The Dynamics of Competition and their Impact on Firm Finance

Ewa Karwowski

Abstract

This paper links Michał Kalecki's and Josef Steindl's analysis of dynamics of competition (Kalecki, 1932, 1933b, 1935, 1939, Steindl, 1945a, 1952) to the concept of overcapitalisation and the theory of capital market inflation (Toporowski, 1993, 2000). In this way it extends the Kalecki-Steindl argument that the maldistribution of profits, meaning the concentration of profits in industries with market power be it cartels or oligopolies, introduces economic instability into the financial realm, where the maldistribution leads to financial fragility.

Economic instability is generated by oligopolistic profits since they have the potential to exacerbate the business cycle while depressing long-term growth through low investment activity due to the excess capacity oligopolies possess. Oligopolistic profits can induce financial fragility if held as excess capital on firms' balance sheets, that is as large volumes of liquid (financial) assets. Consequently, oligopolistic profits contribute to capital market inflation because they induce increased demand for liquid financial assets such as corporate equity.

The paper is organised as follows. In section 1, the arguments supporting cartelisation will be presented. Section 2 will discuss the Kalecki-Steindl analysis showing that concentration of profits in cartels and oligopolies destabilises the economy as a whole. Furthermore, financial fragility might be induced because oligopolistic profits are a potential source of excess capital meaning large volumes of liquid asset holdings not utilised in productive operations. This contributes to capital market inflation as argued in section 3. Finally in section 4, relevant data for the South African economy, which shows strong evidence of capital concentration and existence of oligopolistic profits, will be examined to support the hypothesis that oligopolistic profits are a source of excess capital.