

Collapse of Radical Liberalism as the Main Cause of the Crisis

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Nobody today is able to predict the time when the next crisis of economics will come and what will be the reason for it. It demonstrates the complexity of the discipline. Physics knows precisely: water usually boils at 100 degrees. In economics problems and controversies are accumulated slowly, but their critical level is not known in advance. Each time the crisis emerges under different circumstances. In Russia or overseas financial authorities are not to be blamed: they are not sinless but it is not the only cause of the crisis. Crisis in the USA that became the trigger for the financial turmoil all over the world is in fact the demonstration of the controversies that have been accumulating for a long time. What are they and in which combination have they led to a crisis?

The most serious controversy and the first source of the crisis: behavior and motivation of the managers is in stark contrast to that of the owners. About 50 years ago American economist A. Berley in the book about the so called “revolution of the managers” emphasized: it is difficult for the owner of a big company, “Chrysler”, for example, to make sure whether the interests of the owner are served. Business is run by the managers and the problem they face is mostly technical – ensure the profitability of the firm. Their well-being does not really depend on the reputation and the potential of the firm. That is why, say, bank managers are able to freely distribute the credit, that the owner would have never approved, if it improves the balance sheet of the company.

The second source of the crisis is that in the developed capitalism financial sector is independent and separated from the production, from the industrial sector of the economy where money is created. Later, temporarily becoming “spare” they reach banks or the stock market and become independent from the producer. But at a certain point the scale of such “break” of the finance becomes inadmissible. Some experts estimate that only about 2-3% of the financial operations are related to the material production, rest of the money circulate giving the “living” profit – in the service, banking, insurance sectors that are now facing problems.

And the third source of the crisis – inevitable cyclicity of the development. It is impossible to overcome it, although the defeat of the cycle is sometimes announced. In the 90's in the USA the growth of the economy and the welfare went on continuously for 120 months, in the state of

euphoria people were gambling with the stock market more and more and the quality of the stocks was becoming less important. But the constat enrichment can not be brought by the appreciation of the paper – without the growth of the production. It is precisely a soap bubble. It can not inflate constantly so it pops. It should be noted that crisis is not just evil, but a catharsis, purification, and the earlier it pops, the weaker the crisis.

Excessive availability of money in the last few years have led to the growth of the borrowing by the questionable clientele and surfacing defaults on the debt led with a “chain reaction” to defaults on the bonds and the threat of bankruptcy in the banking sector. Over-the-counter speculations have also been growing: by the december 2007 world market of the financial instruments has reached \$14,5 trillion. Many of the transactions were questionable because of the low quality of the stocks, bonds and mortgage obligations. World financial markets indices have fallen, thus warming the speculation of the stock market players and worsening the crisis.

Instability on world financial markets will probably continue and “rescue” measures aimed at mortgage banks will increase the budget deficit and the government indebtedness. These measures, by the way, are a direct and massive government intervention that americans are urging everyone to get rid of. Possibly, the amount of government debt as a result will be 80-90% of GDP. It should be emphasized that they do not really fear the inflation resulting from the increase of budget outlays. It should be noted that inflation in the USA, as, however, in the Eurozone too, is almost an order of magnitude lower than in Russia. One should not fear the destiny of the Dollar, much less - expect it to fail.

From the first sight, russian economy faces fewer significant urgent problems than the USA or the Eurozone countries. But Russia is an organic part of the world economy for almost 20 years now. And we have no specific margin of strength – besides, of course, reserves of the Central Bank, accumulated thanks to the favorable foreign economic situation, and this very situation is currently changing. The real margin of strength would not have allowed the stock market to collapse fourfold in three months. And one should not think that the policy of “sterilization” of the funds from the stabilization fund as opposed to its usage in the development of the production was justified.

Of course if “surplus” money have just been “eaten”, it would have accelerate the inflation. But the reasonable ways of spending such funds are known – for the modernization of the economy. The problem of inflation would have been solved, because the main source of inflation in Russia is

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not monetary at all, it is about the structure of the economy. Normal economy reacts to the growth in the purchasing power by increasing the production, but Russian – with price increase. As usually, we have two problems, but now they are the primitivization of the economy, that is accompanied by the acceleration of the inflation. There is no other reason for the acceleration of the inflation besides the economic policy of the last 17 years – it was inconsistent not just factually, but also in the verbal explanations of the authorities: as if they have directed the main efforts to the macroeconomic stabilization, but its main element is exactly low inflation. And with price increase of 15% this stabilization is not observed which by the way makes meaningless any talks of the rouble as a reserve currency.

There are two scenarios of the further development of the situation. First is positive. The world demand that is very low today is rapidly recovering, final goods consumers should believe that measures that authorities in all countries enact to counter crisis are proper. At the same time many banks and financial companies will fail. It should partially affect Russia as well. In the end it would even be helpful: now almost half of the credit organizations are such only by their names.

Under a negative scenario markets and investors do not believe in the success of the measures aimed at countering the crisis, world recession is prolonged, industrial employment contraction scales are becoming socially dangerous, world oil consumption is at persistently low level. In this case Russia is forced to rapidly cut imports, and we can not survive without it anymore. It may be hoped that this scenario will not realize. But a number of opportunities is already foregone. For example, for many years discussions of scientific based production do not go further. It should be remembered that it requires coordination of trade, structural and credit policy that is also absent in Russia.

The main point should be understood: crises in both USA and Russia happened because both American and Russian economic structures, each in its own way, have ignored the requirement of the systematic government regulation, thoughtlessly cut the participation of the government in the economic process. If the mortgage abuses and growth in unsecured credit in the USA were noticed two years ago, crisis would not have been so severe. If Russia had enacted the market model of the economy, backing it with respective institutions, monopolistic antisocial capitalism would not have appeared in the country.

For Russia the main problem now is the need to restructure the technological base of the economy. The prevalent view of the many that the government should not intervene with anything,

that industrial policy is a sign of backwardness – anti-market in its essence as it conservates the backwardness of our country among the developed countries that successfully practice government regulation and industrial policy as powerful tools for ensuring their competitiveness on world markets. The development of the advanced technologies without the government will not do: private business will not go for it – costs and risks are too high.

In this context the creation of the government corporations should be considered as a step forward, although there are concerns – the lack of democratic control and a possibility of the abuse of the public funds. But it must be remembered that only giants are able to compete with giants of the West (or the East). It is a proper situation to recall Brecht: “If you fight you may lose. If you don't fight – you have already lost”. Of course, management of the aviation holding company should define precisely, which airplanes, when and how many should they produce. But these targets are not set and it produced a strange impression. Time does not wait and in 5-7 years the ultimate destruction of the soviet scientific potential will take place, human resources that are just sustained but not being renewed will disappear, - and we will lose probably the last competitive advantage for the high tech market.

Abuse of the government measures and resources should also be remembered. But there is no other way nonetheless: similar processes are found all over the world, the more active government role is called for everywhere, the world is tired of the “free” economy and radical liberalism. About to replace it is the system that may be called “new capitalism”.

When managers risk the property that was entrusted to them, inadequacy of regulation supports their ventures. It is necessary to find a right balance between the private initiative and the government oversight. When the balance is broken, a catastrophe happens as it did in 1929. Three models were offered as a response to a “wrong” balance: command soviet system emphasizing the social justice, command hitlerian one with an eye towards national unitedness and anglosaxon (keynesian) – with no restraint on private initiative but with strong government regulation. First two turned out to be unworkable. Keynesian one was rather effective, but ceased to produce needed results by the 70`s. After a number of crises the world got back to the liberalism under the slogan “back to Adam Smith”.

Unfortunately, the transformation of the soviet economy coincided with the new fashion in the world of deregulation. Unstoppable “invisible hand of the market” in Russia has closed everything not related to the quick profit and “pipe” economy. Instead of starting to produce

competitive goods we have almost ceased the production of the final goods at the industrial scale.

Thus, the strong and regular government activity can not be avoided. But the “new capitalism” will have its own problems and the world may reach a different extreme – overhyped togetherness with the vicious protectionism. In this model the social component, social justice should be not the antithesis, but the necessary condition of the increase in the economic efficiency.

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