

## Chapter XIII. The dilemmas of the prosthetics of modern capitalism

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In the beginning, capitalism was a superior hunter in a paradise of abundant prey of productive, employment-generating spending. This enabled huge profits for a great number of firms in the productive economy. But not before long, it began to suffer under the barrier of deficient productive spending. The limitation of ongoing prey reproduction – employment-generating spending being the prey –, like in any predator-prey-system became a disturbing feature of the *conditio capitalistica*. Violent wealth procurement, protectionism, expropriations, taxes, and redistributive debt were used to prosthetically bring up “prey”. Goods procurement by external violence and protectionism became the preferred prosthetic means of a privileged group of the fastest developing and strongest capitalist countries with an edge over peripheral regions. Domestic taxation and expropriations were of additional, albeit limited, effect.

However, prosthetic spending funded by violence and protectionism depends upon hinterlands that remain subservient, but still possess enough funds to sufficiently function in a complementary way. This condition faded away as times went by. Hinterlands’ absorption potential shrank relative to the hunger of the metropolises, and, equally importantly, the hinterlands no longer wanted to remain subservient and complementary hinterlands. They rebelled against the metropolises and liberated themselves. In fact, formerly important hinterlands (e.g., Brazil, Argentina, Japan, Korea, China, Vietnam, etc.) became symmetric competitive capitalist predators and also went out to worldwide hunt for the same prey – employment-generating spending – abroad that the metropolises were after.<sup>1</sup>

Redistributive spending via taxation and expropriations had always only worked where the recipient of the appropriated money had a higher propensity for productive spending than the money-dispatcher. Debt-based redistributive prosthetic employment-generating spending, even largely lost its over-all effect if the debt was

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1 “Countries, willing and able to run offsetting external deficits do not exist” (Wolf, China’s tough fight to escape its debt trap, in: *Financial Times* of 12 April 2017.

repaid with interest, which it normally had to. Then only a small net gain for employment-generating spending remained. Structurally, debt, too, was an apt means to generate aggregated additional prosthetic employment-generating spending over time only, if, while the individual debt might be repaid, there was a continuous aggregate net debt build-up, a growing debt mountain. Continuous debt build-up, though, also requires plentiful or inexhaustible funds of money and lenders willing to hand out loans and holding the resulting debt-claims in the long term. This condition did not sufficiently exist as long as commodity money, gold and silver, was the base money as the mining of precious metals did not provide sufficient relief; physical alchemy failed constantly. Thus, when capitalism was being re-activated and European powers began to fight out their rivalry since around 1500, it was most welcomed by them that a kind of financial alchemy was discovered by private banks in the form of fractional reserves credit money creation, be it as bank notes, token coins or credit entries on bank accounts. Already this first artificial gland added a thick layer of credit money to the commodity money base, enabled a more voluminous debt build-up and extended prosthetic options. How private bank credit money creation could be managed to best fit to the needs of states was the subject matter of the two famous monetary debates in Great Britain between the Bullionists and the Anti-bullionists and the Currency school and the Banking school. If the states welcomed private bank credit money creation to enable the debt-financing of capitalist growth and of their colonial or imperial wars, they were still fearsomely aware that the greed of private banks might yet ruin the precious money creation gland. So, states had to defend this gland against their inventors through fractional reserves requirements, policing banks, selecting one bank as their central bank and allying with it in particular. They adjusted their stand to changing situations. In the frequent times of war, they preferred the risks involved in overstretching bank credit money creation to the risk of losing the war and mostly recklessly encouraged banks to create more credit money. They would then even oftentimes issue state credit money or, sometimes, state fiat money in addition. When peace was restored, states would, though, at first go back to convertible credit money, i.e., to commodity money as the base money again. This was repeated after World War I and even until World War II.

But in 1971, the US undid its return to commodity money of after World War II, and generally switched into a state fiat money regime. State fiat money, thus, became the new base money. Other states followed suit and established their monetary sovereignty. Noteworthy, this change left private bank credit money creation unaffected – only the underlying base money was changed to state fiat money. Hence, the tandem in money creation of private banks and the central bank could remain in place; it became only more powerful than before. The state established a fiat money currency and provided a basic money volume of it. In times of normalcy, private banks would create further money by fractional reserve bank credit money creation above this base. As, theoretically, any amount of the new base money could now be

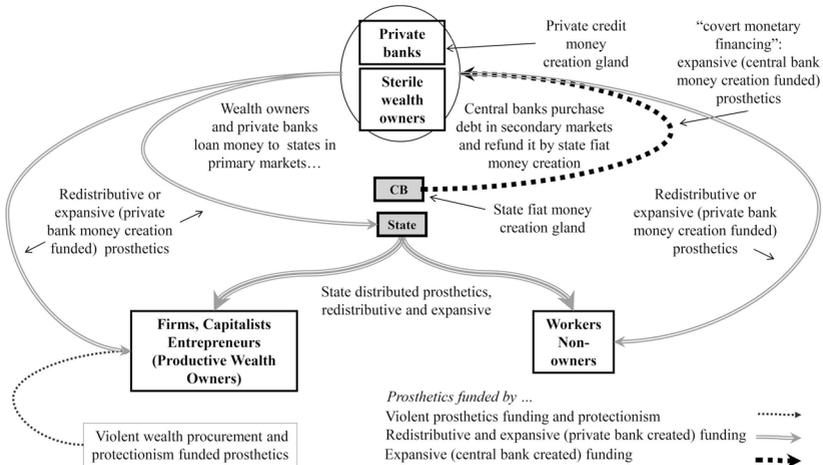
procured at discretion by the state, the bail-out of private banks, if they should get into trouble, had become much easier, too. Accordingly, more liberal reserve fractions could be allowed and a more generous spirit imbued the tandem system. In addition, of course, states retained the option to make further use of their own fiat state money creation gland as an *ultima ratio* reserve money creation facility if private bank credit money creation was insufficient.

At some point, a crucial *novel use* of the state fiat money creation gland in this tandem was discovered. The output of private bank money creation had always been, first, money on the one side, and, second, debt on the other side, which was tradable. The state and the central bank now found out that the central bank could purchase this tradable debt with newly created state fiat money. The baby was initially baptized “open market policies”. At first, it only appeared to be a tool of influencing interest rates and to steer the economy through a corridor between inflation and deflation. That implied that central banks would buy and sell debt according to economic cycles. The idea was that their debt holdings would somewhat grow in deflations and drop back to near zero in inflations (which was mostly conceptually identified with depressions and booms). But babies grow up and the adolescence of the baby “open market policies” consisted in central banks beginning to use debt purchases to stabilize the continuous prosthetic debt build-up by providing market liquidity and “shiftability” (de-investment in loans by individual investors without the loan having to be repaid as such) as “market-maker” or “dealer of last resort”. The ascent of this second reason to hold debt raised the volumes on central banks’ balance sheets visibly. But the evolution of the baby did not stop here. It reached adulthood with the rather recent discovery that the debt, which had arrived at central banks, could stay there for a very long time or for good, and that central banks could be “debt holders” and “debt financiers of the last resort”. Thereby a method had been contrived, by which significant volumes of money could be created *independent of private creditors’ appetite to hold debt lastingly*. After this upgrading of the monetary arsenal, in fact, theoretically nothing was in the way to autonomously procure the needed continuous flows of prosthetic employment-generating spending.

At this juncture, one might say that the state had, in fact, acquired the means to assume the role of wealth owners in Quesnay’s tableau and to purchase the parts of the annual produce, which would otherwise go unsold. Thereby, all capitalist circuits could be closed and the wheels of the machinery could be kept turning, independently of the old-fashioned means of goods procurement by violence, protectionism, domestic taxation and expropriations. States had availed themselves with a new means, which consisted of a novel type of financial transactions. The main form of ancient prosthetics had consisted in the subjugation of foreign tribes and countries and had necessitated ugly “hinterlands”. Modern protectionism, colonialism and imperialism, too, could not operate without creating ugly losing “hinterlands”, with, in fact, even a certain remaining risk of things being

turned upside down – in antiquity as well as in modernity. State fiat money creation, e.g., by central banks buying up sovereign debt from privates with newly created money, at first, rendered the funding of prosthetics independent of foreign countries; violent victimization disappeared and the funding of prosthetics became, like taxation and debt build-up, a purely national and peaceful nice and clean affair. The following tableau shows the economy with this triangle, which makes “milk and honey” flow. It builds upon the original “naked” tableau of “original” capitalism (on page 122) and superimposes prosthetic layers, including the debt build-up, which is enabled by central bank debt purchases and funded by state fiat money creation. *First*, it shows redistributive prosthetic debt (out of existing money, i.e., without money creation) and expansive prosthetic debt financed by private bank credit money creation; this money flows from wealth owners and banks to firms, workers and the state in the form of loans. Due to its combined redistributive and expansive character these loans are shown in thin parallel lines. If central banks purchase existing loans made to states (sovereign debt), or to wealth owners or workers (private debt), then they refinance these loans by state fiat money creation. When they resell the debt to private wealth owners, the newly created state fiat money is abolished once again. Yet, as central banks transform from being “market makers” or “dealers of last resort” to becoming “debt holders” and “debt financers of the last resort” by holding debt lastingly (even if the individual debt is rolled over occasionally), state fiat money creation becomes permanent. The time comes at which wealth owners and banks, when they initially grant loans to states, firms, or workers already expect to soon sell this debt to the central bank. From that point forward, the new debt is in fact funded by state fiat money creation. The evolving cycle between wealth owners and banks, making loans to the state (or privates) and the central bank buying these loans is, *second*, shown in two arrows with *thick dotted lines*. In the *third* place, the tableau shows the state forwarding prosthetics (funded in any forms) to employment-generating wealth owners (firms) and workers in a triple grey line. Prosthetics resulting from protectionism and coming from abroad are, *forth*, shown in the lower left-hand corner. Purchases of firms’ and workers’ debt by the central bank are not shown.

Figure 25: Tableau of capitalism including redistributive and expansive prosthetic spending



The break-through for massive, continued debt holding by central banks took place after the financial crisis of 2008. Since then, they buy great volumes of debt knowing (or they should at least know!) that it will stay on their balance sheets for a long time or forever, or, at least, not leave again in a normal way (i.e., other than by a debt jubilee or a currency reform or substitutes). They, thereby, refinance debt issues to private wealth owners and banks and refund the liquidity to them, which they may possibly use to finance the next round of debt issues. As private wealth owners and banks make their outlays first, and central banks restate them only thereafter, central banks now use “guidance” and publicly announce their intent to buy certain volumes of newly issued debt to induce privates to sign the debt in the first place. The expected later central bank debt purchases, by which they keep their commitments (the dotted black line on the right-hand side), thus, are the real causes for the previous loans by wealth owners and private banks (the dotted arrow on the left-hand side).<sup>2</sup> As is common in economics, the chronologically second step – debt purchases by the central bank in secondary markets – is causally and logically the first step. The expectation of the later debt purchases by the central bank induce wealth owners and banks to make the initial loans, for which state fiat money creation will provide the lasting financing.

2 The relationship between bond purchases by central banks and sovereign debt issues is highly transparent. E.g., writes the *Financial Times* of 5 June 2020 on the ECB’s €1.35 trn. pandemic emergency purchase program on its front page: “Some investors had been concerned that the ECB’s initial bond-buying plan would be insufficient to soak up the €1tn-€1.5tn of extra debt that eurozone governments are expected to issue this year...”.

The more voluminous and the more lastingly central banks hold debt, the more they transmute to financiers of last resort. As they have no  $M-C-M'$ -desires and are not subjected to a financial survival constraint, they are free of concerns that the assembled loan claims (workers' debt, firms' debt, sovereign debt, or sterile wealth owners' debt) might not be honored. Capitalism creates a general and strict discipline of rationality through  $M-C-M'$  in one sector, but it also needs a complementary sector *without this  $M-C-M'$ -rationality* to allow the operation of the first sector. The debt on central banks' balance sheets falls out of the profit logic and transforms into a peculiar existence; we enter a kingdom of undead or unborn. While a legal debt claim is still there, the usual distinctions of a  $M-C-M'$ -world apply as little as Euclidian geometry to a non-Euclidian world. In the case of sovereign debt, there is formal, nominal debt, but nobody cares how much it is. Interest has to be paid, and, in fact, is normally paid, but – at least in the case of sovereign debt – the payor and the payee do not care. The receiving central bank, the payee, does not care as it will return the receipts to the state as quasi-dividends; the payor, the state, does not care either as the paid interest will be returned to it as quasi-dividends.<sup>3</sup> The capitalist logic is outsmarted. Therefore, central banks may allow the purchased debt to rest on their shelves for a very long time and these shelves to, ultimately, become places for debt restructurings, debt forgiveness, hence, crematories for debt or places for the euthanasia of debt, where the already hybridized debt makes the step from the semi-dead to the wholly dead, e.g., after a debt jubilee or a currency reform.<sup>4</sup>

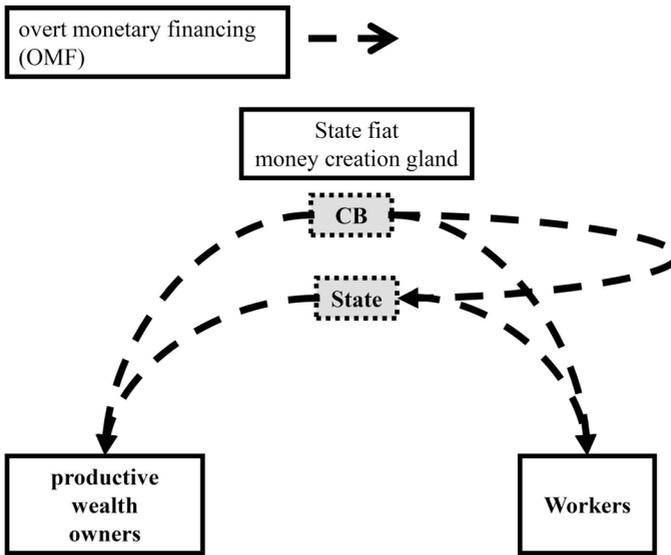
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3 It is, thus, quite logical if *Harding*, Fears about Japan's debt are overblown, in: *Financial Times* of 6 September 2017, after a study of four other options, recommends: "That leaves a more plausible fifth option. Do not resolve the public debt. Live with it. This is surprisingly do-able". On the other hand, as this debt does not really matter, another option for public debt is also feasible. As *Dowding*, We need to think about debt cancellation, in: *Financial Times* of 5 December 2021, reports "senior Italian officials (asked) the European Central Bank to ease debt burdens [following the Corona crisis, G.W.] by forgiving sovereign bonds it owns." Dowding criticizes Christine Lagarde for dismissing the idea too rapidly: "In a world, where a lot of sovereign debt is being bought by central banks, intrinsically, all we are doing is allowing the left hand of government to owe the right hand of the government a lot of money. At some point, they should just shake hands and throw the debt away". Dowding is fully aware that debt cancellation would amount to "helicopter money". "Consider what would happen if governments issued 10,000-year bonds at a zero interest rate and central banks bought them up. That is in effect the same thing as cancelling the debt."

4 Private debtors, whose debt is bought by central banks, of course, continue to care about having to serve their loan debt, even if it is to the central bank. Central banks could also help them, though, by debt restructurings or waiver, or states might compensate the debtors for the debt service or make payments to the central bank on their behalf (for instance US-President Biden's mentioned program of waiving educational loans).

The second tableau shows only the next possible, but not necessary, step, the radicalization and simplification of what exists already today to “overt monetary financing” (OMF). States say Adieu to the Byzantine hullabaloo. Private banks and wealth owners are completely side-stepped; the “tandem-agreement” between the central bank and private banks is now, indeed, cancelled: “The moor (of fractional bank credit money creation) has done his duty; the moor can go”. Prosthetics are, thence, funded without states issuing debt and without central banks purchasing and holding onto it. Central banks simply distribute money to the firms, workers, or the state, where it is needed, who will use it for prosthetics.<sup>5</sup>

Figure 26: Tableau showing prosthetics by “Overt monetary financing”



Now, only the central bank and the state form the prosthetic apparatus that, when reduced to its elementary function, handles deficient employment-generating spending, almost like a heart-lung-machine. The apparatus could even be further simplified by the state revoking its delegation of the fiat money creation to the

5 Central banks can also “buy” debt at the debt issuance from states, i.e., from what are called primary markets, by making the original loans to states. This creates the debt as an asset. Or the can even “buy” debt at the debt issuance from privates (mainly workers or firms) by also directly making loans to them. In this case, the recipients immediately receive newly created state fiat money and never even touch existing money or newly created bank credit money. Legal debt relations are, of course, still formally involved.

central bank, dissolving the central bank, and assigning this power to a department of the finance ministry.

Ultimately, there would not even be a significant difference between the present practice and these variations of “overt monetary financing”. The old way or another, all prosthetics financing by state fiat money creation is caught in dilemmas and is, therefore, approaching exhaustion. Whether new money is created with debt ending on central banks’ balance sheets or without such bookkeeping entries, nobody has control over the masses of newly created money, which is floating around. They cannot but ultimately do what money causes wherever it goes: It will bet up prices and, thereby, domestically, cause inflation, in markets for sterile investments and in markets for productive investment and consumption, if the money goes there. This will worsen the foreign exchange rate of the most inflationary economies. States are crippling their own state-fiat-money-creation glans by its reckless use; the more they use it, the more the consequential inflation falls upon them. What to do? How to defend an auto-destructive state-fiat-money-creation-gland, which has become a primary means of state policies, if you cannot quit what damages it most? First, if you remain addicted to state fiat money creation, try everything else possible to keep inflation under control; for example, keep sovereign debt markets in existence for as long as possible to channel the masses of floating money to places where they do the least inflationary damage – this, in fact, speaks strongly against a switch towards “Open Monetary Financing”. Second, provide incentives for the newly created money to return to the central bank, rather than doing more damage elsewhere, particularly in product markets – this speaks in favor of maintaining the central bank as a separate institution aside the state. If you, nevertheless, witness an erosion of the power of your state-fiat-money-creations-gland, third, you may try to use your geopolitical and military might (and wars) to strengthen your state-fiat-money-creation-gland, at least relative to the ones of other states, meaning that in the 21<sup>th</sup> century it is the dilemmas of state-fiat-money-creation – not primarily the hunt for territories, populations, resources and markets– , which drive the world into new imperialist contests. Today’s mass democracies can hardly be expected to oppose this. The more they become accustomed to the benefits from money creation, the more they are likely to support imperial policies – like the Greek in their people’s assemblies and the Roman legionaries roaring in support of their emperors. Moderation is not their thing; they “want the world” and they “want it now.”