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How do We Arrive at Our Intended Destination?

Thoughts on Sustainable Growth and Financial Risks

What is the greatest traffic risk? That car-drivers and pedestrians, the participants in traffic, do not keep to the rules. What is the greatest risk in the area of state finances? Exactly the same, the breaking and ignoring of rules.

The preceding comparison may seem strange but it highlights that in any system with multiple elements and participants the keeping of rules, which apply to and are known by all, is the basis for its effective functioning.[1]

ON GROWTH

In light of all this we can pose the question of whether economic growth is sustainable. The question is complex but we can state with certainty that, in the traditional sense of the word, material growth cannot be sustained indefinitely. To paraphrase a definition from the science of physics: within a finite system there cannot be infinite growth. It is worthwhile starting out from this general rule. Since the size of any system, in our case the output of the (world) economy, would need to increase twofold in 70 years in the case of a 1% growth rate and in 15 years in the case of 5% growth. This is clearly not sustainable development in the long term.

It is worth reviewing the economic growth of previous decades and centuries in order to understand how the dogma of never-ending economic growth came to dominate our general thinking.

From scientific experience it can be concluded that one of the essential elements for growth is surplus production. In so-called gift economies surplus does not occur: what is gathered is shared by the family – this practice can, in fact, be observed in families today. In the next stage of development, in so-called exchange economies, surplus came about, which then was used to trade with. From here it is a straight path to the market economy, as we understand it today, whose rules and regulations were first described by *Adam Smith* in the 18th century. This system is based entirely on surplus production.

The other defining element of economic growth is population growth; in fact for much of economic history, growth of the world econ-

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omy was, exclusively, a result of an increase in the population. And that is why – contrary to the general belief that, in today's understanding, growth is a general phenomenon – we can only talk of this since the arrival of technological development from around 1750. Prior to this the economy, essentially, did not grow, this paradigm change was only made possible by the arrival of industrial energy production, the steam engine and, later the internal combustion engine. The spread of electricity and mains water supply, and the arrival of information technology can be considered the second and third pillars of the industrial revolution. It should be emphasised that, together with technological development, money has become an extremely complicated resource, especially if we consider those techniques used to try and "make" money from money. With this we have arrived at another important, if not the most important, element of growth: finance, which is linked to the appearance of money.

In any assessment of financial risks an understanding of the concept and functions of money is clearly indispensable. In past times money came into being as an aid to trade (means of exchange), which enabled simple barter trade to be carried out, using rules accepted by the community. In addition money measures value (instrument of value measurement) with the help of which the value of different goods can be compared. Above all this money can be used to store value (instrument of accumulation): in fact the development of this function may have initiated the development of the banking system, the basis of which was the issue of a receipt for valuables stored. From the point of view of growth banks are especially important since it is characteristic of the banking system to invest many times the value of its assets in the form of loans.

Apart from the already mentioned unsustainability it is also a problem that we hold growth to be a basic tenet of economics and the solution to everything, that is, the sole indicator of prosperity: growth means more jobs, higher returns and more consumers. The situation is undoubtedly complicated by the fact that the collateral for the accumulated goods is, to a large degree, based on the promise of growth. The sustainability of the pension system, for example, is dependent not only on actual savings but – since these savings are invested – on whether there is growth. It follows from this that it is also a problem if we overemphasise growth: this can lead to the formation of bubbles and, as a result of this, finally no growth, and no return on investments. In addition to this growth is the basis for the financial system, since without growth there is no new money in the system, interest cannot be repaid, not to mention capital– which is why we can say that our current financial system is, in effect, a global pyramid scheme.

ON THE NEW ECONOMIC WORLD ORDER

In spite of the above, the mainstream schools of economics agree that continuous growth is a realistic and sustainable goal. The question is – and this constitutes the basic difference in opinion between Keynesian and neoliberal economic policies – with which means growth can be achieved: with state intervention or reliance exclusively on the mechanisms of the economy and the market. The fundamental error in both approaches is that they do not take into account the finite nature of natural resources. They are simply considered as one form of capital, and capital – by definition – is replaceable.

There exist, however, certain economic elements, such as the aforementioned natural resources, which cannot be replaced. Consequently, only growth, which can be characterised by declining returns in the long term, can be envisaged and there will be a need for the

introduction of stationary, that is balanced, economic structures for this smaller growth. The current growth-based economy, therefore, should be replaced by a stationary economy. This will present significant challenges for all players in the economy, for heads of state and all those who control state and public finances.

One of the greatest questions of our age is how to switch to a balanced, stationary economic model since growth, as we understand it today, will come to an end, because – as I mentioned above – natural resources will run out, growth has a significant, negative impact on the environment and the financing system is unsustainable for both financiers and borrowers.

The continual striving for growth is, in fact, at odds with the laws of nature. World leaders have to appreciate that we are going to live in a stationary world which will require fundamental changes in financial policies (monetary and fiscal) as well as policies is other sectors (food, water energy and transport). In short, there will be major changes in politics as well as in everyday life. Adapting to a stationary world is an evolutionary process, through which we can avoid the monumental catastrophe which the collapse of the world economy would (or could) mean.

It is important to emphasise that there can be growth of a technical or local variety within a stationary economy. A good example of this is the United States where, in recent years, alongside increasing unemployment, there has been growth, although this is thanks to state intervention, in other words largely due to verbal bravado and the quantitative easing of monetary policy. This is true even if the continuous printing of money is only a treatment of symptoms and not sustainable in the long term.

We may then ask that if growth in the contemporary sense does not exist in the stationary economy what will take its place. First of all it must be stated that the end of economic and material growth does not mean an end to the improvement in quality of life: in a balanced economy there is no growth as we know it today but there is life and development. There is no doubt, however, that this "new order", in relation to competition and cooperation, will be different from the current one. The current economy is a fierce competition in which there are fewer and fewer winners and more and more losers. In contrast the balanced economy is one based on cooperation, similarly to the previously mentioned family economy.

There are certain areas in the balanced economy – mainly intellectual/cultural activities and services– where there are no limits to growth as currently understood. This will not, however, manifest itself in the classical form of mass production and will not automatically mean more "manufactured products". For this reason one of the most important objectives in preparation for the stationary economy is to create valuable and value-creating, service-based employment opportunities for all. This also provides a solution for the distribution of income, since it is extremely complicated to fairly distribute the wealth created by a few, the best solution being for all to receive a share through work.

ON THE FINANCIAL RISKS

The greatest financial risk in the current economic world order is the accumulation of debt. Indebtedness is none other than the illegitimate provision of credit. It is a thought-provoking fact that the level of world debt has increased sixfold since 1980 and has, with one exception, grown faster in each of the last 50 years than total global output. The question is obvious: if debt continuously

grows – at a faster rate than output – then who is going to repay it and how? The answer is surprisingly simple: the debt is never going to be repaid.

Behind this accumulation of debt is an international political game which allows us to keep a record of our outstanding debts while it is clear to all that nobody is going to pay back this mass of debt. Globalisation has played a significant part in bringing this situation about. Developing nations, for example, received huge loans, often for pointless investments in infrastructure and now have to sell their natural resources to service their debts. The very resources of which the developed countries have less and less. At the same time the developed countries' businesses have located their manufacturing facilities in under-developed countries in order to make use of the local natural resources. The decline in manufacturing capacity in the developed world encouraged financial investors to create profit directly with financial instruments. As a result of this money appears to make money which leads to a kind of contradiction: if money is a measure of value, how can it also be a creator of value? There is definitely a need for the national and global market regulation of this contradiction, and I hope and believe that our economists, those involved in financial affairs and, not least, our political leaders will be capable of eliminating this contradiction.

Finally I would add one more point to the above: does the global economy function without states? The answer is obviously no, but we must understand that an investing state takes risks in the same way as an in individual investor. And that is why we need very clear, transparent control systems which are tasked with monitoring not only the legal (lawful) spending of public funds but also its expediency. It is not enough to monitor whether public funds are used in line with the rules we ourselves created, we also need to control that these resources are used expediently and efficiently. In other words: it is not sufficient just to obey the rules of the road, it is also important to reach our destination in the shortest, fastest and most economic way, without hindering others.

Note

[1] The article is an edited version of the presentation by József Pálinkás at the State Audit Office's "Assessment and management of country risks and long-term public finance risks" conference on 9th October 2013