One of the most striking features of the Australian economy is the key role played by large banks and insurance companies. A small number of very large financial institutions not only dominate their own sector of the economy, but also are the biggest owners of shares in manufacturing, mining, transport and retailing companies.

A recent study by Michael Lawriwsky* shows that financial institutions together own 35.3 per cent of the shares in the 226 large Australian corporations in his sample. Individuals hold another 21 per cent of shares while all other companies (including nominees) account for the other 43.7 per cent.

The Australian Mutual Provident Society, for example, owns shares in some 280 of Australia’s largest companies. In many of these companies the AMP is the largest single shareholder. The total value of its shareholdings is a massive $1234.3 million.

The role of institutions like the AMP is certainly important, but it is often misunderstood. In particular, it leads to two persuasive myths.

The first, traditionally popular on the left, sees “money power” as the linchpin of capitalism. Since the banks control the economy the way to break the power of capital is to in turn control the banks. Two traumatic episodes in Australia’s history seemed to confirm this view. Both the 1890s and the 1930s saw massive economic dislocation accompanied by heightened class struggle as the ruling class tried to shift the burden of depression onto the working class. It was easy to cast the banks as the main villains in both cases.

Within the newly formed Australian Labor Party the left embraced this analysis. Frank Anstey (Frank Ashton in Hardy’s Power without Glory), writing in 1916, described how the banks were profiting from the war:

“The essence of capitalist war”, Anstey argued, was “so the nation can levy men - but not Money. Men may die - Money lives. Men come back armless, legless, maimed and shattered - Money comes back fatter than it went, loaded with coupons, buttered with perpetual lien...”

“Out of the war”, he predicted, “will emerge two classes - Bondholders and slaves of Bondholders”.

The very name of Anstey’s pamphlet - The Kingdom of Shylock - powerfully evokes this tradition’s picture of how Australian capitalism really works.

The second myth I want to examine begins from the same observation that banks and other financial institutions are large owners of other capitalist enterprises, but it draws a very different conclusion.

The argument is that the money deposited in banks or paid to insurance companies in premiums comes in the first place from ordinary people. Since these people benefit from the investments made on their behalf by the institution concerned, aren’t they the real owners of the rest of the economy? This particularly applies to mutual insurance companies like the AMP, where there are no shareholders and policyholders legally own all the company’s assets.

Every workers who has a bank deposit or an insurance policy and who receives interest or bonuses from his/her bank’s or insurance company’s investments has therefore become a little capitalist. So much for outdated ideas like class struggle between workers and capitalists!

Both these myths seriously obscure the real role the finance sector plays in the Australian economy, as I will try to show in these Notes.

Highly concentrated

The total assets of all financial institutions in Australia come to about $82,000 million - almost exactly one full year’s Gross Domestic Product. These assets are very highly concentrated in a small number of companies. Thirteen trading banks, for example, control assets totalling $23,130 million while the same number of savings banks have assets of $17,324 million.
Together, therefore, the banks account for almost exactly half of the sector’s assets.

The rest of the financial sector includes 49 life insurance companies (13.3 per cent of all financial assets), 214 non-life insurance companies (5.5 per cent), 93 building societies (7.6 per cent), and 82 finance companies (15.6 per cent). As well, there are a number of small but aggressive and rapidly growing “fringe” institutions such as merchant banks.

These figures show that finance is much more concentrated than other sectors of the economy and are dramatic enough as they stand, but they actually understate the real degree of monopolisation that exists.

For example, of the 13 trading banks operating in Australia, the seven majors account for 87 per cent of trading bank loans. As well, each is linked in turn to a savings bank - and in most cases to a finance company.

While there appear to be a large number of finance companies, this too is overstating things since thirteen companies probably do well over 80 per cent of all finance company business with the top three having over a third of the business. With life insurance it is even more dramatic. There, the four top companies (the AMP, Colonial Mutual Life, National Mutual Life and Mutual Life and Citizens) have 81 per cent of all assets.

These relatively few large financial corporations are the main source of capital for the rest of the Australian economy. They supply this capital in two main ways, either as loans to productive enterprises or as direct investments in these enterprises. Either way, they receive part of the surplus value produced by workers in these enterprises in the form of interest or dividends. In turn, this income is used to pay operating expenses and any left over is reinvested or distributed to shareholders or policyholders.

The advantage for productive enterprises is that they are able to expand their scale of production by employing more workers and more machines. Of course, they have to pay interest on the money they borrow or dividends on new share issues they make. This will be alright, however, so long as the rate of profit they make on this new investment (or rather, their workers make for them) is greater than the interest or dividend rate they have to pay.

In a normally operating capitalist economy the market rate of interest is always less than the average rate of profit. The latter, for a given group of capital goods employed, depends on the share of output appropriated by capital. It is therefore determined within the production process, ultimately by the struggle between workers and capitalists over the rate of exploitation. The interest rate, on the other hand, is determined by struggles between different groups of capitalists, outside the production process.

Does this mean that bankers and the directors of insurance companies are interested in high interest rates while industrialists want low rates? In general this is true but it is complicated by the fact that financial institutions are not really lending their own capital to productive enterprises but are actually lending funds they in turn have borrowed from depositors or policyholders.

What matters to the shareholders and directors of a bank is the difference between the rate at which it borrows money (that is, the rate you, the depositor, receive) and the rate the bank charges on its loans. So long as lending and borrowing rates go up or down together the bank will still make money. In fact, if a general lowering of interest rates leads to an increased volume of loans the bank will benefit rather than suffer.

(You can be sure that, as interest rates start to come down over the next few months following the recent moderation in the inflation rate, it will be the interest rates the financial institutions offer say, debenture holders, that will come down before the rates they charge borrowers.)

So long as the institution itself is viable it may even be in the interests of its directors to hold interest rates artificially low in order to provide cheap funds for their mates in other companies - particularly when these directors may be also sitting on the boards of these companies.

The Bank of New South Wales, for example, is linked in this way to such important manufacturing and mining companies as Amatil, CSR, ICI, Alcoa and Mount Isa Mines and directors from other banks are involved in similar links.

While this mechanism is easy to follow
when it concerns money that banks and insurance companies lend to other enterprises it may not be so clear in the case of equity investments. Nevertheless, the same thing is happening, though to see how we need to look more closely at the share market.

The Sharemarket

At first sight the sharemarket seems to be all about the buying and selling of capital. If you buy up all the shares in a particular company, you become the owner of that company’s capital. However, if this is so, why doesn’t the total market value of a company’s shares (the company’s “market capitalisation”) equal the value of its assets?

A quick look at the financial pages of any newspaper will show these quantities are not generally the same.

The answer is that a company’s market capitalisation reflects not the present value of its assets but a claim on future income from those assets. Shareholders are interested in making the most out of their investments and since, if you have the money, it is fairly easy to buy and sell shares, shareholders will continue buying into any particular stock (and so bidding up the price) until the projected return on their investment is no more than they’d get by, say, investing their money at the current interest rate.

If we assume the company involved is making the average rate of profit on its assets then the difference between its market capitalisation and the value of its assets will reflect the difference between the rate of interest and the rate of profit.

For example, if a company with assets of $1 million declares a profit of $100,000 and (we will assume for simplicity) pays this all out as dividends, then shareholders will receive 10 cents for every $1 share they hold. Now if we assume the rate of interest is say, 5 per cent. anyone who buys a share in this company for $1 or even $1.50 will make more than the rate of interest on his/her investment. This will remain true until the share price is bid up to $2.

At that point the rate of return will be 10c divided by $2.00, that is 5 per cent.

Looking at it another way, so long as the price of the shares involved remains below $2 it would pay anyone to borrow money (at 5 per cent) and immediately invest in shares.

Market capitalisation of this company would then be $2 million, twice the value of its assets since we assumed the rate of profit is twice the rate of interest.

Note that we have left out important questions like risk. That is, we have assumed that the company will continue to pay a $100,000 dividend every year and that investors know this and remain confident of the fact. Of course, if it was all as simple as that, it wouldn’t be capitalism. Nevertheless this does give us a first approximation to how the sharemarket works and shows why a company’s market capitalisation is generally greater than its assets. (For readers who prefer(!) a formula I have given a couple in an appendix,

Lenin actually drew attention to this process, pointing out that it allows stockmarket operators to launch companies and make an immediate killing by exploiting the difference between the amount they originally invest and the market value of the shares these assets represent.

Thus in Imperialism, the highest stage of capitalism† he explains how the Union Mining Company of Dortmund was founded in 1872 with an issued share capital of 40 million marks. “The market price of the shares rose to 170 (that is, up 70 per cent - T.O’S.) after it had paid a 12 per cent dividend for its first year. Finance capital skimmed the cream and earned a trifle of something like 28 million marks.”

In other words, market capitalisation in this case increased 70 per cent, from 40 million marks to 68 million - and the difference was clear profit for the promotors, the Disconto-Gesellschaft.

Lenin goes on to explain that the opposite can happen: “Later, the dividends of the Union declined to nil; the shareholders had to consent to a ‘writing down’ of capital, that is, to losing some of it in order not to lose it all. By a series of ‘reconstructions’ more than 73 million marks were written off the books of the Union in the course of thirty years. At the present time, the original shareholders of the company possess only 5 per cent of the nominal value of their shares but the banks ‘earned something out of every reconstruction’.

How ‘mutual’ is the AMP?

How does this work in practice, today?
Let's look at the AMP Society, itself the largest holder of equity in Australian companies.

Sitting on its board is Sir Vincent Fairfax who also sits on the board of the Bank of NSW and John Fairfax Limited. The AMP in turn owns $15.2 million worth of shares in the former company and $4.2 million in the latter.

Another director is Sir Theo Kelly, chairman of Woolworths. The Society owns $20.5 million worth of Woolworths shares. Or again, consider Mr R. R. Law-Smith, who as well as being a director of the AMP sits on the board of BHP and the National Bank. The Society has shareholdings totalling $71 million in these two companies.

In fact, some 21 per cent of the AMP's massive shareholding is in companies with which the Society's directors are associated.

Who gains from such a relationship? Certainly not policyholders, as a quick look at the AMP's annual report for 1977 shows.

The Society began the year owning ordinary shares valued at $644.2 million. During the year it bought another $96.5 million worth of Woolworths shares. Or again, consider Mr R. R. Law-Smith, who as well as being a director of the AMP sits on the board of BHP and the National Bank. The Society has shareholdings totalling $71 million in these two companies.

When we recall that the consumer price index rose 9.3 per cent during 1977 and that the Commonwealth short term bond rate ranged between 9.91 and 9.26 per cent we can see that this result was hardly spectacular.

In other words, policyholders lent massive resources to the Society and through it to some of Australia's largest corporations for no real return. In exchange they merely had the value of their investments preserved - though they were clearly better off than the savings bank customer who received only 3.5 per cent interest - or in real terms paid his/her bank nearly 6 per cent interest for the privilege of lending out their money to others.

If this is the real role financial institutions like the AMP Society play, then both the myths I described above are discredited.

These institutions occupy a very large place within Australian capitalism, but they do not dominate it, as the "money power" view would have it. Rather they are used by the big corporations in other sectors to mobilise capital, including workers' savings.

On the other hand, the important role these institutions play and the fact that some (though by no means all) are mutual societies in which policyholders legally own the group's assets cannot be used to argue we now have some sort of "people's capitalism" in which everyone has a stake.

In fact, the same people who exploit workers as workers are also exploiting them as policyholders and bank depositors - and borrowers, for that matter.

T. O'S., 21.6.78.

*Ownership and Control of Australian Companies, published by the Transnational Corporations Research Project, University of Sydney.
†Collected Works, Volume 22, p. 235.

APPENDIX

Calculating market capitalisation:

To the extent that the restrictive assumptions I made above hold, the market capitalisation \( C \) of a company invested capital \( I \) is given by \( C = \frac{r}{i}I \), where \( r \) is the rate of profit and \( i \) is the rate of interest.

If the company, in addition to its initial invested capital of \( I \), borrows loan funds equal to \( L \) so that the total funds employed equal \( I + L \), then market capitalisation becomes:

\[
C = \frac{r}{i}(I + L) - L
\]

If \( L = 0 \), this reduces to \( C = \frac{r}{i}I \). On the other hand, if there is no invested capital and the promoters borrow the whole amount they need to capitalise the company, its capitalised value after repaying the loan is:

\[
C = \left(\frac{r}{i}\right)L
\]

This is pure profit for the promoters since they have contributed nothing except the skill to convince others to lend them money. Company promoters teach sharemarket speculators this

Continued on inside back cover —
lesson of how to create something out of nothing every few years — as soon as the last sharemarket crash has been forgotten!

In Lenin’s example above, I = 40 million marks, r, the rate of profit expected from the investment following the initial 12 per cent dividend is 12 per cent, while C is 170 per cent of I, that is 68 million marks. From this we can conclude the rate of interest must have been about 7 per cent, since 68 million marks = \( \frac{12 \text{ per cent}}{7 \text{ per cent}} \times 40 \text{ million marks} \).

The “cream which the promoters “earned” was:

\[ \frac{(12 \text{ per cent} - 7 \text{ per cent})}{7 \text{ per cent}} \times 40 \text{ million marks} \]

= 28 million marks.

Civilisation at the Crossroads: social and human implications of the scientific and technological revolution, $4.50 (300 pp.), 1969.

Some copies of this very important pioneering work are still available. Published by ALR in 1969, the book is the work of a Czechoslovak interdisciplinary research team headed by Radovan Richta. It appeared late in 1967 in Czechoslovakia and undoubtedly resulted from the deep concern with the crisis in economy, politics and ideology which came to a head there at that time.

Its findings in turn provided the theoretical basis for the Action Program developed by the Czechoslovak Communist Party to meet that crisis.

These national aspects do not, however, detract from the universality of the problems dealt with. The book is a first-class piece of research and analysis about issues confronting all advanced industrial societies, as apt today as it was when published. Over 300 pages of text are supplemented by extensive tables and references. At today’s prices, it is selling cheaply.

Antonio Gramsci: The Man, His Ideas, by Alastair Davidson (100 pp.), 1969. $2.

This short book was one of the first works published in English about the life and work of the Italian marxist thinker and communist leader. It is still a valuable reference for those interested in Gramsci’s contribution to marxist thought and socialist politics.

The Debate on "EUROCOMMUNISM"

Documents and articles from overseas publications, as well as contributions to the discussion by Australian writers.

$1.00 per copy.

Available from Australian Left Review, Box A247, Sydney South P.O., Sydney. 2000; or from left bookshops listed on back page.

A NOTE TO CONTRIBUTORS

ALR is only too happy to receive contributions on any subject of interest to the left and the labor movement. We prefer the length to be less than 5,000 words but exceptions are made in special cases.

We prefer articles, on whatever subject, to be accessible to all interested readers prepared to make an effort, and therefore request that unnecessary jargon or “academese” be avoided. For time and space considerations, we reserve the right to cut articles where this does not affect the basic sense of the discussion. Occasionally we propose style or sub-editing changes but only in consultation with the author(s).

We ask that all manuscripts be typed, double-spaced, on paper no larger than quarto size.

We ask those authors who do not hear from us about publication of their articles in a reasonable time to recognise that this is purely due to pressure of other work on our small collective. Usually we have not forgotten you.

APPEAL FOR BACK NUMBERS

Remaining gaps in our stock of back numbers have now been filled with the exception of numbers 36 and 38. We make a special appeal to readers who might have copies of these two issues which they no longer require to send them to us so that requests for them can be met. In addition, we would still be grateful for copies of numbers 29, 32 and 41, as numbers of these held by us are still small.