Neo-liberalism and the Diffusion of Development*

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The level of economic activity under capitalism is subject to prolonged ebbs and flows. When the economy is on an upswing, this very fact acts as an elixir that emboldens capitalists, who begin to expect that the "good times" are going to continue; this makes them less worried about taking risks, more "adventurous", and hence more prone to taking "bolder" decisions in their asset preference. And because of this they also undertake investment in physical assets like construction, equipment and machinery which makes the boom continue, and thereby justifies their euphoria.

The opposite happens when there is a downturn. It introduces a gloomy outlook among the capitalists; they become more acutely conscious of risks, become scared in their asset preference, and curtail their investment, preferring to hold money instead which is a riskless asset (though it earns nothing). This very fact in turn makes the slump prolonged, and thereby justifies their fear of taking risks.

This very obvious feature of capitalism, namely the self-sustaining euphoria associated with a boom and the self-sustaining gloom associated with a slump, has a bearing on the issue of diffusion of development to the third world. We are talking here of diffusion that spontaneously occurs through the working of unfettered capitalism of the sort that neo-liberalism typifies, not diffusion brought about through deliberate third world State action involving protectionism and such like.

For capital, whether of the metropolis or of the third world, the latter constitutes a site of greater risk. The metropolis is the home base of capitalism and capitalists of all description, whatever the colour of their skin, feel safer there than even in their own countries (which is why there is so much of siphoning of funds from the third world by its own capitalists). In a boom however, which is a period of euphoria, the risk of holding third world assets gets underestimated. The euphoria of a boom extends to the realm of asset preference where not only is greater investment in general undertaken by capital (rather than its holding on to the barren but riskless asset, money), but even third world assets are demanded to a greater extent. The differential preference for metropolitan compared to third world assets gets reduced, which, apart from bringing greater direct investment to the third world, also brings greater finance for buying up third world assets. The relative price of third world assets compared to metropolitan assets increases; or, put differently, for any given price of metropolitan assets, the price of third world assets rises, which increases the production of such assets (i.e. increases investment) and hence raises the growth rate in the third world.

Exactly the opposite happens in a world economic recession. As capitalists become more risk-averse, not only do direct investment flows to the third world dry up (which may be further aggravated by protectionism in the metropolis of the sort that Trump is introducing), but finance capital too stops coming to the third world; indeed there develops a tendency for finance, whether originating in the metropolis or even within the third world, to move towards the metropolis. The relative price of third world assets compared to those from the metropolis drops which further chokes off local investment, causing a fall in the third world growth rate.

The foregoing has two implications. The first, which is fairly indubitable is that booms in world capitalism in conditions of neo-liberalism are associated with higher growth rates in the third world, while slumps in world capitalism have the opposite effect. The second implication which is stronger is that the fluctuations in growth rates in the third world are greater than the fluctuations in the growth rates in the metropolis, since the impact of risk-aversion on investment falls even more heavily on the third world than on the metropolis, with third world asset prices relative to metropolitan asset prices also fluctuating. In short, euphoria or gloom in world capitalism has an even greater impact on the third world than on the metropolis in conditions of neo-liberalism.

What this means is that the very "pundits" who were lauding the higher growth in the third world compared to its own past during the boom years of neo-liberalism, and employing such growth as evidence of the beneficial effects of neo-liberalism (conveniently forgetting even at that time that a process of primitive accumulation of capital was being unleashed against peasants and petty producers, which swelled the labour reserves to the detriment all working people including even the unionized workers of the organized sector), will now have to eat their words. As the world capitalist recession continues and even gets accentuated, as finance begins to flow back increasingly to the metropolis as is already happening (resulting in a depreciation of several third world currencies, including above all the rupee, vis-à-vis the U.S. dollar), investment and growth rate in the third world will dry up to an even greater extent than in the metropolis.

Since there is no end to the capitalist recession in sight, and since protectionism as is being practiced by Trump will only worsen the world crisis by intensifying the gloom about the future (even though the U.S. may temporarily gain from this "beggar-my-neighbour" policy, only until others retaliate), the particularly acute distress of the third world that this recession brings with it, will also be a prolonged phenomenon. The third world in short is sinking into a prolonged period of stagnation. This will bring acute distress to the working people, since the primitive accumulation of capital at the expense of the peasants and petty producers that had accompanied the capitalist boom, will continue unabated, while stagnation will only further reduce employment generation within the capitalist sector.

The hype about the diffusion of development to the third world in short will soon disappear. This is not the first time that such a reversal is happening. In the late nineteenth and early twentieth centuries, during the late Victorian and Edwardian booms, there was also a hype about the diffusion of development to the third world. But many of the third world countries which were among the fastest growers of that time are today being counted as the world's "least developed" countries, Myanmar being a classic example. To be sure, the diffusion of development to the third world during the capitalist boom of the recent neo-liberal period has been more pronounced than earlier; and Myanmar's fortune was tied to its oil resources whose exhaustion spelled its doom. But the point is that the phenomenon of yesterday's champions being tomorrow's laggards is by no means uncommon.

The Great Depression of the 1930s had followed the collapse of the long Victorian and Edwardian boom, and during the Depression only those third world countries had flourished which had managed to delink themselves from the web of unfettered world capitalism by imposing controls over trade and capital flows. Notable among these were the Latin American countries that had embarked on a “nationalist strategy” of import-substituting industrialization after overthrowing the local oligarchies that had been in cahoots with imperialism. Colonized economies like India, by contrast, though they did see some industrialization since even the colonial regime had to introduce a meagre amount of what was called “discriminating protection” to appease the local bourgeoisie, did not see enough of it.

We are once more entering a period of significant political upheavals and economic changes within the world capitalist system, as a consequence of the crisis whose impact on the third world, as suggested above, will be particularly acute.

One thing however is indubitable. An impression had been created of late that the third world can overcome its economic misery even while remaining within the orbit of world capitalism, that neo-liberalism was giving rise to a diffusion of development to the third world from the metropolis which was so pronounced that the earlier argument about socialism alone creating conditions for overcoming the third world’s economic travails, had become passé; and even if some residual poverty remained within the third world despite rapid growth, it was only a matter of time before that too would disappear through a “trickle down” of growth. Capitalism in short was the panacea for mass poverty in the third world and not its progenitor as the Marxists had been arguing. The crisis that is enveloping the third world economies at present, is putting an end to that claim.

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