CHAPTER 10

SUMMARY AND CONCLUSIONS

Inflation is one of the most perplexing economic phenomena. On the one hand, all inflations have the same monetary appearance, that is, they all involve an expansion in the amount of money relative to the quantity of commodities and an increase in the money prices of goods and services. From this perspective, there seems to be no fundamental difference between the European inflation of the 16th century, the German inflation of the 1920s, and the U.S inflation of the 1970s and early 1980s. On the other hand, every one of these inflations was part of a unique historical context. In the 16th century, inflation emerged with the first steps of European capitalism, creating a unprecedented income redistribution from wages to profits; in the German episode of the 1920s, inflation arose from the aftermath of a world war, eliminating the national debt and leading to a massive redistribution of wealth; finally, in the recent U.S. case, inflation developed amidst a major restructuring of corporate power and a far-reaching realignment of international economic institutions. It is hence clear that, while inflation is always and everywhere a monetary phenomenon, its institutional and structural essence is never the same.

In a way, we are faced here with a basic question which has bothered philosophers since Aristotle and Plato: the fundamental duality of *form* and *content*. For the economist, the problem arises because the formal definition of inflation is always the same, while its institutional and structural context is forever changing. Against the *static monetary form* of inflation stands its *dynamic social content*; below the *universal appearance* lies a *concrete historical essence*.

The standard way of dealing with this central duality is to ignore it. Most theories begin by assuming that the monetary process of changing prices is also the essence of inflation, that is, by seeing the form of inflation as its very content. From this perspective, the structural and institutional context is merely an exogenous variable, something which could help us explain the inflationary process but is

not an integral part of that process.

Our own approach in this work was to treat inflation as a process of restructuring. Instead of separating form and content, we sought to define the form of inflation in terms of its own content. Contrary to the macroeconomic and structural literature which start from the process of changing prices and then try to explain it through functional relationships with other variables, we proposed to begin by defining inflation as a dynamic interaction between business and industry. For us, the rate of change of prices was largely a corollary of the more fundamental social process in which industrial development is subjugated to business ends. In this framework, inflation is seen as a double-sided process in which the expansion of monetary values in the business sphere hinges on the strategic limitation of production in the industrial sphere, while the control of industry depends on the dynamic restructuring of business institutions. The temporal interaction between these spheres of socio-economic activity is not the 'cause' of inflation, but rather its very essence. In other words, *inflation is always and everywhere a process of dynamic restructuring*. From this viewpoint, the historical evolution of social structures and institutions is not only the explanation of inflation, but also its own description.

As we demonstrate in the first part of our thesis, the basis and implications of this new analytical framework are contrary to some of the fundamental methodological tenets of existing inflation theories. In the macroeconomic literature examined in Chapter 2, the emphasis is on forced deviations from a natural state of full employment and price stability. Since the late 1950s, modern macroeconomics evolved as a love-hate affair with the Phillips Curve. While most writers attacked Phillips' original construct, their criticisms sought to repair rather than impair. The common thread going thorough much of this literature is the desire to 'augment' the basic equilibrium framework with a set of disequilibrating 'imperfections' which temporarily throw the economy off its normal state of stability and desirability. This notion of separating the ideal world of supply and demand from real-life 'distortions' was already evident in Phillips' own article and in the subsequent elaborations by Lipsey and by Samuelson and Solow. Since then, the method of 'forced deviations' has reappeared in various forms, such as the aggregate view of market imperfections proposed by Perry, the informational imperfections stressed by Friedman and Phelps, the random-error school of rational expectations led by Muth, Lucas, Sargent and

Taylor, the institutional imperfections and cultural inertia underscored by Friedman, and the destabilizing menace of exogenous forces accentuated by Blinder and by Bruno and Sachs. The fundamental weakness of these explanations stems not from their lack of 'realism' but rather from perceiving real structures and institutions as extra-economic distortions.

In contrast to the macroeconomic literature, the market-structure approach to inflation examined in chapters 3 and 4, takes the realistic features of modern capitalism not as an 'imperfection,' but as its basic point of departure. While mainstream macroeconomists focus mainly on growth inflation and blame it on various externalities, the structural theorists concentrate on stagflation which they trace to the dual-market organization of modern capitalism. Starting from a basic distinction between market prices and markup pricing developed in the 1930s, structural theories tend to perceive inflation as a dynamic transmission of demand, cost or profit signals. Galbraith, for example, suggested that because of their sluggish reaction to growing demand, giant firms introduced a moderate but persisting inflationary bias which tended to continue throughout the entire cycle. The 'normal-price hypothesis' as developed by Coutts, Nordhaus, Godley and Moreno-Brid, on the other hand, argued that modern firms were impartial to demand signals, and that their prices were set as a fixed markup over 'normalized' cost. Taking the normal-price hypothesis a step further, writers such as Encaoua and Geroski tried to demonstrate that the extent of price smoothing depended on the degree of competition in the underlying industries. Another view on the relationship between market structure and inflation was proposed by Ackley, Kaldor and Sylos-Labini, whose separate analyses accentuated the role of 'pull-push' spirals. In their opinion, the inherent imbalance between competitive markets for raw materials and concentrated markets for finished products, together with the post-1970 destabilization of global financial markets, created an inherent tendency for a ratchet-like interaction between demand-pull and cost-push inflations. Another branch of this literature looked for the primal ignition spark behind the inflation spiral. According to authors such as Weintraub or Wiles, the inflation stimuli originated mostly from wage demands, while others, like Blair, emphasized the primary role of fixed short-term targets for profits. Finally, there were also those, such as Eichner and Kotz, who accentuated the inflationary impact of rising profit targets.

The market-structure literature offers valuable insights into the inflationary process but it also suffers from certain fundamental shortcomings. Much like mainstream macroeconomics, it, too, takes the structure of society as exogenously given and focuses on price and inflation as the main variables of interest. Given this emphasis, it is then hardly surprising that authors of the market-structure literature find it necessary to assume that there are fixed rules of conduct and stable equilibrium relationships which translate changes in exogenous conditions into predictable price movements. Unfortunately, this presumption serves to remove the very possibility that inflation and structural change are two sides of the same process. The common insistence on fixed profit markups negates the primacy of income redistribution as a fundamental process of inflationary restructuring. Even those who emphasize the inflationary role of changing profit targets, tend to anchor their theories in arbitrary rules of conduct and fail to integrate them into a broad framework of structural change.

The structurally-static nature of existing inflation theories stems, to a large extent, from their common utilitarian categories. All existing schools view inflation as a process of changing commodity prices and, although some of them argue that the world of commodities is also a reflection of social relations, they all tend to *measure* those prices as if they were rooted only in the material world of production and consumption. The main problem of measurement is to convert the qualitative diversity of commodities into universal quantitative units and, as we demonstrated in Chapter 5, this could be done only under rigid neoclassical assumptions. Indeed, the main works in this area (such as those written by Court, Dhrymes, Fisher and Shell, Griliches, Hofsten, Lancaster, Stone, Triplett, and Ulmer, as well as the recommendations of the U.S. Price Statistics Review Committee and the United Nations) all indicate that the existing indices are inadequate under alternative, non-neoclassical conditions. Unless we have an atomistic society of rational, utility-maximizing economic agents, unless these agents are organized in perfectly competitive markets and unless they interact in a constant state of equilibrium, the price and quantity indices tend to break down.

But if these indices require the *a*-historic harmony of a static world, how useful are they for the dynamic context of a power-oriented capitalist society? How meaningful are the Consumer Price Index, the Investment Price Deflator, or the GNP measured in 'constant' prices within the antagonistic setting

of collective action, where corporate coalitions, labour unions and politicians are interlocked in a hostile distributional struggle? How relevant are these indices when we substitute tacit coercion and open persuasion for autonomously determined human needs? Can we still use such indices when, instead of equilibrium and stability, there is constant flux and structural change? If the answer is negative, we have no choice but to look for another framework for inflation, one which will integrate the historical content of inflation into its very definition.

The second part of our thesis was an attempt to develop such a new framework. Whereas the common approaches emphasize static structures, we accentuated continuous structural change; against the distinction between monopoly and competition, we proposed a duality of cooperation and conflict; instead of separating the 'real' from the 'nominal,' we linked the world of industry with the institutions of business; in lieu of the atomistic actor and individual action, we started from the group and collective action; in place of passive reaction in a given structure, we looked for deliberate initiative to restructure.

Our analysis of inflation *as* restructuring began from the writings of Thorstein Veblen and Mancur Olson, who, each in his own separate way, stressed the significance of structural change for economic analysis. Writing during the emergence of large-scale business enterprise, Veblen offered a new interpretation for the concept of capital. Contrary to the neoclassicists and Marxists who sought to deduce the pecuniary value of capital from its *productive* essence, he insisted that capital was a purely business magnitude whose value depended on its *negative* industrial impact. The value of capital was a capitalization of earning capacity and, according to Veblen, business earnings depended on distributional, not productive powers. For the businessman, the capacity to appropriate earnings hinged on his strategic control of industrial activity, so the value of capital was in fact a capitalization of 'industrial sabotage.' In the context of rapid technological progress and limited population growth, the power to restrict industrial activity below its full capacity depended on the constant restructuring of political and economic powers, or on what Olson called the 'accumulation of distributional coalitions.'

Taking this as our tentative point of departure, we argued that, under the new order of large-scale business enterprise, the process of capital accumulation manifested itself in two main ways.

On the structural level, there is a constant formation and reformation of business arrangements, mainly through the ongoing process of mergers and acquisitions, which leads to increasing corporate diversification and rising aggregate concentration. The consequences of this restructuring are revealed on the macroeconomic level in the form of lingering stagnation and ongoing inflation. The extent to which business restructuring raises the profits of the large coalitions depends on the ability of these coalitions to limit the overall growth of industrial capacity below that of the market, while their success in doing so is capitalized in the form inflated asset values. In other words, under mature capitalism, the process of capital accumulation tends to appear on the one hand in the form of growing aggregate concentration and a progressive consolidation of corporate coalitions, and on the other hand in the form of persisting stagflation.

From this perspective, it is clear that inflation involves much more that changing prices. If we define the overall price level as a ratio between the total money values in the business sphere and the aggregate congeries of commodities in the industrial sphere, it turns out that the rate of inflation is in fact a universal imprint of a concrete historical process, in which the changing institutions of business enterprise interact with the varying conditions of industrial production. What is needed, then, is a new definition, one which describes the form of inflation in terms of its own historical content. In Chapter 7, we proposed to do that by replacing the standard 'multiprice' definition with an alternative, double-variable index reflecting the 'value-quantity' aspect of inflation. In this new index, the rate of inflation is given by the difference between the rate of change of a business-sphere variable, such nominal GNP or corporate sales, and the rate of change of an industry-sphere variable, like output or employment. The 'multiprice' and 'value-quantity' representations reflect the same inflationary process, but while the former focuses only on the price outcome, the latter also enables us to examine the underlying 'business-industry' origin. Indeed, using these new spectacles, it appears that stagflation is not a new phenomenon at all. By decomposing U.S. inflation into its 'business' and 'industry' components, we showed that, since the late 1940s (and most probably, since the beginning of the 20th century), the ongoing pecuniary expansion in the business sphere was accompanied by a persistent stagnation in the industrial sphere. In other words, contrary to the common wisdom and in line with our own hypothesis, it seems that the combination of inflation and stagnation is not an anomaly, but rather an integral part

of modern capitalist development.

Underneath this stagflation lies the dynamic process of corporate restructuring to which we turned in Chapter 8. According to our general framework, the inflationary interaction between business and industry appears together with the ongoing structural transformation of business arrangements, which is in turn reflected through the process of aggregate concentration. In operational terms, we started from the basic dichotomy between the 'core' and 'periphery' of a given corporate universe. Based on this distinction, we defined the rates of aggregate concentration and dispersion for any given variable as the respective distributive shares of the core and periphery in the overall value of that variable. Focusing specifically on sales and employment, we demonstrated that, for each group of firms, the rates of growth of sales and employment affected both their own rates of inflation, as well as the underlying rates of aggregate concentration and dispersion.

Using this analytical framework for inflationary restructuring, we then turned to examine the post-war experience of the U.S.-based manufacturing and mining sector. Our empirical analysis revealed two basic inflationary regime. It showed that, during the 1950s and 1960s, the combination of low price inflation and limited industrial stagnation was affected by a growing aggregate concentration for sales and an even faster increase for employment. The severe stagflation of the 1970s and 1980s, on the other hand, involved a different pattern of restructuring, with relatively little change in the aggregate concentration for sales and declining aggregate concentration for employment. These structural transformations also brought changes in the relative inflationary contributions of the two groups, with the role of the large firms rising very rapidly since the early 1970s.

To understand the reasons behind these historical developments, we tried in Chapter 9 to anchor them in the process of capital accumulation. After we decomposed inflation into a dynamic interaction of business and industry, and after we took this interaction further by identifying the distinct components of the core and periphery, our last step was to examine characteristic developments for a 'typical' large and small firm. We argued that large firms were preoccupied with *differential pecuniary accumulation*, that is, with increasing the nominal value of their assets faster than the average for their

corporate universe. To do that, the large firms must either broaden their differential 'breadth' of accumulation by raising their employment faster than the average, and/or increase their 'depth' of accumulation by raising their profit per employee faster than the average. The choice between these alternative strategies bears on the inflation process, with differential expansions in the breadth of accumulation leading to low inflation and relatively moderate stagnation, and attempts to raise the differential depth of accumulation creating a strong stimulus for stagflation.

For the large firms of the manufacturing and mining sector, we found that, during the 1950s and 1960s, differential pecuniary accumulation was affected mainly by the rapid process of mergers and acquisitions. By taking over periphery firms, the core corporations were able to achieve a brisk differential expansion in their breadth of accumulation, thus limiting their need for inflationary increases in their depth of accumulation. Indeed, for those firms, following fixed-markup formulas during that period helped minimize risk, which increased their differential rate of accumulation even further. Over time, the rates of aggregate concentration for sales tended to rise, but since the increase in the aggregate concentration for employment was even faster, the rate of inflation in the core was kept below that of the manufacturing and mining sector as a whole. When the merger wave receded in the early 1970s, however, the core firms felt compelled to boost their differential depth of accumulation, thus leading to the onset of a growing inflationary spiral and a rapid redistribution of income from labour to business. The consequence was a severe decline in aggregate demand which, together the progressive penetration of imports, forced the core firms to drastically cut their industrial base and accept lower rates of aggregate concentration for employment. On the macroeconomic level, the result was a transformation to a much more unstable regime, characterized by a combination of higher rates of inflation and unemployment.

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Our basic claim that inflation is always and everywhere a phenomenon of structural change is not a specific hypothesis but a general framework for analysis. Our own emphasis in this work was only on the process of capital accumulation, as it manifested itself through the dynamic interaction between

business and industry, and through the formation and reformation of business coalitions. Furthermore, we focused on a particular sector within a single country, during a relatively short period of time. Given these limitations, it is clear that our work could be viewed only as an initial step. From a historical perspective, one could extend this framework to look backwards into the structural transformation of early capitalism, or to speculate on its future development into the 21st century. In a geographical context, it could be broadened to examine the experiences of other countries, or be expanded to study the global aspects of inflationary restructuring. And finally, if we are to gain a better understanding of inflation, we may also wish to include in our framework other structural processes, such the evolution of the modern state and the role of government policies.