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Money Manager Capitalism

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Money manager capitalism is the name Hyman P. Minsky (1919-1996) assigned to the current economic era in his historical analysis of U.S. capitalist development. This era emerged in the 1980s as institutional investors—holders of the largest share of corporate stocks and bonds by the end of the decade—began to exert their influence on financial markets and business enterprises. The study of money manager capitalism was the main focus of Minsky's attention during the final decade of his life.

Career Context

Minsky's career can be divided into four periods. After earning his Ph.D. from Harvard University in 1954, Minsky devoted two decades to various explorations of the impact of financial institutions on economic performance. Then, in 1975, publication of his *John Maynard Keynes* (Minsky 1975) signaled the start of a period focusing on business cycles, the centerpiece of which was his "financial instability hypothesis." In the first half of the 1980s, Minsky's attention shifted to the problem of increasing U.S. economic instability, culminating in his *Stabilizing an Unstable Economy* (*SUE*) (Minsky 1986a). The final period began after publication of that volume and featured investigations of capitalist development, with special attention to the U.S. economy; the notion of money manager capitalism emerged in the course of those investigations.

Minsky set the stage for the final phase of his career with a 1986 essay on Joseph A. Schumpeter and John Maynard Keynes. He wrote: "The task confronting economics today may be characterized as a need to integrate Schumpeter's vision of a resilient intertemporal capitalist process with Keynes' hard insights into the fragility introduced into the capitalist accumulation process by some inescapable properties of capitalist financial structures" (Minsky 1986b, 121). As that statement suggests, Minsky retained his interest in business cycles and increasing economic turbulence, but they were now placed in a broader context.

Economic Context

According to Minsky (1990, 65), Schumpeter argued that capitalism is resilient "because it takes many particular forms." In Minsky's (1993a, 3) own words, "There are as many varieties of capitalism as Heinz has of pickles"—a reference to that company's "57 Varieties" slogan. Each variety tends to yield different economic results, however, and Minsky was troubled by what money manager capitalism offered.

Minsky expressed concern about the fragile financial structure that accompanied the emergence of money manager capitalism and that made it highly susceptible to an economic crisis, but he was also uneasy about the new era's ability to contribute to the capital development of the U.S. economy. He believed money manager capitalism promised not only a level of investment insufficient to create a full employment economy, but also a composition of investment inadequate to ensure that U.S. capitalism would remain technologically dynamic (Minsky 1990, 72; 1992, 21-26; 1993b, 111-113).

Minsky had other concerns as well. He was apprehensive about the growth of securitization, the declining competitiveness of American industry, the erosion of economic security for U.S. workers, and the widening of income inequality in the midst of overall economic expansion (Minsky 1986c; 1993a). He saw the need for a more robust small-business sector and for widespread community economic revitalization (Minsky 1993c). And he worried that money manager capitalism had become global, rendering it impossible for U.S. policymakers to resolve a financial crisis through unilateral action (Minsky 1986c).

In Minsky's mind, all these concerns were interrelated and connected to the evolution of U.S. capitalism. Finance was central to the nation's economic challenges, but far from the whole story; money manager capitalism was the organizing concept that held everything together. The research constructs he relied on in earlier career phases were no longer sufficient: "To create a worthy successor to the financial system that served us so well between the 1930s and the 1980s requires a deeper look at our institutions than we have taken so far," wrote Minsky (1991, 16).

Capitalist Development

Minsky's "deeper look" came from constructing and applying a theory of capitalist development.

Minsky believed integrating the insights of Schumpeter and Keynes was possible because they had a common perception of the task of economics: "They each define the problem that economic theory must explain as the path of development of an accumulating capitalist economy through historical time" (Minsky 1986d, 285). From this perspective, the economy is a complex, time-dependent system—an "evolutionary beast," changing in response to endogenous as well as exogenous factors, not an equilibrium-seeking and -sustaining system (Minsky 1993b, 104; Ferri and Minsky 1992). Further, the economy's institutional structure is a fundamental determinant of the particular path of development; this structure—which is itself evolving—facilitates, influences, regulates and constrains economic activity (Minsky 1986a, 3-10).

Institutions of credit and finance are at the center of capitalist development. While standard economic theory emphasizes exchange, Minsky's recognition of historical time caused him to emphasize that production precedes exchange and that finance precedes production. "Because credit is essential to the process of development, a theory of economic development needs to integrate money into its basic formulation," he wrote. The result is an approach inconsistent with Walrasian theory: "Monetary factors cannot be added on after a prior or dominant model has determined the basic output and relative price variables" (Minsky 1990, 55).

Another essential element in Minsky's theory is the driving force of the profit motive. This motive was a vital component in Minsky's writings throughout his career. He had long argued that present and prospective profits influence economic activity within the context of a given institutional structure—and that the structure itself changes in response to profit seeking. As Minsky gave increasing attention to capitalist development, profit-driven structural change took on increasing importance in his writings (Minsky 1986b; Ferri and Minsky 1989, 135; Minsky 1993b).

Financial innovation is also an essential element in Minsky's theory—indeed, such innovation is a crucial determinant of institutional evolution. Scholars often observe Schumpeterian forces of creation and destruction in product markets and manufacturing processes, but Minsky emphasized that Schumpeter also gave attention to changes in financial systems. Minsky's theory stresses that financial markets evolve not only in response to the profit-driven activity of business leaders and individual investors, but also due to the profit-seeking entrepreneurialism of financial firms (Minsky 1986d; Minsky 1990; Minsky 1993b). In fact, Minsky (1993b, 106) wrote: "Nowhere are evolution, change and Schumpeterian entrepreneurship more evident than in banking and finance and nowhere is the drive for profits more clearly the factor making for change."

Government action—public policy—is the final key element in Minsky's theory of capitalist economic development. Policy decisions shape the institutional framework that conditions economic activity. As Minsky (1986a, 7) wrote in *SUE*, "Policy can change both the details and overall character of the economy." Thus, economists and policymakers must be concerned with the design of institutions as well as with economic activity within a set of institutions.

Since the economy evolves endogenously, no policy regime will provide a "once-and-for-all" solution to economic difficulties. In time, policies that once worked well may no longer be adequate, due to innovations in finance and business or to the emergence of new problems (Minsky 1986a, 293). Minsky recognized it is neither possible nor desirable for policymakers to engage constantly in major institutional reform, but he stressed that such change is essential when the public becomes greatly dissatisfied with economic performance (Minsky 1986a, 7).

From Commercial Capitalism to Money Manager Capitalism

In the early 1990s, Minsky published two major essays that applied his finance-driven theory of capitalist development to the United States (Minsky 1990; 1993b). They described an economy that evolved through four capitalist stages: commercial, financial, managerial, and money manager. His discussion of each stage centered on three questions: What is being financed? What is the pivotal source of financing? What is the balance of economic power between business and banking?

The stages begin with commercial capitalism, a period that involved the financing of goods in process, storage (inventories) or transit. Merchant banks and commercial banks provided this financing, while business owners usually used their own funds to acquire capital assets. Economic power was fragmented and dispersed.

Financial (or "finance") capitalism emerged to support the establishment and expansion of railroads, mills, and other industrial enterprises. The period saw the rise of investment banks and large corporations. During this stage, investment bankers came to hold a dominant position in the economy.

Managerial capitalism emerged in response to the Great Depression, which redirected the financial spotlight to macroeconomic revitalization. The New Deal and World War II moved the pivotal source of financing from the private sector to the federal government, where fiscal and monetary policy were expected to help ensure economic growth and stability. When the war ended, household and business indebtedness was minimal, and the balance of economic power favored corporate managers—who often operated in oligopolistic markets—not private bankers.

Money manager capitalism was a product of the success of managerial capitalism. In the prosperity and stability of the managerial era, employers offered pension plans to more and more workers. At the same time, financial institutions became increasingly aggressive in managing those retirement funds and the other asset holdings of individuals and organizations, especially in response to the inflation that was a byproduct of government efforts to prevent a deep recession. The maturing of managerial capitalism was accompanied by not only the evolution of a more fragile financial system (the focus of *SUE*), but also the growth pension funds, mutual funds, bank trust funds, and other managed-money funds.

During the long expansion that began in 1982, it became increasingly clear that money managers—institutional investors—were the new masters of the economy and their funds were the new pivotal source of financing. The aim of money managers, and the sole criterion by which they are judged, is maximization of the value of the resources entrusted to them. As a result, business leaders became increasingly sensitive to short-term profits and to the stock-market valuation of their enterprises.

Minsky's dissatisfaction with money manager capitalism is clear from both of his essays on the transition from commercial capitalism to the present era.[1] The rise of institutional investors encouraged further financial-system evolution by providing a ready pool of buyers for securitized loans, the commercial paper of finance companies, and other innovations. It also fueled the trend toward mergers, acquisitions, corporate breakups, leveraged buyouts and stock buybacks, since fund managers have a strong incentive to support whatever initiatives promise to boost near-term portfolio value; managed-money funds often provided the resources raiders needed to secure corporate control. The problem is that such trends exacerbated financial fragility. They were also disconnected from the generation of technological breakthroughs as well as from major product and process innovations. According to Minsky (1993b, 111-112):

> Keynes' famous remark about speculation and enterprise is especially relevant for money manager capitalism: "Speculators may do no harm as bubbles on a steady stream of enterprise. But the position is serious when enterprise becomes the bubble on a whirlpool of speculation. When the capital development of a country becomes the by-product of the activities of a casino, the job is likely to be ill-done."

Extensions and Further Applications

In the two essays described above, Minsky provided the historical analysis that served as the backdrop to the rest of his career. Nearly everything he published afterward can be seen as an examination, application, or extension of their themes. Money manager capitalism influenced his thinking about both economic theory and public policy.

An important extension of Minsky's analysis was offered in his two final journal articles. One summarizes an address he delivered upon receipt of the Veblen-Commons Award, conferred by the Association For Evolutionary Economics (Minsky 1996). The other, co-authored by Charles J. Whalen, appears in the *Journal of Post Keynesian Economics* (Minsky and Whalen 1996-1997). Both describe the connection between the rise of money managers and increasing worker insecurity.

The connection is as follows. Money-manager pressures—often in combination with the force exerted by growing international competition—encouraged corporate restructuring, downsizing, union avoidance, and job outsourcing. Even managers and highly skilled, "professional" employees soon faced a workplace in which productivity pressures and temporary employment were on the rise and where worker benefits, job ladders and training opportunities were being eliminated.

In short, worker insecurity and money manager capitalism are two sides of the same coin. As a team of U.S. researchers concluded in 1997, employment relations in this new era is characterized by a rush toward treating human resources as a cost to be minimized: corporate executives have increasingly come to view labor as just another "spot market" commodity (Cappelli et al. 1997).

A few years later, Whalen (2002) revisited Minsky's analysis, assessing it in the wake of the "dotcom" boom and bust.[2] He concludes that Minsky was correct in identifying money managers as major players in the new economy, especially given the explosive growth in mutual funds in the 1990s. Minsky was right that "block trading" in the money manager era added to market fragility and that institutional investors enabled corporate takeovers. Minsky was even on target with the suggestion that companies exhibited "an almost chronic need" to downsize and pursue workplace flexibility at the expense of worker security (Minsky 1996, 363); in fact, there was evidence this continued even when labor markets were tight at the peak of the boom (Whalen 2002).

Whalen's article also notes some unexpected developments. Minsky did not anticipate that many institutional investors would use their power to change corporations from within, but that is what happened.[3] Minsky also did not foresee either the tremendous growth of venture capital financing or the investment-led boom of the late 1990s. Indeed, at first blush the high-technology developments of that era seem incompatible with Minsky's analysis, which suggested that technological dynamism in the money manager era would require substantial state assistance. However, Whalen finds a partial explanation in the work of Barry Bluestone and Bennett Harrison (2000), who described the boom as the long-awaited information revolution that government initiated and supported for decades (Whalen 2002).

Minsky's notion of money manager capitalism has received increased attention in the wake of the recent global financial crisis and subsequent Great Recession (which is still ongoing in the United States and other countries as of this writing). L. Randall Wray (2009) presents perhaps the best examination of the rise and fall of the money manager era. After reviewing Minsky's analysis of American capitalism's earlier stages, Wray provides a detailed account of how financial-sector innovators and policymakers put the entire global economy at risk. Special attention is given to the relationship of money managers to securitization, credit default swaps, and commodities futures contracts. Wray also explores the role of three crisis triggers: interest rates, commodity prices and tax revenue.[4]

To be sure, while Minsky may have been among the first, he is not the only scholar to highlight the rise of institutional investors.[5] And his attention to money manager capitalism has considerable overlap with the burgeoning literature on "financialization."[6] Nevertheless, it is clear that the study of money manager capitalism is essential to understanding not only the economics of Minsky, but also the contemporary world economy.

Notes

1. For an even earlier discussion critical of the economic impact of money managers, see Minsky (1986d, 291).

2. Whalen also fleshed out Minsky's analysis in a separate article; see Whalen (2001).

3. See also Useem (1996).

4. For more on Wray's interpretation of Minsky's analysis and its applicability to the Great Recession, see Nersisyan and Wray (2010); for a complementary interpretation as well as a discussion of public policy designed to promote economic recovery and reform, see Whalen (2010); and for a look at developing countries in the context of money manager capitalism, see Ventimiglia and Tavasci (2010).

5. Others highlighting institutional investors include Useem (1996) and Hawley and Williams (2000).

6. On "financialization," see, for example, Palley (2007). For a discussion of the overlap between Minsky's economics and financialization, with special attention to the problem of inequality, see Zalewski and Whalen (2010).

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