1st Raúl Prebisch Lecture

THE CRISIS OF CAPITALISM AND THE PERIPHERY

By

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Leaving aside my personal involvement, I think the idea of these lectures is a most useful and timely one under present circumstances, because we need some illumination; our path remains obscure, especially with recent happenings in the field of international economic policy and in our national development. The idea is both useful and timely because we are facing not only the crisis of capitalism but also the crisis of ideologies, the serious crisis of those conventional theories which do not permit a correct interpretation of the realities of present events or a clear picture of what our course should be.

In my opinion the conventional theories exhibit the great defect of having disregarded and continuing to disregard, systematically, the social structure and its constant modifications. They cannot therefore serve towards an understanding of the crucial phenomena of the present. In my opinion this crisis of capitalism is a structural one—a serious structural crisis more complex and difficult than what I experienced as a young economist in the 1930s. That was cyclical, a difficult crisis but it was overcome. The present crisis on the other hand derives from the inherent logic of the system, through the structure within which the latter operates. The most disturbing feature of this crisis is the structural imbalance between the rate of consumption and the rate of accumulation of reproductive capital. I emphasize the word “reproductive” because it denotes the kind of capital which increases employment and productivity, and because there are many other, harmful forms of accumulation.

I shall try to explain very briefly why I believe the crisis to be a structural one. In my opinion the reason is that income distribution and capital accumulation are largely the result of the shifting play of social power relationships created by changes which continually occur in the social structure as technology advances. The upper classes have the obvious ability, owing to their structural position, to appropriate the benefits of ever-growing productivity based on technological progress. These benefits enable them not only to accumulate capital but also to develop, in some cases quite madly, a privileged consumer society at the expense

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of capital accumulation. Many of you will be surprised that I say this with reference to the main dynamic centre of capitalism: the United States of America. The reason is that we thought the problems of accumulation had been solved there, but they have not. Just the opposite has happened, and I shall try to explain why.

We have seen on the one hand the upper classes with their capacity for retaining the benefits of technological progress; on the other lies a phenomenon which has emerged and developed more and more, especially since the Second World War: the trade union and political power of the labour force, a power which enables the workers to claim an increasing share of the benefits of technological progress from those who appropriate them by way of economic surplus, as well as to enjoy that share to a growing degree and adopt the forms of consumption of the upper classes. I say trade union power and political power. Political power leads labour to make use of the State machinery and to look more and more to the State for greater social advantages. Finally there is bureaucratic and military power, which as we all know has swollen abnormally. As a result, the privileged consumption of the upper classes is being inflated by the private and social consumption of the various categories of workers and the civil consumption and military consumption of the State.

The fundamental point to realize is that as these various forms of consumption grow with changes in the social structure, the growth does not take place at the expense of upper class consumption but is superimposed on it, so that as time goes by, as the system evolves by virtue of its internal logic, a time comes when the rate of growth of the various categories of superimposed consumption tends to overtake the rate of accumulation of capital, and especially of reproductive capital; as I said earlier, this is the kind which raises employment and productivity and is therefore of vital importance to any system. Every economic and social system needs a continuous increase in capital accumulation. Here is what I think is happening in the big capitalist countries, above all the United States of America. The phenomenon which worries that country so much is the decline in productivity. This may be due to a number of factors, but in my view the most important one is the structural imbalance I mentioned. The system contains no regulating mechanism to ensure a proper balance between consumption and accumulation. Market forces are not capable of controlling consumption and accumulation. They have a great virtue in other respects. I do not disagree with those who believe that market forces are very important. But their importance is limited. They cannot solve the fundamental problems of the economy in a structural evolution which has reached the stage I have just described.

And not only is the rate of capital accumulation affected; capital exists in forms which do not increase productivity, beginning with capital invested in military consumption. This capital may be effective in other ways but it has no beneficial impact on productivity. What is more, the ceaseless proliferation of goods and services which technological progress has brought with it, this diversification, also means the accumulation of forms of capital which may serve to attract the consumer, excite his sense of social prestige and so on, but which do not increase productivity. This is another aspect of the crisis which is evident in all societies and even in the less developed ones of our own countries.
It helps to accentuate the dynamic imbalance between the rate of consumption and the rate of accumulation.

Also it is all too obvious that part of the big increase in productivity in the post-war period which stimulated these various forms of consumption was to some extent spurious. It was an increase in productivity achieved through irresponsible exploitation of non-renewable natural resources; oil is an obvious example. In order to remedy this situation, which is crucial for mankind, a greater investment of capital is needed per unit of energy and therefore per unit of output. We must also consider the capital which will be required to counteract the degradation of the environment that results from the ambivalent effects of production technology. Thus there is a set of situations, created by the internal logic of the system, which have brought about the crisis.

Do not misunderstand me: when I talk of the crisis of capitalism in the centres I am not saying that it is any way symptomatic of the decadence of capitalism. It is not. Without any doubt the period of history in which capitalism showed a really huge constructive impulse, based of course on the ambivalent nature of technology, was in the many years after the Second World War, from the post-war period to the first half of the 1970s. What I think happened is that from sheer energy, capitalism burst its banks, outstripped itself, there being nothing in the system, in the spontaneous functioning of the system, to prevent this. There is nothing which is capable of bringing this dynamic impulse under control again. It is not that the problem cannot be overcome; however, it will be overcome not through the play of market forces—of what has been called, to use the fashionable expression of recent years, the magic of the market—but by conscious and deliberate State action along democratic lines to create a new macroeconomic regime of capital accumulation and income distribution which will prevent the excesses, attended by such serious consequences, that we are now witnessing.

We still do not like to convince ourselves that these consequences really are serious and we continue to believe that there are easy remedies, that it is a question of accepting some sort of compromise, that the system should make some sacrifice in order to recover its equilibrium. I am referring to monetarist policies. How do these monetarist policies seek to eliminate the imbalance? How do they try to adjust the rate of consumption to the accumulation needs of the system in order to correct the various evils I have mentioned? There are two forms of monetarism. One kind of monetarist policy is to try to correct excessive consumption by restricting it. And how is consumption restricted? By a policy of credit restriction which shrinks economic activity and produces unemployment. This is a very crude procedure, but it is what underlies one type of monetarist policy. It means creating unemployment to such an extent that labour finds its trade union power crippled and accepts a lowering of wages to the extent needed to revive the dynamics of the economic surplus and hence of capital accumulation and privileged consumption by the upper classes.

Do not think that the social implications of this are as straightforward and obvious as I have made them appear. Yet that is the background of the monetarism employed both in the centres and on the periphery, especially the Latin American
periphery. And it derives a certain theoretical support from the conventional theories, because according to these one of the defects of the system is precisely the trade union and political power of labour; therefore that power must be overcome, destroyed, to the point of acceptance of wage levels which enable businesses to be competitive.

What these theories overlook, and this exemplifies, let me say it again, the disregard of the social structure, is the fact that—looking at the system historically, from the end of the nineteenth century onwards—its only strength for revival, for the creation of particular skills at various levels of the labour force, for participation in the fruits of technological progress, has been the trade union and political power which opposes the power of the upper classes to tap the fruits of increased productivity in the form of economic surplus. The conventional theories have always maintained that the system, if left to the play of market forces, tends towards the social dispersion of the benefits of technological progress. But this is not the case; they do not spread through society. They are mainly withheld by the upper classes, which account for most capital accumulation by businesses. Consequently, all that labour can do is to fall back on its trade union and political power, and when this is undermined it may happen that eventually labour gives way because of unemployment. If at some time the economy revives, can the trade union and political power of labour be bypassed once more or will there be another inflationary cycle resulting from the imbalance between consumption and accumulation? That is the big question. In my opinion the problem is insoluble—insoluble from this standpoint.

The other form of monetarist policy is the following: according to orthodox thinking, the growth of the State, of its civil and military consumption, need not lead to a fiscal deficit if there is a strict policy of increasing taxation to the extent that State expenditure cannot be reduced. But here we find that taxation too becomes inflationary when it falls heavily on the shoulders of the workers who, through their trade union and political power, have developed the muscle to compensate themselves for taxes. Thus the increase in State expenditure is reflected either in a clear and manifest deficit or else in taxes which are offset in this inflationary manner; ultimately the situation turns out the same, although its appearances are different. How can this be overcome? What form, what second kind of monetarism is adopted in this case? Naturally the manifest fiscal deficit has to be met, generally in an inflationary manner. This is what has been happening in the United States of America in addition to other forms of social inflation. To finance the deficit by means of credit expansion creates growing inflation, and labour is naturally compensated by higher wages and salaries.

To avoid this outcome, because inflation becomes a worry for all classes of society, a very interesting formula has been invented: that of meeting the deficit neither by taxation nor by inflationary credit expansion measures but by relying on public savings. In other words, by paying for excess State consumption through voluntary limitation of private consumption on the part of persons who buy government securities with their savings. This is why interest rates have risen to the highest levels ever reached in the history of capitalism. But why at the same time does the money created by the banks, the money which flows from the banking system, have to become dearer? Because in order to maintain
these high rates of interest on savings, the interest rates on bank money are raised as well, resulting in severe credit restriction. So this kind of credit restriction is applied through high interest rates. Why must the process be accompanied by an increase in bank rates? In order to ensure that the funds generated by the banking system do not find their way to the financial markets for purchasing securities, in which case the securities would not be paid for out of real public saving but from monetary expansion; in other words the inflationary effects would be the same. Thus a huge rise in bank interest rates through credit restriction makes sense.

But what is the consequence, what is the cost of lowering inflation in this way through public savings? First, dearer borrowing for business. Second, credit restriction deprives businesses of the money they need to increase their working capital, their operating capital. It is absolutely necessary and proper to expand credit in order to provide businesses with working capital, which is eventually translated into an increase in output. But credit restriction and higher interest rates hurt business and create a slump and unemployment, so that the social cost of this monetary policy is the same as that of the other monetary policy. Whether credit restriction is employed directly or to facilitate higher interest rates and attract savings, the consequences are exactly the same. In other words, inflation is reduced but at the cost of squeezing economic activity and producing unemployment, which naturally leads to a downward pressure on wage levels, and that is what we are witnessing in the United States of America.

If this were a cure, if it were not a temporary expedient to be discarded when economic activity recovers, serious thought would have to be given to accepting a temporary social sacrifice in order to stimulate the economy. But this is not the case. It is not a cure. Because when the economy does pick up, the phenomenon of wage and salary adjustment will recur; it is labour's way of participating, this being very difficult for them, if not impossible, through the mere play of economic market forces.

That to my mind is the significance of the two versions of monetarism, and the consequences are not confined to the country in which this policy is being followed, the main centre of capitalism—the United States of America—but produce disturbances throughout the world. The increasing anxieties of European countries, not to speak of the Latin American countries and the other developing nations, are plain; high interest rates are shrinking world economic activity and creating acute and growing unemployment with obvious social consequences, and potentially with very serious political consequences for the entire world. This is the result of a policy, the result of not looking realities in the face and of not seeking new formulas to supersede the traditional ones, which might have worked at a time when there was no trade union and political power or when it was very weak, but which cannot be applied now. Today we face a real situation basically brought about by the evolution in the structure of society.

Understandably, in the light of these events my mind reverts to dramatic episodes of the great world depression of the 1930s which I experienced as a young economist serving my country's Government, and trying to find a way at
least to mitigate the consequences of the serious happenings of that period. Just as the epicentre of today’s crisis is in the United States of America, so the epicentre of the great depression was in the United States too.

We economists, guided by what was being said in the centres, believed that it was a severe cycle but that “recovery”—that was the language used—was just round the corner. But it was not round the corner because banking restrictions caused near panic. There was fierce credit restriction. Unemployment reached huge figures, and that was not all. The United States—and this is very difficult to explain theoretically—decided to fight the depression by raising customs duties sharply against the rest of the world. These two phenomena, the shrinking of the economy and the raising of protectionist barriers, led to the collapse of the multilateral trade and payments system which had been working so well everywhere. The world was hurled into bilateralism; in other words, every country apart from the United States sought to meet the adverse effects of the depression, the loss of its exports, by import restrictions. But in order not to spread these measures the other countries limited their application to the United States. That is the significance of bilateralism. Despite everything these countries kept afloat through a bilateralism imposed by what was happening at the epicentre of the crisis. Then came the war, the Second World War, and many years passed before the multilateral trade and payments system could be re-established. The consequences of that policy, which I believe was wrong and I do not hesitate to say so, were prolonged and far-reaching for the entire world.

So I had to begin my working life as an economist in a major world slump and now, quite late in life, I am witnessing another crisis of capitalism. What has happened in between? The developed countries have had a long period of prosperity, of extraordinary growth rates such as never occurred before in the history of capitalism. And undoubtedly the developing countries were able to take advantage of these extraordinary growth rates in the centres and begin industrial exports, some of them with considerable success. This was beneficial but accompanied by very adverse consequences.

First of all, and I shall refer in particular to Latin America, we allowed ourselves to be mesmerized by the prosperity of the centres. Because of this prosperity, this hypnosis, we gave up a policy which was producing results, namely import substitution, not confined narrowly to individual countries but extended where possible to interregional trade. We went to the other extreme. Before, there had been economists who maintained, mistakenly, that out-and-out import substitution was the solution to development problems. It had to be combined with the export of manufactures. But the pendulum swung the other way with the great prosperity of the centres. We abandoned import substitution, and reciprocal trade arrangements among Latin American countries weakened considerably, because we thought that the world was beginning a new era in which exports of manufactures to the centres were going to clear the big foreign trade bottlenecks which had affected the countries in question. Quite naturally, we allowed ourselves to be seduced by the effects of the prosperity of the centres. We went to the other extreme: no import substitution, no reciprocal trade arrangements, our whole future lay in external growth, in exploiting the markets of the centres.
What is more, the great prosperity of the centres spread quickly, and in many cases uncontrollably, to the Latin American periphery. We tried more and more to imitate the advanced forms of consumption of the centres owing to great disparities in income distribution. There is no doubt that transnational enterprises played a major part in this imitation process. But the heart of the matter was the poor income distribution which characterizes Latin America and developing countries elsewhere. This is what enabled the upper classes to assimilate rapidly the forms of consumption of the centres, to the detriment of the accumulation of reproductive capital; that is the only thing capable of solving our problems of social segregation, this situation where huge sections of the population are left way behind at the bottom of the system, with low incomes, very low productivity and in many cases no job because insufficient reproductive capital has been accumulated to create more employment and raise productivity among the mass of the people.

Something fundamental to economic development has been missed because of the wastage of capital accumulation potential, caused by more and more resources being frittered away on the privileged forms of consumption which have taken root in the Latin American periphery. Of course there is the high population growth rate as well. During these years of prosperity we Latin Americans, on average, achieved high rates of economic growth too, but in absolute terms the masses remained as they were; no progress has been made in solving this grave social and human problem. Thus, by looking to the exterior, we abandoned what in my opinion was a policy that should have been continued, despite all its considerable and undeniable defects and shortcomings, and that should have been refined in the light of experience. This is from the external point of view; internally we have largely squandered the potential for accumulating the necessary capital which would have met the dynamic requirements of the system.

Those years of the great slump saw the beginning in Latin America of a movement of intellectual emancipation which consisted of taking a critical look at the theories of the centres, not in an attitude of intellectual arrogance—these theories have great merits—but in the realization that they deserved critical study. I must say that the United Nations played a big part in this critical inquiry which led us to seek our own path towards development instead of copying others; to ponder the realities of the situation and to try to meet the economic, social and moral requirements of development—the path of equity. Despite huge obstacles we were making progress, but when those great years of prosperity arrived and we allowed ourselves to be blinded by the centres, the search for our own path was broken off. Not only that, but in much of Latin America there was a resurgence of the neoclassical theories which had guided our development before the great world depression, in the hegemonic interests of the centres and of the hegemonic groups in the periphery but without regard for the great mass of the population, which industrialization barely touched. This was the model we tried to follow and gradually modify in the light of experience.

Despite all their benefits, however, those years of prosperity not only threw us off our course and led us to abandon or relax our efforts to find our own path of peripheral development, but left us at the mercy of the neoclassical ideas
which had proved totally inadequate to promote industrialization in Latin America. A number of Latin American countries experienced the excesses of so-called economic liberalism, which is only viable when political liberalism is suppressed. That is to say, two forms of liberalism stemming from the same philosophical ground ended up many years ago by parting company. In some countries the establishment of economic liberalism created the need, or rather was the consequence, of strong-arm governments which broke the trade union and political power of the labour force and believed that market forces would solve their main problems. We were intoxicated by the conventional theories. I think that those countries which adopted them with such enthusiasm are now realizing their disastrous consequences. Yet the northern hemisphere, and above all the most advanced country in the northern hemisphere, continues to propound certain conventional theories which are incompatible with the acceleration and social orientation of development.

Its hope is that market forces, the so-called laws of the market, will solve our fundamental developmental problems. I want to say this: I recognize that market forces have great importance, but they do not solve the basic problems for us. Have they solved our problems of irresponsible exploitation of natural resources, the environment, income distribution and capital accumulation? The market is something of great value and must be preserved, because the alternative is that basic decision-making about the system takes place from above—by those at the top of the pyramid—and this is incompatible with broader democratization and with political and personal freedoms. But it is a great mistake to conclude from this that market forces alone will solve all the problems. The market has no such magic. These forces must be combined with State intervention, which need not extend to the routine details of the economy, simply to the intelligent handling of the mainsprings of the system. In other words, we must be guided by rationality. The conventional theories inspired the belief that there was some rationality within the economy. What rationality, seeing the various evils that we face at the moment? Is it a rationality that in the final analysis serves internal and external dominant interests? There is a rationality here, but not from the collective point of view.

We have been waiting a long time for the play of market forces, according to the leading theoreticians, to solve our problems of development and income distribution. The belief was that market forces would spread the benefits of technological progress. I maintain that this is not so. I maintain that a new rationality must be sought, but not one based on hegemonic interests; rather, one based not merely on economic and social objectives but on eminently ethical ones. That is what must be restored to the economy. A return to political economy and not simply to brute economics, so as to progress by hard effort, through persuasion and explanation, to action. Of course, were we to take a look at our present experiences in perspective, we could not be optimistic. I believe that the struggle should continue, that it concerns not only the international community but our own countries. It is not a question simply of a new international economic order but of a new internal ethical and social economic order. These are the great problems which we have to solve in Latin America through hard sacrifice.