

Review of Robert Brenner's **The Economics of Global Turbulence**

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Robert Brenner's new book The Economics of Global Turbulence is a provocative and extraordinarily ambitious reinterpretation of post World War II global economic history. Brenner's goal is to replace the conventional wisdom about the causes of the rise and fall of the "Golden Age" of global economic development from the end of World War II through the early 1970s, and the generation-long period of instability and low growth that followed, with an innovative theory of his own. He argues that explanations of both the origin of the crisis and its long-term reproduction offered by, for example, traditional Marxist theory and Social Structure of Accumulation (or SSA) theory are almost totally without merit. He proposes instead an explanation that puts the blame for the problems of the past three decades squarely and exclusively on the shoulders of destructive inter-nation trade struggles, especially among the US, Germany and Japan. The unique merit of his approach, he claims, is that it alone can explain why the crisis that began in the late 1960s has yet to end.

The main target of his criticism is what he calls "supply-side" crisis theory. Brenner directs his fire primarily at theories in which capital-labor conflict plays a key role in crisis creation or reproduction. Thus, the real villain in his story is Marx's theory of the Reserve Army of unemployed (or RA theory), one of the key building blocks of SSA theory. I will consider in turn Brenner's analysis of the origin of the crisis in the late 1960s, then his explanation of its longevity.

According to Brenner, the rate of profit is the main determinant of the rate of investment,

and investment is the primary engine of both aggregate demand and productivity growth. Thus, the event which sparked the global crisis was the dramatic fall in the US manufacturing rate of profit between 1965 and 1973, a decline of some 40% as measured by a data series constructed by Andrew Glyn. In that period the world “was suddenly projected from boom to crisis” (93). And the reason why the global crisis did not end in the 1970s is that the profit rate failed to rebound after 1973; the US manufacturing profit rate fell precipitously again in 1974, and remained at a very low level into the mid 1990s: “To explain the origins and evolution of the long downturn through an analysis of the causes and effects of changes in profitability is thus the objective of this study” (8).

Brenner is severely critical of the explanation of the decline in US corporate profitability offered by SSA theorists Bowles, Gordon and Weisskopf in After the Wasteland (Sharpe, 1990). In their view, the fall in the profit rate had four main causes: (1) an erosion of American geopolitical power, and thus a decline in the ability of the US government to control world events and manipulate terms of trade in the interests of its large corporations; (2) a squeeze on profits that resulted from the rise in labor militance brought on by low unemployment after 1964; (3) constraints on the power of capital created by the widening post war social safety net and active use of macro policy to limit unemployment; and (4) an intensification of inter-capitalist competition in the 1960s -- reflected both in the erosion of oligopoly pricing power within US industries and in increased trade competition from rivals such as Japan and Germany. Components 2 and 3 constitute an institutionally enriched RA theory.

Now Brenner might have argued that SSA theories focus too narrowly on costs at the expense of concern with demand constraints and competitive pressure. Instead, he adopts the

more aggressive, high-risk strategy of dismissing supply-side theories as devoid of explanatory power. In the end, Brenner's more aggressive strategy does not succeed. The unfortunate aspect of its failure is that it diverts the reader's attention from the important contribution to our understanding of post war economic development that Brenner does provide, through his emphasis on the centrality of rising international competition.

The simple RA theory of the profit "squeeze" is as follows. Consider a firm whose profits arise from the ability to set output price by marking-up unit labor costs -- total wages divided by the quantity of output. Assume for simplicity that wages are the sole cost of doing business. The profit share will then be given by the size of the mark-up (as a percent of unit cost), with the profit rate determined as the product of the profit share and the output to capital ratio (which reflects the technology of production and the degree of capacity utilization). By construction then, a necessary and sufficient condition for an end-of-expansion profit share "squeeze" is that the mark up fall: the ratio of output price to unit labor cost must decline. As a matter of simple logic, RA theories cannot be purely "supply-side" because they must offer an explanation of why demand constraints prevent firms from maintaining their mark up in the late expansion by raising prices at the same pace as unit labor costs.

RA theory assumes that both the willingness of workers and unions to struggle with firms over wages and working conditions, and their power to influence the outcome of such struggles depend on their sense of job security. In periods of high unemployment, workers fear of joblessness renders them powerless to prevent capital from constraining wage growth, and raising productivity by accelerating the pace of work. Thus, in the early to mid expansion period, capital is able to raise the profit share of income at labor's expense. But when unemployment has

been low enough long enough for workers to become confident that they can retain their jobs, or get equally good jobs in other firms, they fight back, causing real wages to rise and productivity growth to fall, thereby boosting unit labor costs. Unless firms can raise prices enough to maintain the mark up, profits get “squeezed”.

Brenner does acknowledge a “prima facie basis” for the argument that RA dynamics help explain the onset of the crisis. Unemployment rates in the mid-late 1960s were exceptionally low, and the period did see a huge outbreak of labor militance as evidenced by “a major increase in strike activity” from 1963-69 (96). But, he argues, when joblessness was declining from 1958 through 1965, the profit rate rose substantially, while from 1965-69, when the profit rate experienced 80% of its total 1965-73 drop, the unemployment rate fell only from 3.8% to 3.5%: “it is difficult to see how such a small decline could have played a major role in the substantial fall in profitability that began in those years” (97). However, the idea that worker militance is solely a function of the rate of decline of unemployment, and unrelated to the level of unemployment, lacks all credibility. If this were true, we would expect to see constant labor costs even if the unemployment rate were to hold steady at 2% forever!

He also sees the upsurge in strikes as purely “defensive,” a “lagging response on the part of labor” to capital’s onslaught between 1958 and 1965, not an “autonomous” outbreak of offensive labor militance. But this is, more or less, what RA theory argues. Tight labor markets after the mid expansion create conditions in which labor regains enough strength -- call it “defensive” if you like -- to win back the income share taken from it by capital in the recession and early expansion, when labor was weakest.

In addition, Brenner notes that the profit share in non-manufacturing suffered a much

smaller decline than in manufacturing. Because much of manufacturing faced increased foreign competition, while non-manufacturing did not, the effect of increased foreign competition on the mark up after 1965 must have been the primary cause of the drop in manufacturing profitability, he argues. But his data show that the non-manufacturing profit rate exhibited little cyclical volatility over the post war period. Since, unlike the case with manufacturing, the non-manufacturing profit rate rose very little from 1961 to 1965, it is hardly surprising that it did not decline much in the late expansion and recession.

However, Brenner's dismissal of the relevance of supply-side theories of the falling profit rate after 1965 stands or falls on his argument that the RA thesis is incompatible with the relevant data. Real wage growth slowed in the sixties, he writes, while "annual labour productivity growth actually increased during the period of profitability decline" from 1965 through 1973 (98). Since labor's share of income, *ceteris paribus*, rises with an increase in the real wage and falls when labor productivity rises, he concludes that the decline in the profit share cannot possibly "be attributed to pressure from labour on wages or productivity". The "fall of profitability in manufacturing was the result, not of an increase in upward pressure on costs, but an increase in the downward pressure on prices" brought on by heightened trade competition. Since it is his position that the rate of growth of labor costs didn't rise, the decline in the profit share cannot "be attributed to pressure from labour on wages or productivity" (102).

Unfortunately, Brenner's treatment of 1965-73 as a single, uniform, cycle phase makes it difficult for the reader to evaluate his empirical evidence. This period does not correspond to any time segment in RA theory; rather, it mixes parts of two cycles together, then ends in the year that the first OPEC oil price hike began to reverberate through the US economy. Still, a careful

examination of the data for the long economic expansion from 1961 through 1969 shows that Brenner's central conclusion is mistaken. The theoretical challenge here is to explain why the manufacturing profit rate fell in half from the cycle peak in 1965 through the recession year of 1970. (It actually rose slightly in the 1971-73 expansion under Nixon's's wage-price controls.)

Brenner is correct that manufacturing labor productivity did grow at a fast pace on average during the 1960s and early 1970s. But it slowed substantially from mid 1964 through mid 1966, just when the profit rate stopped rising and began its long-term fall, and again in 1968 and 1969, helping bring about the end of the expansion. Indeed, in the crucial period from 1965 through 1969, when the manufacturing profit rate fell by some 33%, labor productivity growth dropped to 2.4% from the 3.5% of the previous four years. To see if Brenner is right about the absence of cost-push in this period, we need to look at unit labor costs, which combine wage and productivity movements. From 1960 through 1965, manufacturing unit labor costs were virtually constant, but from late 1965 through the end of 1967, after full employment was reached, they began to rise at about 1.7% per year; from this point through the last quarter of 1969, unit labor costs rose almost 6% per year. They levelled off again from mid 1970 through mid 1972, after the long boom of the sixties ended. Contrary to Brenner's assertion, then, there was indeed an upward pressure on labor costs that threatened profitability. We reach the same conclusion if we move from manufacturing to the standard NBER national cycle data: after remaining fairly constant from the late 1950s through 1966, unit labor costs and labor's share of income rose substantially for the next five years.

It seems that Brenner's dogged insistence that workers are merely passive spectators in the dynamics of the capital accumulation process led him badly astray. US manufacturing (and

other) firms were indeed confronted with rapidly rising unit labor costs in the second half of the sixties expansion. Unless they could raise prices at the same accelerating pace as unit labor costs, a classic RA-induced squeeze of the mark up and profit share was inevitable. But, as the data show, they were unable to do so. Unit labor costs raced ahead of prices, creating a fall in the profit share in both manufacturing and in the private economy as a whole.

Brenner would have been on more solid ground if he had limited his attack on “supply-side” theories to their failure to sufficiently emphasize and explore the reasons why demand failed to grow fast enough at the end of the 1960s to permit mark up preserving price increases. It is not that the demand side of the argument has been totally neglected by RA-based arguments; Brenner’s “supply side” label is misleading if it is meant to indicate the complete absence of demand analysis. For example, the theory of the “political business cycle” presented by Boddy and Crotty in the mid 1970s emphasized the role played by restrictive monetary and fiscal policy in creating the end-of-expansion slowdown in the growth of aggregate demand that helped squeeze profits. After the Wasteland posits the erosion of oligopoly pricing power, due in part to an increase in trade competition, as one of the four reasons why the US profit rate fell in this period -- a fact Brenner fails to mention. Other sources of demand restraint have been mentioned in the literature -- rising interest rates as the growing demand for credit out paces its supply, a slowdown in investment growth as a result of the buildup in the capital stock and the decline of profit rates toward the end of expansions, and the decline in the trade balance near boom’s end caused by rising inflation and faster income growth. But since this literature is relatively weak in the area of demand analysis, Brenner’s stress on the effect of rising international competition on the mark up in manufacturing after 1965 can help create a better balance between supply and

demand elements of the story.

Having dismissed “supply-side” explanations of onset of profit problems in 1965-73, Brenner has prepared the way for an alternative interpretation of both the origin and the reproduction of the crisis, one based on the unplanned nature of capitalism and the anarchy of competition. Since all firms must invest without knowledge of the effect of investment on aggregate or industry demand, “realization [or demand] problems cannot be assumed away” (24). “In the real world of economic competition, individual capitalists can neither control nor predict the market...; investments yield profits only after the fact, once they have proved themselves in a potentially destructive competition” (25). Integrating Keynesian ideas about uncertainty with a Marx-inspired view of anarchic competition, Brenner attempts to build a crisis theory which connects the supply problems that cause over- and under-investment to the demand problems this investment cycle generates.

In capitalism, firms are always searching for ways to cut costs and increase market share. In stable and prosperous periods, there are often well established firms that dominate industries through superior capital-embodied technology and organizational capacity. These firms can protect attractive industry profit rates through the prevention of entry because, Brenner writes, existing capital is illiquid, “sunk,” or irreversible: once in place, many capital goods cannot be resold, except at a substantial loss. Fixed capital therefore costs the firms nothing. Whereas new entrants must earn a satisfactory profit rate on both fixed and circulating capital, established firms need only earn this rate on circulating capital. New firms hesitate to enter because established firms can survive a competitive struggle in which industry price falls well below the level needed to make entry attractive.

The illiquid nature of real capital also makes the disequilibrium dynamics of contested markets unruly. If the technical advantage of new capital over old becomes large enough, new firms will enter the market. This will cause falling prices, over-investment and excess capacity, and falling average industry profit rates, triggering the onset of crisis. But, Brenner insists, many old firms will refuse to exit without a protracted struggle for survival. “They have ... through long years of operation in their lines, accumulated otherwise unattainable information about markets, favourable relationships with suppliers and purchasers, and above all technical know-how which together constitute perhaps their greatest asset” (33). Because both this “intangible” capital and the firm’s fixed capital “can only be realized in their established lines of production,” entrenched firms will fight to remain in the industry, not just by cutting wages and other variable costs, but by undertaking new investments with even better technology than their new competitors possess. Given the development of complex financial intermediation, both new and old firms respond to the dangers of this struggle “by taking out loans so as to be able to increase investment in the hope of improving competitiveness, or just to hold on in the hope the market will improve” (34).

The chain of events thus moves from an initial period of protected markets and high profits, to attempted entry through investment by new firms, to a struggle to survive fought in part through yet more cost-cutting investment, to a prolonged period of excess capacity and low profit rates caused by this over-investment. This initial crisis period can last for some time, but it cannot go on forever. At some point in the process, over-investment must give way to in a collapse of the capital accumulation process. Since aggregate demand depends heavily on investment, it too will slow down. Already low, the profit rate will be further reduced by the

effects of falling demand and declining capacity utilization. Moreover, the investment slowdown will reduce the growth rate of the capital/labor ratio, and thus lower the rate of productivity growth. As a result, the industry/economy sinks into a period of stagnation or depression that cannot end until the destruction of the least efficient firms and technologies, and the debt commitments that financed them, raises the profit rate once again.

Brenner first applies his theory to the origin of the crisis. World trade, though relatively small in the period immediately following World War II, was dominated by the US. But after the mid 1960s, as “the growth of trade accelerated spectacularly and unexpectedly”(36), US manufacturers found themselves under severe attack from the “lower cost, lower price” exports of Germany and Japan. “As a consequence of the resulting downward pressure on prices” these imports created, the US manufacturing profit rate fell dramatically. Just as in the theory of anarchic competition just described, the entry of new trading blocs into US markets, after a long period in which these markets had been protected both by trade barriers and the dominance of US technology and productivity, caused a crisis of profitability for US producers. According to Brenner, this is **the** origin of the 1965-73 profit crisis.

But there are serious problems with this explanation of the onset of crisis. First, the decline in the US manufacturing trade balance in these years, taken by itself, is simply too small to explain the 50 percent decline in the profit rate in the period. According to Brenner’s Table 10, the combined US trade balance with Germany and Japan fell from plus \$0.2 billion to minus \$2.1 billion between 1965 and 1969 -- the years in which the profit rate suffered the lion’s share of its 1965-73 decline. But this shift of \$2.3 billion is less than one percent of US manufacturing output in 1969, and thus cannot possibly bear the explanatory burden Brenner is forced, by his

dismissal of cost problems, to place upon it. Second, the erosion of the US trade deficit can be largely explained by factors other than changes in the labor cost of German and Japanese exports -- rising inflation, faster income growth here than abroad, and the over valuation of the US dollar. Third, downward pressure on output price in this period came not just from increased trade competition, but from a shift to restrictive macro policy in 1968. Real interest rates rose, while the cyclically adjusted federal budget deficit fell by over 3% of GDP between 1968 and 1969. Finally, the end of the 1965-73 period saw a number of system shaking events that affected US profitability, including the collapse of the Bretton Woods fixed exchange-rate system, the imposition of wage-price controls, and the first wave of global inflation triggered by a tripling of oil prices in 1973.

Though of limited use in explaining the onset of the global crisis, Brenner's analysis of the disequilibrium dynamics of hotly contested, capital intensive markets is first rate, and represents a major contribution to our understanding of its long duration. Nevertheless, his theory of capitalist competition could be improved. First, it should be emphasized, as in the work of Marx and Hyman Minsky, that since investment is often debt financed, crisis will ensue unless profits are large enough to enable the firm to meet its interest and principal repayment obligations. It is therefore misleading for Brenner to suggest that even zero profit on capital in place is sufficient to keep established firms in business. Moreover, the incorporation of finance into the argument adds yet another destructive dimension to competition. Investment undertaken in a low profit period creates rising leverage, and thus increased financial fragility -- which helps prolong the crisis. This is a central element in the story of the post 1980 accumulation process. Second, the concept of uncertainty should play an even more central theoretical role: it helps

explain why sensible firms invest under conditions of low current profits and excess industry capacity. No one knows which firms will survive long enough to take advantage of the high profit rates that are expected to prevail once the losers are driven out of the industry. Third, the theory should be applied to intra- as well as inter-nation competition. For example, one reason why the Japanese economic “model” was so successful for so long was because its institutions and policies kept the destructive forces of domestic competition under control. Last, but hardly least, Brenner never presents a clear explanation of the timing of the transition from over to under-investment. Confusion over, and even contradictory statements about, which phase of the crisis we are in at any particular time plagues the book.

Brenner’s application of the theory of international competition to the issue of crisis longevity proceeds along the following lines. Why did the global economy not experience a normal cyclical upturn in the 1970s? The devaluation of the US dollar in the early 1970s restored US cost competitiveness, shifting the profit crisis to Germany and Japan. But instead of stimulating exit from the affected industries, trade oriented firms in these countries increased their pace of investment in cost cutting technology. In line with Brenner’s theory, US manufacturing then “sought to improve their profitability and competitiveness by launching a powerful wave of investment during the 1970s and radically reducing the growth of wage costs”. Germany and Japan in turn “intensified their competitive warfare, exacerbating over-capacity and over-production, with highly destructive consequences” (37). No one was willing to surrender in this global cost-cutting war. The emergence of East Asia as a major force in international trade in the 1980s only exacerbated the problems of over-investment and over-capacity in world manufacturing, “helping to prevent the recovery of profitability, and to

perpetuate the downturn through the 1980s and into the 1990s” (37). The wealth of institutional and empirical evidence about national and firm-level export strategies presented by Brenner in support of his story of relentless battles fought in pursuit of global trade superiority constitutes one of the real strengths of the book.

As the crisis unfolded, employers everywhere tried to shift the burden of the crisis onto workers, through attacks in the workplace, changes in labor law, and austerity macro policy. They “realized their goals to a significant degree, achieving an ever greater shift in the balance of class power” (137). Why didn’t this victory restore profitability? Here Brenner’s argument appears to be inconsistent. After emphasizing the “powerful wave of investment during the 1970s,” he now invokes under-investment in the 1970s to explain the low profit rate: low investment reduced productivity growth, and thus profits. As noted above, this confusion is caused by a lack of theoretical and historical clarity about the dynamics and timing of the transition from the over- to the under-investment phase of the long-term crisis.

Brenner argues that only a depression deep and long enough to destroy most inefficient plant and excessive debt would be capable of fully restoring the global profit rate. There were short-lived episodes of austerity macro policy in the 1970s, but the problems these created for both capital and labor quickly led governments to reverse course: this “prevented the shakeout of high-cost, low profit firms, especially in manufacturing, that was requisite to the recovery of aggregate profitability” (37). The more severe policy austerity of the 1980s “did accelerate the destruction of redundant capital, especially in manufacturing,” but since it simultaneously kept aggregate demand and capacity utilization rates low, it never stimulated a new long wave of productivity-enhancing investment. This idea is quite similar to the argument presented in After

the Wasteland that the 1980s “cold bath” strategy of austerity macro policy was contradictory: while it did create lower labor costs, it also raised excess capacity and thus led to continued low investment.

Brenner thus presents a vision of a global economy stuck in low gear because of incessant cost-cutting investment by manufacturers forced to compete for survival in world trade. Destructive competition creates and perpetuates over-production and over-capacity, and thus profit rate problems. Low profits and excess capacity in turn prevent the takeoff of the demand-creating, productive-enhancing investment needed to restore long-run growth. This impediment to the restoration of profitability cannot be overcome by Keynesian aggregate demand manipulation. He argues, moreover, that there are no defensible alternatives to his approach to solving the longevity puzzle. RA-based arguments, like those used by SSA theorists, can in principle explain lower profits in the short run, but they are inherently incapable of explaining a long-term crisis because, given time, capital can recreate unemployment and weaken labor by cutting investment, investing in labor-saving technical change, moving production to areas where labor is weak, and using increased immigration to create an excess labor supply.

However, as was the case with his treatment of the origins of the global crisis, Brenner is too quick to dismiss “supply-side” contributions to the explanation of longevity. For example, it is true, as Brenner claims, that the labor movement in the US was too weak to be a direct impediment to the restoration of profitability in the mid-late 1980s and 1990s. But this was not the case in the 1970s; it took the Great Recession of the early 1980s, and the declaration of economic war against labor by capital and the state in this period, to bring labor to heel. (Indeed,

Brenner fails to sufficiently emphasize the qualitative shift in strategy undertaken by capital and the state in the late 1970s and early 1980s -- the period in which global Neoliberalism first rose to prominence.) The failure of capital to cut wages or slash the social safety net in the US in the 1970s is one reason why the decade saw no rise in the profit share or rate. And, of course, labor was much stronger in Europe than in the US.

Ironically, Brenner's theory of destructive competition could be used to complement and strengthen, rather than replace, SSA-type theories of longevity. Assume for the sake of argument that the onset of the crisis occurred just the way SSA theorists said it did. The failure of the profit rate to recover in the 1970s could be explained by the collapse of the Bretton Woods system and the outbreak of exchange rate instability this generated, the burst of global inflation triggered by the two OPEC price hikes, austerity macro policies undertaken in response to inflation, labor's remaining defensive strength, the debt crisis -- and the uncertainty all this created. If Brenner's insights into the nature of competition are essentially correct, as I believe they are, major manufacturing companies around the world, especially those tightly integrated in world trade, should have reacted to this era of declining profits and rising uncertainty more or less the way Brenner suggests. That is, a destructive phase of capitalist competition will be ignited by a long, deep drop in the profit rate, **no matter what its origin** -- an RA-based profit squeeze, excessive trade competition, or anything else.

The key point is this: the incorporation of Brenner's theory of destructive competition into RA-based explanations of the long-term nature of the present global crisis significantly enhances their explanatory power. One does not have to buy into Brenner's claim that excessive competition explains everything and "supply-side" theories explain nothing to appreciate the

contribution that the theory of capitalist competition can make to our understanding of the global crisis of the past thirty years. Those of us who, unlike Brenner, believe that the ongoing global crisis is best understood as the outcome of the complex interaction of a number of different contradictions in the accumulation process -- including the dynamics of capital-labor conflict -- can enrich our understanding through the insights Brenner has given us on the unplanned and anarchic nature of capitalist competition.