Some reflections about the new challenges of the contemporary state

Everywhere that economists and their ilk
mingle we see them reaching for new answers
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Introduction

The scope and power of a state's influence on economic processes are issues which are widely discussed both in the field of economics theory and in business practices. These issues are also at the center of attention of social thought. The state's place and its tasks in the economy have been discussed for a few centuries. Since mercantilism people have been arguing over the role of this institution in economic life and also over the scope of functions which a state should perform in the economy. Many discussions and arguments concerning the range and tools of a state's economic activity still are not widely accepted among members of the academic community. While there is consensus concerning the classical functions of the state, no clear delimitation of the areas and the extent of the impact on business processes has been made. Meanwhile, dynamic changes in social and economic space have changed the scope of the state's impact.

Economics has not kept pace with explaining modern socio-economic phenomena. Therefore it is necessary to identify the modern social and economic challenges faced by the institution of the state. This identification can help to indicate new tasks, new regulation areas and new tools to be considered in the modern economy [Tanzi 2009].

The necessity for this indication results from that fact that many changes have taken place in a turbulent and dynamic environment. Additionally, contemporary states are fragile and frail with regards to economic policy (which is not a counterweight and solution to emerging challenges.) The rules which nowadays apply to states were created many years ago in different economic conditions. These conditions have been changing constantly and therefore a lack of accepted consensus is understandable. However, many politicians and economists (even Nobel prize winners in economic sciences) have been searching for solutions which allow nations to restore equilibrium in the global economy and redefine the role of the state.

The main goal of the article is to show the fluctuation of economic points of view concerning the role of the state in the economy and then to identify and specify some challenges of the contemporary state. The hypothesis states that the contemporary state's tasks exceed the traditional approach adopted in the theory of economics and new challenges require broadening their scope. In the first part of the article, some points of view concerning the role of the state will be shown. It is essential to understand the fluctuation of ideas. Then the article describes some new challenges for the modern state which are determined by a turbulent and dynamic environment.

The fluctuation of views concerning the role of state

There is widespread agreement among social scientists that development is a multidimensional phenomenon, with economic, political, and social aspects, and that the different dimensions of the role of the state are interconnected with one another in complex ways. The understanding of the role of the state in the economy is strictly connected with a belief or disbelief in a perfectly-functioning market mechanism. Over the centuries, economic theory and business practices were in turn under the influence of opposite ideas. Opinions concerning the role of the state in the economy were constantly evolving and the idea of a state's power, as Milton Friedman noticed, fluctuates [Vroey and Malgrange 2011, Hoover 2003, Wakatabe 2009, Wray 2011].

The process of changes within the scope of the socio-economic life, sometimes evolutionary, sometimes revolutionary, has accompanied mankind since the dawn of time. But nowadays these changes are more and more dynamic and therefore they bring uncertainty, risk and instability [Friedman and Friedman 1989].

From a historical perspective the functioning of the institution of the state, its scope and tools of its intervention show a permanent evolution. Starting from the Sumerian city-states and the Greek polis, through the medieval structure of the state, an absolute monarchy, which was reflected in Louis XIV's famous statement *L'Ėtat c'est moi*, the Smithian liberal state, the interventional Keynesian state and up to the present. Throughout all this, the role of the state and the scope of its intervention and instruments of interaction have undergone numerous modifications. At the same time, changes in the socio-economic situation have shown a peculiar recurrence of views.

More than 250 years ago during the period of industrial revolution, a market system based on entrepreneurship, innovation and a self-regulating mechanism began to spread. This system led to rapid economic and social development and civilizational progress and then contributed to huge changes in quality of life for people in the economies which had implemented it. Thus, the market became the *spiritus movens* of all changes.

The theoretical basis of this system was the classical doctrine, with the invisible hand of the market. While rather arbitrary, a majority of economists would agree that the foundations of a market economy are: freedom of individual economic units, private ownership of the means of production and the existence of a market mechanism understood as an essential controller of all economic processes. This system, however, was subject to strong evolutionary forces, although the foundations of it are based on the dominance of private property and the market mechanism function has remained relatively stable.

Nowadays, the list of the basic assumptions and requirements of the market system is longer. Also noteworthy is the political system ensuring the stability of legal order and democracy which allows societies and social groups to achieve collective goals with the help of the state as the main representative of their interests and aspirations.

This elementary system which was based on Adam Smith's doctrine was destroyed by The Great Depression which started in 1929, then by implementation of the New Deal of Franklin Delano Roosevelt and finally after John Maynard Keynes' “General Theory of Employment, Interest and Money” was published in 1936. Among many reasons for its collapse, it is worth mentioning the monopolization of developed economies, human greed and excessive consumption in the years immediately preceding The Great Depression [Chang 2010, Snowdon 2015]. The new and unexpected economic situation needed a redefinition of the place and role of the state in the economy and the exemplification of new tools of economic policy. The new ideas were very successful and during that time the new tools of intervention policy contributed to a stimulation of the economy and a victory over the worst depression in world economic history.

The main goal of the Keynesian revolution, which advocated an interventionist role of the state, resulted in a prevention of defects and market failures without changing the systemic foundation of the market economy. The success of the Keynesian economic doctrine was legitimized by a taming of business cycles after World War II, which was possible by the realization of economic policy explained by the Philips curve.

An adoption of the orthodox Keynesian interpretation of the Philips curve explained the constant, exchangeable relation between the rate of inflation and the rate of unemployment to realize short-term economic policy goals [Snowdon, Vane and Wynarczyk 2005].

The Golden Age of Capitalism (the post–World War II economic expansion) was a period of strong economic growth and economic prosperity in highly developed countries which lasted from the end of World War II until the early 1970s. Then at the turn of the 60s and 70s the emergence of a concurrent high level of inflation and unemployment caused a rejection of this relation.

In the 70s a supply shock on the raw materials market and a crisis of Keynesian economic policy contributed to a revival of classical principles of economics and ideas of economic liberalism. These economic problems stopped the triumphal march of Keynesian theory and facilitated a monetary counter-revolution [Snowdon, Vane and Wynarczyk 2005].

Then, the failure of the socialist model of economics contributed to the creation of a Washington revival of liberal trust in the necessity of deregulation. However, the problems of transition economies and failures in the realization of this Washington consensus indicated the shortcomings of this point of view [Stiglitz 2004]. The crisis of 2007 was the next reason which questioned faith in the market mechanism.

Examples from economic life show that an automatic solution to economic problems by the market mechanism, in which representatives of neoliberal ideas believed in the past and believe nowadays, is a dogma and market failure is a reason for state interference. The existence of externalities, a growing importance of public goods and a lack of perfect information are considered main market failures which justify state interference. In addition, economic literature mentions the socially unacceptable income differences which foster the need to redistribute income in a society and the occurrence of destabilizing macroeconomic phenomena such as high levels of inflation, rising unemployment and fluctuations in economic activity. Also, state inefficiencies can be found in the existence of shortages [Daoud 2011], a lack of institutional elasticity [Meiklejohn 1999], the lagging process of institutional reforms in response to dynamic changes in the socio-economic environment and the changing expectations of social groups. Market failure legitimizes the introduction of legal, administrative and economic regulations, and therefore state interference.

On the other hand, the state as an institution is not able to guarantee full effectiveness of the market. So both market and state failure exposes a society to many problems. Nowadays, society is forced to function in an insecure environment without any guarantee of effective action against increasing problems. An example of this is the contemporary financial crisis being strongly associated with market deregulation, uncontrolled and insatiable greed and a willingness to enrich in excess [Akerlof and Shiller 2009]. The experiences of the last crisis show that not only the last decades, but also prospects for the future seem to be very unstable and unpredictable [Roubini and Mihm 2011].

To sum up, evolving conditions of the capitalist economy influence opinions about the role of the state. Especially since history has evidenced many failures of economic doctrines, both liberal and Keynesian. There has been a recent wave of criticism of the dominant economic theories and their inability to explain some mainstream economic phenomena and obvious imperfections of the proposed models in explaining the impact of institutional solutions regarding economic growth and development. New studies were undertaken based on a new, institutional approach. The results of the research (often interdisciplinary in nature and related to the property rights theory of Harold Demsetz and Armen Alchian, developed by Douglass Cecil North, and to transaction cost theory proposed by Ronald Coase and Oliver Williamson, also to contract theory and agency theory) emphasized the importance of institutions, including the state, for the formation of economic growth and socio-economic development. At the turn of the century, the works of many authors supported the hypothesis that institutions and the state determined the importance of long-term economic growth and explained the observed differences in per capita incomes across countries [North 1990, 1991, Hall and Jones 1999, Acemoglu, Johnson and Robinson 2001, 2004, Rodrik 2013].

Theoretical considerations require a broader approach, extending beyond contemporary analysis and taking into account a diversity of views. Explanation of complex economic realities, as well as many interdependencies in a market economy, implies a necessity for methodological convergence and taking into account not only an economic point of view but also interpretations of results from other social sciences (philosophy, sociology, political sciences, etc.). Mainstream economics is not able to explain, by itself, economic reality. This is the main reason for the development of heterodox economics.

Some new challenges of the contemporary state

Identifying problems that the modern state must face has exposed new areas where regulations are needed. It is impossible to list all of the factors which influence the contemporary state or to sort them according to their importance or different aspects, but some of them are particularly noteworthy.

Nowadays economists can identify many challenges which affect the current role of the state. It is very difficult to evaluate them because states are very different. Modern states operate in diverse political, economic, social, cultural and ecological environments. They have obtained different levels of development, face various trends of economic growth, participate in different multinational agreements and organizations etc. They have different historical, cultural and even religious experiences and a different hierarchy of social and economic goals. But some challenges seem to be important for a majority of states. Among them are: the process of globalization, consumerism, rapid development of information and communication technologies, regionalization vs. internationalization, appearance of new agents and unfavorable demographic changes, especially in highly-developed countries [Bloom and Williamson 1998].

Accelerated globalisation has appeared as the sign of the times. This is a process of greater economic interdependence among countries, which is manifested in an increasing amount of cross-border trade in goods and services, an increasing volume of international financial flows and increasing flows of labor. Globalization as a multidimensional and multi-level phenomena affects all levels of socio-economic life, and its most important consequence is the formation of a global economy [Dunning 1992]. Its main feature is the transformation of the modern market economy. This process takes place with great force and generates multi-dimensional effects, both in the lives of individuals and nations, as well as the whole world. An evaluation of the process of globalization is not clear, and both positive and negative consequences can be indicated. Some of these negative aspects can be easily compensated for by the state, using appropriate measures. For others it is powerless or at least not very effective [Stiglitz 2003].

The progression of globalization processes has emphasized some social and economic problems for the governments of well-developed countries. These include rising unemployment, ageing societies, high costs incurred by the state in terms of social security, economic instability and income stratification, monstrous fiscal policy which concurrently is not able to guarantee efficiency and implementation of the state's objectives, deficits of authorities and financial means (more expensive state versus richer, more powerful and more influential transnational corporations), deficiencies in the functioning and implementation of basic state tasks and a necessity to adapt to rapidly changing internal and external conditions. The effects of rapid globalization are also connected with the fair distribution of the gains from it among all economic agents: individuals, organizations, nations and regions [Intriligator 2004]. This process of internationalization has also led to strong interdependence of economies, including the transmission of local or regional cyclical fluctuations across borders. Globalization is conducive to a dynamic development of services thanks to a knowledge-based economy, but it slows the development of the industrial sector. It also pushes national economies into the background [Mrak 2000]. All of the aforementioned problems create specific conditions for the operation of the contemporary state, and the state as an institution has to face new challenges.

Future shocks, which in the 70's were observed by Alvin Toffler [1970], resulted from rapid technological development. In contrast, more and more common consumerism has become a part of societal life and an inherent feature of modern economies. It carries serious economic and social consequences. Psychophysical barriers related to diminishing adaptation and accommodation of human beings to fast transformation are growing. Problems of knowledge absorption can potentially create situations where an unadjusted and unprepared society faces difficult moral and intellectual choices.

The rapid development of information and communication technologies, globalization and the dominance of the service sector over manufacturing and the growing importance of knowledge (itself an independent factor of production) all generate new conditions for functioning of the market economy [Noland, Park and Estrada 2012]. A post-industrial scientific and technological revolution period changes the composition of economic forces. The triad model: household, business and state in the new environment is complemented by economic agents, whose importance changes the traditional balance on the social and economic stage.

Deepening processes of integration and regionalization and, consequently, the increasing role and importance of institutions and supranational organizations weaken nation-states. Transnational corporations have power over consumers, but also to some extent over the state apparatus [Bremmer 2010]. Globalization dethrones the state and a majority of its tasks are acquired by transnational corporations [*Leviathans* … 2005, Herkenrath and Bornschier 2003].

Decentralization, as the process of redistributing or dispersing functions and powers of the state is becoming a common phenomenon in the contemporary world. This process assumes that the competences and ability to act are attributed primarily to social actors, in other words, non-governmental organizations.

In the modern economy, the consumer model is also changing. The classic consumer is gradually transforming into the prosumer, having wide knowledge of the process of product and service consumption[1] [Ritzer, Dean and Jurgenson 2012, Kotler 1986]. Prosumers take part in the decision-making process, while at the same time actively participate in the creation of production. Thus, economics of the future refers to the idea of "prosumer" economics, a super-industrial society and prosumer economy.

The changing role and importance of economic subjects causes a reduction of the role of the state in some aspects and a reorganization of its activities. In other areas, the state itself relinquishes its rights to other economic agents. The control of economic policy is no longer the exclusive domain of the state, especially in relation to monetary policy.

It is also necessary to consider the supranational and worldwide legal order and the role of the state in such structures, especially the process of internationalization of supranational interests and private sector interests, mainly financial. The creation of new infrastructure on a global level requires formulating strong national foundations. Transition from a national to a global order needs careful analysis of the place and importance of the state in the market economy and its special role in the protection of property and intellectual property rights.

The dynamic development of civilization in the past few decades has caused changes in understanding the social and economic role of the state. In terms of turbo capitalism, which accelerated social and economic changes within the scope of social expectations, a closer relationship to the world economy has taken place. The growing role of transnational corporations along with increasingly close vertical and horizontal integration has led to a loss of some part of national sovereignty and changed the perception of the traditional role of states in social and economic life.

The contemporary state is also involved in many new contradictions. On the one hand, globalization processes, the growing role of supranational institutions such as the IMF, WTO or World Bank [Stiglitz 2002] and the importance of transnational organizations reduce the role of state and significantly weaken its strength as an economic agent [Rodrik 2009, Tonnaer 2013]. On the other hand, the state is still a special participant in economic life: it acts as the organizer of legal and institutional

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1 The term *prosumption* was coined by Alvin Toffler in 1980 in the publication: The Third Wave: The Classic Study of Tomorrow. It refers to a combination of production and consumption. The authors concern in prosumer at first suggest that prosumption is not new but is actually primordial. Prosumption has always existed in the economy, but many social changes (e.g., the rise of the Internet) have greatly expanded both the practice of prosumption and scholarly attention to it. According to the authors, prosumption has its most obvious and direct relevance to the economy. As a result, the authors also frame it in terms of contemporary capitalism.

order and also as buyer and producer. The state seems to be the only entity which can effectively limit destructive operations of other economic actors and ensures social and economic balance. However, difficulties connected with its functioning in turbulent times necessitate changing its place and role because its tasks are at least mismatched. In many cases national institutions indicate weaknesses in the realization of social goals – evidenced by a lack of citizens' economic safety and progressive polarization of incomes. Additionally, intergenerational responsibility remains a very important issue. New processes weaken the institution of the state and its interventional tools. Meanwhile, the strength of the state should be indisputable, because its weakness, as a consequence, can diminish the protection of societal interests. New phenomena change the nature of the state and necessitate a redefinition of the state and its role and tasks.

It is also worth mentioning that an examination of the history of the greatest crises prove that antisocial behaviors of economic units foreshadow them. Nobel Prize winners in economic sciences George Ackerlof (in 2001) and Robert Shiller (in 2013) indicated a wide range of antisocial behavior. Their principles come from animal instincts and understanding them can allow for a more thorough comprehension of the modern economy and the behavior of public and private agents including the state, which is not an impartial institution because it is managed by people [Akerlof and Shiller 2009].

It is impossible to mention all the challenges of a contemporary state. Some of them are stable and their importance and influence can be observed in decades, the importance of others is changing rapidly. In the end, it is worth mentioning some of the most urgent current and near-future challenges for the contemporary state: the erosion of trust in institutions, changes in climate, the growing number of military conflicts and migration processes.

According to some modern economists, the financial crisis is a symptom of a larger erosion of the contemporary capitalist system and its main institutions. This erosion is caused by many contemporary phenomena. Among them, the most important is the economic potency of “big players”, especially transnational corporations and capital groups on one hand and on the other hand transnational organizations such as the WTO, World Bank or OECD. These institutions are public and private, so their goals have to be different because they represent different interests. Additionally, climate problems seem to be more and more important and can only be solved on an international level. Also military conflicts don’t have only regional impact but influence many actors: states, international organizations and cause anxiety and uncertainty in many markets.

Among the challenges of the contemporary state there is also its future evolution, because not only are working conditions of the state changing constantly but also the state itself. In the traditional model (going back to the views of Napoleon and Georg Hegel), the state and its civil servants were all-wise and all-powerful and therefore should decide what was best for the whole society. An extreme example of such a model was communism, which has proved its inefficiency. The solution was state withdrawal from the market and a dedication of its prerogatives to the private sector and the free market. Also, this point of view was wrong because people forgot that only the state could guarantee the free market and respect for the law, standards and Fukuyama agreements [2004]. Nowadays, the power of the state doesn't come from administrative excellence and a perfect system of hierarchy and supervision. Its roots come from the ability to solve problems for civil society and entrepreneurs [Goldsmith and Eggers 2004]. A different point of view of the future of the state is presented by Micklethwait and Wooldrige [2015]. The authors of "The Fourth Revolution" warn decision-makers and societies that if the state is not radically reformed and reduced then Western democracy could suffer and the role of more innovative authoritarian regimes, notably in Asia, could increase.

Alternatively, Martinez [2009] describes how the flawed myth of the "invisible hand" distorted the understanding of how modern capitalist markets developed and actually worked. Martinez draws from history to illustrate that political processes and the state are not only instrumental in making capitalist markets work but there would be no capitalist markets or wealth creation without state intervention.

Such differences in perception of the role of the state in the future causes many problems and therefore challenges. In the past, decision-makers and societies had a choice between a strong or a weak state. But both concepts fail to explain current economic problems and seem to be wrong when thinking about the future. Also noteworthy is the latest book by Tanzi [2014]. "Government versus Markets: The Changing Economic Role of the State" addresses the fundamental question of what governments should do, or have attempted to do, in economic activities in past and recent periods and also speculates on what they are likely or may be forced to do in future years. The investigation assembles a large set of statistical information that should prove useful to policy-makers and scholars in the perennial discussion of government's optimal economic roles. It has become an essential reference work on the analytical borders between the market and the state in the future.

The state also plays an important role in the new economics of labor migration theory. States may significantly shape migration, promoting reliable insurance markets and capital markets, which give people greater security and allow them to pursue investments in the original community. States may introduce policies to alter income distribution rather than reducing migration, however, shifts in income distribution and inequality levels may in fact change the composition of migration [Stark and Yitzhaki 1988]. The state's ability to create institutions and infrastructure and to provide opportunities for individuals [Skeldon 1997], mainly through a broad range of policies, suggests that the state influences migration in multiple ways. The main migration determinants, such as: economic structure, inequality, social welfare, military or religious and cultural conflicts are significantly affected by the state [Vezzoli 2014].

Conclusions

The modern world is changing rapidly. Many new factors influence the conditions of the state's functioning and the contemporary state exemplifies many contradictions. Additionally, contemporary economics is not able to keep pace with a rapidly-changing environment and immediately reacts when new challenges appear. But the state is stable, because of its tasks and functions, the most important and crucial economic agent. It is also the institution which can successfully influence other agents by regulating different social and economic spheres of life. Thus, the strength of the state should be indisputable, because its weakness can, as a consequence, reduce the protection of a society's interests. New solutions for modern states should include, on the one hand, a plan of action for market failures and, on the other hand, should counteract institutional imperfections, especially public. Therefore, such actions are necessary which help to indicate these factors and which help strengthen the state's position. The adopted solutions should comply with macroeconomic stabilization, which has to be accompanied by microeconomic and institutional policy focused on the correction of market mechanism failures. Properly operating public institutions create a structure of incentives which contributes to an increase in national competitiveness.

The new attitude to state's tasks should respect the new challenges of the era. In turn, the state should be equipped with new tools. A modern and efficiently-functioning state has to be able to adapt to complex challenges coming form an unstable, global world. Therefore, it is necessary to take into consideration economic, political, social and ecological dimensions.

The article contributes to the general debate concerning the challenges of the contemporary state and its modern tools. Changes in the traditional perception of the role of the state in the economy are necessary. On the one hand, the volatile and changeable environment determined by dynamic social and economic processes needs a new definition of the state's place in the economy and a new specification for its efficient tools. On the other hand, economists are unable to explain all the processes which take place in a modern economy and define the role of state and exemplify its tools.

During the last few decades we have observed fluctuations in understanding the role of the state in the economy and many theories were created and implemented. Some of them helped to defeat depressions and stagnations in particular periods in economic history, but none of them are universal or provide the right tools in longer periods. These theories are not able to predict the role of the state in the future, they can only adapt to the present economic situation.

To find adequate and efficient tools it is necessary to indicate areas in which the state's intervention seems to be necessary. It is impossible to identify and describe all of the factors influencing the contemporary role of the state and it is not the aim of this article. The wide variety of factors very often doesn't allow one to draw right and clear conclusions. Therefore, the article briefly describes the main challenges, which concludes that the current role of the state has to be redefined and that traditional tools used by monetary and fiscal policy are at least insufficient.

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