CAPITALISM IN THE PERIPHERY

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Since the disintegration of the Soviet Bloc in 1991, there has emerged a unipolar capitalist world economy with USA at the apex. However, *core-periphery thesis* of Immanuel Wallerstien, the *metropole - satellite thesis* of Andre Gunder Frank, the *immiserising growth thesis* of Jagdish Bhagwati, the *under-development paradigm* of Samir Amin, as well as the *imperialism position* of Robert Rhodes are still valid today. What have changed are the rise of Islamic Fundamentalism as a global force and the emergence of the European Union as a powerful economic entity. One thing is clear and that is, unipolar capitalism has come to stay as a socio-politico-economic system, which is resilient because of its capacity to harness creativity and promote innovation *a la* Joseph Schumpeter. Frederick Engel's concept - that every system creates the seeds of its own destruction has been thus kept at bay. It is in this overall theoretical framework that this paper seeks to examine the transition of India - from a state capitalist economy to a relatively free economy in the periphery of the capitalist world economy.

There is no point in entering into a polemic on a serious subject as this, unless the fundamental assumptions are in order. This we will delineate and proceed only thereafter.

- Man is the beginning and the end of all analysis. He is both the subject and the object of social inquiry. Hence, his welfare and well-being takes primacy over all other considerations. After all, the entire *quality of human life debate* springs from here.
- Theory is an abstraction of reality that seeks to explain reality. If a theory cannot explain reality it is a quasi theory, a meta theory or not a theory at all. The distinction between theory and practice disappears. Indeed, once theory has been perfected, reality has no option but to fall in line.
- To speak of equality implies the practice of equality: in law, in governance and all other spheres. But equality does not mean levelling. It implies two tenets: *by each according to his efforts* and *to each according to his needs*. Without this equality becomes a meaningless, senseless, abstract phrase.
- We must wake up and realize that India is predominantly still an agricultural country. The primary sector is relatively

neglected giving rise to disguised unemployment. The manufacturing sector is not doing too well and our secondary sector base is fast eroding in the wake of global competition. The tertiary sector or the service sector contributes about 53% of the GDP and it is here that Direct Private Investment is pouring in. But how can we forget that most of the tertiary sector is an enabler and we need substantial increase in both agriculture and manufacturing sectors so that the products can be enabled for global competition.

Based on the above, any political economist who examines the Indian scenario in the beginning of the 21st century cannot afford to overlook certain facts, primary among which are brought to the fore by the present globalisation policies and the crisis is South East Asian economies.

There is no gainsaying the fact that the capitalist world economy in 2000 AD is unipolar with the United States at its apex. It unequivocally represents a boundary less universe and thrives on the cutting edge of technology. However, there were contradictory tendencies which have manifested themselves in the last decade and which cannot be overlooked.

- Balkanisation of Eastern Europe and the rise of nationalistic tendencies
- Federalization of Western Europe and the unification of markets in the form of a major customs union
- The rise of terrorism and countries that supply the foot soldiers for the jihad also claiming to help the West in their fight against the disruptive forces of Islamic terrorism

From a rational-positivist position we can say that on the macro economic front there has been a crisis of theory. Let us quickly go over the facts.

- Stagflation in the 1960s questioned the erstwhile paradigm that inflation was only possible after full employment equilibrium had been reached.
- The oil crisis in the 1970s showed that the theory of oligopolistic pricing was highly politicised.
- The stock market crash of 1987 proved that conservative economic thought in the form of monetarism, supply side economics and the rational expectation hypothesis had failed.

Conservative right wing political economy was seen to have had questionable paradigms as the dusk of the last millennium set in. For instance, conservative economic theory could not explain the phenomena of:

- Oligopoly pricing
- Product and process piracy
- Oligopsonistic markets
- Bilateral monopoly in luxury goods
- Strategic alliances
- A boundary-less universe

Hence decisions continued to be made under conditions of relative uncertainty and (at least) partial disequilibrium. In this global environment where the Soviet Bloc has disintegrated and there is no really formidable countervailing tendency to the economic might of the United States, we posit three working propositions.

- Export led growth is a fallacy. Since export is dependent macro variable how can it lead growth?
- It is fatal to go in for globalisation unless the liberalization process has been completed. Unless one's own house is in order how can one bargain from a position of strength?
- One cannot treat international trade as

a purely economic phenomenon. In fact, the economics of value-exchange-growth cannot be divorced from politics.

Based on these three premises the crisis that plagued the South East Asian economies has been analysed in this paper.

By 1990 the South East Asian miracle was a feather in the cap of free market capitalism. Economists like Guilder and Laffer swore by it while Friedman recommended it for the entire periphery.

The industrial strategy of Korea, Indonesia, Malaysia, Thailand and Singapore was outward oriented. The conservative economist eulogized this as export led growth. Some even went so far as to recommend it as a growth alternative for the rest of the capitalist periphery. Papers were written and theses were propounded on the theme. The accepted scholarship examined the following facets of this economic miracle.

- High rates of government and private spending
- Reliance on private ownership in the industrial sector
- Low inflation rates and restrained domestic credit policies
- Convertible currencies with low or zero black market premia on foreign exchange

Four facets conveniently missed out by them and which should have been included according to us in this paper are:

- Political alignment with the USA and its NATO allies
- There is no substitute for economic self-reliance through infrastructure growth
- The uneven development between peoples, industries and sectors
- The unequal distribution of income wealth and opportunities within the same geo-political sector

Following the dictates of the West, financial reforms were mooted throughout South East Asia in the early 1990s. These reforms were aimed at upgrading financial institutions so that they could merge with the international capitalist economy. Hence, there was an expansion in the banking sector. The banking sector remained illiquid and heavily under-capitalized.

However, research demonstrates that foreign players entered the market and the strain on the banks to compete increased. Margins were reduced and speculation was increased for short run profit motives. This exposed the financial sector to the instabilities of the international financial markets.

The Bangkok International Banking Facility was set up to compete with Singapore and Hong Kong as financial nerve centres. Short-term debts piled up and the infrastructure was not strong enough to absorb the shocks. Economists like Paul Krugman were satisfied therefore with ascribing the crisis to a failure of the financial reforms. Other mediocre economists merely towed the line contributing little new to the debate from their side.

But let us pause and reflect. Is it really so simple? Bangkok also did not have the political advantage of Singapore and Hong Kong so that it was very much on its own. It was increasingly vulnerable to a reversal in capital flows owing to a dramatic fall in the local currency values.

Since the threat of socialist expansion no longer loomed large on the horizon the interest of the West in propping up South East Asian economies waned. Investment was being diverted to develop Eastern Europe instead. Yet, exchange rates were being maintained and exports continued to fall after 1997. This was, (also significantly), precisely the time when Western capital investment in Eastern Europe had doubled.

Hence the South East Asian economies resorted to expand domestic demand by speculative spending. Without a sound infrastructure to back this move, it proved disastrous. The stock market reacted in a volatile manner and there was panic setting into financial and banking sectors. The free-floating Baht did not help matters. There was a large amount of Direct Private Foreign Investment through multinationals in Thailand, Korea and Indonesia. Hence the ability of the national economic policies had a limited effect on the totality of the situation.

The IMF bail out came on condition that all credits are rolled over. This condition was complied with. Yet, in 1998 the IMF quite strangely relented on its fiscal surplus in Thailand, Indonesia and Korea. Currency markets demonstrated that exchange rate movements were closely linked to the realization of budget surpluses. Why did the IMF strategy fail? Was it because it could not contain the turbulence in the banking sector or was it because trust between the lenders (banks and financial institutions) and borrowers (consumers and industries) had reached a new nadir?

From the side of the *international arena*, to use Wallerstein's term, there was weak macro management because:

- The IMF was poorly placed to rally market confidence in the short term
- The IMF stated that weak financial institutions caused the crisis and this fuelled the panic
- Tough measures recommended by IMF led to closure of ineffective institutions and this exacerbated the panic
- The IMF wanted fiscal contractions to be implemented even when the economies were facing an outflow of foreign investments
- As the lender of last resort the IMF fell far short of the requirement

From the side of the national economy, there was inadequate managerial capability because there had been a steady and concomitant *rise of mediocrity*. To add to it was the question of *moral hazard*, which clearly meant that governmental guarantees against capital raised, investments made and loans taken were worthless. In times of economic crisis the government could not muster enough muscle to bail out the defaulters.

India benefited by default because our involvement within the capitalist world economy was half-baked. Had India gone in for full capital account convertibility then the maelstrom would have sucked us in too. But our bureaucrats made sure that we were slow to react and thereby capital account convertibility had not taken shape. What are the three lessons, which the Indian capitalist periphery in 2006-07 can draw from the South East Asian crisis?

There should always be growth led export if economic development is to be realized. (Export by definition is a dependent variable).

Strengthen the infrastructure before expanding the superstructure of the economy. (While infrastructure is based on capital budget, superstructure is based on current budget and they ideally should be in equilibrium).

International trade is not merely an economic phenomenon, as it has political overtones, which we cannot afford to overlook. (One only has to follow the Doha and Cancun round of talks to understand this).

Now, let us examine the Indian case.

India has one billion mouths to feed. More people are born in the name of religion than die for it making a mockery of birth control. More children are born than jobs are created so unemployment in the long run will increase. Economists like Isher Judge Ahluwalia have said almost as much as in her classic study of post reforms unemployment.

The Indian constitution continually guarantees a rise in *micro nationalism* (through the linguistic division of states) and *macro racism* (through the reservation policy). The Indian constitution speaks of creating a secular state but has a unified criminal law alongside of stratified civil law. One can now realize the wisdom and foresight of Dr. Rajendra Prasad when he refused to sign the Hindu Code Bills put up by Jawaharlal Nehru for the Presidential signature. How can we speak of a Hindu Marriage Act, a Christian Divorce Act and a Special Marriage Act running concurrently in a secular country? The Parliament had in the Shah Bano case, wherein it went against the Supreme Court Judgment and legislated that if the law of the land was at variance with the law of Koran then the latter would be upheld. Nothing could have been an uglier slap in the face of secularism and that too by a group of politically minded persons who have supposedly always championed the secular cause all along. Was secularism being equated to a vote bank, one wonders?

There is far too much politics with our economics and too little economics with our politics is a reality that any analyst who has studied India's State Capitalism will concur. If we recall, industry was nationalized under Indira Gandhi but not socialized. In addition, we know that Keynesian interventionism is meant for an industrialized economy in a state of recession. Under Jawaharlal Nehru and Prasanta Mahalanobis we went in for macro dynamics where (rightly) unemployment was seen as a greater social evil than inflation. This was a time when India's industrialization process had just begun and state capitalism was in the process of being built up. Thanks to that vision we have an industrial base. What went wrong was that we were quick to accept the dictum *to each according to his needs* and overlooked its twin *by each according to his effort.* Sate capitalism was mistaken for social security with only benefits to gain but no deliverables and responsibilities to live up to. Up until 1991, India was registering a modest (Hindu) growth rate. But three successive governments at the centre wrote-off agricultural loans in exchange of votes, jeopardized our national exchequer and we had to go begging to the World Bank for a financial bail out. This marked the entry of India into the capitalist world economy.

Thereafter growth rates grew and when India's economy was industrialized we gave up interventionist economics on the say so of the World Bank. When we blame the public sector for harbouring sick units we conveniently forget that until some years ago the public sector took over sick private sector units in order to protect the unemployed because there was no social security net to absorb them. Just when Keynesian interventionism is most needed we opted for a free market economy and successfully threw the baby out with the bath water. Yet, as a conditionality of the financial bailout Indian planners prodded by monetarists and supply side economists advocated:

- The need for efficiency to precede equity.
- The rapid emergence of an integrated global economy.
- The replacement of state capitalism by private capitalism.

We are yet again on the brink of a global recession and may come out of it by the end of the year 2007, if the US economy pulls us out! It is precisely to prop up aggregate demand and boost disposable income, that the rise of the permanent arms economy and its fall out in Iraq was witnessed. If the situation does not improve, Iran may be next in line for the West in making an excuse to prop up their aggregate demand. Yet we, Indians are continuing to follow the leader: USA. Such is the level of our dependence on the capitalist world economy. We ape the West and talk of globalisation as if it is a new buzz word, conveniently forgetting that it was globalisation that took Arya Bhatt's zero and our decimal system out of India in 4 A.D. through muslim traders going to Europe. We forget that Direct Private Foreign Investment is nothing new. It began with the East India Company under Robert Clive and Warren Hastings more than two centuries ago.

In 2002, we had less than 1% rate of inflation and we proudly spoke of a 6% to 8% annual economic growth when any child that runs knows that a modicum of inflation say 5% is needed for moderate economic growth since the investment multiplier comes into play. Interest rates are falling and shall continue to do so due to pressure from international players. Unemployment rates are rising and we can do nothing to contain them. How can we speak of achieving sustainable economic growth with a straight face under these conditions? And yet, we speak of a growth rate of 8.5% per annum in 2006. A certain amount of inflation, we know, is needed to generate economic growth so the current (stated) inflation rates are questionable even if we were to accept the fact that the choice of the "basket of commodities" could be skewed. It will certainly be a gargantuan task, for instance, if we were to try explaining to a common housewife who regularly does her weekly shopping at the local bazaar that inflation rates are in the range of 3%-5% (as the Finance Ministry would have us believe).

There is then a definite case to be made out for economic planners to re-learn their subject and go back to basics. There is an even greater case to be made out against politicians who do not understand economics to keep away from tinkering with that subject. This is not like working in a laboratory where a failed experiment will cause some financial loss. It is a case of macro mis-management of an economy whose collateral damage cannot be contained.

The fact of the matter, however, is that we have become a part of the capitalist world economy and we have to make the best of it. So, whereas autarky as an option is ruled out; whereas we cannot avoid being an intrinsic part of the capitalist world economy; whereas we cannot give up our economic independence; and whereas we need to consistently convert our core competencies into competitive advantage; in order to thrive on the cutting edge of competition, we as a country must:

- Resort to interventionist macro economic policies without being apologetic about it.
- Prepare a level playing field between private capitalism and state capitalism at home so that industries thrive and competition leads to cooperation.
- Pursue a path of economic growth, which will foster exports and not go about the other way round.
- Build our infrastructure first and only then go in for developing our economic superstructure.
- Tread carefully on the globalisation front unless the economy has been fully liberalized.

- Make our decision-making processes more transparent. If the Indian government could not bail out UTI what chance do we have if history were to repeat itself in the case of the LIC?
- Realize that inflation and unemployment are equally avoidable social evils.
- Learn from history especially from the failed experiments of Mexico, Brazil, Argentina and other peripheral capitalist economies.
- Realize that Direct Private Foreign Investment can only be possible when the cost of borrowing *(i)* is less than the rate of return *(r)*, and then judge, whether we as a country can sustain growth in spite of this.
- Stop looking upon Foreign Institutional Investors as sacred cows especially after the Enron-Anderson imbroglio.

The time for emotional display of sentiment has gone by. The time for realistic thought is at hand. There is certainly a crisis of national level leadership in most fields. There is simultaneously a case to be made for national level ethical conduct and a national level code of good governance to be laid down and scrupulously followed. It is not that the intelligentsia has failed us. It is that we have unwittingly opted for parliamentary democracy without realizing that democracy cannot flourish on empty stomachs and empty minds, both of which we have in ample abundance.

Finally and most importantly we must NOT fight shy of addressing the twin issues of *uneven development* between peoples, industries and sectors on the one hand and the *unequal distribution* of wealth, incomes and opportunities on the other. The question of equality can only be addressed if the civil code and the criminal code are in tandem - which they are not. Let us get one thing straight - we cannot paint everything with the same wide brush and expect good results. Even equality has its limits. There is nothing so unequal as the equal treatment of unequals.

Above all else, let us retain our self-esteem (not to be confused with ego) and proceed with the conviction of a yogi with a stable and serene mind. We gained our freedom in 1947, but we must continue to fight for our independence!

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