



# The current economic crisis and international business. Can we say anything meaningful about future scenarios?

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## ABSTRACT

The paper starts with a list of stylized facts on economic trends in the last few decades with particular attention to international elements. A very brief analysis of the current economic crisis is then attempted. The root cause, the *causa causans*, of the excessive growth of the financial sector and the inevitable current crisis is identified in the lack of profitable investment opportunities in advanced capitalist systems. The short-term remedies include a shift in income distribution to increase the consumption component of effective demand; it also includes serious regulation of the financial sector at both national and international levels. In the medium to longer term governments should consider engaging in large investment projects such as alternative sources of energy, transport as well as in public services. This might help to improve conditions for profitable private sector investment, thus benefiting both the workers and the capitalists operating in the real sector at the expense of the rent-seekers. The paper then draws some inference on key elements likely to impact on futures, particularly with respect to internationalization and the two types of innovation identified in the stylized facts: organizational and technological. Inference is drawn with respect to the economic system as well as to economics as a scientific and academic field. The final discussion draws these various elements together.

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## 1. Introduction

The title of this paper contains a question about whether anything meaningful can be said about the future of international business in the light of the current world economic crisis. If the question is interpreted in terms of our ability to predict the future, the answer is definitely 'no'. However, if we interpret it to mean saying something about the recent and current developments that have a strong bearing on the future, I would say we can and this is what I shall concentrate on in this brief and sketchy paper.

Contrary to common parlance – 'financial crisis' or 'credit crunch' – the current crisis is a full economic crisis in which both the financial and real sectors of economies are affected and which has now spread to many countries worldwide. It has started in the financial sector, as crises tend to do, and as it deepened it spread wider and wider in terms of affected sectors and countries.

What is the context of the crisis? We can try to understand the context by focussing on some key stylized facts of the last 30 or so years with particular reference to international elements within the context.

- Introduction and spread of two types of innovation: organizational and technological. The two types of innovation are closely related and neither would have been possible without the other. On the technological side the main contribution

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comes from the information and communication technologies (ICTs). On the organizational side we can identify three major strands of innovation. The organization of production across countries; the division of the production process into various components and the siting of related segments of the value chain in different locations and particularly in different countries; the involvement of satellite firms in the production process organized and controlled by main centres [1]. These organizational innovations have led to changes in the international division of labour as well as to the development of two types of networks involving the transnational corporations (TNCs)<sup>1</sup>: the network of subsidiaries across countries though internal to the company; and the network of external collaborations with sub-contractors and other partners [2,3].

- The institutions which have been highest in terms of responsibility for both types of innovation are the TNCs. They are heavily involved in the information and communication technologies (ICTs) as well as in the main types of organizational innovation.
- We have seen the deepening of activities across national borders organized and controlled by a main strategic centre: the headquarters of TNCs [4]. The relevance of TNCs has increased consistently. The total number of TNCs originating from 14 developed countries in 1968–1969 was 7276 [5, Table 2.1, p. 12]; for 2008, UNCTAD [6] gives the worldwide number at approx. 82,000. In the last couple of decades there have been sectoral and geographical shifts in their activities. We have seen growth in foreign direct investment (FDI) from developing and central and eastern European countries: the stock of outward direct investment from these regions moved from 3.1% of the total world stock in 1980 to 16% in 2009 [6,7]. There has also been growth in the number of smaller companies that are becoming transnational.
- Incorporation of former Soviet Union and east European countries into the market economies areas.
- Rise of some developing countries to the economic and political world stage particularly China, India and Brazil.
- Increasing financialization of economic systems. Palma [8, p. 6] reports that: ‘...the four components of the stock of global financial assets (equity, public and private bonds and bank deposits) increased 9-fold in real-terms between 1980 and 2007. . . As a result, the multiple of the stock of financial assets to world output jumped from 1.2 to 4.4. . .’. We have also seen large growth in cross-border flows of direct and portfolio investment.
- Changes in income and wealth distribution. Indicators of within-country distribution have seen the top percentiles of the population absorbing higher shares of both income and wealth compared to the decades immediately after WWII [9].
- The changes in distribution appear to have been achieved largely through rent<sup>2</sup> generation – particularly in the financial sector – more than via profits on investment in the real sector as pointed out in [8].
- Increase in indebtedness of private, corporate and state sectors [8,11].
- In the political and economic spheres there has been a shift in ideology from ‘market needs regulation’ to ‘market knows best’. Liberalization and de-regulation in many areas and particularly of labour markets and financial markets [12].
- In spite of the increasing spread of liberal ideologies, governments have been very interventionist in areas such as: privatization; regulation of – and financial support for – privatized industries; and strengthening of intellectual property rights (IPRs) as argued in [13]. We have seen a change in the role of the state: from one that supported capital accumulation and helped to maintain a balance between class forces in the period after WWII, to one in which – in the last 20 years – it supported rent-seeking activities and aided the shift in income and wealth distribution in favour of the better off strata of society. This shift has occurred via various forms of intervention including: legislation, the structure of taxation and social security and the casualisation of labour. The latter together with the changed labour market structure away from manual and into white-collar jobs and the opportunities and threats of international relocation of production aided the process of submission by the working class.

The paper will proceed as follows. The next section analyses the current crisis; Section 3 considers where we may go from now on in terms of: the economic system, the international arena and the science of economics. The last section contains a summary and discussion.

## 2. Understanding the crisis

If a Martian had visited Earth in the last 20 years she would have been pretty puzzled to see a planet where lack of food and infrastructure was endemic in many countries; where even the rich countries had: many people in poverty; inadequate levels of basic infrastructures and public services and yet many resources – including many bright people – were allocated to producing strange financial products that nobody could possibly want and very few people understood among the Earthlings let alone the Martians. Moreover, the people involved in these useless and socially dangerous<sup>3</sup> products were the very ones that were gaining the highest rewards. How had that come about?

If imagining a Martian – let alone her thoughts – is difficult for us let us try to imagine the position of someone growing up or working in post WWII Italy: myself and my father respectively. What we saw around us was fervour (almost a fever) of

<sup>1</sup> The transnational corporations – also known as multinational corporations or international firms – are characterized by direct production as well as ownership of assets in at least two countries.

<sup>2</sup> In classical economics rents are incomes accruing to landowners. In the last few decades and particularly since the publication of [10] the term has been used to indicate also incomes extracted through monopolistic position of any type of assets and/or through the extraction of incomes against which no (or little) contribution to production is made. The concept is not entirely unambiguous though it is widely used.

<sup>3</sup> Warren Buffett in his 2002 Berkshire Hathaway letter to shareholders refers to derivatives as “weapons of mass destruction”.

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