

A WORLD BETWEEN CRISES

(An Essay)

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One of the most often committed mistakes in economic reasoning is the supposition about the continuity of economic processes. However, what dominates in reality is a process of permanent changes, which sometimes proceed in a cascading manner rather than linearly. It must be acknowledged that the capitalist market economy by its very nature is involved in periodical crises. They must occur from time to time, yet the magnitude of the recent crisis is a result of inappropriate institutions and wrong macroeconomic policies based on neoliberalism. While the underlying causes of the crisis and the ways out of it at the era of interdependent global economy is discussed vividly in countless books and papers, yet it ought to be clear that the world is moving from one crisis to another. Thus, one must consider not only the economics of crisis, but also a kind of crisis of economics. There is a need for a New Pragmatism, based on the better understanding of economics as science, describing the economy as a system of forces and flows which constantly give feedback and influence each other.

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The world is changing. Continuously. One may say that the world is volatile (Kolodko 2011). The second decade of the 21st century began quite differently than the first, when the situation of the global economy and of mankind was unlike the one at the beginning of the last decade of the past century. The level of

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production is much higher and its effects are distributed differently, more unequally. Also the model of planetary economy, ever more interdependent by means of numerous cultural, political, and economic ties, has changed. And, finally, there has been a demographic growth. A population of 5.3 billion 20 years ago grew to 6 billion 10 years ago, and has now reached 7 billion. From this perspective, one must look at what is happening in the global economy in a different, new way, as it refers to an ever growing number of people inhabiting the Earth.

The last two decades – marked with the overlapping specific coincidence of megatrends of an epoch-making format – globalisation, technological revolution, post-socialist transformation, liberal political and cultural breakthrough have lulled a considerable part of the social sciences in academia and, what is important, politicians into security. Although it quickly turned out that there is no end to history (Fukuyama 1992) and that such an end is not even forthcoming because history may only end with the end of civilisation, until 2007, there was a general optimism as regards the anticipated future. Very often, this optimism was quite naïve. At the same time, sufficient criticism to the predominant trend in the interpretation of socio-economic development was lacking, without which one can hardly expect a long-term progress. In fact, due to the ever spreading shadow of neoliberalism, the moth's flight into the fire continued, although hardly toward 'the clash of civilisation' as envisioned by Huntington¹ in response to Fukuyama, but towards an extensive global economic crisis, the implications of which extended far beyond the realm of economic relations, on a scale previously unencountered in history, because it affected not only the universal correlative economy emerging from globalisation, but also an extremely large number of people.

Globalisation is a long-term and spontaneous (or even chaotic) process of liberalisation and the concomitant integration of the previously independently functioning markets of national economies in one inter-dependent worldwide market. In this case, integration refers not only to the markets of goods, but also to capital, including the intensively liquid financial capital of recent decades, whilst manpower markets became liberalised and integrated much slower. This alone contributes to the specific dichotomy of the globalisation process: it does not offer the same opportunities to all, and neither are all equally burdened with the concomitant costs.² First of all, however, globalisation has not yet caused emerging of a planetary system of economic policy coordination.³

¹ Huntington first presented his hypothesis in "The Clash of Civilizations", an article published in Summer 1993 in the *American Foreign Affairs*.

² See more *inter alia*: Hutton – Giddens (2000) and Kolodko (2000).

³ Discussed in more detail, among others, by Stiglitz (2002).

Literature concerning globalisation is abundant. Of course, there are authors who strongly defend the process (World Bank 2002). This is understandable as far as the good aspects of globalisation are highlighted. Thanks to this process, through opening and integration, the markets have expanded and production costs have dropped; the free flow of direct investments is the main transfer channel for new technologies and it has contributed to the extremely rapid spread of technical progress; transfers of portfolio equity may support the financing of the deficits in countries that were unable to scrape by in a short period of time; the easier migration of people contributes to the relative reduction of income inequalities⁴ and, in the long run, it promotes an increase in human resources quality through the growth of qualifications.

On the other hand, there are apologetic works that ennoble the contemporary, worldwide capitalism (Norbert 2003; Bhagwati 2004), which certainly solves a spate of problems, but simultaneously creates a similar or even higher number of new ones.⁵ At the turn of the first decade of our century, we are definitely facing more problems concerning the conditions, mechanisms, and results of both short-term reproduction and long-term social and economic growth. And all that because of the 2008–10 crisis.

The 2008–10 crisis? This is how it will perhaps be referred to, similarly to its well-known predecessor eight decades ago, between 1929 and 1933 – the Great Depression – albeit in both cases, the roots can be traced to phenomena and processes that took place earlier, whilst their effects and implications occurred and will occur later.

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The recent years have been quite a shock to many. People were deprived in a violent and surprising way of their illusions. The illusion of the alleged, even if not of the perfectness and, later, of the reliability and functionality of capitalism, which inevitably also showed – not for the first time and neither for the last – its other face. Of course, we can and certainly should take care of cultivating the change

⁴ Relative as, eventually, the inequalities grow. However, migration from countries where income is lower to economies where one earns more reduces the supply of manpower in places that are abandoned and thus, in the long run, wages grow faster there, while the increase of manpower supply reduces wages or frequently only the rate of their growth in places to which people migrate. And so, in the decade between 2001 and 2010, wage differences between Central and Western Europe or between Mexico and the USA dropped more than with reference to the *per capita* GDP.

⁵ As regards the nature of globalisation and its multiple consequences for production, accumulation, trade and consumption see, among others, Kolodko (2003, 2005); Wolf (2004); Stiglitz (2006).

for: positive and advanced aspects of capitalism, using the good sides of the capitalistic market economy, now worldwide.

Many studies criticising or even condemning contemporary capitalism as a system that is faulty, unjust or downright inefficient will be written. Some have already appeared. More papers will be published in an attempt to defend the system from criticism and trying to help it escape from responsibility for the extremely costly disturbances observed in the global economy. They have been published already. In the first case we deal with going too far to criticism with no ability to point different ways of the economic journey toward future.⁶ In the other, it is the system's apologetics that prevails, although the system did not succeed and surely the present crisis cannot be interpreted as an accident at the free market workplace. Attempts are being made to shift the responsibility – both intellectual and political – onto others. No wonder; it always happens in hard times and our time is hard.

Compared to the above, the book written by two American authors, Nouriel Roubini of New York University and Stephen Mihm of the University of Georgia, is a considerable contribution (Roubini – Mihm 2010). It is, with no doubt, the best book presenting in a reliable way the nature of current global economy. Of course, there are more papers discussing its nature⁷ – and there will be still much more – however, none of them has shown the predispositions, dynamics and effects of crisis in such a pertinent, detailed and accurate way.

The authors have achieved all that thanks to skilful interweaving of contemporary and historical threads, macroeconomics and microeconomics, and finally, political economy. More importantly, they do not remain sandwiched in the jacket of narrowly interpreted economic analysis but they get around with great scholarship and intellectual proficiency at the border of economics and other related fields of social sciences, in particular political sciences, as well as elements of sociology and psychology. They are not orthodox; in their explanation of the essence, they reach different theories and economic schools. Therefore, it is a work with interdisciplinary and holistic aspirations saying something substantially new and sound at the same time.⁸

What is more, the book is by no means boring. It is written brightly, using vivid language; the style of narration attracts the attention of readers. One may say that they get around perfectly in the crisis of space and time. Since it is neither the first,

⁶ This is how one may describe, *inter alia*, the popular work by Klein (2008).

⁷ See, *inter alia*, Zakaria (2009); King (2010); Bremmer (2010); Legrain (2010); Rajan (2010); Stiglitz (2010).

⁸ I have discussed in detail the imperative of such a methodology approach in the modern economy, simultaneously using it to construe the long-term development processes (Kolodko 2011).

nor the last crisis we experience. One of the reasons for this might be the fact that one of the authors, Stephen Mihm, is an economic historian; but also because the current crisis cannot be reasonably described without a historical comparative analysis. And thus, the authors often take their readers on a journey into other, sometimes very immemorial times, while simultaneously diving into the classical work by Kindleberger (1978). They do this because they want to demonstrate that the history of economy is indeed a history of crises. At least ever since capitalism supplanted feudalism.

There is no capitalism without the cyclicity of the process of macroeconomic reproduction. There is no market economy without periodical crises. There is none and there will be none. The authors prove that in an unchallengeable way. They are not the first, though. They do not fear to remind us that this was first demonstrated 150 years ago by Karl Marx (1867),⁹ and then proven once again by John Maynard Keynes 70 years later.¹⁰ Although, they drew completely different conclusions from their considerations on the immanent crisis-generation of capitalism: Marx suggested the inevitability of the collapse of capitalism and the imperative of replacing it with intentionally non-crisis prone socialism (communism), whereas Keynes gave hints how to save capitalism from self-destruction. Nevertheless, neither of them (and they were not the only ones) ever had any illusions as regards the capitalistic idyll. It is also surprising that so many people – including intelligent economists and politicians – were fascinated by the myth of the relatively harmonious functioning of the market economy. The more they were enthralled, the more they should be disappointed now. Of course, if they are not victims of a doctrine and dogmas, which unfortunately happens quite often in economics – a science dealing with values and ideas on the one hand, and stuck in a sea of conflicting interests on the other...

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The craftsmanship of Roubini and Mihm (2010) hinges on a perfect combination of the past and the future. The authors use historical analysis – and I believe this is necessary not only in this case – not as a tool for an intellectual discussion on the past, which may in itself be fascinating,¹¹ but as a tool to show the present. They escape the risk of extrapolation, an error which frequently happens in economics: it has been, it is, hence, consequently, it will be so. Well, not really, as the pro-

⁹ Marx's seminal work, *Das Kapital: Kritik der politischen Ökonomie*, was first published in 1867.

¹⁰ This fundamental work by Keynes was published in 1936.

¹¹ See, *inter alia*, Landes (1999); Friedman (2005); Talbott (2008).

cesses of macroeconomic reproduction are not absolutely continuous. Being more precise, we experience overlapping and infiltration of continuity and change. Yet another coincidence in time and space. Things happen the way they do because many things happen at the same time. The future is not a simple function of a trend,¹² and because of the nature of long-term development processes (and, from time to time, stagnation or even regression), it cannot be such a function.

The extrapolation error underlies the fact that it is Roubini who is successful around the world as the person who “foresaw the crisis”. This is true, although he was not the only one. Nevertheless, he was determined to present his opinions – unconventional as they were at that time and place, the time of boom of the supposedly harmonious market – in the cradle of financial orthodoxy, both theoretical and practical. With his evidently unchallengeable arguments, he demonstrated in the lion’s den, i.e. on Wall Street and at the International Monetary Fund, that the financial market, particularly in the USA, was an overinflated bubble already in 2005–06, and the air forced in it increasingly contaminated. In the middle of the past decade the financial bubble was already full of “securities” that were no more secure or trustworthy capital investment and that proved to be of low value or even worthless over time.

Roubini (2004) understood that and tried to share his argumentation with circles that were able to make something rational through adequate reaction of economic policy. As regards the USA, it was mainly about actions in the area of the central bank’s monetary policy, i.e. the Federal Reserve System, the FED, and in the government’s fiscal policy, i.e. the administration of President George W. Bush. Exactly two years before the collapse of Lehman Brothers, one of the flagships of Wall Street, at a seminar organised in September 2006 at the IMF, Roubini tried to persuade his audience of the inevitability of the upcoming crisis. No one listened to him, especially as a few streets away, the management of the FED, then under the excessive influence of monetary orthodoxy on the one hand, and under preponderant pressure of special interest groups of Wall Street on the other, was unable to or had no intention of taking any action that would limit further inflation of the speculative bubble. In addition, the U.S. Department of the Treasury did not dare to oppose the swelling storm. The IMF once again turned out to be an organisation essentially serving the interests of the USA or, more precisely, of the U.S. financial and political elite. Soon, they were to learn that it was not in their best interests.

Although not in all cases, as it usually happens in times of crisis, there were people who benefited from the situation. Several leading American investment

¹² For more on the causal connections between present and future, see Thurow (1996) and Kolodko (2011).

banks are now wealthier, have higher capitals than before 2008 and hold stronger positions both in the American and global market. Roubini and Mihm superbly depict how the management of the aforesaid banks behaved in the critical days of September 2008, which led to the outburst of the open phase of the crisis and Wall Street's collapse – an outburst, because the crisis was caused by a chain of events rooted in phenomena and processes that took place much earlier.¹³

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Even though Roubini and Mihm's "Crisis Economics" is one of the most vivid works criticising contemporary capitalism, the authors do not go to extremes. They do not proclaim the end of the world, or the collapse of the capitalistic political-economic system based on a free market and the dominance of private ownership, as well as the maximisation of profit as the aim of economic activity. Such prophecies of "nearly-the-end-of-capitalism" do occur. Sometimes, it may look as illumination, sometimes it is pure opportunism, as well as political and intellectual bowing to economic cycle.

An example of such an illumination on the American, extremely opinion-making, ground could be the switch made by one of until recently most devoted supporters of the effective markets hypothesis, too often abused by apologists of the free, unlimited market.¹⁴ When one of the advocates of the "Chicago school", Posner (2009), the author of a book on the failure of capitalism, himself a lawyer, was asked what economists had learnt from the times of crisis, he replies that he felt that they learnt nothing. Because "market correctives work very slowly in dealing with academic markets. Professors have tenure. They have lots of graduate students in the pipeline who need to get their PhDs. They have techniques that they know and are comfortable with. It takes a great deal to drive them out of their accustomed way of doing business" (Cassidy 2010: 29).

¹³ The days of bargaining between American financial authorities and Wall Street, including the cynical approach of the management of certain investment banks, are described by Stewart (2009). They are also explained in the documentary movie "Inside Job", directed by Charles Ferguson in 2010.

¹⁴ An eloquent comment was made on my blog, dedicated to the books on global economy and development processes, www.volatileworld.net: "Dear Professor, I am currently a political science student of XYZ university. I understand that everyone has his own truth, but if 90% of the academic staff say, for instance, that the free market will adjust itself or that with current government policy and our economic growth, we will catch up with Germany in 20 years, then first thing that comes to my mind are the words of the Rev. Tischner – bull**it. Everyone has the right to be wrong, that's sure, but such 'great professors' should not yarn that much to student." Compare entry 1015 dated 22.11.2010, <http://www.volatileworld.net>.

That is the point: comfortableness, conformism, tradition. Or, from another perspective, conformism, lack of sufficient intellectual innovation (what a shame!), habit, or even thought stagnation and laziness. The authors of “Crisis Economics” are completely deprived of these vices. It is the heterodoxy, political incorrectness, intellectual naughtiness and lack of susceptibility to the pressure of the so-called thought-conservative mainstream pointed them the right way in their search and offered the right answers on time, not *ex post*. They are right. Others are right too; for instance the afore-mentioned Posner. They were able to switch from neo-conservatism (as it is called in American political slang) to quasi-keynesism, which, on the other hand, is not a sufficient formula to cure current problems. And so, even such a prominent supporter of the Chicago School admits that the present crisis was caused by a defective monetary policy and deregulation.

Roubini has no need for such an about-turn.¹⁵ Regarding Keynesianism, he only reaches to it when necessary, since he knows that the future is in heterodoxy and theoretical eclectics.¹⁶ He was very right a couple of years ago, when almost no one listened to him, and he is right at present, once he has become a star of economics. Exactly. There are stars of economics. And trends. Not as much as in show business, but still.

For many years many wise people were lured by what the authors call conservatism or “contemporary laissez-faire”. They mean the same what others – including me in my works on globalisation, development, stagnation, and crisis – call “neoliberalism”.

The authors of “Crisis Economics” convincingly and aptly demonstrate that we are not experiencing a general crisis of capitalism or, generally speaking, a “Failure of Capitalism,” but certainly a breakdown of its neoliberal version. Already a breakdown but not a collapse yet. I have underlined this in the title of one of the chapters in my book *Truth, Errors, and Lies. Politics and Economics in a Volatile World: The Withering of Neoliberalism and Its Tattered Legacy: Why a Harmful Concept Rose to Temporary Ascendancy in Half the World and What to Do About It* (Kolodko 2011).

So, what should be done? Approaching the issue pragmatically, the authors offer many sensible answers, another valuable advantage of the book, because it not only includes a reliable, convincing and clearly presented diagnosis of the (bad)

¹⁵ I write Roubini, because Mihm, the co-author, mostly contributed the historical sections of the book.

¹⁶ Some authors, whose number is growing, believe that we are now facing the renaissance of Keynesianism, see Skidelsky (2009). In fact, it is a time of yet another escape forward, without looking back too much. It makes sense to take what is best from (neo)Keynesianism, but one should not be limited only to that, given the challenges of the present.

status quo, but also constructive proposals of what to do to make things better in the future. But “better” does not equal “avoiding crises”. The main idea of the argument is the thesis that the crises are an immanent attribute of capitalism. Therefore, we will be facing them in the future as well. However, they may be foreseen in advance. And if one is able to do so, one may be able also to make the future crises less devastating. Finally, from the point of view of reproduction on a long-term basis, as well as the imperative of keeping social and ecological balance, the costs of overcoming the effects of crisis may be distributed once we face them.

Roubini and Mihm write a lot about that. And what they write is wise. The question is to what extent such good advice will become practice in macroeconomic policy and business strategy. Nowadays, when we are still in the shade of crisis, it seems that such things should happen on a large scale. We must be careful, since new crises will come with time, also the one I have elsewhere called an Even Grander Crisis (Kolodko 2011: 346).

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Having said some bitter words on our beautiful field of study – economics – which surely deserves a whole list of them, Roubini and Mihm do not distance themselves from it; neither do they proclaim its end. They demonstrate that the mainstream of economics, based on the simple or even unsophisticated interpretation of neoclassical economics, has not failed completely. What failed is neoliberalism. Or, as the authors prefer to call it, the contemporary laissez-faire. I agree. They show, however, that the science of economics is not without fault. We should add that other authors have also pointed this out, although from different perspectives, drawing attention to the weaknesses of this area of study subjected to politics and the influence of special interest groups.¹⁷

One of the greatest values of “Crisis Economics” – which, in my view, is in no way inferior to the interesting and reliable description of the conditions, causes, mechanism, the process, temporary effects, and long-term consequences of the present worldwide economic crises – is that it demonstrates how periodic crises are usual in capitalism. We live in a world that moves from one crisis to another. A world between crises.

There may be fewer crises in the future and they may affect us less intensively and less frequently. That is the point. In order for this to happen, one must know the sequence of correlations and always remember that things happen the way they do because many things happen at the same time.

¹⁷ See for instance Ormerod (1997); Csaba (2009).

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