

The Economic Growth – a Dream to Come True under the Circumstances of the Current World Economic Crisis

Alexandru Sălceanu

Petroleum-Gas University of Ploiești, Bd. București 39, Ploiești, Romania
e-mail: alexsalceanu50@yahoo.com

Abstract

The economic crisis has not been an unpredictable phenomenon, but it is part of the essence of capitalism itself, being influenced by the speculations on the financial market and stock market, which are hardly regulated. The current situation anticipates a dire period which will last for some time, on a very complicated international background, with expensive credits and protectionist tendencies, along with the worldwide redistribution of power. In order to surpass the crisis, it is necessary to appeal again to reason, which means pragmatism, cooperation, but also compromise, so that we are certain that the financial markets support competitiveness, instead of destroying it.

Key words: *macro-economic imbalance, globalization, major investments, economic growth, surpassing the recession*

JEL Classification: *E44, E52, F43, G32, O16*

Introduction

The economic and social progress that we have witnessed for the last three decades is mainly due to the introduction and spreading of the results of the scientific research in two areas: technical and managerial, which are tightly linked and interrelated.

In the technical field, the main factor of economic rise stems from the information and telecommunications technologies, which favoured the spreading of the positive experience in the developed countries, which led to a rise in labour productivity. In the managerial field, there have occurred changes in the international work distribution, which resulted in off-shoring some activities from the overdeveloped countries in the less developed countries in Asia, America and South-East Europe, which had the advantage of lower costs. This way, in the above-mentioned area, we have witnessed an increase in foreign investments in the Gross Internal Product from 3.1% in 1980 to 16% in 2007. This has resulted in making the financial flows worldwide more dynamic, which generated an increase of the financial assets nine times between 1980 and 2007.

As a result of these positive phenomena which took place at the global level, we have witnessed significant changes in the distribution of income and wealth resulted from this increase in the sense that the richest have become even richer, whereas the poorest have not been able to acquire to the extent to which they contributed to this increase.

The Financial Crisis Brings into Light the Issue of Market Regulation

The liberal ideas according to which the markets, especially the labour market and the financial market, can regulate themselves have proved to be impractical, generating a major imbalance which ended in the current world economic crisis. According to Minsky¹, the instability that leads to a crisis depends on the action on the financial markets, on the price of the assets and on profit flows. Instability is escalating by the ever-increasing production of capital, which makes the capital become more expensive and forces the debtors to pay their debts with the money obtained from taking on more debts and not as a result of production. Experience has proved that " *The neo-liberal financial reforms based on deregulation and globalization of the financial markets have increased access to financing and the possibility to trade assets*"², generating a major imbalance.

The economic crises always represent the symptoms of major imbalance between the three major components of the economic activity: production, request and distribution. The increase in profits obtained by the large multinational corporations was due to the production of high-performance products based on innovation and the low costs with the labour force, as a result of its liberalization. On the other hand, the absorption capacity of this production did not increase so much, generating a major imbalance in revaluating the production obtained. In order for the request to increase as the offer increases, there should be a balanced income distribution among all the members of the society. The rich people of the world spend more of their income on consumption than the poor people. As a result of this situation, those with average income have been encouraged by the banks to contract loans in order to purchase products and services that are considered to be normal consumption nowadays. Under these circumstances, *'People felt the social pressure to consume more because anyone else does it, and they do not want to be the last and they do not ask themselves whether they can afford such a high level of consumption, as no one else does that. In the meantime, consumption is booming and bad investments are being made.'*³

In their profit chase, banks have come up with a lot of toxic financial products whose risks were hardly understood. In this context, the speculative balloons have occurred. They are described by Kindleberger (2005) as follows:

Opportunity – Credit – Euphoria – Financial Disaster

As regards this situation in the banking system, the governments have witnessed helplessly the creation of sophisticated financial products which gave the illusion that one can live better if one is in debt. Apart from this, there were also the huge retributions for the bank managers and for the managers in the international corporations, which made the difference in the society even bigger. The financial sector and its toxic speculations has become an inflated sector, having an instable basis like a cube game, whose collapse once started in America has led to worldwide collapse, generating the worst economic crisis in the world.

Considering the above-mentioned aspects, which show major imbalances in the social and economic development of the world we live in, J. Stiglitz mentioned in 2002 in his paper *Globalization and its Discontents* that the International Monetary Fund and the World Bank, which were supposed to warn and prevent against the world economic crisis, failed to do that. The International Monetary Fund did not provide enough resources to the countries which were in economic decline, and the policies of forced and premature liberalization of the capital market led to an increase in global economic instability. J. Stiglitz considered that IMF should have limited its influence to the macro-economic issues (budget deficit and trade deficit,

¹ Minsky, H.P., *Stabilizing an Unstable Economy*, McGraw Hill, 2008.

² Voinea, L., *Sfârșitul economiei iluziei*, Public Publishing House, 2009, p. 31.

³ Akerlof, G.A., Shiller, R.J., *Animal Spirits*, Princeton University Press, Princeton, 2009, p. 63.

monetary policies, inflation), allowing the governments to have more freedom in setting their development strategy. According to the same author, the World Bank should have limited to the structural issues of the countries, such as: the financial institutions, labour force market, trade policies, helping them to adjust their economic policies in order to diminish the imbalances occurred in economy. Currently, globalization is not beneficial to the poor countries of the world, to the environment and to the stability of the world economy. Stiglitz's dissatisfaction with globalization is not aimed at globalization itself, regarded as a phenomenon that cannot be stopped anymore, but at the doctrine and policy imposed by the international financial institutions.

Referring this crisis, Nouriel Roubini mentions the following: *'A lot of countries expressed an amazing reluctance in starting the total reform that is needed in order to put the financial system on the right track. Instead of this, they speak of patching it here and there as if the disaster that has just happened were due to a few unsuccessful mortgage credits. That's sheer foolishness. The crisis has not been only an effect of standard credits but also of an under-standardized financial system.'*⁴ This crisis was not an unpredictable event, it was not *the black swan*, but it is part of the nature of capitalism itself. Economic crises occurred along with the rise of capitalism at the beginning of the 17th century and we have witnessed them since then almost in the same form. Then and now, the speculations on the real estate market and the stock market, the minimal financial regulations and a few financial innovations have all conspired to the creation of an artificial balloon, which, when it blew up, set the scene for the quasi-collapse of the financial system on the Wall Street, a harsh economic decline in the life of ordinary people and a global recession.

Some Ideas regarding Surpassing the Crisis

Nowadays, we are all interested in coming up with measures that could help us surpass the crisis. The rich countries, such as the USA, have the possibility, by means of some measures financially supported by the government, to foster investments and to start in this way the development engine. In the short run, even a small change in income distribution towards the poor people would ensure a first step in the increase of the request of the consumers. In the medium and long run, the state could undertake major investments in transportation, services, health system and education, which, apart from the advantage of stimulating an increase in request, would also lead to decreasing unemployment, increasing life quality, improvement conditions, with a view to attracting foreign investors. In the developed countries such as Germany, England, France etc the state has already got involved in carrying out such projects and the results have been good. However, it can be noticed that things are moving much too slowly because of the obstacles raised by politicians who aim, along with businesspeople, at their own personal interests, and not at the general interest. For instance, development of alternative sources of energy, cheaper and less polluting, is hindered by the interests in the monopolies in the oil industry.

The economist Muhammad Yunus, a winner of the Nobel peace prize in 2006, has some interesting ideas as regards the causes that triggered the crisis, as well as the ways of surpassing it. *'Most of the financial institutions salvaged by the governments were those that were at the basis of the crisis. In fact, we are saving the organizations that have created the crisis. Why don't we re-think of a system which should not cause the problems that it created in the past? Instead of giving money to the unemployed, we had better set up a social enterprise which*

⁴ Roubini, N., Mihm, S., *Economia crizelor*, Public Publishing House, 2010, p. 54.

*should provide jobs for the people who live on welfare. A social enterprise is not intended to multiply money, but find solutions to some social issues.*⁵

In order to avoid the current negative situations in the financial system, it is necessary to introduce some clear regulations which should encourage development and take into account the following:

- bigger capital instalments for the debt, as a guarantee against non-payment risks in the future;
- control over the incentives granted to bankers, which defy common sense and which prevents them from stimulating risks by themselves;
- dividing the banking activities according to the type and level of risk taken, namely separating the trade operations from the investment ones etc.;
- setting up regulations regarding the responsibility and transparency of the international financial operations;
- setting up some conditions for the increase of the competition level in this sector.

Measures for Economic Recovery

Surpassing the crisis represents a slow and painful process due to the austerity measures taken by governments, which generated an increasing unemployment rate, a fact which strongly diminishes the perspectives of economic growth. In this context, according to the forecasts of IMF, we will witness an economic growth of 4.2%, of 3.3% for Germany and of only 1.5% in 2011 for Romania.

The main concern of governments should be the recovery of the viability of the financial sector and the stimulation of economies, together with withdrawing the governmental support. There must be taken into account the fact that the economies of the emergent countries are slightly going up, but their evolution depends on the recovery of the developed countries. We notice the mainly positive tone of the economic forecasts, which meets the need to regain trust on the part of the consumers and on the international markets, with a view to avoiding the trap of the so-called *self-fulfilling prophecies*.

In order to surpass the recession, complex measures are to be taken, which should take into account the following:

1. Setting up a mechanism of balance between the governmental regulations and self-regulation of markets. In this respect, for the consolidation of the financial system, there should be set precise conditions for the capitalization, transparency and trading of the financial tools;
2. Strengthening the global capital standards with a view to minimising the risks taken by the banks;
3. Changing the programs belonging to those who make the rules, because the economic balance of power has changed at the global level. We refer to IMF, the World Bank and other financial institutions which, when they set up their programs, should take into account the fact that the USA and Europe are not the main actors on the economic scene any more. In this respect, countries like China, India, Brazil, Russia and other emergent countries must be taken into consideration, countries which are entitled to play an important role in a changing world.

⁵ Mihail, S., Rezolvarea crizei economice in viziunea unui laureat Nobel, in *Capital*, Nov 11, 2010

4. Setting up a social pact regarding globalization in order to counteract a part of the negative effects of this phenomenon. In this respect, there must be created social systems which should provide efficient medical assistance for all the people and help for those who change jobs. People should be protected against the two main insecurity sources that get us all worried: getting sick and unemployment.

In order to diminish the negative effects of the crisis, at the end of October 2010 the EU leaders decided on increasing control over each member state and continuing the salvage plan for Greece. The measures of this plan have the purpose of reforming the EU norms in order to avoid any reiteration of the crisis in the euro zone, but without a major change of the Lisbon Treaty. In this respect, The European Council will function as a government, having the following prerogatives:

1. setting up the European Fund of Financial Stability, financed by the EU member states, which has the task of getting out of bankruptcy the countries that need help. The issue is problematic as the Lisbon Treaty prohibits the EU states to help each other;
2. setting up a mechanism of applying some sanctions against the member states which violate the European legislation that regulates the financial activity;
3. close monitoring of EU states in order to avoid the worsening of the crisis. As Hermann van Rompuy, the president of the European Council, noticed, '*The euro currency had the effect of a sleeping pill for some states, which is why EU tries to adopt a system which should make you wake up in time*'⁶. In this respect, apart from the public debt, EU will also monitor the level of competitiveness and the real estate balloons. Obeying such indicators could have prevented the situations in Greece, Ireland and Spain.

Currently, Europe needs policies which should contribute to increasing competitiveness and economic development of the states situated at the periphery of Euro Zone, where the GIP is still decreasing (as is the case with Greece, Spain and Ireland) or is insignificantly increasing (as is the case with Italy and Portugal). Without a positive evolution in this part of E.U economic scope, it is hard to believe that the public and private debts or the deficits in GIP will be stabilised, GIP being the most important indicator of fiscal sustainability. Besides, without this increase, the social and political uprising against the severe expense budget cuts will have as a result the undermining of the austerity reforms and programs.

In Nouriel Roubini's opinion, '*In order for the growth to be resumed, The European Central Bank should adopt a much more relaxed policy which should allow the devaluation of the euro and thus stimulate the competitiveness of the peripheral states*'⁷.

The Situation in Romania

We must be aware that surpassing the crisis cannot be achieved immediately, but it represents a difficult process to which everyone should be part of. The crisis anticipates a dire period which will last for some time, on a very complicated international background, with expensive credits and protectionist tendencies, along with the worldwide redistribution of power. In order to surpass the crisis, the decision-makers in Romania will have to take into account both the international economic context, and also the current economic situation in our country, where major errors have been made, and which basically refer to: consumption based on debt which led to an increase of the current account deficit, managing disastrously the European funds together with corruption, increasing salaries more than productivity, increasing the number of

⁶ <http://www.ziare.com/economie/criza>, *Cum vrea Europa sa evite viitoarele crize economice*

⁷ Interview in "Capital" magazine, *Strategii de supravietuire a monedei euro*, December 27, 2010.

employees working for the state, maintaining the structural deficits, the more rapid increase of the external debt in relation to GIP etc.

The measures that are to be taken by the decision-makers should mainly focus on the following *directions*:

- obeying the fundamental economic correlations, especially between the growth of labour productivity and the dynamics of the salaries;
- increasing the degree of using material resources;
- efficient integration in the European zone, without affecting the relationships with Russia, China and other emergent economies;
- continuing the reorganization in the state sector, where there are too many employees as compared to the other EU countries;
- focusing on investments, especially in agriculture, infrastructure, regenerated energy, public health, education, tourism;
- reorientation of the resources, especially towards the production of goods and services to be exported;
- supply of credits, especially from internal resources generated by the internal savings;
- continuing the fiscal reinforcement, the structural reforms and updating labour legislation;
- continuing the administrative reform and the public services by means of simplifying the administrative and fiscal procedures;
- decentralization and introducing the cost standards into the mechanisms of budget transfer.

The main shortcomings related to the financial system that we have gone through should make us more aware so that in the future we should take into account the following:

- the financial system has to take on its main task, that is supporting the development of the real economy;
- all the financial institutions must limit the proportion between their own capital and the borrowed one;
- the markets for complex financial instruments must become again transparent, including solutions for warranting transactions;
- the transactions with complex financial instruments must be regulated and monitored by the state institutions;

In order to sustainably surpass the crisis, Romania has to obtain a strong economic growth based on investments, especially in the sectors that produce added value, contributing at the same time to decreasing the rate of unemployment and to increasing the income to the state budget.

Conclusions

The financial globalization, materialized into the gradual removal of the barriers to the global capital circulation and integration of the capital markets at the global level, has had a positive effect to the extent that it has allowed the economic resources to be directed where they are more productive. But unfortunately, along the way there have occurred unwanted effects which were generated by the lack of regulations on the financial market, which made it possible for appealing products that were hardly understood to appear, bringing about an economic crisis that has spread all over the world. The current crisis is not something accidental, but it represents a failure of the markets which were hardly or not at all regulated. *‘What is going on*

now is not a rejection of the forces of the market as a mechanism of allotting the resources and stimulating the entrepreneurial spirit, but a case of invalidation of a misinterpretation of what is necessary for a modern economy in order to reach its social and economic goals in the long run'.⁸

The future of the world economy will be influenced by the competition between the liberal democracy typical of the EU states and a form of capitalism with authoritarian tendencies based on the state structures, typical of Russia and China. In order to surpass the crisis, it is necessary to appeal again to reason, which means pragmatism, cooperation, but also compromise, so that we are certain that the financial markets support competitiveness, instead of destroying it.

References

1. *** *Ziarul Financiar* Collection, 2010.
2. Akerlof, G.A., Shiller, R.J., *Animal Spirits*, Princeton University Press, Princeton, 2009.
3. Dăianu, D., *Capitalismul încotro?*, Polirom Publishing House, Bucharest, 2009.
4. Kindleberger, C., *Manias, Panics and Crashes : A History of Financial Crises*, Wiley, 5th edition, 2005.
5. Lankester, T., Commentary. The Banking Crisis and Inequality, *World Economics* 10 (2009) 1 (January–March).
6. Lankester, T., *Criza bancară și inegalitate*, 2009.
7. Minsky, H.P., *Stabilizing an Unstable Economy*, McGraw Hill, 2008.
8. Palma, J.C., Why neo-liberal reports of the end of history turned out to be premature, *Cambridge Journal of Economics* 33 (4) (2009) 829–869.
9. Roubini, N., Mihm, S., *Economia crizelor*, Public Publishing House, 2010.
10. Stiglitz, J., *Globalization and its Discontents*, W.W. Norton & Company, 2002.
11. Voinea, L., *Sfârșitul economiei iluziei*, Public Publishing House, Bucharest, 2009.
12. Wade, R., From global imbalances to global reorganization, *Cambridge Journal of Economics* 33 (4) (2009), pp. 539–562.

Creșterea economică - un vis posibil de realizat, în condițiile crizei economice mondiale

Rezumat

Criza economică mondială nu a fost un fenomen imprevizibil, ci face parte din însăși natura capitalismului, fiind favorizată de speculațiile de pe piața financiară și bursieră, prea puțin reglementate. Această situație anunță o perioadă vitregă, ce va dura, cu un mediu internațional foarte complicat, cu credite scumpe și accente de protecționism, pe fondul redistribuirii puterii în lume. Pentru a ieși din această criză, este necesară întoarcerea la rațiune, care înseamnă pragmatism, cooperare, dar și compromis, pentru a ne asigura că piețele financiare susțin și nu distrug competitivitatea.

⁸ Dăianu, D., *Capitalismul încotro ?*, Public Publishing House, 2009, p.26