12. Food Security and Finance in the World Economy

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Neither the seriousness of the world food problem nor the intimate relationship between the world food problem and the world financial arrangements has received the attention it deserves. Let us begin with the former. Over at least the last two decades there has been an absolute decline in the per capita cereal output for the world as a whole. For the period 1980-85 the average annual per capita world cereal output, according to the UN Food and Agriculture Organization (FAO), was 335 kilogrammes; this declined to 310 for 2000-05. This decline in per capita output has certainly been accompanied by a decline in world per capita consumption, which means that the world on average is hungrier today than it was two decades ago.

What is significant however is not just this, but also the manner in which this reduction in consumption has been effected. During this period, there has been a substantial increase in the average world per capita income; since the demand for cereals (taking into account not only direct but also indirect demand, via processed food and animal feed) rises with income, this demand should also have grown. In the face of declining output, this should have caused rising food prices relative to money wages around the world, and hence also relative to the prices of manufactured goods. We should therefore have expected in this period of declining per capita cereal output a shift in the terms of trade between cereals and manufactures in favour of the former.

But this did not happen. On the contrary, cereal prices fell relative to manufactured goods prices by as much as 46 percent between 1980 and 2000! This suggests that the decline in per capita cereal output, in a situation of rising per capita income, did not generate any specific inflationary pressures on cereal prices, as one might have expected. The reason it did not is because in the very period when per capita cereal output was declining, a parallel process of compression of money incomes of large sections of the world's population was going on. The reduction in cereal consumption of the world's population was effected not through a rise in prices relative to money incomes but through a compression of money incomes relative to prices, for which the term "income deflation" is used below.

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[1] The implicit assumption here, following Kalecki (1954), which is both plausible and commonly-made, is that manufactured goods prices are a mark-up over unit prime costs, which are linked to the level of money wages.

[2] I am grateful to Shouvik Chakravarty, research scholar of the Jawaharlal Nehru University, for making these terms of trade figures available to me from his ongoing Ph.D. thesis.

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compressing demand. Of course the term "inflation" itself is an ambiguous one. In current "mainstream" economics it refers to a state of affairs where all prices, including money wages, are rising simultaneously, so that there is no worsening of the condition of the wage-earners per se and the only sufferers are those with cash balances, most of whom are likely to be rich. But inflation as we know it in real life, both in developed countries and, in particular, in developing countries, where the bulk of the workers do not have wages indexed to prices, is one that hurts the working masses. Keynes called this latter kind of inflation "profit inflation" . In situations where supply cannot be rapidly augmented, "profit inflation" compresses demand to make it adjust to supply. It does so by raising prices relative to money wages, and thereby bringing about a shift of income distribution from wages to profits (whence the term "profit inflation"), which, because a larger share of profits tends to get saved than of wages, has the effect of lowering overall demand.

Now, this demand-compressing effect of a profit inflation can also be achieved through an income deflation imposed on the working masses. For example, if the money wage rate is 100 and the price is 100 to start with, a reduction in the wage rate to 50 with price remaining the same has exactly the same effect of lowering workers' demand as a rise in price to 200 with the money wage rate remaining at the original level.

In the particular case we are considering, a squeeze on the money incomes of a segment of the working population, which also happens to be the consumer of cereals, can make cereal prices fall relative to the money wages of another segment of the working population to which manufactured goods prices are linked. This would both compress cereal demand and also cause the terms of trade between cereals and manufactured goods to shift against the former. In fact even if the manufactured goods' workers also become victims of income deflation, the same result, namely a reduction in cereal demand together with a shift in the terms of trade between cereals and manufactured goods in favour of the latter can follow. Income deflation on a part or the whole of the working population, in short, can both make food shortages disappear and move the terms of trade between food and manufacturing in a direction opposite to what David Ricardo had visualized.

Even though income deflation and profit inflation have exactly identical effects by way of compressing the demand of the working masses, finance capital prefers the deflation to the inflation since profit inflation entails a decline in the real value of financial assets vis-à-vis the world of commodities, and may in extreme situations make wealth-holders turn to holding commodities in lieu of financial assets altogether. Income deflation therefore, even while keeping excess demand in check, exactly as profit inflation would have done, has the added "advantage" of keeping finance capital happy! Not surprisingly, it becomes the preferred means of overcoming food shortages in the era of globalization, which is characterized by the rise to hegemony of a new kind of international finance capital based on a process of globalization of finance .

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[3] See Keynes (1930).

[4] I have discussed the nature of this new kind of finance capital in Patnaik (2000).

[5] This was aggravated by a rush to commodities as a form of wealth-holding by panic-stricken wealth-holders in the immediate aftermath of the collapse of the Bretton Woods System.

The early 1970s were characterized by a tremendous rise in the prices of primary commodities, both in absolute terms and relative to the prices of manufactured goods, owing to an excess demand for such commodities. The subsequent abatement of this inflation, and the shift in the terms of trade against primary commodities other than oil, is often explained as the consequence of a rise in the output of these commodities. But this is untenable. The rise in output, as we have seen in the case of cereals, was absent or insignificant for a whole range of such commodities. Inflation disappeared because it was substituted by an income deflation on the working people over large parts of the world.

II

Three processes leading to income devlation:

- **relative reduction in the scale of government expenditure**
- **the destruction of domestic productive activities under the impact of global competition**
- **long-term shift in the terms of trade against petty producers of primary commodities, particularly the peasantry.**

The primary means of income deflation in the era of globalization—with respect to Third World economies—are the neoliberal policies that come with it. There are at least three processes spawned by neoliberalism that lead to income deflation. The first is the relative reduction in the scale of government expenditure. Globalization, as mentioned earlier, consists above all in the globalization of finance. Huge amounts of finance capital move around the world at a dizzying pace in the quest for speculative gains. Because economies caught in this vortex of globalized finance can be easily destabilized through sudden flights of finance capital, retaining the “confidence of the investors” becomes a matter of paramount importance for every economy, for which their respective states have to show absolute respect to the caprices of globalized finance.

Finance capital in all its incarnations has always been opposed to an interventionist state (except when the interventionism is exclusively in its own favour). An essential element of this opposition has been its preference for “sound finance” (i.e. for states’ always balancing their budgets, or at the most having a small pre-specified fiscal deficit as a proportion of the GDP). The argument advanced in favour of this preference has always been vacuous, and was pilloried by Professor Joan Robinson of Cambridge as the “humbug of finance”[6]. The preference nonetheless has always been there, and has become binding in the era of globalized finance, when states willy-nilly are forced to enact “Fiscal Responsibility” legislation that limits the size of the fiscal deficit relative to GDP. At the same time, this move towards “sound finance” is accompanied by a reduction in the tax-GDP ratio, owing to tariff reduction and to steps taken by states competing against one another to entice multinational capital to set up production plants in their respective countries.

The net result of both these measures is a restriction on the size of government expenditure, especially welfare expenditure, transfer payments to the poor, public investment expenditure, and development expenditure in rural areas. Since these items of expenditure put purchasing power in the hands of the people, especially in rural areas, the impact of their curtailment, exaggerated by the multiplier effects which are also to a significant extent felt in the local (rural) economy, is to curtail employment and impose an income deflation on the rural working population.

The second process is the destruction of domestic productive activities under the impact of global competition, from which they cannot be protected as they used to be in the period of active State intervention, because of trade liberalization that is an essential component of the neoliberal policies accompanying globalization. The

6 See Robinson (1962).

extent of such destruction gets magnified to the extent that the country becomes a favourite destination for finance, and the inflow of speculative capital pushes up the exchange rate.

Even when there is no upward movement of the exchange rate and not even any destruction of domestic activity through the inflow of imports, the desire on the part of the getting-rich-quick elite for metropolitan goods and life-styles, which are necessarily less employment-intensive than the locally available traditional goods catering to traditional life-styles, results in the domestic production of the former at the expense of the latter, and hence to a process of internal "de-industrialization" which entails a net- unemployment-engendering structural change. This too acts as a measure of income deflation.

The third process through which income deflation is effected is a long-term shift in the terms of trade against the petty producers of primary commodities, and in particular the peasantry. What is being referred to here, it should be noted, is the terms of trade movements not between sectors but between classes. Even when there is no shift in the terms of trade against particular commodities, there is nonetheless a decline in the terms of trade obtained by the producers of those commodities because of the increasing hold of a few giant corporations in the marketing of those commodities. This has been a common feature during the neoliberal period, and has the effect, via a shift in income distribution from the lower-rung petty producers to the higher-rung marketing multinational corporations, of curtailing the consumption demand of the former, and hence the level of world aggregate demand, which in turn curtails inflationary pressures on primary commodities themselves.

Globalization in other words unleashes massive processes of income deflation which, while playing exactly the same role as profit-inflation in curbing excess demand pressures, keep commodity prices in check. And this is what we have been witnessing in the entire period between the inflation of the early seventies and the recent revival of inflation.[7]

III

Disturbing aspect of income deflation: unlike profit inflation, which creates an incentive to increase output, it does not have a supply-augmenting effect.

We come now to the disturbing aspect of income deflation. Obviously if there is a reduction of per capita cereal output, then the burden of it has to be borne by the consumers, in particular the working people, either through a profit inflation or through an income deflation. But while a profit inflation, by raising the profitability of foodgrain production, creates at least an incentive for an increase in output, which is all the greater in so far as the terms of trade move in favour of foodgrains and against the manufacturing sector from which some of its current and capital inputs come, an income deflation does not have any such supply-augmenting effect. On the contrary there are at least two distinct reasons why an income-deflation can have a detrimental effect on supplies.

The first relates to the fact that with the income deflation the terms of trade can move, and have moved, against the foodgrain sector and in favour of manufacturing. This, by increasing the input costs relative to final price, has a depressing effect on profitability which is detrimental to output increase. The second relates to the fact

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[7] For a discussion of income deflation in developing countries and in India see U.Patnaik (2003).

that among the victims of income deflation are the peasants themselves, which affects their capacity to increase production, and can make even "simple reproduction", i.e. the maintenance of a given output, difficult for them.[8]

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Income deflation in short has a restrictive effect not only on the demand side but also on the supply side, while the restrictive effect of a profit inflation is confined only to the demand side; indeed on the supply side it has, if anything, an expansionary effect. It was mentioned earlier that the manner in which the decline in per capita cereal consumption was effected in the world economy was as disturbing as the decline itself. The reason lies in the fact that this manner of effecting a decline in consumption, via an income deflation, does not just compress demand, which of course has to be done when per capita output declines; it also perpetuates the tendency towards output decline and hence sets up a vicious cycle that undermines world food security. The neoliberal policies, characteristic of the current phase of globalization, thus have the effect of undermining food security for this reason.

There is however a powerful additional reason as well. Neoliberalism does not just undertake income deflation; it entails a whole arrangement whereby the state withdraws from supporting peasant agriculture and petty commodity production in the name of "leaving things to the market". It entails for instance a winding up of state extension services; a withdrawal of state subsidies, including of cheap institutional credit that used to be given to peasants (and petty producers) either under state directive or by state-owned institutions; a throwing of the peasantry into a direct relationship with the multinational companies *vis-à-vis* which they have unequal bargaining power; and a winding up of the system of procurement operations, which both assured remunerative prices to the peasants and curtailed the amplitude of price fluctuations, thereby reducing risks. When we consider all these aspects, we can appreciate the intimate connection that exists between the neoliberal policies of a globalized regime and the growing hunger that currently afflicts large segments of the world.

IV

We have seen how income deflation (and other policies associated with neoliberalism) affect both the demand and the supply sides in the foodgrain sector. While this fact keeps the sector in a relatively stagnant state, generally without engendering any serious inflationary pressures, even within this state there will be some periods with excess demand and others with excess supply. The inflationary spurt in foodgrains in 2007-08 was one such period when demand might have outstripped supplies, but this situation was severely aggravated by the US government's decision to divert foodgrains for the production of bio-fuels.

There is a view that the inflationary spurt can be explained by the excess demand arising from the fact that in rapidly-growing developing economies like China and India, a variation in the dietary pattern is taking place, entailing an increased demand for commodities like meat, the production of which requires more

8 Since in a state of simple reproduction there is no net investment in the sector as a whole (otherwise there will be expanded reproduction), the entire net output is consumed by the producers. When simple reproduction itself becomes difficult, that means that the producers cannot maintain even their existing level of consumption over time. The mass suicide of peasants in India and elsewhere in the period of globalization suggests that this has been the case.

foodgrains in the form of animal feed. But this is a completely untenable explanation.

No doubt the rich in both these countries are diversifying their diet and are absorbing, directly and indirectly, more foodgrains per capita. But if we take the per capita foodgrain absorption for the population as a whole, both directly and indirectly (via processed foods and animal feed), then we find that in India there is a decline compared to the late eighties.[9] Even in the case of China if we take the per capita absorption of cereals for food and feed (the definition of foodgrains is different in China compared to India), then there is a steady and sharp decline between 1996 and 2003, which gets reversed thereafter, but the level in 2005 is still lower than in 1996.[10]

Since the rate of growth of population in both these economies has been slowing down, the decline in the per capita foodgrain absorption entails a decline in the rate of growth in the overall demand for foodgrains. In the face of such a decline, it follows that—if excess demand pressures arise in the world foodgrains economy—then the reason must lie in an even more rapid decline in the rate of growth of the supply of foodgrains. Hence it is not from the side of Indian or Chinese demand but from the side of foodgrains supply (including the reduction in supply owing to diversion for bio-fuels) that we explain the food scarcity in the world economy in 2007-08.

It follows from the foregoing that the elimination of world hunger requires—apart from eschewing arbitrary diversion of foodgrains for use as bio-fuel—an increase both in the demand and the supply of foodgrains in the world economy. For this it is essential to overcome the financial regime that promotes income deflation and the withdrawal of state support from the peasant and petty production sectors. The current recessionary crisis, itself a fall-out of this financial regime, provides an opportunity to put in place an alternative regime that is more conducive to overcoming world hunger. Let us examine this alternative.

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V

Getting out of the present recessionary crisis requires an injection of demand into the world economy through larger state expenditures financed by enlarged fiscal deficits. If even a part of this enlarged world fiscal deficit is devoted to expenditures for increasing world foodgrains production, then the process of recovery from the crisis will simultaneously entail larger foodgrain production. True, there will be a time-lag between the expenditure devoted to increasing food production and the actual increase, during which there may be food price inflation. But as world foodgrain stocks are fairly comfortable at the moment, such inflation can be kept in check.

The very process of undertaking expenditures for increasing foodgrain production, which will have to focus on Third World countries, will put purchasing power in the Third World countryside. The demand for food generated by this will be immediately met by running down world food stocks, which will get replenished as

[9] See U.Patnaik (2008).

[10] I am grateful to Sriram Natarajan for making his research on China's foodgrain absorption figures available to me.

food output increases over time. And if this process continues then we shall have a reversal of the vicious cycle caused by income deflation: both demand and supply of food will rise over time, causing a progressive amelioration of world hunger.

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Many have argued that overcoming the current recessionary crisis without recourse to protectionism, requires a coordinated fiscal stimulus among a number of major countries, a suggestion that had been originally put forward during the Great Depression itself by a group of German trade unionists and also by John Maynard Keynes. If a specified percentage of the increased government expenditures in these major countries which would be incurred as part of the fiscal stimulus is made available as grants to the developing world, on the condition that these grants should not be simply added to foreign exchange reserves but should be used to sustain larger public expenditure—through enlarged fiscal deficits in the recipient countries for increasing food production and for improving the living conditions of the working people—then a number of objectives can be simultaneously achieved. First, there will be a direct improvement in the conditions of the working population, through larger healthcare, education, sanitation, housing, infrastructure and other facilities. Secondly, there will be a larger demand for foodgrains, directly because of the multiplier effects of the larger public expenditure, and indirectly because some of the current expenditure of the working population on the exorbitantly expensive healthcare and education facilities (the only ones they can currently access) can be released for the purchase of foodgrains once cheaper public facilities become available. And thirdly, there will be a larger supply of foodrgains over time. The improvement of food security in the Third World that will come about as a result, will of course improve world food security.

In addition to the above (or in lieu of it if the above is not accepted), there can be another arrangement, namely that the entire increase in current account surplus which will come about as a result of the coordinated fiscal stimulus, can be mandated to be given as grants to the developing world, again on the condition that it is not simply added to foreign exchange reserves but spent—among other things —on improving food security and conditions of life for the working people.

There is an obvious justification for this: in the absence of a coordinated fiscal stimulus, the increased current surplus would not have arisen at all. In other words, if a habitually-surplus country simply enlarged its own government expenditure, then the most it could hope for is no worsening of its balance of payments compared to the initial situation. If it gets an additional surplus over and above what it had to start with, then that is entirely because of the fiscal stimulus undertaken in other countries. Its enlarged current surplus in short is a booty that lands on its lap because of the actions of other countries. If this surplus is taken away from it, then its employment and output would still remain unchanged, but it would simply have been divested of this booty. Of course it is free to use this booty for raising the consumption of its own working population, but in that case there would be no surplus left afterward. If there is a surplus, then clearly it comes from holding on to the booty thrown on to its lap by the actions of other countries. A case exists for divesting it of this booty.

With these grants, the demand for imports—now emanating from the less developed countries—will increase. And no matter which countries this import demand is directed to, it will succeed in eliminating all increases in surpluses and deficits. If the increased current surplus, say US$100, which is given as grants, is used to buy goods from the countries whose deficits had increased (and they would have increased by exactly US$100 from the initial situation), then the increased deficit would have been simply wiped out. If on the other hand the grant of US$100 is used to buy goods from the increased-surplus countries, then they would be redirecting their sales from the increased-deficit to the grant-receiving countries, which again would wipe out the deficit of the increased-deficit countries. Whichever way we look at it therefore a system of such grants will not only raise world output and employment, but also eliminate all increases in the net indebtedness of countries relative to the initial situation of recession. The grant-receiving countries will not get into debt. What would otherwise have been increased-deficit countries on account of the coordinated fiscal stimulus will have this increased deficit wiped out; and so therefore would the increased surplus countries.

The recession entails, by its nature, a generalization of hunger among the world's population because of the generalized income deflation it gives rise to. But after the recession is over, since the increase in employment will mean that the newly employed would have shaken off the income deflation to which they had been subjected during the period of their unemployment, the rest of the world's population will feel the impact of hunger even more acutely. To prevent this from happening, there has to be an increase in the rate of growth of world food output, which alone can promote world food security. The very mode of overcoming the recession therefore should be such that in the process food security is promoted. The system of grants should be used for this purpose as far as possible. Our collective concern over the problem of hunger requires that proposals such as the above, which reverse the vicious cycle of food insecurity to which the working population of the world, especially the Third World, has been subjected during the neoliberal regime that has imposed income deflation upon it, are urgently implemented.

There has to be an increase in the rate of growth of world food output, which alone can promote world food security.

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