

MODERN MARXIST MONETARY THEORY. Further observations.

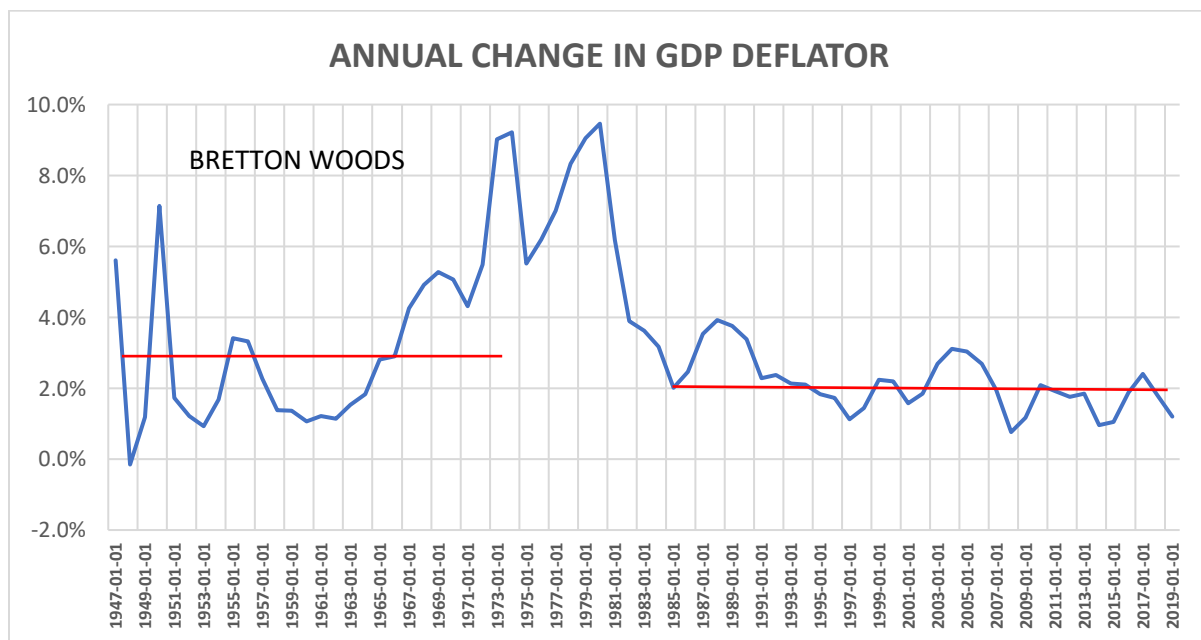
This article follows on from the previous article looking at how prices are affected by symbolic money exchanging legacy value for newly produced value. It looks at a number of variations each of which leads to differing price outcomes. The important point to make is that legacy value is not depreciated or appreciated by changes to current costs of production. Rather it is the interaction between legacy value which is fixed, and current value which is variable, that determines prices.

In the previous article we recognised that revenue or income represented the monetization of value, or what is the same thing, its conversion from privately produced value into social value. This legacy value in its money form thus made up the money supply both potential and active. We also recognised that National Income forms around 92% of M2 or at least 9 out of every 10 dollars, it therefore constitutes the bulk of M2. Therefore any equation which added National Income to M2 was guilty of double counting while failing to understand the true nature of legacy value.

We also recognised that legacy value, having previously been produced, was fixed, it could not be altered. (We exclude capital which is legacy value re-invested.) This meant it differed from metallic money, whose costs of production could vary, meaning its current value was not fixed. This variability could affect prices regardless of the money supply. The same does not apply to legacy value, and therefore prices, as we are about to see.

It is not often that I begin with a graph. I do so because in the previous article I made the bald statement that legacy value money tends towards price stability. This graph proves this. The peaks in the 1970s and 1980s refer to the convulsive adjustment from a regulated exchange rate to free floating rates. But once stability had been achieved from 1985 onwards, prices became less volatile than under the gold standard.

Graph 1.



(Source: FRED Table GDPDEF)

Five propositions.

The 5 propositions boil down to the variations found between legacy value in its monetary form and new value in its commodity form. It expresses the distinct interaction between amount of legacy value which is fixed and current value which is not. When examining these propositions a number of simplifications will be used. We will abstract out hoarding and we will assume that government spending is balanced such that tax revenues equate to government expenditure. However, we will introduce credit money (bank lending) where necessary.

Depreciation does not affect our considerations. Although the individual firm uses depreciation as a sinking fund, when aggregated over the economy as a whole, the depreciation being added to is also being consumed by new investment elsewhere. With the exception of recessions and certain industries, gross annual fixed investment regularly exceeds annual depreciation thus rendering it inconsequential for our purposes.

Finally, we are here considering periods. On average in the USA fluid or working capital turns over 4 times a year or about every 90 days on average. This means that sales revenue is produced on average 4 times a year replenishing working capital and yielding undivided profits. During those 90 days, wage revenue will tend to be generated every 30.3 days (monthly) and also consumed on a monthly basis, which is why M2 will always fall below National Income. All other revenues will be recorded only on the completion of the circuit of capital. Thus annual SNA recording of revenue will inadvertently add up wage revenue 12 times but all other revenues only 4 times. Without understanding the differential between wage revenue and all other revenues it is impossible to account for M2 lagging behind National Income as they are two sides of the same coin.

Here we will examine 5 examples in the raw. However, besides being abstractions they do cover all the eventual variations in pricing found in the real economy induced by the interaction of legacy value and new value. They represent dialectics in motion, the synthesis of the past and the present.

Example 1.

In all cases we are comparing adjacent periods. Here the same number of productive workers are employed in each period yielding the same quantum of labour time. However, between the two periods productivity increases by 2%, meaning that the same number of workers in the same time produce 2% more products measured by volume. In this case, the legacy value which matches the value currently being expended is crystalized in 2% more product. Accordingly there will be a 2% fall in prices. Prices will fall in line with the fall in labour time.

Example 2.

In the current period production has expanded significantly. Workers are not necessarily more productive, but the number of productive workers employed has increased by 5%. Consequently the number of products measured in volume will have increased by 5%. The main conclusion to be drawn is that legacy value and current value no longer equate. There is less legacy value in existence to circulate current production. If this was the final situation, then the prices of current production would be depressed despite the fact that actual costs of production remain constant.

This is where credit money comes in. When Marx viewed the rapidly expanding capitalist world economy, he recognised that this could not have taken place without the emergence of a sophisticated financial sector oiling this expansion. The same could be said of China which grew on the basis of hugely expanded credit money. The alternate argument that saving can substitute for credit money holds no water when viewed on a grand scale as it would actually reduce the amount of legacy value expended at a time when that legacy value is already inadequate. (We remind the reader that we are not dealing with concrete reality, but in the jargon, mind games.)

Example 3.

In this example we have a fall in the number of productive workers such that the expenditure of labour time now falls below the expenditure of labour embodied in legacy value. However, because of the rise in productivity the volume of products remains the same. Thus productivity compensates for the fall in the number of workers. In this case legacy value exceeds current value though the volume of production remains unchanged. In this example the market price of the new products will not fall despite the fall in their actual costs of production.

Example 4.

Here we find a fall in the amount of labour time and an increase in the volume of production. Thus whereas in example 3 production was unchanged, now it has increased. Let us say there has been a fall in labour time of 5% but a rise in productivity of 10%, yielding an increase in the volume of production of 5%. In this case there will be a fall in market prices, but not by the full 10%, but only by 5%.

Example 5.

This is the final example. Here nothing has changed between legacy value and currently produced value. The value embodied in legacy value and the value emanating from production balance and there is no adjustment to volumes of product. What has changed is that there has been a fall in the rate of investment meaning less legacy value is being converted into capital and therefore circulated. Under these conditions there will be a general fall in prices regardless of the fact that prices of production are unchanged. Here we have a realisation problem.

These 5 examples exhaust the possibilities lodged in the interaction between legacy value and value.

Looking at some periods more concretely.

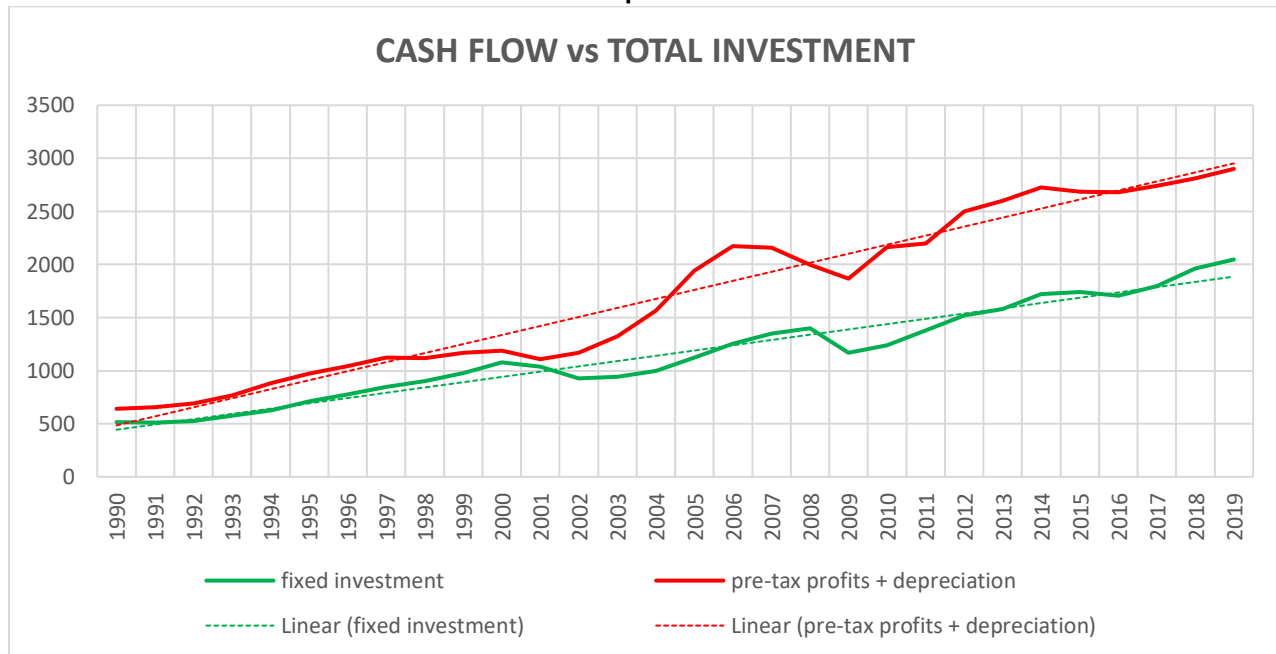
In the adolescence of capitalism, when both labour time and productivity are both on the increase, and where legacy value is constrictive, it is clear credit money generation is needed, and also, it is associated with sharp falls in market prices. Most if not all the falls in labour time are reflected in market prices including market prices of production, setting aside the industrial cycle.

In periods of structural change as occurred between 1973 and 1983 resulting in a collapse in the value of current production, the result was rampant inflation, or what is the same thing an excess of accumulated legacy value compared to current value. Of course this inflation was exacerbated in the USA by the depreciation of the dollar based on the new economic realities.

With exception of the late 1980s when defense spending drove up inflation, over the following 35 years inflation seldom rose above 2%. Some of this was due to cheaper prices flowing in from China as it

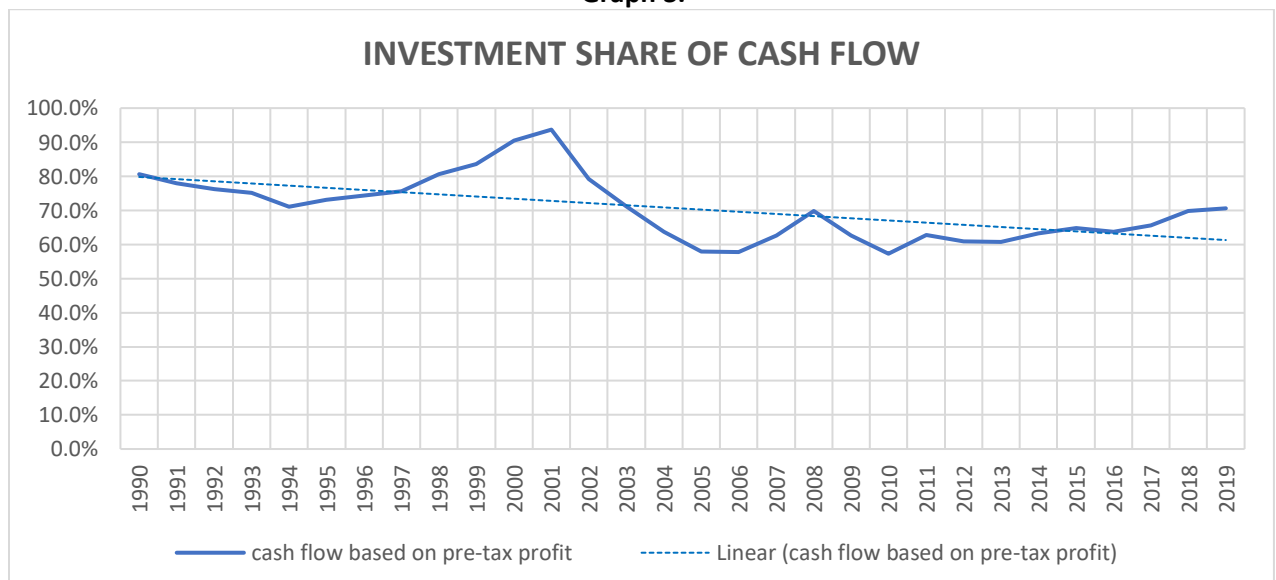
industrialized and became the workshop of the world, and some of it was due to globalisation itself which centralized value in the hands of corporations headquartered in the USA, the EU and Japan. This led to relative under-investment and thus to an interruption in the circuit of legacy value. It was also due to the subdued class struggle allowing the employers to steal all the productivity gains without using inflation. This can be seen in the two graphs below. (Data from the attached spreadsheet table 1.14 1989 – 2019.)

Graph 2.



The data above relate to fixed investment only. Changes to circulating capital are deliberately excluded as they have already fed into the profit figures. Cash flow is based on depreciation and pre-tax unadjusted profits. Pre-tax is chosen to avoid changes to cash flow resulting from changing tax rates. All data relates to non-financial corporates.

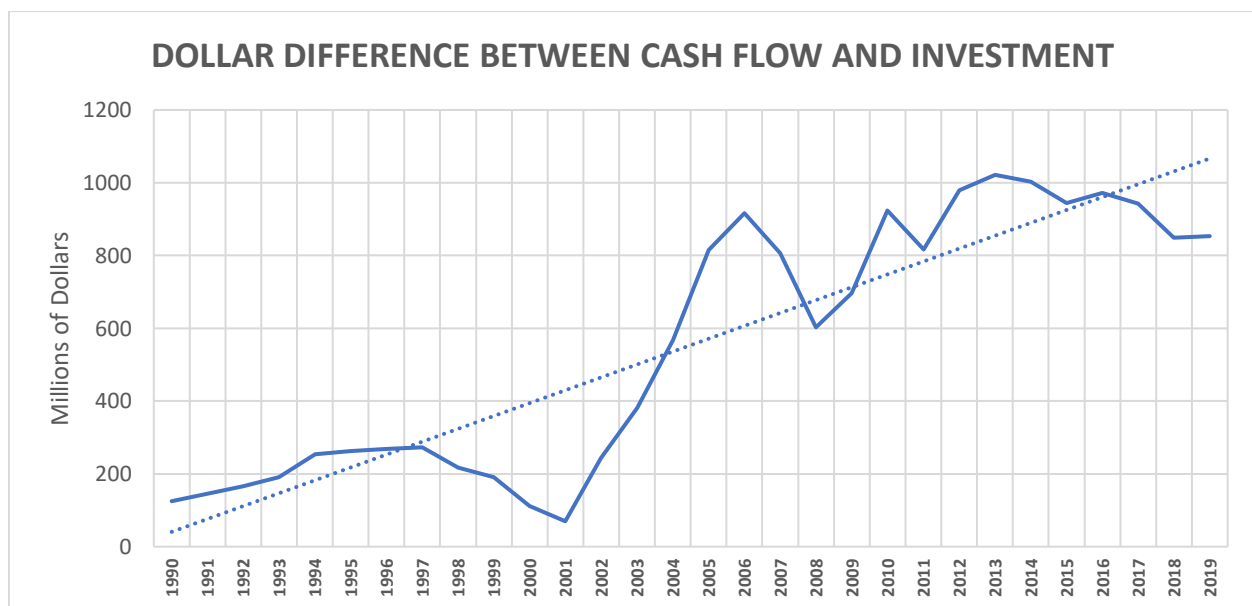
Graph 3.



Graph 3 gives a better appreciation of the relative balance between cash flow and investment. There appears to be an improvement in the rate of investment post 2017 but that is deceptive. Since 2014 the mass of profits has fallen in absolute terms arresting the growth in cash flow. In 2019 cash flow adjusted for inflation (GDP deflator above) fell 2% compared to 2014 whereas investment rose 10%. Despite real growth in investment, the rate of profit has continued to fall, a case of throwing good money after bad.

The main point however is that there has been a relative and absolute fall in investment compared to cash flow with the exception of the period immediately prior to the dotcom crash. This century the dollar difference between the two shot up to reach over \$800 billion before the financial crash, a level it has held, and continues to hold, despite the fall in the mass of profits post 2014. This was equal to at least 5% of GDP at the time though under it currently.

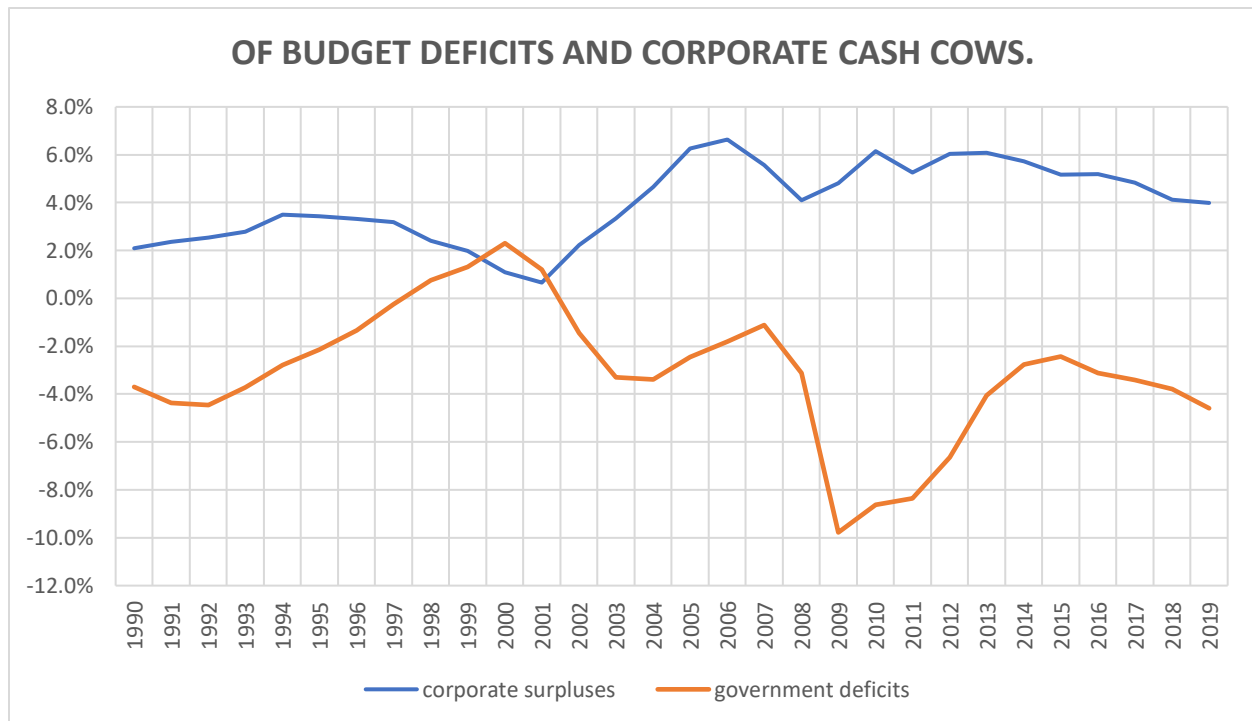
Graph 4.



This huge body of surplus cash funded the share buy-back fad intended to drive up share prices, mirroring in magnitude, the rise of these hoards. In effect hoards passed from corporations into the pockets of their shareholders. The was euphemistically called, “capital efficiency”, because capital was passed on to those who knew best how to invest it, i.e. the speculators.

The net effect of these hoards was to slow down the circulation of legacy value. However this was balanced by the growing fiscal (budget) deficits this century as the graph below shows. Adjusted for tax, corporate cash flow surpluses and fiscal deficits literally cancelled each other out. Over the 20 years the surplus measured 4.6% (pre-tax) while the budget deficits measured 3.5%. Thus the state helped circulate legacy value while shareholders sat at the roulette tables on Wall Street.

Graph 5.



Since the advent of globalisation there has been no issue of realisation in mature economies because legacy value has tended to exceed current value. Given that the direction of travel is from more expensive to cheaper production, everything else being equal, legacy value should exceed current value, except under conditions of accelerating investment where labour time is significantly increased. This being so, it is unlikely that the legacy value was inadequate to circulate current value. Therefore the issue of demand setting prices in conjunction with actual costs of production does not arise. Generally the issue of realisation is associated with a sharp deceleration in the circuit of capital as trade credit shatters. It is an issue of the industrial cycle.

Legacy Value and Labour Vouchers.

Legacy value is post-partum. In a society based on exchange, the labour of the individual only becomes part of the labour of society indirectly having first to be exchanged. Therefore, the new revenue that emerges can only emerge after the monetary completion of the exchange. Prior to this, expenditures are based on spending past revenues. This can be most clearly seen with wage revenue. The capital that pays for wages is variable capital and it represents past accumulated labour. In the course of the typical 90-day circuit of capital employers need sufficient capital on hand to pay their workers until the circuit completes and new money replenishes the old with a surplus. That variable capital must represent revenue drawn from previous circuits of capital reconverted into capital. During the current 90 days workers will have produced sufficient labour to reimburse their employer for any wages paid. Similarly unless the employer chooses not to starve, they will need revenue on hand to consume while waiting for the 90-day circuit to complete when once again they will be rewarded with new revenue. Thus revenue being consumed generally results from the conversion of past labour into revenue.

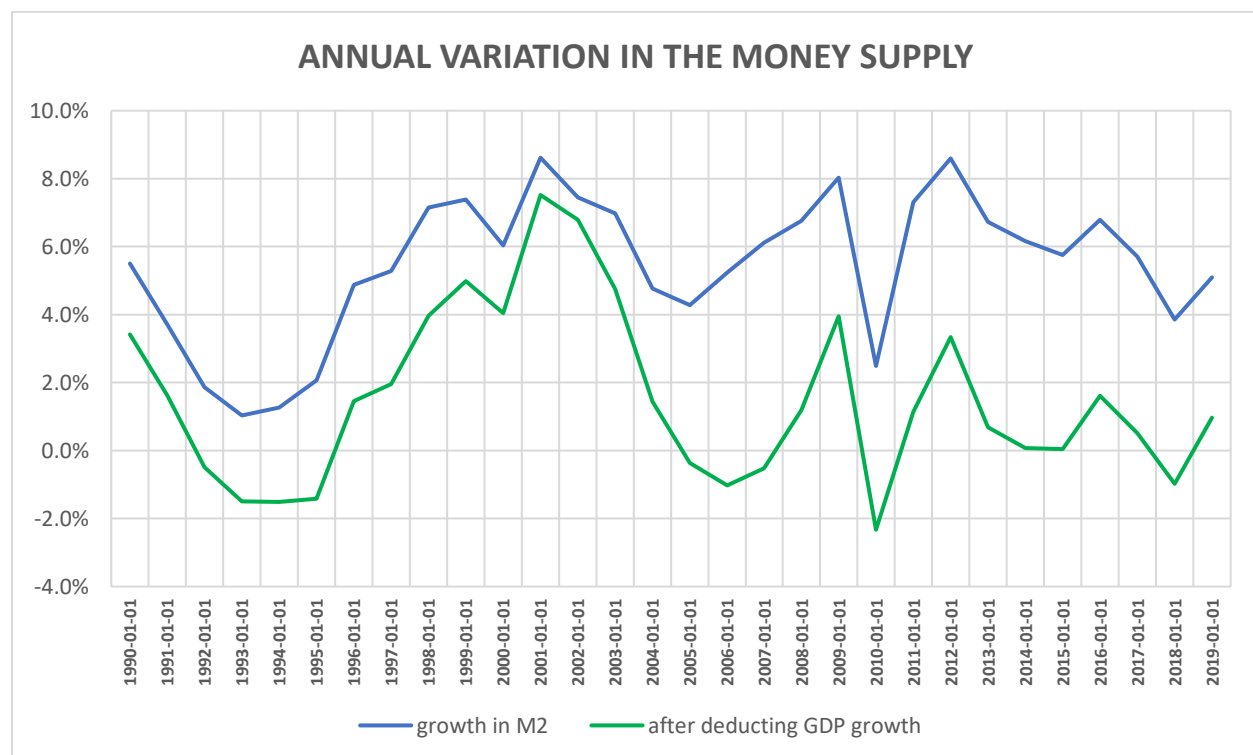
In a communist society based on labour vouchers things stand completely differently. Here the labour of the individual becomes part of the labour of society directly. Thus labour vouchers are claims on current production or more precisely on current inventory as it emerges. (See, Note 1 at the end.) Everything happens in real time. In a harmonized world economy, which means goods will no longer be dragged thousands of miles to be completed or delivered, most articles of consumption will be produced and be ready to be consumed/delivered within days. Already inventory turnover in the irrational capitalist economies takes only 5 to 6 weeks. (Housing does not come into this as the finance for this will come from a homes' tax.) The advent of the producer-consumer means an end to the past circulating the present.

Some theoretical questions.

It is important to bear in mind we are not discussing competition in the normal sense, that is within an industry and between industries all inside the same time frame. Rather we are discussing a peculiar form of competition between time frames, how the past influences the present. Now it is true that legacy value will influence current competition. If legacy value is insufficient to circulate current value, then competition will intensify resulting in a fall in general price levels, and vice versa when legacy value is greater than current value, it will moderate competition leading to a rise in price levels, everything else being equal.

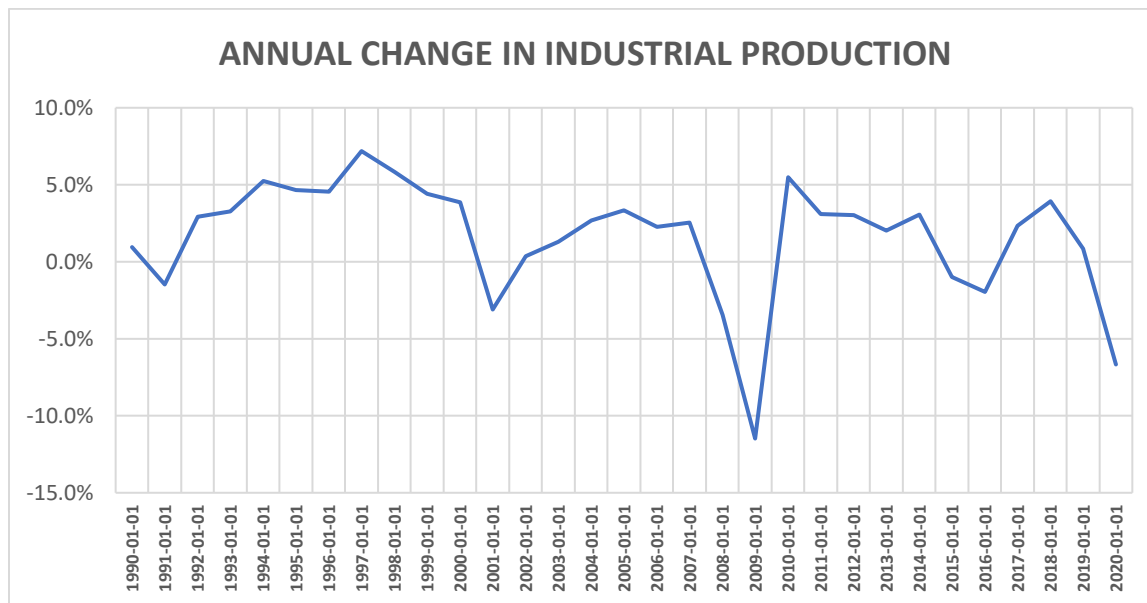
But everything else is not equal. To this equation must be added two additional variables, credit money and fiscal spending. Credit money tends to expand by up to 6% on the upside of the industrial (cycle) and to fall by up to 3% on the downside, thus a variation of 9% in the money supply. This is shown in the green graph which is more important graph because by removing the element of the money supply added by GDP growth (revenue) it reveals actual credit money growth or contraction.

Graph 6.



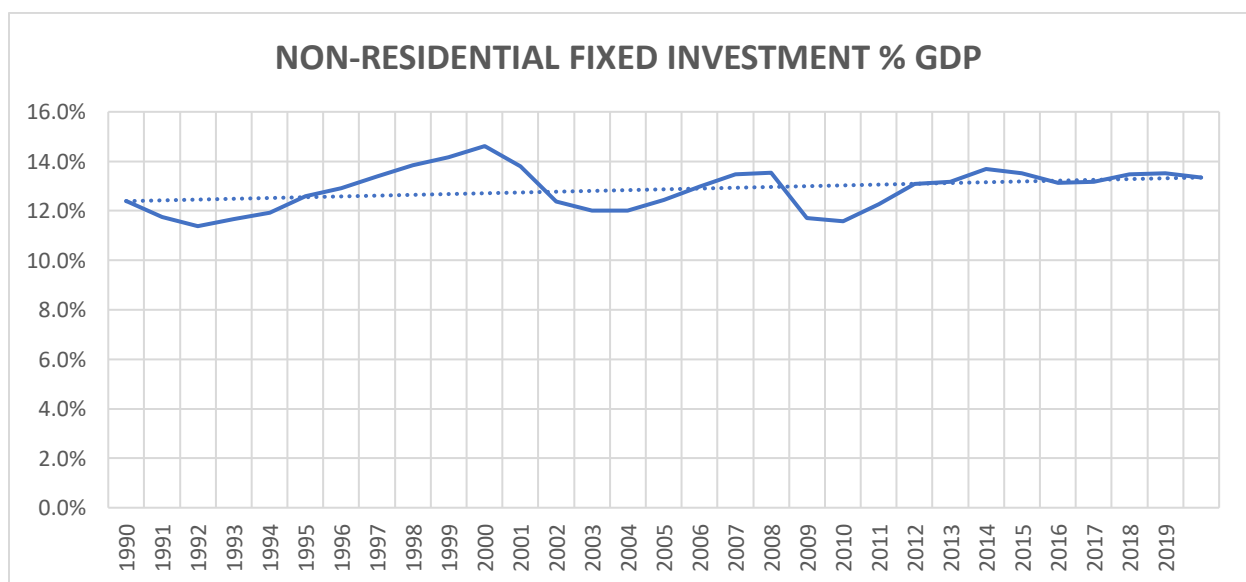
When viewing the next graph below we should bear in mind that the value of industrial production is less than a third of GDP. Thus adjusted to GDP levels the changes will be one third as large. This reduces the the greatest variation found, 18% (1997 vs 2009) to 6%. It thus fits well into the range set by variations in credit money found in Graph 6.

Graph 7.



And of course there is the issue of fiscal spending which this century has added about 3% p.a. on average to the money supply. All of this taken together, it is unlikely that there was insufficient monetary demand to constrict prices. There has been a rapid expansion in personal consumption aided by capital gains, and even a modest increase in non-residential fixed investment.

Graph 7.



It is this 21st Century reality that has led me to conclude, that when aggregated, demand plays no role in determining market prices of production by its inadequacy. Only at the terminal phase of the industrial cycle, occurring twice, has there been a chronic problem of realizing value due to lack of demand. However, without chronic deficit spending by governments, except Germany, the under-consumption of the capitalist class could have led to a lack of demand. Finally, the easy money conditions assisting the growth of credit money also helped. This century, real credit money growth has averaged 1.6% p.a. adjusting for the peaks and troughs, but how much of this has been wasted, is incalculable.

Conclusion.

The discussion over the prospects of rising inflation has taken center stage in capital markets. Larry Summers continues to accuse the Biden Administration of unleashing inflation in the order of the “Vietnam War” when he recently addressed the Federal Reserve in Atlanta. However, it is clear that high frequency data is beginning to show a deceleration in production and retailer movements around the world compared to their earlier highs. Thus the view that there will be a sharp bell curve in inflation seems to be bearing out.

It is this intensity of debate around pricing which set the stage for these two articles examining modern money based on legacy value. Modern Marxist Money Theory is based on recognizing that modern money is the monetization of legacy value in the form of revenues held in cash or on deposit regardless of the currency in which it is denominated. Whereas the value of actual physical money (gold) can vary with changes to its weighted cost of production, legacy value is fixed because it represents labour already produced and monetized. Thus its relation to prices differs from that of metallic money.

Contrary to the popular belief that symbolic money is always volatile, Graph 1 shows that once floating rates had settled, inflation from the mid-1980s was less volatile and lower on average than inflation under Bretton Woods. Of course the confounding factor was the class struggle which was much more subdued from the 1980s onwards. Thus, while the two periods are not strictly comparable, the latter period shows that symbolic money regulated by legacy value can underpin price stability because the mass of legacy value is fixed by past production.

Finally the formula set out in the earlier article on MMT: $P \times T^{ft} = R + NL - H + Sp + FQ$ appears to capture the influence of the additional factors adding to or subtracting from legacy value, altering prices. The link to the article is below. However, what must not be lost sight of, is that legacy value provides the bulk of the money supply, because it provides on average around 92% of all money on demand.

<https://theplanningmotivedotcom.files.wordpress.com/2021/05/mmt-part-1-1.pdf>

Note 1. It could be argued that if workers saved some of their labour vouchers and used them in the future, they could take advantage of falling prices. However, in a communist society, the pressures that give rise to saving would be non-existent because there will be a comprehensive safety net. The social fund which workers contribute to will comprehensively cover accidents (insurance), social care including childcare, pensions, education at all levels and so on and so forth. In fact, there will be a recognition that individual savings could disrupt planning itself.

Brian Green, 22nd May 2021.