Inflation, Politics, and Social Change*

Institutional and Theoretical Crisis in Contemporary Economy-and-Society

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Introduction

Inflation at a very high rate, or even at a moderate rate for a long period of time, is closely linked to sociopolitical crisis. This is most obvious in Third World countries, but also increasingly apparent in the case of industrialized countries, particularly when inflation can only be regulated at the substantial cost of high unemployment and the underutilization of production capacity. Economic advisors and political leaders have failed thus far to come up with a coherent counter-inflationary strategy, one effective as well as politically sustainable over the long-run.

This paper stems from a long-term, comparative and multi-disciplinary project to investigate inflation as well as stagnation processes in several industrialized countries. We posit that inflation results from institutionalized societal conflict over the distribution of income. The state, unable to resolve these conflicts, accommodates them—with the intentional or unintentional cooperation of the banking system—through an expansion of credit and of the

* This is an abridgment of a paper presented at the Xth World Congress of Sociology, Session on Economy and Society, Mexico City, August 16-20, 1982. The full-length version, along with other reports on international inflation, are found in T. Baumgartner, T. R. Burns and P. DeVillé, The Shaping of Socio-Economic Systems, Gordon and Breach, New York, 1984. A large part of Part III of the paper appeared in our collaborative article (Baumgartner et al., 1982).

The research reported in this article has been supported by the Social Science Research Council (HSFR) of Sweden.
money supply at a rate in excess of what is necessary to finance the actual increase in the production of marketable resources.

In Part I we suggest why contemporary economic theory and policy are incapable of dealing with the current crisis and indicate the requirements for a new paradigm. Part II singles out some of the societal developments which have made inflation endemic in modern capitalist societies and which limit the capacity of the welfare state to regulate inflation and at the same time prevent economic stagnation. Part III presents preliminary conclusions from our research in the form of eight theses about inflation. We go on to point out that the present monetarist revival, and its political advocates in the form of Thatcherism and Reaganomics, will be unable to provide a long-term solution to inflation. Other policy approaches are necessary which go to the heart of the present crisis and the struggles over income, nationally and internationally.

Old and New Paradigms

Contemporary economic theory and policy is incapable of dealing successfully with the current crisis of stagflation. There exists a serious, irredeemable mismatch between economic models and actual economic and sociopolitical conditions and developments. Such models can neither make intelligible the role of sociopolitical and institutional factors in inflation and stagnation, nor provide a basis for effective policy and strategy.

Some economists have recognized the importance of such sociopolitical and institutional factors,¹ yet none has tried to initiate a radical restructuring of the conceptual and analytical apparatus of economic theory. Economists remain largely content to retouch the margins, whereas it is the core that needs rethinking. At most they engage in policy analysis which remains completely separated from the analytical core of economic theory.

In Section 1 we suggest why contemporary economic theory and policy is incapable of dealing with the current crisis. In Section 2 we go on to indicate several of the questions which a new theoretical framework or paradigm should address.

The Failure of Contemporary Economic Theory and Policy

The capitalist economies up to the 1930s were shaken by recurrent depressions. The greatest crisis of them all, the world depression of the 1930s, led to the introduction of "New Deal" programs in various Western countries in order to alleviate or counteract tendencies towards overproduction and stagnation, falling investment, bankruptcies and unemployment.

The Keynesian theoretical framework provided a model and guidelines for social policy, which to a greater or lesser extent "worked," more effectively in some countries than others.

It should be stressed from the outset that the Keynesian framework took certain societal conditions for granted. It assumed that the institutions essential