Book Reviews

Yanis Varoufakis (2011)
The Global Minotaur: America, the True Origins of the Financial Crisis and the Future of the World Economy
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This is a fascinating book: not only do we learn about the Global Financial Crisis (GFC) that has plagued the world since 2007–2008, but we also learn some Greek mythology! The 'Minotaur' comes from Cretan mythology: King Minos of Crete asked Poseidon for a sacrificial bull as a divine endorsement of his rule, but he decided against the sacrifice and in vengeance the gods had Minos' wife (Aphrodite) fall in 'lust' with the bull, and they produced a Minotaur (Minos' bull or *taurus*, half-human, half bull)! The other states had to pay tribute to King Minos. However, King Aegeus of Athens eventually slaughtered the bull and freed Athens from Cretan domination. For Varoufakis, the Minotaur represents the USA, and the tributes paid to the USA are the capital flows from the rest of the world. Is the US Minotaur going to be 'slaughtered' by China? This book is based on a previously published 'academic' book, *Modern Political Economics*, jointly authored with Joseph Halevi and Nicholas Theocarakis, but the book under review is single authored. Varoufakis provides an excellent exposition of the origins of the GFC.

To provide an explanation of a crisis we need to explain (a) the underlying causes of the crisis; (b) what is the (immediate) trigger that led to the crisis; and (c) the transmission processes (the propagation mechanism). The underlying causes of the GFC can be traced to the stagnation of real wages and increasing inequality in the USA (and also Europe, although Europe is not mentioned by Varoufakis). In the USA, although the economy was going through a prosperous period, real wages for workers remained almost constant for over two decades and inequality was increasing. Workers, in an attempt to cope with stagnating wages, took out larger and larger loans based on their inflated housing values, and the financial sector was more than happy to lend. The government with its increasing expenditures on defence (the Iraq and Afghanistan wars) and lowering of taxes (especially for the rich) had increasing debts. This led to an attempt to keep up consumption expenditures by increased private sector debts with collateral based on inflated asset/house values. A loose monetary policy and an inadequately regulated financial sector provided low-doc loans (subprime mortgages) that led to a rapid growth of asset and housing bubbles. At the same time, as the Americans were consuming more than their GDP (dis-saving), they had increasing current account deficits which were being financed by foreign borrowing. The deregulation of the financial sector (repeal of the Glass-Steagall Act) led to unregulated lending which was growing at an enormous rate. The impact of the growth of private and public sector debts made the economy fragile and susceptible to shocks.

The immediate cause (the trigger) of the GFC, most economists would agree, is the collapse in September 2008 of Lehman Brothers, which was not rescued by the American government. The transmission or propagation mechanism of the crisis was the slowing of housing demand that led to a crash in housing prices, the bursting of the financial assets and housing price bubbles (herd behaviour) and defaults and bankruptcies. This was transmitted to the financial sector via the growth of complex financial instruments (e.g. collateralised debt obligations, CDOs and credit default swaps, CDSs) that had been created based on the so-called 'assets' (the subprime mortgages) when the financial institutions suddenly found that their assets were worthless. The inevitable consequence of this downgrading of assets meant than many financial houses were no longer solvent, and the collapse of Lehman Brothers was the final straw that broke the back of the financial industry. The financial collapse has led to a collapse in confidence; banks stopped lending as their portfolios were bereft of assets; there was a huge decline in private sector investment; a fall in consumption expenditures; a big increase in the saving ratios; and a global recession and increasing unemployment and long term unemployment.

What features of the capitalist economies helped to perpetuate the massive increases in asset prices? Was this a consequence of a globalised world? Varoufakis has a lot to say about the underlying causes of the crisis and the propagation mechanism.

The book has two mutually related aims: to explain what caused the Global Crisis and to demonstrate the defects of the dominant neoclassical model that claimed that such a crisis could not occur. Early on the author points out that this crisis is the 'mother of all crises': it spread throughout most of the OECD and also affected many less developed countries. Towards the end of his book, he states, '[C]rises require a failure of coordination between different people and sectors, a collapse in an economy's capacity to collectively utilize its individual resources' (p. 141).

The theme of the book is very well laid out in the introductory chapter. The author provides six explanations for the crisis: (i) a failure to understand risk; (ii) regulatory capture; (iii) irrepressible greed; (iv) cultural origins (Anglo-Celtic beliefs in flexible labour markets, etc.); (v) toxic theory (efficient markets hypothesis, rational expectations, etc.); (vi) systemic failure of capitalism, the role of the USA in financing its debts and deficits from the surpluses of Germany and Japan.

Chapter 2, 'Laboratories of the Future', provides a brief historical account of the development of capitalism *á la* Marx, the role of crises, Goodwin's predator-prey model, and the role of finance in modern capitalism with the ability to create bubbles, and the end of the Gold Standard after the 1929 Great Crash.

Chapter 3, 'The Global Plan', provides a historical account of the Marshall plan to save global capitalism, the breakdown of the Bretton Woods agreement, the ending of the US dollar's convertibility to gold in 1971, and the 'surplus recycling mechanism': the absorption of surpluses created in Japan and Germany by the

USA. Varoufakis argues that the European Union was a clever US plan to bring Europe into the US axis of economic influence. He ignores the view that the EU was meant as a third force: to stand against the USA (a view strongly held by Charles de Gaulle) and as a bulwark against communism.

Chapter 4, 'The Global Minotaur', discusses the role of the USA in the global economy. The author argues that the major flaw in the Bretton Woods agreement (similar to a major flaw in the European Union) was that there was no automatic global surplus recycling mechanism. In the early post war years, the USA recycled its surplus dollars to Japan and Germany (especially) under the Marshall Plan. However, after the end of convertibility of the dollar to gold, the USA had increasing deficits financing wars in Vietnam and South East Asia. Varoufakis argues that the USA persuaded OPEC to raise oil prices (as they are denominated in US dollars) which would increase the demand for US dollars. The rest of the world continued to finance the US deficits as the US dollar was still regarded as a reserve currency (although later the Europeans would have liked to make the Euro the reserve currency). The US economy was expanding, with stagnating real wages and increasing profitability that led to an inflow of foreign capital. The cheap loans that the USA made to Soviet satellites in the 1960s became a burden when interest rates soared under Volcker's regime of high interest rates. This, Varoufakis suggests, led to discontent in the Soviet satellite states that eventually led to the demise of the Soviet Union. This is an interesting twist on the usual interpretation of history.

In Chapter 5, 'The Beast's Handmaidens', Varoufakis argues that the Europeans, Irish, British, and Japanese were in awe of the American 'great moderation' and happily followed US supply-side economic policies. Wall Street, is for Varoufakis, a ringleader of the handmaidens engaged in a roller coaster ride of mergers and take-overs. The development of various 'clever' derivatives (CDOs and CDSs), that were supposed to remove (reduce?) risk from financial markets, expanded at an almost exponential rate. This expansion helped the asset price bubble supported by 'toxic theory' that suggested that markets were efficient and bubbles did not exist. Free markets reigned supreme with the growth of Thatcherite and Reaganite governments. Huge capital flows from Germany, Japan, and China fed the financial booms in Wall Street and supported the twin deficits. In 2005 Paul Volcker had foreseen the impossibility of a never ending increase in debts being funded by foreign capital flows: 'The difficulty is that this seemingly comfortable pattern can't go on forever' (p. 145). Curiously, the author does not discuss the Asian Crisis of 1997 which was a fore-runner to the GFC.

Chapter 6, 'The Crash', provides a blow by blow account of the early stages of the crisis in 2007, the collapse of Bear Stearns, problems faced by BNP Paribas, and the Swiss UBS. In December 2007, President Bush (a free marketeer *par excellence*) intervenes to save house owners from foreclosure and the Federal Reserve (the Fed) steps in providing (almost) unlimited credit to the financial system. By September 2008, Lehman Brothers collapses as the US government refuses to save it. This is often taken to be the start of the GFC. Several European banks and finance houses that held 'toxic assets' are in trouble and the whole western world is in a tailspin, with central banks suddenly doing an about-turn on monetary policy (usually by interest rate management) and no longer targeting inflation. During the crisis, several banks (and car manufacturers) were nationalised but as things got better the banks were denationalised and back in the driving seats! 'In short, socialism died during the Global Minotaur's Golden Age, and capitalism was quietly bumped off the moment the beast ceased to rule over the world economy. In its place we have a new social system: *bankruptocracy* — rule by bankrupted banks ... ' (p. 167).

The financial crisis spread all over the western world with declining GDP and increasing unemployment, and even the developing world found its growth rates slowing down. Tiny little Iceland went through a dramatic crash! European Union countries, especially Portugal, Ireland, Italy, Greece, and Spain (PIIGS), have been experiencing a continuing recession with their banks and financial houses facing bankruptcy, and the existence of the Euro is under continuing threat. The UK disposed of its Labour Government and replaced it with a coalition of the Conservatives and Social Democrats, which imposed austerity measures that have led to a double dip recession. These economic crises have led to political crises, and that is still continuing.

However, Varoufakis does not seem to study the underlying problems of the real US economy: private sector investment had started falling from about 2006, while US house prices had begun to fall from 2005. The fall in private sector investment, through a Keynesian multiplier, would lead to a fall in GDP, while the fall in house prices led to the un-sustainability of the boom in CDOs that were based on subprime loans, which led via herd behaviour to everyone trying to dump these so-called assets, and a collapse in the financial sector. What is interesting is that the home of free markets and private enterprise went into a massive nationalisation program!

Chapter 7, 'The Handmaidens Strike Back', turns to the methods employed by the USA and European Central Bank to attempt to rescue countries in crisis and the banking system. Varoufakis argues that the Geithner-Summers plan of 2009 of creating a simulated market for CDOs was essentially a method of helping the banks to convert toxic assets into 'clean' assets helped by the Fed and the Treasury. He provides a convoluted example of this creative accounting. He then discusses the European Financial Stability Facility (EFSF) that was set up to save the European economies and their banking system: borrowing 440 billion Euros on behalf of the Eurozone to help the insolvent member states. These EFSF bonds would then be lent to countries like Ireland, Greece, etc. However, since the initial problem was caused by the European banks holding toxic assets, this method, he argues, simply transferred the problem to the EFSF. This inevitably results in the next marginal country facing problems as the speculators attack. This system favoured the elites from the financial system and from the military-industrial complex. We have seen in recent days that the problems of Ireland, Portugal, and Greece have spread to Spain, Italy and France. The collapse of the US economy into a recession has meant that it is unable to provide a continuing demand for the output of the other OECD economies.

Chapter 8, 'The Minotaur's Global Legacy', discusses the symbiotic relationship between Japan and the USA. The post-war growth of the Japanese economy was sponsored by the USA, Japanese exports were purchased by the USA, and in return the Japanese recycled their surpluses by investing in the USA. The Japanese boom came to an end with a collapse in the housing and asset price bubbles in the early nineteen-nineties, and it faced a liquidity trap situation. (It is interesting that the Japanese experience of loosening monetary policy for several years did not help the economy to come out of the recession. It apparently did not warn the IMF and other central bankers that simply loosening monetary policy would not cure the underlying problems of the global crisis.) The European Union provided Germany with an expanding market for its exports, leading to current account deficits in the other European countries. This was continued with the introduction of a fixed exchange rate within the European Union by the introduction of the Euro (except for the few countries that refused to join, especially the UK). The US financial crisis spread throughout Europe, but the policies introduced by the European Central Bank failed to stave off disaster for Greece, and now other countries. This, he argues, is because there was no 'surplus recycling mechanism' in the European Union with fixed exchange rates within the Euro countries: the large surpluses of Germany were not being recycled to the remaining members of the EU. His solution to the EU crisis is based on three elements: first, the ECB would assist banks to write off the debts of deficit countries; secondly, the ECB would take on significant amounts of debt financed by Euro Bonds (not individual country bonds); thirdly, the European Investment Bank would invest in the deficit countries. The author does not discuss the necessity of a unified fiscal authority that acts as an equalising agent to help out the poorer states in the Union. The chapter ends with a brief discussion about whether China would be able to save the world by providing an expanding market.

Chapter 9, 'A Future without the Minotaur?' argues that the crucial problem of the world economy is the absence of a 'global surplus recycling mechanism' (GRSM). For some time, the USA managed to have a surplus which it recycled to Japan and Germany (post-World War 2), then when it created large deficits with the wars in South East Asia, it left the gold standard and was being supported by the surpluses of Japan and Germany. But as a result of the crisis the US economy contracted and that affected the German, Japanese and Chinese economies. Can the Chinese economy take over the role of the Global Minotaur (the USA)? His argument is a loud, NO! He favours Keynes's policy prescription in the 1940s of an International Clearing House with its own currency, the Bancor.

The book is a real *tour de force*. It is based on a Marxist conception of underconsumption (or stagnationist hypothesis) that causes a crisis. To avoid the crisis, capitalists seek out markets to prevent an economy from falling into recession. The USA (the Global Minotaur) in the immediate post-WW2 period exports goods to the rest of the world, and its dollar surpluses are recycled in the war-ravaged economies of Japan and Germany. As the US economy grows during the so-called great moderation, wages do not grow in line with productivity, but the rapid growth of credit, thanks to the deregulation of the finance sector, helps to continue growth in domestic demand. The expanding European economies also provide a market for the USA. The expanding Japanese economy becomes an exporter of goods to the rest of the world and it recycles its surplus capital flows into the 'Asian tigers'. As the German economy becomes stronger, it too needs a larger market and it creates the European Union to absorb its exports. But eventually these growing exports create balance of payments surpluses, and there is no mechanism for recycling these surpluses. In this analysis, the author somehow underplays the significant (ironic) role that *communist* China has played in the last decade in funding the *capitalist* US trade and budget deficits by investing its surpluses in the US economy.

It is interesting that the author treats the USA (a political entity) as determining the development of the world economy. In fact what he is presumably arguing is that the finance capitalists (the bankers) were in charge in creating US government policy that favoured them. Was there a coalition of finance and industrial capitalists from the USA and European countries that had re-arranged the deck chairs on the 'Titanic world capitalist enterprise' waiting for the crisis? Is it possible for the world economies to continue on the more-or-less continuous growth of the post-war period in a world where climate change threatens our very existence?

Although the author emphasises the problem of the non-existence of a global surplus recycling mechanism in a world without a global currency, somehow he does not discuss the important role of the *expectations* of players in the international financial markets. Once the US housing market started collapsing with falling house prices, many of the so-called assets of the banking and financial institutions were non-existent. The most exposed to these toxic assets would face bankruptcy, but that simply made other firms vulnerable to attack by financial agents trying to recoup their losses by selling their assets at whatever price they could get. It is a game of 'pass the parcel' and who is going to be left holding the 'toxic' parcel when the music stops? As the weakest in the chain seem to have been countries like Iceland, Ireland, and Greece, their economies have suffered and, as a result, other countries' banks that held bonds from these countries are no longer viable. Once expectations of falling asset prices take hold, everyone tries to sell, and there are no buyers at reasonable prices. Herd behaviour takes over. At present (May 2012) the Greek economy is in tatters, many of the other banks have taken a 'haircut' (or partial default), and the contagion is spreading to Spain, France and Italy. The Euro has been under threat for some months, and it is likely that Greece may eventually leave the Euro, which may lead to other countries following suit. The crisis has a long way to run yet.

What is interesting from a political economy perspective is that the global crisis had led to the collapse of some governments, and some countries are being led by un-elected governments (e.g. Italy), by coalitions formed to introduce 'austerity' measures, and the growth of nationalistic or fascist parties. These austerity measures are being forced on many economies to (supposedly) solve the problem of growing government debts, but will almost certainly lead to double-dip recessions (like the UK) with growing debts with declining GDP. Not only is the world economy facing severe problems, but the political and social structures of many countries are under threat.

Overall, this is a well written and thought provoking book that should be on the reading lists of undergraduate students in Economics, and in Politics. It would also be a good idea for their teachers to read this book.

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China's Changing Workplace: Dynamism, Diversity and Disparity
Edited by Peter Sheldon, Sunghoon Kim, Yiqiong Li and
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The escalating level of workplace changes appears to be a worldwide phenomenon. The reasons are complex, including the speed of globalisation through foreign direct investment (FDI), explosion of information technology, emerging market economies and their outward FDI, and the stumbling economic development in Europe linked with the global financial crisis. This book offers timely and valuable information about a country where workplace changes are unique, unprecedented, and highly relevant to people and organisations both inside and outside of China. The changes are unique because China's workforce is the largest in the world, and the country ranks second only to the USA as FDI recipient in the global economy. It attracts many top multinationals, including Fortune 500 firms. The changes in Chinese workplaces flow from the dramatic nature of the country's economic and institutional reforms since the late 1970s. The most important and influential change is China's conversion from a planned economy to a market-oriented economy. The marketisation (*shichanghua*) process represents a wholesale change beyond economics, encompassing social values, social structures and workplace-related legislation and practice. Such changes are highly relevant to both the domestic Chinese workforce and to foreign investors, who need to understand the sweeping changes in order to manage the local workforce to build competitiveness. The changes are also relevant to foreign workforces, as China is now the largest outward FDI economy among all developing countries. Given that, workplaces in foreign countries will see more Chinese employers and managers, with managerial policies and practices of Chinese firms abroad inevitably influenced by the changing workplace at home.