The Road out of Crisis and the Policy Choices Facing Russia

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Abstract

This paper was presented to the May 2013 conference of the PostGLobalization Initiative (http://pglobal.org/) in response to a request from the organizers to present suggestions for the policies required to get out of the economic crisis which opened in 2007, and their implications for the Russian economy and government.

Drawing on materials from the 'Key Trends in Globalization' website (http://ablog.typepad.com/), the paper analyzes growth in four types of country typified by the EU, the USA, India, and China. The fastest growth has been registered in China, which has followed a policy of expansionary money with strong banking controls, combined with an investment-led stimulus. Strong growth has also however been registered by countries that apply a subset of these policies, for example India, which has strong capital controls and a significant – and frequently understated – state presence in the economy. Growth is also weakest in those countries, such as the EU economies and Britain, where governments and banks specifically rule out and impede both the expansion of government spending, and state investment of any shape or form.

The paper shows that it is these economic policies that produce growth, and neither some special characteristics unique to particular countries, such as their political systems or wage régimes, nor some pre-ordained new hegemonic order which decrees that the BRICS must rise because it simply happens to be their turn. Least of all can economic success be attributed to the adoption of neoliberal market policies.

The specific combinations that brings the most growth invariably involve direct public involvement in investment, whose collapse is the primary and most deep-seated underlying cause of the present protracted crisis. Particularly effective – and, the paper argues, essential in the medium to long term – are policies oriented towards human development. These produce an immediate increase in consumer demand as illustrated by the effect of Brazil's poverty-elimination policies; most decisively, however, they make possible the consolidation of the resultant surge in consumer demand, whose effect will be shortlived if unaccompanied by developmental measures, on the basis of a parallel and stable increase in investment demand and productive capacity – which requires bringing into being the type of workforce that is required to make use of leading-edge technology. On the other hand, industrial development in the modern economy depends critically on human development, precisely because of modern technology, which is ever more dependent on the specifically human contribution of skilled and creative labour. Human and industrial development, in the modern world, therefore march hand in hand.

Such policies, contrary to established neoliberal dogma, require the direct involvement of the national state in both human and industrial development. Any country can develop such policies – taking into account national specificities of course – whether or not it shares China's particularities.

Policies of this type are particularly relevant to countries such as Russia and South Africa which run the risk, in an era of resource shortage accompanied by wild fluctuations of commodity prices, of subordination to a narrow, destructive and unstable development of their extractive industries, leaving them at the mercy of countries which retain command of the production of high-tech goods.

Such policies will succeed all the more, to the extent that those countries who are carrying them out co-ordinate with each other on the basis of mutual justice and equality, to establish financial, material, and trading institutions that afford genuine economic independence.

The decisive reason that such independent national policies are required is that the crisis, above all in the so-called 'advanced' economies – better now named the 'no-longer-developing' or NLD economies – has deep-seated origins in the long-run fall in the rate of profit, and no immediate or automatic recovery can be expected. This has led to a rise in parasitic sectors rooted in extractivist and financial capital, which have shown themselves capable of inflicting great damage on developing economies, if not prevented from so doing.

The paper finishes with an evaluation of the specific policies best suited to the BRICS and more generally 'Southern' or emerging economies, arguing for a policy of 'combined development' focused on developing and applying the most advanced technologies available in the world today, combined with an industrial policy whose centre is human development – forging and nurturing a talented and creative workforce with the high levels of education and skills required to make modern technology effective - instead of passing through some mythical 'stage of development' requiring a focus on mineral wealth or low wages.

JEL codes: O1, O10, N0

Keywords: Crisis; Development; Growth; Inequality; State; Culture; Environment; Technology; Creativity; investment' BRICS; Russia

The Road out of Crisis and the Policy Choices Facing Russia

Alan Freeman, Moscow, May 2 2013

Introduction

Getting out of the crisis is a very practical question. It is about what to do next. I will of course talk about long-term strategic issues – because without a sensible strategy, you can't produce sensible tactics. However at this time in the evolution of the world's geopolitical economy, you can't stop at strategic analysis.

The neoliberals have always had a crazy strategy; now, perhaps for the first time for a long while, their tactics are not working either. Previously, they could mobilize a sufficient base of support, and commanded sufficient resources to neutralize the opposition, that they were able for many years when the inadequacy of their remedies were clearly visible, to get away with doing some very stupid things. Now, they are in such a mess, that this is ceasing to work. There is a generalized crisis of *governance* in the world. Those of us with a more sensible strategy therefore have a responsibility: we have to be clear about what to do next. So I am going to outline some practical steps that may help get Russia out of crisis or, to be more precise, *keep* it out of crisis and launch it on a sustainable path of economic development that will shield it fully from the storms to come.

Getting out of the crisis requires action; that means government action which means state spending, and that means state investment

Getting out of the crisis is not just a pipe-dream. In fact, the crisis has polarized the world between those countries who just keep taking the neoliberal medicine, which are in the biggest mess (the UK, now entering its fifth successive year of economic decline, is the outstanding example) and those that have rejected neoliberal remedies and have applied a state stimulus coupled with strong financial and capital controls. Most notable is China, where there have now been three decades of straight growth. The neoliberals love to disguise the fundamental fact that, above all in crisis, the state is required to create economic growth: they constantly invent reasons for facts that directly contradict their main theses: the successful countries have 'cheap labour', or they are part of an 'Asian Miracle', they are 'dictatorships' or even that they are caused by 'globalization'.

If cheap labour was enough, why isn't most of central Africa a big success story – and why is the standard of living in China growing faster than almost anywhere else in the world? If 'dictatorship' is the cause of growth why are countries like India, for all their weaknesses, pulling away from the West in terms of their growth rates? If this is just an 'Asian' miracle, how do we account for the improvement in Brazil's economy and several others that have adopted similar policies?

As for 'globalisation' as Radhika Desai has ably explained, this is not an economic fact but a *policy,* made in the USA and imposed for years by bodies like the IMF and the World Bank, which proposes that countries should remove the state from the economy, sell off all their public industries to foreign multinationals, and abolish controls on finance and the movement of capital. Those countries that have adopted these policies have suffered catastrophic declines in GDP, starting with the former countries of the USSR and Eastern Europe when they adopted shock therapy. Those countries, such as China, which entered the WTO in order to *trade* with the world, but did not adopt all the other prescriptions of globalization, have seen a completely different pattern of growth.

These myths, therefore, are put about to conceal two simple economic facts: the more the state gets involved in the economy, the less dramatic the effects of the crisis, and the more the state *invests,* the greater the prospects for real growth. Of course this basic fact has to be qualified in many ways, which I will discuss in this paper. It has to invest in the right place, and in the right way. It's far more effective if it is done democratically, and investment has to go hand in hand with raising the standard of living of the population, and reducing inequality. Also, countries which are under virtual siege from the USA or European powers, up to and including constant military incursions, destabilization and sanctions which are, in fact, simply a kind of economic warfare, will obviously suffer deep distortions to their economy which, if they are prevented from defending themselves adequately, can throw the economy off course. But these are *additional* factors, which do nothing to alter the fundamental economic facts. I now turn to these.

First, in all those countries where the state is acting to counter the crisis, the economy has been doing relatively better; second, wherever the state has provided an *investment* stimulus, the country has been doing a lot better. Table 1 shows this for three of the largest economic regions of the world. There are now many places where you can find charts, country by country, which illustrate this same basic point. Where the state intervenes in the economy, the economy – above all since the crisis broke out – has done better. This is a simple basic fact of economic life

TABLE 1: RELATION BETWEEN ECONOMIC POLICY AND GROWTH

Region/ Country	Policy applied	Growth
EU	Loose money, few banking controls, no stimulus	-2% over last 4 years
US	Loose money, few banking controls, consumer stimulus	1.2% over last 4 years
China	Expansionary money with strong banking controls, investment-led stimulus	9% over last 4 years
India	Strong state banking controls, consumer stimulus	9.4% in 2010 falling to 5.3% in 2012

Source: Key Trends in Globalization website

This does not mean, of course, that any and all state action will help to rebuild the economy. The state has to choose the actions that work the best. In table 1, we see a key distinction at work, between those countries that have confined themselves to a consumer stimulus – which, of course vital since without it, the economy will not generate the consumer demand it needs to sell its products – and those countries that have additionally applied an investment stimulus – where the government and the state directly become involved in production, above all new production. This is the real key to the kind of economic growth that 'gets a country out of the crisis' instead of simply weathering it, which is what is happening in the USA.

This is a long-term, deep, structural crisis, and will not put itself right

The same pundits who will offer you every explanation under the sun to avoid recognizing that the state is critical to restoring growth, will also offer every explanation under the sun, moon and stars to avoid recognizing the cause of the crisis, namely, capitalism. The religious character of modern economic theory, which I will speak about at the first session of this conference, is organized around the theory of 'equilibrium'. This theory states, in effect, that the capitalist economy has a natural, harmonious state to which it will always revert, and that all movement away from that state is either a temporary 'adjustment' or the result of some external act: bad bank management, workers demanding wages that are too high, or, best of all, the state messing things up.

With every year that passes, these explanations become harder to sustain. I will illustrate this by looking at the biggest and probably most market-driven of all countries, the USA.I focus on five charts illustrating the long-term character of the decline in the US economy. Chart 1 shows that this crisis is very different, and much more marked, than the previous four recessions. Chart 2 reinforces this point and also shows that in successive cycles since the 1960s, overall growth during the cycle has been steadily shrinking. Particularly if one remembers that the 1946 'blip' was basically caused by demobilization – and rapidly rebounded – it shows that US growth in the crisis has been worse than at any time since the Great Depression. It shows moreover that the great 'US miracle boom' after the year 2000 is a complete myth: growth over that cycle, trough to trough, was the lowest ever, and even at the peak of that cycle, growth did not attain the level of *any* previous peak.

Charts 3 and 4 explore this in relation to two of the key indicators of any economy's health: employment and capacity. Capacity utilization has been on a systematic downward trend since the end of the 1960s and reached its lowest ever just before the crisis broke. As regards employment, around which there is such a myth-making industry among western economists that it is a source of stimulus in its own right, the critical point is the rise of *long-term* unemployment, the red line in chart 5. Long-run unemployment is the surest sign of a structural, deep-seated crisis.

CHART 1

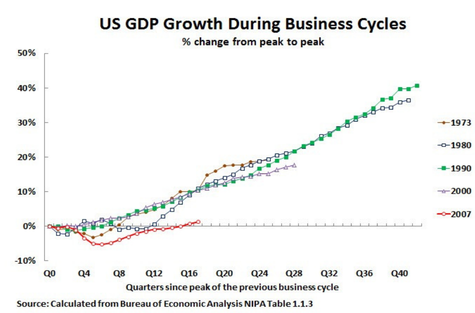


CHART 2

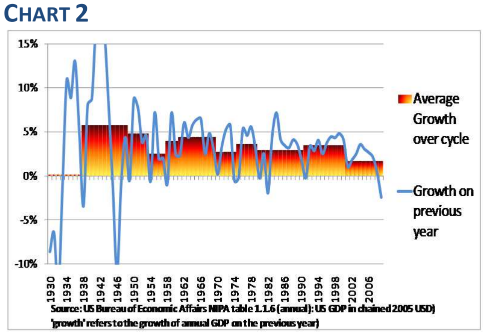


CHART 3

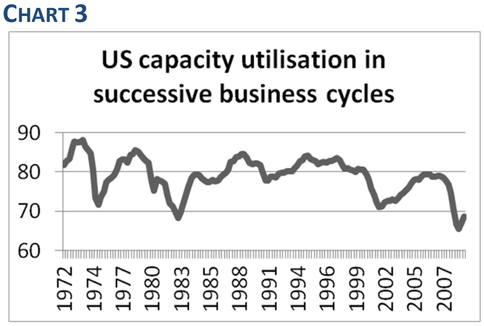
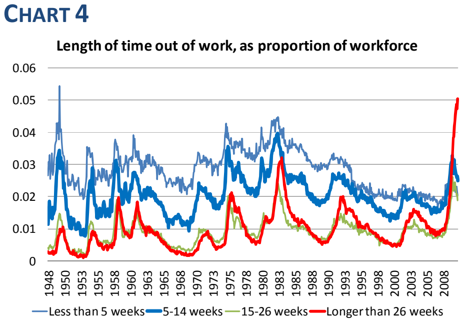


CHART 4



Behind all of this lies a very long-term trend in capitalism, which is widely associated with Marx but which in fact is to be found in the work of most of the classical economists and also Keynes, which is its tendency after a boom to sink towards a 'stationary state' – in fact, a state of prolonged stagnation which we call 'Depression'. Several factors are at work in producing such depressions and there are several explanations for them; I have my own view, supported by much evidence, shown in charts 5 and 6, that the underlying cause at least of the US and UK recessions is the decline in the rate of profit in those countries.

However, I want to stress that in order to understand this crisis, it is not essential to agree with that view. What is essential is to recognize that:

(1) the crisis is deep and structural,
(2) it is the result of long-term factors,
(3) that these factors are inherent in the nature of the capitalist economy

CHART 5

US Profit rate, corrected for financial capital

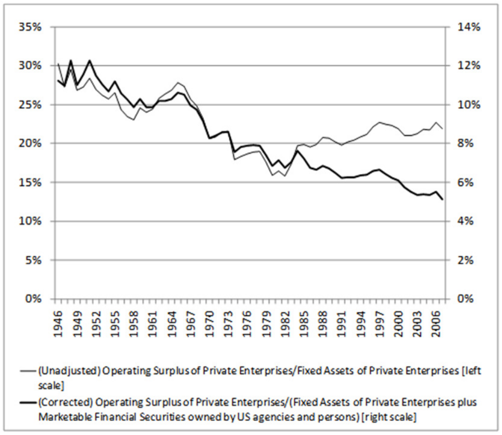
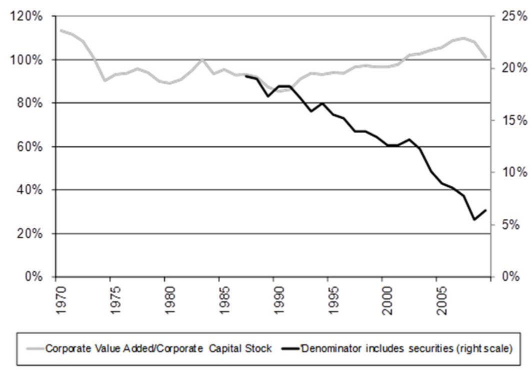


CHART 6

UK Profit rate, corrected for financial capital



The trillion-dollar question is then 'can capitalism extract itself from such a structural crisis?' This is a hotly-debated question, and the debate started here in Russia with the work of Kondratieff and the Conjunctural Institute. The foremost proponent of self-restoration was Schumpeter, who developed an extended theory of 'long cycles' based on Kondratieff's statistical work. Schumpeter, and also Kondratieff to a lesser extent, firmly believed that these long cycles were *periodic*, of the same nature as the ordinary business cycle – sometimes they would go up, some times they would go down, and always, after a down there would come an up, and after an up would come a down.

Of course, there is some statistical evidence to support this. Not least, there is the very important fact that in each previous 'Long Depression' capitalism did in fact get out of crisis. After the 'long Depression' of the 1870s there came a quite long period of rapid growth normally called the *Belle Epoque*, and after the 1929 Depression came the postwar golden age.

But before we ascribe miraculous powers of self-healing to the capitalist economy, the most important question to ask is *how* they got out of these crises. And the answer is – absolutely massive state intervention.

CHART 7

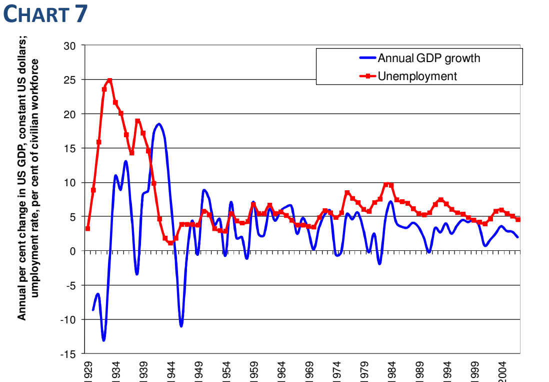
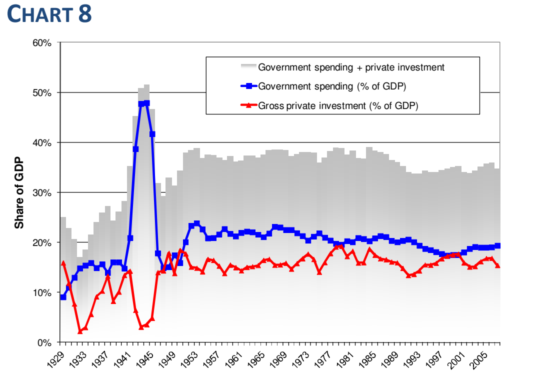


CHART 8



Source: US Bureau of Economic Analysis, author's calculations.

In 2008 I wrote a very short paper (http://www.academia.edu/171968/How_much_is_enough), which was also registered in February 2009 at the www.repec.org open access site, so you can verify I didn't just come up with this yesterday. In it I looked at what the USA did to get out of the last Depression. The most basic point is that this did not happen with the New Deal, as many people think. It came with the War. Take a look at chart 8. During the war, the state's expenditure grew to *forty-eight percent* of GDP. The state in fact virtually displaced private capital as the source of funding for investment. Moreover, there is strong evidence that economic recovery began first in Germany and Japan, as they embarked on their preparations for war.

Now look back in time and ask yourself: what was going on in 1893, which is when the recovery from the previous long depression began? The answer is blindingly obvious: the industrialized countries were embarking on the biggest programme of military spending and activity in their history, populating the whole world with their armies, and finally provoking World War I and indeed, the Russian revolution. This is not 'self-restoration'. The reason the economists pass over this is their strange view that somehow war is not part of capitalism, that it is like when rain interrupts a tennis match, so that what happens during it doesn't really count.

These facts, and the length of the present crisis, dispel the myth of 'self-restoration': the idea that the economy can put itself together. In fact the exit from all previous such crises of this size was a big expansion in state spending, the most recent being the postwar expansion of the USA, Germany and Japan. A much higher level of state involvement was maintained after the war with the welfare states of the 'North' and the developmental states of the 'South' and in fact, every time this is weakened, the crisis gets worse.

Now, does this mean that in order to get out of the present crisis, we need another war? Hopefully not. It does however suggest that unless we find a different way out of it – which will involve spending as much through the state on peaceful growth, as was previously spent on military growth, then a renewed drive towards war by capitalism becomes quite probable.

This way out has to be led by investment

A third set of myths that the economic pundits will tell you is that the state does not work as a vehicle of recovery because 'Keynesianism has been tried'. Keynesian demand management, they will tell you, was tried during the 1970s and all it produced was inflation.

Unfortunately for truth, what was tried was not Keynesianism – just as much of what Marx gets blamed for is not Marxism. Keynes, as Radhika Desai has patiently documented in her book, was fully aware that the simple management of consumer demand would not be sufficient. Of course, unlike Marx, he did not seek to replace capitalism but to restore it; however, being an intelligent economist he understood what that would take. There are two key phrases in his writings which many Keynesians, and all his critics, ignore. First, he calls for the 'socialisation of investment'; and second, for the 'euthanasia of the rentier'. Today that translates into the complete reconstruction of the banking system to its original function of supplying credit for investment, under public direction; and for the state to simply step in wherever the holders of financial assets of any kind are withholding them from investment, and conduct the investment itself.

How it deals with the holders of the assets is entirely a matter of political expediency. There is no golden rule that says they must be expropriated, or that they must be compensated. What matters is that they should be put where they can do no harm and that the priority of national development take priority over any private, fractional concern. The priorities of government and banking have to be entirely, and massively, redirected to fill the gap that not only the rentiers, but even the productive capitalists, are creating as a result of their systematic abstention from investment.

CHART 9

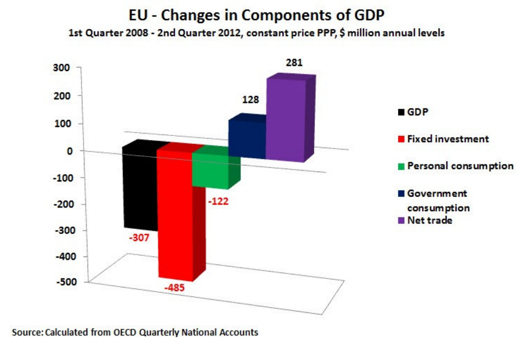


CHART 10

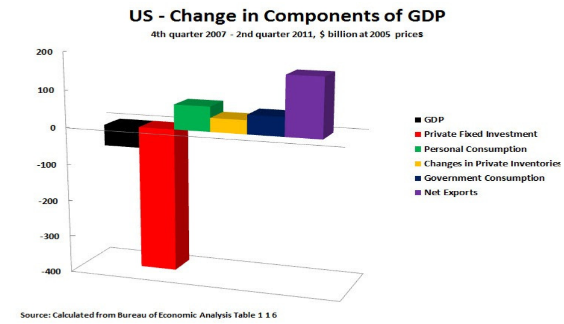
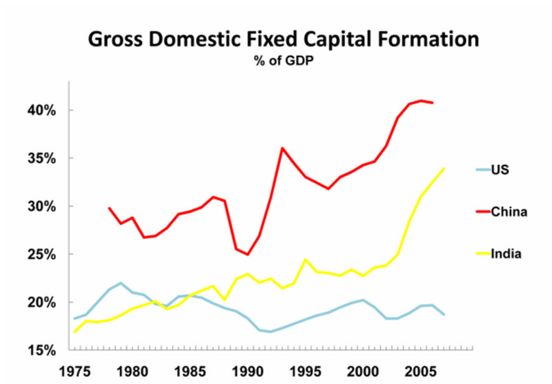


CHART 11



The evidence for this is likewise not hard to find. In fact, the central mechanism of crisis has been a collapse of investment. Charts 9 and 10, from the 'Key Trends in Globalization' website, illustrate this for the European Union and the USA. In the EU, investment has declined more than four times the fall in consumption. In the USA the picture is even more dramatic, since *all* components of GDP are showing positive growth except investment, which completely outweighed the others driving GDP growth negative. In my presentation I will provide up-to-date, country by country evidence of this simple fact. Chart 11 illustrates the stark reality behind the relative performance of the USA on the one hand, where investment has fallen to half the level it had reached even in the stagnant years of the 1970s, and in India and China where it is respectively three and four times the US level. This, not any 'special Asian case', nor 'cheap labour' or 'currency manipulation', much less 'authoritarian governments' is what lies behind the growth rates of these countries.

Against these self-evident facts, the most extraordinary range of doctrinal arguments are deployed. One of the most pernicious is the claim that if the government spends money, it will increase debt. In fact, detailed research into the UK economy by Professor Victoria Chick and statistician Geoff Tily shows that *every* time the UK government increased its spending in a crisis, its debt went down, and every time the government sought to reduce its debt by cutting spending, its debt went up. The reason is very simple: it is that when the government puts money into the economy, economic growth increases and its tax revenue goes up; conversely, if it takes money out, its tax revenue goes down. There is a mountain of empirical evidence to show that provided the government takes care where the money is spent – as any prudent investor must – to ensure that the returns to its tax coffers are greater than the investment, then its debt decreases. This is why, for example, the capitalist economies with the lowest debts – Norway and Sweden – are those with the highest level of government spending.

This has been strongly confirmed by two rather important events in the theoretical sphere. One somewhat comical, but actually quite serious occurrence is that an economics undergraduate has discovered an elementary arithmetical mistake in a 2010 paper by the two eminent neoliberals Reinhart and Rogoff. I recommend that you read this at http://www.businessweek.com/articles/2013-04-16/twitterverse-goes-nuts-over-economists-clash

or in more detail at http://www.washingtonpost.com/blogs/wonkblog/wp/2013/04/16/is-the-best-evidence-for-austerity-based-on-an-excel-spreadsheet-error/.

"Growth in a Time of Debt" (2010) by Reinhart and Rogoff argues that countries' economic growth slows when government debt levels rise, with a break point at debt equal to or exceeding 90 percent of gross domestic product. It is repeatedly cited in the U.S. and elsewhere to justify budget cuts by policymakers and legislators and is one of the most widely-used sources of justification for austerity policies. And it's based on a mistake. "the average real GDP growth rate for countries carrying a public debt-to-GDP ratio of over 90 percent is actually 2.2 percent, not -0.1 percent as as published in Reinhart and Rogoff," authors Herndon, Ash, and Pollin conclude. Now, in 2009 when *Growth in a Time of Debt* was being written, of the 187 countries in the world, 113 had growth rates below 2.2 per cent. So for 60 per cent of the countries of the world, going into debt was – according to Reinhart and Rogoff's own analysis – when corrected by a student – more likely to do good than harm.

A more serious discussion surrounds the somewhat technical question of the IMF's 'multipliers'. Basically, these measure how much 'bang for the buck' a country will get – according to the IMF's estimates – depending on what it invests in. On this I will simply cite Mick Burke's excellent piece in S*ocialist Economic Bulletin* (http://socialisteconomicbulletin.blogspot.ca/2012/10/the-importance-of-debate-on-imfs.html) :

> It is unusual for 'academic' research published by the IMF to find its way into popular media. But this has happened to the latest World Economic Outlook where the IMF deals briefly with the issue of 'multipliers' that is, the economic impact of changes in government spending. The short article has caused an usually high level of commentary among economists and commentators because the data suggests that the multipliers are perhaps more than double the level generally implied by official research and forecasts. Nobel Laureate Paul Krugman has commented that the research shows that, 'the reason for the worsening outlook is that policy makers have gotten the basic economics wrong'. In Britain Chris Giles economic editor of the Financial Times has led a counter-attack by questioning the validity of the research. A string of other commentators have joined the debate on both sides, including a Greek finance minister.
>
> The key point in the IMF research is that the multipliers are much higher than previously thought by leading bodies such as the IMF, OECD and others. 'The main finding, based on data for 28 economies, is that the multipliers used in generating [IMF] growth forecasts have been systematically too low since the start of the Great

> Recession, by 0.4 to 1.2….' Whereas the IMF's (and others) own forecasts implied a multiplier of 0.5, the actual multipliers may be in the range of 0.9 to 1.7…
>
> There is virtually a religious Golden Rule in (semi-) official literature which places the upper limit on all multipliers at 1. A multiplier lower than 1 implies that GDP will be reduced by less than the total change in government spending. Implicitly, the private sector will always respond in the opposite direction, increasing its spending when government reduces its spending, and vice versa.
>
> This is the crux to the whole debate on multipliers. If government spending 'crowds out' private spending then it should be avoided as detrimental to total economic activity. At the same time, it is claimed that 'austerity' measures will not prove damaging as they will be offset by increased private sector activity. This false logic explains why the OBR [the UK's 'Office of Budget Responsibility', a leading architect of austerity – AF] forecast a 20.3% rise in business in the last two years while the actual increase has been 2.5%.

What is at stake here is the following: actually, not only is the evidence – and a growing current of opinion within mainstream economics – swinging towards recognizing that many government multipliers, particular in times of crisis, are greater than 1 and have been underestimated; in fact it is quite widely known and recognized that state *investment* produces the greatest multiplier effect. Indeed, the only argument against this is the poorly-evidenced 'crowding out' thesis, according to which, if the government invests in industry, private capital will withdraw.

But the cause of this crisis is that private investors have withdrawn *anyway*. There is a growing gap between their huge holdings of money and financial instruments, and their investment in new production, for which even quite right-wing central bankers are beginning to berate them. As Burke rightly notes:

> There can be no single multiplier effect. The size of the impact of changes in government spending must depend on firstly on the type of change in government spending. At the same time, even where an increase or decrease in government spending has a very large impact in terms of altering output in other sectors, the impact is not infinite. The size of the impact is itself constrained by the existing capacity of the economy. Therefore the largest multiplier effect can be found where government spending requires the greatest degree of inputs from other sectors (that is, where the division of labour is at its highest level) and which increases the productive capacity of the economy as a whole.
>
> As a result, the overwhelmingly majority of research finds that the greatest multiplier is attached to direct increases in government investment. These are usually held to be much higher than inducements to private sector investment (which may simply be saved and from which profits must be deducted). They are also higher than the multipliers attached to consumption (which does not increase the productive capacity of the economy).

The evidence is mounting. Not merely do those countries that use investment stimulus do systematically better than those who apply austerity, but the *mechanisms* of that improvement are slowly, grudgingly, but inevitably recognized even by some of the most diehard opponents of state intervention.

What does this mean for the BRICS?

How does this pan out in terms of practical policies for BRICS countries, and specifically for Russia and its close partners? The most obvious point is that austerity is the diametric opposite of what is needed and is making the crisis worse everywhere it is applied. I do not know of a single country, in this, the seventh year since the recession began, that has 'restored' its economy or even its exposure to debt, by such measures.

The reason is that austerity is a multiplier in reverse. Taking money out of the economy by reducing state spending is like sawing off the branch of a tree that one is standing on. The reduction in spending destroys jobs and business. The loss of jobs and business takes more money out of the economy. This further destroys jobs and business and eventually, the net result is a loss of tax income that is greater than the size of the cuts. Then more cuts have to be imposed, and the whole process goes down another notch. The conservative government has just announced that austerity will now have to be extended until 2018, having originally claimed it would get rid of the debt within three years.

This is also why the 'debt reduction' programmes being imposed on countries such as Greece, Spain and Portugal simply don't work. Even the IMF is beginning to question the wisdom of trying to get money out of people by putting them out of work.

However, as I noted at the start of this presentation, we see a different side of the coin in many developing countries, most notably those that are following policies of state stimulus and particularly those who are pursuing investment stimuli. Is this a purely BRICS phenomenon? No, because there are countries like Vietnam which are quite small but by means of such policies, are stimulating their growth. However there several good reasons that the BRICS are playing a leading role. The first is an issue I first drew attention to in a book that Boris Kagarlitsky and I published together, back in 2004. There, challenging the thesis of 'globalization' I put forward the argument for 'continentalisation' – both to show that it was the real process taking place, and to show the deleterious effect on countries that didn't recognize its importance.

Tables 2-7 show how 'unequal' are some of the main regions of the world. The rows represent 'quintiles' of population – each represents nations containing about 20% of the population of the region. The numbers in the rows show the ratio between GDP per capita in that quintile and GDP per capita in the bottom quintile. The thing to pay attention to is whether these numbers, in any given year, are far apart or close together. If they are close together – as for the Euro Zone, where the richest 20% were (in 2002) only 1.77 times better off than the poorest – then the region has a high degree of economic integration. It can take advantage of this by beneficial trade, since trade between equals generally does not harm an economy; it can set in place uniform regional measures to take the economy forward, such as European investment plans, regional banking, regional transport policies, and so on. Of course it is the failure of the Europeans to follow through on this by means of genuine fiscal redistribution between the European countries – of the type one sees, for example, between American states, or Canada's provinces – that has made the present crisis additionally acute and provoked the never-ending series of debt explosions.

The key point is that those regions which were doing *best* at that time were those with the greatest economic integration. In the emerging markets, Asia was the best – and economically the most integrated. Followed by Latin America, where the process is now advancing apace. The *worst* off are precisely those regions like Africa which have essentially been forced to abandon any prospect of regional political or economic unity – and the 'Countries in transition' where the dissolution of the economic bloc that was the USSR was utterly catastrophic.

Behind this lie three facts. First, many modern processes of production do require a continental scale to operate. A small nation such as, for example, Cuba or Byelorussia simply does not have the breadth of resources and the sheer quantity and variety of labour to make the variety of products that it needs, without introducing significant inefficiencies. But second, the major economic powers of the world *are already continental* – notably the USA. Therefore, in order to compete on a level playing field with the USA - essential in order to trade with the USA without huge losses through unequal exchange – requires a continental economy. And thirdly, within a regional economy, domestic demand simply constitutes a larger proportion of GDP, so that demand management is a much more practical option.

TABLE 2: DISPERSION OF INEQUALITY BETWEEN THE NATIONS OF THE EURO ZONE

	1970	1975	1980	1985	1990	1995	2000	2001	2002
Q2	1.57	1.31	1.49	1.65	1.48	1.31	1.43	1.40	1.37
Q3	1.76	1.64	1.75	1.74	1.59	1.65	1.58	1.52	1.47
Q4	1.89	1.95	1.96	1.86	1.63	1.93	1.63	1.58	1.54
Q5	2.26	2.33	2.28	2.28	1.91	2.17	1.87	1.80	**1.77**

TABLE 3: DISPERSION OF INEQUALITY BETWEEN THE NATIONS OF ASIA, WITHOUT CHINA

	1970	1975	1980	1985	1990	1995	2000	2001	2002
Q2	1.46	1.06	1.16	1.18	1.42	1.15	1.23	1.27	1.25
Q3	1.47	1.06	1.16	1.18	1.42	1.15	1.23	1.29	1.26
Q4	1.54	1.23	1.73	1.37	1.53	1.52	1.31	1.34	1.35
Q5	2.74	2.16	3.13	2.39	3.16	4.16	2.65	2.50	**2.67**

TABLE 4: DISPERSION OF INEQUALITY BETWEEN THE NATIONS OF LATIN AMERICA

	1970	1975	1980	1985	1990	1995	2000	2001	2002
Q2	1.26	1.44	1.28	1.79	2.38	1.77	2.01	1.73	1.65
Q3	1.42	1.54	1.32	1.93	3.15	2.23	2.29	1.87	1.72
Q4	2.60	2.77	2.94	2.49	3.17	2.61	3.43	3.35	**2.36**
Q5	5.24	3.84	3.95	3.39	3.72	3.45	4.33	4.20	**4.22**

TABLE 5: DISPERSION OF INEQUALITY BETWEEN THE NATIONS OF THE MIDDLE EAST

	1970	1975	1980	1985	1990	1995	2000	2001	2002
Q2	1.24	1.87	2.28	1.28	1.19	1.25	1.06	1.14	1.15
Q3	1.61	2.66	2.95	1.53	1.30	1.58	1.19	1.31	1.43
Q4	2.24	3.48	4.37	1.81	2.10	2.93	2.27	1.64	**2.25**
Q5	5.20	8.71	17.82	6.37	5.02	7.78	6.79	6.48	**6.94**

TABLE 6: DISPERSION OF INEQUALITY BETWEEN THE NATIONS OF THE COUNTRIES IN TRANSITION

	1970	1975	1980	1985	1990	1995	2000	2001	2002
Q2	1.70	1.48	1.57	1.51	1.75	2.27	2.02	2.16	2.39
Q3	2.19	2.29	2.47	2.81	3.78	4.87	3.37	3.75	**4.23**
Q4	2.31	2.58	2.81	3.20	4.29	5.27	3.42	3.89	**4.37**
Q5	2.36	2.61	2.84	3.23	4.33	8.46	8.01	8.40	**9.38**

TABLE 7: DISPERSION OF INEQUALITY BETWEEN THE NATIONS OF AFRICA

	1970	1975	1980	1985	1990	1995	2000	2001	2002
Q2	1.85	2.24	1.94	1.47	1.50	1.79	2.24	2.16	2.30
Q3	2.15	3.35	3.12	2.02	1.82	2.24	3.15	3.07	**3.12**
Q4	3.53	4.13	4.67	2.76	3.94	3.80	4.08	3.99	**4.22**
Q5	9.48	9.89	10.23	8.85	10.61	18.24	18.61	17.04	**17.63**

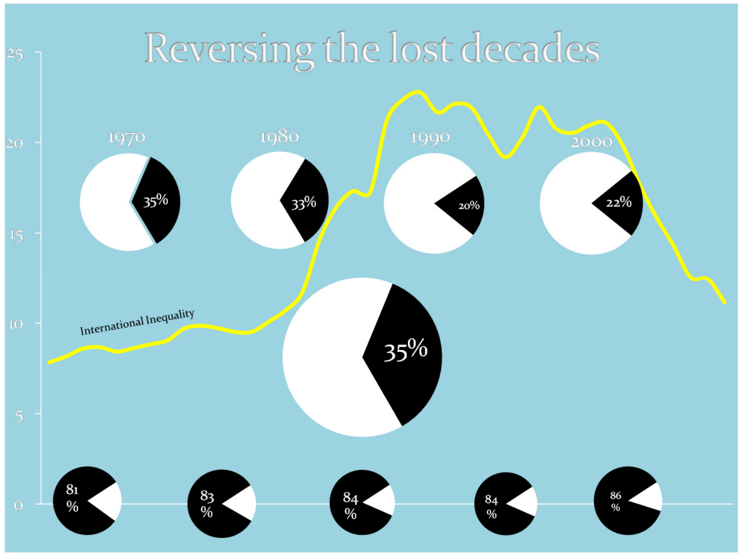
How can this assist Russia? First of all, the Russian economy is itself continental in scale – but not in scope. It is narrowly focused on a small number of products, most dangerously on mineral resources. I have not studied recent Russian data in detail, but I would venture that it is probably the least diversified of the continental BRIC economies. Moreover in the wake of shock therapy it lost ground in a number of key industries where it had a real technological lead – something about which many big European conglomerates were particularly happy since it placed Russian markets at their disposition. Therefore, diversification is an absolutely logical strategy for Russia, whereas many smaller countries have little choice but to focus on certain specializations, and obtain the remainder of their needs in trade.

One part of the true logic of the BRICS, over and beyond the growing of the state in their economies is in fact the realization of such continental advantages. It is, in effect, a group composed of the continental power of China, the subcontinental power of India, the emerging Latin American continent, and the latent economic continent of the Russian landmass and its surrounds. This is one reason why, whatever this audience thinks of its politics, the USSR was a completely logical economic structure. It is why breaking up the USSR was so important a goal of the western powers – after all, if the only thing they wanted was capitalism, why not keep it together but turn it into a capitalist union instead of a socialist one? They understood full well, the cant about globalization notwithstanding, to substantially weaken the USSR by breaking it up. And in fact everywhere the advanced powers intervene either economically, politically or militarily, a major part of their agenda is to bring about the breakup of viable economic units, substituting smaller and smaller entities less and less capable of competing with their own, highly-integrated producers.

Second, I think it will help understanding about the choices facing Russia to grasp that the newly-emerging inter-continental and multipolar world is also a tremendous potential source of functional economic partnerships. The economies of Russia, China, India and Latin America are far more complementary than those of, say, Russia and Europe. By leveraging the benefits of economic co-operation on a South-South basis, the efficiency gains of continentalisation can be maximized.

This notion of economic partnership runs completely counter to the false complementarity offered by the IMF in its almost nakedly colonial notion that the industrial countries should supply 'capital' and the rest of the world should supply 'labour' and resources. A fifth great myth which has been spread under the *aegis* of 'globalization' is that the poor nations do not require advanced industrial or hi-tech products, because they obtain them from the West through trade. Since these hi-tech products are precisely what is required to produce efficiently enough to stand up in world markets, this is a fairly blatant attempt to reduce the 'developing countries' to the status of a permanent hinterland of the rich countries. This, in fact, is what happened during the 'lost decades' of neoliberal policies, as is shown in chart 12. This chart calculates an 'inequality index'; it is the ratio between the average GDP per capita of the first world as a whole, and that of the third world, as a whole. During the neoliberal years this increased to its highest ever level in world history, in fact *doubling* between 1980 and 1990. The ground is now being recovered – not by 'globalisation' but as a consequence of the internal collapse of the globalizing project, and the considerable policy space that the third world has acquired by throwing off its chains and taking their own destinies back into the hands of their own states.

CHART 12: INTERNATIONAL INEQUALITY UNDER 'GLOBALISATION' AND AFTER



What development policies?

The most difficult practical question is, of course, in what to invest? The details of any counter-crisis development plan have to be devised by the people of the country in question since only they have the detailed practical knowledge and will live with the consequences. However there are a number of important guidelines that I think can be deduced from the general level of the world's productive forces and which I'd like to share with you.

We have already noted that the 'great expansions' of 1893 and 1942 were launched, in the industrialized capitalist world, essentially in a giant outburst of military spending. This brought with it, of course, a general development of the productive forces: in order to build warships, Europe needed steel, fuel, modern machinery, and all the prerequisites of the modern resource-based economy. Similarly the USA's ramping up of its wartime apparatus bequeathed, to the private owners into whose hands it soon devolved at rock-bottom prices, levels of productivity in the new emerging industries of oil, electricity and transport which allowed it to command a devastated postwar economy for over a decade. Not least, it came out with nuclear power.

The point of this is not, of course, that a new militarization is the road to a new expansion. It is that a very large scale investment is most effective when it *advances the productive forces* – when the investment in new technologies begets further investment in capacity, creating new spheres of demand and new products, in the economically virtuous circle that created, for example, the 'car and gadget' economy of the postwar US.

Two problems now arise. Their solution is complementary. On the one hand, a further expansion which simply uses up natural resources just isn't going to work. Even if climate change is overcome, there remains the far more fundamental fact, as Mark Swilling and his colleagues at Stellenbosch University have noted, that the resources of the planet are simply running out. We are actually pushing the limits of the amount of materials we can extract from the earth's crust.

CHART 12: PROPORTION OF EMPLOYEES IN SERVICE INDUSTRIES, ADVANCED COUNTRIES

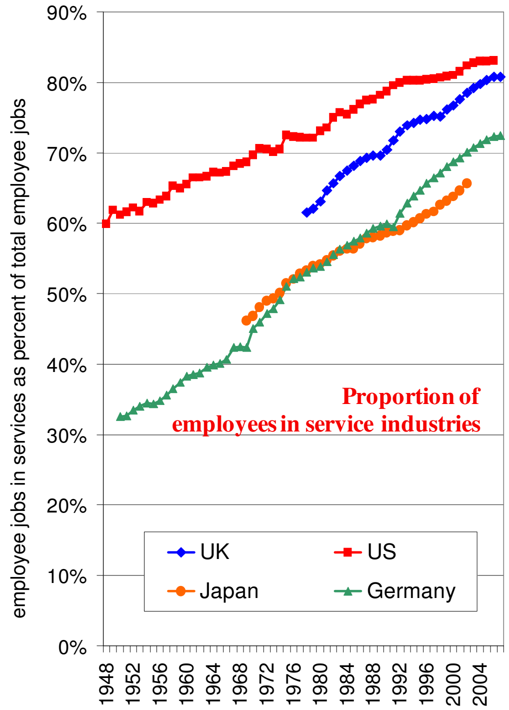
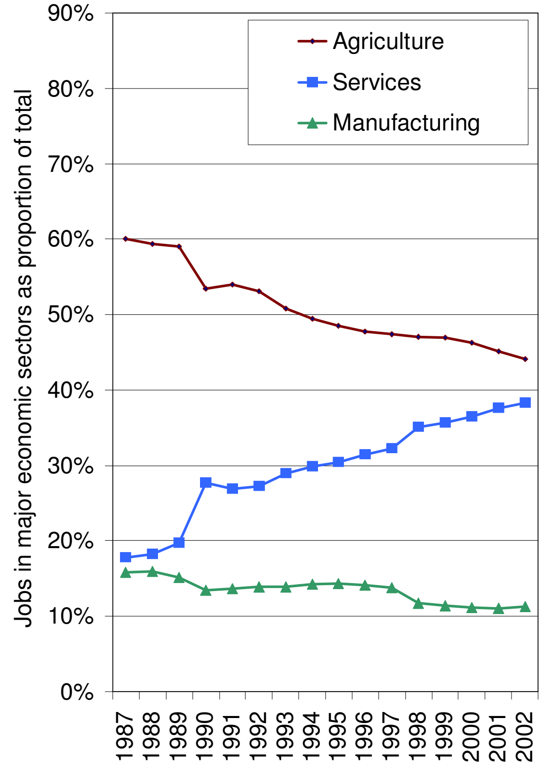


CHART 13: PROPORTION OF EMPLOYEES IN MAJOR SECTORS, CHINA



But secondly – and this applies most critically to the advanced countries – there is actually no room within the economy to develop new technologies that increase *material* productivity – that simply produce more 'things'. In a development that has slowly crept up, without economists really paying proper attention, the production of *services* – that is to say, interaction between humans, has become the principal economic activity of human beings.

Chart 13 shows that, in the advanced countries, service labour accounts for over 75 per cent of all labour – in the USA, an even higher percentage. Chart 14 shows that this trend is not confined to the advanced countries. Service labour now accounts for nearly 50 per cent of the Chinese economy and, astonishingly, manufacturing labour is actually declining. In a classic of 'combined development' China is leapfrogging the slow grind of 'industrialising' its workforce, positioning itself with modern technology to move directly into the markets for services that are beginning to dominate most high value-added production in the world market. It is a long way from attaining Western levels in average productivity, of course. But that is no obstacle to seeking, acquiring and capturing leads in such crucial sectors as high-end electronics.

These two 'problems' provide the solution to each other, at least at the planetary level. Using what Swilling and his team call 'resource decoupling' it is possible to have economic growth at the *same time* as using less resources. This growth, however, has to focus more and more on the development of *human capacity* – in the self-realization of the human, through expanded cultural, educational, and spiritual development, and in the substitution of new, resource-decoupled technologies, itself a major stimulus to economic growth. Indeed, reports are beginning to filter out which show that an important 'tipping point' has already been reached in the cost structures of new investments in sustainable power generation, such that they are already sufficiently competitive with fossil investments to pose a significant economic threat to existing fossil fuel power producers. In this situation, especially with the entry of new oil production technologies in the US, it would be absolute folly to remain committed to a growth path dependent on oil reserves.

At the centre of a balanced development policy is the *development of the human resources:* hence education, health, welfare, systematic wage increases, artistic and cultural development, the place-building of our cities as centres of design and creative achievement. This is needed to create both the workforce of the future, the key resource needed, and to ensure domestic demand is maintained and expanded as a driver of growth, particularly as export markets decline.

However, it is foolish to suppose that this can be achieved by some kind of enforced ascetism from the poorer countries. This idea lies behind the (sometimes) well-meaning attachment of many western intellectuals of the 'Gross National Happiness' policy being pursued by Bhutan. The west would be only too happy to have the peoples of the rest of the world sit around in loincloths contemplating virtue on a dollar a day, while they continue expand their own material consumption without limit. What is actually required is a massive equalization of incomes, worldwide, and that is not possible without a massive rise, over several decades, in the standard of living of the great majority of people on the planet.

There is a second reason however, and this is the key to a balanced development policy which develops, together, resource-decoupled delivery of the basic necessities to a standard required by modern civilization, the reconstruction of the production industries, and the establishment of world-leading high-end technologies, central to which is a focus on design quality. This is to recognize that the *purpose* of investing in infrastructure and modernization – that is to say houses, schools, universities, research centres and also cities, transport, a health industry and an ecological industry – is to create a human workforce capable of both consuming, and producing, the products of the future. These will be products in which design, creation, and diversity are the hallmark of achievement; it is simply impossible to construct large-scale industrial sectors that can deliver such projects on the basis of living in slums and poverty.

At the centre of modern growth therefore come industries which *raise the quality of life*; this is because spending on qualitatively better living is the main direction in which new spending is going – in other words, that's where the growth is. With the generalisation of the internet, the creative industries constitute the main unexploited potential for innovation. With the limits of resource-utilisation being reached world wide, the green industries are the second because technical change is being driven by 'resource replacement'.

Conclusion

I have by no means covered all the issues needed to deal with the question I have been asked to address. However this is quite sufficient to introduce the topic and I look forward to the discussion. It is worth however mentioning a few issues that do require treatment, and that I have not the space or time to cover.

First, we have to rethink the meaning of 'the public sphere' and 'government'. Public spending does not have to be conducted by large bureaucratic monstrosities and in fact this kind of spending is very unsuited to the modern cutting-edge, design-led industries. Rather the state has to guarantee the income of innovators and artists and ensure that their discoveries are widely disseminated in the economy; it has to provide big incentives for the adoption of resource-decoupled technology like green energy, and so on.

Second, and I think that Radhika Desai will probably have dealt with this, but it cannot be stressed sufficiently in the Russian context, a new financial order is required: the creation of South-South financial institutions based on sound Keynesian principles of growth-led investment, lender responsibility, and national sovereignty, that can protect developing and industries from the disasters of the 'lost years' and nurture infant industries with appropriate state-directed credit. In terms of the present debate about the role of the Russian banking system, the choice of an adequate development, anti-crisis policy cannot be divorced from the management of finance in such a way that it is a clear instrument of such policies and not – as in Europe – the biggest obstacle to them.

A third, somber point which should not be forgotten, and which brings me back to the question of the military solution, is the following: the biggest danger now in the geopolitical economy of the present conjuncture, is that the so-called 'advanced economies' are becoming 'rogue economies'. Europe is a failed state and the USA is a failed continent. The first has been taken prisoner by its bankers, and the second is a virtual hostage of the Tea Party Their capacity to inflict financial and also military damage is great, and because they are digging a big economic hole for themselves, it becomes more and more risky that crazy political forces will be unleashed.

Therefore the economic relations have to be accompanied by political relations such as mutual defence, a 'détente-oriented' international policy, restoration of the principle of sovereignty, and the construction of clear non-aggression pacts as an integral part of economic policies of mutually beneficial co-operation. This is not a separate issue from the 'exit from the crisis' but part and parcel of it; in order to construct an independent economics, the 'South' must protect the right to an independent politics.

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