

NOTES ON THE CURRENT CRISIS I

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The problem touched in this little note is how to come to grips with the present world crisis from an economic point of view in as simple a way as possible. No doubt it will be amateurish, but professional economists seem to get lost in their own analysis and to establish a language so removed from how other people, including most politicians think that it becomes counter-productive. By that is meant: no fruitful basis is found for political action; moreover, the way economic analyses are carried out they may even block for such action. On the other hand, what is attempted here is also quite economic, starting with supply and demand, or S and D.

Imagine a world with one supplier, a producer; one market, a "demander"; and then just one product. From:

$$(1) \quad Pr = \frac{S}{N \times H}$$

or productivity equals supply produced divided by the product of number of workers and number of hours, we get [for one product]:

$$(2) \quad S = Pr \times N \times H$$

This equation gives us the supply. It is a tautology, which does not mean that it is useless; pointing to three ways of increasing or decreasing the quantity produced. So far I have found that way of expressing the supply side quite useful.

But the demand side is more problematic. As a point of departure let us try to indicate what we want. We want an expression for demand in such terms that the usual approaches in every day economic behavior within and between nations can be formulated by simple operations within the equation. Obviously the demand has something to do with the level of want, W. It also has to do with the price, P, per unit. The buying power, let us call it B, enters the picture. And then there is a fourth dimension: the quality, Q, of the product offered. Of these four

entities two are economical, B and P, and two are psychological, W and Q. Seen another way, two of them relate to the product, Q and P, and two to the demander, W and B. Either way one arrives at the same expression that does not seem too unreasonable:

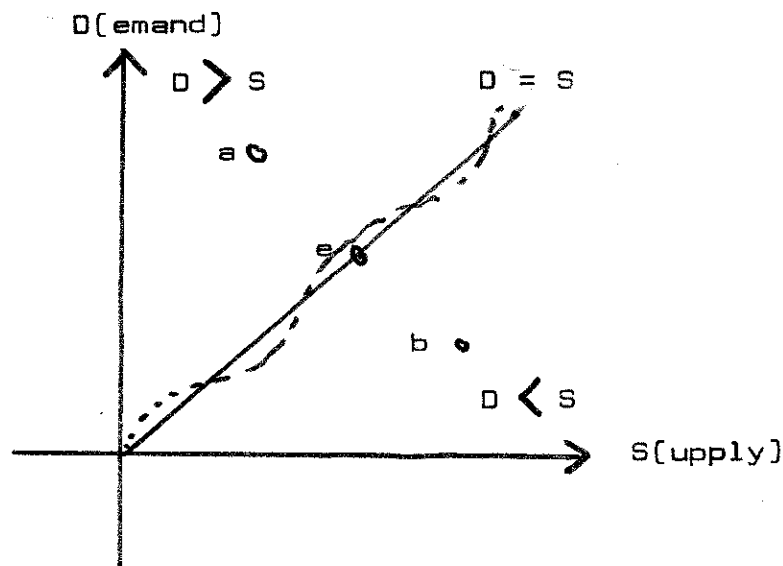
$$(3) \quad D = [W \times Q] \times \frac{B}{P} \quad \text{or} \quad D = \frac{Q}{P} \times [W \times B]$$

which would give us

$$(4) \quad D = k \times W \times Q \times \frac{B}{P}$$

where k is a coefficient, and D as usual stands for the quantity demanded; meaning effectively wanted, bought if available.

The focus then shifts to the S, D relation:



By definition it is assumed that the economic system seeks equilibrium,  $D = S$ , but will overshoot and undershoot, making it oscillate around the  $D=S$  line - upwards in times of expansion, downwards in times of contraction. In position (e) above there will be no drive for change within this framework of reasoning; in positions (a) and (b) there would be such forces tending towards equilibrium. The moves are easily described:

	<u>contraction</u>	<u>expansion</u>
<u>under-production</u>	decrease demand	increase supply
<u>over-production</u>	decrease supply	increase demand

All four are associated with political drama when the deviation

from equilibrium is of some magnitude. Whether contractive or expansive modes of adjustment are eventually engaged in depends, of course, on all the constraints on the system. But in an expansionist culture, like certain modes of Occidental civilization, expansion will probably be tried first, regardless of other constraints.

The major focus of this note is "the current crisis" - in the West, in the First World, which is here seen as a crisis of over-production - the supplier being the First World (OECD countries with the exception of Japan), the demander being the world, and the products being many/most products produced by the First world. However, before commenting on that with the very simple tools provided here, some words about under-production. Under this condition there is a scarcity of goods/services but an effective demand for them. If the supply cannot be increased by means of more workers and/or more working-hours, it will have to be through increased productivity; the trade-off between the three belonging to the essence of the politics of growth, expansion. But there is also the other possibility well known from countries that "get stuck": to decrease the demand. This can be done in a product-oriented manner through low quality and/or high prices or in a demander-oriented way, through decreased buying power and/or more modest wants. The assumption might be that after some period of demand-reducing efforts people will start forgetting about the product, eg person cars. And so on, and so forth.

In a general crisis in which supply outstrips demand for a number of products and stockpiling is non-economical, this way of thinking about supply and demand gives us the following:

To decrease the supply:

- S<sub>1</sub>: decrease the productivity
- S<sub>2</sub>: decrease the number of workers (unemployment)
- S<sub>3</sub>: decrease the number of working hours (leisurism)  
per day, week, month, year and/or working life

To increase the demand:

D <sub>1</sub> : increase the want	}	demander-oriented
D <sub>2</sub> : increase the buying power		
D <sub>3</sub> : increase the quality	}	product-oriented
D <sub>4</sub> : decrease the price		

To this should be added the idea of introducing new products, but we stick to the problem as here defined, with one product. One might also add the idea of introducing new markets; but then it is already assumed that for the producer, the First World, the market in question is the world market. One may try to increase the want level or the buying power level for parts of this world market or for all of it, but that is not the same as opening up a fundamentally new market.

The seven strategies indicated in this list are certainly not mutually exclusive. But before entering into that, some words about the origin of the crisis. Four factors will be briefly considered: the role of the Second world [the socialist countries]; the role of the Third World [-OPEC] countries; the role of the OPEC countries and the role of the Fourth World countries [the world South-East countries], particularly Japan. The point of departure, then, is a world where the First World had a virtual monopoly on the production of goods/services for the world market; obtaining raw materials [including energy] cheaply, partly through the colonial structure, obtaining labor cheaply the same way, being guaranteed markets with absolute monopoly through colonialism. The only problem would be availability of risk-taking capital. Through capital- and/or research-intensive production the productivity could be increased, offsetting declines in number of working hours. Slowly, also, want and buying power in other countries were increasing. The First World was "doing fine".

The first threat to the system was the Second world, the socialist countries. In principle they were no longer avail-

able as reservoirs of production factors or as markets. However, over time this type of withdrawal from the world system broke gradually down. Their re-entry as a source of production factors took the form of joint ventures; their re-entry as a market was based on the capacity of the socialist economies to increase the wants for the type of goods/services produced by the capitalist countries, and increased buying power -- all of this mainly for capital goods (not for consumer goods). A condition from the socialist countries for playing the game was, of course, so level of access for their products on First World markets. As seen by the trade balances the latter did not offset the former.

The second threat to the system was the Third world, by and large decolonized countries. The story is very much the same: it may have looked as if both the supply of production factors and the availability of markets would disappear or be seriously curtailed. However, more or less "joint" production took care of the first challenge; wants were increasingly made compatible with First World supply structure. The buying power of the elites increased dramatically, that of the people, however, lagging equally dramatically behind. Some production took place, entry into First World markets was demanded and, kicking and screaming, in some cases granted. As seen by the trade balances the latter certainly did not offset the former.

The third threat to the system was the OPEC action which had a much simpler structure. They simply increased dramatically, the price of a product supplied by them, not changing the quality, knowing that the demand would still be there because First World buying power was and is very high, and - more importantly - because the want is so high that the demand is nearly inelastic within a considerable price range. OPEC, understandably, preferred trade at the higher levels of that range to trade at the

lower levels. As a net result a higher proportion of accumulated capital went into energy procurement and prices of Western products went up. World indebtedness patterns started changing with OPEC countries as the ultimate creditors. On the other hand, their demand was and is for what the First World can supply: their wants are to a large extent First World wants and with their buying power offsetting even considerable price increases they can go for the best quality there is. Again, it may perhaps be said that the threat was successfully absorbed after some panic winter 1973/74 and negative economic growth [the first one since World War II] in 1974.

It is the fourth threat to the system that is the important one because, for the first time, the First World is threatened through competition. Obviously the Japanese approach was product-oriented. They did not create wants and buying power - that is what the First World has done in the Third world through colonialism and neo-colonialism/technical assistance and the Second World has done to itself by accepting so many of the goals of capitalist society. What the Japanese did was to build on existing wants and buying power, and then simply make products that are (1) higher in quality and (2) lower in price. A choice between the better and more expensive on the one hand and the poorer and cheaper on the other is always a difficult one; it becomes a question of trade-off between price and quality. But the choice between the better and less expensive on the one hand and the poorer and more expensive on the other is never difficult for a true homo economicus. To prefer the latter one would have to be (a) a nationalist, (b) a masochist and/or (c) badly informed. The Japanese and their successors [mini-Japans, the pre-Chinese, the Chinese themselves when they enter the scene] make use of advertising to improve information, assume that First World citizens are not very good at masochism in economic affairs, but will run into dif-

ficulties with nationalism. However, what they have obtained is significant enough: demand is shifted towards their products because of higher quality per price unit, for a wide range of products. If this is the case in the First World it should be a fortiori the case in the Fourth World from where the products come: why should they buy First World products if their own are better? Whether it also holds in Third World and Second World countries is another question: in both parts of the world the First World has been the major reference group and hence major outside supplier as major oppressor and major enemy. But this also works against them in the Third World because there may be a scepticism against the former colonial masters - and Japan was that only for a short period and only for a small part of the world. The Second World may be the part of the world where quality is so inextricably associated with First World origin that it will still take time for higher levels of economic rationality to emerge. This is not a stable protection for the First World, however, being based (in my view) on the third category above: the Second world is simply badly informed.

So, there is a crisis - not in capitalism but in First World capitalism because it is beaten on a broad front, and in its own game. How that was possible for Japan is outside the scope of the very simple paradigm used here. It may also well be that it will not last very long. If buying power goes down in the First World as a result of the crisis the price will have to be decreased even further for demand to remain stable. Knowing that this is price to the consumer some of that can be obtained through artificially low values of the yen (adding to artificially high values of the dollar). But price decrease beyond that may play into the hands of Japan's competitors in the Fourth World: mini-Japans and so on. In short, Japan may be outcompeted by her own wake.



However, with more Fourth World suppliers on line to perform the same "miracle" [it is actually only a miracle because the First World has this tendency to see itself as unbeatable] the crisis has probably come to stay, as a consequence of the major social institution of the First World on the world level, in addition to war: free trade [or more precisely, free flow of production factors and products]. A second look at that institution is now taking place and may lead to the First World closing itself to Japanese products through tariff and non-tariff barriers; feeling there is little to lose the trade balance being so negative as it is. This will almost definitely lead to chain effects. Efforts to have Second, Third and Fourth World countries do the same will backfire: Japan will double her efforts to get into these countries, and at the expense of the First World. The First World in general, and the US in particular, may retaliate by refusing to import from these countries - thus dividing the world into two trade zones; the First World and the Rest. This is actually my long run prediction.

But before that the First World have much work to do with the seven strategies given above. Two major strategy combinations stand out:

#### I. MAINSTREAM STRATEGY

It is based on competition on the world market in order to win back lost positions, and seems to focus almost only one one of the four ways of increasing the demand for own products: cutting the price, "in order to become more competitive". Since it is the price to the buyer that counts this is a question of cutting down on production costs [capital - frozen or liquid, labor, raw materials, research, administration] and/or distribution costs [transportation, insurance, storage] and/or profit margin [at all points in the economic chain]. As First World societies

are capitalist societies one would expect most imagination to be steered in the direction of cutting down labor costs, by dismissal or freezing/cutting salaries and/or by relocation to places where lower wages are not cancelled by lower productivity. There should be many other places to start cutting, eg on the particular type of profit margin to the state known as taxes.

However, it is probably assumed that a decrease in the supply side (to the world market) will have to take place at the same time, at least as a transitional measure, and this can be obtained by decreasing the amount of work ( $N \times H$ ) done. At the same time productivity is to be increased, compensating or not for the decline in work. But this means more research and capital, in general, to be bought at a certain cost which may or may not be lower than the price of the work. Raised as this approach is - to become more competitive through lower unit price by less labor - one may suspect that it is in great part a rationalization of the decrease of number of workers (conservative version) or decrease of number of working hours (social democratic version) engaged in to avoid over-production anyhow. However that may be it is, of course, doubtful, whether this approach will make First World products competitive in quality [for the same price] with Japanese products and in price [for the same quakity] with other Fourth World products.

## II. COUNTERTREND STRATEGY

If the above are the typical blue (liberal/capitalist) and red (marxist/socialist) approaches, then the countertrend strategy indicated below is the typical green strategy. It is not based on competition on the world market [except for some select products], but rather on withdrawal into regional, national and local self-reliance -- a complex concept involving <sup>(at least crisis)</sup> a mix of self-sufficiency in essentials and equitable exchange beyond that. In

the terms of the present exercise this would mean a new type of reciprocity: not "I trade with you and you with me/I buy from you on the condition that you buy from me" to "I help you to become self-reliant and you help me". Reciprocity is not given up, but world trade would - if this were carried out - be at a (much) lower level.

The strategy would then assume that if one exports less one also has to import less. If there still is a demand it will have to be met by internal supply, in other words by producing new products - in principle compensating, through import-substitution, for the export-substitution/reduction. In addition to this there would be another major element in the strategy: to decrease the productivity so as to permit high levels of workers and working hours. In practice this would mean labor-intensive rather than (or in addition to) capital-intensive production, and creativity-intensive rather than research-intensive production. In the latter there is, of course, also creativity - but it is frozen into the production process through standardization and is only the creativity of a very limited number of people. In other words a move towards artisinal rather than industrial type production.

Looking at these two approaches there seem to be two major dividing lines:

- [A] domination vs withdrawal in the world market
- [B] high vs low level of productivity

For a civilization, the occidental one, in its expansion mode so used to dominate the world and to have patterns of production that give leading roles to those who can supply capital, research and administration whereby high productivity can be obtained the mainstream strategy is precisely that, a mainstream strategy. And the countertrend strategy becomes precisely that - a countertrend. The rest is fight, struggle, politics - not economics.