Globalization and the coming worldwide Great Depression

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I'm glad to attend the workshop held by Focus on the Global South and the Ministry of Agriculture and Rural Development of Vietnam. Though the theme of the workshop is Trade Liberalization and Development, I think it more consistent with fact to relate globalization with recession. Here I try to illustrate how the globalization in the name of liberalization of trade, investment and capital flow leads to shrinking of world market demand, and the complete recession of world economy. Further more, I want to argue that the next decade will witness a worldwide Great Depression, and, in fact, with the collapse of Nasdaq in April 2000, the onset of the Great Depression may already have arrived. At the end of this paper, debates on China's accession to WTO and possible consequences are introduced briefly.

. Intensified competition result in economic crisis

In the dictionary of western economics, no word is more praised that competition. Perfect competition market is most efficient market, and will meet people's economic demand to the extreme, where economy runs like a nice machine, supply produce demand automatically, and no any dangerous of economic crisis.

However, in deed, competition is the very source of crisis. When investments in dominant industry were in excess, the price of raw material would rise sharply, and the price of products would fall sharply, hence all the enterprises in the dominant industry would face shrunk profit, and go bankrupt one by one. With more and more insolvent companies, banks fell down in volume, and all the related industry went bankrupt. All this means an economic crisis. After the insolvency wave, surplus production capacity and stock were cleared out, supply was scarce to demand, competition between counterparts was eased up, and profit soared again, then the crisis was past. In the crisis history, the return to prosperity was always accompanied by a new dominant industry and a new market, without which the crisis would last for a long time.

The core of competition could be described as a group of people with ambitions to maximize their individual benefit while chasing the same resources or same market. In Economics founded by

Adam Smith, maximizing individual benefit will automatically result in maximizing social benefit. However, it is a common experience that in a game different people contesting the same resources maximum of one side means minimum of the other side; or in more dramatic language, it is a kill-or-die struggle. Therefore, competition could be viewed as daily war. As known to all, when war is most violent both sides will lose most soldiers and weapons, similarly, when competition is most violent all sides will lose most profit, and majority will go bankrupt. Only after a great deal of resources have been wasted, could the remaining ones be allocated to those who are most competitive and good at using strategy to defeat others, meanwhile the industry would be monopolized relatively by several big enterprises. In fact, every crisis widens the monopolized area and raises barriers to entry. As known to all, the consequences of 200 years' competition since the first industrial revolution is that 500 hundred companies listed by Fortune monopolize the world's main industries such as coal, oil, steel, automobile, aircraft, ship building, chemical, machine tool, electric generation, semiconductor, computer, software, communication, and media. During recent decade, there has been a so called merger-of-the-giants wave in the developed countries, culminating in American OnLine swallowing Time Warner; the case is valued 350 billion US$.

It's worth noting that not any industry which falls into crisis leads to an general or overall crisis; conversely, a general crisis doesn't necessarily mean every industry must be in crisis. However, when dominant industry, for example textile industry in earlier 19th century, railroad industry in mid and late 19th century, automobile and chemical industry in earlier 20th century, semiconductor, or computer and communication industry in late 20th century, falls into crisis, then an general crisis follows. Those dominating industry, such as hotel industry in New York or sock industry in Japan, might fall into crisis in economic boom times because of excessive investments and violent competition. On the other hand, some new industry might grow fast during a crisis, for example in 1880's when American railroad crisis led to a general crisis, oil industry was still enjoying generous profit by way of trust-forming.

In conclusion, 'tempered' competition leads to economic boom, and intensified competition leads to economic crisis. Boom will be prolonged by financial system at the expense of the subsequent crisis being worsened.

. Tempered competition is the basis of the post-war gold age

There is a post-war gold age from 1950 to 1973 in the western world. Developed countries as a whole shared average annual growth rate of 4.4%, double that of the following thirty years. The gold age produced many optimistic declarations, such as the struggle between labor and employer disappeared, economic crisis was banished, economy would grow automatically and continually. The gold age drew attention also from Marxist economics. In China, it is commonly considered that it is the result of technology development and self-conditioning capacity of capitalism.

However, viewed from above theory about competition and crisis, this age appeared only in the context of tempered international competition. It's widely known that U.S is the only winner in

World War Two. In the days shortly after the war, America produced half of the world's products, and owned 70% gold reserve in the world. The American commodities were far better and cheaper than those of Japan and Germany. Hence, the ruling elites of U.S were once eager to be the only producer in the world, making use of all the military, political and economic advantages to serve the American capital, forcing the others to open market, import American goods, as the result, ruining economies of such nations as Germany, Japan, Britain, France and Italy, taking over their influences in their colonies, and eventually realizing its dream to dominate the world. Therefore, American aids were only used for the purpose of emergency relief in crisis situation, but not for reconstruction and development purpose.. In addition to aids, U.S demanded "the removal of all the discriminatory agreement in international trade", and denounced any restrictive trade policies designed to improve balance of payment status. Most important, U.S planned to dismantle German and Japanese military industries in the name of preventing the recurrence of military aggression. If all these had come to pass, U.S would have been the sole world factory, and Europe and Japan would have become suppliers of raw materials and primary products. Such a world couldn't be expected to enjoy a prosperous gold age lasting for more than twenty years.

American ambition was frustrated at last. With more and more American goods flooding into every country, and the military industries of Germany and Japan being dismantled, unemployed workers grew so rapidly that communist parties in Europe and Japan showed their strength. The ruling elites of U.S finally found that their number one enemy was Soviet Union and its socialist partners, hence American foreign economic policy turned to the opposite side, from eliminating rivals to helping them. Three main tools were used to realize the transition, first, the famous Marshall plan; second, stop dismantling; third, devaluate Japanese Yen, Deutsche Mark, and British Pound; for example, Yen was devaluated to 1US$ to 360Yen. Besides, Japan became American weapon supplier in the Korea war. All these measures could be summarized as super liberalization policy. American market was relatively open to Europe and Japan, but allowing the latter protecting their domestic markets. Hereafter, production ability of Europe and Japan were able to be reconstructed, domestic demands were enlarged, American goods also shared the enlarged market. Though Europe and Japan exported more and more to America, the trade balance still favored America. The world economy entered a positive-feedback loop..

As mentioned above, the positive loop is possible because of the American powerful competitive force. In 1950, the labor productivity in American manufacturing industries was 3 times that of the Britain, 4 times that of Germany, many more times that of Japan. American manufactured goods were 6 times that of Germany, 30 times that of Japan.

However, American advantages were disappearing gradually because of its high wages and low accumulation rate. During 1955 and 1970, total assets in American manufacturing industries increased by 57%, while major Western European countries by 116%, and Japan by 500%. 1960, average hourly cost of American manufacturing industries is about 3 times that of west Europe, 10 times that of Japan. The cost gap between America and its main economic rivals were so large that American foreign trade surplus and gold reserve decreased continuously. By 1971, America showed trade deficit for the first time. The percentage of American GNP in world total GNP went down from 36.3% in 1955 to 33.7% in 1960, and 31.3% in 1965, 30.2% in 1970, 24.5%in 1975. In fact, signaled by the collapse of Breton Woods System, American competitiveness declined to a level roughly equal to that of Europe and Japan.

In a word, U.S. made great concessions to its economic rivals to win the cold war, which laid the basis of the post-war gold age.

. Intensified competition leads world economy to decline spirally

With the collapse of Breton Woods System, US dollar was devaluated. Henceforth, the ratio of US$ to Yen dropped from 1:360 to 1:120, and its ratio to other main currencies went down as well. Devaluated dollar held by foreigners had less purchasing power, while it was conducive to export of American goods, and served to enhance American competitiveness. At the same time, America-based transnational corporations shifted their production lines overseas more rapidly and in larger scale to reduce the labor cost. For the third element of its strategy, U.S. forced its rivals and underdeveloped countries to open market more widely, by, among things, making increasing use of special 301 clause to protect its own market; thus it effectively made a turn from super trade liberalization to super trade protectionism.

This three-step strategy directly led to stagnation-inflation of world economy in seventies. Devaluation of dollar triggered a battle on exchange rate; Yen, Mark, and Pound raced to devaluate, which means uncontrollable inflation; meanwhile, Europe and Japan’s exports to America were reduced, and import from America increased, their economic growth reined in, but American economic situation saw only little improvement, with trade deficit growing not as fast as before.. There is a third effect: not only U.S., but also Japan and Europe, were all eager to shift their production base to the third world countries, which reduced world demand sharply. For example, when an American company such as General Motor closed a factory in Detroit, and reopened it in Mexico, it would replace each 30000$ job in US, by a 3000$ job in Mexico, with a net saving of 27000$, which could be used to reduce price, increase profit, investment, and /or high-ranking managers’ salary. Because workers’ wage would go to consumption, and profit would become investment, the above consequence would mean shrunk world demand. In Mexico, it seemed a good thing to have gained a 3000$ job, but GM’s technology and brand-name plus Mexico’s low wage could eliminate Mexico’s national automobile industry, and erase more employments, hence reduce Mexico’s domestic demand. Further more, when world demand kept shrinking, while more profit was reinvested, the danger of over-investment and crisis became very real..

Theoretically, if there were no new industrial revolution, with the competition between U.S., Europe and Japan becoming more and more violent, stagnation-inflation would last until enterprises go bankrupt en masse, and worldwide great depression would take place. However, there is a way to postpone the coming of great depression: by what I would call deficit consumption, which means to consume future income in advance.

To get rid of stagnation-inflation, Regan administration reduced tax to improve US enterprises’ international competitiveness, and spent more money on armament to enlarge domestic demand. This of course means more budget deficit. Regan administration accumulated a great deal of financial deficit, and the boom in eighties is called a “deficit boom”. President Bush followed Regan’s policy relying on continued deficit. As a result, by 1994, U.S government debt reached a new peak, $4600 billion, and interest payment annually was $300 billion. All these debts directly owed by the US government plus loans guaranteed by the government has reached truly staggering levels. Meanwhile, corporate debt and personal debt soared continuously. By the first quarter of 2001, American government, corporate and personal debt added up to $31600 billion, among which government debt totaled $7080 billion, corporate debt $15180 billion, persoal debt $7230 billion. Japan and Europe also have incurred enormous amount of debt. Japanese government debt is as high as 130% of GNP. European countries have less government debt than U.S. and Japan because of Masstricht treaty, but with high corporate debt and resident debt. It’s reported by British Financial Times that of all the hundreds of billions of dollars loaned by European big banks to communication companies, only 1% of the loan could be recovered.

Moreover, the debt scale in developing countries has been expanding. Several severe financial crises exploded Mexico financial crisis in 1982. Mexico, Brazil, east Asia, Russia, Turkey, Argentina, all these neo-liberal models collapsed and were forced to accept the structural adjustment prescription ordered by IMF, put on fire sale sovereign assets like land, mineral resources, railroad, telecommunication ect., and adopt austerity measures which means drastically reduced social spending and public services; as a result, people’s living standards were set back by decades. Sub-Sahara area is regarded as the forth world, where no news could attract others except famine and war. The total debt of the third world rose to $1000 billion in1987, which was almost 5% of all the GNP in the third world, and economic growth was thwarted by debilitating debt-servicing payments.. However, the debt was doubled by 1996 to nearly $2000 billion.

But who are the creditors? They are a small group of monopolies and financial oligarchies. In other word, this small group provided loan to governments, corporations, and residents to maintain the weak economic growth, and twice postpone the onset of a new Great Depression in early eighties and then in early nineties.

As known to all, U.S. and the world were in severe recession in the late eighties and early nineties. From the collapse of NYSE stock market in October 1987, American economy went downward and fell to recession in 1990. In fact, it was not until the second quarter of 1993 when American economy began to recover strongly, and started the so-called new economics era. But it’s hard to explain how could American economy keep booming while Japan was in deep depression, Europe in low growth, Latin America and south-east asia in crisis, and former Soviet countries lost a half of their GNP? Did American competitiveness become stronger again? No. Substantive Trade deficit capital deficit accompanied the New Economy. American trade deficit is $338.9 billion in1999, and reach $450 billion in 2001. At the same time, a great deal of capital from Japan, Europe, Russia, China, and other areas and countries flooded into U.S. It’s estimated that $800 billion fled from South-east Asia into U.S. after the violent financial storm in1997.

It’s a ridiculous circle. Countries export goods to U.S and earn a lot of dollars, but use dollars to buy American government bonds and stocks, then Americans have money to buy imported goods. Such a vicious circle couldn't last for a long time before the new Great Depression sets in. Because the depression was postponed twice, all the finance and money tools were used up, its magnitude and intensity must be greater than the Great Depression in last century.

. Globalization paves road for accelerating violent international competition

The three steps adopted by U.S to cope with the decline of competitiveness and stagnation-inflation means the growing up of neo-liberalism, also the arrival of the era of globalization. Free capital flow was advocated by way of flexible exchange rate. Free Investment was designed to ease the shifting of production base to the third world. Free trade was accelerated to increase American exports. These are three pillars of the neo-liberalism globalization since seventies.

But every pillar intensified international economic competition. Because of free capital flow, international competition was no longer restricted in technology and labor cost. The deflation of foreign exchange rate means all goods exported from this country are made cheaper and more competitive, therefore often triggers a deflation chain and violent competition. Secondly, free capital flow threatens every nation's currency sovereignty except U.S; therefore governments often find currency level out of work after signing free capital flow treaty. Thirdly, and more severely, flexible exchange rate absorbs a great deal of money to speculate in exchange market, hence less money would be used to invest in real production, and world demand would be shrunk. In 1966, of all the American foreign exchange, those related to import and export took a portion of 80%. Thirty years later, this portion fell to 1-2%. This means a large quantity of money stays in foreign exchange market.

Because of free investment, transnational corporations are able to chase lowest labor cost and lowest tax all over the world, and thus force every country to bow to them and repress labor movement and reduce tax. Workers in developed countries are threatened by closing or shifting factory, and reluctantly accept lower wages, more lay-offs, and worsening working conditions, while developing countries find their independent industries going bankrupt in large numbers.

Because of free trade, small or median enterprises and agriculture in every country compete with each other, so prices and wages go downward spirally, and majority of them would be merged or go bankrupt, which means to reduce investment and consumers demand further.

Now it's easy to understand that, neo-liberalism and globalization is the result of intensified competition between developed countries; in turn, it intensifies systematically international competition, and pave the road to the new worldwide Great Depression.

However, does this mean the globalization is a natural process? No, the globalization essentially is a man-made process which is motivated by multinational corporations, dominated by U.S., organized by IMF, GATT/WTO and WB, handled internationally by elites in politics, capitalists, and academics. Neo-liberalism is its ideological banner; so-called Washington consensus is the evidence of collusion.

Here I must differentiate market economy from neo-liberalism. Those defending neo-liberalism argued that if free market in a state is possible, why free market internationally couldn't be possible? However, a domestic free market economy must be balanced by a relatively powerful and democratic government. Only when one man one vote in politics can restrain one dollar one vote in economy, could the gap between poverty and wealthy be controlled, public utilities like highway, railroad, bridge, airport and port be constructed and managed efficiently, coordinated economic law, civil law and criminal law be enforced, economic cycles be responded to by financial and monetary policies. Without this premise, without a world government elected by all the people in the world, to dismantle protectionism and eliminate economic sovereignty, international free market could only lead to a world jungle.

. How is China involved in the globalization process?

When China began its reform opening-up policy in the end of seventies, Regan and Thatcher were starting a neo-liberalism storm in the west; when China decided practicing socialist-market economy, the globalization wave were at its peak. Hereby, from gestation to birth, Chinese market-oriented reform, which took the west as the mode l was cultivated by neo-liberalism, and welcome the globalization process without precaution, neglecting its jungle law effect. Chinese economic academia is enthusiastic to spread neo-liberalism. They are busy educating people that market economy is not only most efficient but also most fair; a good government should do nothing more than a night-keeper, "small government, big society"; to smash worker's iron bowl and eliminate state-owned enterprises will bring more efficiency; education, health care, pension, and employment safeguard should be reduced to its minimum, some of them should be privatized. They favor export-oriented economy, reducing even canceling tariff, and give foreign enterprise a very favorable policy.

It is no accident that, all these measures are the same as those dictated by IMF to the third world country, only with some consideration of Chinese characters, which make it more easy to be operated, relatively slow, so the problem showed out comparatively slow. By the end of nineties, the problem became so sharp that the decision maker could no longer close their eyes. On the one hand, state-owned enterprises, town or village owned enterprises and private enterprises went bankrupt in bulk; on the other hand, joint-ventures and export oriented enterprises grew and invaded the former market rapidly. The former want joint-ventures to pay high tariffs, and sell more product overseas; the latter demand lower tariff, and to be treated as Chinese enterprises.

In the debate of joining WTO, the difficult choice was raised and heatedly discussed. I don't think joining WTO is a good decision. The reason is very simple: No China's enterprise has international competitiveness. The total annual gross revenue of China's first 500 enterprises equals to that of General Motor, and the average gross revenue of China's first 500 enterprises is only 2% of that in the world. It’s right that total volume of several products in China ranks among the first in the world, for example steel, cement, coal, cotton, fertilizer, electricity, color TV, refrigerator, air conditioner, or motorcycle, but the large quantity is produced by hundreds of thousands of firms, each of them remains small in scale. This means China’s average industrial concentration is too low to compete with their foreign counterparts. The level of equipment is more backward, which results in more energy consumption of per unit product, lower quality and performance. Further more, China’s enterprises are seriously short of capital in general and have no ability to improve technology and market share rapidly. Besides, few China’s products are famous internationally, so high quality products couldn’t enjoy high prices, which means lower profit and higher cost.

Naturally, if China’s enterprises compete with transnational corporations under same conditions, a great number of them must go bankrupt, or be merged by the latter. In fact, industries of beverage, beer, detergent, bicycle, paper, medical, elevator, computer, aviation, and machine tools are all controlled by transnational corporations, at least the high value-added markets of these industries have totally gone to foreign companies. Other industries under more strict protection of government, for example automobile industry, petrochemical industry, steel industry, coal industry, even agriculture, are under serious threat of transnational corporations. Some firms of these industries have become the production base of transnational corporations. Hence, China’s enterprises have been imposed decreasing profit since 1996, and forced to dismiss workers, reduce wage and freeze up benefits, many of which went bankrupt. It’s necessary to note that this means bad debts in China’s main banks have been soaring. The ratio of bad debts of China’s banks is quite high, the main cause of which is found in the fierce competition, especially competition from foreign enterprises and imported goods; a second cause is corruption.

Here I want to emphasize the agriculture. As known to all, the rural population in China adds up to 900 million, 500 million of which have the ability to work. The average household owned land is only 0.4 hectare. To insure such tiny land produce enough food, the price of food must be maintained at a high level, which means the price of the Chinese agriculture products such as wheat, rice, and corn of China is constantly higher than that of international market. The price of agriculture has kept decreasing since 1996. The price fell to such a level that per hectare wheat brought 120$ loss to peasants in the autumn of 2000, while an average peasant’s annual income in pure agriculture area is only 80$, and almost 600 million people live in pure agriculture area. If the “ Agriculture Cooperation Agreement between P.R.C and U.S.A” is implemented after China joins in WTO, the income of peasants must go down steeply, more land must lie wasted, more massive peasant influxes into cities to find only poverty trap and despair.

As the result, China’s GDP might increase temporarily, but employment, tax and wage per GDP unit will decrease continuously. More important, China will lose an independent industrial system, and become the production base of transnational corporations. Most rural population will lose their land and income. Financial system might collapse because of increased bad debts. Meanwhile, China will have no ability to construct a social security system with enough money because the government couldn’t impose enough tax upon foreign enterprises, which will certainly deteriorate public security.

However, holding on, not changing, current policy is the best answer, because it has least resistance, even if a decision with least resistance is a most dangerous one. Therefore, China is involved formally in the globalization process by joining WTO.