# Fiscal Transfers to Capitalists*

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It is common for governments these days to provide fiscal transfers to capitalists, whether through reduced corporate tax rates, or by providing direct cash subsidies, to encourage greater investment by them and thereby stimulate the economy. During Donald Trump's first presidency there had been a cut in corporate tax rate with this objective in mind. In India the Modi government, as is well-known, has given massive tax concessions with the same objective. Even a minimum knowledge of economics however would show that such transfers to capitalists are counter-productive in a neoliberal regime.

This is because such a regime is characterised by "fiscal responsibility" legislation that fixes the upper limit to the fiscal deficit as a percentage of the gross domestic product, and normally the government operates at this ceiling; transfers to the capitalists therefore have to be matched by reductions in expenditure elsewhere, typically in welfare expenditures undertaken for the working poor, or by an equivalent increase in tax revenue garnered from the working poor. Now, the effect of handing over, say, Rs 100 to the capitalists by reducing transfers to the workers by Rs 100, is to reduce the level of aggregate demand and hence employment and output; far from reviving the economy, transfers to capitalists have the effect of further contracting the economy. The way in which this comes about is the following.

Investment undertaken in any period is the result of investment orders given earlier, and hence of investment decisions taken in the past; this is so because investment projects have long gestation periods and it is as true of private investment as of public investment. If the tempo of investment is to be stepped up, then a decision for doing so will be taken in the current period and the actual tempo will increase only subsequently. Hence investment in any period must be taken as a given magnitude that does not change during the period in question. What does change during the period in question is the level of consumption; and here, because the workers consume a higher share of their incomes than the capitalists, any shift of purchasing power from workers to capitalists has the effect of lowering consumption (the same happens if the government reduces its consumption in order to make transfers to capitalists).

What is more, transfers from workers to capitalists (and even from the government to capitalists) have the effect of reducing net exports (that is, the excess of exports over imports), since capitalists' consumption is more import-intensive. But let us deliberately understate our argument by assuming that transfers to capitalists, that are financed at the expense of the workers, do not change net exports. Since the gross national income, Y, of a country must equal the sum of consumption C, investment I, government expenditure G, and the surplus on the current account of its balance of payments (X-M), that is,

$$\mathbf{Y = C + I + G + (X\text{-}M) \quad \ldots\ldots \quad (i)}$$

transfers to capitalists, by lowering C, lower the right-hand side, which depicts the level of aggregate demand. The equality in the above equation therefore can be

restored only through a fall in Y, that is, through a reduction in output and employment.

When this happens, the degree of unutilised capacity in the economy increases, which has the effect of lowering the investment decisions of the capitalists taken in the current period and hence their actual investment in the subsequent period. The economy, therefore, far from getting stimulated, actually contracts.

But the story does not end there. Any such contraction in itself, that is, if other things remain the same, has the effect of reducing profits. Thus while transfers to capitalists as such, have the effect of increasing profits, the fact that such transfers are obtained by reducing the purchasing power of the workers, have the opposite effect, of reducing profits. And under fairly realistic assumptions, these two effects cancel each other out exactly, so that total profits of the capitalists remain exactly the same as would have obtained without the transfers. The assumption under which this result holds is that the working people consume their entire income.

This is a fairly realistic assumption because the proportion of the total wealth of the economy that is owned by the bottom segment of the population is quite minuscule. In India for instance the bottom 50 per cent own only 2 per cent of the total wealth of the country; since all wealth necessarily arises from savings, this only shows that they scarcely save anything at all. Hence our assumption that the working people do not save and that the entire savings in the economy come from the rich, apart from the government, is quite realistic.

Let us, only for a moment, assume that the rich, in this case the capitalists, save their entire income; then private savings equal profits. Since in any economy, total domestic savings must equal total domestic investment minus the inflow of foreign savings, and since government investment minus government savings is what is called the fiscal deficit, this amounts to saying that private savings, and hence profits, in the economy, must necessarily equal private investment plus the fiscal deficit minus foreign savings F coming into the economy during the period; that is,

**Profits = Private Investment + Fiscal Deficit – F …(ii)**

Since we have argued that private investment and the inflow of foreign savings (which is the just the negative of X-M above) will remain unchanged during the period, as will the fiscal deficit because of the "fiscal responsibility" legislation, profits must remain the same despite the transfers to capitalists.

Dropping the assumption that all profits are saved makes no difference to the above argument. If a proportion $\alpha$ of profits is saved, then equation (ii) simply becomes:

**$\alpha$. Profits = Private Investment + Fiscal Deficit – F… (iii)**

If the right-hand side of (iii) remains unchanged, for reasons we have just discussed, then profits must also remain unchanged even if $\alpha$ is not equal to one. Budgetary transfers to the capitalists in short, in a neoliberal regime where the fiscal deficit cannot be increased to finance such transfers and where, therefore, workers' incomes have to be reduced correspondingly, have the effect not only of precipitating a contraction in output and employment, but of not even increasing the magnitude of capitalists' income if the workers consume their entire income.

Budgetary transfers to the capitalists in other words cause inequality to increase in an economy without even increasing the capitalists' income, because they cause an output contraction that negates the profit-increasing effects of such transfers.

They do however have one other important effect which is the real reason why the government resorts to them, and that is to change the distribution of profits among the capitalists in favour of the monopoly stratum, away from non-monopoly capitalists. This is so for the following reason. We have seen that total profits remain unchanged despite budgetary transfers to capitalists because while transfers are an addition to profits, the fact that they are associated with taking away incomes from the workers, and reducing aggregate demand, lowers profits to an exactly equal extent; but while this is true in the aggregate, the capitalists who face reduced demand and the capitalists to whom the bulk of the transfers accrue are not the same. In particular, large capitalists are not affected much by the reduction in workers' consumption demand; but they get the lion's share of the budgetary transfers. They are therefore net gainers, while smaller capitalists whose presence is more pronounced in the market for workers' consumption goods, become net losers, even when total profits remain unchanged at the aggregate level.

Budgetary transfers to the capitalists are thus a means of aiding what Marx had called "centralisation of capital", of hastening the replacement of smaller capitals (or even petty producers who produce goods for workers' consumption) by large capitals. This is what its "crony capitalists" want and the government obliges them. Such transfers are undertaken in the name of stimulating the economy, but they do nothing of the sort; on the contrary they succeed only in contracting the economy, but even in such a contracting economy, they strengthen the position of the monopoly capitalists.

There is some recognition in the media and among opposition parties that small producers in the country were harmed by demonetisation and the introduction of the Goods and Services Tax. There is however less recognition of the harm done to them by the tax concessions and other forms of budgetary transfers made to the capitalists.

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