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Asia's Financial Crisis, Speculative Bubbles, and Under-Consumption Theory

Jonathan E. Leightner

One hundred and ten years ago, A. F. Mummery and J. A. Hobson wrote, "the East-end problem, with its concomitants of vice and misery, is traced to its economic cause, and that this economic cause is the most respectable and highly extolled virtue of thrift" [Mummery and Hobson 1889, 99; here after cited just by page number]. During the Asian miracle, economists praised Asia for its high savings rate. In direct contradiction to this previous praise, I will argue that Mummery and Hobson's "under-consumption" or "over-savings" theory explains an important part of the Asian crisis. Furthermore, if Mummery and Hobson are correct, then economists need to make significant modifications to their macroeconomic models and to their policy prescriptions.

Under-Consumption and the Asian Crisis

The core of Mummery and Hobson's Under-Consumption Theory relies upon a realization that consumption (not saving or investment) is the economic force that leads to community prosperity. Here "consumption" means what modern macroeconomists call "final demand sans investment." Thus, "consumption" includes government purchases of final goods and services and exports in addition to the purchases of consumers. The demand for investments, whether in the form of intermediate goods or additional capital, is derived from consumption. If no one buys the additional goods produced from saving/investment, then society has accrued all of

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