# ECONOMIC INSTABILITY – A CONCEPTUAL APPROACH

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Questions of the type: " How can one describe the behaviour of an economic system?, "How can one define economic equilibrium?" or " Is the normal condition of an economy a balanced or an unbalanced one?" have always dominated economic thinking along its whole history.

In the opinion of the author, the normal condition of an economy, if considering at least its duration and main tendencies, as well as – why not? - the advantages it acquires along its evolution, is that if disequilibrium, viewed as a positive instability which forces the development of the system. Disequilibrium and economic instability are considered equal, as both notions define the conflictual condition among the unequal forces manifested in economics.

In one way or another, either explicitly or implicitly, each school of economic thinking makes use of the notions of equilibrium or disequilibrium, stability or instability of the economic macrosystem. Economic theory attempts at elucidating, explain and anticipate the behaviour of the economic variables, of the economics, viewed as a whole. The extent to which suitable explanations are provided for the real economic phenomena under development refelcts the attempts made by investigators at creating models, at extending and improving the existing ones, by modifying and eliminating any analyitcal restrictions, starting from quite different premises, potentially closer to the economic reality.

The essential aspiration of mankind, in general, of economists, especially, seems that of attaining both equilibrium and the "best possible" condition. Such wholly understand able human wishing probably comes from the attempts made at eliminating the apprehensions usually accompanying any disequilibirum, uncertainty, instability moments. Axiomatically, equilibrium assumes two aprioric ideas, first - the optimally native human behaviour and, secondly - the ontological tendency of the ecomonic millieu towards a balanced condition. The aspiration, tempting tendency of the macroeconomic environment towards equilibrium is also a consequence of the optimally native individual behaviour, known as being based on the instinct of self-preservation. Some difference should be nevertheless established between the individual level, based on survival through self-protection, and the macro-society one, which should necessarily include two basic components, namely:

- optimal superior aggregated behaviour;
- self-adjusting capacity of the economic system.

In a study published in 1973, A. Leijonhufvud observed that "the key problem to be elucidated in macroeconomic theory remains always the extent to which economy, or its branches, all subjected to the free market regulations, may be judged as a self-adjusting action"[1]. Extending the idea to the whole area of analysis, one may assert that the economic theory attempts at explaining the equilibrium or disequilibrium condition of an economic system, as well as at elucidating and measuring the – either temporary or durable - deviations from an ideally considered condition, of its causes and consequences.

From a classical, mechanical perspective, equilibrium may be defined as a *balanced condition among various forces of an economic system*, e.g., equality between the demand and the offer of some market. On the other side, equilibrium may appear as a *resting condition of a system or of its compounds*. At this point, analysis hesitates between a mechanical perception (such as the Keynesian equilibrium of resources underutilization) and an approach capable of grasping the conflictual or cooperation relations established among the economic agents. In this respect, Fr. Perroux considered that "an ecomonic assembly faces general equilibrium when the resultant of the modifying energies of the agents forming it is null"[2]. F. Hahn, exploiting the relation between information and the activity of the economic agents, appreciates that "an economy faces equilibrium when the messages induced in the system do not determine the economic subjects to modify the concepts on the basis of which they act or the objectives had in view"[3]. For E. Phelps, one of the leaders of the "New microeconomics", equilibrium expresses the condition in which "the level of wages and of prices is, in time and space, the one expected by the economic agents"[4].

Nevertheless, numerous researchers drew attention upon uncertainty, instability, economic disequilibirum. Uncertainty is always associated to life, to search, development and action, while equilibrium is associated with certainty and stability. One should not forget, however, that "search for certainty is always a source of nihilism. Certainty and nihilism are twin notions, as both of them fail to accept reality, the change, contradiction and even some of the most courageous scientific ideas"[5]. In a classical interpretation, the equilibrium between demand and offer is a rather static one, similar to the Newtonian-type equilibirum, a spontaneous pattern, reality being manifesting in an instant moment of time. Professor Anghel Rugină showed that classical thinkers, such as L. Walras, W. Pareto, A. Marshall were almost exclusively concerned with the problem of stability related to a condition of stable equilibrium. In the second half of the 60'ies, the pioneering studies of R. Clower and A. Leijonhufvud, together with the researches of some prestigious economists, such as: R. Barro, H. Grossman, J. Dreze or E. Malinvaud, bring essential contributions to explaining the so-called "stable disequilibrium" condition (which is more and more frequently replaced by the term of non–Walrasian equilibrium), viewed as a normal economic condition, as a „sui generis" equilibirum.

A. Rugină considers that "the results of sociology, economics and of the classical political science are organically valid exclusively for the pattern of a free and stable society, for an economic system viewed as an ideal world towards each of us should be oriented". The question to be answered remains: is the world in which we are living a really ideal one? Is economic balance a possible explanation, a normal condition or is it only a tautological concept?

In real time, it is nevertheless obvious that uncertainty and disequilibrium are actually characterizing the state and evolution of any economic system, which explains the solution now generally accepted, involving the design of some patterns capable of recognizing and describing economic disequilibrium as a normal condition of economy.

That is why, specialists are increasingly interested in non-equilibrium systems, viewed as structures which interact with the environment through entrophic flows, once they had understood that, under non-balanced conditions, economy, similarly with the simple matter, may manifest – in most general situations – an extremely complex behaviour. The Nobel Prize Winner Ilya Prigogine used to say: "… I like to assert that, at equilbrium, matter is blind while, far from equilibrium, it starts to see things …".

Human society has never advanced under stable conditions, on the contrary, its progress was recorded when instability, crises, uncertainty and tension were busily acting at the level of the global markets. Simplifying things, one might say that equilibrium, perfect stability represents the end of the road, when everything is stationary and all variables are a priori fixed in a motionless algorithm.

The observation may be made that, from a historical perspective, the capitalism of the last two centuries had to face numerous crises, stability and equilibrium being always arbitrary and temporary notions. Instability, the tesnion of the market and the continuous change were the main springs of economic evolution and progress. The same Ilya Prigogine considers that no scientific explanation can be provided for viewing economic equilibrium as a premise or starting point in economic analysis: "In certain situations, equilibrium may be attempted at, however the economic advance may rather depend on specific and necessary disequilibria"[6]. In spite of the almost frantic human aspiration towards equilibrium in the real life, the economic systems are no longer characterized by durable and stable equilibrium, at least not for significant periods of time. The moments of equilibrium may be rather viewed as exceptions, "points of intersections" through which an economic system has to pass during its evolution. The durability of an economy involves positive and/or negative tensions, which means disequilibrium. Evolutive instability should be preferred to a passive equilibrium.

At the level of all subsystems which create an economic complex, it is the market that assures the conditions for the adjustment of the sell-buying processes of goods. This is actually the simplest definition of the market: the assembly of all demands and offers for certain goods. By putting together the markets of all products – not as a simple summing up, but as a complex network, one may obtain the market of a national economy. "The market as such – said Alvin Toffler – is nothing but an exchange network, a control panel through which the goods or the services are oriented, like messages, towards adequate destinations". The markets ceaselessy receive and send forth messages towards various economic agents. The messages may be of acceptance or rejection, including – almost always – criticism and suggestions for future behaviours.

The dynamics and success of capitalism are equally due to and supported by the dynamics of the market. Nevertheless, even if the free market has always acted as the engine of economic growth and prosperity, being described by Hayek as a "combat of the humans with the impersonal economic forces, which made possible the development of a civilization never attainable by other means…"[7], it should not be viewed as an all-heal, and its functioning should not be considered as perfect.

Pre-eminently, the market is never objective. Sometimes, the market could wrongly reject a valid initiative; Schumpeter, discussing his conception on innovation, recognizes that, in some situations, the market may misunderstand the hypothesis of the enterpriser, so that the respective market should be reconstructed, for validating the new combination, incompatible with the previously-established hypotheses.

" The markets were created by neither God, nature or by the economic forces, they had been simply created by businessmen", said Peter Drucker. The natural condition of an economy is that of unstability, continuous tension between offer and demand, a situation generated by the permanent tendency of the economic agents of increasing their profit. Henri Guitton sees the market as "a struggle, a game in which each one tries to gain"[8], while F. von Hayek considers that "the market is viewed by the agents involved in the exchanges of goods as a threat, an arbitrary force which establishes the prices and, implicitly, their profits, their main interest being in controlling and influencing it".[9] Such a – frantic, sometimes – attempts of the economic agents, of controlling the market, backed up by the interventions of the state organisms creates and maintains the instability of the market systems.

Almost instantaneously, such a normal condition of the economy is associated to the descending phase of the economic cycle, instability being related to lower profits, massive unemployment, inflation and reduced investment flows. The real state of the markets is that of instability and volatility of the economic variabiles, the term „volatile" referring to unexpected changes, quite difficult to identify or maintain permanently. Such a definition may be easily applied for describing economic volatility, as well. In the economic sciences, volatility measures the amplitude of variables' fluctuations during an economic cycle, representing an important source for identifying the causes and effects of its alternating phases.

The demand, the offer and the price, representing economic variables subjected to instability, are not abstract notions. Their content is closely related to the behaviour of the economic agents on the market, to the way they respond to the action of the exogeneous or endogeneous factors which disturb the stability of a market. In this way, the factors generating cyclic fluctuations in economy are identified with those causing market instability.

Any analysis of the economic cycle is focused upon some categories of determining factors, such as[10] :

- level and variability, in time, of the utilization of labour and unemployment, known as depending on the nature of the economic branches, and associated with slight modifications of the real wages.
- output fluctuations, serially correlated with the fluctuating utilization of labour and unemployment.
- Fluctuations of the global economic cycle, correlated with currency modifications, manifested as reversed connections between inflation and unemployment (Phillips curves).
- Positive correlations, within an economic cycle, between the national revenue, consumption and extent of labour utilization.

Any economy may be "attacked" by various shocks - causing fluctuations – from the part of either offer or demand. Modifications of the aggregate demand may be determined by modifications of demand in either the private or public sector, as a result of some modified fiscal or currency policy. The shocks of the offer may be determined by productivity or by a modified offer function for various production factors.

G. von Haberler, who analyzed the factors inducing .cyclicity and, implicitly, instability, classifies them into active and passive factors, thus differentiating between the "per quam" and the "sine qua non" causes and conditionings.[11] In this way, crops fluctuations or variation in currency demand and, implicitly, in goods, represent active factors, while the structural phenomena of the economy are viewed as passive factors. That is why, a demarcation line is necessary, at least from didactic reasons, for a subsequent factorial analysis. As a matter of fact, such a dichotomy is difficult to obtain - for example, the extent to which some measure of banking politics affects equally the currency demand and, implicitly, the crediting one, the preference for liquidity and the level of investments, but also the strucural basis of an economy represent active or a passive factors. [12]

In any moment of time, a surplus of demand and/or offer is manifested on any market, in the same way in which the economic agents always have stocks of goods and reserves of productive factors. Such situations induce tensions and instability, the market system never attaining equilibrium. Economic instability expresses the modifications suffered by the limited resources and technologies, by the restricted acquisition of goods and services from the part of the buyers, as well as by some uncorrect, long-term decisions of economic politics.

In spite of the significant progresses recorded in the elucidation of several theoretical problems, numerous confusions, mis-interpretations and incorrect proposals are still affecting the practical conclusions of the macroeconomic theory on the understanding of the present causes of the economic fluctuations. The large diversity of the economic politics networks are closely related to the schools of economic thinking to which they belong: Keynesian, neoclassical, post-Keynesian, etc. The difference among these schools is refelcted both in the way they approach instability and in the solutions they put forward for assuring the stability of economic growth.

The theoretical debates are mainly concentrating around three main problems: i) the speed with which the markets (the labour market, especially) react to changes; ii) the manner in which anticipations are expressed and approached; iii) the relative importance of the two – long- and short-term - time horizons.

A different and, equally, special perspective for explaining the unstable evolution of an economy has been expresses by the 2004 Nobel Prize Winners in Economy, Finn Kidland and

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Edward Prescott, apreciated for their contributions to dynamic macroeconomy and for their „real cycle" theory.

Contrary to the traditional ideas on cycle and growth, according to which the economy follows some trend and the fluctuations, which are only temporary, orientate the economic activity on a winding road, on one side and the other of the main tendency, the economists of the „real cycle" consider that this trend, this tendency simply does not exist. In their opinion, the theory of growth is the same with the theory of the economic cycles. At economic level, they differentiate between two types of shocks causing fluctuations and instability: 1) exogeneous (calamities, wars, higher prices for strategic resources) and 2) shocks caused by technical advances and productivity. The evolution is explained by shocks, the irregular character of growing being induced by the irregularities of the technical progress. According to them, currency politics plays no role in influencing the cyclic development of the economy, while the cycles do not express the manifestation of some disequilibria but, on the contrary, an optimal adaptation of some economy towards equilibrium.

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