

SHE Society of Heterodox Economists

*School of Economics
University of New South Wales
Sydney 2052 NSW Australia*

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ACCUMULATION AND EFFECTIVE DEMAND IN EAST ASIA SINCE THE 1990S

JOSEPH HALEVI

Division of Political Economy
University of Sydney

PETER KRIESLER

School of Economics,
University of NSW

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Accumulation and Effective Demand in East Asia since the 1990s

Joseph Halevi

Division of Political Economy, University of Sydney

Peter Kriesler

School of Economics, UNSW

Abstract

In order to understand current developments in Asia, particularly the pattern of growth and accumulation, it is necessary to consider the historical development of the region. In the paper we attempt to understand these recent developments from the stagnationist tradition in Marxist literature which is discussed in the next section. Using the stagnationist framework, three distinct phases of Asian capital are identified. The early phase was characterized by European interest in the region and with the start of Japanese industrialization, while the second phase is marked by the rise of Japan as the oligopolist power in the region. Finally, the rise of China as a significant economic force leading to structural change in the region is considered.

Accumulation and Effective Demand in East Asia since the 1990s

Historical Background

There is an important stagnationist tradition in the Marxist literature which goes back at least as far as Rosa Luxemburg. In the twentieth century it culminated in the writings of Kalecki and Baran and Sweezy. The essence of this view is that there are long run stagnationist tendencies in capitalist economies caused by the fact that the level of productive capacity is always higher than the level of effective demand.

These stagnationist tendencies are reinforced with the development of the monopoly phase of capitalism. Oligopolistic corporations are associated with both a rise in the share of profits at the expense of labor's share, as well as a reduction in the drive to accumulate. As the propensity to save from profits is higher than from wages, this redistribution is associated with lower levels of effective demand, further exasperating the problem.

This is well summarized by Baran and Sweezy:

Under monopoly capitalism The normal condition is less than capacity production.

The system simply does not generate enough 'effective demand' .. to ensure full utilization of either labour or productive facilities. Baran and Sweezy 1966 p. 146

The stagnationist tradition acknowledges that these tendencies may be postponed by a Schumpeterian process of creative destruction in times of profound technological change. External markets can also act as exogenous sources of effective demand which can mitigate the stagnationist tendencies. External markets refer to demand from markets external to the sphere of production. These external markets can be either domestic or foreign. By domestic external markets, we refer, in the tradition of Baran and Sweezy, to a number of possible external sources of effective demand

including advertising, finance, insurance, real estate, government expenditure and expenditure on the military¹.

Foreign external demand is the result of net exports. Countries can increase domestic demand at the expense of their trading partners, by increased exports, a point noted by both Keynes and Kalecki, who also stressed the global limitations of such policies. Keynes and Kalecki clearly understood the importance of international trade as a mechanism for exporting unemployment between nations (Keynes, 1936, ch. 16; Kalecki, 1976; Halevi, 1984). In other words, the balance of payments may become an important constraint on the growth of effective demand if countries maintain chronic deficits.

This problem was specifically addressed by the successful development of East Asia in the post-WW2 period, which relied on external markets with the newly industrializing economies (NIE's) growth strategies explicitly focused on exports.

However, even in these cases, the balance of payments may be problematic as the level of the productive stock of capital is deemed low relative to population, particularly where capital goods – including intermediate industrial products – are mostly imported. Even if a country has a large productive capacity its accumulation may be constrained by the balance of payments bottleneck which will arise when factories and services are near full capacity. If capital goods including intermediate products have to be imported, then any increase in investment will increase the size of the external deficit, which may then become an obstacle to full employment policies even if the economy is an advanced one in terms of per capita income. This is the result of fundamental problems in the international monetary system which has always placed the burden of adjustment on the deficit country, so reinforcing the stagnationist tendencies already inherent in the system (Kriesler and Halevi 1996 and Halevi and Kriesler 1998).

¹ Kalecki also acknowledges the importance of the last two sources of expenditure.

This view should be contrasted with the dominant neoclassical view, according to which any increase in saving is a benefit to the economy rather than the burden that Marxist economics in the above traditions see it as. The reason for this is that with an underlying loanable funds vision of capital markets, the increased saving – supply of loanable funds – immediately translates into an increase in investment demand for loanable funds. It is this view, associated with the Washington Consensus, which argues that policies are needed to increase national savings as the only way of both improving growth rates and addressing current account imbalances. Similarly, according to this position, Japanese current account surpluses, post-1970, have led to capital outflows which, in turn, have funded investment elsewhere:

[T]he current surplus in the Japanese balance of payments is a *beneficial* feature of the world economy, and Japanese savings, as manifested in the country's balance-of-payments surplus, can be used for Asian economic development. Healey
(1991) p. 25 Emphasis in original

Elsewhere we have discussed this position in full noting that there are serious logical and theoretical problems with these arguments. (Halevi and Kriesler 1998 and Kriesler and Halevi 1996) The loanable funds idea underlying it is based on the view that saving constitutes a stock of loanable funds for investment, and that savings must precede investment, so that savings causally determine investment, with the rate of interest equating the two. This idea is rejected by most heterodox economists, for reasons outlined in our earlier papers. Rather than being of benefit to other nations, large current account surpluses are merely ways of exporting unemployment, and lead to severe contractionary pressures in the deficit countries.

Capital Accumulation in Asia: Growth to the 1990s

From the 19th century until launching in China of the Four Modernizations program in 1979, the process of capitalist accumulation in (East) Asia has gone through two phases. In 1979 it entered a crucial third phase which started to have a significant external impact by the end of the 1980s and

gathered momentum after the Asian crisis of 1997. Thus it can be said that only around and after the 1997 financial crisis did the new regime of accumulation which was incubating in China change and sweep aside the previous one based on Japan's hegemonic role in the East Asian zone bordering China.

We can now summarize the main features of the phases of capitalist accumulation in East Asia

Phase I: The first phase of accumulation is characterized by both the European imperialist encroachment upon China and the industrialization of Japan strictly connected to its imperialist expansion into China, including formerly Chinese Manchuria under Tsarist Russia and into Korea. This imperialist expansion by both Europe and Japan into China and by Japan into Korea was a factor of grave retardation of the development of both countries. The logic was that of subordinating the economic structure of East Asia to capitalist accumulation in the respective metropolis. The expansion of Japan into China and Korea (1895, 1905, 1910) was based on an alliance, both political and financial, with Britain which sustained Japan's expansion and extended large loans to Tokyo, thereby turning Japan into a major debtor.

WW1 solved the external debt problem of Japan, thanks to the alliance with Britain. WW1 acts as a classical external market and as an import substitution device. The search for markets restarted in earnest with the Great Depression and the related Manchuria incident in 1931. This event, which started the long war against China and, in appropriate historical terms, WW2, is the factor which propelled the heavy and chemical industry process of capital accumulation in Japan, operating therefore in an eminently Kalecki/Rosa Luxemburg form of imperialism *cum* accumulation. At the same time however, the imperialism of Japan's capitalism had one crucial weakness regarding the structure of the balance of payments. While the Yen area was generating a surplus for Japan it was not doing so in terms of the trade with the dollar and sterling areas (Nakamura 1983). Japan's imperialism towards China clashed more and more with the role ascribed to China by the United States (US) – defined by the open door policy elaborated in the years leading to the war against Spain in 1898 which brought the US to Asia through the conquest of the Philippines. Washington's

move towards sanctions and oil embargo against Japan turned the dollar and sterling components of the balance of payments of Japan into an insurmountable obstacle out of which grew the conditions for total war. Thus Phase 1 ended in practice in 1937 when the all out war against China encroached directly on US interests in China and compelled a rather reluctant US government to set up an oil embargo against Japan which then led to Japan's decision to attack the United States.

Phase 2: What remained of Phase 1 was the structural change caused by the heavy and chemical industrialization of Japan. Kosai Yutaka has presented convincing estimates regarding the extent of the war damage (Kosai,1986). While the damage was extremely severe in shipbuilding it turned out to be milder in the machine producing capacity of the economy, although more serious than in the case of Germany. But Japanese capitalism lost the functional connections between markets and raw material supplies that it has been establishing through imperialism for half a century up to 1945. Thus Phase 2 can be seen as formed by three sub-periods. The first sub-period is centered on creating the conditions for an economic anchor for Japan and the second is marked by the formation of a Japanese oligopolistic zone in the East and Southeast part of Asia. The third begins in 1971 with the US abandonment of the dollar-gold convertibility. Both periods up to 1971 are characterized by US public expenditure connected – in a pure Baran-Sweezy fashion – to military expenditure and to the special institutional arrangements made by the US to have Japan quickly accepted within the General Agreement on Tariffs and Trade (GATT) in 1955. These included the signing of 13 trilateral trade treaties offering to third countries greater access to US markets provided they forwent the use of clause 35 of GATT which allowed setting up trade barriers against any country not accepting trade reciprocity (Forsberg, 2000). US policies allowed Japan to lift the balance of payments ceiling which is another way of saying that the limited availability of internationally profitable effective demand was less of a constraint on decisions concerning investment and accumulation.

Why was the United States interested in uplifting and protecting Japan even at the expense of the penetration of its own multinationals into Japan? There was indeed a grand design of reshaping

world capitalism with the United States at its core flanked by two growth poles: Europe with West Germany at its centre and Japan in Asia. The difference between these two poles resided in the fact that while Europe was the economic hinterland of Germany, Japan could not be ensconced in Asia because of the Chinese revolution and the national liberation movements in the region, including the VietCong led by Ho-Chi-Minh. Thus there was no natural area for Japan in the region. Japan had to be taken on board by Washington in a much more direct way that was the case with Germany, while, at the same time, the United States took upon itself the task of fighting the national liberation movements. This fact led Washington to transform the Korean War into a roll back war, and to get involved in Vietnam. Such a strategy was part and parcel of US policies to control raw materials through its own multinationals and to control world liquidity through the dollar supremacy which then was connected to a US surplus in the current account. With hindsight it seems clear that US authorities did not foresee the costs, in terms of the current account, of their own imperialism and were convinced that American technological superiority and sheer economic size would carry the day. US policies created a shelter for Japan in which the *keiretsu* could organize the much needed retooling in order to fan out into world markets without reciprocity from the Japanese side. American special procurement payments during the Korean War were the most noticeable example enabling Japan to overcome balance of payments constraints. But as shown by US historian Michael Schaller, US war expenditure in Vietnam had an equally important impact on Japan.

The second sub-phase is that of the Vietnam War which Schaller has characterized as Japan's re-entry in Asia (Schaller, 1985). Propelled by US war expenditure the area becomes structurally dependent upon Japan, first in terms of imports. The crucial pillars of the area of Japanese oligopolistic hegemony are The Republic of Korea (hereafter Korea) and Taiwan notwithstanding that, unlike later Thailand, Malaysia, and Singapore, the two countries did not develop solely and not even principally on the basis of direct multinational investment. Yet it is in relation to Korea and Taiwan during the years of the Vietnam War that the model of structurally dependent

accumulation was fashioned and it has been this model, rather than the so-called “flying geese” paradigm, that continued after the end of the second sub-phase shaping capitalist power relations in East Asia (Lim, 1985; Hart-Landsberg 1993). This factor has been recognized also by economists involved with establishment institutions and policy making bodies, but precisely for this reason they have smoothed out the implications regarding the fundamentally asymmetrical and contradictory forces at work (Hatch and Yamamura, 1996). The essence of the asymmetries lay in the role of Japan as a poor buyer but as a strong oligopolistic seller, while solutions to financial crises had to be undertaken by the US (Woo, 1991).

In this context the third sub-phase is represented by the sharpening of US disengagement as the global coordinator of developed capitalism which began in 1971 with President Nixon’s declaration of the abandonment of the Bretton Woods parity between the US dollar and gold, made Japan into the adjustment variable of US monetary and exchange rates policies. The ensuing sharp revaluation of the Yen, transformed the part of East Asia under US geopolitical and military control, into an increasingly important rear for the dominance of Japanese monopoly capital. Japan countered the devaluation of the US dollar in the 1972-79 period by further tying Asia to itself. Technology transfers to Korea, for instance, meant a widening trade gap in favor of Japan and , increased structural dependence of Korea. In countries – such as Thailand, Malaysia and Indonesia – structural dependence was brought about by the dominant role of the Japanese *keiretsus*.

The third sub-phase – which is specific to the American-Japanese Asia – ran for a while parallel to the beginning of the third big phase in the history of Asian capitalist development. That is, parallel to the inception and incubation of the Deng Xiaoping reforms in China. Indeed during the 1980s the events in China, while momentous in social, political and geopolitical terms, were relatively separate from the macroeconomic trends occurring in the rest of American-Japanese zone of East Asia. The impact of the Chinese situation became apparent by the end of the decade and by the time of the East Asian crisis of 1997-98 China became the real centre of gravity of the Asian continent. This means that the disengagement of the US from its role as global coordinator of world capitalism

must, as far as the American-Japanese East Asia is concerned, be seen as part of the third and final sub-phase of Phase 2.

We have seen that the third sub-phase begins in 1971 with the ditching by the US of the dollar-gold parity and with a sharp devaluation of the US dollar against the Yen thereby pushing Japan to further extend its economic domination over non-communist East and Southeast Asia. By 1979 with the loss of Iran to the United States and the ensuing rise in oil prices US policy makers decided to fence off any threat to the dollar and enacted a high interest rates cum large military spending deficit policy. This set of policies led to a revaluation of the US currency – albeit well below the pre 1971 level - to a military led growth revival in the United States and to the opening up of an unbridgeable deficit in the current account, in which Japan and the rest of East Asia had a big share.

By 1985 the policy became unsustainable as it was generating tensions within US capitalism and also with the Europeans who, already mired in high unemployment, were witnessing a flight of capital towards the United States. On the 22nd of September of 1985 in the Plaza hotel in New York an accord was reached between the United States and the major capitalist countries on lowering US interest rates starting a steep devaluation towards the Yen which lasted till May 1995. In that monetary context, Japan's strategy towards Asia aimed at recouping - through Asia's growth and exports and Japan's own economic hegemony - the squeeze in profit margins of Japanese corporations on their exports to the US and also on the activities of transplants.

The US market has for Japan greater competition than the Asian one so that it was impossible to transfer fully the increase in the value of the Yen onto Japan's exports towards the USA. Furthermore, for the same reasons, the transplants could not pass fully the increased dollar costs of imported technologies and machinery onto their final US prices. It is in this context that East Asia, whose currencies were pegged to the US dollar, became a very important source of Japan's net balance of payments position. The Asian crisis of 1997 was a real crisis of capital accumulation determined by the dynamics of structural asymmetries and not by the factors usually mentioned in traditional studies. With the collapse of little capitalist American Japanese Asia Phase 3 of the

history of Asian capitalism which had already begun in China with Deng Xiaoping reforms came to the forefront of world development.

Post Asian Crisis: Phase 3

It would be difficult to address exhaustively in this paper the reasons why China has become the anchor of capitalist accumulation in Asia. This would require full research on why the capitalist world trusted the intentions of Deng Xiaoping's policies. Our own view is that in the case of China's entrance into the capitalist world the old Mao adage 'politics in command' actually operated from the US side. Consider that when the *4 Modernizations* were launched in 1979, China and the United States were together on all the main international issues in Asia and shared opposition to the Soviet Union. They agreed in supporting the ousted Khmer Rouges in Cambodia, both vehemently opposing Vietnam's intervention there; they agreed in supporting the armed opposition to the Soviet Union in Afghanistan and they also agreed in supporting Pakistan relatively to India. Given that throughout most of the 1980s the cold war had been revived by the presidency of Ronald Reagan, the China card played a crucial role in US policy. Hence Washington was willing to grant credibility to China's capitalist reforms particularly as they were intended not just to open China to some kind of local ersatz capitalism, but especially to the multinational companies, both directly and indirectly through outsourcing.

Moving now back to economic reasoning, once this process of development of Chinese markets kick started the new industrialization, owing to the size of its internal markets, the process of structural adjustment spread throughout the economy, leading to the development of many of the stages of production involved in manufacturing. As a result of these structural changes, inter industry linkages were kept domestic, so that expansion in one sector fed through to increased demand for other developing sectors. As a result any improved export performance fed into a cumulative process spreading the benefits of industrialization through the economy, with minimal leakages abroad. (Kaldor 1989)

The first step to take for the assessment of the role that the PRC has been acquiring in influencing the tendencies in world capitalism will be to ascertain the degree of sustainability of the accumulation process in China, not in relation to some normative objectives but in relation to the Marxian and Post-Keynesian notion of profitability and effective demand. This requires the analysis of dualism based on the following criteria which cannot be obtained from orthodox economics.

To what extent does China's accumulation validate or not the conditions of *comparative productivity change advantages*? (Pasinetti, 1981). These have nothing to do with the static fixed factor endowments theory of comparative advantages. Instead it is a rather Smithian dynamic principle according to which if productivity increases are not retained within the same economic system (defined in terms of its polity, currency and institutions), but are instead leaked abroad mostly through fall in export prices, the country will develop in a dualistic manner without an adequate growth of domestic demand. The adequacy of the growth of domestic demand is not measurable by aggregate GDP figures but by whether or not the growth of productivity in the leading sectors flows back in roughly equivalent increases in wages and productivity in the domestic sectors. While such a gap cannot be avoided its systemic persistence and widening will set a limit to the expansion of per capita demand of wage earners creating conditions of chronic underutilization of capacity. The *principle of comparative productivity change advantages* has a special corollary which works in reverse. We have seen that the country as a whole may find itself on an unwarranted accumulation path if the productivity of the dynamic, say exporting, sectors does not flow back as greater domestic purchasing power but is instead leaked abroad through persistently lower export prices. The corollary lies in that whenever the growth of productivity of the dynamic export oriented sectors exceeds significantly the growth of productivity of the equivalent sectors abroad, the sectors in the foreign countries cannot hold onto their own productivity growth and must shed workers as well as undertake capital flows externally. The paradox is that a less advanced industrial country has a much greater chance of developing sectors

whose productivity growth is both much higher than that of the rest of the domestic economy and that of the corresponding sectors abroad.

The PRC is a unique case in the world of transfer of global capital towards an economy which in absolute terms is now bigger than France's but in relative per-capita terms is so much lower than any of the advanced OECD countries. And this situation is likely to last for quite a long period. There have been other cases of industrial development for large countries such as Brazil, Mexico and India but neither in per capita nor in absolute terms have they ever surpassed any of the big capitalist countries of Europe and of course Japan. Japan, when it began to outgrow in absolute terms the large Western European countries it did so when it reached the stage of industrial maturity with a high wage level per unit of labor. The PRC by contrast can stay for a long time on the lower end of the scale with the dynamic sectors operating according to the *principle of comparative productivity change advantages* and its reverse corollary for the industrialized world. The PRC can therefore be in absolute terms bigger than, say, Germany, while remaining in per capita terms below Turkey.

International oligopolies have here a double edged role. On one hand by investing in productive facilities they expand the array of sectors having dynamic productivity growth, but on the other hand, they tend to reinforce the dualistic features of that growth domestically and the corollary internationally. Let us make the following cases.

- (a) A multinational company invests in China for the local market as it is now the case for autos. In this instance the capital goods will be provided by the parent company and the domestic Chinese economy will supply the basic commodities. Profits will spring mostly from the low wage costs and from productivity gains. By contrast if after a while the foreign company starts ordering its capital goods from Chinese industries, then there is a structural flow back both in terms of productivity growth and in terms of the expansion of the array of domestic sectors. But, and this we know from advanced economic theory, even orthodox, there is no guarantee that market mechanisms will ensure such a

transition. It will more likely depend on the determination of the central authorities to steer investment of multinationals into developing the capital goods sectors in China.

- (b) Assume a foreign multinational invests in order to export by supplying itself with capital goods ordered from the home country or from any of the high wage countries of the US/Europe/Japan “Triad”. Then this means that the foreign multinational is only interested in using the lower wage costs coupled with its own price making capacity in the developed countries (markets). This case, which according to research seems to be quite significant as only 15% of the total value added of China’s exports is from domestic production, just perpetuates dualism while hollowing out the corresponding sectors abroad.
- (c) Assume a foreign multinational subcontracts/outsources its orders in China. There may be then a greater use of domestic inputs, but the entire operation is based on the principle of maximizing the ‘benefits’ stemming from low wages and from the price making powers of the multinational in question.

Both in the case of (b) and of (c) the expansion of per-capita income and demand in China is constrained by the strategic role played by low wages, so that demand may expand absolutely but less so in per capita terms, while at the same time hollowing out the productive basis of the advanced countries. Cases (b) and (c) are for the long term objectives of the PRC’s authorities to transform China into a significant industrial and military power to be discarded. Yet they may nest into the Chinese political economy thereby creating a permanent structural fault or weakness in the way per capita income and demand progress in the country. Given the Communist Party of China’s orientation to have a sort of “new economic policy” (NEP) with world capitalism, the best solution is to have multinationals which (i) invest in China for both the domestic and the export markets and (ii) produce in China the capital goods and the required technologies or at least a growing part of them. This eventuality however does not solve the question of the hollowing out of the advanced countries. At the same time however even for China reliance on foreign multinationals cannot

continue for too long a period because the crucial decision making processes and crucial technological development will occur outside it. Thus only by creating its own oligopolistic multinationals will China find itself in a position of being on the path of becoming an advanced industrial and military power. But if China does not get substantial technological transfer to be incorporated into its own corporations, that is, not just for the foreign corporations operating in China, the country will not escape easily from dualism and technological dependency, while at the same time generating a hollowing out of the productive system of other economies.

Let us now consider the gravitation of foreign direct investment to China coupled with the corollary of the special principle regarding productivity change advantages. The corollary establishes the case for the hollowing out process and this leads to insurmountable problems of effective demand for the advanced countries. At this stage in what way is the link between the State and capital accumulation modified? According to the Marxian view the State defends the interests of capital in a sometimes complex process of mediation but also sometimes quite straightforwardly. Since the so called globalization cum privatization phase set in, we are in the straightforward phase and the State only mediates between the different capitalist groups. But if productive bases are hollowed out and the interests of US/Europe/Japan based multinationals and outsourcing companies lies in China, the material ground of the advanced states weakens. A contradiction develops between what is required from the State and its material capacity.

The Chinese State cannot be a substitute for the global role that the State of the advanced capitalist countries is for world capital and for the reproduction of capitalist relations: First, because it does not have the power to play that role. Secondly, and because of the first reason, the Chinese State if it really intends to stay on an advanced capital accumulation path must strengthen the material basis of its own political capacity. This will make it privilege Chinese corporations and support them in the competition on foreign markets against the very foreign companies that are investing in China. Hence lured by the Chinese State but not necessarily defended by it, the gravitation of world capitalism towards China creates a conflict between the multinationals of the Triad and their

respective states in Europe, Japan and the US. In general there is no political or economic solution to this type of conflict which is already manifesting itself since the EU has defined a red danger zone encompassing the sectors which are exposed to the hollowing out process.

The US is the most vulnerable country, and this is well known. The US is counting on two factors:

- i) The military one which brings about the control of crucial energy areas and prolongs the dollarization of energy products.
- ii) The willingness of the PRC's central bank to refinance US external deficits. Yet this second aspect contains a major inconsistency. In order to secure beyond any doubt the refinancing of its external deficits by Beijing's Central Bank US authorities must accept the institutional politicization of their external deficits. In other words the clearance of the deficit becomes a political not an economic issue. If it were left to economics the refinancing would not be guaranteed. This explains why the US monetary authorities while favoring the opening and liberalization of the capital accounts in the balance of payments of the Asian countries under direct US influence, are quietly supportive of the Chinese position of keeping their own capital accounts closed. And recently, the previous Federal Reserve chairman, Mr. Greenspan, also came out against freeing the exchange rate of the Yuan. But this factor weakens the state capacity of the US in favor of China.

The contradictions between China and the US can be understood by referring to the different strategic view about China in the world economy held by US multinationals and the Chinese Communist Party. For the former China's position is simply that of a low cost producer, for the latter the inflow of capital and direct investment is part of a policy with world capitalism and therefore it is supposed to be just a stage in the transformation of China into a leading industrial and military power. In the long term these two views are not compatible while at the same time the actual role of China contributes both to the profits of, say, Walmart, and to the hollowing out of the US and of its State capacity.

Europe is in an intermediate position which reflects also the contradictions within Europe. The countries with heavy machinery sectors and telecommunications technologies (Germany with Austria and Switzerland, Sweden and Finland) whose trade balance in those sectors is highly positive are supportive of the Chinese pattern of growth. Financialized economies like the UK are also but for altogether different reasons. By contrast countries with still a large consumption goods sector such as Italy, Spain, Greece and France are increasingly at odds with China and they were behind the move to define a red zone of danger in terms of sectors vulnerable to being hollowed out. In this context the case of France is interesting because France is poised to sell to China its advanced weapons as well as public sector's goods such as railway technologies. Yet clearly they think that the hollowing out process is stronger than the expansion into China despite the fact that their automotive companies are heavily involved in the PRC.

At first sight East Asia and Japan are the least vulnerable because they have a substantial surplus with China. But these aspects will have to be explored in more details because reliance on exports towards China may actually create the conditions for their subsequent hollowing out. In fact a great deal of these are made by Japanese and Korean multinationals for investment purposes which will translate into a growing flow of exports from China back into Japan, Korea etc. There would be nothing wrong if the present flows of net exports were to be accompanied by significant export led growth in those countries. So that by the time exports from China become positive, those countries will have already achieved a high level of utilization of their own productive capacities. But this is not case especially for the most important of them: Japan. Furthermore exports towards China depend very much on the trade patterns between China and the US and between China and Europe. While China has changed the direct dependency of Japan and East Asia on net exports towards the U S, the process of integration is not China-centered since the effective demand loop is closed by China's net exports to the US. In this sense the PRC growth and the greater gravitation of East Asia's trade flows towards China do not change the basic picture of the U S as defining the perimeter of realization.

Europe's stagnation is unlikely to be solved through the domestic boosting of effective demand. This phase is over in Europe since it is difficult in Europe to increase demand without empowering wage earners as there is much less room to channel the surplus towards sectors, such as the military industrial complex, which remain outside the range of wage earners. Hence Europe will require an increasing amount of net exports, a paradoxical situation since the greater an economic area becomes the smaller should be the importance of net external flows. But this is not the case for Europe where stagnation has acquired chronic features. Coupled with the increased importance of Chinese net exports towards the US, the problem of the refinancing of US external deficits is likely to become the catalyst of the various crisis tendencies operating in the present phase of capitalism.

In earlier work (Kriesler and Halevi 1996 and Halevi and Kriesler 1998), we considered the implications of Japanese surpluses for Asian development from the beginning of the post war period up to the beginning of the 1990s; concentrating on the role of effective demand... There we concluded that Japanese surpluses with the rest of Asia created an effective demand sink, leaking demand from that region and promoting strong stagnationist tendencies. Had the region been autarchic, the effect of this would have been to lead to low growth levels, with high levels of unemployment. The tendency was counteracted by the region's strong trade surpluses with the US, which acted as an external source of effective demand. An important additional consideration, which needs to be incorporated into this thesis, is the implications of the rise of China as a major international trading partner for effective demand in the region. As Hart-Landsberg and Burkett (Chapter 4, this volume) make clear, the emergence of China has effectively changed the structure and destination of Asian trade, but has not changed its reliance on the US as an external source of demand necessary to alleviate the region's stagnationist tendencies. In other words, the loop has changed, to incorporate China, but still ends in the US, so that there is the same problem with just one additional major link in the chain. This has been manifest by a number of important changes to trade. "China has increasingly reorientated its exports of manufacturing away from East Asia (minus Japan) and towards the two most important international markets, those of the US and the

European Union” (Hart-Landsberg and Burkett, Chapter 4, this volume). As a result of the substantial increase in Chinese exports to these markets, exports from the rest of East Asia Association of South East Asian Nations (ASEAN) and NIE’s included, have fallen dramatically. In other words, Chinese exports to those areas have replaced those of the other Asian nations. On the other hand, East Asian exports have been reorientated towards China, so that over the 1990s, China’s deficit with the area increased a thousand fold. (Hart-Landsberg and Burkett, Chapter 4, this volume).

The capitalist development of China introduced new contradictions into the world system of accumulation. During the US-Japanese hegemony in the little Asia bordering China the contradictions were mainly connected to the neomercantilist orientation of Asian growth, a neomercantilism supported by the US itself over almost 40 years. The contradiction was mostly between the states involved, their national companies and the USA and its multinationals. Now the contradiction is within the capitalist economies investing in China, and operates directly on the scale of the advanced capitalist world. Increased reliance on production stemming from branches operating in China undermines the connections between the State and the respective capitals in a fundamental way. How it will pan out we cannot tell as processes are always path determined. If, for example, there is a change in the willingness of America to absorb the trade surpluses of China, thus acting as an external source of effective demand then it is clear that the underlying stagnationist tendencies for the area will manifest themselves in the form of crisis lowering growth and employment throughout the region. However, it is not possible to forecast the actual outcomes, since they are dependent on economic, social and political factors which themselves will be determined by the paths of events. In particular, political attitudes in America and Europe are currently in a state of flux, and it is unclear what shape any emerging consensus, if there is one, will take. Clearly, however, it is the political consensus of these areas which will play a vital role in the economic future of Asia.

Conclusion

We can conclude by considering the significance of the emergence of China for the underlying structural forces at work in the Asian region. As we have argued, these forces have reinforced domestic stagnationist tendencies, particularly due to the role of Japanese surpluses as a further leaking of effective demand from the other Asian economies. In the initial stages of growth and accumulation, it was the foreign external markets provided, in particular, by the USA which prevented the region from collapsing due to long run problems with effective demand. The emergence of China has not essentially changed the stagnationist tendency of the Asian region. Rather it has led to changes in the structure and direction of Asian trade, but it has not changed the reliance of the region on external sources of demand (mainly the US) so as to prevent slow down of growth and the emergence of mass unemployment. Although China has introduced new links into the chain of demand, it is not in itself an adequate source of effective demand for the region.

As a result, the underlying stagnationist tendencies of the region would lead to low growth and employment levels, except for the external sources of effective demand, dominated by America. Given the political climate in America, it is not clear whether, or for how long, it will continue serving this role, and, therefore, how long crisis in the area can be averted.

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