

Cheap Wars

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Capitalism and War

The recent flurry of wars – from Afghanistan and Iraq to Gaza and Lebanon – has revived talk of Imperialism, Military Keynesianism and the Military-Industrial Complex. Capitalism, many radicals have long argued, needs war. It needs it to expand its geographical reach; it needs it to open up new markets; it needs it to access cheap raw materials; and it needs it to placate opposition at home and pacify rebellious populations abroad.¹

The common perception is that war serves to boost the economy. According to this argument, military conflict – and high military spending in preparation for such conflict – generates overall growth and helps reduce unemployment. This feature of military spending turns it into an effective fiscal tool. In years of slack, the government can embark on Military Keynesianism, increase its spending on weapons and pull the economy out of recession.

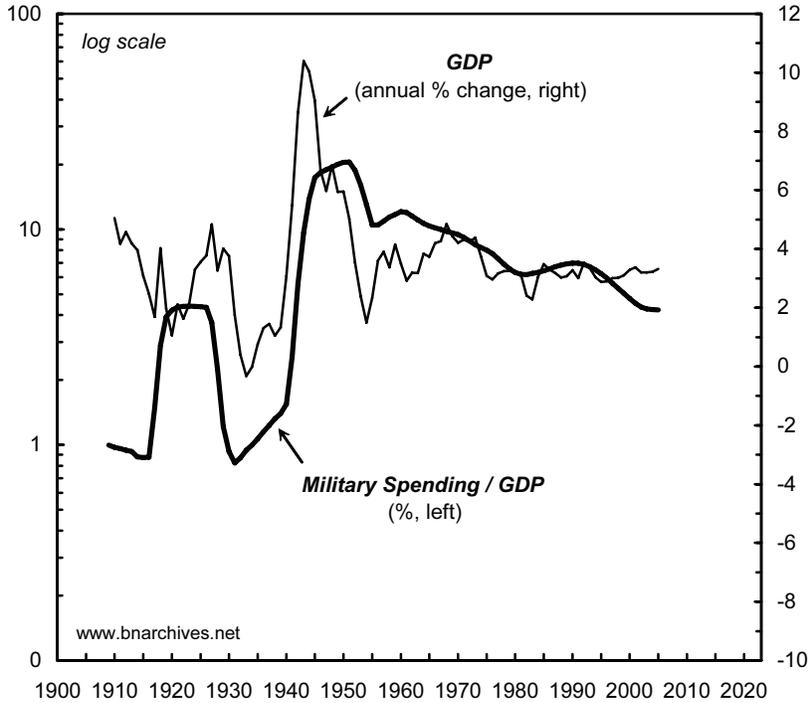
Over the longer haul, military expenditures are said to undermine the peaceful, civilian outlook of liberal regimes. Spending on the military boosts the business interests of the large armament corporations, hardens the outlook of the security apparatus and emboldens the top army brass. Together, these groups become increasingly fused in an invisible, yet powerful, Military-Industrial Complex – a complex that gradually comes to dominate policy and pushes society toward foreign aggression and military adventurism.

The Rise and Demise of Military Keynesianism

Theories of Military Keynesianism and the Military-Industrial Complex became popular after the Second World War, and perhaps for a good reason. The prospect of military demobilization, particularly in the United States, seemed alarming. The U.S. elite remembered vividly how soaring military spending had pulled the world out of the Great Depression, and it feared that falling military budgets would reverse this process. If that were to happen, the expectation was that business would tumble,

¹ Not all radical thinkers share this view. Some argue, to the contrary, that war and militarization, although embedded in and often caused by the capitalist reality, are harmful to capitalism and undermine its vitality.

1. U.S. Military Spending and Economic Growth



NOTE: Series shown as 10-year moving averages.
 SOURCE: U.S. Department of Commerce: GDP (GDP), GDP in constant prices (GDPR), military spending (GFML); Data for years prior to 1929 are from Gleditsch et al. *The Peace Dividend* (Elsevier, 1995) and from the BCA Research Group.

unemployment would soar, and the legitimacy of free-market capitalism would again be called into question.

Seeking to avert this prospect, in 1950 the U.S. National Security Council drafted a top-secret document, NSC-68. The document, which was declassified only in 1977, explicitly called on the government to use higher military spending as a way of preventing such an outcome.²

NSC-68 marked the birth of Military Keynesianism. In the decades that followed, military expenditures seem to have worked as the document envisaged. The basic process is illustrated in Figure 1. The graph shows the relationship between U.S. economic growth and the country’s military spending. The thin line plots the

² United States, National Security Council, [NSC 68: United States Objectives and Programs for National Security. A Report to the President Pursuant to the President’s Directive of January 31, 1950. Top Secret.](#) Washington DC, 1950.

annual rate of economic growth against the right scale. The thick line shows the level of military spending, expressed as a share of GDP and plotted against the logarithmic left scale.³ Both series are smoothed as 10-year moving averages to emphasize their long term tendencies.

The data show a co-movement of the two series, particularly since the 1930s. The rise in military spending in preparation for the Second World War coincided with a massive economic boom. Military spending had risen to 43 percent of GDP by 1944 and averaged 20 percent of GDP during the 1940s. This rise was accompanied by soaring economic growth, with annual rates peaking at 18 percent in 1942 and averaging 6 percent during the 1940s (the peak levels of the early 1940s cannot be seen in the chart due to the smoothing of the series).

After the war, military spending began to trend downward, but remained at very high levels for the next couple of decades. The adoption of Military Keynesianism, along with the wars in Korea and Vietnam, helped keep military expenditures at 12 percent of GDP during the 1950s and at 10 percent during the 1960s. Economic growth during this period averaged over 4 percent – lower than in the Second World War, but rapid enough to sustain the buoyancy of American capitalism and the confidence of its capitalists.

Both big business and organized labor supported this set up. The large corporate groups saw military spending as an acceptable and even desirable form of government intervention. At the aggregate level, these expenditures helped counteract the threat of recession at home and offset the loss of civilian markets to European and Japanese competitors – yet without undermining the sanctity of private ownership and free enterprise. At the disaggregate level, many large firms received lucrative contracts from the Pentagon, handouts that even the staunchest free marketers found difficult to refuse.

The large unions endorsed Military Keynesianism for different reasons. They agreed to stay out of domestic politics and international relations, to accept high military expenditures, and to minimize strikes in order to keep the industrial peace. In return, they received job security, high wages and the promise of ever-rising standards of living.

The consensus was aptly summarized in 1971 by President Nixon, who pronounced that ‘we are all Keynesians now.’

But that was the peak. By the early 1970s, the Keynesian Coalition of big business and organized labor started to unravel, Military Keynesianism began to wither and the welfare-warfare state commenced its long decline.

³ A logarithmic scale has the effect of amplifying the size on the chart of smaller values and compressing the size of larger ones. This transformation is useful when there are very big jumps in the data – such as during the 1940s – jumps that would otherwise make the variations of smaller values look too miniscule to discern on the chart.

The Globalization of Ownership

Underlying the rise and demise of Military Keynesianism was an epochal reversal in the spatial nature of ownership – a U-turn from gradual de-globalization in the first half of the century to massive globalization in the second half.

Until the 1950s, the ownership of capital, in the United States and elsewhere, was retreating into its national cocoons. The statistical footprints of the process are clear. In 1900, the ratio of foreign-held assets to world GDP reached a peak of 19 percent. But the subsequent turmoil of two world wars, depression, import substitution and capital controls have taken a heavy toll. Foreign ownership ties were broken or frozen, and the ratio of foreign-held assets to world GDP fell continuously, reaching a mere 6 percent in 1960. At the trough of the process, the accumulation of capital was conducted largely within national boundaries.

This decline ended in the early 1970s. Capital again broke through its national envelope, and as neoliberalism and deregulation gained momentum foreign ownership started to rise. The ratio of foreign-held assets to world GDP increased exponentially, doubling every decade: it rose to 25 percent in 1980, climbed to 50 percent in 1990, and reached over 90 percent by 2000.⁴

The effect on profit of this reversal has been dramatic. U.S.-based firms now receive roughly one third of their earnings from their foreign subsidiaries, up from 5 percent in the 1950s – a six-fold increase.

This reversal in the global pattern of ownership fundamentally altered the power structure and institutions of capitalism. With capital bought and sold on a world scale and profits increasingly earned outside the country, capital accumulation became less and less reliant on domestic sales. With less emphasis on local activity, Keynesian policies grew out of fashion. And with Keynesianism on the decline, the business-labor accord started to unravel.

The welfare state, previously seen as a bulwark against communism, became a burden. Labor was no longer likely to revolt – particularly with jobs being shipped to ‘emerging markets’ and with union membership on the decline. Furthermore, capitalists were no longer fearful of recession. On the contrary, they often encouraged it as a means of disciplining workers, reducing wages and reversing the hard-won social gains of working people.

The warfare state was also coming under pressure. The turning point was the collapse of Soviet Bloc. With only one superpower remaining, large military budgets were now difficult to justify. In the 1990s, military spending around the world took a nose dive, falling by as much as 1/3rd from their all time peak in the late 1980s. As Figure 1 shows, expenditures on armaments in the United States, the world’s largest

⁴ Data on the ratio of foreign assets to GDP are from Maurice Obstfeld and Alan M. Taylor, *Global Capital Markets: Integration, Crisis and Growth* (Cambridge: Cambridge University Press, 2004), pp. 52-53, Table 2-1.

spender, dropped to an average of 4.5 percent of GDP in the first half of the 2000s, down from 7 percent in the 1980s.

The New Wars

The demise of the welfare-warfare state opened the door for the new rhetoric of *neo-liberalism*. Proponents of free markets hailed the new regime for its peaceful tendencies. Its detractors agreed – but only partly. On the one hand, they concurred that neoliberalism, in its quest to secure free trade and open capital flow, tries to establish political stability and international peace. On the other hand, they faulted neoliberalism for its invisible violence, inflicted through hyper exploitation, mass poverty, rising inequality, economic uncertainty and human insecurity.

Both the adherents and the critics, therefore, were surprised by the sudden bellicosity of the early twenty-first century. Old theories of imperialism and militarism were quickly dusted off and tucked onto neoliberalism. Instead of productivity miracles and No Logo, analysts started to talk about ‘new imperialism’ and ‘neoliberal wars.’

For the most part, though, these hybrid theories are misleading. The new conflicts of the twenty-first century – the ‘infinite wars,’ the ‘clashes of civilization,’ the ‘new crusades’ – are fundamentally different from the ‘mass wars’ and statist military conflicts that characterized capitalism from the nineteenth century until the end of the Cold War. The main difference lies not so much in the military nature of the conflicts, as in the broader role that war plays in capitalism.

To begin with, in a world open for business there is no need to physically conquer new territory – not for raw materials and not for additional markets (note that Iraqi oil production has nearly ceased since its conquest in 2003, while its market for foreign imports, negligible to begin with, has contracted).

The same goes for military spending: with the share of foreign profits soaring, there is no longer a business imperative for high military expenditures. While U.S. military budgets have risen marginally in the wake of the new wars – from 3.9 percent of GDP at the end of Clinton’s presidency to 4.7 percent presently – this is an increase whose effect on aggregate demand is insignificant by historical standards.

The U.S. attacks of the 2000s also make little military sense. Countries with proven nuclear capabilities, such as Pakistan and North Korea, have been left alone, while others that presented no real danger – specifically Afghanistan and Iraq – were invaded, occupied and now tie down much of the U.S. standing army, with no end in sight.

Finally, the televised war footing and constant talk about terrorism may have frightened the western population. But unlike the success of nationalist-liberal ideologies during the two world wars and the Cold War that followed, the new rhetoric of infinite war hasn’t made the masses fall for neoliberal capitalism.

The wars of the 2000s are indeed new. And they are new, at least in part, because capitalism itself has changed.

The New Order of Capital

The central change concerns the underlying nature of capital, a transformation that began in the late nineteenth century but became evident only recently.

Existing theories, anchored in the reality of the early nineteenth century, continue to examine capital from the 'material' perspective of consumption and production. Neoclassical economists anchor their analysis in utility, while classical Marxists base it on labor time. In contrast to these approaches, we suggest that, under modern conditions, capital can no longer be viewed as a 'material' entity. As we see it, capital represents neither neoclassical utility nor Marxist abstract labor, but rather power – the power of its owners to shape the process of social reproduction as a whole.

Based on a power understanding of capital, we argue, first, that the analysis of capitalism should focus not on capital 'in general' and many capitals 'in competition,' but specifically on the *dominant capital* groups at the centre of the political economy. Second, we claim that accumulation should be understood not absolutely, but *differentially* – that is, in reference to the ability of dominant capital to 'beat the average' and increase its relative power.⁵

The implications of this power perspective are far reaching. For our purpose here, they suggest:

1. That over time, corporate mergers, rather than economic growth, become the main engine of differential accumulation ('breadth'); and
2. That under certain circumstances, dominant capital can benefit greatly from inflation and stagflation ('depth').

In our research we found that, over the past century, global accumulation indeed oscillated between these two regimes of merger and stagflation. The most recent phase, which lasted through much of the late 1980s and 1990s, was clearly one of breadth. In that period, dominant capital benefited greatly from the opening up to corporate takeover of the former Soviet Union and other 'emerging markets,' as well as from the collapse of the welfare state and the massive privatization of government services.

This breadth cycle, with its emphasis on neoliberalism, deregulation, sound finance and disinflation, came to a close at the turn of the new millennium. The financial crisis that began in Asia and later spread to the core markets, the crumbling of

⁵ These issues are articulated in Jonathan Nitzan and Shimshon Bichler, '[Dominant Capital and the New Wars.](#)' *Journal of World Systems Research*, 2004, Vol. 10, No. 2, pp. 255-327.

the 'new economy' and its scandalous accounting practices, and talk of global terrorism and the infinite war to defeat it, have together made capital movement look less tempting and mergers far less promising. Furthermore, two decades of neoliberalism have weakened pricing power, raising the specter of price and debt deflation for the first time since the Great Depression.

Faced with these predicaments, capitalists generally and dominant capitalists particularly began yearning for a little dose of 'healthy' inflation both to avert debt deflation and to kick-start differential accumulation. As it turned out, the solution for their predicament – intended or otherwise – was a new 'Energy Conflict' in the Middle East (that is, a conflict related directly or indirectly to oil). Over the past thirty-five years, these conflicts have been the prime mover of oil prices, and oil prices have provided the spark for broad-based inflation. It was a turnkey mechanism for triggering inflation, and it was read to use.

In this sense, military conflict has come to assume a new, roundabout role in the accumulation process. Until the 1950s and 1960s, the main impact of military conflict worked through large military budgets which directly boosted aggregate demand and overall profits, as well as the income of the leading military contractors. But with the re-globalization of ownership and the on-setting of détente, military budgets started to contract. Initially, they fell relatively, as a share of GDP, but since the late 1980s, they also began to drop absolutely, in constant dollar terms. Although these expenditures still nourish the military contractors, their direct effect on capital accumulation has diminished significantly.

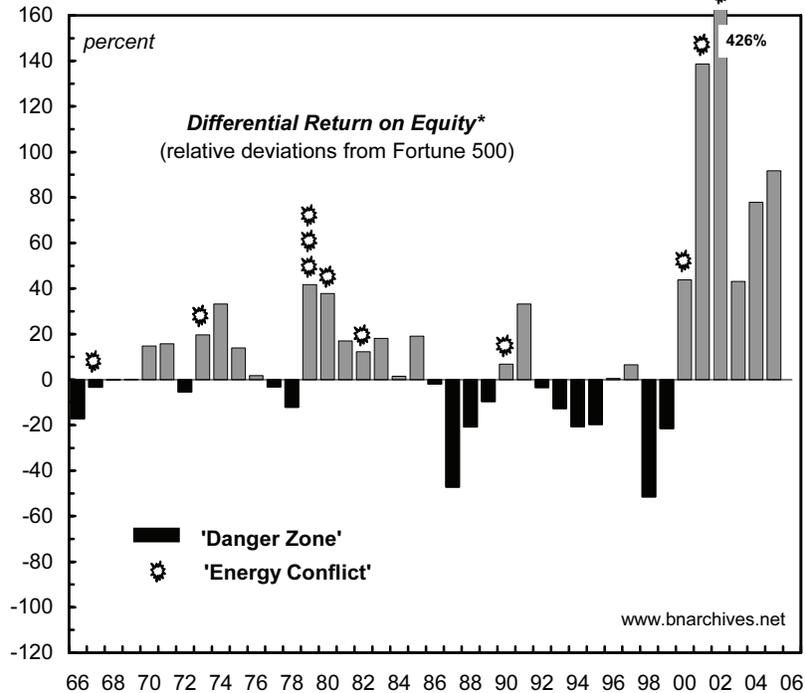
However, military conflict as such hasn't lost its appeal; it still has a big impact on accumulation. The novelty is that the impact now works mostly *indirectly*, through inflation, relative prices and redistribution.

Energy Conflicts and Differential Profits

The key beneficiaries of this new, indirect link are the large oil companies. The geographic centre of this process is the Middle East. After the Vietnam War, the Middle East has become the hot spot of global conflict, with obvious corollaries for the price of oil. The relationship between these conflicts and the differential profits of the oil companies, however, has received little or no attention.

The reason for this neglect is not difficult to see. Most analyses of Middle-East conflict and oil are situated in the disciplinary intersection of 'international relations' and 'international economics.' Their basic reasoning boils down to a statist struggle over raw materials. On the one hand, there are the industrialized countries that need cheap oil in order to sustain their growth and expanded reproduction. On the other hand there are the countries of the Middle East, organized through OPEC, whose intention is to extract from the process as much rent as they can. This broad conflict is complicated by various factors: for example, inter-state rivalry – say between the United States and the Soviet Union (previously) and Europe and Asia (presently);

2. Leading Oil Companies: Differential Profits



* Difference between the return on equity of the oil companies and of the Fortune 500, expressed as a per cent of the return on equity of the Fortune 500.
 NOTE: The leading oil companies include British Petroleum (BP-Amoco since 1998), Chevron, Exxon (ExxonMobil since 1999), Mobil (until 1998), Royal-Dutch/Shell and Texaco (until 2000). Company changes are due to merger. Until 1993, the Fortune 500 included only industrial corporations (firms deriving at least half their sales revenues from manufacturing or mining). From 1994 onward, the list includes all corporations. For 1992-3, data for Fortune 500 companies are reported without SFAS 106 special charges.
 SOURCE: Fortune and Compustat.

religious and ethnic hostilities in the Middle East itself; or the interests of various sectors and capitalist fractions in the industrialized countries.

In this polemic of high politics and resource economics, few have bothered to break through the aggregate front, fewer have done empirical work, and almost no one has dealt with the question of how exactly accumulation by the oil companies fits into the picture. Figure 2 offers a glimpse into what is missing from the story. The chart shows the history of differential accumulation by the 'Petro-Core' of leading oil

companies – specifically, BP, Chevron, Exxon, Mobil, Royal-Dutch/Shell and Texaco.⁶

Each bar in the figure measures the difference between the rate of return on equity of these companies and the average rate of return on equity of the Fortune 500 benchmark (with the result expressed as a percent of the Fortune 500 average). The grey bars show years of differential accumulation; that is, years in which the leading oil companies beat the average with a higher rate of return. The black bars show periods of differential *decumulation*; that is, years in which the leading oil companies trailed the average. For reasons that will become apparent in a moment, these latter periods signal ‘danger’ in the Middle East. Finally, the explosion signs show ‘Energy Conflicts’ – namely, conflicts that were related, directly or indirectly, to oil.⁷ The figure exhibits three related patterns, all remarkable in their persistence:

- First, *every* energy conflict in the Middle East was preceded by a danger zone, in which the oil companies suffered differential *decumulation*.
- Second, *every* energy conflict was followed by a period during which the oil companies beat the average.
- And, third, with only one exception in 1996-7, the oil companies *never* managed to beat the average without an Energy Conflict first taking place.⁸

Furthermore, this pattern fits into the larger processes of breadth and depth. The figure points to three distinct periods, each characterized by a different regime of differential accumulation, and each led by a different faction within dominant capital.

During the depth era of the 1970s and early 1980s, differential accumulation was fuelled by stagflation and driven by conflict. The leading faction within dominant capital was the Weapondollar-Petrodollar Coalition of large armament and oil firms. In this context, the oil companies managed to *beat* the average comfortably, with only occasional setbacks which were quickly corrected by Middle East conflicts.

During the breadth period of the late 1980s and 1990s, merger replaced inflation as the main engine of differential accumulation. The oil and armament companies

⁶ Due to mergers, the data in Figure 2 pertain to British Petroleum until 1997 and to BP-Amoco since 1998; to Chevron and Texaco until 1999 and to Chevron-Texaco since 2000; to Exxon and Mobil until 1998 and to ExxonMobil from 1999; and to Royal-Dutch/Shell throughout.

⁷ The conflicts include the 1967 Arab-Israeli conflict; the 1973 Arab-Israeli conflict; the 1979 Israeli invasion of Lebanon; the 1979 Iranian Revolution; the 1979 Soviet invasion of Afghanistan; the 1980 beginning of the Iraq-Iran War; the 1990/1 first Gulf War; the 2000 beginning of the second *Intifada*; the 2001 Coalition invasion of Afghanistan; and the 2003 Coalition invasion of Iraq (whose publicized preparation began in 2002).

⁸ Although there was no ‘official’ conflict in 1996-7, there was plenty of violence, including an Iraqi invasion of Kurdish areas and U.S. cruise missile attacks.

lost their primacy to a 'new economy' coalition led by civilian high-tech companies. Neoliberal rhetoric replaced the lingo of welfare-warfare state, conflicts in the Middle East grew fewer and farther between, and the oil companies commonly *trailed* the average.

Events over the past few years suggest that this second period may have come to an end, with the ebbing of the merger boom and the return to primacy of the Weaponodollar-Petrodollar Coalition. The latter coalition, whose fortunes had dwindled since the stagflationary bonanza of the 1970s and early 1980s, has come back with a vengeance. Having helped re-install the Bush family in the White House, the coalition started looking for new enemies and was only too happy to exploit the opportunity offered by the 'new Pearl Harbor' of September 11.⁹

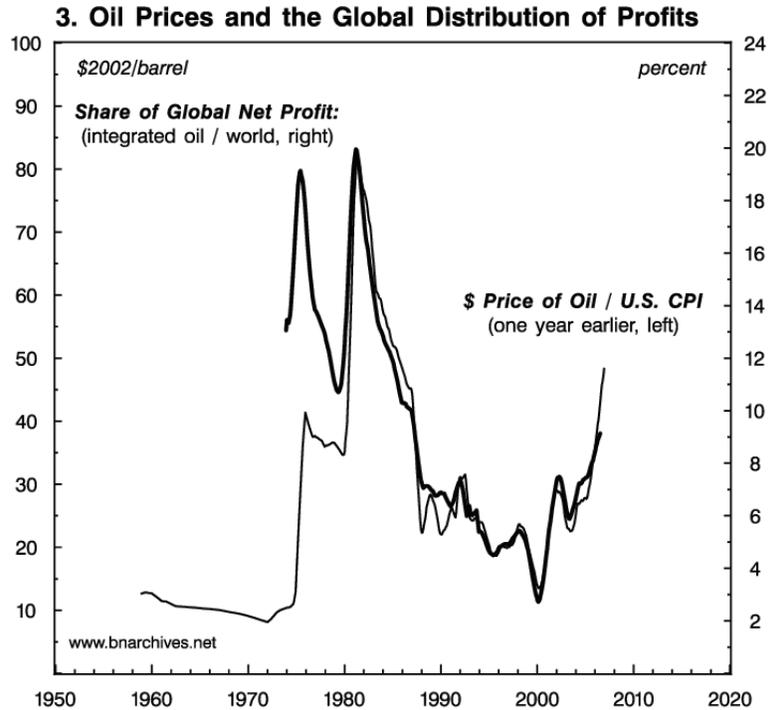
The argument and statistical patterns presented here were first articulated in the late 1980s, further developed in the mid-1990s, and most recently updated in 2006.¹⁰ However, the last few observations in Figure 2 are new, and they suggest a quantitative departure from past patterns. Until the late 1990s, the differential performance of the oil companies oscillated between 50 percent above or below the Fortune 500. Recently, though, the scale changed. During the period of 2000-2005, the world's

⁹ In 2003, as the Iraq war unfolded, we wrote the following text:

Our own view is that Middle East conflicts were integral to the power processes of global accumulation. . . . In the process, [the Weapondollar-Petrodollar] coalition had become increasingly fused with its 'parent' governments on the one hand and its OPEC 'hosts' on the other, leading to a growing 'capital-state symbiosis' between them. Whether or not there was 'conspiracy' here, and what the precise nature of such a 'conspiracy' was, remains an open question. Unfortunately, these types of issues are not the usual staple of primetime television. Occasionally, however, the truth does come to light, albeit with a little delay. . . . Perhaps in due course someone will publish the secret 'Exxon Papers' or a declassified 'NSC Report on Energy and War in the Middle East,' thereby opening a window into the backroom story of Energy Conflicts in the region (['Dominant Capital and the New Wars.'](#) *Journal of World Systems Research*, 2004, Vol. 10, No. 2, p. 313).

As it turned out, the relevant documents surfaced rather quickly. Less than a year after the publication of our paper, Greg Palast uncovered the existence of two secret – and rather different – plans for the future of Iraq's oil. The 2003 U.S. invasion of Iraq, Palast argued, reflected the conflicting strategies of two opposing factions. The first, vocal faction, led by the neo-cons and the Pentagon, planned to privatize Iraqi oil, flood the market and undermine OPEC. The other faction, led by the large oil companies and elements within the State Department, shared none of these fantasies. It let the neo-cons finish the job of conquering Iraq, and then sent its representatives to take control of the country's oil production. In the end, there was no privatization, no flooding of the market and no undermining of OPEC – an organization of which the United States, as the ruler of Iraq, was now a de-facto member. See Greg Palast, ['Secret US Plans for Iraq's Oil.'](#) *BBC News*, March 17, 2005; Greg Palast, *Armed Madhouse* (New York: Dutton, 2006).

¹⁰ Jonathan Nitzan and Shimshon Bichler, ['New Imperialism or New Capitalism?'](#) *Review*, 2006, Vol. XXIX, No. 1, pp. 1-86.



four leading oil companies earned \$338 billion in net profit – *one third of a trillion* – representing an average rate of return of 20 percent, nearly twice the Fortune 500’s.

The Primacy of Prices

The link that connects Middle-East conflicts and differential profitability is the price of oil. This link is illustrated in Figure 3. The thick line in the chart shows the percent share of all listed oil companies in global corporate profit. The thin line shows the ‘relative’ price of crude oil, computed by dividing the dollar price per barrel by the U.S. consumer price index, and lagged one year (reported corporate earnings represent the moving sum of the past four quarters; the full impact on profit of a change in the price of oil therefore is felt only after a year).

The correlation between the two series is extremely tight.¹¹ This statistical fact points to the immense importance that prices have come to play in the process of accumulation. In this particular chart, the tight correlation makes much of the media discussion and learned analyses of the oil arena redundant. In order to know the reported differential profits of the oil companies a year from now, you don't need to speculate about Peak Oil, about rising demand from China, or about the coming heat waves in Europe. This type of guesswork, although interesting for other purposes, is unnecessary here. The only thing you need to know is the current price of oil.

To illustrate: the official data are not yet in, but we already know that, over the past 12 months, the price of oil averaged roughly \$65 in 2002 dollars. The correlation in the chart suggests that, a year from now, the reported global profit share of the oil companies will hover around 15 percent.

Now, let's backtrack and examine the history presented in Figure 3. The data show that, during the oil crisis of the 1970s and early 1980s, the cost of crude petroleum shot through the roof. In 1979 a barrel of oil cost over \$90 in today's prices. During those happy stagflationary times, the oil companies pocketed nearly 20 percent of all global profits. But as differential accumulation moved into breadth and mergers picked up, inflation fell and oil prices dropped even faster. The oil companies' global share of profit collapsed, reaching a mere 3 percent by the end of Clinton's presidency.

The reversal came with the new millennium and the Bush presidency. With the 2001 invasion of Afghanistan, the Middle East entered a protracted period of war, oil prices have risen to \$65-75, and the share of the oil companies in global profit – although not yet at historical highs – is moving higher and higher.

How big are the gains of the oil companies? During the five-year period from August 2001 to July 2006, the average net income of the global oil sector amounted to \$108 billion per annum. This figure compares with an annual profit of only \$34 billion in the year from August 1999 to July 2000 – a jump of \$75 billion if we round the numbers.

How much did it cost to generate this jump in profits? For argument's sake, let's assume that since 2000 the entire increase in the price of oil – and therefore the whole increase in oil profits – was due to the new Energy Conflicts in the Middle East. Assume further that so far the U.S. government has spent on its Afghanistan-Iraq operation the annual equivalent of 1 percent of its GDP – roughly \$100 billion a year.

These assumptions, although simplistic and inaccurate, indicate the overall magnitudes involved: the war costs \$100 billion a year and it generates an extra \$75 billion in annual oil profits. In other words, for every \$1 the U.S. government spends on the wars, the owners of the oil companies earn an additional €75 in net profit.

¹¹ The correlation coefficient between the two monthly series measures 0.80 (out of 1) for the period since January 1974, and 0.92 for the period since January 1979.



SOURCE: IMF: L64@C111 (consumer prices), L65EY@C111 (hourly wage);
Compustat: I0010 (S&P 500 Composite).

Clearly, such phenomenal cost-benefit ratios can be generated only indirectly. And that is perhaps one of the important features of the new wars: a fairly modest increase in military spending brings about massive changes in prices and distribution – changes that go beyond the immediate arena of the conflict, and whose magnitude can match and even exceed the military budget itself.

Sweet Inflation

As noted earlier, the new wars came as the long breadth phase of differential accumulation was winding down. The immediate beneficiaries were the arms contractors and the oil companies of the Weapondollar-Petrodollar Coalition. But gradually, as global differential accumulation shifted from breadth to depth, the gains spread to dominant capital as a whole.

Figure 4 vividly illustrates this process for the United States. The thin line in the graph plots the rate of inflation, measured as the annual rate of change of the consumer price index. The thick line is a ratio between profits and wages. It measures the ratio of the earnings per share of the S&P 500 (the largest publicly traded corpo-

rations listed in the United States, which could be taken as a proxy for dominant capital) to the hourly wage rate in manufacturing.

Movements in this latter ratio indicate redistribution. When the index rises, it means that the profits of dominant capital rise faster (or fall more slowly) than the wage rate. When the index falls it suggests an opposite process – namely, that the profits of dominant capital fall faster (or rise more slowly) than wages.

As the chart shows, in late 2000, inflation started falling, and in 2002 it reached 1 percent – a postwar low. The decline was accompanied by a massive drop in the ratio of profit to wages, which fell by 55 percent from its 2000 peak. In the wake of these developments, the Federal Reserve Board Chairman, Alan Greenspan, warned of an ‘unwelcome substantial fall in inflation,’ and was encouraged by leading financiers to ‘go for higher inflation.’¹²

These deflationary warnings came in April 2003, after the U.S. had already invaded Iraq. Our own view at the time was rather different. In January 2003, just before the invasion, we wrote:

. . . if oil prices continue to rise, inflation will most likely follow, the spectre of deflation will be removed and the large companies could sound a big sigh of relief. For these companies there would also be an icing on the cake. Inflation usually works to redistribute income from labour to capital and from small firms to larger ones. It will therefore make the leading companies better off relatively, if not absolutely.¹³

And indeed, Greenspan didn’t have to work too hard. The new wars have done the job for him. The neo-conservatives sent their army to the Middle East, the price of oil soared, and inflation – although hesitant at first – eventually started to follow.

The distributional consequences weren’t lost on investors and workers. While wages remained flat, profits – particularly those earned by dominant capital – surged. As a result, the ratio of profit to wages climbed rapidly – rising 250 percent since 2001 and sending the overall share of profit in GDP to its highest level since data began to be collated in 1929.

The huge distributional impact of a small increase in inflation is symptomatic of the new order. During the welfare-warfare state, inflation usually involved a wage-price spiral that worked to limit the differential increases in profits. For instance, a 4 percent increase in prices typically would be accompanied by a rise in wages – say, of 3 percent. A result, the markup ratio of sales to wages would increase by 1 percent, generating a relatively modest rise in profits. The situation now is very different.

¹² Alan Greenspan, ‘Testimony of Chairman Alan Greenspan Before the Joint Economic Committee,’ U.S. Congress, May 6, 2003; Bill Dudley and Paul McCulley, ‘Greenspan Must Go For Higher Inflation,’ *Financial Times*, April 23, 2003, pp. 17.

¹³ Jonathan Nitzan and Shimshon Bichler, ‘[It’s All About Oil](#),’ *News From Within*, Vol. XIX, No. 1, January 2003, p. 11.

Workers in the United States are locked in global competition with workers in China, India and other 'emerging markets,' which means that wages do not rise – and sometimes even fall – in the midst of price inflation. In this context, a 4 percent inflation translates to a 4 percent increase in the markup and to a far larger increase in profits.

All in all, then, the new wars are definitely cheap. For a minimal cost, they stir up inflation and generate large increases in profits. But cheap wars have another side to them. They are hard to win.

Cheap Wars

The idea of a mass, 'voluntary' army was born out of the French Revolution. The new soldiers turned out to be cheaper and more loyal than mercenaries, and they fought well. However, the masses needed to be educated so that they could read the newspapers and follow the propaganda – hence the birth of compulsory 'elementary' schooling. Later on, the proles started to demand additional perks. They wanted culture, insurance, pensions and veteran benefits. In the 1910s, the elites cheated them. They sent the masses to be butchered by the millions in the trenches of World War I, and then abandoned those who returned as veterans. This experience raised the ante. In the early 1940s, the citizens-soldiers had to be offered a whole welfare state, so that they would be willing to get butchered, again, in the Second World War. What initially looked like 'soldiers for free' turned out to be a rather expensive way of fighting wars.

The last expensive war was Vietnam. With neoliberal globalization replacing the welfare-warfare state, there was no longer a need for mass armies with high overhead. Instead, the capitalists started to invest in 'smart weapons' that could be operated by high-school dropouts and cause plenty of damage. They abandoned the draft in favor of purely professional armies – partly governmental, partly private.

A similar process has taken place in Israel. During the 1970s, in the hay days of the Israeli welfare-warfare economy, military spending amounted to 25 percent of GDP, the draft included most Jewish citizens (excluding the ultra-orthodox), and the government spent heavily on social services.

But with the breadth regime of the late 1980s and 1990s, Israeli capitalists became decreasingly dependent on the war economy. Israel began its reconciliation with its neighboring Arab states, and the military was both reduced and transformed. Military spending dropped to 6 percent of GDP, and many military activities were privatized. The duration of military service has been shortened, and fewer get drafted. In parallel, the welfare state has been progressively dismantled, with education, public health care and other social services consistently eroding. Hundreds of thousands of guest workers have been brought in, and the labor unions have been reduced to token institutions.

The consequences of this process are illustrated in Figure 5. The chart contrasts the average monthly wage rate with the Tel-Aviv stock price index (both expressed in constant prices and rebased for comparison purposes, with January 1980=100).



NOTE: Monthly series are in constant prices (deflated by the CPI), are shown as 12 month moving averages, and are rebased (January 1980=100).
 SOURCE: IMF: L62@C436 (stock market index); L65@C436 (wage index); L64@C436 (CPI).

The figure shows that, until the early 1990s, the fortunes of workers and capitalists moved more or less in tandem. But with the onslaught of the breadth regime, their roads parted. During the 1990s and early 2000s, wages have hardly increased, while capital gains have risen to the stratosphere.

Israeli reservists, who are now being called to fight in the unfolding war, probably have not seen this graph, but the reality behind it is certainly familiar to them. They know about deteriorating social services, about job insecurity, about overly expensive housing, about the loss of open spaces. They know that getting wounded in a war is a bad deal that yields meager compensation. Most importantly, they know that the elite that sends them to fight doesn't really care about them.

These sentiments are quite explicit and appear regularly in the press. The following is a typical report of the difficulties faced by reserve soldiers:

Defense Minister Amir Peretz has refused to use a law allowing IDF reservists called up for service recently to enjoy an exemption on fines and interest

associated with debts they incur during their call-up period. . . . [The reservists] are furious after discovering they are still required to pay the fines and interest even though they were unable to issue payments on time because they were called up. . . . 'The reservists are forgotten, the way they always forget us,' said one of the [reservists organization's] leaders, Alex Minkovsky. 'We're calling on the social-minded Defense Minister Amir Peretz to wake up and do something. We're flooded by inquiries of reservists who are suffering crises on a daily basis.'¹⁴

Dominant capital has no such complaints. As it turns out, a day before Defense Minister Peretz refused to heed the reservists' plea, his government privatized the country's oil refineries for \$800 million. In an interview, the winning bidder, Tzadik Bino, sounded almost embarrassed:

The state should not have privatized the refineries, and neither should it have privatized El-Al [the national airline], Bezeq [the national phone company] and Magen David Adom [the emergency medical service]. . . . The next stage would be to privatize the IDF. . . . We are still fighting for our existence, and it doesn't pay to transfer strategic assets to private hands.¹⁵

The old warfare-welfare state was dominated by charismatic figure heads, 'leaders' such as Churchill, de Gaulle and Ben Gurion who seemed removed from any 'particular' interests. By contrast, the neoliberal state tends to be populated by retainers – many of them corrupt and criminal – like Bush, Chirac, Berlusconi, Sharon, Netanyahu and Olmert, who don't even try to hide their true loyalties.

The capitalist elite, which is served by and sustains these politicians, no longer bears a clear national attachment. Many of Israel's largest companies are owned by foreign investors and multinational companies. Similarly, most of Israel's large owners – from the Recannatis, to Fishman to Khan – have become global investors. Israel for them is merely one of many assets in a diversified world portfolio. Unlike during the 1970s, when they had all their eggs in the same Israeli basket, now they don't need to worry too much about what happens in the country. Their local holdings represent only a fraction of their investments, and they are highly vendible.

A recent quote from the financial section of the daily *Ha'aretz*, written in the midst of the fighting in Lebanon and Gaza, indicates the extent to which foreign asset diversification has been accepted as natural by 'ordinary' investors:

Over and above the 'regular' risks of emerging markets such as China, Brazil or Russia, Israel has a continuous security risk. . . . This risk cannot be ig-

¹⁴ Tani Goldstein, '[Reservists Want Peretz to Okay Perks.](#)' *Ynet*, August 1, 2006.

¹⁵ Tani Goldstein, '[Bino to Ynet: "There Was No Need to Privatize the Refineries."](#)' Hebrew, *Ynet*, August 1, 2006.

nored even in peace time. The global diversification of investment therefore is not a privilege. It is a necessity. . . . It means that, in the interest of reducing risk, Israeli investors have to permanently allocate a fixed proportion of their assets to investment overseas. How much is 'enough'? Until recently, the convention was 25%, but perhaps the share of foreign assets should be raised to 50%. Our bodies have to stay here. But why should our savings suffer the same fate?¹⁶

Under these circumstances, it is little wonder that the Israeli 'war machine' has lost much of its military edge. The incentive to fight for "one's country" when that country is so socially fractured is much reduced – particularly when confronted with socially embedded and highly motivated religious militias.

And so the cheap wars linger, death and destruction mount, and the profits continue to accumulate.

¹⁶ Ami Ginsburg, '[What Did We Learn From the First Two Weeks of the Second Lebanon War?](#)' Hebrew, *Ha'aretz*, July 28, 2006.