Labouring finance: who pays for firms' debt in transitional capitalism?

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(preliminary and incomplete)

The purpose of this paper

The fact that the GFC has had an impact on employment is no surprise. In this paper I attempt to draw some lessons from the GFC experience of Eastern European transitional economies. I focus on one particularly outcome, which I believe is important to understand the current modality of articulation of the finance-labour nexus in some contemporary forms of global capitalism: among firms that went through mass layoffs, firms experiencing sharp changes in their ability to meet fixed assets investments with their internal funds laid off high human capital employees (permanent and skilled), thus contradicting theoretical human capital theories à' la Becker. In so doing, the GFC hints at some fundamental transformation that the process of firms' financialization has initiated in emerging economies of Central and Eastern Europe.

The always historically specific character of the way capitalism values labour, which is emphasized by Marx in Capital (p. 290), confirms the need to explore in further details the nature of the finance-labour nexus.

Transitional capitalism: the 1990s

- A higher level of decentralization occurred in the early 1990s with private credit developing
- Trade liberalization
- Central to CEE economies' experience of a transition to capitalism is the transformation of the labour markets with the rapid spread of temporary employment.
- Integration in GPN: salient features

(i) Attempts to diversify production and move away from traditional sectors (resource intensive or labour intensive industries.

(ii) The main weakness in this period is still the relative underdevelopment of capital-intensive industries.

(iii) Desire to attract foreign direct investment. FDIs were particularly important in the manufacturing industries of the Central European countries (Czech Republic, Hungary, Poland, Slovakia and Slovenia).

(iv) Increasing exposure of firms to financial markets.

A "qualitative division of labour" within Europe.

- Since the early 1990s the patterns of CEEs' trade with the European Union were characterized by an international division of the production process (i.e. the international splitting of the value added chain)

- The entry into regional global markets means a reorganization of production towards vertical specialization along comparative advantages that are specific to particular stages of production (upstream or downstream stages).

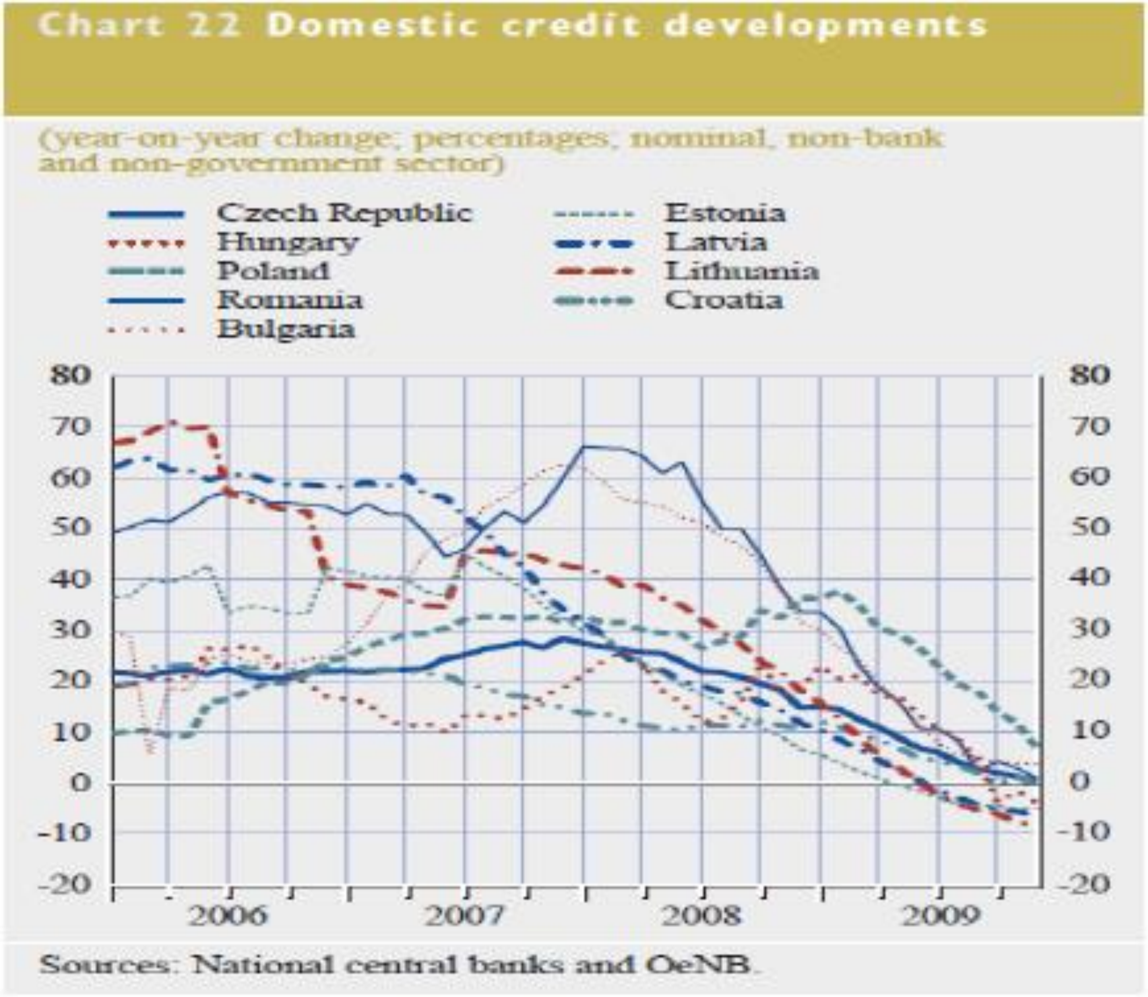
- The integration of these economies in global production chains involved an ever-deeper specialization of their trade patterns compared to pre-transition era.

- To understand the dependence to financial markets that these CEE firms were developing, it is important to emphasize that these economies' comparative advantages were still located at the two ends of the production process: in upstream production (primary goods) and in downstream production (consumption goods); disadvantages were located in intermediate and capital goods. In fact these economies lacked competitiveness in the production of investment goods.

1997-2007

- Between 1997 and 2007, a period of general overall macroeconomic stability, but increasing financial volatility and risk (the Great Moderation), these economies showed distinctively positive performance indicators, particularly in terms of economic growth and inflation.
- Despite these positive indicators there were growing concerns arising from rising global imbalances, exploding asset prices, rapidly growing leverage in all sectors, but particularly in the domestic financial sector, in the households credit sector and in the business credit sector, and an emerging sub-prime crisis as signalled by the number of mortgage delinquencies of loans originating between 2000 and 2007.
- According to Mark Allen (IMF) deleveraging became an imperative spread among financial and non-financial firms in CEE economies.

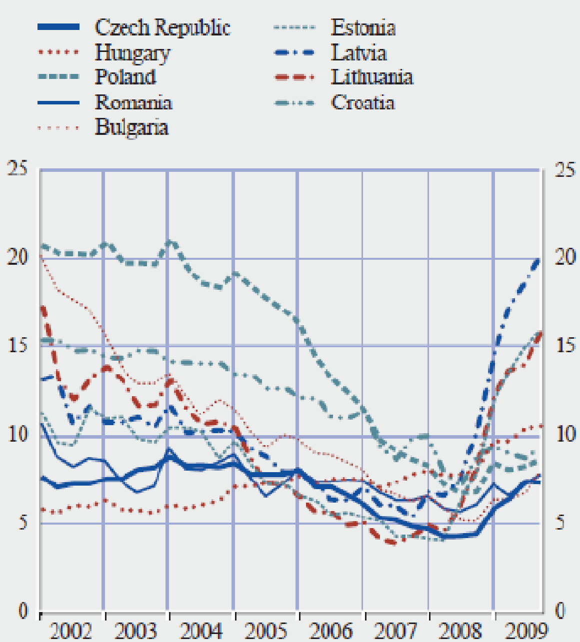
Source: Gardo' and Martin (2010)



Aggregate labour market effects of the GFC in CEE economies

Chart 29 Unemployment rates in CESEE

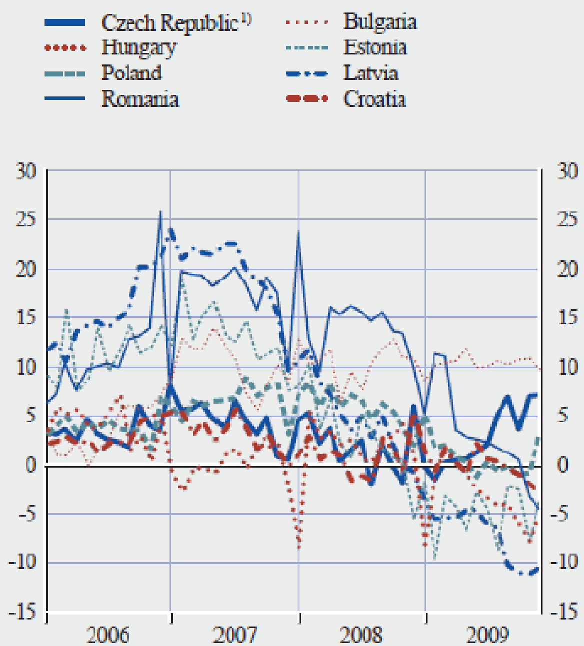
(percentage)



Sources: Eurostat and OeNB.

Chart 30 Wage developments in CESEE

(real gross wages; whole economy; monthly average; year-on-year; in percentage; HICP-deflated)



Sources: WIIW, National statistical offices and OeNB.
1) Czech Republic = wages in industry.

The GFC as a lens

I agreement with Bryan et al., (2009) I use the GFC "beyond the excesses of the sub-prime crisis".

I propose that the GFC is a lens through which processes of transformation of capitalist economies can be observed and questioned.

Understanding the employment effects of the GFC in Eastern European economies serves here the scope of shedding light on the way financialization reshapes the relationship between labour and capital during crucial phases such as transition to global capitalism.

What is the impact of firms' financial distress on firms' labour demand?

- Financial markets' distress transmits to firms because credit restrictions impact directly on firms' financial constraints
- Credit restrictions also affect firms' leverage: as interest rates rise net worth falls and so the ratio of debt to net worth rises.
- Managerial aversion to leverage may exacerbate the effect of leverage on firms' strategies to reduce costs and increase efficiency.

(iii) *Predominance of external finance to purchase fixed assets*: Over the current fiscal year, the estimated proportion of this establishment's total purchase of fixed assets that were financed from internal funds or retained earnings was 50% or lower.

Firms' leverage and labour demand

To test these arguments:

- Nickell and Wadhwani (1991) and Nickell and Nicolitsas (1999), both studies of UK quoted firms,
- Ogawa (2003), focuses on Japanese .
- Cantor (1990) focused on the US corporate sector to conclude that leverage significantly alters the manner in which firms respond to demand shocks.
- Brown et al. (1992) show that high-leveraged firms cut employment and capital expenditures more than low-leveraged firms during periods of substantial decline in operating returns.
- Sharpe (1994): an increase in financial leverage increases the sensitivity of the macroeconomy to demand shocks in a sample of US firms.
- Funke et al. (1999) finds similar results in as et of German firms.
- Heisz and LaRochelle-Cote (2004): a set of Canadian firms.

A particular modality of employment adjustments

- Among firms that went through mass layoffs, firms experiencing sharp changes in their ability to meet fixed assets investments with their internal funds laid off high human capital employees, in this context permanent workers and FT skilled production workers (as opposed to unskilled production workers).

- This result confirms the one that Milanez (2012) recently found in a sample of Californian firms between 2006 and 2011.

- Both these papers contradict theoretical human capital theories à la Becker, according to whom firms would lay off workers in inverse order of the amount of accumulated human capital. Furthermore, these results question the traditional interpretation of temporary employment contracts as a way capitalist firms respond to fluctuations in product demand.

In pursuing an interpretation key of the finance-labour nexus the way it emerges in these economies, I face a number of challenging questions: Are skilled individuals more likely to be fired because they are equivalent to less skilled workers?

The idea of a reduction of complex labour into simple labour happens, according to the Uno School, in the context of the production-process of capital (Itoh, 1987, p. 39).

If so, does firms' exposure to financial markets operates a homogenization of labour against the tendency, often perceived as fundamental for the operation of global capital, towards workers' segmentation (Bowles and Gintis, 1977)?

Is this indifferentiation (between skilled and unskilled labour and between temporary and permanent workers), the hyperbolic product of a process of differentiation of labour carried out by all neo-liberal apparatuses in the way envisioned by Negri (1989)?

And again, is the reduction of skilled labour to unskilled labour an exception to an old rule (e.g., human capital is valuable) or rather a rule in a new context in which capitalist firms are called to operate?

If the latter hypothesis has to be pursued, are we facing the passage envisioned by Foucault from a localized and stable organization of economic power centred around one "culture" (e.g., neo-liberal culture of entrepreneurship and human capital), to an unstable set of heterogeneous technologies that produce and manage labour and labour relationships through market competition (Foucault, 1994)?

GPN integration: a new theory of development

GPNs are rapidly reshaping the lexicon of economic development

Development is becoming synonymous with economic upgrading, a process whereby complex economic actors such as firms, rather than nations as a whole, are recipient of the main advantages that derive from economic integration.

Economic upgrading, a process that allows firms to climb a series of horizontal and vertical ladders both within and between production networks so to get to produce more advanced products and to operate in higher productivity/higher value added segments of global production, shapes the economic culture in transitional economies (Milberg and Winkler, 2010).

Not surprisingly, the new development theories named as Compressed Development, rather than simply questioning the relevance of traditional factors deemed responsible for integration in trade flows, have attempted to explain the rapid integration of some firms and the exclusion of others into global production networks.

Labour and capital in GPNs

Despite the central role that labour plays in the creation of value in GPNs, labour issue have been relatively neglected in studies of global value networks (Carswell and De Neve, 2013).

This is somehow paradoxical if we think that all the various routes through which economic upgrading can take place, namely process upgrading, product upgrading, functional upgrading and intersectoral upgrading (Gibbon and Ponte, 2005) rely on complex processes of technological innovation where skilled labour is an input of production complementary to capital and technology.

The point I want to stress is that GPNs reveal labour's proximity to capital. As Carswell and De Neve write on p. 103: "Fundamentally in this new order, a country's ability to generate highly skilled competencies and skilled personnel becomes its greatest asset in being able to positively integrate into global value chains, to gain control over new competencies and shift functions and places within a value chain, to create barriers to entry, and finally, to ensure upward income distribution through successful participation in such value chains."

In GPNs, the sorts of skilled workers and the firm are becoming one. The purpose is the creation of barriers to entry, so that rents can be produced and eventually shared.

In this context, human capital is not automatically rewarded for its contribution to production. Rather, "the spatial and vertical distribution of profit and incomes within global value chains should be viewed as indicators of barriers to entry". The idea of labour as a contributor to rent creation is here clear. Less clear is how rent distribution is informed by traditional concepts of skill and human capital. Given that human capital is valuable only to the extent that it contributes to produce rents, the problem is rent creation rather than "an unequal (i.e. unfair) exchange or unfair appropriation of profit by leading firms" (Carswell and De Neve, 2013, p. 103).

The examples of failed upgrading into high value segment of the GPNs are numerous (clothing production process in Ukraine, or Taiwanese firms' integration into electronic manufacturing in the 1970s.

The possibility of failure is what makes the evaluation of human capital an ex-post rather than an ex-ante matter. Any attempt to succeed in economic upgrading requires firms' access to financial markets and accumulation of debt.

Failure to produce economic upgrading makes skilled labour equivalent to unskilled labour. The precarious status of skill and human capital in GPNs emerges from the dispossession of labour of its skill: while skilled labour is at the heart of any successful climbing of the value ladder, the result is always open, fluid and subject to change as dictated by market competition.

It is in this context that the GFC reveals the tendency of capitalism to reduce all types of labour to simple labour and the role that finance plays in this reductio ad unum.

Skilled and unskilled labour in GPNs are organized around a particular sort of technology, or machine (Deleuze, 1995, p.180), which tends to abstract bodies from skill. GPNs make these machines of control visible as they manifest the fluidity of capital and labour alike in financialized firms--the financing of labour.