FINANCIAL CRISES AND STRUCTURAL CHARACTERISTICS OF THE ECONOMY

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Abstract: *Economic structures are a major cause of long-term growth or stagnation. Different economic structures have different ranges of structural learning, innovation, and different effects on income distribution, which are key determinants of economic performance. Through theory about economic structures it is explained why institutions work differently in space and time. This paper shows using a case study in the United States, that the source of recent financial crises rests on the structural characteristics of the economy. Constant deindustrialization is increasing inequality, and a debt-intensive credit boom has emerged to offset the deflationary effects of this structural change. The strong application of the austerity system in Europe and other parts of the world, even after the evidence points to less frugal policies, illustrates the theory of power it has over public policy. The economic structure should be put at the center of analysis, to better understand the economic changes, income disparities and differences in the dynamics of political economy through time and space. This paper provides a critical overview of the rapidly developing comparative studies of institutions and economic performance, with an emphasis on its analytical and political implications. The paper tries to identify some conceptual gaps in the literature on economic growth policy. Emphasis is placed on the contrasting experiences of East Asia and Latin America. This paper argues that the future investments in this field should be based on rigorous conceptual difference between the rules of the game and the game, and between the political and institutional, embedded in the concept of management. It also emphasizes the importance of a serious understanding of the endogenous and distributive nature of institutions and steps beyond the narrow approach of property law relations in management and development. By providing insights from the political channels through which institutions affect economic performance, this paper aims to contribute to the consolidation of theoretically based, empirically based and relevant to policy research on political and institutional foundations of growth and prosperity.*

Keywords: *Financial crises, Structure, Economy.*

1. INTRODUCTION

The claim that “inclusive” institutions are a deep determinant of economic growth remains unsatisfactory. This paper also develops an alternative theoretical and empirical case that economic structures are the root cause of economic performance. Economic structures determine the rate of structural learning, affect institutional performance, affect income distribution, and establish the direction of political transitions, and thus economic performance. The paper highlights the feedback loops between institutions, political power and economic structures, so markets alone will not provide transformations that increase growth. The operation of this framework is illustrated by the use of a case study in the US and the discovery of the structural origins of the financial crisis.

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2. ECONOMIC STRUCTURES, INSTITUTIONS AND ECONOMIC PERFORMANCE

The first explanation of why some countries are rich and some poor was tried by Solov (1956), who cited the main reason for the difference in capital accumulation and technical changes, but this explanation was not enough. Growth theories (Aghion and Hovit 1992; Grossman and Helpman 1991; Romer 1990) argue that differences in research and development and human capital lead to different growths in technical change and accumulation. Yet why do some countries invest more in education and innovation?

North (1990), Acemoglu and Robinson (2013) and other new institutional economists argue that differences in institutions can explain differences in economic performance across time and space. Institutionalists believe that economic growth is a function of economic and political institutions, but they neglect the role of economic structures in the dynamics of growth. In their opinion, institutions do not cause growth, but the economic structure of the state is the basic cause of economic performance. Therefore, differences in economic structures through time and space can explain differences in economic development. This paper presents a new theoretical framework that explains how important economic structures are for growth and this is supported by the American case study.

But what are economic structures? Some goods like high-tech production have room to increase yields, and others like bananas are known for showing reduced yields. Today, a country has an increased production structure of yield if it produces high-value goods that are technically sophisticated and vice versa, which means that the economic structure of declining yields consists of low value-added goods that are technologically simple. Basically, economic activities reflect the productive capabilities of the economy, and the production structure of a country is simply a summary of its technological capabilities.

High value-added goods and technologically complex goods are produced in market structures that favor innovation (Nelson and Winter 1990; Schumpeter 2008) and they maintain higher wages and profits over a longer period (Reinert 2008). Also, increasing economic rates of return provide longer career scales and they serve as an important means of labor success, which improves income distribution. Furthermore, democratic transitions help to increase the production structures of yields and this increases the spread of technical knowledge (Acemoglu 2008), which is the most important immediate cause of growth. Based on the above, it can be concluded that a country acquires an economic structure when the state adequately applies production.

It is obvious that without a minimum rule of law and some form of ownership, no production will be undertaken. It follows that exchange institutions have non-trivial effects on production. However, exchange institutions do not guarantee the production or production of goods with increasing yields. Institutions are in the best conditions necessary, but in themselves insufficient to produce production. Government subsidies and tax breaks, if applied appropriately, can have direct effects on the level of production and encourage the production of certain goods relative to others. This difference makes it possible to emphasize the analytical limitations of the new institutional economy, especially the work of Acemoglu et al. (2005) and Acemoglu and Robinson (2013). These theorists distinguish between „extractive" and „inclusive" institutions. The first concerns undemocratic political institutions on the one hand and the weak rule of law and the absence of private property rights on the other.

However, poor countries, which by definition lack production technologies, cannot record strong growth by "taking over" exchange institutions from developed countries. In fact, their resources are poorly allocated, with imperfect exchanges becoming less problematic when it is realized that poor countries have little to exchange. Some theorists argue that exchange institutions cannot produce structural transformations that increase growth. Their theory is that the work of institutions is determined by the economic structure of the country. Empowering institutions is not expensive, but reduced returns on economic activity simply do not produce enough added value to cover the costs of setting them up. The reverse is true in rich countries with increasing return economic structures.

The paper argues that professional rents are becoming an important source of de facto political power, which in turn is used to strengthen the economic structure in order to preserve the distribution of professional leases. This creates a balance between political power, institutions and economic structures and explains why structural changes to boost growth are the exception rather than the rule.

3. ECONOMIC STRUCTURES AND INSTITUTIONS

The debate on institutions and development is focused on the direction of the cause-and-effect relationship. While new institutional economists argue that institutions cause growth, the literature on industrial policies (Chang 2003; Khan and Jomo 2000; Reinert 2008) argues, among other things, that growth and development determine the direction and rate of institutional change. Based on the above, two statements can be made:

- There is a two-way cause-and-effect relationship between institutions and economic structures,
- The type of economic structure determines the performance or efficiency of formal institutions.

Institutions do not exist in abstraction; they co-evolve with the productive structure of the economy. The IMF's structural adjustment programs and World Bank's second-generation reforms are major institutional changes that revise the rules for managing business and social interactions. These reforms affect economic performance because they change the structure of economies. However, structural transformations also trigger institutional changes (Ancochea 1999; Chang 2011; Reinert 2007). The discovery of gold in California led to what is popularly known as the California Gold Rush. This discovery changed both the sectoral distribution of GDP and the type of economic activities produced. As with institutions, the exploitation of this natural resource does not exist in abstraction; it must be regulated in the new institutional framework. Similarly, institutional changes are needed when oil is discovered.

Accordingly, it is concluded that institutions cannot be underestimated and their causal effects in isolation are production structures. Even new institutional economists understand the importance of economic structure and its relationship to institutions. Their emphasis on property rights and the rule of law, etc. is a means of reducing market transaction costs in order to maximize profits from trade. By focusing on exchange, they imply that the problem of production is solved, but with such an assumption, no development policy can be made.

The view that institutions are the rules that shape human interaction (North 1990) does not encompass the link between institutions and economic structures. This definition allows for one direction of cause - from rule to consequence. But even with the consequent events (state intervention and / or external shocks), institutions are formed or modified.

4. CASE STUDY IN THE USA

During the 1800s, the agrarian economy contributed the most to U.S. GDP and much of world production. But the shocks of productivity on farms and the expansion of cultivation significantly reduced agricultural prices and incomes in the early 1900s (League of Nations 1931; Tymoshenko 1933), and this had an important effect on the structure of the economy. The decline was particularly severe between 1929 and 1932 - agricultural incomes were reduced by 50%. One of the important implications of this secular decline is the decline in agricultural employment, which has led to huge unemployment, as new sectors and economic activities have not taken full advantage of the growing number of unemployed.

This period of structural change inevitably changed the distribution of occupational rents to rural labor, which increased inequality between villages and cities and worsened deflationary tendencies of transformation. It is useful to keep in mind that the initial levels of inequality were already high during this period. Piketti (2014) notes that from 1800-1910. private capital as a percentage of national income averaged 700% in Germany, France and Britain, while in the United States it ranged from 300 to 500%. In agrarian economies, ownership of capital was highly concentrated, leading to significant inequalities in wealth and income. Although some landowners lost private wealth during the agrarian transformation, the decline in agricultural employment has countered any tendency to reduce wealth inequality. During this transformation, manufacturing, construction and trade services were emerging sectors, which showed a structural change towards the center of production space or towards an increasing structure of yield production.

World War I (VVI) served as a temporary stimulus to the economic growth of the American economy and accelerated the transformation in the growing economic structure of yields, but the process remained incomplete. Rising rural and urban inequality and mass unemployment in agriculture are changing de facto political power, which has de jure affected political power, among other things, to reduce the highest income tax rates, and this has worsened inequality. Great inequality and forced austerity during the First World War created a large base of borrowed funds that did not find profitable paths in agriculture, and the newly emerging industrial sector was not enough to take advantage of the excess savings. They gave way to the unfortunate idea of a cheap loan or model, buy now and pay later. Consequently, this created a debt-driven growth model as consumption exceeded declining agricultural and urban revenues.

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