

Give Karl Marx a Chance to Save the World Economy: George Magnus

By **George Magnus**
Aug 28, 2011 7:00 PM GMT-0500



Illustration by Jordan Awan

Policy makers struggling to understand the barrage of financial panics, protests and other ills afflicting the world would do well to study the works of a long-dead economist: [Karl Marx](#). The sooner they recognize we're facing a once-in-a-lifetime crisis of capitalism, the better equipped they will be to manage a way out of it.

The spirit of Marx, who is buried in a cemetery close to where I live in north [London](#), has risen from the grave amid the financial crisis and subsequent economic slump. The wily philosopher's analysis of capitalism had a lot of flaws, but today's global economy bears some uncanny resemblances to the conditions he foresaw.

Consider, for example, Marx's prediction of how the inherent conflict between capital and labor would manifest itself. As he wrote in "[Das Kapital](#)," companies' pursuit of profits and productivity would naturally lead them to need fewer and fewer workers, creating an "industrial reserve army" of the poor and unemployed: "Accumulation of wealth at one pole is, therefore, at the same time accumulation of misery."

The process he describes is visible throughout the developed world, particularly in the U.S. Companies' efforts to cut costs and avoid hiring have boosted U.S. corporate profits as a share of total economic output to the highest level in more than six decades, while the [unemployment rate](#) stands at 9.1 percent and real wages are stagnant.

U.S. income inequality, meanwhile, is by some measures close to its highest level since the 1920s. Before 2008, the income disparity was obscured by factors such as easy credit, which allowed poor households to enjoy a more affluent lifestyle. Now the problem is coming home to roost.

Over-Production Paradox

Marx also pointed out the paradox of over-production and under-consumption: The more people are relegated to poverty, the less they will be able to consume all the goods and services companies produce. When one company cuts costs to boost earnings, it's smart, but when they all do, they undermine the income formation and effective demand on which they rely for revenues and profits.

This problem, too, is evident in today's developed world. We have a substantial capacity to produce, but in the middle- and lower-income cohorts, we find widespread financial insecurity and low consumption rates. The result is visible in the U.S., where new housing construction and automobile sales remain about 75% and 30% below their 2006 peaks, respectively.

As Marx put it in *Kapital*: "The ultimate reason for all real crises always remains the poverty and restricted consumption of the masses."

Addressing the Crisis

So how do we address this crisis? To put Marx's spirit back in the box, policy makers have to place jobs at the top of the economic agenda, and consider other unorthodox measures. The crisis isn't temporary, and it certainly won't be cured by the ideological passion for government austerity.

Here are five major planks of a strategy whose time, sadly, has not yet come.

First, we have to sustain aggregate demand and income growth, or else we could fall into a debt trap along with serious social consequences. Governments that don't face an imminent debt crisis -- including the U.S., [Germany](#) and the U.K. -- must make employment creation the litmus test of policy. In the U.S., the employment-to-population ratio is now as low as in the 1980s. Measures of underemployment almost everywhere are at record highs. Cutting employer payroll taxes and creating fiscal incentives to encourage companies to hire people and invest would do for a start.

Lighten the Burden

Second, to lighten the household debt burden, new steps should allow eligible households to restructure mortgage debt, or swap some debt forgiveness for future payments to lenders out of any home price appreciation.

Third, to improve the functionality of the credit system, well-capitalized and well-structured banks should be allowed some temporary capital adequacy relief to try to get new credit flowing to small companies, especially. Governments and central banks could engage in direct spending on or indirect financing of national investment or infrastructure programs.

Fourth, to ease the sovereign debt burden in the [euro zone](#), European creditors have to extend the lower [interest rates](#) and longer payment terms recently proposed for [Greece](#). If jointly guaranteed euro bonds are a bridge too far, Germany has to champion an urgent recapitalization of banks to help absorb inevitable losses through a vastly enlarged European Financial Stability Facility -- a sine qua non to solve the bond market crisis at least.

Build Defenses

Fifth, to build defenses against the risk of falling into deflation and stagnation, central banks should look beyond bond- buying programs, and instead target a growth rate of nominal economic output. This would allow a temporary period of moderately higher

inflation that could push inflation-adjusted interest rates well below zero and facilitate a lowering of debt burdens.

We can't know how these proposals might work out, or what their unintended consequences might be. But the policy status quo isn't acceptable, either. It could turn the U.S. into a more unstable version of [Japan](#), and fracture the euro zone with unknowable political consequences. By 2013, the crisis of Western capitalism could easily spill over to [China](#), but that's another subject.

([George Magnus](#) is senior economic adviser at UBS and author of "Uprising: Will Emerging Markets Shape or Shake the World Economy?" The opinions expressed are his own.)

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