

## Editorial: Paolo Sylos Labini (1920-2005)

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In a few weeks will fall the tenth anniversary of the passing of Paolo Sylos Labini (PSL), to whom the name of the *PSL Quarterly Review* is dedicated (Roncaglia, 2008).

PSL was a teacher and friend to many members of the Board of this *Review*, as well as of *Economia civile*, publisher of the journal. He contributed frequently to the first series of the *Review* (Sylos Labini, 1949; 1957; 1967a; 1981a; 1982; 1984; 1987a; 1988a; 1999; 2003a; 2005a; Modigliani *et al.*, 1998a), as well as to its Italian sister journal, *Moneta e Credito* (Sylos Labini, 1959; 1967b; 1981b; 1981c; 1983; 1987b; 1988b; 1989; 1989; 1990; 1991; 1998; 2000; 2003b; 2005b; Modigliani *et al.*, 1998b).

Sylos Labini's contributions to the two journals are discussed by Roncaglia (2007; 2008); a number of articles in memory of his life and works are collected in the website of the Paolo Sylos Labini association (at <http://www.syloslabini.info/online/paolo-sylos-labini/articoli-in-ricordo/>), while among the obituaries and memories of the eminent Italian economist it is worth recalling here at least (Corsi, 2006a; 2006b; 2007; Corsi and Guarini, 2010; and Roncaglia, 2006a; 2006b). Furthermore, the Italian journals *Il Ponte* (vol. XLI, n. 3) and *Economia e Lavoro* (n. 3-2007) devoted a special issue to PSL's legacy. Finally, interested readers may find a large collection of PSL's works freely available in the Open Archive maintained by the University of the Tuscia, at the URL <http://dspace.unitus.it/handle/2067/163>.

In its new series, under the new name, the *Review* dedicated a discussion to Sylos Labini's oligopoly theory (Rancan, 2014; Roncaglia, 2014), spurred by the rediscovery of unpublished correspondence between PSL and Franco Modigliani (Modigliani, 2014). *Moneta e*

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*Credito* dedicated a special issue (Palazzi, 2014) to some of PSL's most notable contributions to the Italian journal *L'Astrolabio* (Sylos Labini, [1963] 2014a; [1963] 2014b; [1964] 2014c; [1965] 2014d; [1967] 2014e; [1968] 2014f; [1972] 2014g). The Italian journal will publish in the forthcoming two issues the proceedings of two conferences in memory of PSL to be held in Rome on 18 November 2015 at the Lincean Academy, and on 4 December 2015 at Sapienza University.

Already in the first special issues of their new series, in 2009, both the *PSL Quarterly Review* and *Moneta e Credito* included a notable article by PSL on the growing imbalances in the US economy (Sylos Labini, [2003] 2009a; [2003] 2009b). Given the topicality of such contribution in the wake of the Great Recession, and the nature and scope of the debate on the crisis in this *Review*, it seems appropriate to highlight here a few main features of this article. As the following brief discussion shows, Sylos Labini's contribution already contained precise reference – often backed by data for the USA and other economies – to trends and 'explanations' of the crisis that several mainstream economists (e.g. Robert Lucas) claimed were impossible to see before the crisis itself: from the accumulation of excessive household debt to excessively complacency on the side of the Fed, to speculative bubbles in the US stock exchange and real estate markets and the deflationary pressures caused by radical innovations. It is worthwhile to briefly recall these elements here to highlight how PSL's example shows that the economists can and often do provide useful services to society, provided they build on solid theories.

Sylos Labini's 2003 contribution is based on a presentation he gave in April 2002 at a conference organized by the CGIL (the Italian Confederation of Trade Unions), when he "expressed serious worries about the American economy, which strongly conditions the economies of the other countries, particularly in Europe" (Sylos Labini, 2009a, p. 59). In his 2009 article, PSL extends the analysis to derive the 'prediction' of a growing risk of a major economic crisis in the USA.

PSL's starting point is that accurate forecasts are impossible in economics, but "detailed diagnoses" allow for "hypothetical predictions". Sylos' detailed diagnosis is based on "certain similarities between the

situation that arose in America in the 1920s – a period that ended up in the most serious depression in the history of capitalism – and the situation that has emerged” during the 1990s (*ibid.*).

In PSL’s view, the main similarities (also with the current situation in Japan) are:

- 1) the importance of innovations (electricity and cars in the 1920s, electronics, information technology and telecommunications in the 1990s);
- 2) high and increasing profits;
- 3) growing stock exchanges speculation, fed by the high profits and expectations of their rising even higher;
- 4) accumulation of short term and long term debts both in the corporate and households sector.

The main determinants of these trends, in PSL’s view, are: (i) market forms; (ii) income distribution; (iii) debt sustainability. PSL’s argument starts from a consideration of how prevailing oligopolistic market forms produced certain consequences in terms of price dynamics and income distribution. Specifically, big firms are able to introduce innovations and, within certain limits, to regulate prices. Thus, when productivity increases more than the increase in demand, prices may remain stable while employment decreases. Such price rigidity with employment flexibility implies that crises take on a new form in modern economies: whereas deflation can certainly occur in terms of reductions in demand, a sharp reduction in prices is a highly unlikely occurrence.<sup>1</sup>

Moreover, the top managers of large oligopolistic firms assign themselves lavish compensations in the form of very high salaries, bonuses and free shares, which greatly contribute to the increase in income inequality. While in the 1920s the share of income going to the highest quintile rose by 6 percentage points, between 1992 and 2001 the gap between the lowest quintile and the highest widened by 4.3

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<sup>1</sup> Already in 2002, PSL noted that “[h]ouses represent a special problem: in certain periods dominated by speculative operations their prices can fall quite suddenly” (*ibid.*, p. 63).

percentage points. PSL adds: “when income inequality increases at least two problems arise: the demand for consumer goods slows down while speculative operations increase, together with the debts contracted to finance them” (*ibid.*, p. 60).

PSL identifies two growing speculative waves: in the stock exchanges and in the real estate markets, adding that “the interests involved are so great that the central bank and major banks, which sometimes join in the speculation themselves, support these waves with their policies” (*ibid.*, p. 61).

As a consequence of these trends, the “essential problem” in the USA economy is the accumulation of debt. Citing Einaudi (1934), PSL strongly highlights the centrality of debts, saying “I am unable to take seriously those who complain or speak of crisis and do not discuss debts” (*ibid.*, p. 64). A former student of Schumpeter, PSL is well aware of the importance of debts to finance investments. However, in Minskyan fashion he highlights the mutual feeds of real and financial cycles. Indeed, according to Sylos Labini, when the conjuncture is favourable, debts are transformed into expenses and thus feed the effective demand for investment and consumer goods, but when the conjuncture is unfavourable, debts contracted just to pay those falling due imply a reduction in effective demand, which feeds a negative spiral.

Sylos Labini considers four kinds of debt: families’, firms’, public and foreign debt. He is especially concerned about the former two. He highlighted how by offering their houses as collateral, families could obtain loans from the banks easily and on good conditions, thus being enabled to buy durable consumers goods that they could not have afforded on their current incomes. Among the main risks of such trend is, evidently, that of a “slump in the price of houses”.

To argue his case, PSL develops a synthetic indicator of sustainability by considering the cumulative difference between the interest rate (as a proxy of the debt burden) and GDP growth (as a proxy of the ability to repay debt). By showing the time series of this indicator for both private and public debt, PSL is able to show that US public debt was well on a sustainable track – despite what many neoliberal economists were saying at the time – whereas private debt was clearly

unsustainable. From this diagnosis, PSL inferred that the USA was necessarily going to face a financial crisis in the private sector, most likely with “strong repercussions not only on Europe but on the whole world”.

In the face of an incipient crisis comparable to what took place in 1929, PSL hopes for international coordination, although he is sceptical on the likelihood of such coordination. He recognizes that a large scale crisis in the hegemon country would likely have more than just economic consequences, e.g. forcing the USA to “put aside its plans for imperialistic expansion”, though he might have been too optimistic about what would replace it (*ibid.*, p. 73).

In his conclusions, PSL highlights one of the main topics of his lifelong research: the mutual nexus between civic and economic development. Sylos Labini’s words are worth quoting at length:

“[t]he squalor of the economic prospects is accompanied by squalor in our civil life. I think that we have to react by adopting a strategy in two, partly overlapping stages, [...] addressing the economic crisis of the industrialized countries and then aid to the hungry countries. [...] In the second stage this strategy would imply the engagement of many people in remunerated and voluntary activities, and would offer ideals worth pursuing for the new generations, in the place of the obsessive pursuit of money dominating and impoverishing social life in the advanced countries today: young people have, as it were, a biological need of ideals” (*ibid.*, p. 78).

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