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Democracy and Market Economics in Central and Eastern Europe:

Are New Institutions Being Consolidated?

Ten Questions on System Transformation and "Globalization"

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We are going through a historic period of the century in terms of systemic changes in society. Namely, I am referring to systemic changes caused by the self-inflicted collapse of so-called socialist society and the subsequent process of constructing new types of society. This process began towards the end of the 20th century and is still ongoing and coincides with "Globalization", which was said to have begun in the 1980's and has been rising in prominence ever since. Many economists take it for granted that globalization means nothing more than the extensive and intensive development of capitalism, and the collapse of socialist societies is a part of the historical process of capitalization. Is it true that contemporary globalization is identical to the "capitalization" of economy?

Some might claim the transformation is the transition from socialist economy to capitalist economy. Others may say that it is the transition from planned economy to market economy. Do these two schools of thought differ from each other or do they express the same sentiments using different terms? Could it be intimated that these views are too straightforward and overly stereotyped to depict contemporary society?

The concepts generally used by economists are seldom clearly defined and are therefore hardly self-explanatory. This brings up several questions: Firstly, if the capitalist and the socialist systems switched historical roles with each other at the different stages of human history? Secondly, whether the present transformation is final and complete or set to change its role again in future or not? Also, does it hold that the formerly existing socialist system actually worked on the basis of economic planning? If we presume the answer is yes, then what kind of planned economy was it in fact? If not, then what was it at all? Many questions arise from the stereotyped usage of terms used by economists, who deliberately decline to analyze the precise meaning of terms and concepts. They could rightly be asked the precise definition of market and plan, or of capitalist and socialist economy. These are not particularly easy questions to answer if we consider in what sense that the West European countries can be said to be capitalistic when we observe their redistribution rates of GDP that amount to nearly half of GDP.

What is the transition or transformation in the contemporary world if anything at all? Transition moving from "where" to "where"? Transforming from "what" into "what"? These answers are also hardly apparent and therefore it is worthwhile raising certain questions. As long as we stay in the flat world of stereotyped economic concepts, we will never succeed in understanding the historical and deeply layered movements of society. What is called for here is an element of philosophical thinking or the use of moral science for analyzing the depth of society and history, which orthodox economists have long lost by ignoring classical economics.

Question 1: Transition or Transformation? – Transition moving from “Where” to “Where”? and Transforming from “What” into “What”?

Interestingly enough, various analysts use different conceptual pairs for characterizing the contemporary transformation of society. Therefore, first of all, I would like to check the most prevalent pair concepts in order to make their understanding clear.

When one asserts that contemporary transition is from **planning** to **market**, it is taken for granted that the socialist regime was based on planned economy and non-socialist economies have their roots in market economy. Is this true or false?

When the transition is from **socialism** to **capitalism**, the given system change is conceived as an ideological change. Is this really the case?

Under transition from **socialism** (**communism**) to **market**, the usage of concepts is not evident. It could be understood that the change would be from an ideologically distorted system to economically reasonable system. However, the pairing of concepts is neither precise nor correct.

When that the transition is from **state** to **market**, it expresses some symbolic essence of the change in terms of sovereignty of economic decisions. Again, the pairing of concepts is not appropriate.

Then, how should the fundamental change of human society in our era be understood? In the most abstract sense the change is in the fundamental disciplines of human activity and behavior from allocation (distribution) to exchange. The change of disciplines extends from daily human life through economic activity to political life. In its extent and influence we might say that the change is not a mere shift, i.e. a transition from one state to another state, but transformation of social constituents based on entirely different disciplines.

This is why I use the term “transformation” rather than “transition”, and why I propose to use more profound conceptual pairings in constructing comprehensive and multi-layered understandings for our contemporary overhaul of society.

Question 2: Were the so-called socialist economies planned economies at all?

As history shows, there never was economic planning in its true sense throughout the history of socialism; that is planning based on precise economic calculation. The reasons are so simple and need not be explained in great detail.

First, there were no computers, which could be used to make economic calculations throughout the socialist regime. Even if the most advanced super-computers are available for economic planning today, timely and reliable economic calculation is almost impossible in the scope of national economy because of the complexity and difficulty of economic calculation. Then, how was it possible or not possible for the socialist planners to execute their economic calculations with paper and pen?

Second, no value parameters existed to which economic calculations could be made in the old regime. Prices were distorted by political intentions and market imitation was never possible.

Third, communist leaders primitively believed that political intervention with economic process could be legitimatised by socialist theory. The actual impossibility of economic calculation also helped political leaders intervene with economic decisions. Thus, political valuation was always given priority over rational economic calculation, which resulted in the arbitrary management of the national economy.

Then, in fact, what in reality was so-called "socialist society"?

Soon after the "socialist revolution", the national economy merely became a mere authoritative rationing system of materials based on political decisions, which in fact derived from the war-time rationing system used during the First World War. Therefore, I named the socialist system of the 20th century as "Wartime Socialism".

What is the essence of the "Wartime Socialism"? It is the authoritative allocation system of goods and services in the name of planning, and the difficulty of allocation enforced the entire system to only routine rationing exercises, which inevitably lead the national economy into long-term stagnation.

Table 1 Comparison of Social Moments between the Two Activities

Social Moments	Basic Economic Activity	
	Exchange	Allocation
1. Nature of communication	Informational and bilateral	Physical and unilateral
2. Institutionalization	self-organizing market system	Bureaucratization
3. Personal relationship	Depersonalization-civilization	Personalization-decivilization
4. Organization	openness and transparency	Closeness and secret
5. Social behavior	Independence and self-responsibility	Dependence on authority
6. Complexity	Continuously increasing	Degeneration into simplicity
7. Self-development	Autonomic and continuous	Destructing and –deteriorating

Notes: (1) A moment is a driving factor for autonomous developments in a positive or a negative direction which exists at each stage of basic exchange and redistribution behavior.

(2) Nowadays, every national economy consists of two main economic activities: exchange and redistribution. The question is how the mixture of the two is composed in a given economy. The socialist economies were exclusively organized based on the redistribution principle, where almost 70-80 % of GDP was centrally redistributed. On the contrary, so-called capitalist economies largely introduced the redistribution principle after the Second World War, and thus various mixtures of the two combinations have been experimented with, which leads to the success of the further Development of national economies. The self-induced collapse of the socialist economy can be explained by its inner moments that degenerate and destruct economy and society.

If we observe the true reasons behind the self-induced collapse of the socialist system, then we cannot say simply that the transition should be from planning to market based. Such a stereotyped dichotomy, which I would like to name "flat concepts of two-dimensions", does not help us to comprehend the fundamental transformation of society. When we analyze a social movement on the scale of a century, we should get into more profound philosophical analysis, which helps deep and multi-layered conceptualization of understanding.

We need far more fundamental concepts for analyzing key changes of society than the mere dichotomy of planning and market. This is the reason I introduced the most fundamental comparison of basic social activities, which makes it possible for us to carry out a profound analysis of human society.

Table 2 Tax Structure and Tax Revenue as Percentage of GDP, 2000

	A. Direct Tax /GDP	B. Indirect Tax /GDP	C. Social Contribution /GDP	Redistribution Rate A+B+C /GDP
Hungary	9.5	18.1	11.5	39.1
Poland	10.2	13.9	10.0	34.1
Czech Republic	8.9	13.2	17.3	39.4
CEC average	10.9	15.1	12.9	37.5
Sweden	23.4	15.6	15.2	54.2
Austria	12.4	16.4	14.9	43.7
Germany	11.4	11.7	14.8	37.9
Spain	9.8	13.3	12.1	35.2
Portugal	10.3	15.4	8.8	34.5
Greece	10.5	15.9	11.4	37.8
EU15 average	14.9	14.4	15.2	41.6
USA	15.1	7.6	6.9	29.6
Japan	9.2	8.0	9.9	27.1

Source: OECD, *Revenue Statistics 1965-2001*, Paris, 2002.

Question 3: Is it right to classify the West European countries with high GDP redistribution rates as capitalist economies?

Not only the pair concept of plan and market, but that of capitalist and socialist is also a highly commonplace and vulgar understanding of the contemporary change of society. There has never existed pure capitalist or socialist society. Especially after World War Two, all the developed countries introduced the redistribution system of income, which originated from the socialists' ideas. Hence, what can be observed today is a large variety of market limitation systems that utilize income redistribution policy, even after large scale privatization has been executed in European developed countries since 1980's.

What is the observation today?

First, the ownership of production has overwhelmingly moved into private hands over last twenty years in Europe. Nowadays production in European countries is organized in non-public ways. However, does it mean that the production sphere has been captured by capitalist ownership? Privatization of European companies in 1980's and

1990's was executed mainly in the utility industry and the banking sector. The newly borne companies are owned by many shareholders, a large of part of which are institutional investors. That is, a newly privatized company is not individually owned by capitalists in the classical sense, but collectively owned by large non-personal legal entities and individual persons.

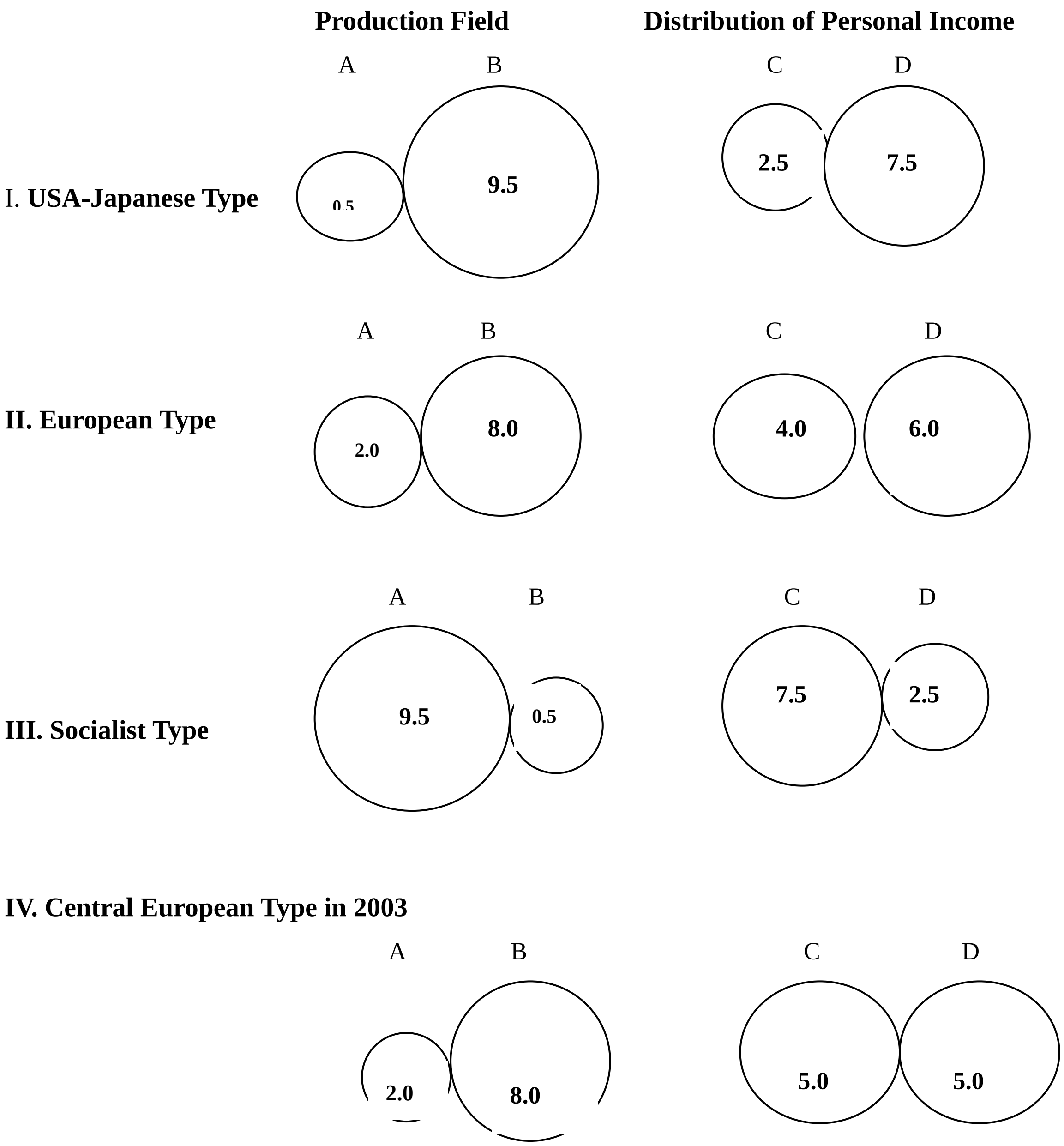

Figure 1 an Illustrative Comparison of Structures in Production and Income Distribution

Notes: A and B represent the weight of state-public enterprise and private enterprise respectively. C and D show the distribution of personal income between the portion paid to the public budget and the remaining portion available to inhabitants.

Second, there can be observed a strong contrast between USA (Japan) and Europe in terms of income redistribution. The USA and Japan seem to prefer personal disposable income to socially redistributed income on one hand, and Europe is oriented toward maintaining a high rate of redistribution for constructing a peaceful and human-friendly society on the other. That is, even if production sphere is almost entirely opened for private ownership, the government retains high degree of the income flows in order to lessen the discrepancy in social strata and injustice arising from excess market competition.

Then, how can the present make up of the European economy be characterized? I would say that although the exchange principle is widely introduced in the production sphere to increase competitiveness, the government has played the key role of providing social stability by exercising the allocation principle. The adjectives “capitalistic” or “socialistic” are too simple and too ideological to characterize the present forms of the social system.

Question 4: Actually, what was and has been the essence of privatization in the transforming economies? Who takes advantages of privatization? Why and how has the mafia economy (so-called Red Mafia) been brought about from the countries under strong dictatorship in the former regime?

Generally speaking, system transformation in our era is a reorganization of society on different disciplines. In the ex-socialist countries the reorganization has been executed in a historically short period of time by destroying the old political regime and ending the state ownership of production. Who took the initiatives of this transformation and who took advantage of privatization?

Privatization in the transforming countries was and has been the *de facto* relocation and reallocation of state assets among the people. In countries that suffered from capital shortages the voucher privatization system was adopted, except in Hungary, which invited foreign capital during the first stage of transformation. There were millions of cases of scandal involving voucher privatization, including misinforming over the true value of companies and suspect privatization procedures. In the chaos of the destruction of the old regime those who took advantage of privatization and acquired large portions of state assets were former party leaders, elite bureaucrats and top managers of state companies in the old regime. It is simply because they knew what the most valuable were and where they lied. Insider information and personal contacts made it possible for them to create wealth for themselves out of the destruction of the old regime. The classic case is Russia, where all of the Forbes ranking billionaires are shareholders of huge oil, gas and metal companies which were privatized in suspect ways under the reign of former President Yeltsin. How could they obtain state assets worth billions of dollars? It was in reality the theft of state assets through utilizing various cases of intrigue for acquiring state assets almost free of charge.

Table 3 General Description of Voucher Privatization

Country	Year voucher distribution began	All shares issued in waves or continuously?	Are vouchers bearer, tradable or non-tradable?	Is investment in funds allowed, encouraged or compulsory?
Albania	1995	Continuously	Bearer	Encouraged[1]
Armenia	1994	Continuously	Bearer	Allowed[2]
Bulgaria	1995	Waves	Non-tradable	Encouraged
Czech Rep.	1992	Waves	Non-tradable	Encouraged
Estonia	1993	Continuously	Tradable[4]	Allowed[5]
Georgia	1995	Continuously	Tradable	Allowed[2]
Kazakhstan	1994	Waves	Non-tradable	Compulsory
Kyrgyzstan	1994	Continuously	Bearer	Allowed[6]
Latvia	1994	Continuously	Tradable	Allowed[5]
Lithuania	1993	Continuously	Non-tradable	Allowed[5]
Moldova	1994	Waves[7]	Non-tradable	Encouraged
Poland	1995	Waves	Tradable	Compulsory
Romania[8]	1992	Continuously	Bearer	Compulsory[9]
Romania	1995	Waves	Nontreadable[10]	Allowed
Russia	1992	Continuously	Bearer	Encouraged
Slovakia	1992	Waves	Non-tradable	Encouraged
Slovenia	1994	Continuously	Non-tradable	Allowed
Ukraine	1995	Continuously	Non-tradable	Allowed

Note:

1 By July 1996 only one or two funds had applied to receive vouchers.

2 Although a legal entitlement exists to invest vouchers in funds, in practice this option was limited.

3 The results of the first voucher auction were cancelled in March 1995, and fund licenses were suspended from then until August 1996.

4 Vouchers were nontradable at the outset of the programme, but cash trading was legalised in the spring of 1994.

5 Citizens could also exchange vouchers for other things such as apartments or land.

6 Citizens could invest their vouchers in housing as well as shares. They can sell their vouchers to funds, but no formal mechanism exists for them to subscribe to funds.

7 Although the design of the Moldavian program was based on the offer of companies in waves, the waves were small in the early stages, and thus had many of the characteristics of a continuous issue.

8 In 1991 Romania introduced a scheme based on the distribution of certificates of ownership in five private ownership funds. In 1995 a supplementary mass privatisation programme was introduced involving the distribution of coupons that could be exchanged for company shares or fund shares, after wich the funds are to be transformed into financial investment companies.

9 Under certain circumstances certificates of ownership in funds could be exchanged for company shares.

10 Certificates of Ownership were bearers, coupons were registered and nontradable.

Source: Saul Estrin,"Some Reflections on Privatisation in Belarus", Economic Trends Quarterly Issue *Belarus*, July-September 1999.

Thus, in Russia, where natural resources are abundant, privatization was accompanied by the large-scale theft of state assets.

On the contrary, Hungary simply did not have any natural resources to be stolen by the old regime elite. Nevertheless, even in Hungary, much real estate under party ownership was stolen or sold at nominal prices amidst the disruption of transformation around 1990. Moreover, the banking consolidation carried out in two steps in the 1990's cancelled out the debts of state banks and thus *de facto* gave public money to borrowers and bankers, who cooperated in deceiving banks to gain money without providing proper collateral.

In the Czech Republic where the first voucher program was introduced the insider transaction of vouchers was widespread, creating a complex black economy.

Whether they be Russians or Hungarians, Yugoslavs or Czechs; how is it possible to establish a ruling mafia out of the elite of the old regime? As long as this is a general and prevailing fact, then we as social scientists should investigate the "**Mafiazation**" of the old socialist elites. The very existence of the "**Red Mafia**" hints that the old system itself might have been non-ethical for much of the history of socialist society.

Table 4 Value of Russian Companies Compared with Market Value(in million US dollars)

Company	**At Vouchar Auction Prices** (1993-94)	**At Russian Stock Market Prices** (August 1997)
Gazprom	250	40,483
United Energy Services	957	17,977
Lukoil	704	15,839
Rosetelecom	464	4,172
Yuganskneftegaz	80	1,656
Surgutneftegaz	79	6,607

Source: Paul Klebnikov, *Godfather of the Kremlin*, Harcourt, 2000, p.135.

Table 5 The Six Most Expensive Loans-for-Shares Auctions (in million US dollars)

Company	Industry	auctioned **%**	Auction Price **(nov.-Dec.,1995)**	Market Cap implied by auction price **million US dollars**	Market Cap on the stock market **(August 1, 1997) million US dollars**
Lukoil	**Oil**	5	35	700	15,839
Yukos	**Oil**	45	159	353	6,214
Surgut	**Oil**	40	88	220	5,689
Sidanco	**Oil**	51	130	255	5,113
Sibneft	**Oil**	51	100	196	4,968
Norilsk	**Metal**	51	170	333	1,890

Source: Paul Klebnikov, *Godfather of the Kremlin*, Harcourt, 2000, p.209.

Question 5: Is corruption in the transforming countries a social inevitability? Does the study of corruption consist of the scope of research of transformation or not?

We should carefully divide corruption into two types: one is the *de facto* theft of state and party assets during the most chaotic period of transformation, and the other is new types of corruption that arose after the establishment of a functioning market economy.

The former explains the origination of billionaires in the transforming countries. The battle on dividing public assets in the initial stage of transformation made possible the initial capital accumulation for so called newly emerged entrepreneurs. These were actually very capable party bureaucrats, government officers and managers of state companies in the old regime. The emergence of entrepreneurs in transforming countries cannot be put down as a remarkable success story written in a business and management textbook. The formation of initial capital accumulation under the transformational chaos should be recorded in the archives of history.*

* The recent charges against the top managers and shareholders of Yukos in Russia are an example of the first type of corruption. Of course, the charges are of a political nature; nevertheless theft of a huge amount of state assets and connected murders should not go unpunished, even if time has elapsed. Thousands of people were assassinated in the1990's in Russia during the battle for the dirty acquirement of state assets, which saw the liquidation of business opponents, and almost no one has been accused of the crimes. On the contrary just asset accumulation has been accomplished in a small circle of billionaires. As with the Yukos case, the US government expressed concerns that the Russian government should not violate investors' interest. Thus, the US government *de facto* defends the present managers and shareholders of Yukos. This is typical behavior on the part of financial investors including their representative, the US government too, who seek only their own financial interests under the slogan of "free capital market" in the name of defending "Globalization". They ignore the social background of the events that have significant social relevance in a given society that are not in investor interests. This example shows the typical and fundamental defect of financial investors, who have therefore sharp conflict with the society invested in the era of "Globalization". That is, it is crucially important for the given society to establish a right and just social system, and on the contrary the financial investors have no interest in the social background and the relevance of the country invested into.

The latter is a rather new phenomenon under the conditions of "**State-Market Economy**". As long as the state is the largest consumer, producers are trying to sell their products to government, i.e. the public sector. If they are unable to find markets in the public sector, their success and existence on the market is very limited. This is a fact of life of business in CEC today. Therefore, in succeeding in selling to the public sector, non-transparent negotiation backed up by personal protection is the key behind business success. This creates a new type of corruption under the "State-Market Economy", which bares similarities to that of the old regime.

As described above, the study of corruption is an indispensable part of the study of society, which shows us the nature and working of the society constructed on some economic and social disciplines.

Question 6: Have the "transition economies" already been transformed into "capitalist" economies or into "some other" types of economies? Or are they still in the process of transition? How is the present form of the "transition economy" characterized?

What are the observations? First, more than 80 % of state ownership has been transformed into private and non-public ownership in Central European countries. Does this mean that capitalist economy is already established in the CEC? If "Yes", who are the capitalists?

Second, due to the huge inflow of FDI, many state-owned companies have been sold to foreign strategic investors, who are in fact multi-national companies. In the case of the banking sector, a large portion of monetary assets are under foreign capital control. Then, are the foreign investors the new capitalists that have conquered the CEC?

Third, public burden (payroll, income tax, VAT etc.) in newly transformed countries is very high, even when compared to West European countries. Although the macro redistribution rate of CEC is not higher than the West European countries (as shown in the Table 2), it does not mean that the portion of personal disposal income in CEC is larger than that in West European countries. On the contrary, public burden on the level of personal income is far heavier in CEC that in the West European countries.

Fourth, because of the former reason and the low level of personal income, the domestic consumption market is not highly developed in CEC. The scope and extent of the market economy in CEC is still very narrow and shallow.

Fifth, the largest market in CEC is still in state orders. That is, the largest consumer is the government!! How is it possible to understand the national economy where the consumer market is dominated by government under privatized conditions in the production sphere?

How can we characterize the present economies of CEC in transformation? The best label might be the "State-Market Economy", where market economy is functioning, but the most influential consumer is the state. It sounds highly contradictory and ironic, but it depicts the actual situation of national economies during the present stage of the transformation.

Table 6 Weight of Foreign Capital in Banking Sector on Asset Base

	1999	2001
Estonia	62%	97%
Latvia	66	97
Czech Republic	48	93
Croatia	31	89
Albania	63	87*
Slovakia	-	83
Lithuania	45	81
Bulgaria	47	75
Poland	56	69
Hungary	65	62
Macedonia	12	53
Slovenia	11	16

Note: June 2002

Source: Evan Kraft, *Foreign Banks in Croatia: Another Look*, paper presented to the Zagreb Seminar of "A New Dialogue between Central Europe and Japan, 2002".

Table 7 Tax Rates in CEC (1999)

	Hungary	Poland	Czech Republic
Standard Rate of VAT	25%	22%	22%
Corporate Tax	18	34	35
Highest Rate of Personal Income Tax	42	40	40

Table 8 Payroll Taxes in CEE

	Percentage of Gross Wages	year
Slovakia	50.0	2001
Hungary	48.5	2000
Czech Republic	47.5	2000
Slovenia	38.1	2000
Poland	35.1	2000
Estonia	33.0	2000
CEE average	42.7	2000-01
EU average	23.5	1997-98

Source: The World Bank, *Transition*, July-August-September, 2002, p.8.

Question 7: Can it be said that the "market" system is compatible with democracy? Is "market" more compatible and friendly with democracy than "planned economy"?

A similar question is frequently raised in the discussion on globalization. When one asserts that globalization is compatible with democracy, it implies that market function is compatible with democracy. However, how is this proved?

Here there is also an incorrect paring of concepts. Democracy should be understood along the lines of social disciplines, and not of a concrete economic function. The reason why the market appears to be compatible with democracy is that the market mechanism is assumed to be based on "exchange" disciplines of society, which in principle allows society to perform in a democratic way (as shown in the table 1).

In summary, society has the chance for democracy to be compatible with economic mechanisms providing the mechanism is based on the exchange principle. However, this can only be true in principle and in an abstract sense. The general statement that either market or globalization is compatible with democracy is false, because the conceptualization is not correct. Argumentation calls for deeper analysis of concepts and cannot be done by only putting various concepts on the same plain, i.e. in the same conceptual dimension, without considering the degree of abstractness of the concepts.

Almost all economists who are covering "Globalization and Democracy" are falling into the trap of conceptual fallacy, which ignores the level of abstraction of concepts and therefore results in the mere pairing of concepts in a flat two-dimensional space.

Question 8: Is the dichotomy of capitalist (market) and socialist (plan) effective in analyzing contemporary economy? Do we need multi-dimensional or multi-layer concepts?

As seen in the previous question, many of today's economists have lost philosophical insight into society and fall into a conceptual trap, although they are never conscious that their argumentation is lacking in the dimension of concepts. They are just trying to combine various concepts with each other like completing a Jigsaw Puzzle in a plain flat space. It can be referred to as "flat thinking". Clumsy parings, such as "Market or Plan", “Capitalism or Socialism”, “Capitalism and Democracy”, “From Communism and Market”, “From State to Market” etc. are all typical cases of flat thinking.

As natural sciences are systematized and once this was also the case with human philosophy, scientific analysis consists of building-up of conceptual layers, such as from quantum theory to universe theory in physics, and from abstract concepts to more concrete concepts as seen in Hegel’s philosophy. However, nowadays social scientists have lost the sense of building-up concepts for making multi-layered analysis by ignoring K. Marx and G.W.F. Hegel. They have lowered themselves to doing nothing more than finding new ideas for the explanation of new phenomena at most by combining ideas in a flat two-dimensional space.

“Poverty of philosophy” is a general characteristic of contemporary social scientists including economists, who are the worst at philosophical thinking, and such poverty causes nothing but harm to the discussion on globalization.

Question 9: What is globalization today? Does so-called globalization have anything to do with system transformation? Is the transformation also a part of the phenomena of globalization or something more than that?

Contemporary international economists argue whether globalization promotes world welfare or acts against it. The argument is clearly stimulated by the Anti-Globalism movement. However, such a general statement leaves no significant meaning to discuss, because it is almost identical to discussing whether civilization promotes the welfare of human beings or not.

Therefore, first of all, we have to make clear what the globalization discussed today actually is and what kind of the new characteristics it has.

Does it mean the globalization of trade? However, were the past hundred years not a history of the globalization of trade? As far as the internationalization of trade is concerned, it is not a new phenomenon at all in modern human history. Then, what is new in world trade today? Has the collapse of socialist countries broadened the world market? Has it resulted in the capitalization of the world economy as a whole?

Could it mean a new technological revolution, which makes a worldwide network possible? Then, what is it concretely at all? Does it mean the revolutionary spread of the PC (along with Internet connections) and mobile phones? Then, does globalization mean in fact to extend the internet connection and mobile phone, for example, to African people for example?

Does it mean globalization of capital markets? Actually, the 24 hours connection of world capital markets is a new phenomenon stemming from the 1990’s, which makes it possible turnover money incessantly without the need for rest.

Table 9 Net long-term Resource Flows to Developing Countries (1991-2000) billions of Dollars

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000*
Total (I+II)	**123.0**	**155.8**	**220.4**	**223.7**	**261.2**	**311.2**	**342.6**	**334.9**	**264.5**	**295.8**
I. Official flows**	**60.9**	**56.5**	**53.6**	**48.0**	**55.1**	**31.9**	**42.8**	**54.6**	**45.3**	**38.6**
II. Private flows	**62.1**	**99.3**	**166.8**	**175.7**	**206.1**	**279.3**	**299.8**	**280.3**	**219.2**	**257.2**
A. Capital markets	26.3	52.2	100.2	85.6	99.1	147.8	127.2	103.5	33.8	79.2
a.Debt flows	18.8	38.1	49.2	50.5	63.0	98.7	97.0	87.9	-0.6	31.3
b.Bank lending	5.0	16.2	3.4	8.7	30.5	33.7	45.2	50.0	-24.6	0.7
c.Bond financing	10.9	11.1	36.6	38.2	30.8	62.5	49.0	40.9	25.4	30.3
d. Other	2.8	10.8	9.2	3.6	1.7	2.4	2.7	-3.0	-1.6	0.3
B. Equity flows	7.6	14.1	51.0	35.2	36.1	49.2	30.2	15.6	34.5	47.9
C. FDI	35.7	47.1	66.6	90.0	107.0	131.5	172.6	176.8	185.4	178.0

Source: CEPR, *Making Sense of Globalization*, Policy Paper No.8, July 2002, p.44.

We have to admit that the PC expansion and world links of the capital market give ordinary people instant access to the world capital markets. However, the volume of expansion is not as revolutionary as generally considered. If you look at Table 9, it can be seen that the volume of capital flow into developing countries is not that spectacular, but in fact rather modest. At least the developing countries do not seem to be impacted by any significant influence from global transactions whatsoever.

Regarding the ex-socialist countries, newly-opened equity markets are still very small and have not contributed to revolutionary expansion of the world capital market. Nevertheless, more than half of the money invested into these markets is poured in by foreign investors, mainly institutional investors who seek high returns in rather volatile markets like Russia. It is true that Central-Eastern European and Russian markets have provided a new opportunity for turning over money, but it represents only a marginal portion in world investment in terms of volume of transaction.

What is significant is the fact that the largest increase in capital flow can be observed in the developed countries in the second half of 1990’s, mainly due to the boom in equity investment in the USA, where everyone can buy shares over the internet and telephone. Except in the USA, financial investment did not rise at all and in the 1990’s it never played a central role in other areas of the world economy. On the contrary, a steady increase in FDI can be seen in developing countries in the 1990’s, which can be explained by the development of intensive economic relationships among developing countries.

However, it is fairly doubtful whether world economic development over the last two decades can be characterized as globalization, describing the 1990’s as a revolutionary epoch in modern human history like the industrial revolution.

I have to say that “Globalization” in the 1990’s is *de facto* a slogan for financial investors who are eager to turn their money over 24 hours a day, and therefore demand the opening and liberalizing of capital markets everywhere around the world. In this sense the so-called Washington consensus, whether the inventor of the terminology, Williamson

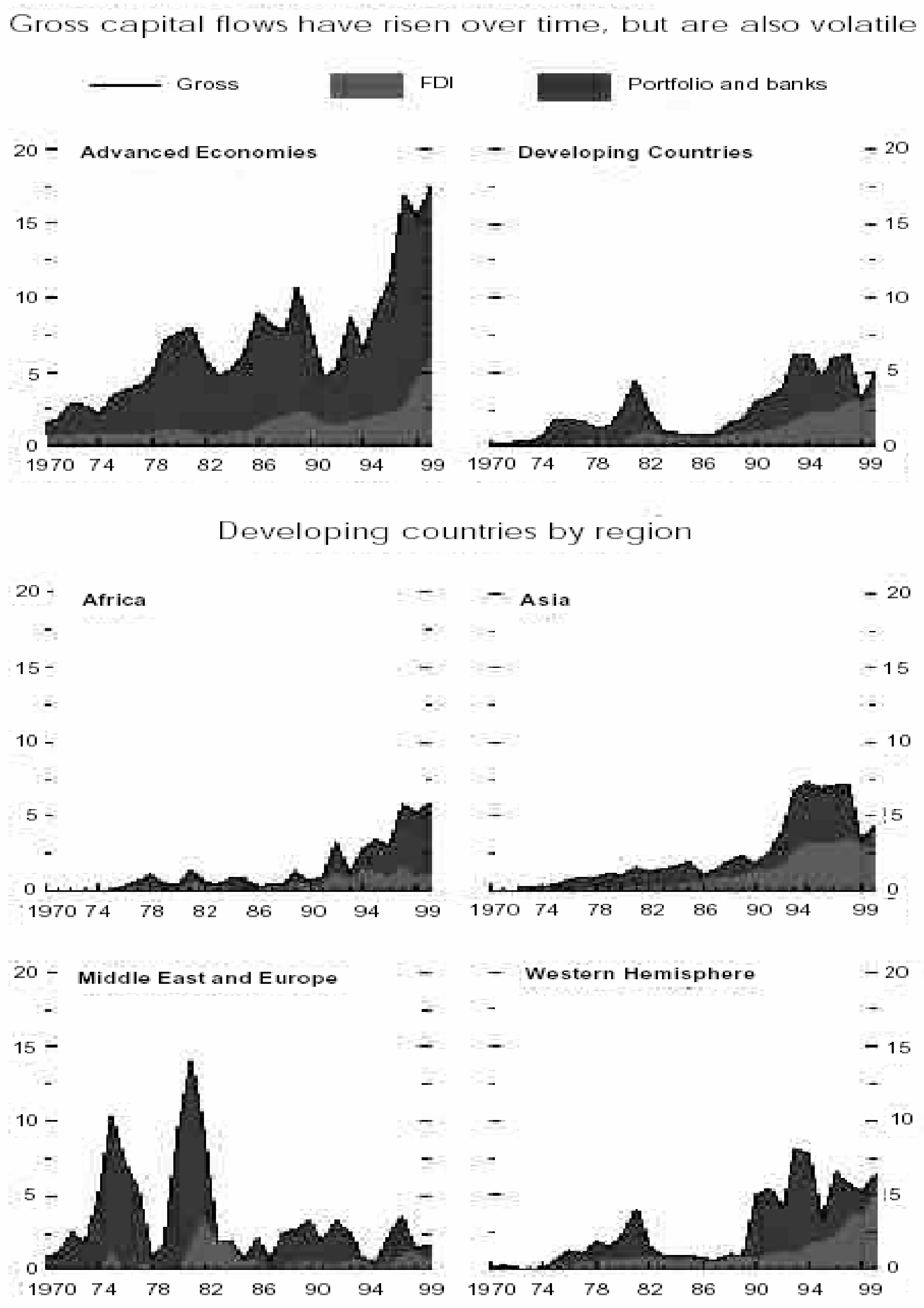

Figure 2 Gross Capital Flows

Source: CEPR, *Making Sense of Globalization*, Policy Paper No.8, July 2002, p.47.

intended to or not, has contributed to market-liberalism. This is condemned as **market fundamentalism**, because privatization, deregulation, the securing of property rights, the liberalization of capital and trade transactions, and interest liberalization, all of which Williamson listed, are indispensable preconditions for "freedom of investment". In other words, either "Globalization" or "Washington Consensus", as it is known, contributed to preparing conditions for expanding financial investment for the sake of US and European investors. This is the historical fact of "Globalization" and "Washington Consensus" in the 1990's.

Question 10: Is globalization an effective concept with which to characterize contemporary changes in the world? Is globalization equal to capitalization of economy?

If globalization actually leads to the freedom of investment, then it can be identified as "Capitalization" of world economy. Capitalization in this case is so as to transform the world economy into a completely liberalized capital market, through which investors easily choose objects of investment from the menu of markets and place money orders even from his or her bedroom via the internet or mobile phone. A worldwide market for foreign exchanges is already in place today. This is a typical worldwide network of transactions. Can every economic transaction be organized in a worldwide network like the FOREX market? At least it is a desire of financial investors to establish a completely free market network on a worldwide dimension.

This may be the ideal scheme for American financial investors. However, human society and the national economy are not as simply organized as a capital market and do not function as investors desire. What is the fundamental defect behind this type of thinking?

It lacks understanding of "national economy", where production is executed and has its own geographical borders. Although money is indifferent to the place or country of origin, production is always connected to specific places and countries that have clear borders.

"Capitalizing economy" is the typical thinking of financial investors (capitalists), and although this reasoning may be valid as far as the capital market in advanced economies is concerned, such thinking cannot be simply generalized and extended to capital markets in the rest of the world. **National economies are simply not playgrounds for financial investors**.

Each national economy has to carry out its own tasks in its development stage. It is of crucial importance for the national economy to build up and keep its own reproduction system in order. It is the first priority for the national economy, and the "functioning-up" of capital markets does not hold first priority in many countries. Here there is a contradiction and clash of interests between investors and investment receiving countries.

A country that is suffering from capital shortage tries to attract foreign capital for economic development resources. Investors are not philanthropists. They put money into a country where there exists a good chance of return. However, from the standpoint of return, an overly established market does not offer advantages, because large booms that provide a chance of high-returns are not expected. Therefore, investors are always looking for emerging markets where the capital market is still under development, and therefore evaluation of companies are also not fully established. Volatility and defects of the market are attractive points on the behalf of investors, and thus emerging markets can invite money as long as the country has economic potential. In this point, interests of both the investor and the country invested into coincide. However, from the standpoint of investors money should be free to be withdrawn from a market when investors want. Thus, financial investors demand a completely free market to function in that allows them to put in and withdraw money anytime they want. On the contrary, from the standpoint of the receiving country money should be tied to the market as long as possible. This contradiction periodically leads to economic crisis in the developing country caused by capital being withdrawn.

Market opening and liberalization are, first of all, financial investment buzzwords . "Capitalization" of the world economy is an illusionary desire of investors, who think the world economy can be organized like network transactions of capital investment in the USA. Financial investors are prone to think that indicators of capital markets send us almost all the important information on the national economy, and therefore the national economy can be fully observed through financial markets. When investors speak of markets, they refer to capital markets, and not the market of material products. Here we can see another type of defect in thinking: **Capital-Marketism** or **Financialism**.

I feel inclined to say that today's "Globalization" tends to be a modest and obscure expression of "Capital Marketism" or "Financialism", which is based on a very narrow understanding of national economy on the part of financial investors.

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