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To cite this version:
Joel Rabinovich. The financialisation of the nonfinancial corporation. A critique to the financial rentieralization hypothesis. 2018. hal-01691435

HAL Id: hal-01691435
https://hal.archives-ouvertes.fr/hal-01691435
Submitted on 24 Jan 2018

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The financialisation of the nonfinancial corporation. 
A critique to the financial rentieralization hypothesis

Joel Rabinovich, joel.rabinovich@edu.univ-paris13.fr 
CEPN, UMR-CNRS 7234, Université Paris 13, Sorbonne Paris Cité

December 2017

Abstract: One aspect in which nonfinancial corporations are said to be financialised is that they emulate the asset and income structure of financial corporations. This is what we call the financial rentieralization hypothesis. In this article we show that the evidence used to sustain it, in the US setting, has to be reconsidered. Our findings show that, contrary to the financial rentieralization hypothesis, financial income averages 2.5% of total income since the ‘80s while net financial profit gets more negative as percentage of total profit for nonfinancial corporations. In terms of assets, some of the alleged financial assets actually reflect other activities in which nonfinancial corporations have been increasingly engaging: internationalization of production, activities refocusing and M&As.

Keywords: financialisation of the non-financial corporation, firm strategy, corporate governance, USA

Résumé: L’une des définitions de la financiarisation d’une société non financière est le fait qu’elle acquiert la structure de revenus et d’actifs des sociétés financières. C’est ce que nous appelons l’hypothèse de rentierisation financière. Dans cet article, nous montrons que les données à l’origine de cette hypothèse, dans le cas des États-Unis, doivent être reconsidérées. Nos résultats constatent que, contrairement à l’hypothèse de rentierisation financière, les revenus financiers représentent en moyenne 2,5% des revenus totaux depuis les années 1980, tandis que le profit financier net pèse négativement sur les profits totaux des sociétés non financières. En termes d’actifs, certains des actifs dits financiers sont en réalité issus d’autres activités dans lesquelles les sociétés non financières sont de plus en plus engagées : internationalisation de la production, recentrage sur des activités principales, fusions et acquisitions.

Mots clés: financiarisation des entreprises non financières, stratégie des firmes, gouvernement d’entreprise, États-Unis

JEL Codes: G3, L2, F23

1. Introduction

Financialisation is nowadays a buzzword. More than that perhaps, the buzzword of the 2010s, as Christophers (2015) claims. Starting originally in a Marxist tradition (Magdoff & Sweezy, 1987), it has later expanded to broader economic heterodox literature, typically post-Keynesian (G. A. Epstein, 2005), geography (Christophers, 2012), parts of mainstream sociology (Lin & Tomaskovic-Devey, 2013) and, very recently, it can even be found in mainstream economics (Admati, 2017). Such a wide disciplinary and theoretical usage has come with a lack of precision or, the flip side of this, a multiplicity of approaches.

Van der Zwan (2014) finds three different strands: financialisation as a change in everyday life, as a change in corporate management and as a new regime of accumulation. Lapavitsas (2014, pp. 3–4) puts forward a different (class-based) analysis, distinguishing among changes in nonfinancial corporations (NFCs), banks and households. We find this a clearer distinction as it allows for a better identification of each actor involved. The focus of this paper will be the financialisation of the NFC.

Even when considering a narrower scope such as the financialisation of the NFC, there is no general agreement on the precise dynamics it involves. However, the use of the term is, in most of the cases, restricted to two broad, non-exclusive phenomena: the primacy of shareholder value orientation and the increased acquisition of financial assets from which NFCs derive a growing proportion of financial income. Table 1 shows some of the most-cited papers regarding the financialisation of the NFC. On one side it confirms, as in Van der Zwan (2014), that shareholder value orientation and the financialisation of the NFC have been sometimes used as synonyms. On the other hand, it puts a specific nonfinancial dimension which is the involvement in financial activities by NFCs.

Table 1. Financialisation of NFC literature

<table>
<thead>
<tr>
<th>Paper</th>
<th>Shareholder value orientation</th>
<th>Financial Acquisitions + Increasing Proportion of Financial Income</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>Epstein (2015)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tori &amp; Onaran (2015)</td>
<td>X</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Davis (2016)</td>
<td>X</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fiebiger (2016)</td>
<td>X</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Moreover, it is claimed that the involvement in financial activities has been dramatic: the ratio of financial assets to non-financial assets has gone from 40% in 1950 to 120% in 2001 (Orhangazi, 2008, p. 866), while the ratio of portfolio income has gone from less than 10% in 1950 to 40% in 2001 (Krippner, 2005, p. 185). Based on this and her own evidence, Davis (2016, p. 138) states that there has been a “shift in NFC activities toward banking activities”.

However, in this article we will scrutinize the empirical evidence used to support that type of claim, or what we define as the financial rentieralization hypothesis. We define this hypothesis as the contention that there has been an aggregate trend in which NFCs increasingly resemble financial corporations (FC) both in terms of their asset and income composition. To underscore, we are concerned here with the general trend, whilst understanding that there could be significant variation in particular firms, as cases studies have shown (Froud et al., 2006) and we will confirm. We will focus on the main pieces of evidence that have been adduced: the increase in financial assets held by NFCs and the increase in financial income received by NFCs, while also analyzing their cash flow statements. We will concentrate on the United States (US) between 1950 and 2016 since this is where most of the literature is focused.

In order to perform our analysis, we make use of three different and complementary databases. The Federal Reserve’s Financial Accounts of the USA and the Statistics of Income (SOI) from the Internal Revenue Service (IRS) produce aggregate, domestic information for all corporations. Moreover, the latter presents information disaggregated by size of assets. The third database is Compustat firm-level information for listed US corporations that presents consolidated data for the parent company along with its national and international subsidiaries. This provides an approximate notion of the worldwide activity of those firms. Additionally, the latter database allows us to present a novel analysis of NFC’s total sources and uses of cash based on their Cash Flow Statement. We also present a novel comparison of NFCs with FCs in all moments (asset, income and cash flow structure) in order to produce a benchmark index for the extent of emulation.

Our results show that mimicking finance was not a strategy verified in aggregate terms. The highest proportions of assets held by FCs are ‘Receivables’ and ‘Other Investments and Advances’. Both of them have remained fairly constant or even decreased for NFCs. In terms of income, financial income has increased in the last decades but remained around 2.5% of total income since 1980, even decreasing in the last years, and moved hand in hand with financial expenditures. Moreover, the latter are higher for the whole period and the difference in fact increases since the ‘80s. As stated by Fiebiger (2016), if NFCs are specializing in banking activities in order to make profits out of them, it seems that the result has not been positive overall. These results also hold when we distinguish between sizes of enterprises.

The rest of the paper is organized as follows. Section 2 revises the literature that suggests a movement to finance, or what we call as the financial rentieralization hypothesis. Section 3 presents the data and section 4, the methodology. Section 5 shows, separately, the results from the empirical analysis of asset, income and cash flow composition. Section 6 focuses on differences by size, while Section 7 discusses the results. We finally give some concluding remarks in section 8.

2. Moving to finance

This idea can be traced back to the Monopoly Capital thesis. In an economy trapped in a state of stagnation, as characterized by Baran and Sweezy (1966), regular ways of absorbing surpluses such as capitalist consumption and investment become insufficient. Speculation appears as one of the new channels for mopping up surpluses (Magdoff & Sweezy, 1987).
Although not necessarily sharing the idea of a stagnant economy, Crotty (2005) and Orhangazi (2008) also state that NFCs started using, in the beginnings of the ‘80s, an increased percentage of their internal funds to buy financial assets and financial subsidiaries, or start new financial arms themselves. For Krippner (2011) the degree of high labor militancy at home and increased international competition abroad induced nonfinancial firms to withdraw capital from production and divert it to financial markets. Similarly, Davis (2016) states that due to declining profitability, slower global aggregate demand growth and increased exchange rate volatility, NFCs shifted away from fixed capital toward financial assets. In Stockhammer (2004) and Tomaskovic-Devey et al (2015), the emphasis is put on a shift in management preferences caused by the hostile take-over movement and changes in pay structure which aligned their interests with shareholders. Due to these transformations, non-financial business becomes more rentier-like abandoning growth-oriented priorities and investing in financial markets.

Both macro (Crotty, 2005; Krippner, 2011; Orhangazi, 2008) and micro (L. E. Davis, 2016; Froud et al., 2006) level data have been used to prove the financial rentieralization hypothesis. Among the former, the increase in the ratio of financial assets to non-financial assets based on the Federal Reserve’s Flow of Funds database, which has gone from 40% in 1950 to 120% in 2001, is usually used to show the movement from productive to financial activities (Orhangazi, 2008, p. 866). This is complemented with a ratio that intends to show an increasing share of income coming from financial sources (Krippner, 2005, p. 185). In the case of the micro evidence, we find scholars focusing either in some case studies as in Froud et al (2006) or analysis based on the aggregations of micro data as Davis (2016) who uses firm-level data to demonstrate a shift in the asset structure of NFCs towards financial assets and a declining gap between the cost of borrowing and the financial income for large NFCs.

In terms of econometric analysis, in most of the cases, the objective is to estimate the impact of the financialisation of NFC on investment distinguishing two different channels. The first is related to the increased transfer of earnings from NFCs to financial markets in various forms such as interest payments, dividend payments, and stock buybacks (Orhangazi, 2008, p. 877). The second channel is related to the flow of income that nonfinancial corporations earn due to their investment in financial assets and financial subsidiaries such as interest and dividend income (Orhangazi, 2008, p. 877). The latter is, evidently, the closest to our research. Results on this channel are mixed: while Hecht (2014, p. 32) and Auvray & Rabinovich (2017, p. 27) find no statistically significant effect of financial income on US NFCs’ investment decisions, Stockhammer (2004, p. 735) and Orhangazi (2008, p. 880) do find negative statistically significant effect in some specifications.

3. Data

One of the novelties of this paper is to deal, simultaneously, with three different and complementary databases. Table 2 provides a summary of the information contained by each of them used in this paper. The complementarity arises not only from the fact that that two of them provide domestic information while the other includes international as well, but also because Compustat is the only one that identifies separately a particular relevant asset.

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1 Crotty (2005) argues that it was in order to face the low profits and high costs of external funds in the ‘80s.
2 We will go into the details of this ratio in Section 4.
goodwill. There is also complementarity in terms of the disaggregation by size: although Compustat identifies listed firms individually, those firms are big per se. The disaggregation by the SOI, on the other hand, covers all size of assets and therefore allows to distinguish different dynamics.

Table 2. Summary of data

<table>
<thead>
<tr>
<th>Database</th>
<th>Financial Accounts of the USA</th>
<th>Statistics of Income - Corporation Income Tax Returns</th>
<th>Compustat</th>
</tr>
</thead>
<tbody>
<tr>
<td>FCs</td>
<td>-</td>
<td>Finance, Insurance and Real State</td>
<td>Firms identified by the primary SIC codes from 6000 to 6799</td>
</tr>
<tr>
<td>NFCs</td>
<td>Nonfinancial Corporate Business</td>
<td>All industries less Finance, Insurance and Real State</td>
<td>All firms excluding financial firms identified by the primary SIC codes from 6000 to 6799³</td>
</tr>
<tr>
<td>Consolidated/Unconsolidated</td>
<td>Consolidated</td>
<td>Consolidated</td>
<td>Consolidated</td>
</tr>
<tr>
<td>Geographical scope</td>
<td>Domestic</td>
<td>Domestic</td>
<td>Domestic and international, listed corporations incorporated in the US</td>
</tr>
<tr>
<td>Dissaggregation by size</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Assets</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Financial</td>
<td>17 items</td>
<td>8 items</td>
<td>4 items</td>
</tr>
<tr>
<td>Nonfinancial</td>
<td>4 items</td>
<td>8 items</td>
<td>4 items</td>
</tr>
<tr>
<td>Non-Identifiable</td>
<td>1 item</td>
<td>2 items</td>
<td>2 items</td>
</tr>
<tr>
<td>Sources of income</td>
<td>-</td>
<td>12 items</td>
<td>4 items</td>
</tr>
<tr>
<td>Cash Flow</td>
<td>-</td>
<td></td>
<td>34 items</td>
</tr>
</tbody>
</table>

For the asset analysis, we will use the three databases although focusing on the Financial Accounts of the USA and Compustat. For the sources of income we will base our study on the SOI and Compustat. While the former has the biggest amount of items and many of them are different types of financial income, the latter allows to identify another type of financial income: that belonging to the financial division. Finally, for the Cash Flow Statement we will focus only in Compustat⁴. The complete list of items used in Figures and Tables is available in Table A1.

4. Methodology

For the asset analysis we identify two methodological discussions: what type of assets should be considered as financial and how to measure their evolution. The first question is relevant since, as Crotty (2005) and Orhangazi (2008) recognize, practically the entire increase in financial assets over total assets is due to a residual variable, ‘Unidentified Miscellaneous Assets’, which is considered as financial by the Financial Accounts of the USA. Trying to identify individually the assets it contains, with the help of the other databases, will be fundamental to assess whether or not there has been such an increase in Financial Assets.

³ This classification includes holding companies (except bank holding companies) denominated under NAICS code 551112, ‘Offices of Other Holding Companies’. Therefore, we should not miss information of NFCs held by holding companies.

⁴ The Financial Accounts of the USA also have this kind of data but the information is presented clearly in Compustat. For example, while Compustat presents separately issuance and share buybacks or issuance and reduction of long-term debt, the Financial Accounts of the USA shows net information.
The second questions relates to measurement. With a very similar aim as ours, Davis (2016) carries out an exhaustive analysis of NFCs’ balance sheet taking four categories of financial assets in Compustat – ‘Cash and short-term investments’, ‘Total current receivables’, ‘Other investments and advances’, and ‘Other financial assets’. In her case, those categories are normalized by sales in order “to avoid possible biases stemming from the fact that an increase in financial assets relative to assets requires by definition a decline in nonfinancial assets relative to assets” (L. E. Davis, 2016, p. 118). However, if we are telling a story about how NFCs become more intensive in financial assets, by definition, this is compared to other types of assets. Normalizing by sales fails to capture this dimension because, a priori, all types of assets could be able to increase. Therefore, we chose to normalize by total assets.

In terms of sources of income, using different datasets Krippner (2005, p. 185) -SOI-, Crotty (2005, p. 107) -SOI-, Orhangazi (2008, p. 866) -Financial Accounts of the USA- and Davis (2016, p. 135) -Compustat- arrive at similar conclusions: basically, that financial income has become a significant source of income for NFCs. Davis (2016, p. 134) correctly states that “an expansion into financing activities may reflect a differential between firms’ cost of borrowing and returns to lending, or financial profitability.” However, when comparing both of them, the returns to lending have been always lower than the cost of borrowing. Moreover, from 1980 and beyond, the returns to lending display a clear downward trend.

For Krippner, Crotty and Orhangazi, we identify two types of problem: one related to measurement and one stemming from their bias towards financial income without considering financial expenses, i.e. some kind of net financial profit. In the case of the former, although Orhangazi (2008, p. 865) intends to show that NFCs are “deriving an increasing share of their income from financial sources” and Krippner (2005, p. 182) the “growing importance of ‘portfolio income’... relative to revenue generated by productive activities”, in practice they do not measure financial income relative to total income but financial income relative to some measure close to profits.

As shown in the mathematical Appendix, this type of ratio can give meaningless or paradoxical results in which the cost of financial activities is increasing and, ceteris paribus, the ratio of portfolio income is increasing. As Crotty himself (2005, p. 105) notes: “caution is required in interpreting the meaning of this time series because the numerator does not deduct the cost of acquiring and holding financial assets, while the denominator includes profit, which is a net revenue concept. This gives an upward bias to this series that could be substantial”.

The best way to compute the importance of financial activities for NFCs would be to measure financial profit as a percentage of total profit or, as a second best, to measure the financial income as a percentage of total income. We construct both measures bearing in mind that the proxy for net financial profit should be interpreted only as a proxy in the sense that we take all financial expenses instead of only those related to acquiring and holding financial assets.

Even after building the two measures, the results should be interpreted with caution since there is a high probability that financial income is under-estimated. This is due to the way in which corporations fill their annual reports. Those corporations with a strong financial activity usually present income statements from their industrial and financial divisions consolidated.

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5 For Krippner (2005), it’s profits plus depreciation allowances, while for Orhaganzi (2008) it’s operating surplus.

Therefore, an important proportion of financial income appears as part of total revenue in aggregate statistics. It is only with Compusat that we are able to identify income from the financial division although starting in 2010.

For the Cash Flow Statement we compute the evolution of total sources and uses of funds. This analysis, of flow variables, will complement that of the asset structure.

5. **Results**
   a. **Asset structure**

Table 3 confirms that the most important change in terms of assets has been the dramatic increase of ‘Unidentified miscellaneous assets’.

Table 3. Composition of assets, NFCs, 1950-2015.

<table>
<thead>
<tr>
<th></th>
<th>50-59</th>
<th>60-69</th>
<th>70-79</th>
<th>80-89</th>
<th>90-99</th>
<th>00-09</th>
<th>10-15</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-Financial Assets</td>
<td>0.778</td>
<td>0.754</td>
<td>0.740</td>
<td>0.693</td>
<td>0.600</td>
<td>0.536</td>
<td>0.530</td>
</tr>
<tr>
<td>Financial assets less unidentified miscellaneous assets</td>
<td>0.221</td>
<td>0.242</td>
<td>0.227</td>
<td>0.210</td>
<td>0.230</td>
<td>0.236</td>
<td>0.263</td>
</tr>
<tr>
<td>Unidentified miscellaneous assets</td>
<td>0.001</td>
<td>0.003</td>
<td>0.033</td>
<td>0.097</td>
<td>0.171</td>
<td>0.228</td>
<td>0.207</td>
</tr>
</tbody>
</table>

Source: Tables B.103 and L.103, Financial Accounts of the USA

Until 2010, the total financial assets not including miscellaneous items have, in fact, remained lower as a proportion of total assets than the decade of the ‘60s. Figure 1 analyzes the evolution of those assets. It can be clearly observed from this figure that the major increase in ‘Financial assets less unidentified miscellaneous assets’ in fact derives from direct investment abroad which goes from 10% in 1946 to almost 50% in 2015. Needless to say, it’s dubious to directly consider FDI as a financial asset if we take into account that it implies lasting interest with the intention to exercise control over the enterprise, (which is how it is distinguished from foreign portfolio investment). Moreover, 84.7% of all US foreign affiliates are majority owned (Fiebiger, 2016, p. 5).

[Figure 1]

We now move to ‘Unidentified miscellaneous assets’. Crotty (2005, p. 104) stated that, at the time of his research, even Federal Reserve economists didn’t know which kind of assets were in that category or even if they were financial at all. The FED (2017) later clarified the definition:

Unidentified miscellaneous assets, which is calculated resiliually, may include such items as deferred charges and prepaid expenses, goodwill, other intangible assets, and intercorporate holdings of corporate equity. Intangibles can include such items as copyrights, patents, distribution rights and agreements, easements (gas, water, and mineral rights), franchises and franchise fees, trademarks, and client lists.

It is worth noting that almost all these assets are intangibles rather than financial. Consequently, sometimes they have been excluded from the broader list of financial assets

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7 “Financial assets are entities over which ownership rights are enforced by institutional units, individually or collectively, and from which economic benefits may be derived by their owners by holding them, or using them over a period of time; they differ from other assets in the System of
(Doepke & Schneider, 2006). Among unidentified miscellaneous assets, goodwill has a relevant preponderance (L. E. Davis, 2016, p. 117). This asset is defined as the amount that an acquiring company pays for a target company over the target’s book value (IFRS 3 — Business Combinations). Theoretically, it is explained by the routines, procedures, cultures, etc. which are not individually identifiable but add to company’s value. In practice, given the difficulties to measure such items, the amount of goodwill depends on the fluctuations of the stock market, especially on the bull process verified in the weeks preceding M&A (Serfati, 2008). Nevertheless, the fact that goodwill has increased as a proportion of total assets has to be interpreted cautiously. This is due to the fact that goodwill is valued through impairment (IAS 36 — Impairment of Assets). Contrary to amortization, by which assets’ value is reduced according to a specific schedule, impairment implies that the value of an asset, in this case goodwill, is decided by a test that compares the total profit expected to be generated by that asset with its book value. Therefore, goodwill does not necessarily disappear from the accounts throughout time.

In spite of the increase in goodwill, there is still the possibility that unidentified miscellaneous financial assets include other financial assets. We analyze this possibility using the statistics compiled by the IRS and the information for listed US corporations from Compustat. In the case of the former (Figure 2), the information is not straightforward. Although it presents a clear negative trend for ‘Net Depreciable Assets’ and ‘Inventories’, along with a positive trend for ‘Net Intangibles’, the main increase arises from ‘Other Investment’ which, as in the case of ‘Unidentified Miscellaneous’, contains many different types of Assets (IRS, 2013):

This category generally included long-term nongovernment investments and certain investments for which no distinction could be made as to their current or long-term nature. Examples of non-government investments included stocks, bonds, loans to subsidiaries, treasury stock reported as assets, and other types of financial securities.

The situation is different for Compustat, where the definition of the categories is more precise. Figure 3 shows that the most prominent change is the increase in intangibles (goodwill + other intangibles) which, starting from less than 0.5% in 1961 reaches around 25% in 2015. Goodwill has been, in most of the years, around 50% of total intangibles (and closer to 60% since 2002). The remaining intangibles are defined by Compustat as ‘Other Intangibles’ which, as in the case of Goodwill, have also little to do with financial assets. Most of the assets from ‘Unidentified miscellaneous assets’ besides goodwill, such as patents, copyrights and licenses, are included in ‘Other Intangibles’.

[Figure 2, Figure 3]

However, the graph still portrays an increase in some financial assets. ‘Cash and Short Term Investments’ display a U-shaped curve starting in 10% of total assets in 1961, then falling to 5% in the beginning of the ‘80s before increasing back to 10% in the ‘90s where they have since remained. ‘Other Assets’ and ‘Other Current Assets’ have also increased (especially the former) although they are residual categories that include different type of assets. ‘Other Investments and Advances’ have also increased from 2% in 1961 to 5% in the present. ‘Receivables’ present a discrete jump in 1988, from 11.8% to 17.5% not due to a change in

National Accounts in that there is a counterpart liability on the part of another institutional unit (except for monetary gold and Special Drawing Rights (SDRs)” (OECD, 2001)

We later confirm this for listed NFCs (Figure 3).
NFCs’ strategies but because of a change in regulation. In October 1987, the Financial Accounting Standards Board issued its Statement No. 94 which tried to reduce the off-balance sheet financing by requiring the consolidation of all majority owned subsidiaries in financial statements (Wiedman & Wier, 1999). Parent companies had off-balance subsidiaries in order to transfer corporate receivables and leases, reporting only their net asset position in their own balance sheet improving their debt/equity, return on investment and receivables turnover ratios (Cormier, Andre, & Charles-Cargnello, 2004).

It is also important to remark that Compustat presents consolidated information and therefore we are not able to distinguish between parent and subsidiary information (i.e. it’s not possible to assess the stock of FDI like we did in Figure 1). Being consolidated, on the other hand, implies that all subsidiaries are included, even the financial ones.

On the other hand, if we compare the asset structure of NFCs and FCs we can see in Figure 4, that for the latter: (1) the amount of ‘Cash and short term investments’ has decreased, instead of increased, over practically the whole period; (2) the main component is ‘Receivables’ - more than 40%; (3) ‘Other investments and advances’ comprise a higher proportion of assets.

[Figure 4]

Figure 4 also allows to calculate a rough benchmark in order to identify which NFCs resemble more the structure of FCs. Their two most important assets are ‘Receivables’ and ‘Other Investments and Advances’, which average 46% and 23% of total assets respectively. The former is a particularly important asset in the financial rentieralization hypothesis since it represents the monetary obligations owed to a company by its debtors or customers. We take an arbitrary lower percentage for NFCs and identify three cases: a) NFCs with more than 40% of ‘Receivables’ over total assets, b) NFCs with more than 15% of ‘Other Investment and Advances’ over total assets and c) NFCs with more than 35% of ‘Receivables’ over total assets and 10% of ‘Other Investment and Advances’ over total assets. Figure 5 shows the results: since the ’80s, an average of 7% and 5% of listed NFCs accomplish criteria a) and b) respectively although with a clear lower trend. Moreover, only an average of 27 NFCs since 1980 meets criteria c) -less than 1%. In the case of FCs, 50%, 58% and 28% respectively accomplish those criteria since the ’80s.

[Figure 5]

In a nutshell, we believe that the evidence provided is not enough to sustain that there has been a “dramatic growth in financial asset holdings” (L. E. Davis, 2016, p. 117). Even though some financial assets have increased, it does not mean that NFCs are making profits out of them. To effectively sustain this kind of argument we would need evidence showing to what extent interest income, capital gains and dividends have displaced more ‘traditional’ sources of income. This requires, in other words, examining the income statement of NFC – the topic we analyze next.

b. Sources of income

Measuring financial income as a percentage of total income (Figure 6) tells a completely different story than the financial rentieralization hypothesis regarding the importance of that type of revenues on the general income structure of NFCs. Even considering dividends from foreign and domestic corporations (which are not necessarily financial), this type of income is usually below 2.5% and only in 2005 it surpassed the barrier of 3% due to a tax holiday on
repatriated profits. If we only take gains on capital and noncapital assets and interests, the aggregate is usually below 2%.\(^9\)

[Figure 6]

Concerning the ratio of net financial profit and total profit, Figure 7 shows that financial expenses have been higher than all financial income combined during the whole period. Moreover the average of financial losses for the 1980-2013 period practically doubles the 1955-1980 one. As Fiebiger (2016) states, if NFCs are specializing in banking activities, it seems that the result has been bad for them. Additionally, Figure 8 shows that, in fact, financial income and interest expenditures share practically the same trend, which is also similar to the evolution of the interest rate. Therefore, the evolution of financial income seems to be more a by-product of monetary policy (Fiebiger, 2016, p. 10).

As we have done in the case of the asset structure, it’s useful to have in mind the income structure of FCs (Figure 9). Once again we observe substantial differences with NFCs. For FCs, interests and capital gains amount for an average of approximately 40% of income and net financial profit is positive for the whole period.

[Figure 7, Figure 8, Figure 9]

However, as we indicated in the Methodological section, there is a high probably that an important proportion of financial income might not be specified as such. We face this potential issue using Compustat. When we compute income from financial divisions, financial profitability is still negative and, calculated as a percentage of revenues for the whole sample, we obtain an average of 0.5%. Although the number is minor, it is nevertheless impressive considering that only 34 corporations have income from financial divisions. It is in many of these cases (but not in all of them) where financial income represents a significant proportion of total income (Table 4).

Table 4. Corporations with income from financial divisions and its proportion over total income.

<table>
<thead>
<tr>
<th></th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
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<td>0.063</td>
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\(^9\) Which does not mean that, taken on their own, figures for that type of income are not impressive. For example, in 2001 total financial income for NFCs was US$ 425,144 million.
Having analyzed the income structure of NFCs we have presented data that, as in the case of the asset structure, tend to deny the financial rentierization hypothesis. In particular we showed that: (1) financial income has moved hand in hand with financial expenditure and both are closely related to the movements of interest rate; (2) financial activities have reported losses for the whole period, which have been higher on average over the period of financialisation; and, finally, (3) financial income is a small part of the aggregate income structure of NFCs, even after adding income from finance divisions. In the next section, we study the remaining financial account: the cash flow statement of NFCs.

c. Cash Flow Structure

The cash flow statement is a useful tool for assessing the sources (Figure 10) and uses (Figure 11) of funds. In terms of the sources, ‘Net increase in long term debt’ has been maintained as a permanent positive source of income, growing especially in moments of lower income from regular operations. This last item, until 2002, had a negative trend as a source of income, increasing later. The category ‘Other funds from operations’ has also increased during the period.

[Figure 10, Figure 11]

Regarding the uses of funds, one of the most prominent changes is the decrease in capital expenditure across the period from 77% of total funds in 1977 to 34% in 2016. This decline was matched, as a counterpart, by an increase in the purchase of common and preferred stock from 1.5% in the beginnings of the ’70s to 20% in 2016 (and a reduction in the relative importance of dividends as a mean of distributing value to shareholders) along with acquisitions averaging 13.3% of total funds since mid ’80s.

Regarding financial acquisitions, their proportion is low: (1)’Net increases in investments’\(^\text{10}\) has an average of 3.7% (and started the sample with 3.5%), (2)’Change of short term investments’ presents a negative average of 0.3%, (3)’Other investing activities’ displays an average of 2.5% and, finally, (4)’Changes in cash and cash equivalents’ alternated positive and negative values with an average of 2.6% and a period of systematic higher values (1996-2005) in which it reached 13% in 2003.

\(^{10}\) We take the net value (difference between increase in investment and sale of investments) because, due to the Statement No. 94 in 1988, the values of each them rise separately. This category includes increase in long-term receivables, increase in investments in unconsolidated subsidiaries and long-term investments combined with short-term investments.
If we compare these uses of funds with those of FCs (Figure 12), relevant differences appear. For FCs, ‘Net increase in investments’ had an average of 66% until 1987 when it was disaggregated into the old category and two new: ‘Other Financing activities’ and ‘Change in short-term investments’. When taken all the categories together, the average remains around 70% of all uses of funds.

[Figure 12]

To conclude, this section confirms the trends we found above. Firstly, increases in acquisitions match increases in intangibles and goodwill. Decreases in capital expenditure explain the decrease in net property, plant and equipment and positive sustained values for some financial categories might explain the increase in cash and short-term investments. Moreover, the fact that financial investments are not a major use of funds is conformant with the low proportion of financial income relative to total income. Finally, permanent positive values for net long-term debt issuance explains the increase in the liabilities of NFCs as pointed by Davis (2016, p. 128).

So far, we have presented comprehensive evidence pointing towards the rejection of the financial rentierization hypothesis as an aggregate trend among NFCs. However, there might still be the case that the aggregate data we presented hides significant variation across firm size and sector. In the next section we perform the same analysis we have done so far, this time for different sizes of NFCs.

6. Size analysis

In order to analyze size differences we use IRS and Compustat data. Figure 13 shows the asset structure of different sizes of firms. A couple of trends can be clearly distinguished. Starting from the lowest percentiles, all firm sizes show a clear increase in ‘Cash, government obligation and other current assets’ met mainly by a decrease in ‘Notes and accounts receivables less reserves for bad debts’ and also ‘Inventories’. In these segments, ‘Depreciable assets less accumulated depreciations’, ‘Other capital assets less reserves’ (which includes intangibles) and ‘Other investments and loans’ have remained fairly constant.

This picture changes dramatically for the upper percentiles, especially within the top 1%. Firstly, the decrease in ‘Depreciable assets’ as a percentage of total assets is concentrated in the upper segment of the distribution, mainly in the upper 0.1% but especially in the upper 0.05%. This group also presents some other interesting features. It is the only one in which there is no increase in ‘Cash, government obligation and other current assets’. Moreover, it is also the only where we verify an increase in ‘Other investments and loans’. To recall, this category is very broad and may include both financial and nonfinancial assets (related to the international activities of NFC). As we did in previous sections we are able to verify whether

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11 In term of sources, net long-term debt issuance had a more important role with permanent positive values around 40% until 2009 when it starts a massive deleveraging.
12 The percentiles are not arbitrary but based on how IRS provides information (i.e. almost fixed categories for asset size during the whole period). Although it is not possible to distinguish percentiles in the lower 60%, it presents a great versatility for the upper ones.
We show, for each percentile, the proportion of financial income over total income and net financial profit as we defined them in Section 4. For the upper 0.1% and especially for the 0.05%, financial income has increased as a percentage of income (7 times for the latter). However, we should note some nuances. First of all, the percentage does not pass the 3.5% level for biggest firms and 1.4% for the 0.05%-0.1% segment. Second, net financial profit has been negative for all years considered and most importantly, it was higher in 1961 and 1962 compared to all the ‘financialized’ period for the 0.05%-0.1% segment\textsuperscript{14} and most of those years for the upper 0.05%. This is a strong piece of evidence that suggests that, even for the biggest NFCs, financialisation must not be understood as mimicking FCs.

Figure 14 also allows us to check whether the increase in more clear financial assets -‘Cash, government obligation and other current assets’- in other firm sizes was associated with an increase in financial income and financial profits. For the 1%-10% and 10%-20% both financial income and financial profits were higher in 1961 and 1962 compared to 2004-2013. Only in the 20%-40% and 40%-100% segments we observe some years in the recent period with either higher financial income or profit. However, financial income is never higher than 0.3% for the former and 1% for the latter. Moreover, net financial profit is always negative for the former and mostly negative for the latter. These general trends are maintained also for the manufacturing sector (Figures A1 and A2).

Finally, Figure 15 shows the asset and cash flow composition of NFCs belonging to the Top 5% and 1% in asset size from Compustat. In all items, they share the same trend as the whole sample although with different levels. Especially for the Top 1% we verify a slightly higher proportion of financial assets such as ‘Cash and short-term investments’, ‘Receivables’, ‘Equity investments’ and ‘Other investments’. ‘Net increases in investments’ are also higher for this segment. However, the ratio between financial income and total sales is around 2%. Therefore, even for this type of corporations, the general structure resembles more nonfinancial rather than financial corporations.

Taking advantage of the different geographical scope of the databases, we can make further comparisons. First of all, Figure 16 displays the increase in ‘Cash and short-term investments’ for all NFCs in Compustat since the beginnings of the ‘90s but, at the same time, ‘Cash, government obligation and other current assets’ for the upper 0.05% in IRS started to decrease. Focusing only on trends and not levels, the difference suggests that the increase in cash and short-term investments has gone to international portfolios. We also carry out a similar exercise for physical investment (Figure 17). Focusing only on Compustat shows that bigger firms started with a higher proportion of ‘Net property, plant and equipment’ than the rest but since 1988 this reversed. Comparing then the aggregate measure of Compustat with the higher segment of IRS illustrates that, although for the latter ‘Depreciable assets accumulated depreciation’ has always been lower, in 1963 the difference was 8.7% while in 2013 it increased to 53%. Since both variables are not strictly the same, the values should not

\textsuperscript{13} IRS only presents the disaggregation of income for 1961, 1962 and 2004-2013. That’s why we take those years.

\textsuperscript{14} Also for the 0.1%-1%, 1%-10% and 10%-20% segments.
be interpreted literally, but suggesting that a significant proportion of investment has been carried out outside the USA.

[Figure 16, Figure 17]

7. Discussion

As we mentioned in Section 2, the alleged movement to finance was in a hostile context for US NFCs. Compared to the “relatively quiet and uncompetitive ‘60s” (Shleifer & Vishny, 1991, p. 54), US corporations in the beginnings of the ‘80s faced a number of major economic challenges: high inflation, high interest rates, low profits and increased foreign competition. Due to inflation, corporations’ real assets (i.e. property, plant, equipment) increased in value while high interest rates left corporations undervalued in the stock market (Fligstein & Markowitz, 1993). Moreover, at that time, stock market valuation suggested that in many cases the individual parts of the corporation were worth more than the combined entity (LeBaron & Speidell, 1987).

In this situation, returns for shareholders were relatively low (Zey & Camp, 1996). However, contrary to the dispersal which had prevailed in previous decades, shareholders were increasingly organized in the form of pension and investment funds. In this way, they could exert pressure through the board of directors. Management also felt pressure through leveraged buyouts carried out by corporate raiders (Useem, 1999). This gave rise to two broad changes in corporate governance regimes: firstly a move to financial conceptions of the firm, according to which the company is a moldable set of assets, and secondly an emphasis on shareholder value maximization, which guides management to maximizing short-run returns on those assets (Fligstein, 2002; Lazonick & O’sullivan, 2000).

In response to this new context, US NFCs underwent several changes. First, many corporations were taken over, broken up and refocused on fewer activities, especially their core competences (Prahalad & Hamel, 1990). Large firms were in the ‘90s approximately half as diversified as they were in the ‘80s (G. F. Davis, Diekmann, & Tinsley, 1994). For a sample of large acquisitions made between 1971 and 1982, Kaplan and Weisbach (1992) find that by the end of 1989, acquirers had divested almost 44% of the target companies. Contrary to the wave of mergers in the ‘60s and ‘70s, takeovers in the ‘80s tended towards consolidation and specialization. They were characterized in some cases as correctives to the previous wave of mergers (Martynova & Renneboog, 2008; Shleifer & Vishny, 1991). Moreover, this new wave of acquisitions was able to take place because Reagan’s antitrust policy allowed practically any type of merger (G. F. Davis et al., 1994).

Increased pressure to maximize shareholder value was also transmitted through the introduction of new technologies, downsizing their workforce and offshoring (Fligstein & Shin, 2004; Milberg & Winkler, 2013). As a consequence, transnational NFCs increasingly redefined their core competences to focus on innovation, product strategy, marketing – in general higher value added activities - while reducing direct ownership of non-core activities (i.e. those associated with lower value added) (Gereffi, Humphrey, & Sturgeon, 2005). Moreover, economic globalization, technological innovation and deregulation triggered another merger wave in the ‘90s, this time global in dimension, with the European and Asian takeover market

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15 This has been termed as the “diversification discount” (Rajan, Servaes, & Zingales, 2000).
becoming more important and cross-border transactions growing substantially (Martynova & Renneboog, 2008).

Our results not only show that, for the aggregate, the financial rentieralization hypothesis does not hold but also provide empirical support to those other strategies followed by NFCs. In terms of assets, the biggest increase was verified in ‘Unidentified miscellaneous assets’ in which ‘Goodwill’ has a dominant role. Other intangibles such as patents, copyrights and licenses are also part of that category and partly reflect the movement towards higher value added activities. Of the rest of the financial assets that can be identified, it is FDI that demonstrates the highest increase. Strikingly, neither intangibles (goodwill and other intangibles) nor FDI are financial in the traditional definition while, in fact, both of them reflect other changes experienced by NFCs: M&As, reorientation towards core activities and offshoring respectively.

This does not mean that no financial asset has increased in proportion, as is the case for ‘Cash and short-term investments’ since the ’90s. However, the fact that NFCs are holding a higher proportion of cash and short term investments does not seem to be related to a significant increase in the flow of financial income or an increased financial profitability. Therefore, the increase in cash and short-term investments is due to other motives. Corporate finance literature identifies different group of answers for this phenomenon such as growth opportunities (Fazzari, Hubbard, Petersen, Blinder, & Poterba, 1988; Opler, Pinkowitz, Stulz, & Williamson, 1999), riskier cash flows (Acharya, Almeida, & Campello, 2007; Bates, Kahle, & Stulz, 2009), tax costs associated with repatriating foreign income (Foley, Hartzell, Titman, & Twite, 2007), R&D activities (Brown & Petersen, 2011; Pinkowitz, Stulz, & Williamson, 2012) and agency issues (Fama & Jensen, 1983; Jensen & Meckling, 1976). For the latter, in sharp contrast to the financialisation theory, the accumulation of cash and liquid assets is regarded more as wasted resources rather than profitable investments. Additionally, Figure 16 can provide empirical evidence for the tax avoidance motive by showing that NFCs are keeping a higher amount of cash and liquid assets outside the USA.

The results from the analysis of uses of cash do not support either the financial rentieralization hypothesis. Financial investments represent a relatively minor and constant use of cash over the period which is considerably lower compared to the increase in acquisitions and buybacks. While the former confirms the increased importance of M&As, the latter highlights the effectiveness of the pressure exerted by the maximization of shareholder value movement.

8. Conclusion

This paper has contributed to the literature on the financialisation of US NFCs by providing an exhaustive empirical analysis of the dynamics it involves. We identified that this concept is usually applied to two different phenomena: the primacy of shareholder value orientation and the increased acquisition of financial assets from which NFCs derive a growing proportion of financial income. Our primary concern has been to scrutinize the empirical evidence regarding the second usage of the term which we defined as the financial rentieralization hypothesis. The main contribution of this paper has been to show that, for the aggregate of NFCs (but also for different sizes considered on their own), this hypothesis does not hold. The evidence used to sustain it usually shows an increase in the financial assets held by NFCs along with higher proportion of financial income.
However, in terms of assets, one of the main changes has been the growth of goodwill. In the Financial Accounts of the USA this asset is part of a miscellaneous category classified as financial even though most of their assets are intangibles. Foreign Direct Investment is another asset which has increased and is considered as financial by the Financial Accounts of the USA although it should not be necessarily considered as such. Far from supporting the *financial rentieralization* hypothesis, the increase in intangibles in general, goodwill in particular, along with FDI point to other paths followed by US NFCs which are the refocusing in higher value added activities, M&As and internationalization respectively.

For FCs, intangibles and goodwill play a minor role. On the contrary, the most relevant assets are ‘Receivables’ and ‘Other Investments and Advances’. These type of assets have remained fairly constant (or even decreased) for NFCs while, at the same time, the proportion of NFCs with a significant amount of Receivables and Other Investments and Advances has decreased over the past 25 years. ‘Cash and short-term investments’ is the only financial asset that has increased since the beginnings of the ’90s. Nevertheless, the proportion of financial income over total income is fairly low and, more important, has been decreasing in the last years. Moreover, if we compute a financial profit over total profits it remains negative for the whole period and worsens since the ’80s. This clearly indicates that NFCs look for other motives when they acquire this type of assets.

Looking forward, we identify some paths that would be interesting to explore. Firstly, if decreasing investment over the last few decades cannot be explained by financial crowding-out, then we are in need of new explanations. Secondly, if financial income is not a relevant source of income, then future investigations should aim to other ways by which NFCs are able to maintain, at the same time, strategies of downsizing and distribution to shareholders, i.e. the paradox of profits without investment. Examples of these other paths are the financialisation—offshoring nexus (Auvray & Rabinovich, 2017) and market power and technological changes (Durand & Gueuder, 2017).

Finally, although in this article we have shown that *financial rentieralization* is not a strategy followed in general, further studies should focus on the determinants of those cases in which NFCs do mimic FCs. In this paper we have indicated two ways in order to do that. First, it would be necessary to focus on those cases with a significant proportion of ‘Receivables’ and ‘Other investments and advances’. Second, we provided a list of NFCs with information regarding income from financial division showing that, for them, financial income plays a more relevant role.
Figures

Figure 1. Composition of financial assets less unidentified miscellaneous assets, NFCs, 1946-2015. Source: Table B.103 and L.103, Financial Accounts of the USA

Figure 2. Composition of assets, NFCs, 1955-2013. Source: IRS
Figure 3. Composition of assets, NFCs, 1961-2016. Source: Compustat

Figure 4. Composition of assets, FCs, 1961-2016. Source: Compustat
Figure 5. NFCs with significant proportion of Receivables and Other Investment and Advances, 1950-2016. Source: Compustat

Figure 6. Financial Income as percentage for total income, NFCs, 1955-2012. Source: IRS.
Figure 7. Net Financial Profit as percentage of total profits, NFCs, 1955-2012. Source: IRS.

Figure 8. Variations of financial income, financial expenditures and federal funds rate, NFCs, 1956-2013. Source: IRS, Financial Accounts of the USA.
Figure 9. Financial Income as percentage for total income, FCs, 1955-2012. **Source:** IRS.

Figure 10. Sources of cash, NFCs, 1971-2016. **Source:** Compustat.
Figure 11. Uses of cash, NFCs, 1971-2016. Source: Compustat

Figure 12. Uses of cash, FCs, 1971-2016. Source: Compustat
Figure 13. Composition of assets by different size of assets, NFCs, 1959-2013. Source: IRS

- Notes and accounts receivable less reserve
- Inventories
- Cash, Government obligations and other current assets
- Other investments and loans
- Depreciable assets accumulated depreciation
- Other capital assets less reserves
- Residual
Figure 14. Financial Income as percentage for total income and Net Financial Profit as percentage of profit, NFCs, 1961, 1962, 2004-2013. Source: IRS.
Figure 15. Composition of assets, NFCs, 1961-2016 and Uses of cash, NFCs, 1971-2016. Top 5% and 1% in size of assets. Source: Compustat
Figure 16. Evolution of ‘Cash and Short-term Investment’ and ‘Cash, Government obligations and other current assets’ over total assets, NFCs, 1961-2013. Sources: Compustat and IRS

Figure 17. Evolution of ‘Net Property, Plant and Equipment’ and ‘Depreciable assets accumulated depreciation’ over total assets, NFCs, 1961-2013. Sources: IRS and Compustat
Appendix

Table A1. Definitions of variables in figures

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<td>Other investment</td>
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<tr>
<td>Other Intangibles</td>
<td></td>
</tr>
<tr>
<td>Other Assets</td>
<td>Compustat Data Item 69</td>
</tr>
<tr>
<td>Residual - Figure 3 (Other Assets + Other Current Assets)</td>
<td></td>
</tr>
<tr>
<td><strong>Figures 6, 9, 14, A2</strong></td>
<td></td>
</tr>
<tr>
<td>Other interest</td>
<td>IRS</td>
</tr>
<tr>
<td>Interest on government bonds</td>
<td>IRS</td>
</tr>
<tr>
<td>Net Capital Gain</td>
<td>IRS</td>
</tr>
<tr>
<td>Net gain, noncapital assets</td>
<td>IRS</td>
</tr>
<tr>
<td>Dividends domestic corporations</td>
<td>IRS</td>
</tr>
<tr>
<td>Dividends foreign corporations</td>
<td>IRS</td>
</tr>
<tr>
<td><strong>Figures 7, 14, A2</strong></td>
<td></td>
</tr>
<tr>
<td>Net Financial Profit = Other interest + Interest on government bonds + Net Capital Gain + Net gain, noncapital assets + Dividends domestic corporations + Dividends foreign corporations – Interest Paid</td>
<td>IRS</td>
</tr>
</tbody>
</table>
Figure 8
Financial Income = Other interest + Interest on government bonds + Net Capital Gain 
+ Net gain, noncapital assets + Dividends domestic corporations + Dividends foreign 
corporations
Financial Expenditures = Interest Paid
Federal funds effective rate

Income Before Extraordinary Items
Depreciation and Amortization
Extraordinary Items and Discontinued Operations
Deferred Taxes
Other Funds from Operations
Sale of Property, Plant and Equipment
Sale of Common and Preferred Stock
Net Long-Term Debt Issuance = Long-Term Debt Issuance - Long-Term Debt Reduction
Net Increase in Investments = increase in Investments - Sale of Investments
Equity in Net Loss (Earnings)
Sale of Property, Plant and Equipment and Sale of Investments - Loss (Gain)
Short-Term Investments - Change
Capital Expenditures
Acquisitions
Other Investing Activities
Purchase of Common and Preferred Stock
Cash Dividends
Other Financing Activities
Net Receivables = Accounts receivable - Accounts Payable and Accrued Liabilities
Cash and Cash Equivalents - Increase (Decrease)
Other Uses (Equity in Net Loss, Sale of Property, Plant and Equipment and Sale of Investments, Net Receivables)

Mathematical Appendix

We define the ratio of portfolio income as calculated by Krippner and Crotty in the following way (we do not take into account depreciation allowances but it does not change the result):

\[
R_{pi} = \frac{I_f}{I_f + I_{nf} - C_f - C_{nf}}
\]

Where \( R_{pi} \) is the ratio of portfolio income, \( I_f \) financial income, \( I_{nf} \) non-financial income, \( C_f \) financial costs and \( C_{nf} \) nonfinancial costs.

We are interested to know why this ratio could be moving so we calculate total differential of \( R_{pi} \).

\[
dR_{pi} = \frac{(I_{nf} - C_f - C_{nf}) \cdot dI_f}{(I_f + I_{nf} - C_f - C_{nf})^2} - \frac{I_f \cdot dI_{nf}}{(I_f + I_{nf} - C_f - C_{nf})^2} + \frac{I_f \cdot dC_f}{(I_f + I_{nf} - C_f - C_{nf})^2} \\
+ \frac{I_f \cdot dC_{nf}}{(I_f + I_{nf} - C_f - C_{nf})^2} \\
\]

If \( \uparrow C_f, ceteris paribus \rightarrow \uparrow dR_{pi} \)
Figure A1. Composition of assets by different size of assets, Manufacture, 1959-2013. Source: IRS
Figure A2. Financial Income as percentage for total income and Net Financial Profit as percentage of profit, Manufacture, 1961, 1962, 2004-2013. Source: IRS.
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