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RESEARCH ARTICLE

Economic Science Lost in the Dialectic of Globalization

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Abstract

The dialectic of globalization suggests that a "territorial" state is going to be replaced by a "market" state. A "market" state is a state dominated by big transnational corporations (TNC) and big transnational banks and presumably demands some sort of world government. Such a drastic but evolutionary change should be followed by new economic knowledge. Cutting-edge technology in the possession of TNCs does not allow the renewal of national economic policies whether those contain protectionism or a Keynesian approach. Economics, as it can be found in standard textbooks, is based on the principle of diminishing returns and deals with economic policies of "territorial" state. In this context, the entire field of microeconomics along with macroeconomics begs to be reconsidered from the point of view of increasing returns and the global economy. The World has entered into economic globalization without an appropriate economic theory. Economic science has lost itself in the labyrinth of globalization.

Keywords: *Globalization, Power, Interests, Economic theory, Mega-capitalism.*

Introduction

Since the time of Adam Smith and David Ricardo a nation ("territorial") state was the space within which the Pareto optimum was supposed to be reached by free functioning of market forces. Keynes's "General Theory" was focused on the nation state more deeply. Keynes's macroeconomic management deals with the issue how to improve market imperfections and market failure in order to increase well-being of a nation and nation state citizens. Globalization at work, particularly that one which is described in Krugman's [1] "Increasing Returns and Economic geography" or in Summers [2] "The New Wealth of Nations", is a nationless process without a proper global economic management. As long as both politicians and some of the most influential economists were convinced (were true believers) either in free market or in the "New economy", endless prosperity has been expected. Many distinguished economists were convinced that the international Pareto optimum, particularly relevant for the EU enlargement, was quite a realistic achievement only if EU follows the dictate of a strong radical free market reform [3]. Therefore, the creation of a unique economic market within Europe, the formation of the European economic space without a political union was quite feasible and had a promising future. "Laissez-faire" was considered as a magic solution for every issue.

As long as the functioning of the Euro zone is concerned, Keynes's economy was taken as useless. Likewise, the enlargement process was dictated by the Maastricht criteria and promising Euro zone benefits were expected by newcomers. However, the contemporary world financial crisis has raised many questions. One of them is Europe's ability to respond to this serious economic crisis. Is the European Union a fine-weather union or/and can it survive the heavy economic storm?

Ferenc Gyurcsány, the former Hungarian prime minister, had sent a warning: "We should not allow a new iron curtain to be set up and divide Europe in two parts. This is the biggest challenge for Europe in 20 years. At the beginning of the 90s we reunified Europe. Now it is another challenge – whether we can unify Europe in terms of financing and its economy." But Angela Merkel, the German chancellor, dismissed the call for an Eastern Europe aid fund, saying: "I see a very different situation among eastern countries, I do not advise going into the debate with massive figures."

National interests are inserted in the heart of Europe. Consequently, Tomas Klau (Paris director of the European Council on Foreign Relations), said "This crisis affects the political

union that backs the euro and of course the EU as a whole and solidarity is at the heart of the debate."

Let us recall that the EU is saddled by the Maastricht treaty, the Stability and Growth Pact, 17 EU member states share the euro as their common currency, etc. However, what the EU lacks is: joint fiscal policy, joint tax policy, joint industrial policy and joint social policy. Europe has social-democratic states with well developed welfare policies (for example, the Scandinavian countries), it has corporatist states such as Germany, France and Netherlands plus a whole bunch of new member states which are trying to emulate free market liberalism. Those new member states are the ones in deep economic turmoil. If we add Ireland, Greece, Portugal, Spain and Italy we get half of the European Union already entrapped by the economic crisis. And all of these countries are devoid of any serious Keynesian macroeconomic management. While European Central Bank is obsessed with price stability, at the same time national governments, those of euro-zone member states, are devoid of monetary policy.

EU is a perfect case in point to illustrate the labyrinth of transition from a “territorial” (nation) state into a “market” sate on the basis of profound globalization process and functional integration of the global economy.

In this research we elaborate on interdependence between economic reality, economic interests, economic ideas and economic theory particularly in the world of globalization. In the first part we interpret those causalities in a historical context having in mind both economic events and relevant economic literature since World War II. This part relies heavily on Stojanov’s research published in 1990 under the title “World Economy and Small Medium-Developed countries” [4]. In the second part of the paper we elaborate on lessons about neoclassical economics, both micro and macro, in the period since the Second World War as we were able to deduce by following both mainstream and non mainstream literature [5]. Finally, we conclude that globalization process lacks an adequate economic theory and that the economic science is entrapped by the dialectic of globalization. Dialectic of globalization, as we discus and propose, is a political economy approach to globalization very different from the standard and well known technical approaches and definitions of globalization. Such an approach to globalization leads us to systemic interpretation of economic crises, and consequently towards a new vision of the world we see tomorrow. Our approach to globalization enables us to cast new and different light from the standard one on the role of economic science, both micro and macro, in the global economy.

Thoughts on the Relevance of Economic Policies

In the development of economic thought to this date, there has been a fascinating interdependence between economic events, economic ideas and economic policies. One of the most obvious examples of the interaction since the Second World War is the change of focus from unemployment, a Keynesian idea and economic policy, to inflation that is a Monetarist idea and policy. An analogous change occurred in the acceptance of Phillips curve and Okun's law from the Second World War until 1970 and their replacement by the vertical Phelps curve together with the notion of rational expectations.

With the formation of the IMF and GATT, the stage was set for the greatest prosperity that the world economy has ever experienced. In the years immediately after 1945, the supply curve of national economies showed a positive Keynesian slope. During the fifties and sixties “it came to be accepted wisdom that businessmen were always in a position to set prices at a margin over costs that would provide them with a rate of return at which they would be happy to invest more.” According to Marris [6], the OEEC in the 1961 report stated: “The share of labour, apart from cyclical shift, remained remarkably constant in almost all countries around 1950. With high employment, business has been able to maintain a profit margin.”

During the fifties it became generally accepted that the Phillips curve (namely, a Keynesian type of economic policy) was completely compatible for national economies in their attempts to control deflation and also inflation.

It is certainly true that in comparison with the 19th century economic liberalism and internal economic equilibrium came to have the priority over the balance of payments equilibrium. Foreign trade and currency measures were targeted to achieve affirmative and useful effects from the foreign trade multiplier and accelerator in the interests of economic growth of the national economy. Keynesian economic policy at home was supplemented by a choice of a growth strategy based on the dynamic approach to the theory of comparative advantages.

At the beginning, while the argument for protecting new industries was valid, a policy of

import-substitution was the dominant strategy for the economic growth of small open economies as well as for large countries. In time, a small open economy, which had become the price taker, became more and more geared to an export growth strategy and became not only the price taker but also the rule taker. Focusing on the production of an increasing number of tradables has ever increasingly turned small and medium countries into dependent countries. Unless, of course, the countries concerned had opted for the Prebisch or Myrdal models of isolation from the world economy with all the negative consequences of such a decision for their economic growth (as it was the case of Latin America). In spite of this, the production of firms in small open economies completely became (more or less) a part of the offer curve of the national economies. The process of transnationalization of the world economy had begun.

Currencies of the European Economic Community (EEC) member states became convertible which resulted with the interdependence of their markets and their economic policies in 1958. Europe has very quickly become a competitor to the USA. From 1960 to 1965 wages in Europe and Japan, the two main US competitors, rose from between 2-6% annually while wages in the US fell during the same period by 0.7%. The new wage relationships caused a balance of payments surplus in America which reached 6.6 billion dollars in 1964 [6]. However, the acceptance of the full employment concept based on the slogan "we're all Keynesians today" required in the USA (and not only there) an expansive monetary policy. In the meantime, the expenses of financing the Vietnam War increased with the result of inflation soon becoming enemy number one for the American economy. In 1971, for the first time since 1888, America had a trade deficit of 2 billion dollars. The offer curve of the American economy had become vertical. The world was at that point looking for a new economic policy. When the supply curve became vertical, it became counterproductive.

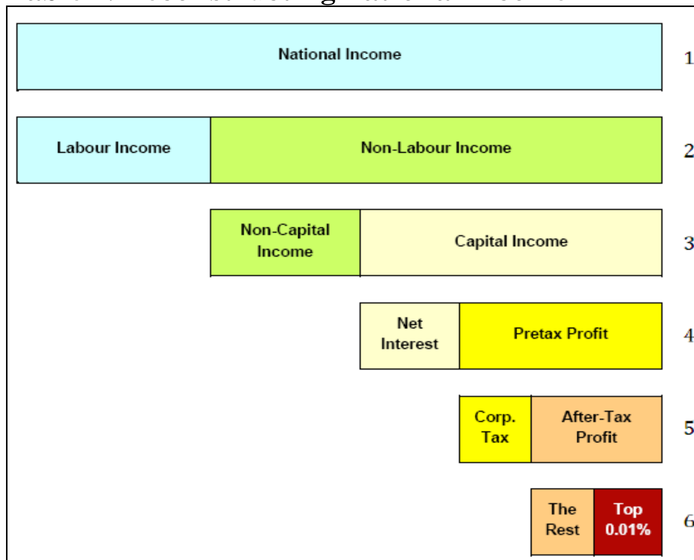
Nevertheless, economists went on trying to cure stagflation by counterproductive Keynesian methods supported by a policy of fluctuating exchange rates. By shifting to fluctuating exchange rates, in an attempt to save Keynesianism, the effect of the Phillips curve deepened the stagflation over the world. This showed that although the world might have become interdependent, isolation was still very much alive. In other words, priority was still given to national interests. The supranational concepts, like the process of transnationalization in the world economy, were to gain impetus as soon as the time was right. It was certain that at some point (or another) the prosperity of the world economy will to come to an end. According to Dumas [7] "the long expansion of the 1950s and the 1960s consisted to a considerable degree of more of the same. This relates directly to the inadequacy of present capacity, not only in the implied need to invest in new industries and write down the capacity in shrinking traditional industries but also in the need to transform by new investments the productive processes of industries with still saleable products but outmoded method. Both the incentive to apply advanced labour-saving technology and the actual development of such techniques has to be linked to the large increase in wage cost over the past thirty years."

The world economy had to enter into a phase of structural transformation. This was well presented by Schuker in his "American Reparations to Germany" in which he gave a reminder that for 300 years (and more) the world economy had experienced what he called "long waves". Long waves went together with the process of capital concentration and centralization (namely, with the growth of firms and their efficaciousness [8]. As a result, Keynes was replaced by Monetarism after 1980. Monetarism had a slogan: "Governments do not solve the problem, they are the problem". The Welfare State had played out its role of the guardian of economic progress and prosperity. The new economic policy operated under the slogan: "The best industrial strategy consists of tough penalties for business failure, high rewards for success and low interest rates without inflation". Since then, Monetarism became the "mainstream" economic policy. Even so, Monetarism is still a national economic policy; it still has a national identity. While operating with national economic development goals, Monetarism achieved structural transformation of the economy in all countries where it took hold. During that process it led to the centralization of capital and the creation of gigantic companies. The redistributive effects of the monetarist type of economic policy can be best seen from table 1.

These observations, along with the forward-looking outlook of capitalists, suggest that the current crisis may be the result of capitalists becoming not weaker, but stronger and that capitalist power may be approaching its social asymptote – a level too high to sustain, let alone increase.

In the world economy such a process created conditions for expansion of transnational corporations. According to Lumb [9], competition in traded goods rose significantly, since such goods are exposed to global competition. Between 1979 and 1989 in America, 1.4 million jobs were lost in industry, yet industrial production increased by about 30%. Integration between the transnational corporations of the USA and Europe attained 200 billion dollars annually.

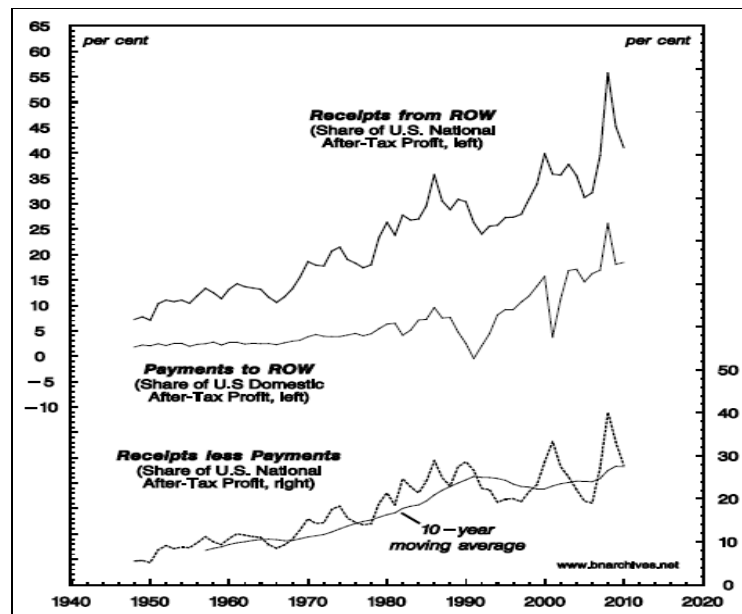
Table 1: Deconstructing national income[1]



Source: Bichler and Nitzan (2012)

In 1989 in Europe alone, the business of European transnational companies was integrated by more than 50 billion dollars. Between 1984 and 1988, direct European and Japanese investment in the USA increased by 108 billion dollars and 37 billion dollars respectively.

The net profit of the Top 0.01% are earned, at least in part, outside the United States – in what the statisticians call ROW (rest of the world). The growing importance of ROW profit is shown in Fig. 1. The raw data that underlie this figure are fraught with hazards of estimation and interpretation, but the overall long-term trends they portray are probably valid. The thick series at the upper part of the figure plots the proportion of US after-tax profit coming from outside the United States (including both the foreign dividends and reinvested earnings of US-based corporations). According to Bichler and Nitzan (2012), the data show that during the 1940s and 1950s, ROW profit amounted to less than 10 per cent of the total, but that its growth has been rapid and that its level now hovers around 50 per cent of the total! And here arises an interesting question: indeed, who or what is to prevent US corporations from using their power world-wide? Except maybe foreign competitors coming from Europe, China, Asia and Russia which taken altogether constitute the global "market" state.



Source: Bichler and Nitzan (2012)

Fig. 1: Rest of the world: Receipts and payments of after-tax profit

Graham's contention concerning the production of "goods in common" is vindicated today [10]. It seems that the production of "goods in common" demands the formation of a world economic policy and a world government. In other words, it means replacing national economic policies with a world economic policy. Any theory of international trade formed according to the principles of the theory of comparative advantages, regardless of whether the production curve is the result of differences in technology (Ricardo) or in proportional availability of factors of production (Heckscher-Ohlin), may with increasing difficulty explain the Leontief paradox. In an imperfect market, Vernon's theory of foreign trade impulse is a far better explanation of the true role of firms on the market and in the international division of labour. Even though Vernon's theory of foreign trade impulse still places the firm and its products in the aggregate offer curve of a national economy. Multinational companies are concerned only by where to locate their production. Decisions

[1] Line 1 is national income. This line represents total income, measured in dollars and cents, earned in a society during a given year. Line 2 shows that national income comprises two sub-categories: labour and non-labour income. In line 3, we see that non-labour income consists of two components: the income of capitalists and the income of non-capitalists other than employees (i.e. proprietors, rentiers and the government). Line 4 shows that capitalist income includes two types of income: net interest and pretax profit. Line 5 shows that pretax profit consists of corporate taxes that go to the government and after-tax profit that belongs to the capitalists. Finally, in line 6 we see that after-tax profit can be broken down to the profit of the Top 0.01% and the profit of all other firms.

concerning financial sources are of secondary character since the international financial markets are largely integrated and show a tendency towards complete integration.

In this context, according to Soderstein and Reed [11] as well as Porter [12], the characteristics of products or industries are being emphasized quite rightly rather than the characteristics of countries. The comparative advantage characteristics that underlie trade patterns are viewed as dynamic and often endogenous rather than as static and exogenous. As a result, the welfare implications of trade considered in this framework and of intra-industry trade in particular, are fraught with ambiguity and fragility unknown to the classical and neoclassical paradigms. Krugman's, Lancaster's and the work of others [11] on the economy of increasing returns under imperfect market conditions has been confirmed by contemporary practice. Main economic actors on the global scale are not nation states any more, particularly so if one thinks about small or underdeveloped nation states. The main actors are transnational corporations (TNC). These entities locate their activities where skills, capabilities and markets are clustered: capital flows only where the returns are the greatest and highly skilled people move were opportunities lie. The data prove that high-knowledge activities are produced primarily in increasing return to scale environments that are dependent on urban agglomeration, while low-intensive activities are produced more in environment of constant return to scale [13]. New economy consequently contributes to economic divergence between countries. The more developed one country is, the more mega-regions might be found either within the same country or across the border with another rich country. According to Florida et al. [14], Europe's largest mega-region is the enormous economic composite spanning Amsterdam and Rotterdam in the Netherlands, Ruhr and Cologne in Germany, Brussels and Antwerp in Belgium, and Lille in France. With a population of nearly 60 million people, and producing nearly $1.5 trillion in economic output, this mega-region's output is bigger than Canada's as well as China's or Italy's.

A mega-region requires a mega-regional economic policy, not a national economic policy. A poor mega-region on the other hand requires centrally-driven economic policy. The more poor regions there are in a country, the greater is the need for centrally managed economic policy. Additionally, an economic policy needed by a poor region is different from an economic policy required by a rich region, let alone rich mega-region.

What Elementary Micro and Macroeconomics Teach both Students and Governments Today!?

Micro Aspect

The elementary textbook from Microeconomics teaches us that when the marginal rate of substitution in consumption between goods (X) and (Y) equals the marginal rate of transformation between goods (X) and (Y), an economy reaches the state of equilibrium. At that moment the economy enjoys the privilege of general equilibrium with both microeconomic and macroeconomic efficiencies and properties of a general equilibrium. In other words, the Pareto optimum is reached. According to Theory of comparative advantage (which we consider to be a component part of the neoclassical economic model) and Say's law, two countries with common tastes and consumer preferences and with the same technology may enjoy benefits of open foreign trade. They can enlarge "common" GDP by means of international division of labour and by international specialization in production. Under the condition of "international" Pareto Optimum, free foreign trade contributes for both countries (global world) with the following effects:

- Optimal allocation of resources world-wide.
- Optimal and enlarged consumer's surplus without endangering the producer's surplus (win-win situation).
- Equalization of prices and wages in both countries (world-wide).
- Convergence of GDP growth rates in both (all) countries engaged in foreign trade.

All of these optimums are achieved together with:

- Full employment in both countries (world-wide)
- Price stability (world-wide)
- Balance of payments equilibrium

If we take into account the above mentioned achievements (effects) it looks as though the neoclassical paradigm firmly suggests all countries theoretically, and transition countries even practically, not to disturb the automatic mechanism of market forces. The paradigm pleads for entrepreneurial animal and rational spirit. However, since 2007, the global financial crisis has raised questions about the validity of the majority of determinants of the neoclassical economic doctrine. The "invisible hand" disappeared and the so-called visible hand of

prudent and concurrently frightened state is in the town again. In this paper we try to examine some of the traps and deceptions of the neoclassical economic thought that have been dominant in last thirty years worldwide. Then we go back to the economics of Keynes and Marx for obvious reasons: the present economic crisis might be more a normal consequence of market economy malfunction (with long-term tendency of repetition) rather than liquidity crisis alone. We find that at least two determinants are of decisive nature in composing the economic thought and economic actions during history and present time: a) interests and the ideology of the power elite in leading and dominant countries and b) state of the business cycle of the dominant economy. These factors can be easily found even in the time of Adam Smith (for example, Smith's remark about the fate of MPs in Parliament lobbying for the free importation of goods that compete with the domestic-infant industry) and may be followed to this day. At the same time these factors may serve as a basis for establishing a new economic paradigm and a new society.

Neoclassical Dogmas Failure–Macro Aspect

On Development, Trade and Income Distribution

More than fifteen years the Washington Consensus (WC) used to be an economic mantra preached and practiced by economists all over the world, especially in transition economies. An economist, emanating from a transition economy in particular, who dared to raise any sort of doubt in the validity and efficiency of the WC (even for a war-torn transition country), was very often blamed to be old-fashioned and/or a Marxist. However, some of the leading and distinguished world economists have recently started serious discussions on the validity of WC as a whole, let alone of its usefulness for low-developed countries (LDC's) and transition economies [15]. The role of the state in economics, the export based development strategies and openness of foreign trade as determinants of economic growth, import substitution, and to a great surprise –unequal distribution of welfare between the rich and the poor are under reconsideration [15].

Suddenly, questions on economic justice and unequal exchange have become the theme of the day, despite the pure fact arising from the neoliberal doctrine according to which the value of GDP is determined by labour and capital, and where such divisions are simultaneously efficient and fair according to the principle of marginal cost and marginal revenue. Krugman [15] in regards to that very same topic deliberates as follows: "we do not know why inequality began surging circa 1980, or why there has been a sharp increase in wage inequality among people with similar levels of education. So we should not expect too much from attempts to understand inequality trends in developing countries, where the data are much less helpful". In an attempt to explain the reasons for unequal distribution of welfare (under the conditions of free and open to foreign trade and GDP growth), Krugman cites two serious problems that have misled economists for years: "First, people expected the positive effects of liberalization on growth to be large. Second, there was a general view that free-trade policies would tend to be equalizing rather than unequalizing. This view came partly from theoretical considerations: a simple Heckscher-Ohlin (H-O) trade model suggests that opening labour-abundant economies to trade should raise wages while depressing rents of capital or land. I at least was guilty of the belief that the low levels of inequality in South Korea and Taiwan were, at least in part, the result of their outward-looking policies. And I was not alone in the belief that a shift to outward-looking policies would have an equalizing effect".

And that is not all. In the same paper Krugman continues: "In my caricature of early Washington Consensus views, I argued that people – certainly me – expected trade liberalization to be equalizing in the developing world, because labour-abundant countries would export labour-intensive goods and import capital-intensive goods, raising wages while depressing returns on other factors. Clearly, that has not happened in Latin America." Why?

An acceptable answer to this question has been offered by numerous distinguished economists. Among others it was Branko Horvat [16] who, after having extensively discussed the assumptions of the H-O theory, concluded: "One obvious consequence is that trade will not equalize factor prices. Wages in poor countries are much lower than in rich ones and no amount of free trade will equalize Indian and American wages. What is necessary is economic development, and this is not a matter of trade but of investment .Productive capital is extremely unevenly distributed around the world." Close to Horvat's observation on the role of the H-O theory as a determinant of competitiveness of a country and its effect on the economic growth and development are: Easterly [17], Adelman [18], Panic [19], Pitelis [20], Stiglitz and Hoff [21], Murakami [22]. However, the opinions of these

and many other world-wide respectable economists simply have not been respected by the economic ideology and economic policies dictated by the most influential power groups and their economists (US Treasury, IMF, World Bank, WTO).

About Macroeconomic Stability

Non-mainstream economists have for many years raised eyebrows regarding the view that the so-called nominal macroeconomic stability includes everything that is necessary for the prosperity of a country. Non-mainstream economists suggest that nominal macroeconomic stability does not provide any sort of comparative advantage for a country, let alone a developing one, in a competition with a developed country [23, 24]. These days, and especially since the Barcelona Development Agenda, economists stick more and more to the attitude that real macroeconomic stability is what really matters for an economy. Ocampo [15] calls for a broader view of macroeconomic stability that includes not only price stability and sound fiscal policy, but also a stable real economy. "It was natural in 1990, for example, after the episodes of high inflation and hyperinflation that Latin America experienced in the 1980s, to emphasize price stability. But *real stability* – variability in unemployment or real growth – is as, or arguably more, important. Price stability, as we have learned, may not lead to growth or full employment, and excessive zeal in pushing for price stability may stifle growth and lead to high levels of unemployment."

Therefore, it is not surprising when Dornbusch [25] argues that: "the worst enemy against transition to a free market economy is central bank staging fights against inflation or unduly concerned with maintaining a hard currency. Stable and moderate inflation is important for economic performance and there is a time and preference for everything. In Europe today, overdoing inflation fighting and playing desperate currency games do more to harm the cause of free market reform than the ideologies debate put together." Dornbusch's opinion concerning inflation combating efforts in transition economies is shared by Krugman [26]: "what about the other half of the WC, the belief in the importance of sound money? Here is the case even weaker. If standard estimates of the costs of protection are lower than you might expect, such estimates of the cost of inflation–defined as the overall reduction in real income – are so low that they are embarrassing. Of course, very high inflation rates (the triple or quadruple-digit inflation) that have, unfortunately, been all too common in Latin American history seriously disrupted the functioning of a market economy. But it is very difficult to pin down any large gains

from a reduction in the inflation rate from say 20% to 2%. Moreover, the methods used to achieve disinflation in LDC's above all, the use of a pegged exchange rate as away to build credibility, have serious costs."

On Convergence Issue

Neoclassical and "the old view of growth assumed that where capital is scarce, it has a high return. There was a natural possibility about this: when you give a machine to a worker who previously did not have one, it has a big productivity effect. Together with the assumption of constant return to scale, and the existence of unalterable factors such as labour supply, the assumption of diminishing returns has a sharp prediction. During the transition to a new steady state, growth in capital-scarce countries will be high because of the high returns to capital. Consequently, poor countries should catch up fairly rapidly with rich countries" [17]. Similar views on growth, development and catching up process are expressed by Maddison [27]: "If the world consists only of two groups of countries (developed and developing countries) the pattern of world development could be interpreted as a clear demonstration of the possibilities for conditional convergence suggested by neoclassical growth theory. This supposes that countries with low incomes have "opportunities" of backwardness, and should be able to attain faster growth than more prosperous economies operating much nearer to the technical frontiers." However, Maddison points out a very crucial observation and fact never before mentioned, but possibly hidden in the neoclassical paradigm, about exogenously given technology and capital. Maddison concludes that "this potential can be only realized if such countries are successful in mobilizing and allocating resources efficiently, improving their human and physical capital to assimilate and adopt appropriate technology. The resurgent Asian countries were successful in seizing these opportunities. All other regions of the world (the rest of Asia, Latin America, Eastern Europe and former USSR, Africa) have not. Their relative position has deteriorated sharply since 1973." Fisher [28] in "Economic Growth and Economic Policy" shares Maddison's conclusion pointing to the role of technical progress as one of the main determinates of economic growth of a country, and of a developing country in particular. "The modest long-run rates of growth of the industrial economies and lessons

learned from that growth are not necessarily relevant to the LDC's. The prime reason is that those countries are far from the technological frontiers; technical progress could play a

significant role in their future growth without any major technological breakthrough taking place. A quick look at the evidence is not supportive of the hypothesis. Except for Japan, most of the countries currently in the ranks of the industrial market economies have been among the high income countries for at least a century." World-wide experience with economic growth of different developing countries lagging more and more behind the developed ones the more they apply the neoclassical economic prescription, have led Vanek [29] to conclude the following regarding the theory of comparative advantage (as an important component part of the neoclassical economic paradigm):

- The point of departure of my paper is that the traditional theory of comparative advantage on which modern globalization is based is incorrect and not applicable to the present day conditions of world trading. Instead I propose a theory of destructive trade which explains much better what happens in world trading today.

- Destructive trade leads to a world where a minority of the rich dominates a majority of the poor and what is worse, the situation tends to grow ever worse, the rich becoming relatively richer and the poor poorer. Technically, the situation is explosive.

Discussion on the convergence between LDC's and developed countries in terms of the role of free trade and the role of capital flows can hardly escape the Lucas paradox. This paradox is reflected in the fact that capital does not flow into poor countries where capital is scarce, against the neoclassical view that the return on capital accumulation should be higher where capital is rare. Lucas concludes that the neoclassical paradigm should be abandoned, while Reinhart and Rogoff conclude that the risk premium due to bad behaviour is the main culprit [15]. Cohen points out that the capital/output ration is, in general, the highest among poor countries: This can be coined as an anti-Lucas paradox. "The intuition that we offer is that poor countries, lacking other inputs such is infrastructure, use physical capital as a substitute for the scarcity of those missing inputs."

At this moment it seems useful to get an insight into the critics of the neoclassical economic paradigm and the theory of comparative advantage provided by Stiglitz and Charlton [30], Horvat [16], Rodrik [31], Panic [19], Pitelis [20], Adelman [18]. It is not a surprise that Adelman [18] introduced the term "KISS" ("keep it simple,

stupid") in her "Fallacies in Development Theory and their Implications for Policy". She writes: "I shall argue that the discipline of economics has enshrined the "keep it simple and stupid" principle as an overarching tenet, imbibed in graduate school that can be violated only at the violator's peril. This principle demands simple explanation and universally valid propositions. It has led to three major fallacies, with significant deleterious consequences for both theory and policy: single-cause theories of underdevelopment; a single-figure-of-merit criterion for development; and the portrayal of development as a log-linear process."

Historical and simultaneously challenging evidence corroborated with plenty of examples of developmental experiences of many countries throughout the history, and in favour of thesis by Adelman, Stiglitz, Horvat, Pitelis, Easterly, etc., can be found in the book by Angus Maddison [27] titled "The World Economy".

On Economic Crisis

Neoclassical economics does not recognize the possibility of crisis. Still, the world economy at the end of September 2008 looked like as it is at the brink off the most serious economic crisis-slump in the world economic history ever before. In the meantime, the US President and the members of the US Congress proposed a 700 billion $ bailout package. The package represented the biggest financial intervention since the beginning of the development of capitalist market economy. Not so long ago, the mere decision on the proposal for a government intervention would be a serious and life threatening mistake for an economist. He/she would be blamed of manipulation and stupidity. However, history teaches us that there was the year 1929. Therefore, at the end of 2008 (as well as 2011) a question could be asked: did or did not the US Congress (and the powerful economists) learn the lesson from 1929? Milton Friedman believed that the crisis of 1929 would have never happened should the central banks have existed and intervened in the economy. He considered the 1929 crisis as a liquidity crisis. However, after the government intervention in the 1930s had pro-inflationary effects, and even signs of stagflation, Keynes stated: "Three years ago it was important to use fiscal policy in order to support investment. Soon it might be equally important to contract

some investment. As much as it was important to maintain the budget deficit in time of the crash, now it is useful to resort to a different policy. I think we are approaching or we have approached the point when intervention from the centre becomes useless“. In 1937 Keynes was deeply disturbed by high inflation rate (12% in the United Kingdom) that has already coexisted with the 12% unemployment rate [32].

The interpretation of Keynes's explanation of the economic crisis, which is accepted worldwide, is that the crisis of 1929 was due to insufficient demand consumption [33]. If such an explanation was right and a proper one, the state intervention like the one proposed by the US Congress (in 2008), could successfully bridge all three Keynes's traps (liquidity trap, trap of expectations and the trap of marginal efficiency of capital) but under drastically changed political circumstances. Therefore, from the angle of the 2008 crisis, it seems utterly important to find out who was right and who was wrong in explaining the 1929 crisis: Friedman (namely, neoclassical economists-monetarists, like A. Metzler) or Keynes (but not Keynesians who treated the 1929 crisis as a crisis of insufficient consumption)? Could it be that Marx was right as far as explaining the crisis in the 19th century and the crisis in general? This is why we resort to both Keynes and Marx for some of the lessons to be learned.

Keynes and Marx on Economic Crisis

Keynes

International “mega-mergers” taking place all over the world ever more confirm Marx’s proposition [34] which can be expressed as follows: “as soon as formation of capital were to fall into the hands of a few established big capitals the vital flame of production would be altogether extinguished. It would die out. Things are produced only so long as they can be produced with a profit. Development of the productive forces of social labour is the historical task and justification of capital. This is just the way in which it unconsciously creates the material requirements of a higher mode of production”. The last case in point that confirms this thesis is the acquisition of Merrill Lynch by J.P. Morgan and Lehman Brothers by Bank of America during September, 2008. Keynes [35] thought (as we read it) that the decline of the marginal efficiency of capital was/is the main cause of economic crises. Namely, he thought that the aforementioned decline provokes the trade cycle. “By a “cyclical” movement we mean that as the system progresses in, e.g., the upward direction, the forces propelling it upwards at first gather force and have a cumulative effect on one another but gradually lose their strength until at a certain point they tend to be replaced by forces operating in the opposite direction. We mean also that there is some recognisable degree of regularity in the time sequence and duration of the upward and downward movements. There is, however, another characteristic of what we call the Trade Cycle which our explanation must cover if it is to be adequate; namely, the phenomenon of the “crisis” – the fact that the substitution of a downward for an upward tendency often takes place suddenly and violently, whereas there is, as a rule, no such sharp turning-point when an upward is substituted for a downward tendency“. According to Keynes, [35] prosperity suddenly changes the face and it is violently converted into a crisis. The market mechanism does not function the other way around so quickly, if it does at all automatically. Keynes thought that crises are not caused by the rise in interest rates. Crises are a consequence of a sudden decline of the marginal efficiency of capital. “The later stages of the boom are characterised by optimistic expectations as to the future yield of capital-goods sufficiently strong to offset their growing abundance and their rising costs of production and, probably, a rise in the rate of interest also. It is of the nature of organised investment markets, under the influence of purchasers largely ignorant of what they are buying and of speculators who are more concerned with forecasting the next shift of market sentiment than with a reasonable estimate of the future yield of capital-assets, that, when disillusion falls upon an over-optimistic and over-bought market, it should fall with sudden and even catastrophic force.”

“At the outset of the slump there is probably much capital of which the marginal efficiency has become negligible or even negative. But the interval of time, which will have to elapse before the shortage of capital through use, decay and obsolescence causes a sufficiently obvious scarcity to increase the marginal efficiency, may be a somewhat stable function of the average durability of capital in a given epoch. If the characteristics of the epoch shift, the standard time-interval will change.” In addition, the duration of a slump has a definite relationship with the “normal rate of growth in a given epoch”. During the slump capital is sold off. Goods are sold regardless of the price. A decline of the marginal efficiency of capital badly affects the propensity to consume by both drastically lowering the level of investment and by firing the workers. We think that Keynes’s thoughts could

be considered as especially relevant for developed societies of today since a "serious fall in the marginal efficiency of capital also tends to affect adversely the propensity to consume. For it involves a severe decline in the market value of Stock Exchange equities. Now, on the class who take an active interest in their Stock Exchange investments, especially if they are employing borrowed funds, this naturally exerts a very depressing influence. With a "stock-minded" public, as in the United States today, a rising stock-market may be an almost essential condition of a satisfactory propensity to consume; and this circumstance, generally overlooked until lately, obviously serves to aggravate still further the depressing effect of a decline in the marginal efficiency of capital." Crises cannot be softened by lowering the interest rate. "I conclude that the duty of ordering the current volume of investment cannot safely be left in private hands". This sentence has been written by J.M. Keynes in 1936 [36].

Marx

According to Marx [34], the stage of hyper-production, which we can call the stage of stagflation (according to its full description expressed in "The Capital"), converts into a new stage of business cycle called slump. A slump represents deep deflation. The preceding increase in prices, over-production of goods (or production of goods over the level of production which guarantees the expected profits), must be reduced within the "normal limits". This process is a painful one and it expresses itself through the fall in prices and income, mass unemployment and closure of companies. "The value of commodities is sacrificed for the purpose of safeguarding the fantastic and independent existence of this value in money. As a monetary value, it is secure only as long as the money is secure. For a few millions in money, many millions in commodities must therefore be sacrificed. This is inevitable under capitalist production and constitutes one of its beauties." The demand for means of payment is a mere demand for convertibility into "money", so far as merchants and producers have good securities to offer; it is a demand for "money-capital" whenever there is no collateral, so that an advance of means of payment gives them not only the "form of money" but also the "equivalent" they lack, whatever its form, with which payment can be made. This is the point where both sides of the controversy on the prevalent theory of crises are at the same time right and wrong. Those who say that there is merely a lack of means of payment (and we may say that Friedman has seen the causes of the Great Depression of 1929 in such a way as Paulson and Bernanke do nowadays), either have only the owners of "bona fide" securities in mind, or they are fools who believe that it is the duty and power of banks to transform all bankrupt swindlers into solvent and respectable capitalists by means of pieces of paper. Those who say that there is merely a lack of capital are either just quibbling with words, since precisely at such times there is a mass of "inconvertible" capital as a result of over-imports and over-production, or they are referring only to such cavaliers of credit who are now, indeed, placed in the position where they can no longer obtain other people's capital for their operations and now demand that the bank should not only help them to pay for the lost capital, but also enable them to continue with their swindles.

Who are the Neoclassical Economists?

Basic Principles

Neoclassical economists have come to know about certain principles of the economy or the knowledge of market and economic principles. According to them, the invisible hand, automatically establishes equilibrium on both factor and product market and in the whole national economy. Under the condition of pure competition, position of a firm is nothing more than a function of its income and expenditures. We should immediately recall one of the basic principles of neoclassicists, and this is the principle of diminishing returns and increasing costs. Starting from the principle of diminishing returns, the firm seeks to maximize its profit. To this end, the firm decides on the choice of factors of production, thus forming a specific production function. The position of the firm is not the same in the short- and in the long-run. Profit maximization in the short-run brings the company, and the industry as a whole, in a position to deal with the (long-run) problem of production without profit. Such situation forces the firm to operate in at least two directions: to try and to reduce production costs, on the one hand, or to move their capital in other industries, on the other hand.

Thinking about the behaviour of firms in large part corresponds with thinking about the behaviour of households. The goal of each household is to maximize the households' utility. In this objective, the household creates supply and demand for labour. Certainly, the demand for labour is the function of firm's profit and its position in the market.

Neoclassical economists have accepted the assumption of pure competition as one of the basic assumptions of every analysis. The time in which they lived gave them the right to do so. The market operates under conditions of pure competition when, according to Baumol [37], the following conditions are met:

- There are a large number of manufacturers. Firms provide supply of homogeneous products. Each firm can not affect the price nor as a buyer nor a seller. The company is the so-called "price taker" – Isn't today this assumption an abstraction?
- The homogeneity of the product. A large number of bidders on the market offer a homogeneous product. From a buyer's point of view it is irrelevant from whom he buys the goods. - Is not this assumption also an abstraction?
- Entry and exit freedom is present on the market. Companies enter and leave the market guided, above all, by the criterion of profit maximization and let us underscore the expected profit. - Is not this assumption also an abstraction?
- Market entrants have perfect information. It includes market transparency and full awareness of the company about the state and prospects of the market, especially when it comes to prices, supply and demand. - Is not this assumption also an abstraction?
- We may supplement this picture of pure competition by including international markets, rules of free trade, and the one-price law. Commodity arbitrage and the one-price law make it possible to equalize the prices of goods at the international level. - Is not this assumption an abstraction?

Neoclassical Economics as a Virtual Economics

If all the assumptions regarding neoclassical economics are abstractions, is not then neoclassical economics a virtual economy? Are not Pareto optimality and Say's law virtual ones? On the point of Pareto optimality national economy is confronted with the principle of "capitalist communism": the same amount of capital brings about the same amount of profits. This is why Keynes classified the neoclassical economy as a special case and created the "General Theory". Is Keynes' theory a general theory or theory related to one phase of the economic cycle - recession or depression? If so, and we believe that it is, Monetarism is then tied for the second phase of the economic cycle – stagflation. Therefore, even Monetarism is not general-complete economic theory. Thus, Keynesianism, Monetarism, neo-Keynesianism, post-Keynesianism, the School ofrational expectations are not general economic theories. These are the offspring of the virtual neoclassicism related only to a specific state of the economy on the path of its continuous movement and dynamics. These theories are theories of economic policy (nothing more than economic schools) related to the economic regulation of movement of a national economy - the "territorial" state. We think that for a time in which we live, and this is a time of globalization, those schools are increasingly less relevant and sometimes even counterproductive.

Do we have a Theory of Economic Globalization – The Economic Theory for our Time?

There are many definitions of globalization. We prefer our own, which says that globalization is a process of privatization of the world's economic resources by big capital, which is very often virtual and hybrid and expressed through exponential expansion of derivatives. In the last two decades [38] these derivatives reached a fascinating amount of 457 trillion Euros. And, if privatization represents a political process with economic consequences, we dialectically can conclude that globalization is a process of transformation of "territorial" (national) state into "mega-capitalism". In other words, into a world "market" state dominated and led by transnational banks and transnational corporations.

The basic economic entities of our time are becoming transnational corporations as the entities which reflect globalization process. The basic microeconomic principle of their behaviour is the principle of increasing returns and diminishing costs! Are any of the assumptions of virtual neoclassicism valid in a global world? If not, then neoclassicism in the global economy deserves to go into the memory hole. The global economy does not have a proper theoretical construct. We are caught in the trap of economic realities of globalization and the application of virtual economies and / or possibly its offshoots (schools) relevant to the "territorial" state. Virtual neoclassicism was allegedly designed to lead to economic convergence both in "territorial" and in global economy. But, in reality, it has led to economic inequality and divergence in the "territorial" state. In a global, market economy

and the "market" state it must produce even more divergence. Is European Union's crisis case in point to testify this despite the intervention of Brussels and partly of each Member State? The European Union has become the functional integration of large capital centres more than the community of nations. The principles of "territorial" state and "market" state have been mixed and, therefore, it is not surprising that the EU's future is uncertain.

Consequently, under conditions of globalization, small and medium-developed countries can hardly have their own strategy of economic development. Their strategic decisions cannot be isolated, independent and national. Their dimensions of comparative advantages are changing. They are becoming not only "price takers" but "rule takers" as well. If such a state is also an indebted one, it must therefore form its own development strategy that will hold up the rules of the game dictated by the large capital centres (namely, transnational corporations and mega-banks). Certainly, in the transition period to full globalization, developed countries and their transnational corporations are not only "price" but also the "rule makers". They are the carriers of cybernetic neo-colonialism as sublimation of interests of developed countries and their large capitals-corporations in the field of global economy.

Globalization provokes a number of issues related to the process of economic development and its effects on both the host country and the capital exporting country. For example, an American transnational corporation produces a product in China while exporting capital from US. Then, it imports the produced goods from China back to the US. From the point of view of standard balance of payments statistics this transaction is clean and clear. However, from the angle of property rights (especially capital), policy and economic issues seem to be much vaguer on how to treat such a transaction. Does the US import its own goods produced by its own capital and knowledge, or does it import Chinese goods? Foreign direct investment and transnational corporations in the global economy provoke confusion between the "territorial" state and "market" state. The balance of payments issue, at first glance, is perhaps only the beginning of opening the Pandora's Box which will have to be opened and studied by the new economists. Once opened, the Pandora's Box of globalization will have a profound impact on relations between the "territorial" and "market" state as well as on the relations between virtual neoclassicism and real corporatization of the world.

Conclusion

Towards Mega-Capitalism

After reviewing the historical experience concerning development of both economic reality and economic theory, we have concluded that the strongest interest groups are the ones that define the economic system, economic policy and economic institutions. If these interest groups today are depicted in a form of corporate power centres, as we believe to be so, then we are free to suggest that we are heading towards "Mega-capitalism"!

"Mega-capitalism" is the next stage in the development of capitalism, which will be dominated and led by both mega-corporations and mega-banks. This, in turn, will result with global cybernetic robotization of workers (namely, cybernetic slavery). This process might be supported by neuro-economics, which we would define as cybernetisized neoclassical economics applied under imperfect market conditions. Sure, the process will be followed by the death of the "territorial" state. This process reflects the centralization of capital on a global scale. This process, however, is evolutionary and repetitive since the beginning of the capitalistic way of production. A man-worker is no longer a mere factor of production on the labour market (as stated in the neoclassical theory). A man-worker becomes cybernetisized object (a robot) which contributes to the morbid maximization of the first principle of capitalism: profit.

In addition, Krugman in The New York Times [39] sees the world as a corporate world dominated by: lobbyists, guns and money. Of course, there is a possibility for a different scenario of the future that is ahead. That scenario depicts a path that is leading towards the so-called cybernetic post-capitalism, depending on whether the evolution of development of capital (capitalism) will occur spontaneously or will it be partially regulated by different interest groups. Evolutionary transformation of capitalism would give the right to Marx [34] and Keynes [36] and their visions of a new society as they expressed in the "Capital" and in the "Economic possibilities for our grandchildren". The first principle of the welfare society is to become global citizens, and that means the elimination of the "market" state. Hilferding's fate of the world has been similar except the fact that the path towards post-capitalism is paved by the "expropriation of expropriators".

If, however, the process becomes retrograde and the "territorial" state overthrows the "market" state, then the thoughts and reflections of the French School of economic war (which is these days advocates the so-called "intellectual protectionism") might become very realistic and attractive. We think that modern technology and cybernetisation of the economy and civilization might not survive this retro course of events without global social, economic and political earthquake a few degrees stronger than that of 1929.

Taking everything in consideration, we are left to conclude that the process of globalization of the world economy and therefore world politics is not only heading towards an unknown future but also it lacks any significant economic and theoretical explanation.

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