Can “Double Movement” Explain Globalization and Its Crisis?*

Gökçer Ö zgür and Hüseyin Özel

Department of Economics,
Hacettepe University
06800 Beytepe, Ankara, Turkey

gozgur@hacettepe.edu.tr;
ozel@hacettepe.edu.tr

Abstract

This paper asks whether the process of financial globalization and its recent crisis can be explained by Karl Polanyi’s notion of the double movement and argues, in tune with this notion, that capitalist market relations depend on certain institutional arrangements and yet the development of the market forces deteriorates these institutions arrangements to such extent that even the “capitalist business itself had to be sheltered from the unrestricted working of the market mechanism” (Polanyi 1944: 193).

Starting with the 1970s, during the globalization process the regulatory role of central banks is seriously deteriorated; and financial deregulation and innovation enabled banks to operate beyond their traditional banking activities, and international economic instabilities grew in this era. The global financial system lost most of its checks-and-balances that were built after the Great Depression, especially by the Bretton Woods System. Thus, it is argued that contemporary financial turmoil is the result of these developments; once again uncontrolled market forces shake the foundations of the market.

* First draft, please do not quote without permission.
Introduction

The starting point of this paper is Polanyi’s thesis in The Great Transformation that “capitalist business itself had to be sheltered from the unrestricted working of the market mechanism” (Polanyi 1944: 193). As Polanyi stated with his notion of the “double movement,” capitalist market relations depend on certain institutional arrangements and yet the development of the market forces deteriorates and undermines these institutional arrangements.

The present paper argues that starting in the 1970s, globalization process evolved as an institutional configuration in terms of the fall of the Bretton Woods System and the rise of the US dollar as reserve currency, worldwide capital and financial liberalization, and overall market ideology. As this institutional set-up has been establishing, the double movement also manifested itself in the global imbalances and resulting asset price speculation; which led to financial crises firstly in developed countries and secondly at the center of the global system.

In this era, the regulatory role of central banks is seriously deteriorated; and financial deregulation and innovation enabled banks to operate beyond their traditional banking activities. The global financial system lost most of its checks-and-balances that were built after the Great Depression. The global trade imbalances, new layers of financial intermediation, and reserve currency character of U.S. dollar only reinforced these changes and made a global surge of credit expansion a possibility. The credit expansion, a necessity for market functioning, fueled a new cycle of asset price speculation. It is plausible to argue that contemporary financial turmoil is the result of these developments. Once again uncontrolled market forces shake the foundations of the market.

Therefore, the in the first section, Polanyi’s notion of the double movement is discussed with reference to its three dimensions, namely, institutional, class and ideological dimensions. In the second section, after mentioning the first, liberal phase of capitalism until the 1930s, briefly the development since the Great Depression that leads to the globalization, the third section will focus on the developments that lead to current crisis of the system, and the fourth section will concentrate on credit expansion and asset price speculation. Final remarks will be given in the conclusion.

1. The Three Dimensions of the “Double Movement”

Karl Polanyi, in his Great Depression (Polanyi, 1944), argues that the “collapse” of the capitalist economy in the 1930s was due a “double movement,” which
can be personified as the action of two organizing principles in society, each of them setting itself specific institutional aims, having the support of definite social forces and using its own distinctive methods. The one was the principle of economic liberalism, aiming at the establishment of a self-regulating market, relying on the support of the trading classes, and using largely *laissez-faire* and free trade as its methods; the other was the principle of social protection aiming at the conservation of man and nature as well as productive organization, relying on the varying support of those most immediately affected by the deleterious action of the market—primarily, but not exclusively, the working and the landed classes—and using protective legislation, restrictive associations, and other instruments of intervention as its methods (Polanyi 1944: 132-33).

The double movement should be conceived in a broad perspective within which all the agents existing in the capitalist society interact with each other (Özel 1997, chapter 3). It is possible to distinguish between three interrelated aspects of the double movement, namely the institutional dimension, the class dimension, and the ideological dimension. The double movement, taken conceptually, refers to constant tensions, contradictions, and struggles that exist in a capitalist society between two important institutional spheres, namely, economic and the “political” spheres, whose separation is necessary for the market to function smoothly. While the market continuously extends its influence so as to include every spheres of life, the “rest of the society” resists and checks this extension. This contradictory process is usually carried out through class struggle. Mostly working classes will resist to the extension of the market, or at least try to modify the market in the form of constant interventions, including but not limited with the state interventions, while the capitalist class and its allies will support this extension by all means, including overt use of force as in the period of fascism. In this constant struggle, ideology plays an important role. Polanyi also depicts the double movement as the struggle between *laissez-faire* ideology and “protectionists” ideology. Therefore, in order to understand the globalization process with reference to double movement, each aspect must be taken into account, for it is the existence of the interaction between these aspects that makes the globalization process a contradictory one.

One of the most significant characteristics of the capitalist society, according to Polanyi, is the institutional separation of the economic and political spheres, for in order for the market be self-regulating it must be subject to no political or in general social intervention. In other words, capitalist system is characterized by the *disembeddedness* of the market (Polanyi 1944: 71; Polanyi et. al. 1957: 68). As similar distinctions between the “civil” and the “political” society, in Hegel and Marx (1975: 90), or between “community” (*Gemeinschaft*) and “society”
(Gesellschaft), in Tönnies (1988), and between “communal” (Vergemeinschaftung) and “associative” (Vergesellschaftung) social organizations, in Weber (1947: 136), all suggest, transition to capitalism is characterized by such a separation. Marx, for example, argues that whereas in the Middle Ages “every sphere of private activity had a political character, or was a political sphere” (1975: 90), in capitalism, the economic sphere has separated from the political one and has come to be defined on the basis of “private egoism.” In Hegel’s “civil society,” Marx argues, the individual lives an egoistic life, and she becomes an “isolated monad” (1975: 229), while in the political sphere, she becomes an abstract “citizen” (1975: 220). This dual existence of individuals also gives rise to two different types of conduct, namely instrumentally-rational behavior in the market, and a value-rational behavior in the political sphere. As Marx argues, Hegel’s distinction between “civil society” and “political state,” is nothing but the manifestation of the fact that economic sphere becomes a separate, autonomous one in capitalism. Marx argues that “The abstraction of the state as such was not born until the modern world because the abstraction of private life was not created until modern times. The abstraction of the political state is a modern product” (Marx 1975: 90). There was no distinction between civil society and the “political state” in the Middle Ages; that is, “every sphere of private activity had a political character, or was a political sphere, in other words politics was the characteristic of the different spheres of private life” (Marx 1975: 90). In capitalism, on the other hand, not only has the “political” become separated from the “private,” the private itself has come be defined on the basis of “private egoism,” i.e., on the basis of “economic” motives. Therefore, the individual becomes an “isolated monad who is withdrawn into himself” (1975: 229), who is characterized by egoism, whereas in the political sphere, the individual becomes an abstract “citizen.”

For both Marx and Polanyi, the issue is not simply the separation between the civil society and the state itself but the meaning and the causes of this separation: what this distinction implies is the institutional separation of the economy from the social relations within which it was embedded and hence, as a result, human totality is broken into separate entities. This also brings about the question of the role of the state in a capitalist society. The state plays a dual role in such a society; while it is the governing organ of the ruling classes, it also claims to represent the whole society.

Yet, the fact that the state, i.e. the bureaucracy, claims to represent the whole society poses a very interesting contradiction for the capitalist society, for the state is an agent which at the same time both promotes and is forced to restrain capitalist relations. Since even the very existence of the state depends upon capital accumulation in a capitalist society, it is quite
understandable that the state would promote capitalist relations by all means. In this regard, it should be noted that state’s centralized power, which actually is a result of the fact that the state has the monopoly over the means of violence in capitalist societies, gives it a unique position in both enforcing and protecting property rights and the formation of money and the credit system (Giddens 1986: 152-54). In this regard, Polanyi argues that from the very beginning the market system required active state intervention, even to the extent that the system itself was a product of state intervention. But such a position that the state has, also gives it the power to intervene directly into the economic sphere by political means. That is to say, while on the one hand the state has the function to maintain the separation between economic and political spheres, it also becomes an agent that carries out the “protective countermovement” directed to prevent the social fabric from disintegrating under the dominance of the market.

This protective movement, of which the state appears as a representative, is actually part of a more general process: against the social “breakdown” caused by the extension of the market, according to Polanyi is the “self-protection” of society, or more accurately, the resistance to the commodification process carried out by different classes and organizations within the society to the extension of the market into every aspect of life, that is, to the fictitious commodities (Polanyi: 1944: 76). In this double movement, state from the very start of the market system played an important role; not only did the state actively participated to the establishment of the market system., it also carried the banner of the protective countermovement regarding the fictitious commodities.

Therefore, the state had always played an essential role in both promoting and restricting the working of the market. Nevertheless, although state plays an important role in the self-protection of the society, this is not because state is an autonomous force above the society, but because of the fact that it is an integral part of the market society. That is to say, the essential characteristic of double movement is given by the struggle between classes and their effects upon the institutional structure, including the state as an “arena” of the class struggle.

Although Polanyi usually talks about the “self-protection of society,” which makes the double movement appear as a struggle between two abstract entities, “market” on the one side and, society” on the other, it should be emphasized that this movement is actually carried out by the classes, for “services to society performed by the landed, the middle, and the working classes shaped the whole social history of the nineteenth century” (Polanyi 1944: 132-33). In this regard, one can contend that the double movement can be conceived at two distinct yet related levels: the class level, for the social classes, above all the working class, are the causal agents who actually carry out the protective countermovement, and the institutional level, for the
protectionist countermovement caused the strains in the institutional structure of the market system, which eventually led to the catastrophe. These two angles, the interaction between the institutional strains inherent in the market system and the conflict of classes, are essential in understanding the whole history of capitalism, including its catastrophe, i.e., fascism, in the 1930s (Polanyi 1944: 134).

In order to understand the institutional strains that had arisen in the organization of the market system as a result of the protectionist counter movement, Polanyi considers the four distinct institutional spheres, two economic and two political, on the basis of which the market system is built: Domestic economy, with its main institution, the market; domestic politics, with the “Liberal state”; International Economics, with the Gold Standard, and the International politics, with the Balance of power system, before its “collapse” in the thirties. These disruptive strains are, according to the institutional spheres they belong, unemployment, tension of classes, pressures on exchange rates and the imperialist rivalries, respectively (Polanyi 1944: 209). All of these conditions characterize the crisis of the capitalist “world order,” the result of which would have been the “collapse” of the system out of which fascism came as a “solution.” Nevertheless, according to Polanyi, it must be emphasized that these conditions themselves “were set by the “double movement” (Polanyi 1944: 214).

In other words, the protective movement against the extension of the market, which had immediately begun as soon as the market system was instituted, caused these strains. In this regard, Polanyi identifies two factors as the sources of these disruptive strains: First, the conflict between international and national spheres within the market system, for the functioning of the system required the gold standard and the balance of power at the international level which both demand that the domestic economy and politics must be at the their service, thereby negating the popular and nationalist considerations, and, second, even more important, the institutional separation of the economic and political, for the tensions between the social classes created in the market sphere sooner or later had to be transferred to the political, which in turn creates further problems in the market.

Such a double movement is not necessarily limited to a simple clash between the classes in the society, even though both of these movements were conducted mainly by classes and the principles they represent, even when these principles are not compatible, from time to time, with their immediate “interests.” And it is the existence of this struggle between the classes and its effect on the economic sphere, the market, which makes capitalist society inherently unstable. But there is a double, or indeed circular, process at work here: since these classes themselves and their conflicts emanate from the economic sphere within a capitalist society, conflicts between
them will necessarily have social dimensions, that is, they will spread throughout the society, even if these conflicts may be economic in character, and this in turn creates further disruptive effects on the economic sphere whose impairment will intensify the tensions existing in the society. That is to say, “[s]ince society was made to conform to the needs of the market mechanism, imperfections in the functioning of that mechanism created cumulative strains in the body social” (Polanyi 1944: 201) In other words, the process of double movement will tend to break the institutional separation of the economic and political upon which the market system is built. The result of such a process would be the dissolution of the social fabric and the attempt to reestablish this institutional separation require eradication of every form of social opposition against the market, by any necessary means, including the use of force as the fascist period has shown.

In sum, in each form of protection the result would be the same: First, impairment of the market because of the protectionist intervention, then tensions between classes which requires political means and struggle, and then further impairment: According to Polanyi, “the strain sprang from the zone of the market; from there it spread to the political sphere, thus comprising the whole of society. But within the single nations the tension remained latent as long as the world economy continued to function. Only when the last of the surviving institutions, the gold standard, dissolved was the stress within the nation released (Polanyi 1944: 219)⁵ Therefore, the double movement is quite a complicated process, transgressing the boundaries between economic and political spheres in the capitalist society, although the main form of agency that has carried out it were the classes themselves, since only they could convey the struggle back and forth between these two spheres. But such a tension had to create strains not only in the economic sphere, but in the whole society, including the state for state become an “arena” of the class struggle, especially after the working class movement gained its strength, in which both economic and political means were used (Polanyi 1944: 133-34). Out of this struggle, there can arise different “solutions,” as the fascist period had shown. The fascist “solution” was nothing but a means of eradicating the social opposition which was led by the working class movement.⁶ But such a “solution” actually characterizes the “collapse” of the society with all institutions that are both expressions and means for the affirmation of freedom and hence humanity. In fact, it even signifies the collapse of the whole western civilization, for it is the denial of the very values that characterize this civilization. According to Polanyi, the “Christian discovery of the uniqueness of the individual and of the oneness of mankind is negated by fascism. Here lies the root of degenerative bent” (Polanyi 1944: 258A) The only way to restore these values is then, to accept both the “uniqueness of individual” and the “oneness of mankind,” which indicates two
inseparable characteristics that define humanity, which, he thought could be achieved only with socialism.

In other words, the true meaning of the double movement is the struggle between those forces that represent the “disembedded” economy and those that represent the attempt to “reembed” it into the society. For Polanyi, human beings are “humanized” by the plurality of institutions, like church, family, work, through which they can acquire an identity based on “the possession of responsibility, skills and conscience (Glasman 1994: 64). According to him, “[i]nstitutions are embodiments of human meaning and purpose” (Polanyi 1944: 254). In other words, those institutions that lie beyond the market can function for individuals to affirm their connectedness with other individuals through having personal direct relationships. In other words, these institutions, together with deliberately created associations or communities, aggregates etc., including political parties and trade unions, can function as “safe havens” to escape from the destructive, i.e., alienating, reificatory, effects of capitalism. Although this is for the most part an individual act, it nevertheless presupposes some form of collectivity, for the function of these institutions are to affirm sociality, direct, personal relationships; in short, to sustain the conditions of Gemeinschaft. In other words, seeking or forming Gemeinschaft-like associations, institutions, aggregates etc. can be seen a way out of the alienating forces that are effective in capitalism, especially to the extent that these forms can check the extension of the market.

Yet, sheer force is not the only possible way to eradicate potential sources of oppositions to capitalism, which brings about the third dimension of the double movement, namely, the ideological dimension. Since ideology, as the “common denomination” (Kosík 1963: 43) of the capitalist society, embraces all sections and classes of the society, it could be possible to lead people according to the “needs” of the system, through convincing them that “there is no alternative.” As long as this TINA formation becomes successful, no coercive action is necessary on the part of the ruling classes. If this is the case, as in the “neoliberal” phase of the system since the 1980s, it is not very easy to distinguish between the two conflicting tendencies in the double movement, extension of the market and resisting to it, for even the very human properties can be so distorted in discourse, through the reproduction of capitalist “ideology,” that they can be used in reproduction of capitalist relations. To the extent that individuals’ minds are reified enough to sustain capitalist relations, the institutions created to counteract the destructive effects of capitalism themselves becomes vehicles of reproducing very same capitalist relations.

In particular, the double movement seems to have been undermined in the “globalization” process to the extent that alienation, fetishism, and reification dominates every sphere of life,
including the mode of thinking of the modern individual. Thus, the success of the counter-
tendency to protection depends crucially upon conscious rejection of the mode of thinking that
capitalism dictates. To the degree that this reificatory aspect of capitalism deepens, the chance to
success of the double movement decreases. That is, double movement will be paralyzed to the
extent that it is “suppressed by the power of international capital on the one hand and inhibited
by the incapacity of increasingly divided, fragmented and individualized societies to organize
themselves to act in the interests of society as a whole” (Bienefeld 1991: 26) Such a society, in
which “the concept of a "perfect market for babies" as the ‘solution’ to the abortion debate may
be deemed perfectly acceptable,” argues Bienefeld (1991: 27), “was deemed "impossible" by
Polanyi and defined as "barbaric" by Marx many years before, but it will not be regarded in this
way by those who have come to accept it as the best that is humanly available.”

It can be argued that the basis of ideology as “false consciousness” is formed by the fact
that the very reality itself in capitalism is inverted or “false”; that is, ideology is just a
“reflection” of this inverted reality which forms the “common denomination” (Kosík 1963: 43)
in the society that unites, say, a capitalist and a worker in their vision of the reality. On the other
hand, from a functional point of view, this vision also implies a class-dependent position: even
though it is created by the reality, mystified social relations are not only reflected uncritically,
but they are also idealized, naturalized and eternalized through the reproduction of ideology. In
this regard, however, it should be emphasized that although they have the potential not to fall
under the influence of it, individuals participate in the reproduction of ideology in an active way,
through the attempts (of self-deception, wishful thinking, or willful ignorance) which are for the
most part intentional (Whisner, 1991; 1989).

Therefore, the double movement represents two contradictory features of the capitalist
reproduction process: in this process, although a social institution is an expression or
objectification of human essence, because of fetishism it also becomes a means to reproduce
capitalist relations. For this reason, when considering the double movement regarding money
and finance, it is essential to understand all three aspects of the process. “Globalization”
especially as a financial process, is carried out by two sides of the double movement; the state
and especially the central bank (and other regulatory institutions formed during the Bretton
Woods era), on the one hand, and the private banks and other financial agents and institutions, on
the other. Yet, in order to understand this process in the financial sector, it is necessary to
consider the history of the double movement regarding money.
2. Financial Liberalization and Deregulation as Part of “Double Movement”

Polanyi argues that even capitalist business had to be sheltered from the working of the market mechanism (Polanyi 1944: 193). For him, money, the last fictitious commodity, had to be protected against capitalist expansion as well. Besides, the counterprotection regarding money required active government intervention. During the “liberal” phase of the market system until the 1930s, in order for the international monetary system, the gold standard, to work, it called for domestic price changes when a change in the exchange rates is bound to occur. Such a system requires the existence of commodity money, gold, which was essential for foreign trade. On the other hand, however, since the amount of gold could not be increased at will, token money becomes essential for the domestic business, for it is the basis of the credit system. Then, a pressure upon the exchange rates will also put a pressure upon the domestic business for it will affect the credit system (Polanyi 1944: 194).

The developed solution to this would be the modern Central Banking for the protection of the productive activity, by controlling the domestic money supply, so that the price changes caused by the changes in the exchange rates could not have destructive effects. Actually, at the start, the central bank’s currency management was supported by the ruling classes, for it was seen as

the part of the rule of the game under which the gold standard was supposed to function. Since maintenance of the gold standard was axiomatic and the central banking mechanism was never allowed to act in such a way as to make a country go off gold, but on the contrary, the supreme directive of the bank was always and under all conditions to stay on gold, no question of principle seemed to be involved. (Polanyi 1944: 197)

This would not be a problem as long as the price changes could be kept at small rates. But if the necessary price movements are so drastic and at high rates that it could create danger for the domestic business, the attempt of the central bank to keep price movement at certain levels would be a direct interference to the working of the gold standard. Therefore, it is this incompatibility of the central banking with the gold standard which led the liberals (e.g. Mises) to propose that Central Banking must be relinquished, in order for the international Gold Standard to be self-regulative (Polanyi 1944: 195). However, in this case central banking became a political issue, transcending the economic-political distinction, for the price movements would directly affect the real incomes of the people. For this reason, in the 1920’s and 30’s, “[c]urrency had become the pivot of national politics” (Polanyi 1944: 24). While currency directly effects people’s real incomes through price changes, because of the gold standard its basis and hence its
control depends on the political factors outside the country. Such a strain caused a nationalist emphasis in the domestic politics, for the protectionism had a nationalist stamp, via money, which was different from its nineteenth century counterpart, an "easy-going" conception of nation. Therefore, “[p]olitically, the nation’s identity was established by the government; economically it was vested in the central bank” (Polanyi 1944: 205). In short, in the first, liberal phase of the market system, the strains over the central banks had become not only an economic but also a political issue that threatens the very existence of the system. It seems that the same applies to the final, “global” phase of the system, except that central banks seem to have no power over the financial sector of the globe.

In the post-war era, a new institutional configuration had been set up. The international balance of power was re-established in terms of U.S.-Western Capitalism and U.S.S.R-East European Socialism, as well as Third World developmentalism.\(^9\) Secondly, the liberal state of nineteenth century was replaced with welfare state in the north and developmentalist state in the south. The Bretton Woods appears as the new international payments system; and finally the idea of self-regulating market disappears.\(^10\)

However, this international political economic structure started to disintegrate in 1970s. The rise of free market liberalism once again put the double movement in motion, and the duality in the sense that “separation between economic and political spheres” came to realize. This transformation not only reshaped the institutional configuration of capitalism, but it also changed the relationship between capital and labor, as well as the ideological aspects.\(^11\)

Once again the movement started through the state(s) by questioning its (theirs) “protective” roles. The end of Bretton Woods system, stagflation, and oil shocks were not idiosyncratic events; these represented the end of post-war institutional framework. The capitalist system, once again, lost its international payment system and left unprotected against the ruinous effects of exchange movements. Similarly, the fiscal system of Keynesian welfare system was bankrupt, or the capitalists were no longer willing to accept the bill of this system through inflation.

Consequently, the interventionist state and the capitalism organized around it found itself in crisis and the ideology was again leaned toward “self-regulating market system.”\(^12\) Similar to “nineteenth century civilization” double movement mechanism was once again put in motion as the overall faith once again given to “free market” and its principles. Intervention, Keynesian policies, welfare state, regulations, trade unions were all seen as obstacles before a free market system, and these were held responsible for the economic and social problems of 1970s. Thus, removal of these obstacles or barriers would automatically establish efficiency in markets.
Moreover, the economic institutions, especially the financial ones, that kept the system together were also falling apart. At the international scene, it was no longer possible to keep U.S. dollar gold convertibility due to rising U.S. current account deficits; and domestically banking system was also in serious trouble due to fixed interest rates and rising inflation. In this economic environment, U.S. abolished the dollar gold convertibility and adapted full capital liberalization in 1973. Most of the developed economies followed U.S. example by introducing liberalization in capital markets even though they waited for some years for full international capital mobility.13 This change marked the emergence of a new international payment system, in which international currency was no longer tied to a commodity or pseudo-commodity money. However, the end of dollar gold convertibility did not mean the end of U.S. dollar as a reserve currency. As most of the commodities were still traded in U.S. dollar, and international reserves were still kept in dollars, it gained an important new position. For the first time, a fully fiat money become the reserve currency with very important consequences-of which will be discussed in the next section.

Another dimension of financial liberalization took place at the domestic institutions. In the post-war era commercial banks had dominated the financial system, and these institutions were highly regulated as a legacy of Great Depression.14 However, rising inflation and new competitors such as money market mutual funds (MMMFs), mutual funds (MFs), retirement funds (RFs) started to squeeze banks’ profits during 1970s; and banks started to ask for deregulation and liberalization (Edwards and Mishkin, 1995; Samolyk, 2004). Unlike commercial banks, the amount of interest that these institutions could pay was determined in the market, and the degree of regulation was much weaker. Similarly, the rise of retirement funds also attracted household savings; and as these institutions needed to invest the funds they collected, they created a huge demand for financial assets. In U.S., the Employee Retirement Income Security Act (ERISA) of 1974 introduced funding requirements for pension funds and thus, pension funds needed to buy debt instruments which led to “asymmetrical increase in borrowing through capital markets” (D’Arista 2002: 3). This new demand for financial assets also meant firms’ need for bank loans were in decline as direct finance opportunities were rising. Consequently, commercial banks started to loose their monopoly position in terms of collecting funds and making loans out of them. As being at the center of the system, U.S. commercial banks showed the full extent of these changes: commercial banks used to have more than 50 percent of all financial assets during 1960s, but this rate started to decline after 1980s and fell to less than 25 percent by early 2000s. As a direct consequence of these developments mutual funds and retirement funds increased their share in this era (Özgür and Ertürk, 2008: 6).
These competitive pressures should be known in order to understand the full extent of financial deregulation and innovation activities. Faced with these harsh conditions, commercial banks sought liberalism as a remedy for the troubles they had. As a result of their attempts, regulations on interest rates were abolished and reserve requirements were eased. In fact, these changes represented only the tip of the iceberg for commercial banks. Even these deregulations could not guarantee the former strength of commercial banks, and as a result, banks needed to start new types of financial activities through financial engineering and innovation. Banks started to move beyond traditional banking activities and were no longer limited to collecting deposits and making loans. Non-traditional banking such as selling loan guarantees and securitization activities become very widespread during late 1990s and 2000s. As secondary markets established for all kinds of loans, banks started to sell off loans from their balance sheets. This activity not only increased the turn-over rate of funds in banks’ balance sheets, but it also increased banks’ risk appetite; banks no longer needed to worry about the risk of the loans, as these risks were passed to third parties. These activities are known as “originate and distribute” (O&D) model and the O&D model become an important aspect of banking in the last decade. (Borio, 2008: 4). The revenues from such non-traditional activities increased throughout 1990s and started to constitute more than 50 percent of all bank revenues after 2000 (Özgür and Ertürk, 2008: 7).

Similarly, hedge fund activities, and derivatives markets increased their share in financial markets starting from 1990s. Both these changes are the direct results of deregulation attempts. The redefinition of derivative activities by International Swaps and Derivatives Association (ISDA) in 1999 and 2003 are responsible for the rise of derivative activities in recent years (Mengle, 2007: 12). Likewise, the change of legal framework of hedge funds in 1996 led to a rapid growth in the number and asset size of hedge fund activities (Brown et. al., 1999: 94).

While financial institutions were experiencing such radical changes in developed economies, developing economies had gone through their own liberalization process. In fact, the liberalization of developed economies is crucial to complete the re-birth of liberal system at a world scale. Developing countries went through liberalization activities first in early 1980s as a result of debt crises, and in East Asia in mid-1990s due to pressures from IMF and U.S. Treasury (Stiglitz, 2002: 98-104; Crotty and Lee, 2004). In developing economies, financial liberalization meant opening the borders for full capital mobility and removing all the barriers against foreign investors. In many liberalization cases, developed economies experienced a surge of foreign capital and economic boom immediately after liberalization; yet faced capital flight and economic crisis (Kindleberger and Aliber, 2005: 4-7). Financial liberalization bred financial
instability in the developing economies, and the only solution these economies could find against capital flight and instability was accumulating international reserves most of which are denominated in U.S. dollar.

These changes in developed and developing economies made the establishment of free market possible at a global scale. On the one hand, liquidity increased as a result of greater financial activities, and on the other hand the evaluation of risk is passed to the asset markets. The basis of these deregulation and liberalization activities depends on the Efficient Market Hypothesis. It was widely believed, once credit is collateralized and securitized, asset markets would give the optimal results in terms of pricing and risk taking. Thus, all these changes took place for the sake of efficiency and “free market” spirit.

3. The So-called “Global Imbalances” and the Dollar Hegemony

Financial liberalization activities of previous decades were not merely regime changes; they have long-lasting effects and are also responsible for the current financial turmoil. U.S. economy started to experience large current account deficits during 1990s and 2000s and this process has to be understood in accordance with the financial liberalization process. Financial crises of developing economies in 1990s showed that developing economies are vulnerable to capital flights; and in a liberal capital regime the only protection seemed as current account surpluses and international reserves. The so-called “global imbalances” and the dollar hegemony should be understood as a direct outcome of overall financial process; and the effects of this process were also responsible for breeding financial instability.

There is a vast literature on global imbalances among mainstream economics and this literature tries to explore the causes of global imbalances, whether these imbalances are sustainable or not, whether an adjustment will take place, if it will how. The main argument is usually based on the idea of “global savings glut,” meaning China and other Asian countries are responsible for global imbalances. However, there are also other studies that confirm foreign investors are not investing in U.S. capital markets to finance U.S. deficits, but they do it because it is safe and profitable due to international reserve position of U.S. dollar. And once capital flows to U.S. economy, it stimulates borrowing, expenditure, and asset prices, as well as exchange rate. Capital inflow, dollar appreciation, and higher imports are responsible for U.S. deficits. As a result, the line of causality between current account deficit and capital inflows has to be reversed.

During 1990s and 2000s, U.S. economy could manage to attract capital inflow both from developed and developing economies and by 2002 the share of U.S. capital import in world total
reached to 73 in net numbers (Graph 1). Capital inflows into U.S. economy almost doubled between 1998 and 2002; and this rise could not be explained by a change in savings patterns of Asians. It is not a coincidence that capital inflows to U.S. economy increased after the turmoil of East Asian, Russian, and Latin American crises (Aliber, 2005: 149). Even though the share of U.S. started to decline after 2002, the bottom of stock market, capital inflows to U.S. did not slow down. Foreign investments concentrated on equities until 2002, and after then debt instruments, especially agency debts become the major recipient of foreign capital (U.S. Treasury, 2008: 3; and U.S. Treasury, 2000: 2).

![Graph 1: The Share of U.S. Capital Import in World Total](image)


In early 1990s, U.S. Treasury also supported this trend for access to cheap funding for its borrowing needs; and for this purpose kept a positive risk dollar premium (D’Arista, 2002: 10-11; and DeLong and Eichengreen, 2002: 227). However, by late 1990s dollar premium turned into negative numbers, yet foreign capital kept flowing into U.S. economy (Balakrishnan and Tulin, 2006: 4). From this perspective, financial instability among developing countries as a result of liberalization is responsible for capital inflow into U.S. economy.
Developing countries, especially Asian economies, are usually held responsible for this capital inflow to U.S. And as mentioned above, mainstream economists argue that abnormal savings rates and capital surpluses are the causes of so-called global imbalances. However, a close look at the macroeconomic balances of developing economies tells a different story. Developing economies, and some Asian countries had negative savings-investment gaps and current account deficits prior to 1998 (Table 1). Newly Industrializing Asian Economies (NIAE)†, ASEAN-5 countries‡ and China had only had moderate current account surpluses before 1998. Emerging and Developing Economies (EDE) had current account deficits, and even Middle East countries were in deficit in some years. All these economies started to build considerable current account surpluses only after 1998.

Moreover, positive savings-investment gaps emerged not due to a rise in savings but due to a fall in investments in many Asian countries after East Asian Crisis. NIAE, as group, showed a stable savings rate in the last three decades; these economies experienced a rapid rise in investments prior to 1998 and a rapid fall after then. Some other Asian countries such as Indonesia, Korea, Philippines, Thailand showed a similar pattern; and “the deep recessions and very sharp depreciation of 1998 led to” this “reversal…” (Felipe et. al., 2006: 36-37). EDE on other hand did actually experience a rise in savings rate, but investments were also in rise and savings were growing faster than investments. The only country group experiencing a rapid growth in savings rates was Middle Eastern economies; and oil prices must be responsible for it.

† Hong Kong, Korea, Singapore and Taiwan.
‡ Indonesia, Malaysia, Philippines, Thailand, Vietnam.
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>NIAE</td>
<td>-9.14</td>
<td>11.08</td>
<td>16.80</td>
<td>2.14</td>
<td>64.61</td>
<td>38.86</td>
<td>47.97</td>
<td>55.71</td>
<td>80.99</td>
<td>83.52</td>
<td>80.21</td>
<td>90.01</td>
<td>103.59</td>
<td>76.22</td>
<td>90.98</td>
</tr>
<tr>
<td>EDE</td>
<td>43.45</td>
<td>-31.32</td>
<td>-35.18</td>
<td>-93.07</td>
<td>-105.95</td>
<td>90.75</td>
<td>46.64</td>
<td>83.19</td>
<td>151.27</td>
<td>226.09</td>
<td>447.76</td>
<td>630.63</td>
<td>633.40</td>
<td>714.44</td>
<td>262.44</td>
</tr>
<tr>
<td>Middle East</td>
<td>81.68</td>
<td>-0.36</td>
<td>5.61</td>
<td>4.47</td>
<td>-23.46</td>
<td>71.92</td>
<td>40.44</td>
<td>29.89</td>
<td>57.47</td>
<td>97.07</td>
<td>201.35</td>
<td>252.87</td>
<td>254.11</td>
<td>341.62</td>
<td>-10.16</td>
</tr>
<tr>
<td>China</td>
<td>0.29</td>
<td>-11.51</td>
<td>12.00</td>
<td>1.62</td>
<td>31.47</td>
<td>20.52</td>
<td>17.41</td>
<td>35.42</td>
<td>45.88</td>
<td>68.66</td>
<td>160.82</td>
<td>253.27</td>
<td>371.83</td>
<td>440.01</td>
<td>496.57</td>
</tr>
<tr>
<td>Japan</td>
<td>-10.75</td>
<td>51.15</td>
<td>43.94</td>
<td>111.40</td>
<td>119.07</td>
<td>119.61</td>
<td>87.79</td>
<td>112.61</td>
<td>136.24</td>
<td>172.07</td>
<td>165.69</td>
<td>170.44</td>
<td>210.97</td>
<td>157.08</td>
<td>76.36</td>
</tr>
</tbody>
</table>

Table 1: Selected Macroeconomic Variables

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>NIAE</td>
<td>-6.12</td>
<td>5.10</td>
<td>3.03</td>
<td>0.21</td>
<td>7.27</td>
<td>3.48</td>
<td>4.57</td>
<td>4.94</td>
<td>6.74</td>
<td>6.28</td>
<td>5.35</td>
<td>5.46</td>
<td>5.73</td>
<td>4.39</td>
<td>6.30</td>
</tr>
<tr>
<td>EDE</td>
<td>1.22</td>
<td>-0.92</td>
<td>-0.68</td>
<td>-1.73</td>
<td>-1.76</td>
<td>1.42</td>
<td>0.72</td>
<td>1.25</td>
<td>2.01</td>
<td>2.53</td>
<td>4.21</td>
<td>5.02</td>
<td>4.14</td>
<td>3.84</td>
<td>1.56</td>
</tr>
<tr>
<td>ASEAN-5</td>
<td>-1.18</td>
<td>-2.15</td>
<td>-4.64</td>
<td>-5.35</td>
<td>7.35</td>
<td>5.05</td>
<td>3.86</td>
<td>3.67</td>
<td>4.03</td>
<td>2.88</td>
<td>1.96</td>
<td>4.90</td>
<td>4.94</td>
<td>2.76</td>
<td>2.20</td>
</tr>
<tr>
<td>Middle East</td>
<td>19.46</td>
<td>-0.10</td>
<td>1.29</td>
<td>0.95</td>
<td>-4.59</td>
<td>11.40</td>
<td>6.38</td>
<td>4.68</td>
<td>8.07</td>
<td>11.69</td>
<td>19.71</td>
<td>20.98</td>
<td>18.23</td>
<td>18.83</td>
<td>-0.64</td>
</tr>
<tr>
<td>China</td>
<td>0.09</td>
<td>-3.75</td>
<td>3.07</td>
<td>0.22</td>
<td>3.09</td>
<td>1.71</td>
<td>1.31</td>
<td>2.44</td>
<td>2.80</td>
<td>3.55</td>
<td>7.19</td>
<td>9.53</td>
<td>10.99</td>
<td>10.00</td>
<td>10.28</td>
</tr>
<tr>
<td>Japan</td>
<td>-1.02</td>
<td>3.77</td>
<td>1.45</td>
<td>2.11</td>
<td>3.08</td>
<td>2.56</td>
<td>2.14</td>
<td>2.87</td>
<td>3.22</td>
<td>3.73</td>
<td>3.63</td>
<td>3.91</td>
<td>4.81</td>
<td>3.19</td>
<td>1.53</td>
</tr>
</tbody>
</table>

Current Account Balances (Percent of GDP)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>NIA (I)</td>
<td>34.93</td>
<td>21.48</td>
<td>29.32</td>
<td>31.46</td>
<td>43.35</td>
<td>28.22</td>
<td>25.32</td>
<td>24.87</td>
<td>24.84</td>
<td>26.44</td>
<td>25.87</td>
<td>26.10</td>
<td>25.97</td>
<td>27.44</td>
<td>22.80</td>
</tr>
<tr>
<td>NIA (S)</td>
<td>28.25</td>
<td>31.31</td>
<td>34.38</td>
<td>33.57</td>
<td>33.16</td>
<td>31.70</td>
<td>29.79</td>
<td>29.75</td>
<td>31.48</td>
<td>32.63</td>
<td>31.37</td>
<td>31.56</td>
<td>31.82</td>
<td>31.90</td>
<td>29.07</td>
</tr>
<tr>
<td>NIA (S-I)</td>
<td>-6.68</td>
<td>9.83</td>
<td>5.06</td>
<td>2.11</td>
<td>-10.18</td>
<td>3.48</td>
<td>4.47</td>
<td>4.88</td>
<td>6.64</td>
<td>6.20</td>
<td>5.50</td>
<td>5.46</td>
<td>5.85</td>
<td>4.46</td>
<td>6.27</td>
</tr>
<tr>
<td>EDE (I)</td>
<td>-6.68</td>
<td>9.83</td>
<td>5.06</td>
<td>2.11</td>
<td>-10.18</td>
<td>3.48</td>
<td>4.47</td>
<td>4.88</td>
<td>6.64</td>
<td>6.20</td>
<td>5.50</td>
<td>5.46</td>
<td>5.85</td>
<td>4.46</td>
<td>6.27</td>
</tr>
<tr>
<td>EDE (S)</td>
<td>24.05</td>
<td>22.80</td>
<td>25.42</td>
<td>25.16</td>
<td>26.26</td>
<td>27.99</td>
<td>29.82</td>
<td>31.57</td>
<td>33.31</td>
<td>34.23</td>
<td>35.12</td>
<td>33.72</td>
<td>34.23</td>
<td>35.12</td>
<td>33.72</td>
</tr>
<tr>
<td>EDE (S-I)</td>
<td>-1.71</td>
<td>-1.80</td>
<td>1.32</td>
<td>0.71</td>
<td>1.31</td>
<td>2.10</td>
<td>2.57</td>
<td>4.24</td>
<td>5.02</td>
<td>4.14</td>
<td>3.86</td>
<td>1.56</td>
<td>3.86</td>
<td>1.56</td>
<td>3.86</td>
</tr>
<tr>
<td>Middle East (S)</td>
<td>42.42</td>
<td>17.50</td>
<td>20.94</td>
<td>24.55</td>
<td>19.73</td>
<td>31.49</td>
<td>29.67</td>
<td>28.32</td>
<td>32.29</td>
<td>35.67</td>
<td>42.40</td>
<td>43.85</td>
<td>43.87</td>
<td>44.25</td>
<td>27.49</td>
</tr>
<tr>
<td>Middle East (S-I)</td>
<td>17.18</td>
<td>-3.67</td>
<td>-2.62</td>
<td>2.27</td>
<td>-4.46</td>
<td>11.34</td>
<td>6.36</td>
<td>4.67</td>
<td>8.06</td>
<td>11.64</td>
<td>19.70</td>
<td>20.97</td>
<td>18.23</td>
<td>18.83</td>
<td>-0.64</td>
</tr>
</tbody>
</table>

1 Newly Industrialized Asian Economies: Hong Kong, Korea, Singapore, Taiwan
2 Emerging and Developing Economies
3 ASEAN-5: Indonesia, Malaysia, Philippines, Thailand, Vietnam
Source: IMF, World Economic Outlook Database, April 2009
Once the data on developing economies are taken into consideration the mystery of so-called Global Imbalances disappear. Some economists believe that these imbalances are not problematic as long as U.S. economy finances her deficits. These arguments based on the belief that U.S. economy will never fall short of foreign capital inflows, and as long as foreign capital flows into U.S. economy there is not a problem. Similarly, as most of international claims on U.S. are in U.S. dollars, foreign capital is not very different from domestic one. However, these imbalances and capital inflows themselves are problems for the U.S. and global economy. Current global financial turmoil is based on excessive rise in asset prices in U.S. economy, and foreign capital inflow played an important role in this process. U.S. deficits and excessive credit expansion in fact responsible for the asset price speculation and its demise in recent years. The real cause of recent global financial turbulence should be reconsidered through these imbalances, and their causes.

4. Credit Expansion and Asset Price Speculation

Financial liberalization went through two major channels since 1970s. Firstly, most of the regulations and controls are removed in financial markets, and the industry started to be dominated by asset markets and non-traditional banking activities. Secondly, financial liberalization increased vulnerability of developing economies against capital flows and increased their need for protection, through accumulating international reserves. As a result, massive inflow of foreign capital, together with unregulated financial markets and exotic financial instruments, led a surge in domestic credit and asset price build up in U.S. economy.

Economic history shows that financial liberalization attracts foreign capital inflows and massive capital inflows, especially in developing economies, end up with financial crisis (Reinhart and Rogoff, 2008). Various examples of financial liberalization showed economic boom and credit expansion immediately follows liberalization attempts, which gradually builds up asset prices. Financial instability and crisis comes after as a result of either excessive hikes in asset prices or deterioration of current account balance. The examples of Japan, and Scandinavian countries in 1980s, Mexico in early 1990s, East Asian countries in 1990s, and U.S. stock market boom in late 1990s all show similar tendencies (Aliber, 2005). During asset price booms, credit expansion increases and result in investment spending; and in the downturns, reduced values of assets contract credit mechanism and spending. Asset/property prices have a direct influence on the willingness to borrow and lend. From the borrowers perspective (either firms or households), rising property prices reflect rising collateral values and improved balance
sheets, so property prices easily stimulate borrowing activities. And higher collateral values also increase the creditworthiness of borrowers and banks’ willingness to lend as well. As a result, the cyclical movements of asset prices become responsible for the fluctuations in economic activities (Borio and Shim, 2007: 3).

U.S. is not a developing country, and considering that most of her international liabilities are also in her domestic currency, it may sound odd to argue that financial liberalization is breeding instability. However, financial liberalization in U.S. did have certain effects on the asset price speculation and resulting instability. U.S. financial liberalization led to rise of non-bank financial institutions, securitization activities, financial engineering, and growth of shadow banking. All kinds of loans could be turned into securities and sold in secondary markets, and banks’ function in this process was to originate loans and distribute to some one else. As a result, banks’ loan monitoring standards declined considerably. On the other hand, the existence of loan guarantees and off-balance sheet banking activities enabled non-financial businesses to directly borrow from financial markets. And U.S. markets are flooded with all kinds of assets. Such changes increased access to credit on the one hand, and increased the issuance of financial assets on the other. As a result the burden of external financing declined considerable in the last two or three decades.

The deterioration of risk monitoring, emergence of off-balance sheet activities, and deregulation are not sufficient to explain the real causes of financial instability. U.S. financial liberalization was the first step and the dominance of liberal regimes in developing economies completed the picture. As shown in the previous section current account surpluses in developing economies and capital inflows to U.S. economy continued during 1990s and increased after 1998. These capital inflows to U.S. concentrated on equities during the Dot-Com Bubble of 1990s and switched to debt instruments during 2000s (Kraay and Ventura, 2007: 459-460). In both episodes asset prices and credit expansion fed each other, especially due to procyclical activities of financial institutions.19 The overall confidence for “market” and “its valuation” also contributed to the deepening of problems. Policy-makers and regulators saw no harm in these practices, as they were blinded by low and stable inflation as well as central bank credibility. Regulatory institutions on the other hand were designed to detect firm-level instabilities, so system-wide excessive movements remained unnoticed (Borio and Shim, 2007: 4). In this economic environment U.S. economy experienced two asset price bubbles; i.e., stock market bubble in 1990s, and housing market bubbles in 2000s.

In both speculative bubbles, the activities of “institutional investors” and their ability to trade assets by credit also contributed to rise in asset prices. As economic historian Kindleberger
explained in detail, credit became the fuel of speculative euphoria (Kindleberger and Aliber, 2005: 25-30). By the end of 1990s, institutional investors were responsible for 75 percent of all trading in the stock market (Evans, 2003: 124).

After the end of stock market boom, credit expansion created a new speculative mania, in housing market and mortgage-debt instruments. The O&D model enabled banks to increase mortgage loans without worrying about risk or capital requirements due to securitization. As new financial intermediaries emerged in charge of trenching these mortgage loans, underwriting securities, and supplying insurance, credit expansion could continue. As the mania started to emerge in these markets, financial institutions moved into riskier areas, subprime mortgage loans. Mortgage loans increased demand for housing and pushed housing prices; higher prices meant higher collateral values and higher collateral values stimulated demand for loans (Kregel, 2007: 19-21). This scheme ended when risky borrowers defaulted on their debts. The smooth expansion of credit prepared its own demise in the sense that Minsky warned decades ago: “stability is destabilizing” (Wray, 2008: 8).

In sum, financialization process, credit expansion and resulting asset price speculation are responsible for the turmoil. Massive and long-term capital inflows increased the asset values and diminished risk perceptions; U.S. economy is not different than any other economy in this sense. What makes the U.S. case unique is, she attracted capital inflows due to U.S. dollar’s international position as the reserve currency. Though it was a reserve currency even after the end of Bretton Woods, U.S. dollar reinforced its position through global financial liberalization and resulting instabilities. And as long as these conditions prevail, similar capital inflows, asset price bubbles, and resulting instabilities can take place. The basis of current global turmoil is neither the greediness of some investors nor their wrongdoings; the establishment of “free and liberal markets” in international economy and finance seems to be the fundamental cause.

5. Conclusion

Starting from 1970s, a new international institutional set up started to emerge and fully established in 1990s. This new system was a re-establishment of “self-regulated market mechanism” This system was based on U.S. dollar as the reserve currency, a uni-polar world based on U.S. supremacy, self-regulated market, and non-interventionist government. The establishment of these institutions took place at a global scale through various attempts of liberalization and deregulation. Double movement, as usual, also played a role in this establishment: the liberalization of markets brought turmoil and crises in developing countries
during 1990s, and created a bigger mess at the center of the system since 2007. Liberalization and unrestrained-uncontrolled market system prepared the foundations of current crisis.

Free market system and its ideology are started to be questioned as an immediate response to crisis. Similarly, western governments and central banks initiated huge rescue programs andlooded markets in 2008 and 2009. All these developments represent serious hits on the international economic and political system that dominates. Yet, the double movement has not completed its course. As long as financial liberalism lasts and U.S. dollar remains as the reserve currency, world economy may go through similar phases. And these potential threats can create even bigger problems and reactions.

The current economic crisis represents an example of self-destructive power of the market system and it is obvious that even capitalists need protection against it. These events reveal only institutional dimension of double movement. Class and ideological dimensions have not shown their faces yet.
References:


Lukács, George (1971). History and Class Consciousness: Studies in Marxist Dialectics,


NOTES

1 Likewise, according to Georg Lukács (1971: 229), although particular aspects of economic process exist in precapitalist societies, they are independent of each other and they do not link into a separate economic system. Only with capitalism do these aspects form a close-knitted, insoluble unity which is independent of the rest of the society. In precapitalist societies, “economic life did not yet possess that independence, that cohesion and immanence, nor did it have the sense of setting its own goals and being its own master that we associate with capitalist society” (Lukács 1971: 238). For Lukács, it is this “self-contained autonomy (which was what made it an economy, properly speaking)” (Lukács 1971: 251), gave rise to the Classical political economy, for this view was nothing but a reflection of the emergent autonomy of the economy.

2 For example, according to Tönnies (1988: 216-17), the state, as a characteristic association of Gesellschaft, is on the one hand established for the purpose of “protecting freedom and property of its subjects, i.e., implicitly, of representing and enforcing the natural law based on the validity of contracts,” and therefore like any special interest-group it is subject to the natural law which is conceived as “the will of Gesellschaft.” But on the other, state is above the law, for it claims to be the society itself.

3 “There has always been a close association between the nation-states, themselves products of capitalism, and ‘societies,’ even to the extent that the ‘capitalist society’ is a ‘society’ only because it is a nation-state” (Giddens 1986: 141). That is to say, the term “society” has come to be identified with the people living within the boundaries of a nation-state and thus the “discovery” of the society goes hand in hand with the establishment of the nation-state. For a discussion of the ambiguities of the term “society” and its relation to nation-states, see Giddens (1984: 163-8; 1986: 135-36).

4 Block and Sommers (1984: 71-72) suggests that the “double movement” should be considered as a “metaphor,” operating as a “heuristic” but carries no specific causal argument by itself.

5 Allen Sievers (1949: 344-47), characterizes of the history of the market capitalism with the following turning points: strain, which begins in 1879 marking the date at which the protectionist movement started to inhibit the self-regulating character of the market mechanism; collapse, referring to the collapse of the Concert of Europe, thus triggering the events that led to the war; rejuvenation (attempt to establish the international political order and the gold standard); almost immediately followed by the fourth phase: strain, characterized by the crisis and the rise of the popular government, and finally, collapse and abrupt transformation in the form of fascism, Russian five-year period, and the New Deal.

6 Polanyi’s analysis of fascism iterates the themes that appear in the other, especially Marxist, analyses of fascism. For a brief comparison of Polanyi’s analysis of fascism and other liberal and Marxist theories of fascism, see W.L. Goldfrank (1990). Also see Neumann (1944), Fromm (1941), Lowenthal (1945), Horkheimer (1973), and Hobsbawm (1994: ch. 4). Most of these analyses emphasize the fact that fascism characterizes the “limit conditions” of capitalism which are defined by the atomization and impotence of the individual, and thus there is no form of opposition which might be a threat to the working of the system..

7 For example, Daniel Fusfeld (1993: 8) criticizes the Republican conservatives who glorify both the free market and what they call “family values” in that they cannot see the destructive effect of the free market on the family values.

8 Yet, here only the first and the third aspect of the double movement are considered; the class aspect lies beyond the scope of the present paper.

9 For global polarization, see: Amin, 1997: 14-17.
Similarly, Social Structures of Accumulation school defines the post-war era on four major issues. These are, Pax Americana, capital-labor accord, moderate competition, and Keynesian welfare state (Bowles et al., 1990, quoted in O’Hara, 2006: 47).

The end of welfare state and third world developmentalism in developed and developing countries, respectively. The end of capital-labor accord, and the rise of neo-liberal ideology.

The transformation was not actually complete until the debt crises of 1980s and the fall of U.S.S.R. which integrated developing countries and former socialist countries into this new liberal system.

For the exact dates of liberalization see Kaminsky and Schmukler, 2008: 260-262.

Banking business was strictly limited to collecting deposits and making loans; and the maximum amount of interest that could be charged were also regulated. Similarly banks were strictly prohibited from entering into other fields of financial system such as investment banking, insurance, and asset trading (Wray 2007). On the other hand banks had a monopoly over collecting household savings and making loans (Edward and Mishkin, 1995).

However, it is impossible to test the validity of the theory empirically; and as Eugene Fama (one of the founding fathers of the theory) had once accepted “models of market equilibrium start with the presumption that markets are efficient” (FRB Minneapolis, The Region, “Interview with Eugene Fama,” December 2007, quoted in Crotty: 2008: 11).


The leverage ratio (the ratio of total assets to shareholder value) is the key in this mechanism. A rise in the value of total assets reduces the leverage ratio, and consequently financial institutions can afford to borrow more with lower leverage ratios. As a result of higher borrowing activities, they command greater amount of funds and increase their assets (Adrian and Shin, 2008).