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Is American capitalism running out of steam? Comparative insights from the Great Depression and the Great Recession[1]

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From 2007 to 2009, the United States (US) experienced a major financial and economic crisis, a 'Great Recession', whose depth, severity, and global impact evoked numerous comparisons with the deepest structural crisis of the twentieth century – the Great Depression of the 1930s. There are significant similarities between the circumstances and dynamics surrounding both crises. And yet, those similarities should not distract from even more important differences.

The boom and the bubble: then and now

The Great Depression and the Great Recession were triggered by asset-price bubbles – a stock market bubble in the late 1920s and a housing bubble in the 2000s – but pre-existing structural imbalances in the US economy were the reason why the burst of speculative bubbles induced a general economic collapse. One fundamental imbalance was the highly unequal growth of property income relative to labour income. The combination of relatively stagnant labour income and surging corporate profits played a leading role in the run-up to the downturns and was chiefly responsible for the slow recoveries. The boom and the bubble in both instances were driven by similar dynamics: sluggish wage growth and falling labour share of national income, deepening inequality with heavy concentration of wealth gains at the top, corresponding mounting indebtedness among lower- and middle-income households, surging corporate profits and a corporate saving glut seeking financial ventures. Thus, two causal mechanisms underlay the structural fragility of the economy then and now. On the one hand, the stagnation of labour earnings represented a key factor behind rising income inequality and a drag on consumption which was temporarily alleviated by credit expansion; hence, the rising household debt levels which eventually became unsustainable. On the other hand, rising corporate profits created an overhang of idle money, eager to lend itself to speculative ventures, which played a key role in fuelling the stock market bubble of the 1920s and the housing bubble of the 2000s.

How and why this time was different

The Great Depression and the Great Recession were triggered by asset-price bubbles, but to trigger something does not mean to cause it. While some features of the US economy then and now gave rise to similar dynamics, those similarities cannot justify claims that the policies enacted to bring the economy out of the Depression can work again in some modified form to rid us of the consequences of the Recession. The US economy now is fundamentally different.

The accumulation of surplus capital as a result of surging corporate profits was among the leading causes of both crises, but in the first, the surplus of capital led to overinvestment relative to effective demand. In the second, there is surplus of capital relative to profitable investment opportunities in the domestic economy in addition to looming prospects of weak demand.

The Great Depression originated in overinvestment relative to consumer demand against the backdrop of labour abundance and low wages that ultimately drove the economy into an underconsumption trap; hence, the depth, length, and severity of the slump. Consumption in highly unequal societies depends critically on the combination of continuous borrowing by low- and middle-income households and luxury spending by the rich. In time, the relative importance of the latter is bound to increase as rising debt-to-income ratios impede further borrowing. The effects of the stock market crash were almost immediately felt in the consumer goods' market as collapsing fortunes diminished orders for dispensable luxury goods. Producers reacted to falling demand by curtailing investment. Superficially, these dynamics resemble those underlying the run-up to the Great Recession, but that is not all there is to it.

The US economic and military success in the post-war age of high mass consumption was based on dramatic expansion of potential output during the Depression years due to the combination of continued growth of productivity in manufacturing and the spill-over effects into transportation and distribution resulting from the extension of public infrastructure. The extraordinary level of productivity reached during World War II significantly overshot both the pre-Depression and the post-war trend.

The Great Recession was preceded by massive overinvestment in construction which should not be confused with a general investment boom. The housing bubble was sustained through strong institutional support for homeownership which gave rise to the lowest mortgage-lending standards in history, low interest rates, a financial industry eager to innovate, and a massive demand for high-yield assets by institutional investors, corporations, wealthy individuals, governments, sovereign wealth funds, and so on. Multiple trillions of idle money in the global economy were looking for profitable ventures. The Great Recession started in the

US but had global origins, and not merely global impact. It was, in fact, the first crisis of capitalism as a system of globalized production characterized by the geographical separation between production and consumption along with the persistent imbalances this spatial configuration generates. Yet most accounts of the crisis tend to ignore how profoundly the globalization of production has transformed the structural underpinnings of domestic demand and profitability.

Unsurprisingly, analysts finding it difficult to frame the Great Recession as either a demand-side or a supply-side crisis frequently invoke the spectre of financialization as the main culprit. But financial bubbles are temporary occurrences that neither create nor alter long-term development trends. The housing bubble of the 2000s was no exception. The sluggish investment underlying the present weak recovery follows a long-run trend of relative slowdown of capital accumulation in the US since the late 1960s. The Great Recession may have opened the door to a different world but did not create it. It exposed tendencies that have been lurking in the background for decades. This newly uncovered world is characterized by sluggish domestic investment and weak labour-income growth.

Structural inadequacy of aggregate demand was one of the factors underlying the Great Recession. The overextension of credit was among the key reasons why effective demand appeared healthy before the crisis. The curtailment of credit through tightening lending standards, prompted by rising debt burdens and insolvency of borrowers, accounted to a significant extent for the drop in consumer demand after the crisis started. The full effects of rising debt on the American economy have not yet been felt but are bound to be. The demographic profile of debt distribution is characterized by a growing burden on younger generations which is likely to alter the dynamics of consumer spending in the future. Furthermore, US consumer spending is heavily oriented towards imported goods as manifested in the US current account deficit (CAD) which peaked at $806.7 billion (about 6% of GDP) in 2006. The major contributor to the CAD is the negative trade balance and, in particular, the deficit on the balance on goods which reached $838.3 billion in 2006. More than 50% of the latter came from the combined deficits in consumer goods and automotive vehicles, parts, and engines. Another 40% came from the deficit in industrial supplies and materials including intermediate inputs used by US firms. Despite the impressive decline of the CAD to $390 billion in 2014, the deficit on the balance on goods was still $741 billion and is unlikely to decline significantly in the near future. The import-oriented structure of US consumption and production explains why buoyant consumer spending during the bubble years and beyond has done relatively little to stimulate domestic investment.

Similar considerations should be taken into account regarding profitability trends in the US economy. Marxist economists, in particular, observe movements of the profit rate with keen interest because they see the growth dynamic of a capitalist economy as directly linked to the general rate of profit it generates. While there is no agreement whether the rate of profit rose or fell before the recent crisis, most accounts point to a rise. The mass of profits has undoubtedly risen, thereby providing one of the fundamental causes of both crises. However, the feasibility of measuring the US rate of profit as the ratio of domestic profits to the stock of domestic investment is questionable. The profits generated within a multinational corporation cannot simply be split into domestic and overseas components because the spatial reorganization of production through offshoring and outsourcing raises profitability both domestically and globally. Thus the improved profitability of domestic business may simply be evidence that US multinationals have successfully optimized operations through global restructuring.

The idea that capitalism's capacity to continuously revolutionize its means of production may be running out of steam is anathema to the great majority of economists, mainstream and Marxist alike. And yet there has been a recognizable slowdown in capitalism's general technological capacity to innovate in a way that could spur new investment and raise productivity growth to levels comparable with the post-war Golden Age. Different factors account for the decline. On one hand, there are grand-scale, civilizational factors, such as the forces of the second industrial revolution (1870-1990) that were unique and cannot be repeated. The resulting rapid rise in living standards is also becoming impossible to sustain. On the other hand, it can be argued that the tendency to monopolization, characteristic of US capitalism, has eroded competition and hampered innovation. The combination of structural supply-side and demand-side weaknesses does not bode well for US and global capitalism.

Conclusion

The growth prospects for US capitalism then and now are vastly different. World War II served as a huge stimulus for the depressed economy. The institutional regulation of demand whose foundations were laid down by the New Deal and solidified in the post-war period played an essential role in stabilising accumulation under Fordist, mass-production capitalism. The present crisis is different. It cannot be solved through the institutional re-regulation of demand because the existing problems extend to the core structure of capital accumulation.

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1 This piece draws on Ivanova, Maria N. (2017) 'Profit growth in boom and bust: the Great Recession and the Great Depression in comparative perspective,' Industrial & Corporate Change 26(1): 1–20. Available at https://academic.oup.com/icc/article/26/1/1/2907947/Profit-growth-in-boom-and-bust-the-Great-Recession