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Keynes' Social Vision and Financialization

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Beyond his immeasurable contributions to positive economics, Keynes also presented a singular social vision built on his economic thought. Predicting that a policy of permanently low interest rates could "[keep] us permanently in a quasi-boom," Keynes declared that this prolonged state of full-employment could possibly lead to full investment, a state in which no new real asset investment would carry a net marginal benefit, in the United States and United Kingdom in "twenty-five years or less [from 1936]" (The General Theory 159, 160). He therefore declared that "the rentier aspect of capitalism [is] a transitional phase," as full real asset investment will "mean the euthanasia of the rentier, and, consequently, the euthanasia of the cumulative oppressive power of the capitalist to exploit the scarcity-value of capital" (The General Theory 186). He promised that this vision would come about as long as we continued to worship "avarice and usury and precaution…for a little longer still," before "[reaching] our destination of economic bliss" (Economic Possibilities 7).

With less than a decade until the centenary of Economic Possibilities, by which time we are supposed to be "at least be within sight" of this Keynesian utopia (Economic Possibilities 4), I attempt to assess Keynes' vision of the utopian society and the conception of the euthanasia of the rentier he saw arising from full real asset investment, in light of economic history and theoretical advances since The General Theory and Economic Possibilities. Unfortunately, I conclude a crucial assumption of the economic logic behind Keynes' predictions is not empirically validated, and that the Keynesian utopia therefore remains very distant.

The fundamental nucleus of Keynes' idea, that the end of investment in real assets is the end stage of the capitalist economy, has been proven right by subsequent economic developments. In recent years, governments in advanced economies have struggled with the increasing ineffectiveness of conventional monetary policy due to the secular decline of real interest rates. The seriousness of this limitation of monetary policy is reflected in the fact that the zero lower bound problem is no longer a theoretical curiosity but a serious policy issue (Kocherlakota 2017).

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Taiwanese Foreign Investment Regulations—An Analysis

CHRISTIAN HEINZIG

To support economic development in Taiwan, President Tsai Ing-wen's administration encourages foreign investment into the island, such as buying or selling stocks and bonds. In the first half of 2022, foreign investment into Taiwan jumped 275% from a year prior, gaining more than $8 billion and setting the scene for 2022's foreign investment to reach a 15-year high. To regulate foreign investment, Taiwan's government passed the Acts Governing Investment in Taiwan by Overseas Chinese and Foreign Nationals (referred to in this analysis as "Regulation 1") and the Act Governing Relations Between Peoples of the Taiwan Area and the Mainland Area (referred to as "Regulation 2"). Interestingly, the two regulations favor Overseas Chinese and Foreign Nationals, who reside outside Taiwan, and domestic companies within Taiwan over Mainland Area Investors, which ultimately decreases Mainland Chinese influence in Taiwanese companies. This comparison matters because it highlights that, in Taiwan, an investor's affiliation significantly determines their investment advantages and disadvantages.

Regulation 1 contains an amendment called "Article 4-1" that does not exist in Regulation 2. Article 4-1 exempts Offshore Overseas Chinese and Foreign Nationals from regulations if their investments in corporate bonds, non-equity-type financial bonds, and trust fund beneficial certificates do not involve finalizing payback and/or interest payments against Taiwan's currency. With unregulated investments in these bonds and certificates, Offshore Overseas Chinese and Foreign Nationals benefit from bonds that are liquid, diverse, and less volatile than stocks, and from gaining more control over the management of their assets.

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Economics Advising Office's Blog: http://uwecon.wordpress.com

Experience Economics

Economics students at the University of Washington have various opportunities to explore their passions beyond the classroom. We've invited one of our members, Srinandan Ramachandran, to tell us more about his Study Abroad experience.

Study Abroad at the UW Rome Center

SRINANDAN RAMACHANDRAN

This quarter, I had the opportunity to study at the UW Rome Center, and my friends at the EUB have asked me to share my experience. The program I attended was called Biology Rome: Ecology of the Mediterranean led by Professor Kenneth Sebens, one of the world's most prominent scientists and the former director of Friday Harbor Laboratories. The curriculum included coursework in ecology, Italian, scientific writing, and frequent field excursions. My Italian and Scientific Writing instructors taught me insights into the culture of their country that I otherwise may not have picked up naturally.

My passion is the intersection between economics and environmental studies, so when I saw this opportunity, I quickly jumped at it. As an underclassman, I had tried to apply to study abroad programs, but they had been canceled due to COVID. This was the program's first year and there was a lot of uncertainty leading up to the departure date. Nevertheless, the Rome Center staff was kind and accommodating, and my move-in went smoothly. I had three other roommates: one was in my program, and the other two were engineering students.

The UW Rome Center is near Campo de' Fiori, a marketplace in Rome. The building is centuries older than the Seattle campus, but since it has been renovated, it looks brand new on the inside. It is centrally located in the heart of Rome, close to famous sites such as the Colosseum, the Trevi Fountain, and the Pantheon.

I had the chance to travel all over Italy, visit cutting-edge aquatic research centers, and learn from one of the top experts in the world. A large portion of what I did was providing Professor Sebens with reports on the current scientific literature on the Mediterranean Sea. While I often had to study extra hard to keep up with the main ecology class, I felt that my economics classes, particularly ECON 230 (Fishery Economics), gave me a unique perspective on the problems confronting the Mediterranean Sea. In particular, I was able to look into the impact of invasive lionfish and seagrasses in the Mediterranean beyond biological factors and think about the role economics and public policy play in shaping solutions.

In my spare time, I enjoyed being a tourist. Italy has an excellent train system, and I stayed in hostels to minimize costs. I traveled all over Italy, including Florence, Milan, Amalfi, and Venice. The highlights of my trip were hiking the whole Cinque Terre trail in one day and a weekend excursion to Ischia, a small island off the coast of Naples. I had the chance to eat a multi-course Italian dinner, snorkel at two different sites, and get some dance lessons.

I consider myself extremely fortunate and grateful to have had this opportunity. I would also like to thank Professor Turnovsky and the EUB, Professor Sebens, and the UW Rome Center staff. If you can do so, I highly recommend exploring study abroad programs both within and beyond the Economics department.

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This phenomenon reflects the inexorable slowing of real asset investment as returns on real asset investment decrease in highly advanced economies (Summers 2014). The theory of secular stagnation points to declining population growth and declines in the capital requirements of new technologies, among other causes, to suggest that real asset investment is declining, causing GDP growth to slide. Secular stagnation theory contends that the neutral real interest rate has dropped out of reach of conventional central banking interventions. Rachel and Smith (2015) estimate that since the 1980s, shifts in the level of desired investment have caused the real risk-free interest rate to drop by 150 basis points, demographic shifts have caused a further drop of 90 basis points, and that shifts in capital intensity may also have caused drops, supporting Summers' contentions. In large part due to decreases in demand for capital for investment and long-term demographic trends impacting investment, real interest rates are facing substantial secular decreases, seemingly suggesting that Keynes' prediction of full investment is close to being fulfilled. Still, it is important to note that other factors like inequality and increased savings may also contribute to interest rate declines.

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Nonetheless, in equating full investment with the euthanasia of the rentier, Keynes implicitly assumes that there is no demand for capital at full investment, yet this is not borne out by empirical evidence. Pollin (1996) found that from 1982 to 1990, the ratio of internal corporate funds in America to capital investments exceeded 100%, which is to say, none of the growth in corporate debt was needed to finance real asset investment expenditures. According to Pollin (1996), driven by mergers and acquisitions, the ratio of corporate borrowing to capital expenses rose from 1982 to 1990, in spite of high real interest rates and ample internal funds for real asset investments. The disconnect between real asset investment and demand for capital presents a difficulty for Keynes, as it suggests that the scarcity of capital may be sustained past full real asset investment with demands for capital for speculative purposes.

Summers (2014) notes that depressed real interest rates encourage greater risk-taking, thereby causing "greater reliance on Ponzi finance and increased financial instability." Therefore, financialization naturally accelerates when investment decreases, mediated by interest rate mechanisms. Pollin (1996) and Rachel and Smith (2015) further note that short-termism, as encouraged by the incentive and organizational structure of publicly-traded companies, may be one of the factors depressing real asset investments and encouraging this financialization.

It seems then, that the rentier has managed to dodge its euthanasia, freeing itself from the bonds of real asset investment through financialization. Keynes' optimistic notion of the natural evolution towards the euthanasia of the rentier, or any possibility of the euthanasia of the rentier, has to be discarded. For better or worse, financialization is already too deeply embedded in the economy to be fully excised and it is certainly infeasible from the perspective of political economy.

The defining characteristic of the financial sector is its fragility, far more so than real asset investment (Minsky 1992; Sen 2020). As financialization supplants real asset investment, it causes more frequent and more severe economic crises as the financial sector, with its inherently fragile and unstable nature, grows to undergird more and more of the economy. In Minskyan terms, the economy is moving into the money-manager stage and taking on all the attendant new risks.

The end of real asset investment remains in the indeterminate future, but is approaching rapidly. As advanced economies transition into the era of full financialization, the outlook is considerably more dismal than Keynes' hopes. Keynes predicted that the greatest social concern of this age would be how to grapple with an overwhelming abundance of leisure and material. Instead, advanced economies are faced with the new economic dangers of financialization and its continual crises. Without a radical expansion of our economic imagination, Keynes' utopia is out of reach.

Sources for information in this article can be provided upon request

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Furthermore, according to Article 4-1, Taiwan's government guarantees that they do not collect their share of interest income tax from the issuance of corporate bonds if the bonds are held to the coupon date, sold to a domestic bond dealer, or traded outside Taiwan with other offshore investors. Domestic corporate bond issuers benefit because they can avoid interest income tax, which means there is more money in their pockets.

Through the legal framework of Article 4-1, Taiwan's government incentivizes domestic issuers to issue bonds—instead of stocks—which limits foreign ownership in Taiwanese companies, especially Mainland Chinese ownership. By not applying Article 4-1 to Mainland Area Investors, Taiwan's government discourages issuing companies from working with them since that would incur interest income tax.

Regulation 1 also contains an amendment called "Article 5" that does not exist in Regulation 2. Article 5 exempts domestic issuing companies from regulations on investments they receive from Overseas Chinese and Foreign Nationals. The issuing company may issue overseas convertible corporate bonds, overseas corporate bonds with warrants, overseas stocks, or overseas depositary receipts. With overseas convertible corporate bonds, issuing companies benefit because they can save money on their interest payments, achieve interest tax savings, and have the option to defer their stock dilution. With overseas corporate bonds with warrants, issuing companies can benefit from high returns in the long-run, benefit from a low-cost alternative investment option to standard stocks, and manage their capital assets better by accumulating gradually instead of immediately by margin or credit. With overseas stocks, issuing companies benefit because they can buy the currencies that the stocks are quoted in, which helps to neutralize currency fluctuations as well as take advantage of the market cycles of different countries. With overseas depositary receipts, issuing companies can raise foreign capital, increase their global visibility, and receive gain beyond just the capital gains and the dividends from the shares with a favorable exchange rate movement.

Through the legal framework of Article 5, Taiwan's government protects its domestic issuing companies by not

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having them bear any significant costs from regulations, and benefits by receiving foreign investment from more favored investors—Overseas Chinese and Foreign Nationals. By not applying Article 5 to Mainland Area Investors, Taiwan's government sends the message that investment interactions with Mainland China should be avoided altogether.

Clearly, these regulations favor Overseas Chinese and Foreign Nationals, reduce Mainland Chinese influence in Taiwan's foreign investments, and restore more autonomy to domestic companies. Researchers, investors, companies, and others involved in Taiwanese foreign investment can apply this insight to make more informed decisions about their investments, such as taking advantage of interest income tax exemptions. Moreover, if Taiwan's government continues to stringently regulate Mainland Area Investors, then they can generate more tax revenue and invest that capital into domestic industries that need it, such as the expensive and evolving semiconductor industry. This industry acts as the backbone of the digital economy and influences nearly every aspect of modern life. Taiwan accounts for 100% of installed capacity to mass produce high-end semiconductors at technologies below 7 nanometers, which the United States' military relies heavily on. If the semiconductor industry suffers supply chain disruptions or needs to establish new fabrication facilities, it requires billions of dollars to do so—and a portion of that funding can come from the tax revenue attached to these regulations.

Although foreign investors in Taiwan often complain that the island's regulations are absurdly bureaucratic, they nonetheless agree that such regulations help to mitigate the uncertainty of the way the government will treat their investments. Investment already entails risks, but by investing in a country like Taiwan that has the advantage of an established regulatory regime, investors can minimize those risks. That, along with many other reasons, is what distinguishes Taiwan as a fierce competitor when it comes to foreign investment.

Sources for information in this article can be provided upon request

UPCOMING EVENTS:

Economics Undergraduate Survey: In Winter Quarter the EUB will be carrying out a survey of economics students to get feedback about the program directly from you. Keep an eye out for it in your email.

Economics Tutoring: The EUB offers free tutoring every weekday at various times every quarter! Check the schedule on the EUB website to see tutoring times. If you need help with an upper level class, however, make sure you check the website to see which tutor can help.

Contribute to the Economizer: The Economizer will be seeking guest writers for our Winter Quarter issue. Interested writers should check their emails from the department in early Winter quarter for submission instructions.

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