year-on-year growth rate in first quarter of 2018 was close to 2 percentage points below that recorded in the first quarter of 2015. Moreover, the recent higher than 3 per cent rate of growth in the US is clearly due to the stimulating effects of the $1.5 trillion tax cuts, which is expected to wane in the coming year.

The Link to Policy

This halting and uneven recovery was related to the actual response to the crisis in the realm of macro-economic policy. In the initial phases of the crisis, the need to save the financial system and stall the slide into recession focused attention solely on those tasks. A combination of fiscal and monetary stimuli were deployed for the purpose, though fiscal spending in the advanced economies was directed more at recapitalising banks rather than addressing mortgage foreclosures or reviving demand. The financial system benefited in two ways. First, it received financing from the budget, through measures such as the Troubled Asset Relief Program (TARP) in the US, that allowed financial institutions to partly retrench questionable assets and partly issue new equity to increase their common tangible equity ratios and declare solvency. Second, it received financing at near zero interest rates from the central banks against the assets that had no open market buyers and were therefore worthless when marked to market. That finance could be used to invest in new low yielding assets, which however offered good net returns because of the low or absent cost of capital. However, once finance had found its feet once again and went on to record profits based on such implicit carry trades, governments were prevented from continuing with proactive fiscal policies on the grounds that this would lead to unsustainable public debt levels.

In the event, by the time government could focus attention on real economy revival, the only instruments they could leverage where monetary policies in the form of low and even negative interest rates and "quantitative easing" or massive liquidity infusion through the purchase of bonds. The US Fed, for example, saw the size of assets on its balance sheet bloat from around $800 billion to more than $4 trillion, the counterpart of which were the liabilities that drowned the system in liquidity.

Thus, the rescue effort launched after the crisis went through two phases. In the first phase, in order to prevent the recession from becoming a modern-day repeat of the 1930s Depression, governments opted for debt-financed spending in the form of a fiscal stimulus to revive demand, on the one hand, and funds infusion for financial sector recapitalisation, on the other. This did have a salutary effect on growth, quickly retrieving economies from the depths of the recession. But once this was done, governments succumbed to the pressure not to use debt-financed fiscal spending as a means of stimulating a recovery and focused on monetary policy measures, such as liquidity infusion and interest rate reduction, to combat recession and spur recovery. Indeed, because of the domination of the ideology of fiscal prudence at all costs, governments in advanced countries and most emerging markets have in general resolutely abided by a conservative fiscal agenda and refused to return to the proactive fiscal policies adopted in the immediate aftermath of the crisis.

The result of this shift from dependence on fiscal policy to reliance on the monetary lever was that some of the buoyancy induced by the initial fiscal stimulus was lost. Output growth fell from its peak and settled at a new normal that, though not a recession, was too weak to be a robust recovery. Monetary policy proved to be less effective in reviving growth, the recovery was weak and halting and the road to recovery prolonged.

Wages and Unemployment

Remarkably, while the end of the worst of the recession has brought down the unemployment rate significantly, this has not helped accelerate wage growth. According to the *Global Wage Report 2018/19* of the International Labour Organisation (ILO), the rate of growth of average monthly earnings adjusted for inflation of workers across 136 countries registered in 2017 its lowest growth since crisis year 2008, and was well below figures recorded in the pre-crisis years 2006 and 2007. What is more, if China, where wage growth has been rapid and whose workforce size substantially influences the weighted average global figure, is excluded, the level wage growth in 2017 (1.1 per cent) is much lower than the figure for all countries including China (1.8 per cent). The deceleration in wage growth outside of China appears true of both developed and developing countries.

A similar trend in the OECD countries had been flagged in the *OECD Employment Outlook 2018* released in July 2018. It noted that: "On average, hourly wage growth in the OECD countries was still 0.4 percentage points lower in last quarter of 2017 than it was in late 2008." That report, in an editorial tellingly titled "Wageless growth: Is this time different?", went even further and suggested that the current recovery is different from those that followed previous crises, since falling unemployment has not been accompanied by comparable increases in wages.

This low wage growth in both absolute terms and when compared to the previous year and the pre-crisis period has surprised observers for two reasons.

The first, as noted, is that it occurs in a period when the recovery is seen as having been underway in the US, when the worst was seen as over in recession affected Europe, and when growth in the developing countries, especially the emerging markets, was seen as reasonable. According to the ILO, global GDP growth rose from 3.3 per cent in 2016 to 3.7 per cent on 2017, which was its highest level since 2011. Moreover, the most recent upturn is seen as persisting. Growth in the developing economies had risen from 4.4 per cent to 4.7 per cent between 2016 and 2017 and from 1.7 to 2.3 per cent in the advanced economies. And growth in 2018 is expected to be even higher.

Second, the evidence suggests that this recovery, however uneven and hesitant, had reduced unemployment as measured. As is widely recognised, unemployment rates are misleading in poorer countries where, because of the absence of any social security or social protection, those in the working age have to take up some kind of work, even if at low wages and for short periods of time, just to avoid starvation. But, more reliable figures from the developed countries suggest that unemployment is on the decline. According to the ILO: "The average seasonally adjusted unemployment rate among the EU28 countries stood at around 6.5 per cent in April 2018, the lowest rate recorded in the European Union (EU) since December 2008." A similar trend has been reported by the OECD, which found that the average employment rate in its member countries was 2 percentage points above pre-crisis levels, and unemployment rates have been in "slow descent".

If growth is improving and unemployment is on the decline, then one should expect that wage growth would improve. The fact that it is falling poses a conundrum. Especially surprising is the fact that "the pattern of "declining unemployment with flat wages" is particularly pronounced in Germany and the United States – two countries where unemployment rates have been gradually reduced over the last seven to eight years but where the growth rate of nominal wages has remained relatively constant, fluctuating between 2 and 3 per cent per year."

It could be argued that if productivity growth has not improved as much as GDP growth has, then wage growth may be held back even if employment is rising, because there is inadequate surplus per worker that can go to shore up wages. But here too the evidence does not provide an explanation. The figures show that workers are not getting a fair share of whatever productivity growth is occurring. Wage growth has lagged behind productivity growth, leading to a fall in the share of wages in national income. In the assessment of the ILO, "the decoupling between wages and labour productivity explains why labour income shares (the share of labour compensation in GDP) in many countries remain substantially below those of the early 1990s."

An alternative explanation for these contrary trends in output and employment growth and wage growth could be that growth in the former variables may have been exaggerated. While talk of a recovery has been on since 2017, in most countries, other than the US, the increases in growth rates have been marginal and prone to reversal. In the G20 as a whole, the recovery in the fourth quarter of 2017 from a late 2016 low took the year-on-year quarterly growth rate to a level that was not very much higher than that in the fourth quarter of 2013, and much lower than the peak recorded at the end of the immediate post-crisis recovery in 2010. Even the US recovery has been volatile till very recently.

What has been more convincing as an indicator of improving performance is the unemployment rate in the US, which fell from close to 10 per cent in the middle of the crisis to 4.1 per cent at the end of 2017. That was even below the 5 per cent figure recorded in January 2008 when the crisis was yet to break. But there have been doubts expressed about the falling unemployment rate as well. The labour force participation rate in the US, or the proportion of those 16 years and above reporting themselves as available for and seeking work, fell from 66.2 per cent in January 2008 to 62.7 per cent in December 2017. This was a reflection of the 'discouraged worker effect', where those unable to find work for a long period just stop looking for work and are not counted as part of the labour force or among the unemployed. The result is a fall in the employment rate relative to what would have otherwise been the case. According to one estimate, if the labour force participation rate in December 2017 were the same as in January 2008, the corresponding unemployment rate would have been 6.1 per cent. Thus the contradiction between falling unemployment and decelerating wage growth, may be partly explained by the fact that the former has been exaggerated.

But some fall in the unemployment rate cannot be denied. And in the rest of the OECD as well, "labour markets are back to pre-crisis levels in terms of job quantity, with only a few notable exceptions". But this higher level of employment has been accompanied by a rise in the proportion of casual and precarious jobs. This poor job quality keeps nominal wage growth low, despite the reported 'tightening' of the labour market. Many factors could explain the worsening quality of employment in the advanced countries, not least among them the effect of competition from imports from China and elsewhere and the labour market reforms they have triggered. Global sourcing through purchase and production by transnational firms, by expanding the reserve army of labour available to a now globalized metropolitan capital, keeps wages in the advanced countries low, because of competition from labour abroad and the fragmentation of labour markets with precarious employment conditions at home. Since it is the more labor intensive segments of manufacturing that tend to get relocated abroad, employment growth is also limited. Policy measures aimed at rendering labour markets "flexible" expands the scope for creating precarious jobs with low earnings. Finally, uncertain and precarious employment reduces in turn workers' bargaining power, which too depresses wages and limits wage increases even in "good times".

Even the normally optimistic OECD is forced to recognise this and state that: "“There has a been a significant worsening of the earnings of part-time workers relative to that of full-time workers associated with the rise of involuntary part-time employment in a number of countries. Moreover, the comparatively low wages of workers who have recently experienced spells of unemployment, combined with still high unemployment rates in some countries, have pushed up the number of lower-paid workers, thereby lowering average wage growth."

The Actual Policy Response

This poor performance on the wage front is of significance because of the effect it has on a policy dilemma facing central banks and government. The intensity of the primary policy response to the 2008 financial crisis in the advanced economies, in the form prolonged use of "unconventional" monetary policies involving near zero interest rates and massive liquidity infusion, is evident from the numbers. In the United States, the Federal Reserve resorted to a policy of "quantitative easing" involving purchases of Treasury Securities of between $45 million and $75 million a month. A similar policy was adopted by the European Central Bank, which after some initial hesitation accelerated its acquisition of bonds in 2014 in response to extremely low growth. As a result, by December 2017, the six central banks that adopted policies of "quantitative easing" — the US Federal Reserve, the European Central Bank, the Bank of Japan, the Bank of England, and the Swiss and Swedish central banks — held more than $15 trillion of assets, more than four times the pre-crisis level.[1] The US Federal Reserve held assets worth a little less than $1 trillion before the crisis and by December 2017 recorded assets of $4.5 trillion, around one quarter of US GDP. The ECB accumulated assets of $4.9 trillion, around two-fifths of the EU's GDP.

Accompanying this exclusive reliance on monetary policy was an unwillingness to resort to financial re-regulation to correct the systemic failures in the financial system that precipitated the crisis. From the very beginning it became clear that the discussion on reform in the US was riven by the tension between those fighting to restrict the response largely to bailing-out finance and tinkering with the existing framework of rules and regulations, and those who felt that the experience demanded a fundamental restructuring of finance and a return to strong regulation of the pre-1980s kind. A hint that the actual regulatory package that would get implemented would include significant compromises in favour of Finance Capital came when the Obama administration in June 2009 announced the contours of a likely reform package led by a statement by the President. While declaring that the economic downturn was the result of "an unravelling of major financial institutions and the lack of adequate regulatory structures to prevent

[1] *Financial Times*, August 16, 2017

abuse and excess," the Obama statement did not blame the dismantling of the regulatory regime that was put in place in the years starting 1933 for these developments. It attributed them to the fact that "a regulatory regime basically crafted in the wake of a 20th century economic crisis—the Great Depression—was overwhelmed by the speed, scope, and sophistication of a 21st century global economy." Glass-Steagall was not the model for reregulation but the outdated 'other', which needed to be substituted with a new regime. Implicit in this was the understanding that there was no question of reversing the dismantling of the regulatory walls that separated different segments of the financial sector or of restrictions set on institutions and agents in individual segments, especially banking. The issue was posed as one of redesigning the regulatory framework to adequately take account of the changes in the world of finance. The overarching aim, however, was to claim that the attempt was to rein in the tendency of the financial sector to proliferate risk and create conditions for a systemic failure that, because of the externalities involved for the functioning of the real economy, required using tax payers' money to rescue the system.

Discussions on these and other proposals, running parallel to investigations on the developments that led up to the crisis in 2007, resulted in the bill introduced by senators Barney Frank and Chris Dodd, and finally passed in revised form and signed into law in July 2010. With the financial crisis having broken in 2008, when the real economy recession had already set in, this was indeed a quick response when compared with Glass-Steagall, which came in 1933, a full four years after the onset of the Great Depression. As has been noted, the Dodd-Frank Wall Street Reform and Consumer Protection Act "marks the greatest change to the financial landscape in decades, affecting the regulation of domestic and foreign financial institutions, banking entities and commercial companies". However, the Act's provisions are of any value only when they are translated into rules and interpreted by financial regulators.

There are, however, some indications that many of the original proposals and the thrust of the clauses incorporating them are being substantially diluted in the course of implementation. Among the many ways through which this has been occurring are three that have been particularly effective. The first is, of course, heavily funded lobbying to dilute the interpretation of the provisions of the Act and the rules being made based on it. The second is litigation aimed at challenging the interpretation made or the rules framed by different regulatory agencies. For example the International Swaps and Derivatives Association Inc. and the Securities Industry and Financial Markets Association filed a lawsuit against the CFTC's attempt to curb speculation by setting position limits or caps on the number of derivative contracts a trader, through its many arms, can have in a particular market. In response, in mid-May 2012, the CFTC met and decided with a 5-0 vote to raise to 50 per cent from 10 per cent the threshold for when a company is considered to have an ownership or equity stake in another firm and must add trading positions to the aggregate. The third is to starve the regulatory agencies of the resources needed to implement their now expanded regulatory ambit. SEC Chairman Mary Schapiro, for example, complained that Congress had not substantially added to the budgets of regulators after saddling them with almost 400 rulemaking requirements and a range of new enforcement powers. Republicans opposed to stronger regulation have reportedly sought to weaken new laws by starving regulators of funding. CFTC Chairman Gary Gensler is reported to have said: "The CFTC is an under-resourced agency. We've now been tasked with overseeing the $300 trillion U.S. swaps market – nearly eight times larger and far more complex than the futures market we've historically overseen. We're barely larger, however, than we were before we were given these new responsibilities."

The Consequence

One consequence of the persisting freedom with which banks and financial institutions can function, barring some tightening of capital adequacy norms and leverage rations, is that the cheap money infused into the system found its way to speculation in asset markets. It emerged that there were three problems associated with the pursuit of cheap and easy money strategy. The first was that it was not too successful in triggering a recovery, which has been ten years coming and is still, as noted, moderate in intensity and volatile in nature. The second was that it triggered forms of the speculative, carry trade in which low cost money is borrowed to invest in assets varying from government bonds, equity and emerging markets paper of different kinds to real estate and alternative assets, leading to a self-reinforcing rise in asset prices globally. The third is that, in the pursuit of this policy, while growth has moderately revived and unemployment fallen, inflation has remained stubbornly low. Europe has struggled to get inflation up to the ECB target of 2 per cent. The headline rate is just about getting there and core inflation—excluding energy and food— is 1 per cent or so, having been below 2 per cent for the last decade. In Japan too inflation is below the central bank's 2 per cent, though unemployment is down to a long period low of around 2.5 per cent. This undermines the conventional argument for central bankers to unwind their balance sheets, reverse the spike in liquidity and raise interest rates. But failing to do that keeps asset price inflation high, increasing the possibility that the bubble could burst, precipitating another financial crisis. Quickly unwinding central bank balance sheets by selling accumulated assets, could, however, set off a collapse in asset prices and deliver another kind of financial crisis. This strengthens the case of those who argue that, since inflation is low, there is no reason to change the prevalent monetary policy stance.

This has troubled global policy institutions, who fear that having got drunk on easy money, the financial sectors in advanced economies may implode once again. In June, Claudio Borio, the head of the Bank of International Settlements' monetary and economics department underlined the fact that: "The most fundamental question for central banks in the next few years is going to be what to do if the economy is chugging along well, but inflation is not going up." In his view, "Central banks may have to tolerate longer periods when inflation is below target, and tighten monetary policy if demand is strong — even if inflation is weak — so as not to fall behind the curve with respect to the financial cycle." (*Financial Times*, June 25, 2017).

In sum, central bankers need to reverse much of what they did over the last decade, even if they don't have high headline inflation, but only asset price inflation as a justification. Faced with this situation, central banks are deciding to scale back their policy of "quantitative easing" in the form of liquidity infusion through asset purchases. The Federal Reserve has already implemented that, while the European Central Bank has announced an end to bond buying. But none is willing to commit to a quick unwinding of balance sheets, for fear of precipitating a different kind of crisis as markets react to a radical change in the easy money environment they have gotten used to. Even if bond sales by central banks are resorted to, the measure will go only a part of the way. Asset holdings by central banks will remain well above their pre-crisis levels for quite some time. Whether this gradual approach will prevent a financial crisis stemming from a collapse of inflated asset prices, which some fear an end to the era of easy money could precipitate, only time will tell.

Fears of a Crisis

In October 2018 The IMF pointed to two factors—rising US interest rates and a stronger US dollar—that are contributing to downside risks. However, these factors in themselves are not recovery-threatening. The first, namely rising interest rates as part of a dose of monetary tightening, was long overdue. For almost a decade now the US Fed and central banks in other developed economies have been focused on quantitative easing and interest rate reductions, as antidotes for the recession. There was little disagreement on the need to unwind balance sheets, reign in liquidity infusion and raise interest rates. The only question was when, and how fast. The signs of a recovery in the US offered as good an opportunity as any to begin this long overdue exercise. To the extent that the rise in US interest rates and the improved performance of the US economy trigger a shift of investment in favour of dollar-denominated assets, a strengthening of the dollar would follow, making that too an expected outcome.

The reasons why these inevitable movements in interest rates and the dollar are identified as sources of concern relate to the consequences they have in the current global environment. Rising interest rates in the advanced nations is reversing the flow of capital from developed to developing. This is because much of the portfolio investment in "emerging markets" undertaken during the years of easy money reflected the "carry trade" encouraged by differences in interest rates. Investors borrowed cheap in dollar and euro markets and invested at the much higher interest rates in emerging markets. With those interest rate differences closing portfolio capital tends to flow out from developing countries. That outflow, besides limiting liquidity, weakens currencies, triggers speculation, and leads to a collapse (as happened in Argentina and Turkey) or a significant fall (as in Brazil, South Africa and India) in the value of local currencies vis-à-vis the dollar. This accelerates capital outflow.

Rising interest rates are also hurting private players in emerging markets who borrowed quite happily during the cheap money years, but now find that their debt service burden is rising sharply. This is true across the globe. But it is particularly true in the emerging markets where firms and other borrowers chose to pile up foreign debt, which was cheap but carried the risk of turning costly in local currency terms if the latter depreciates. Today they are faced with a double whammy. Rising interest costs that increase debt service commitments and sharply depreciating currencies that increase the domestic currency value of those commitments even more, hurting their bottom line and even presaging defaults.

The potential for currency crises, debt defaults and a liquidity crunch inherent in this situation, portends a substantial growth slowdown and even a return to recession. That is the "downside risk" that the IMF is concerned about. That downside risk is great because of the huge build up of debt in recent years. According to the IMF, "total nonfinancial debt in countries with systemically important financial sectors now stands at $167 trillion, or over 250 percent of aggregate GDP, compared with $113 trillion (210 percent of GDP) in 2008." This close to 50 per cent increase in non-financial debt over the last decade is surprising. A major cause for the 2008 crisis was the build-up of household and corporate debt, facilitated by a process in which risks were 'shared' through the creation and sale to third parties of securities backed by debt assets. So 'deleveraging', or reduction of debt on the balance sheets across firms and households was widely seen as crucial to any process of post-crisis restructuring. Contrary to that requirement the world now discovers that the debt overhang has risen sharply in the years since the crisis.

The IMF recognises why this has happened. "The unconventional monetary policies implemented since the global financial crisis were aimed at easing financial conditions to support the economic recovery", it notes. "In such an environment, total nonfinancial sector debt—borrowings by governments, nonfinancial companies, and households—has expanded at a much faster pace than the growth rate of the economy." Thus, the debt build up is the result of the use of monetary policy measures such as easy money policies and low interest rates in response to the recession induced by the financial crisis. But, if that crisis was the result of excess debt, then measures that increase rather than reduce the dependence on debt are not just the wrong medicine but counterproductive, as the danger of another crisis suggests. What is worse, that medicine has not delivered a robust recovery, with the return to growth restricted to a very few economies. In sum, governments and central banks got it wrong, when they relied on monetary measures as antidotes for the recession. That, however, is something the IMF is not willing to accept, since it would imply that greater reliance on proactive fiscal policies, or enhanced state spending, that it and the financial interests rail against, were possibly the better option.

The problems created by the reliance on unconventional monetary policies do not end with the danger of a debt bust. Stock markets across the world are coming off their highs. This is happening even in the US which is recording good growth and improved corporate earnings, with the official unemployment estimate of 3.7 per cent being at its lowest in almost half a century. Over the week-ended October 12, the US stock market saw a massive sell-off, bringing to an end the longest bull run in its history that had taken stock indices to unprecedented highs. This establishes what was clear for long, that the bull run was the result of speculative fever triggered by the easy and cheap money environment. To the extent that easy access to credit fuelled the speculative boom in the stock market, the bust can result in defaults, as over-indebted investors find they are unable to recoup their capital and repay their creditors. That is another outcome that could squeeze liquidity and stymie growth.

Finally, despite the central role of opaque asset backed securities in aggravating the 2008 financial crisis, the issue of such securities has not diminished. Noting that "leveraged finance, comprising high-yield bond and leveraged loan-based finance, has doubled in size since the Great Financial Crisis," the Bank for International Settlements argues that this was facilitated by developments in the securitisations market. "Originator banks are finding it easier to securitise and sell these loans. This can be seen in the growing investment in loans by securitised structures such as collateralised loan obligations, especially in the last couple of years." Nothing much has changed on the financial front since the crisis.

What is different this time around is that the danger of a crisis is not focused on the advanced nations, with the rest of the world, especially the emerging markets only experiencing the after-effects. In fact, in 2008, countries like China and India were still seen as growth poles that could help moderate the intensity of the global crisis and even lead the recovery. This time around the disease afflicts the emerging markets as well, which are bearing the brunt of the financial volatility unleashed by the reversal of 'overused' rather than 'unconventional' monetary policies.

Implications

Whatever be the coming denouement, it is clear that unlike in the 1930s the crisis of 2008 and after has not led to any fundamental restructuring of capitalism. The absence of such restructuring, the resulting halting recovery, the stagnation in real wages and the worsening of inequality has led to a loss of legitimacy. That loss of legitimacy is reflected in the Brexit vote, the rise of Trump to Presidency, the crisis in the EU and the eurozone, and the loss of dynamism in the emerging markets, which too are faced with the vulnerabilities created by globally mobile finance capital that has inflated their asset markets. All of these don't help resolve the problem but contribute to it in different ways. The chaos breeds anger, but that anger remains unchanneled into the backing of forces that can push ahead with the restructuring that must occur if capitalism has to get itself another lease of life.