Pathways of Financialization in Africa

Professor Sarah Bracking

19th February 2019

https://youtu.be/Ndzu1sjV_f8

Objectives

Premises

- Structural adjustment laid the foundation for informalization and criminalisation at all scales
- Many assets now vertically linked to offshore spaces and opportunities for corruption
- global processes of Financialization are linked to national and local processes of accumulation through dispossession and displacement (Harvey)

Ongoing struggles

- a 'Financialization of power' process acts to repurpose political systems to service this extractive Financialization
- Leads to corruption and state capture at national scale and illicit financial flows
- New forms of private sector corruption are also part of this repurposing

Solutions

- Contributory system of tax
- Mandated national domicile

the garbage

May 2005 - Killarney in Bulawayo: burnt out and homeless
http://www.solidaritypeacetrust.org/image-gallery/?album=14&gallery=31

1. From SAPs to financialization

SAPs: the pursuit of 'openness' and 'free markets' did not lead to economic deregulation *per se*, but to the construction of regulating institutions which privileged the preferences of capital-holders over others

while neoliberal economic orthodoxy advocated less intervention in markets, policy in practice lead to more, and of a different type: interventions did not reduce, but changed in type under neoliberal processes.

the regime in which the Bretton Woods Institutions were central to international lending weakened and with it the power to dictate macro-economic policy. New lenders, such as China, India, Russia and Brazil emerged: some African states with natural minerals and oil reserves were able to reduce debt, dependency and their need for public lending.

However, the paradigm change in the political economy of development which SAPs ushered in is largely intact and resilient, despite the global financial crash of 2008.

Very few countries seek to regulate capital flows or use Keynesian techniques to increase money supply – the quantitative easing of the US and European countries 2008-2014 notwithstanding.

Two main pathways to financialization: collapse and crisis; 'business-as-normal'

1.1 Crisis and informality

- Economic informality and inflation grows during political crisis (cf Zimbabwe, Congo, Cameroon, Sierra Leone, Somalia)
- This is not only chaotic, but organised for survival and accumulation, “instrumentalisation of disorder” (Chabal and Daloz, 1999)

Zimbabwe

- Bulawayo’s ‘World Bank’ on Fort Street; cross border traders
  - Is not only horizontal but vertical or ‘gangster’ (Mawowa and Matonga, 2010, 323)
- ‘Roadside currency trade linked to illicit diamond and smuggling, US$800 million and US $400 million respectively in 2007 alone (Mawowa and Matongo, 2010, 321, citing Gono, 2007, 5-6)
- Patriotic nationalism lead to Murambatsvina (2005) and Industrial Chimurenga (2001 -); deliberate displacement of people, and destruction or seizure of assets and businesses (Bracking, 2005)
- Export of wealth by Politically Exposed Persons (PEPs) and High Net Worth Individuals (HNWIs)
- ‘Accumulation by dispossession’ (Harvey,2005)
- Political crisis (and peoples displacement and dispossession) generates financial displacement and wealth migration

1.2 Political economy of displacement: business as normal

- So, where did the money go?
- Into the ‘normal’ economy, which is actually well suited to accommodate this process of dispossession and financial displacement
- Violence, theft, economic fraud and corruption assist in this process
- There are also key industrial strategies that shape this process, some more legal than others, which include
  - thin capitalisation
  - inverted company structures
  - transfer pricing
  - multiple accounts, offshore accounts, offshore record keeping
  - re-domicile in a booking centre or tax haven

- Illicit financial flows are a consequence of Financialization
- The offshore economy is a facilitator of financialization

Illicit financial flows are a consequence of Financialization

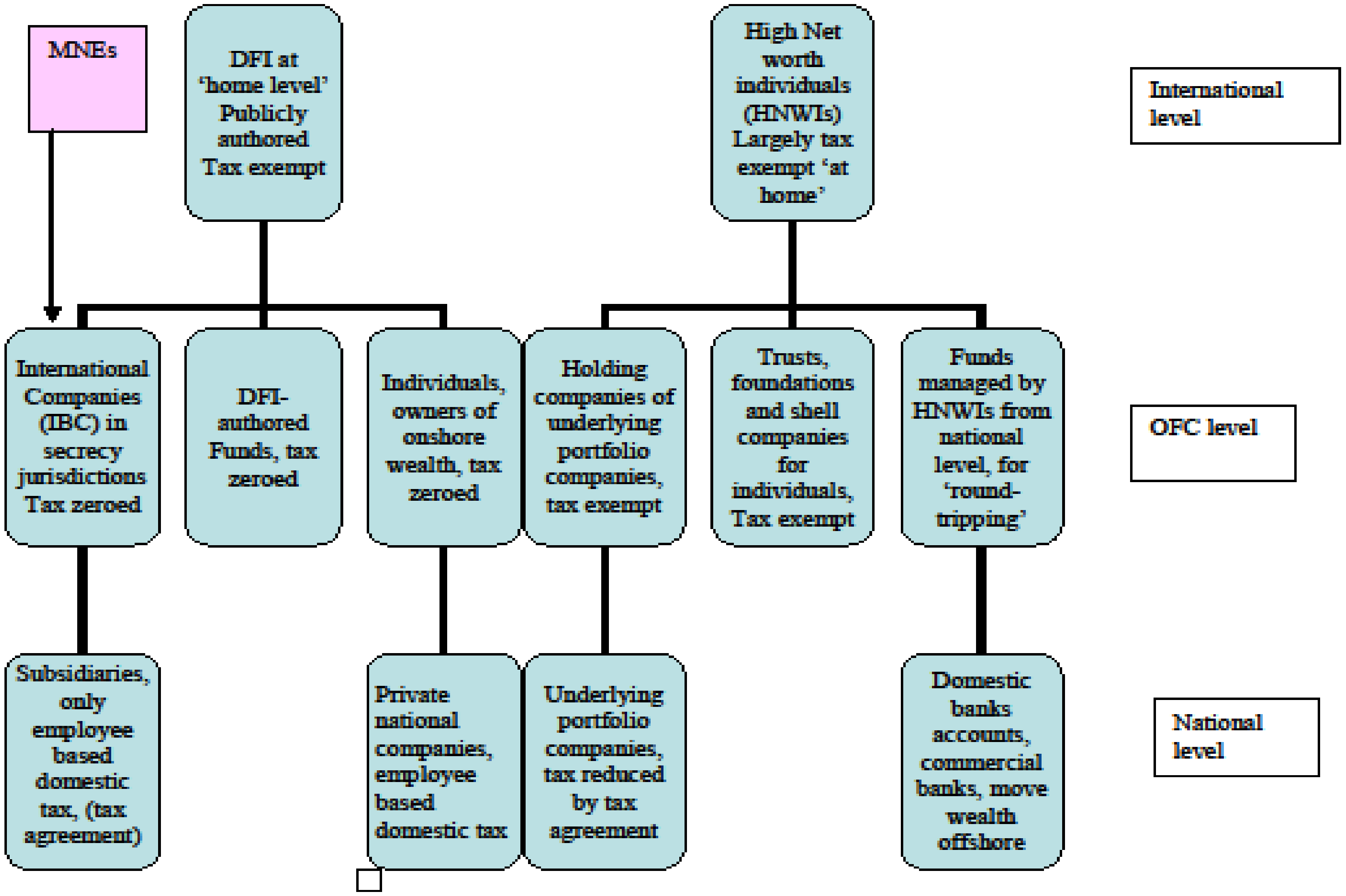
- sub-Saharan Africa lost more than $528 billion from 2002-2013 due to corporate ‘trade mis-invoicing’ (GFI, 2013).
- This is almost double the foreign direct investment inflows to Africa during the same period - $284 billion.
- 60- 65 % of Africa’s illicit flows are commercially originated and 5% are generated in acts of political corruption (GFI, 2014).

Appendix Table III-1. DOTS-based Estimates of Potential Trade Misinvoicing by Country, 2015 (cont.)

(Percent of total developing country trade with advanced economies unless noted)

Country	Potential Import Misinvoicing		Potential Export Misinvoicing		Inflows (b)+(c)	Outflows (a)+(d)	Total trade with advanced countries (millions of US $)	Inflows [(b)+(c)] (millions of US $)	Outflows [(a)+(d)] (millions of US $)
	Over-Invoicing (a)	Under-Invoicing (b)	Over-Invoicing (c)	Under-Invoicing (d)					
Costa Rica	3.8	2.5	0.1	11.3	2.7	15.1	15,275	409	2,299
Croatia	2.2	4.9	7.1	1.5	12.1	3.7	21,351	2,583	800
Djibouti	27.1	69.6	0.4	4.8	70.0	31.9	518	363	165
Dominica	0.4	97.4	0.0	1.0	97.4	1.4	261	254	4
Dominican Republic	4.6	0.7	0.9	2.9	1.6	7.5	16,040	258	1,208
Ecuador	2.8	3.2	2.3	4.2	5.5	7.0	20,587	1,133	1,442
Egypt	9.5	15.0	2.0	7.7	17.0	17.2	39,623	6,717	6,833
El Salvador	11.8	1.0	2.5	2.4	3.4	14.2	7,547	260	1,071
Equatorial Guinea	0.0	0.0	0.0	0.0	0.0	0.0	5,195	0	0
Eritrea	25.1	11.0	1.2	15.2	12.2	40.3	135	16	54
Eswatini, Kingdom of	20.3	16.7	29.6	28.4	46.2	48.7	211	98	103
Ethiopia	15.5	27.0	8.1	2.5	35.1	18.1	5,505	1,930	994
Fiji	17.8	18.6	0.8	4.4	19.4	22.2	1,894	367	421
Gabon	5.2	2.7	20.4	13.0	23.1	18.2	4,985	1,151	908
Gambia, The	10.6	53.6	0.0	9.5	53.7	20.1	183	98	37
Georgia	19.4	9.1	1.7	7.8	10.7	27.2	3,086	331	841
Ghana	8.4	8.0	1.3	17.9	9.3	26.3	9,019	837	2,372

The offshore economy is a facilitator of Financialization



Deliberate bankruptcy	**Practices in which the owners and/or managers of a company knowingly take excessive remuneration, strip the firm's assets, or otherwise conduct corporate affairs for short-term private gain at the expense of the firm's continued operational viability. This sometimes also occurs in the context of avoiding future financial obligations of the operating entity, such as pension funds.**
Illicit financial flows	"Money that is illegally earned, transferred, or utilized" (Kar and Cartwright-Smith 2007, iv). This concept incorporates the related category of illegal capital flight (but not legal capital flight), where flows are specifically in violation of laws and regulations. According to Global Financial Integrity, it does not currently include the proceeds of criminal smuggling, trade mispricing, or mispriced asset swaps, which are not direct money flows (see Kar and Cartwright-Smith 2007, iii–iv; ADB and GFI 2013, 1).
Jurisdiction shopping	In the corporate context, the active selection of a particular jurisdiction in which to domicile part or all of an economic entity away from its material operations in order to avoid or evade tax (see Palan 2002, 172). This often involves the fictional fragmentation of a firm into a complex and opaque set of distinct legal entities located in different jurisdictions.
Tax evasion	Criminal nonpayment of tax. Tax avoidance is a related practice that also leads to nonpayment but is technically legal.
Thin capitalization	Underinvestment of a domestic company relative to its offshore parent in order to evade or avoid tax. It is often accompanied by an inverted company structure in which the bulk of the assets are kept offshore, with an onshore shell (see Heggstad and Fjeldstad 2010). This is an established term, and some countries have "thin-cap" regulations.
Trade mispricing	Abuse of pricing in trade between apparently unrelated parties, such as through the deliberate overinvoicing of imports or underinvoicing of exports, usually for the purpose of tax evasion.
Transfer pricing	"A transfer price is a price, adopted for book-keeping purposes, which is used to value transactions between affiliated enterprises integrated under the same management at artificially high or low levels in order to effect an unspecified income payment or capital transfer between those enterprises" (OECD 2001). Transfer pricing is "not, in itself, illegal or necessarily abusive" in all definitions (Tax Justice Network 2013), but here we will assume a mispricing element.

2. Financialisation: 4 schools

1) financialisation of capitalism itself, whereby:

- “more of the economy is deemed to consist of finance, and more of the wealth it circulates is deemed to be generated through finance” (Christophers, 2012: 273).
- a “shift in the creation of value to a relatively autonomous and increasingly dominant financial sphere” (Labban, 2010, 545).
- Finance act as frontier, accumulation by dispossession (Harvey); the ‘Four Cheaps’ (O’Connor)
- dates back to Arrighi’s seminal *The Long Twentieth Century* (1994), and was picked up in the work of Stockhammer (2004) and Krippner (2005).

2) increased influence of financial concepts, languages and evaluative practises in everyday life (Christophers, 2012: 273; Martin, 2002; Langley 2007, 2008).

3) ‘shareholder value’ has increased influence in the business world (Froud, et al, 2000; Lazonick and O’Sullivan, 2000; Peters, 2011).

4) A technical definition: an asset is financialized when it is used to create a derivate income stream which circulates as liquid value (Hildyard, 2016, Bracking, 2016)

2.1 Mainstream account

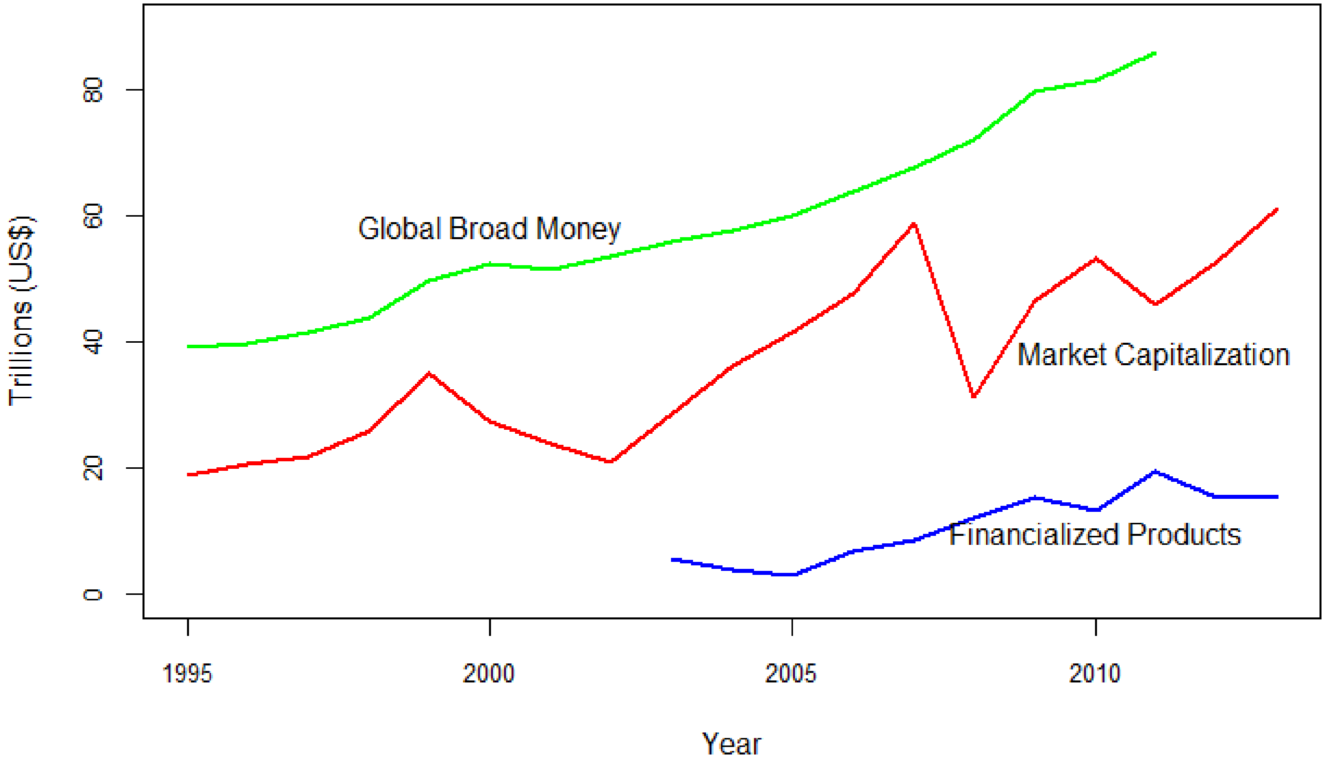
financialisation refers to:

1) the depth and spread of financial markets
2) combined with new innovative and complex financial instruments, including a spectacular range of short term and abstracted derivatives and futures products (see Hildyard, 2008)
3) accompanied by a growth in all types of debt finance at the global, national, firm, household and individual level
4) the consequent dominance of financial over productive capital (Castree, 2009: 189; Stockhammer, 2010)

2.2 Problems:

- *empirical evidence remains weak and contested*
  - for ‘such a shibboleth of contemporary scholarship” evidence remains “remarkably and curiously thin” (Christophers, 2012: 272).
- many definitions refer as much to the *consequences* of the greater dominance of finance, than to the causes of, or processes of the same.
- there is a problem of *scale* and the space and place at which change is supposed to extrapolate and signify global or structural change.

2.3 Empirical test: global scale



2.4 Financialisation?

- Yes, at a global scale value stored as money growing relative to value in production
- Irving Fisher in the neoclassical school in 1907: "The orchard produces the apples; but the value of the apples produces the value of the orchard…We see, then, that present capital-*wealth* produces future income-*services*, but future income-*value* produces present capital-*value*" (Fisher, 1907, 13-14, original emphasis)
- Financialization as process acts to create a fixed asset from which one or more legally contracted derivative income streams can be drawn
- *Its all about class power – using money!*

2.5 Financialisation manages space and time

- financialisation affects the past in that the historical accumulation of capital is financialised and mortgaged in a copyright, royalty and intellectual property regime
- the future 2) is also financialised in debt repayment schedules, and even collaterisised and securitised
- 3) financialisation can make an asset or conjurer it to existence in the present.
- 4) accumulation can progress with only a fictive or virtual asset in any of the past, present or future.

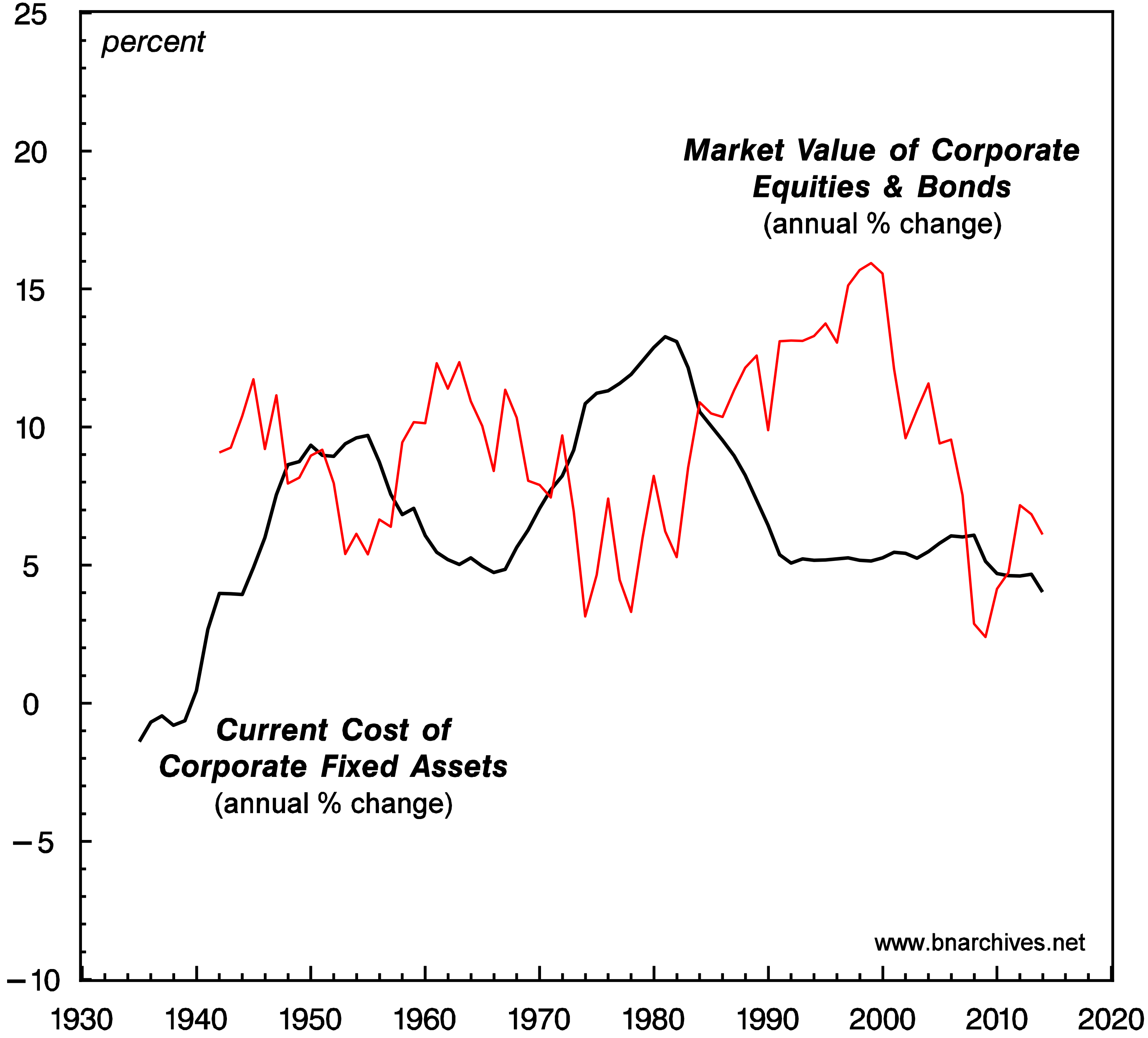
To generate rents…



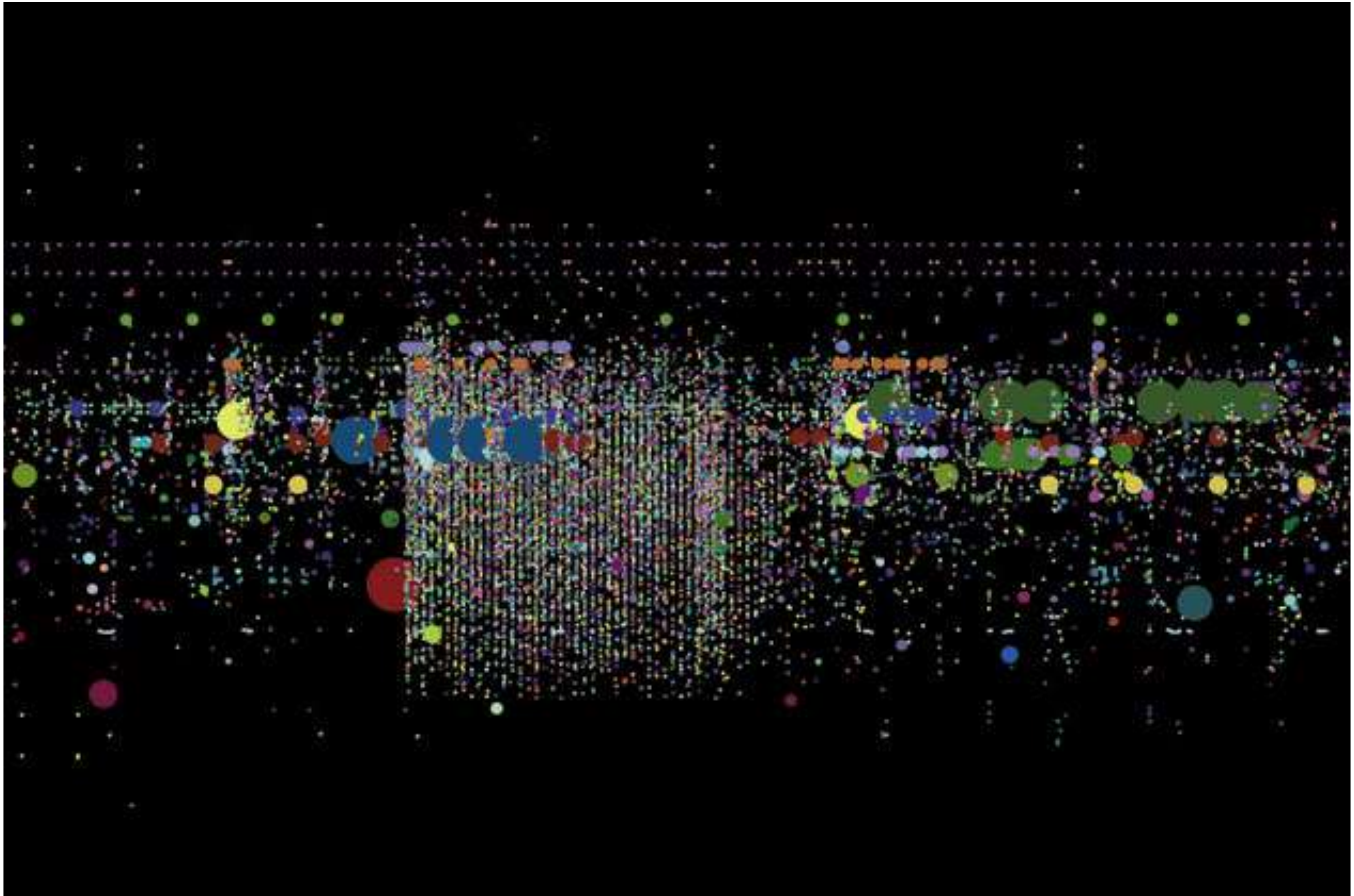

3. Four heresies

- Over-accumulation theory of crisis and disequilibrium theory of crisis don’t seem to be working
  - In other words, finance is not necessarily a positive or neutral bearer of ‘much-needed FDI’: is more likely to drain investment from domestic economies
- Greater value in circulation does not mean a greater velocity of circulation
  - Already limited by the speed of light. Profits are no longer found in asymmetries of market information in pit trading, but in preferential relationships with banks
- Increased liquidity does not imply increased speculation and cannot be explained by theories of overproduction
  - Money-holders have retreated to rentierism and class networking to secure profits
- Marxist forms of ‘value in production’, ‘value in circulation’, ‘value in process’ cannot be found given current synthetics
  - Economics is found wanting, particularly on the Left

Comparison of the market value of corporate equities and bonds with the current costs of corporate fixed assets.



Velocity of circulation: 6th May 2010



Allegheny Mountains

3.1 Financialization as socio-technical arrangement

- Its greater velocity of circulation is only limited by the speed of light
- High frequency trading reduced spreads and ability to profit from asymmetries of market information
- In response, retreat to dark pool trading, rentierism and offshore storage (corruption made easier…)
- For example, the flash crash, new cables, dark pools…

3.2 Insider trading institutionalised?

- Case against Barclays: funds tested the legality of the way it managed its dark pool alleging price manipulation was caused as it failed to tell investors of its hidden HTF clients, particularly Tradebot, representing it instead as 'safe', with low proportions of 'aggressive' HFT trading.
- Meanwhile it was recruiting HFT traders, allowed them the 'codes' from its dark pool servers, and provided proprietary feeds and co-location services at prices that only HFT firms could afford,
- Thus Barclays rigged its dark pool in favour of the HFT firms
- However, the Judge ruled that the exchanges held immunity from private law suits and money damages since they were discharging the regulatory duties conferred on them by the US SEC; and ruled the Plaintiffs had not proved their claims of price manipulation

3.3 End of speculation?

- The contracted derivative income stream is all, and is captured as a rent.
- Why risk capital when profits can be legalised as contracted and confirmed rents (with a ‘small’ bribe)
- Sustainability is an externality
- Holders of money have perverse reasons to take rents at the expense of everyone else.
- Leads to large projects with tranched finances
- Triple AAA, top tranche money-holders are de-risked
- Tail risks and liabilities put on the public sector

3.4 Financialisation is beneficial liquidity (overaccumulation)?

- “You cannot build an entire social cosmology [economics] on the assumptions of individual rationality, equilibrium and perfect markets – and then blame the failures of this cosmology on irrationality, disequilibrium and imperfections. In science, these excuses and blame-shifting are tantamount to self-refutation.” (Bichler and Nitzen, 2015, 67).
- “God is revealed to us through his miracles, and the same, argue the economists, holds true for the fundamental quantities of economics: they reveal themselves to us through their prices” (2015, 53).
- Since neither Marxists or neoclassicists can measure their base units – SNALTS and utils respectively - the main component of financialisation cannot be measured, since “the real price that the mismatch diverges from is itself “totally nominal’” (Bichler and Nitzen, 2015: 58).
- Crashes are not a rebalancing after disequilibrium: they are acts of theft between cycles of fraud

4. Conclusion: pathways to financialization

- Informalisation and criminalisation at national scale has repurposed national politics to enable Financialization and the move offshore: both processes internationalised
- And vice versa (synergistic), processes of Financialization have encouraged elites to try informalisation and criminality

Cf. Nitzan and Bichler, *Capital as Power* thesis:

- "capital is not a narrow economic entity, but a symbolic quantification of power…[capital] represents the organized power of dominant capital groups to reshape – or *creorder* – their society" (2009, auth emph)

c.f: Braudel viewed capitalism as a three tiered construction:

- the bottom layer of which is material life, the "stratum of the non-economy, the soil into which capitalism thrusts its roots" (Braudel, 1982: 229).
- The second tier is of the market economy, where a degree of automatic coordination occurs which links supply, demand and price. Most economics roots itself in explaining this level.
- But there is a another higher level "the zone of the anti-market, where the **great predators** roam and the law of the jungle operates. This…is the real home of capitalism" (Braudel, 1982: 229-230)

This zone is 'on the top floor of the house of trade' (Arrighi, 1994: 25), a 'shadowy zone' of finance