Schumpeter vs. Minsky on the Evolution of Capitalism and Entrepreneurship

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Abstract: Joseph Schumpeter and Hyman Minsky have devoloped, during their lives, both a theory of the business cycles and a theory of capitalist development. Minsky was influenced by Schumpeter during the period he spent at Harvard University in 1942 and he thought that Schumpeter vision of the capitalist process required an integration of financial markets and investment behaviour: roughtly speaking, Minsky's financial keynesianism was what Schumpeter needed to complete his own theory of the devoloping of a capitalist economy. Minsky explored an even broader historical framework during the last decade of his life: the theory of capitalist development along the idea that there are many types of capitalism. As pointed out by Whalen (2001) to analyse each stage of capitalist development following Minsky's perspective, one should ask what is the distinctive activity being financed, what is the pivotal source of financing, and what is the balance of economic power between those in business and in banking/finance activity. Capitalist development is shaped by the institutional structure, but this structure is always evolving in response to profit-seeking activity. The financial system takes on special importance in this theory not only because finance exerts a strong influence on business activity but also because this system is particularly prone to innovation. In this paper, I shall focus particularly on this analysis trying to up-date his taxonomy, taking into account the process of global financialisation, and comparing it with Schumpeter's previous scrutinity on the evolution of capitalism.

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"Whereas all capitalisms are flawed, not all capitalisms are equally flawed" (Minsky 1986b, 295).

Introduction

Joseph Schumpeter and Hyman Minsky have devoloped, during their lives, both a theory of the business cycles (cf. Schumpeter, 1939; Minsky, 1982) and a theory of capitalist development (Schumpeter,1934, 1942; Minsky, 1990a; 1990b; Minsky, 1993a). According to Schumpeter indeed the dynamic of a capitalistic economy is generated by the innovative process. This process does not unfold in continuous and uniform manner, but through a periodic succession of cycles (Schumpeter, 1939). Minsky was influenced by Schumpeter during the period he spent at Harvard University in 1942[1] and he thought that Schumpeter vision of the capitalist process required an integration of financial markets and investment behaviour: roughtly speaking, Minsky's financial keynesianism was what Schumpeter needed to complete his own theory of the devoloping of a capitalist economy. The point raised by Minsky is important because it relies on chapters in Schumpeter's book titled "The Theory of Economic Development" (1934) that were often overlooked by many economists. In this book, Schumpeter considered indeed money, credit and finance as essential to the innovation process promoted by the entrepreneurs (cf. Knell, 2015).

Minsky has developed the so-called "Wall Street" paradigm, a financial theory of investment[2] and the often cited financial instability hypothesis (FIH) (Minsky, 1976; 1982). These contributions, and his subsequent writings, have all received significant attention in recent years due to the recent financial crisis conceived as a "Minsky moment".Nevertheless Minsky explored an even broader historical framework during the last decade of his life: the theory of capitalist development along the idea that there are many types of capitalism (cf. the epigraph). In this paper, I shall focus particularly on this analysis trying to up-date his taxonomy and comparing it with Schumpeter's (1942) previous scrutinity on the evolution of capitalism.

The paper is structured thus: in section 1, I try to describe how Schumpeter's vision on the evolution of capitalism was the purposes behind Minsky's exploration of a theory of capitalist development. In section 2, Minsky's theory is then outlined and compared with Schumpeter's scrutinity on the topic, with particularly regards to his 1934 and 1942 books. Section 3 takes into account the process of current financialization and its impact on entrepreneurship; Section 4 puts under scrutiny the threats

[1]Minsky began indeed his doctoral dissertation research under Schumpeter who untimely death in early 1950. For this reason Minsky's PhD was finished (1954) under the supervision of Leontief.

[2] On the importance of the financial factors for corporate investment in Minsky, see: Eichner and Kregel, 1975; Skott, 1989; Crotty, 1990, 1992; Lavoie, 2014; Davis, 2017.

for financial stability link to the financial globalization reported by Minsky since ‘90s. Finally, I summarize my conclusions.

1. Schumpeter on the evolution of capitalism

Schumpeter identified innovation as the critical dimension of economic change. He argued that economic change revolves around innovation, entrepreneurial activities, and market power. He sought to prove that innovation-originated market power can provide better results than the invisible hand and price competition. He argued that technological innovation often creates temporary monopolies, allowing abnormal profits that would soon be competed away by rivals and imitators.

Schumpeter was probably the first scholar to theorize about entrepreneurship, and the field owed much to his contributions. Schumpeter argued that the innovation and technological change of a nation come from the entrepreneurs. He coined the word *Unternehmergeist*, German for "entrepreneur-spirit", and asserted that "... the doing of new things or the doing of things that are already being done in a new way" stemmed directly from the efforts of entrepreneurs.

Once the entrepreneur has been defined in general terms, the question arises as to who really puts on the entrepreneurial functions in what historically has been termed as capitalist economy and that, in fact is the kind of economic order which specifically concerns Schumpeter. Related to this there is another question, who are the beneficiaries of the profit in this order of economy. The latter question is related to the former but is not identical to it because as the role of the entrepreneur is essential to generate the profit the entrepreneur may not be the receiver of the profit.

In order to answer these questions one should keep in mind that for Schumpeter innovation generally means construction of new plants or, at least, a radical transformation of the old plants. It is absolutely not indispensable but it should be considered that the innovations which do not follow what has been said earlier are innovations of minor relevance and do not characterise the process of development. The creation of the new plants can come up either through birth of new firms or through expansion of old firms. In this regards Schumpeter distinguishes between two stages of development of capitalism, the first named “competitive capitalism” and the second “trustified capitalism”. The first stage is characterised not by excessively big firms in relation to the market dimension and here the introduction of innovation generally means the creation of new firms. Instead, in the second stage big firms become more diffused and these firms are capable of sustaining the innovative process within their own set up so that innovations do not help the birth of new firms which, then, compete with the old ones.

Having said that and given the fact that the identification of an entrepreneur is never an easy task because no one is just an entrepreneur and nor is he in a perfectly continuous manner, Schumpeter points out that in the period of competitive capitalism entrepreneurial function is generally carried out by the proprietors of the firms themselves.

However the question becomes much more complex in the era of dominance of big firms in which the entrepreneurial function can either be performed by someone who controls the firm, in a joint stock company by the proprietor of majority of shares or by those who are responsible for running the firm or even by ordinary staffs and can reside in a single person or in a collective body.

Once the profit has been generated whether it is received by the entrepreneur or not is a matter of institutional nature. In case of family firms the profit is received by the same people who have performed the entrepreneurial activity, and in this case, it, generally, constitutes the origin of those great fortunes upon which industrial dynasties are founded. In the industrial system based on the big joint stock companies, instead, the profit, as such, belongs to the firm and its distribution becomes a question of company's policy: it can be received by the shareholders, or by the board of directors or even by the staffs and workers, independently of the fact that who actually has carried out the entrepreneurial act. Despite the vagueness of the problem about who receives the profit it is a well established fact that for Schumpeter the profit cannot be the reward for the risk as has been often believed by other economists. Schumpeter points out that the risk is taken by the capitalist and not by the entrepreneur, and the entrepreneur takes the risk only in so far as he is also the owner of the capital.If one were to accept that innovations are incorporated in new plants, immediately arises the problem that how such innovations would be financed. At steady state every firm finances its operations by using current revenue.

However, the entrepreneur who has to construct the plant in which his innovations would be realised needs a new purchasing power, not existing before, through which he will acquire the possibility of controlling certain productive resources which are diverted from old uses and employed for the new uses as suggested by the innovation. This availability of new means of payment (by money (notes or deposits) manufactured for that purpose) is achieved by credit which according to Schumpeter is the other fundamental characteristic of the economic development.

Schumpeter thought that bankers stands between those who wish to form new combinations and the possessors of productive means. Banking activity indeed makes possible "the carrying out of new combinations, authorises people, in the name of society as it were, to form them. He is the *ephor* of the exchange economy (Schumpeter 1934, 74)[3].

As in the planned economy the realization of the innovative process would require an order from the planning authority to divert the productive resources from their current use to the new service, likewise in capitalist economy the credit performs analogous function in the hands of the entrepreneur because it allows the entrepreneur to utilize a part of the wealth of the system to his own ends. In the logic of Schumpeterian system the possibility that saving may preceed investment has to be discarded, as saving does not exist or in a steady state exists in negligible measure: in fact the main source where it is formed is nothing but the profits taken away from diffusion process determined by the competitors. It is clear, therefore, that including saving among the factors that give kick-start to development it would include in the premises part of what is needed to be explained. In other words financing investments for the innovations outside the loan business is a phenomenon that belongs to an already developed system.

Schumpeter cautions against considering this logical order to correspond necessarily to the historical succession. If credit creation by the banking system, logically, is the beginning of the capitalist process, this does not also assign it an historical priority. In fact, it should be kept in account that historically in the beginning of the capitalistic development firms were sufficiently small so that they could be financed by means coming from the formation of the saving by the preceding economic systems.

[3] The Ephors were elected magistrates who supervised the kings in Sparta, so Schumpeter's analogy is with bankers effectively deciding which'new combinations' will beformed. They act indeed as "social accountants".

Probably it can be said that for Schumpeter this initial stage of "primitive financing", in the capitalistic system that has developed historically, has been followed by other two stages as suggested by his distinction between "*competitive capitalism*" and "*trustified capitalism*".

The first would correspond to the great development of the credit system which manifests through the complete deployment of its *essential* function, financing the innovations. Naturally there exist on the one hand secondary functions of the credit system (financing the current business transactions) and on the other utilization of the saving coming from internal funds-revenue (profits) for financing the entrepreneurial activities; but the fundamental characteristic of the period in question would remain the fact that the bank continuously recreates in the system the financial terms of development facing systematic annulment, by competitors, of the dynamic revenue. In the second stage, albeit on a different level and decidedly in different conditions, some characteristics of the initial stage is somehow reproduced, at least, in the sense that the development and consolidation of firms of ever growing dimensions and the reinforcement of all the direct methods to hamper the competitor's performance are a phenomenon that tends to stabilize permanent sources of saving within the firms themselves and, therefore, to relegate the bank within the limits of its secondary function.

Schumpeter began the first edition of "The Theory of Economic Development" (1934), by describing the circulation of money and real goods and services in terms of a 'Kreislauf' or monetary circuit, but alludes to the importance of credit money at the end of the first chapter. Schumpeter considered money to be analogous to capital as bank deposits allow them to give credit to producers for their purchases of *circulating* capital goods. Still, Schumpeter (1934:107) took this idea one step further claiming "credit is essentially the creation of purchasing power for the purpose of transferring it to the entrepreneur." The availability of credit creates allows entrepreneurs to gain access to investment goods necessary for innovation "before they have acquired the normal claim to it." Schumpeter reasoned that money was credit-driven and determined endogenously by the demand for bank loans by entrepreneurs engaged in innovative activities. Entrepreneurs not only had an insatiable desire to gain profit through innovation, but the could finance new innovations through endogenous money creation.

The Schumpeterian distinction between "competitive capitalism" and "trustified capitalism" serves in clarifying another important question for economic theory; it concerns the definition itself of the concepts of competition and monopoly. So for Schumpeter the real competition that takes place in the capitalist economy is not which is practised between small firms which produce the same goods but is that which innovative firms, those in which entrepreneurial activity is carried out, practise with respect to other firms; it is not the competition between identical goods, all of them produced in the same way, but is that which new products do to the old ones or the new productive processes do to the old ones. This competitive process has been called by Schumpeter the process of "*creative destruction*", a term which emphasises that the actual competition comes about by the effects that the innovations have on the existing firms.

This concept of competition carries with itself a concept of monopoly, even this being different from the traditional one. First thing to be noted is that the concept of innovation inevitably results to some degree of monopoly: before innovation is being diffused it is monopoly of the entrepreneur and the profit that he receives is due to this monopoly. According to Schumpeter the transition from competitive capitalism to trustified capitalism, i.e. the transition from a phase in which innovations generally are incorporated with the new firms to a phase in which innovations prevalently are carried out by the existing firms, doesn't result either into an intensity reduction of the economic growth or in the deterioration of its quality, instead, it may be surmised that during such transition the growth might even be accentuated.

Schumpeter, therefore, rejects the thesis, advanced by many and about which we will need to talk about later, according to whom capitalism is destined to a final crisis for reasons related only to its economic mechanism. Rather he is convinced that it would be impossible for capitalism to survive but this conviction is based also on non-economic considerations.

While a professor at Harvard Schumpeter then developed his theory of capitalist development and he discussed on the fate of capitalism. Many economists and political scientists of the day argued that large businesses had a negative effect on the standard of living of ordinary people. Contrary to this prevailing opinion, Schumpeter argued that the agents that drive innovation and the economy are large companies which have the capital to invest in research and development of new products and services and to deliver them to customers more cheaply, thus raising their standard of living. In *Capitalism, Socialism and Democracy* (1942, 123), Schumpeter wrote: "As soon as we go into details and inquire into the individual items in which progress was most conspicuous, the trail leads not to the doors of those firms that work under conditions of comparatively free competition but precisely to the door of the large concerns – which, as in the case of agricultural machinery, also account for much of the progress in the competitive sector – and a shocking suspicion dawns upon us that big business may have had more to do with creating that standard of life than with keeping it down".

Nevertheless, as had been mentioned earlier for Schumpeter capitalist economy is destined to undergo a period of final crisis that calls for a transition to different forms of economic organisation. In this sense the position of Schumpeter is closer to that of the classics, and particularly to Marx because he has in common the idea that the crisis of capitalism is not resolvable in the ambit of capitalism itself, while on the basis of a Keynesian framework one tries to define an economic condition in which a relevant and continuous public intervention can keep the system alive, albeit modifying some of its characteristics. It has also been said that Schumpeter's argument are based on considerations which are not strictly of economic order but they rather refer to changes in the social structure that result in capitalism deriving from the mechanism of its own evolution.

The Schumpeterian thesis – presented in 1942 in his work "Capitalism socialism and democracy"- is essentially based on the the evolution of the economic and social environment in the last stages of capitalism. The relevant increase of the size of the firms, that gives each firm a very large share of the overall market, requires business and group planning that makes bearable the serious risks. These risks derive from the close dependence of the efficiency of the productive development that takes place at a point in the economic system from what happens in the rest of the system itself. This basically means that the formation of capital becomes more and more controlled by the workings of the management boards rather than the initiatives of individual entrepreneurs. In other words, the close relation that existed at the beginning of capitalism between the single entrepreneur and innovation is snapped; the innovation itself is being reduced to a routine process; the economic process tends to become depersonalised and automatized.

In the society, then, the entrepreneurial function, *conceived individualistically* loses its importance and move towards *managerial capitalism*[4]. But, as forecast by Schumpeter, there exists a second

[4] This aspect has been pointed out also by Minsky (see section 3).

reason of the weakening of the entrepreneurial activity when the capitalistic economy achieves a certain state of development.

In highly developed societies there was a tendency to systematically permit forms of intervention and acts of economic policies which tended either to a strong increase the public investment as part of the overall investments or to a redistributive process which in the end had the effect of rescheduling the distribution of income between consumption and savings in favour of consumption (consider, for example, the huge programmes of social security).

This kind of evolution may be justifiable on the basis of Keynesian considerations: it is a matter of complex indispensable policies to maintain the effective demand to a sufficient level to guarantee a high level of employment. But what Schumpeter draws from it, is that the accumulation of capital, in the ambit of private economic activity, is becoming less important for the development of the system, as a result the position, related evidently to the accumulation, of the private entrepreneur becomes less and less important.

As Schumpeter maintains, if the full deployment of entrepreneurial activity on a private and individualistic basis is the essential connotation of capitalism, developments mentioned earlier lead in the long-run, to a profound transformation. This aspect is considered irreversible by Schumpeter as regards an economic system in which the capitalist class gets weaker and weaker, approaching the economy in a planned form which he believes, if not desirable, certainly perfectly possible: ‘a socialist form of society will inevitably emerge from an equally inevitable decomposition of capitalist society’ Schumpeter (1942, p. 129).

2. The influence of Schumpeter on Minsky’s theory of capitalist development

As outlined in the introduction, Minsky’s theoretical analysis has the merit to stand on the shoulders of two intellectual giants. As well-known his writings on business cycles made considerable use of the prior works by Keynes. However (cf. Whalen, 1999 and 2001) that is, in the mid-1980s, he became convinced that the structure of the U.S. economy and of devoloped capitalist economies have so fundamentally changed that an analysis of structural evolution was essential.
It was at this point that Minsky turned to the insights of his Harvard’s mentor: Joseph Schumpeter. In a 1986 essay, Minsky (1986c, p. 121, quoted by Whalen, 1999) 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 believed that such an integration was possible because Schumpeter and Keynes (along with Marx and the institutionalists) had a common perception of the task of economics. From this perspective, the economy is a complex, time-dependent system[5].

[5] If the first element in Minsky's theory is the focus on economic activity as a process in time, then the second element is that capitalist dynamics can take many forms. The path of the economy through time can be progressive, stagnant or deteriorating--and tranquil or turbulent. In fact, it may be highly irregular(cf. Whalen, 2001 and Sau, 2013).

A fundamental determinant of the particular path of capitalist development is the economy's institutional structure. It is this structure that facilitates, influences, regulates and constrains economic activity. Moreover, given the notion of the economy as an evolving system, Minsky also stressed the dynamic nature of the institutional structure. Like Schumpeter, Minsky's recognition of historical time caused him to emphasize that production precedes exchange--and that finance precedes production. Thus, credit and finance are, in compliance again with Schumpeter’s analysis, at the center of capitalist development. Moreover, because credit is essential to the process of development, a theory of economic development needs to integrate it into its basic formulation: "the in-place financial structure is a central determinant of the behavior of a capitalist economy" (Minsky 1993a, 106)[6].

The profit motive was also an essential element in Minsky's writings, 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 previous section I have already recognized Schumpeterian forces of creation and destruction in products and manufacturing processes. But Minsky emphasized that Schumpeter also gave attention to changes in financial systems. As a result, Minsky's theory stresses that financial markets evolve not only in response to profit-driven demands of business leaders and individual investors but also as a result of the profit-seeking activity by banks and financial firms (cf. Minsky 1986b; Minsky 1990a; Minsky 1993a).

Minsky (1957a), was indeed concerned with “profit-seeking activities” that drives “evolutionary changes in financial institutions”, which then leads to the endogenous creation of money. He claimed that it was almost impossible to control monetary aggregates because of financial innovations and new financial instruments. Later, Minsky (1986b: 120) recapped the origin of this idea: the Schumpeterian vision of the experimenting entrepreneur who innovates need but be extended to financial firms and their clients to explain why portfolios migrate to a brink at which a shortfall of cash flows or a rise in financing terms may lead to a market revision of asset values. Here Minsky linked Schumpeter’s idea of the innovating entrepreneur with that of financial innovations produced by financial institutions. Minsky (1993 p….) concluded: “Nowhere is evolution, change and Schumpeterian entrepreneurship more evident than in banking and finance and nowhere is the drive for profits more clearly a factor in making for change”. Financial innovation is then another essential element in Minsky's theory since such innovation is a crucial determinant of institutional evolution. In his thought, financial structure is neither neutral, nor dichotomic on the real sector of the economy, financial evolution plays indeed a crucial role in the dynamic patterns of the economy.

3. Minsky’s theory of capitalist evolution

As I stressed in the previous section, Minsky's theory of capitalist development is finance-driven, and the relations between finance and investment are given center stage. The stages are related to what is financed and who does the proximate financing. Following Whalen’s (1999) taxonomy, Minsky's

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[6] On this topic see also the relevant book by Hilferding (1910 reprint 1981).

capitalism varieties may identify at least five stages — and we might now be on the verge of creating a sixth. The five stages can be labeled as follows:

merchant capitalism (1607-1813),

industrial capitalism (1813-1890),

banker capitalism (1890-1933),

managerial capitalism (1933-1982),

and money-manager capitalism (1982-present).

Merchant capitalism emerged from European feudal society and took root in America with establishment of British colonies in the 1600s. The distinct activity to be financed were production and transportation of goods, acquisition of inventories. The pivotal source of financing was provided by merchant banking and commercial banking. The main instrument of this stage was a bill of exchange or other instruments that relate credits to specific commodities. Such a bill is drawn on a banker and assert that the banker garatees that the receiver of goods will pay the shipper. As regards the entity to be financed it was characterized by owner-managed enterprises--usually proprietorships or partnerships--with few employees and often few transactions per day. Merchant capitalism was undermined by growing population and by the arrival of the industrial revolution. Minsky stressed also attention to the profit motive, since profit was the driving force for individuals whose names have become synonymous with the arrival and expansion of industrial capitalism.

As to *industrial capitalism* it was characterized by the fact that the distinctive activity to be financed, due to industrial expansion, were factories manufacturing, capital-intensive transportation, mills, and mines. The main source of financing was through the activity of investment banking like J. P.Morgan. This stage saw the seeds also of the New York Stock Exchange. As regards the fundamental entreprise financed, the partnership gave way to the industrial corporation. The industrial revolution led to a great increase in the importance of machinery in production and therefore on non-labour costs that prices had to cover.

Banker capitalism was established when investment bankers responded to cutthroat competition in the 1880s and 1890s. Its arrival is characterized by investment bankers turning their attention toward the financing of industrial consolidation (cartels, trusts and mergers). Indeed, there was a merger wave in its aftermath. Private economic power, in this stage, had become greatly concentrated: financiers and managers exerted their own formidable force during banker capitalism — at both the enterprises and industry levels. Taylorism as the new "scientific" techniques (inspired by Frederick Winslow Taylor) combined assembly-line production and enabled managers to generate significant increases in factory output. The group that holds the greatest economic power was represented by investment bankers since they acquired a controlling position in the economy arranging mergers but also by securing large ownership shares and seats on the boards of directors of newly combined corporations.

The transition from *banker capitalism* to *managerial capitalism* was driven by the Great Depression since it made manifest the need for public economic policies to stabilize economic activity in the face of the Great downturn. This downturn was even getting worse in the aggregate, since individual bankers, businesses and farmers did anything except cut loans, slash prices, reduce employment, and increase agricultural yields. The New Deal by Franklin Roosevelt shift the distinctive activity financed through a series of policies and reforms that ushered in the next stage of U.S. capitalist development macroeconomic growth and stability. Bold government action in the realm of monetary and fiscal policies along regulation of the banking activity (the Emergency Banking Act, banks reorganizations, and institutional reform including deposit insurance, securities regulation, and compartmentalization of financial institutions). The Glass-Steagall Act (1933) contained institutional innovations that avoided a complete breakdown of the financial system and massive debt deflation by providing a strict separation between commercial and investment banking.

The so-called *managerial capitalism* saw corporate managers running giant corporations, and the pursuit of corporate growth was regarded as the major aim of firms (Stockhammer, 2004b). The institutional settings that enabled this process were, however, historically specific to the Fordist accumulation regime which characterised the so-called Golden Age between the end of World War II and the early 70s. And, as already stressed, they were largely the direct consequence of the institutional arrangements that followed the crisis of 1929. In the 1930s, indeed, Governments over the world, have progressively been aware of the dynamics that has led to the financial crisis. This is the reason why they severely limited the influence of financial capital, ending up by reinforcing the role of corporate management.

The pivotal source of financing was through the Central Bank. As regards the fundamental entity financed it regarded the private sector broadly speaking financed through the banking system and conglomerate form was dominant in the market. Unfurtunately the financial system evolved versus a more fragile situation characterize by a reductions in margins of safety a greater reliance on debt financing, and a turn toward short-term financing.

These were the seeds for the stage that followed represented by *money-manager capitalism*. Characterized by an explosion of activity by finance companies and other non-bank financial institutions--as well as a steady stream of bank innovations such as the securitization of loans and the creative use of off-balance sheet commitments. But one of the major innovation in the financial system in this period (i.e. 1980s) was the rise of managed-money funds--pension funds, mutual funds, bank trust funds, and so on. Over time, such funds accumulated vast amounts of money. *Money-manager capitalism* is characterized not only by a substantial growth of financial assets but by the shift of responsibility for holding and managing those assets to mutual and pension funds (Minsky, 1996). The ownership of financial instruments by dozy of shareholders has been supplanted by the professional, *eagle-eyed* money managers.

Fear of wealth losses promoted by inflation damaging upon bank deposits also contributed to the increase in managed-money funds. As this stage progressed, "individual wealth holdings increasingly took the form of ownership of the liabilities of managed funds rather than the holding of a portfolio of the liabilities of individual businesses" (Minsky 1993a, 110-111, quoted by Whalen, 1999, p. 12).

Money-manager capitalism stemmed since the 1980s (and, as I shall to argue later, characterizes our times), as institutional investors, by then the largest repositories of savings in developed countries, began to exert their influence on financial markets and business enterprises. The aim of money managers is the maximization of the value of the investments made by fund holders. As a result, business leaders became increasingly sensitive to short-term profits and the stock-market valuation of their firm. In the previous age of managerial capitalism, corporate managers "were the masters”of the economy, by the 1980s, money managers became the masters! Minsky knew (as well Keynes

(1936; p. 154-55)[7] that these aspects would lead to greater instability of financial markets. He then concentrated on the effect of this new power of the money managers in increasing the sensitivity of firms to stock market valuations and the threat of takeover just at the time when all economies were opening up to a wider, world competition (i.e *financial globalization*). The rise of institutional investors encouraged continued 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. These managed-money funds often provided the resources that raiders needed to secure corporate control.

Furthermore in many developed countries during this period, Governments have also promoted the evolution of the financial system by removing many regulations imposed after the IInd World War (particularly in the US). Tax law changes have also encouraged takeovers, buyouts and other types of corporate restructuring (Wolfson 1994, 111-112). This process of deep financialization was tightly linked to neo-liberal paradigm as well as to globalization process inspired by Washington Consensus (cf. Lavoie, 2012; Sau 2013; 2015). Neoliberals wanted deregulation, privatization, the intensification of competition, labor market flexibility, and mechanisms designed to modify the behavior of managers. Performance pay became "the in-thing and the best that could be designed was pay packages strongly oriented toward stock options. With the stock market value of the firm as the ultimate objective, it was said that remuneration of managers ought to be a function of share prices" (Lavoie, 2012,p. 217).

The managerial view of the firm, as described by Schumpeter and Minsky has lost out to the shareholder view. The standard story emphasized that managers of corporations have been forced to take the interests of the owners into prime consideration while the shareholder value argument said that managers ought to maximize the stock market value of the firm.

Financialization has meant a change in the way corporations are being run, as well as changes in the behavior of economic agents, in the microeconomic and macroeconomic policies being pursued by governments and central banks, and in the regime of capital accumulation and the distribution of income. Most obviously, it has meant changes in financial regulation through deep deregulation. Furthermore, financialization has been accompanied by a series of economic theories (Efficient market hypothesis –EMH-) that have justified or fueled this process (Sau, 2013). This process has been measured by the evolution in a range of variables, most notably the large rise in the relative importance of the finance, insurance, and real estate sectors since the early 1980s, whether measured

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[7] "It might have been supposed that competition between expert professionals, possessing judgment and knowledge beyond that of the average private investor, would correct the vagaries of the ignorant individual left to himself. It happens, however, that the energies and skill of the professional investor and speculator are mainly occupied …….with foreseeing changes in the conventional basis of valuation a short time ahead of the general public….. Thus the professional investor is forced to concern himself with the anticipation of impending changes, in the news or in the atmosphere, of the kind by which experience shows that the mass psychology of the market is most influenced. This is the inevitable result of investment markets organised with a view to so-called "liquidity"…. This battle of wits to anticipate the basis of conventional valuation a few months hence, rather than the prospective yield of an investment over a long term of years, does not even require gulls amongst the public to feed the maws of the professional; — it can be played by professionals amongst themselves…. 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 a by-product of the activities of a casino, the job is likely to be ill-done", (Keynes, 1936, Ch 12, p.154-56)

in terms of gross domestic product (GDP), profits, or employee compensation. Transactions based on financial futures and derivatives have exploded.

Furthermore, over the last years the financial investment of *non-financial businesses* has grown considerably, as have share buybacks and dividend payout ratios (Ohrhangazi, 2008). It follows that the accumulation of real capital has been declining (Stockhammer, 2004; Davis, 2017, Scarano, 2019). Financialisation, the shareholder revolution and the development of a market for corporate control have shift power to shareholders and that changed management priorities, leading to a reduction in the desired growth rate[8]. The process of financialization "was based on weakened labor unions, relatively low real wages, high profit shares, high real interest rates, and large capital gains, either in the equity or in the real estate market" (Lavoie, 2012, p. 219).

Minsky (1993a,b) was well aware that, thanks to the massive deregulation process in financial markets promoted by the neo-liberal paradigm, *money managers* have assumed a crucial position in financing mergers and organising hostile takeovers as a device to discipline managers of non-financial businesses, and thereby forcing them to follow their interests and objectives. Yet financial investors usually have a shorter time horizon than traditional corporations and banks (Stockhammer, 2004b). They are interested in short-run returns and therefore tend to underinvest in long-run projects, changing the growth strategies of the controlled corporations[9].

While, under the stakeholder view of managerial capitalism, firms often took a long-term view, with the generalization of the shareholder model led to short-termism, with the managers being mainly concerned on the stock market prices even though large firms do not finance any of their investments through stock issues. Unlike the previous stages the emphasis was not on capital development of the economy, rather upon quick return of the speculator, upon trading profits. The shareholder model, instead of aligning the interest of the managers to those of the owners, induced managers to fool actual and would-be shareholders, by messing with the computation of earnings per share (Parenteau, 2005, p. 128).

As remarqued by Minsky (1993a) in this stage of capitalism the financiers are not acting as the Schumpeter's *ephors* of the economy that screen, promote and finance the most profitable projects, todays money managers activity is more akin to Keynes's characterization of the financial arrangements of advanced capitalism as the by-product of a *casino*.

As I have argued, in the first three post-war decades, the role of shareholders in corporations was severely limited by heavily restrictive financial regulation and capital flows control, which were the political reactions to the financial and real crisis of the 1930s. In the 1950s and 1960s, giant corporations usually aimed at financial independence through retained earnings. They were able to borrow from financial institutions and markets, but were not normally forced to act so and could avoid subjection to control by financial corporations and outside shareholders. In this kind of corporations,

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[8] Stockhammer (2004) has tested this phenomenon empirically, for the USA, the UK, France and Germany. In all Countries, evidence supported the negative effect of financialisation on accumulation.

[9] The two typical constraints corporations face are the finance constraint and the profit–growth trade-off. On the first front, according to the pecking order thery, inside and outside finance are really different. In fact, as stressed again by Minsky, corporations follow the principle of increasing risk, and then are reluctant to accept high leverage rates, since a failure will put their existence at risk. The banks, in turn, take corporate current profit and wealth as proxies for business reliability, granting credit only to firms that are profitable. In this way, financing by means of retained profits can become a preferential corporate strategy, which ask the company's commitment to maximizing the return on investment for potential shareholders. The growth–profit trade-off, instead, takes into account the fact that an increase in investment can harm future profits because of the start-up costs of investment or the socalled Penrose effect (increasing managerial costs of fast growth).

“managers were a self-perpetuating group that identified itself with the corporation and its fate. The board of directors and the chief executive officers were “organization men” and the control rested securely in their hands. Their major objectives were the corporation market share and its strategic positions in the market” (Scarano, 2019, p. 13).

However, this situation has been changing since the late 1970s, through the progressive erosion of financial regulation by means of the invention of new financial instruments, such as junk bonds and other high-risk and high-return securities[10]. By means of this financial deregulation, the financial markets have progressively exerted increasing pressure on non-financial corporations (NFCs), by means of hostile takeovers first, and then with the “shareholder revolution”, characterised by a growing presence of institutional investors within their shareholding (Lowenstein, 2004; Orhangazi, 2008)[11].

Again according to Stockhammer (2004, 2006), the “shareholder revolution” is one of the main features of the present neo-liberal era, which has produced radical changes in corporate behaviour in the name of creating “shareholder value.” According to him, this revolution has been the consequence of the financial liberalization and the emergence of very liquid share markets in the 1980s and 1990s, together with the successive rise in shareholders’ capability to influence public company managers by means of the creation of “a market for corporate control”. The managements of large non-financial corporations, in fact, would have committed themselves to increasingly producing shareholder value because of the expanded possibilities for financial investors to use the capital market to estimate and compare performance of their corporations and to discipline them with the threat of hostile takeovers. In this new context, the managers of large corporations could easily be replaced by shareholders if corporate performance proved inadequate in creating value for them (Stockhammer, 2006).

Since ‘90s mutual and pension funds held growing fractions of equity, increasing their ownership shares at the expense of cross-shareholdings between non-financial firms. These institutional investors allocated capital among industries and firms in a decidedly market-based way, imposing profitability norms on enterprises and looking to short-term profit. They exerted their power over the management with exit strategies, creating difficulties for the firm to obtain new financing. Their arrival unleashed competition for global saving among companies. However, investment funds were set up by the banks, especially in Europe (Levine, 2003). Thus, the threat of growing control by large financial intermediaries in public companies could be an incentive for managers to change their investment behaviours, increasingly orienting them towards short-term profit investment and discouraging long-term strategic investments.

However, this tendency to produce an increasing shareholder value could not only be the result of new forms of corporate governance and new financial intermediaries, but rather the traditional way to maximise the equity capital self-valorisation in a different competition environment and given new

[10] Moreover, up to 1982 the Securities and Exchange Commission (SEC) could counteract massive stock repurchases as illegal attempts to manipulate stock prices by the companies. Since the end of 1982, instead, during the deregulation onset of the neoliberal phase, the SEC has partially liberalised stock repurchases, provided that they be less than 25% of the average daily trading volume over the previous four weeks and the buybacks be carried out at neither the beginning nor the end of the trading day (Lazonick, 2013).

[11] As pointed out by Scarano (2019) French regulationists have been emphasising corporate governance since the 1970s, because the pursuit of “shareholder value’ is closely associated with the short-termism of non-financial corporations (Boyer, 2000; Grahl Teague, 2000; Aglietta, 2000; Aglietta and Breton, 2001), and Lazonick and O’Sullivan (2000) have perceptively shown the connections between shareholder value and company downsizing throughout the neoliberal phase of capitalist development (Lapavitsas, 2011).

financial investment opportunities. This puts the emphasis on other transformations of the capitalist system in its neo-liberal phase, which have been in part gathered under the label of financialization.

Today the term financialization may be used to refer to three different, even though interconnected, phenomena. The first is the reduction of reliance on bank loans by large non-financial corporations and their growing autonomous ability to raise funds in financial markets. The second is the expansion of banks' mediating activities in financial markets and their tendency to lend mainly to households. The third is the increasing involvement of households in the financial markets, as both borrowers and asset holders (Orhangazi, 2008; Lapavitsas, 2011; Scarano, 2019). Financialisation may be scrutinized both at a macroeconomic level and at a corporate (micro) level. As regards the former, financialisation in practice simply becomes synonymous with the expanding financial sector within the economic system. This expansion of financial markets in one of the main characteristic of the neo-liberal era and it has been mostly due to innovations in securitization and credit enhancement, which have favoured new trading strategies (Bodie et al., 2014). As to the latter (i.e. corporate level), it can highlight the changes in the behaviours of the managers of non-financial corporations and their new relations with the financial markets; that is, the adoption of shareholder value orientation by them associated to increasing investments in financial assets (Stochammer, 2004a, 2004b)[12].

These structural transformations are among the main results of the previously examined evolution in corporate governance, which have produced radical changes in the objectives of top managements, favouring an increasing propensity to substitute real investment with short-term financial investment in the process of corporate investment decision-making in order promote the 'pursuit of shareholder value'. In fact, according to Sawyer (2017) and Scarano (2019, p. 20) "financialisation has changed the relations between the financial sector and the real sector precisely because the passing of ownership of non-financial corporations into the hands of money managers has itself, in turn, fuelled the pursuit of this objective". In pursuit of higher quarterly earnings per share, American companies have conducted great stock repurchases to increase their own corporations' stock prices (Lazonick, 2013). In this way, trillions of dollars have been subtracted from real investments and job creation over more than three decades.

In compliance with Minsky (1993a,b, 1996) Stockhammer (2004a and 2006) has stressed that this phenomenon is an important factor in the slowdown of accumulation[13], not because investment in financial assets is necessarily in conflict with physical investment, but because it is a symptom of the changes in management strategies, closely connected with a change in the institutional setting of the firms. This aspect, therefore, could also be viewed as a symptom of *money managers capitalism*. As pointed out above, in the same period the non-financial corporations (NFC), while reducing their

[12] In the last three decades, in fact, a new kind of phenomenon has been powerfully emerging. Mainly in the US, but also in continental Europe: i.e. non-financial corporations (NFCs) have been increasingly investing in financial assets and creating own financial subsidiaries, deriving increasing shares of their income from this kind of pure financial activities (Stockhammer, 2004a; Orhangazi, 2008). In the same period, NFCs have increased transfers of earnings to the financial markets in the forms of interest payments, dividend payments and, mainly, stock buybacks.

[13] As pointed out by Scarano (2019, p. 13): "a marked slowdown in accumulation was experienced by most OECD countries from the 1960s to the 1990s. The growth rates of non-residential business capital stock, which is a measure of productive capacity of a country and is closely correlated with its GDP, reached their lowest points between the first half of the 1980s and the middle of the 1990s in most European countries and the United States. In the USA, the UK and Italy non-residential business capital accumulation saw a slight increase in the second half of the 1990s, but this was not the case in France and Germany".

accumulation of capital goods, progressively increased their financial investment (Stockhammer, 2004). Accumulation, while picking up again thereafter, never got back to the levels of the previous Fordist period, and non-financial corporations have continued to invest heavily in financial instruments (Stockhammer, 2004b) and that, even after the 2008 great financial crisis.

Successively to financial liberalization, in fact, NFCs have been facing portfolio choice problems in their investment decisions between fixed and financial assets and increasing availability of alternative financial investments can channel NFCs' retained earnings to short-term financial portfolios instead of long-term real investments.

4. **The threats of global money manager capitalism**

Minsky (1996) has concentrated his analysis on the effect of the new power of the money manager in increasing sensitivity of firm to stock market valuation and the threat of takeover, just at the time when all economies were opening up to a wider, world competition.

As everybody knows, there are a number of different ways to define globalization, each of which underlines different aspects of a progressive worldwide integration process between people, companies, and governments. However, here I prefer to confine my attention to its major economic features, which can be summarised as free trade improvement and a progressive worldwide liberalization of the capital movements. Free trade has been only partially implemented under the umbrella of the WTO, with many surviving tariff regimes, and countless nontariff barriers particularly nowadays[14]. Mainstream literature very often has outlined the successful of free and globalized movements of capital. According to neoclassical theory, free capital flows should only be a form of intertemporal trade and then their functioning rules should be no different from those of free trade. Thus, free flows of external capital should contribute to smoothing consumption and production paths, improving social welfare. By contrast Minsky was not soo optimistic. He outlined indeed that capital account liberalization was the theoretical field where economics largely failed in explaining events in the real world like financial crisis and debt-deflation. Free movements of short-term capital, such as portfolio flows and short-term bank loans, have so far been related to a long series of serious economic and financial crises because of their volatility and exposure to surges in and sudden withdrawals from the financial markets. Thus, successively to economic and financial crises in Asia, Latin America and Russia in the late 1990s, some economists underlined the possible dangerous effects of these kinds of capital movements for developing countries. Instead, long-term capital flows, such as FDI, were usually regarded as more positive for the long-term economic growth of developing countries, because they are generally more stable and can improve their production capacity and technology (Stiglitz, 2000 and 2018).

Thus, the economic literature analysing the effects of liberalization of capital flows on the developing countries usually highlights the difference between short-term and long-term flows. However, following the observations by Scarano (2019), free movements of capital can produce significant effects on the developed economies, too. Much less analysis has been dedicated to these effects, but

[14] While writing this paper this situation seems to be changing since President Trump has implemented further tariffs and barriers on US trade to cope with international competition and he has opened the door to the so-called "trade-war".

they can play a major role in producing the present tendency to stagnation in this kind of economies, and they are closely connected with another major phenomenon of our time: financialisation by non-financial corporations, which can greatly contribute to reducing their real investment in the developed countries, contributing to decreasing their growth rate and increasing their unemployment rate.

In this context, however, the distinction between short-term and long-term capital flows can be less evident and significant. Free movements of capital, moreover, can play a major role in financialisation of NFC from two different points of view. If real investment depends on the term structure of interest rates over the full range of financial and real investment opportunities, then real investments in the developed countries also depend on the differential between their rates of returns and the rates of returns on real investments in the developing or emerging countries. However, this differential does not only act by means of FDI, but also by means of the possibility of financial investment in foreign securities, associated with real investment in foreign countries. Financial globalization, multiplying the potential range of financial instruments available to big corporations' portfolios and creating new ways to indirectly access the high profits produced in the emergent markets, can play a major role in changing the portfolio composition. Moreover, the managers of "financialised nonfinancial corporations" can decide to substitute direct national real investments with financial investments in foreign corporations, thus also obtaining a greater liquidity for their portfolios.

Furthermore, financial investments by non-financial corporations are usually very different from the traditional forms of takeover and corporate holding because their profitability depends not only on the ratio between profits and invested capital, but also on the terms of capitalisation of the expected future profits realised through the financial markets. Thus, the growing liquidity of non-financial corporations' portfolios can contribute to heightening the usual volatility of the rates of return on financial assets as well as the vulnerability to contagion-induced financial shocks (cf. Scarano, 2019). Moreover, countries with a large financial sector have a riskier financial account structure, compared, for instance, with commodity-exporting countries, which show a safer financial account structure. All this obviously increases the overall uncertainty of financial investment profitability itself. And this growing uncertainty, in turn, leads to a greater tendency to money hoarding by non-financial corporations that crowded out real investments. Thus, the relation between fixed investment, uncertainty, increasing integration of international capital markets, the widening gap between real and financial sector transactions and corporate portfolio choice seems to be a very important factor.

The analysis of the evolution of capitalism by Minsky (at the end of his life) was then striking and longsighted since he observed, well in advance, and stressed rightly that money-manager capitalism was becoming global and that a further international economic and financial integration would take place in the years ahead; "managed money capitalism is international in both the funds and the assets of the funds" (Minsky 1990a, 71) and "global financial integration is likely to characterize the next era of expansive capitalism. The problem of finance that will emerge is whether the financial and fiscal control and support institutions of national governments can contain both the consequences of global financial fragility and an international debt deflation" (Minsky 1995b, p. 93)

This insight by Minsky's theory of capitalist development suggests therefore that a sixth economic stage might now be emerging. This suggestion comes from the fact that national and international entities have recently sought to contain the global financial crisis and particularly to cope with the contagion effects on the real economy stemmed after the sub-prime crisis in the US.

Conclusions

In this paper I have tried to show how both Schumpeter's and Minsky's theory of capitalist development continue to guide us and challenge us to explore important questions on the evolution of capitalism. Nevertheless I have discussed how these two giants of economic thought have analysed the evolution of capitalism with different results.

On one hand, Schumpeter in his 1942 book, stressed that in the latest stages of capitalist evolution, entrepreneuship would have been in impasse, and he has forecast that a socialist form of society will inevitably emerge from an equally inevitable decomposition of capitalist society; on the other hand, Minsky made it clear that the evolution of the capitalist systems is not necessary a progressive process. Indeed, as I have showed in this paper, *money manager capitalism* and the *global financialisation process* inspired by the neoliberal paradigm, may represent serious threats to the system itself.

To analyse each stage of capitalist development following Minsky's perspective, one should ask what is the distinctive activity being financed, what is the pivotal source of financing, and what is the balance of economic power between those in business and in banking/finance activity. Capitalist development is shaped by the institutional structure, but this structure is always evolving in response to profit-seeking activity. The financial system takes on special importance in this theory not only because finance exerts a strong influence on business activity but also because this system is particularly prone to innovation.

In the last section of this paper I have outlined that, developing Minsky's theory more thoroughly, might also involve explorations of the deep financial globalization process. This scrutinity may indeed justify the analysis of a sixth-stage in capitalism evolution that is: *global financial money-manager capitalism*.

Summing up, if Minsky's and Schumpeter's views have tried to understand the economic behavior of capitalist economies as evolving entities, their perspectives will continue to guide and challenge us for many years to come.

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