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Financialization and the Monetary Circuit: A Macro-accounting Approach

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Acknow

This paper has a long history. The first draft stems from my work with Riccardo Bellofiore at the University of Bergamo in 2010–2011. The current version has greatly benefited from my weekly conversations with Malcolm Sawyer in Leeds. Finally, I am grateful for comments by Alessandro Vercelli, Giuseppe Fontana and Hervé Baron. The usual disclaimers apply.

Notes

[1]We abstract for the moment from the repayment of interest to the banks. Following Zezza (2012), hereafter it is implicitly assumed that the 'financial period' (starting with the creation of bank loans and ending with the paying off of the debt) is longer than the 'production period' (i.e. the time corporations need to sell output to both wage-earners and banks). This allows us to treat interest payments consistently.

[2]If households do not hoard deposits, then even the sums paid by corporations as interests on bonds flow back to the corporate sector.

[3]A corporation might buy back its own shares in order to sustain the price of shares, to adjust the liquidity of its balance sheet, or to distribute income to its owners in the form of capital gains.

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subtraction from household real income, rather than from the corporate one. Nevertheless, for the sake of simplicity, in the rest of the paper we will continue to assume that banks use all of their retained earnings to purchase equities.

[8]It is a simple matter to demonstrate that this method leads to results that are equivalent to cost-plus pricing.

[9]This suggests that implementation of an expansionary monetary policy by the central bank via the reduction of interest rates may have a 'crowding out' effect on traditional banking activity unless it is offset by a strict regulation of the financial services industry.

[10]One might be tempted to think that asset inflation can have only microeconomic effects but no macroeconomic consequences, since capital gains realized by some units (either households or corporations) offset capital losses suffered by others. However, this is not true whenever: (i) there is asymmetric information, so that agents realizing capital gains react more quickly than agents suffering capital losses; (ii) capital gains and losses entail a redistribution of income among different sectors; or (iii) bank loans are linked to the value of assets, allowing agents to realize capital gains immediately.

[11] Figure 2 shows that, if the stock buyback is 'internal' to the corporate sector, then the households sector cannot draw from the financial market the liquidity it needs to
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[12] Government sector deficits financed through the issue of money represent an additional source of funds for the private sector. The same goes for balance of payments surpluses. In the Euro Area, the financial condition of countries marked by external surpluses may be easily likened to that of corporations depicted in Figure 2, whereas the situation of deficit countries can be likened to that of the household sector. In both cases, behind the appearance of sustainability, there are increasing imbalances between sectors or countries, which are bound to lead to financial fragility and to crisis.

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