Guest article:

Overhaul Capitalism to Save Democracy

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Abstract[2]*: Why have our societies become so deeply divided, which is inimical to democracy? How do growing distributional conflicts impact governance structures? Why does fake news take often precedence over truth? What should be done to avert that the rule of law is undermined by the rule of the mob? It may be that the current crises (public health and economic) are harbingers of a new turning point in the evolution of capitalism. This evolution is interlocked with cycles of ideas, of public policies, and institutional change. A mixed economy took shape over time, in which a public sector and a private sector cohabit, based on market dynamism, entrepreneurship, with the shares held by the two sectors shifting in accordance with historical and local conditions. The debate that has started after the outbreak of the last financial crisis is about the path of capitalism, of the mixed economy, of democracy. We need to steer the course of events in the right direction via wise policies. Safeguarding democracy relates to the urgency to deal with climate change as an existential threat.*

Keywords*: Capitalism, central banks, climate change, community, economic crisis, democracy, European integration, fairness, finance, globalization, government, illiberalism, income distribution, inclusion, liberalism, market fundamentalism, mixed economy, pandemic, reforms, socialism, stakeholder, State.*

Introduction

Mankind will prevail in the fierce war against the coronavirus, a hidden, treacherous foe that has been attacking randomly and leaving many human deaths behind. The struggle with this pandemic has an end in sight because we have effective weapons to combat it now, such as vaccines, which are to be used on a grand scale, worldwide. But this is not the end of the story, for biological enemies may "visit"' us again. Therefore, humankind needs much more robust medical systems and better preventive schemes and procedures. We will overcome the severe economic downturn as well. As a matter of fact, an economic recovery is underway which would be bolstered by a fast rollout of vaccines[3]. But this crisis will leave deep scars, given that economies are undergoing sweeping changes. These changes add to tensions and intricate issues and policy dilemmas that precede the Pandemic. The financial crisis that erupted a decade ago prodded social scientists and policy-makers to think more thoroughly about serious problems that afflict economies and societies. In the text below, I hook up with ideas that I have expressed

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[2] This is a version of "The Coronavirus Crisis and the Economic Crisis. Is Capitalism at a New Turning Point?", that was published in *Europolity*, No. 2, 2020, with a Romanian version published in *Contributors*, 14 September 2020.

[3] The World Economic Outlook, IMF, April 2021.

in recent years and extrapolate them to the fallout from the current crises[4]. In view of recent and more remote events it pays to ask ourselves why have our societies become so deeply divided, which is inimical to democracy? How do growing distributional conflicts impact governance structures in advanced economies? Why does fake news often take precedence over truth, with some social media playing a nefarious role in this respect? What should be done in order to avert that the rule of law is undermined by the r*ule of the mob*, when so many people seem to lose confidence in governing elites and succumb to sirens of anarchism, violence-peddlers, and authoritarianism.

It may be that the current crises (public health and economic) are harbingers of a new turning point in the evolution of capitalism. History has lessons to learn, although interpretations may vary owing to intellectual propensities, or interest-related biases. This does not invalidate the rationale to revisit critical moments in the evolution of modern capitalism, which can be pretty illuminating as to its technological, economic, and social drivers.

My guiding idea is that the evolution of capitalism is intertwined with cycles of ideas, of public policies, and institutional change. The concept of 'learning by doing' can be applied to capitalism's ups and downs, its windings, yet following a clear-cut evolution over the past hundreds of years. A mixed economy took shape over time, in which a public sector and a private sector cohabit, based on market dynamism, entrepreneurship, with the shares held by the two sectors being moulded in accordance with historical circumstances and local conditions.

Modern capitalism, in advanced economies, has among its core principles the notion of 'equal opportunities'. To what extent reality befits this principle is an open question and is part and parcel of the current quest to re-examine the functioning of capitalism. I would argue that the debate that started after the outbreak of the financial crisis more than a decade ago is not, chiefly, about capitalism vs. socialism, but about the path of capitalism, of the mixed economy, of democracy; that we need to steer the course of events in the right direction via wise policies.

There is the lesson of communism, that had in its genes an anti-democratic ideology and unsurmountable structural flaws of its *command economy*. And there is the lesson of National Socialism in Adolf Hitler's Germany, of fascism in general. Totalitarianism crushes and humiliates the human being, who has the innate right to freedom; it does proclaim and imposes the single thinking/ideology and the single party rule, and it creates monstrosities. But capitalism embodied by unrestrained markets, lack of proper rules and regulations, by *market fundamentalism*, is itself detrimental to the functioning of a fair market economy, to democracy. As Robert Reich put it, this occurs when those with the most economic power are able to shape "the rules of the game" to their advantage (2016, p. 163). The crux of the matter, in the end, is for whom the economic system does work, as democracy hinges on it. When markets work for too few people "undemocratic liberalism" (Yascha Mounk, 2018) comes into the open.

The great stake in the current debate on the future of capitalism, is to safeguard democracy as *liberal democracy*. While the distinction made between liberal democracy and *illiberal democracy* is not devoid of meaningfulness, it can plant seeds of confusion. This is because democracy has liberalism in its genes (Dăianu, 2018); democracy boils

[4] Referenced works include 'Which way goes capitalism' (2009), 'When finance undermines economy and corrodes democracy' (2011); 'Liberal vs. Illiberal Democracy' (2018); 'The New Protectionism' (2017); 'The Coronavirus has laid bare the need to revamp the EU' (2020).

down to power in the hands of citizens (the people) and decision-making made via institutionalised checks and balances, through a myriad of civic organizations that serve the interests of citizens at large – what John Kenneth Galbraith referred to as *countervailing power*. Safeguarding democracy relates to the urgency to deal with climate change as an existential threat. This is because climate change brings with it the spectre of "hydraulic civilizations" (Karl Wittfogel's concept is useful in this respect), unless we revise public policies and repair our relationship with Nature.

In the following sections, I mention characters, ideas and institutions, events, which illustrate key policy and institutional shifts in the evolution of capitalism as an economic system: the paradigm shift after Great Depression (*The New Deal*) and the Bretton Woods arrangements (section 1), the paradigm shift of the 1970s and 1980s with deregulation and globalization, China's economic rise (section 2), the *Great Recession*, the Pandemic, climate change, with re-regulation of finance, a rethinking of globalization (section 3), a return of Keynesian policies and of the State (section 4). The last section highlights critical policy issues in order to safeguard democracy and cope with climate change and other major challenges.

1. The New Deal and Keynesian Policies: A Paradigm Shift

The New Deal was introduced by President Franklin Delano Roosevelt in the wake of the *Great Depression*. His administration grasped the importance of reforming public policies and mechanisms (including a budding social insurance system) in order to tackle big social and economic problems.

Regulations were introduced in finance as a major legislative novelty through the Glass-Steagall Act that was enacted in 1933. Investment banks were separated from retail banks, most banks turned regional – an architecture that resonates with what Andrew Haldane and Robert May proposed in 2011 in order to control inter-connectedness as a means to contain contagion. There were a novel approach to Fed's activity and new institutions to prop up economic development (e.g.: Tennessee Valley Authority, as a development institution, including its planning function). State intervention was required and strengthened by the preparations for entering World War Two (WW2).

The Great Depression and National Socialism in Germany, his *mefiance* vis-à-vis corporatist structures and his thinking in line with the Austrian School, made Joseph Schumpeter be sceptical about the future of capitalism ("Capitalism, Socialism and Democracy"); he saw whatever was remote from unrestrained free markets as leading to socialism[5]. At Cambridge (UK), a powerful Marxian current became vocal in the likes of Maurice Dobb, Joan Robinson, Piero Sraffa. Oskar Lange and Michał Kalecki advocated socialism, yet they did not think in terms of a command economy, but rather of a 'market socialism' (as was attempted in former Yugoslavia) and this led to a fascinating public debate, together with Dobb, versus Friedrich von Hayek and Ludwig von Mises on *the Economic Calculation*[6]. It can be surmised that Schumpeter was not acquainted with all the horrors of Stalinism, since he passed on in 1950 – long before the collapse of communism and three years before the death of Stalin. And he did not get the chance to witness the rebuilding of Europe in the aftermath of WW2.

The overhaul of capitalism that started with the New Deal in the United States

[5] His presentation at the American Economic Association in 1949.

[6] A volume that brings together the main protagonists of this lively debate, with some of their key contributions, is Alec Nove and Mario Nuti (1972).

and what evolved institutionally and policy-wise in post-war Europe was a major turning point for capitalism. Economic development in the West after WW2 fostered market reforms in the East later on (in Hungary and Poland prior to 1989), and prompted the fall of communism, eventually.

In Europe, Keynesianism, as a school of thought and as the basis for policies to combat deep recessions, was preceded by Keynesian practices. Public works were undertaken in Sweden and in the United Kingdom before Keynes' *Magnum Opus* (1936) went to print. And, in the aftermath of WW2, economic reconstruction policies marked a so-called "Golden Age", either in France, home to *economic dirigisme* (the Plan Commission created by General Charles de Gaulle in 1946 and led initially by Jean Monnet, one of the founding fathers of the European project), or in Italy via IRI (*Istituto per la Ricostruzione Industriale*, a remnant of the fascist regime, but that lasted half a century after the war was over), in Federal Germany with its *Ordnungspolitik*, a policy based on rules and neo-corporatism that brought together the social partners' positions (*Mitbestimmung*/co-determination)[7]. Ludwig Erhard, one of the intellectual fathers of *Ordnungspolitik*, is a revered name in Germany, along with Chancellor Konrad Adenauer.

In the United States, in Europe, intellectual elites graduated from top notch universities which nurtured professional excellency and meritocracy (the Ivy League in the US on the East Coast, UCLA, Stanford, Berkeley, etc. on the West Coast, Chicago University and Northwestern University close to the Great Lakes, in the North). Although these days some criticise elitist schools , which are seen as representative for an 'Establishment', and which, allegedly, reproduce political and social strata 'cut-off' from the rest of society, one can easily overshoot in making judgements. A society needs elites, competent people. The fact that, not unfrequently, networks operate and reproduce themselves, that they appear to have become impervious to outsiders, should not lead to throwing the baby out with the bathwater. This does not mean that elites cannot make monumental mistakes[8], as was the case with finance deregulation, or with promoting boundless globalisation – which both fuelled scepticism and resentment towards experts.

It is worth mentioning in this context the confusion entailed when truth is perverted and fake news is deliberately spread out (much facilitated by the Internet). In a powerful message, Michiko Kakutani quotes Hannah Arendt (1951): 'The ideal subject of totalitarian rule is not the convinced Nazi or the convinced communist, but people for whom the distinction between fact and fiction (i.e. the reality of experience) and the distinction between true and false (i.e. the standards of thought) no longer exist' (2018, p. 11). Since truth is fundamental to democracy, this trend should worry us to the utmost.

Bretton Woods and the multilateral system

During WW2, a system for regulating international economic relations based on multilateralism was designed and subsequently put in place. In time, the world witnessed the founding of the United Nations (that succeeded the League of Nations), the International Monetary Fund, the World Bank, regional development banks (for Latin America, Asia, Africa), the General Agreement on Tariffs and Trade (replaced by the WTO subsequently), etc.

The English economist John Maynard Keynes was the prominent brain in the

[7] For an analysis of post-war economic reconstruction in western economies, see also Rudiger Dornbusch, Wilhelm Noelling and Richard Layard (ed.) (1993).

[8] 'The Death of Expertise' in the overdramatized words of Tom Nichols (2017).

talks at the US town that lent its name to the Bretton Woods Arrangements. These arrangements pursued a system of multilateral ordering of international of economic and financial relations, with relative stability of exchange rates, management of capital flows to support the efficacy of monetary policies[9]. The cornerstone of the Bretton Arrangements was the US dollar as the world's major reserve currency and which was tied to gold. What mattered also enormously was the US economic and military status in the world, in which *Pax Americana* had superseded *Pax Britannica* – despite the existence of a communist subsystem which was dominated by the Soviet Union.

When the US became over-stretched (to use Paul Kennedy's concept) globally owing to multiple wars and the erosion of its economic supremacy, the dollar was cut off from gold (in 1971) and the switch to flexible exchange rates was made, thus boosting financial transactions and fostering the development of financial arbitraging instruments. Seeds were planted that germinated in the over-financialization of economies[10] and the burgeoning of financial crises.

There is a debate nowadays on whether to revert to a more stable system, similar to the Bretton Woods arrangements. Yet the crisis of globalisation and the resurgence of nationalism, a spreading 'inward looking' syndrome, inter alia, do not favour a new Bretton Woods regime. The rise of China as a geopolitical and economic rival for the West, the nature of its public governance model, big national security challenges in the West, have all changed the geopolitical equation in the world radically.

Yet, there are global commons to be provided - like dealing with climate change and pandemics. Therefore, it is essential to consider areas of cooperation among geopolitical rivals.

2. The paradigm shift of the 70s-80s: liberalisation, globalisation and 'efficient markets'

The 70s and the 80s were marked by discontent vis-à-vis the excesses of Keynesian policies. There were also episodes of very high inflation, although major economies witnessed deep recessions – *stagflation*, as a combination of high inflation and recession. Monetarism came to the fore in central bank practices at that time. Paul Volcker at the helm of the Fed curbed double-digit inflation in the US, even at the cost of very high unemployment – which, in a way, was at odds with the Fed Employment Act of 1946, that mandated the central bank to pursue high employment as well.

Milton Friedman, Karl Brunner, Allan Meltzer and other monetarists set the stage for the rise of Ratex (rational expectations) as a school of thought, the latter having Robert Lucas and Thomas Sargent as leading academics. Ratex was based on the assumption of quasi-perfect markets and the uselessness of stabilisation interventions on the part of governments. The *Great Moderation* years (two decades of subdued inflation and steady growth, ahead of the *Great Recession*) seemed to score decisively in favour of this approach. But Ratex proved its own limits, for markets are not perfect, just like optimisation algorithms on the basis of which individuals and firms operate.

[9] A combination of goals that is defined conceptually by the so-called 'impossible trinity' in macroeconomic policy: the impossibility to achieve free movement of capital, exchange rate stability and autonomous monetary policy simultaneously.

[10] For the enormous growth of the financial sector in recent decades, see Robin Greenwood and David Scharfstein (2015), Thomas Philippon and Ariell Reshef (2013). Greenwood and Scharfstein show that while finance made 2.8% of US GDP in 1950, it contributed to 8.3% in 2006. The share of finance in corporate profits rose much more over the same period of time.

Behavioural economics (Herbert Simon as a forerunner with his 'bounded rationality', Daniel Kahneman, Robert Shiller, Richard Thaler, Amos Tversky, etc.) came with major nuances regarding how people make decisions, with ingredients such as affection, simple rules, emotions, empathy, loyalty, individual and group identities being pretty important in people's choices.

But human being's acquisitive nature (*Homo Oeconomicus*, which is not at odds with *Homo Faber*) is, arguably, not dented by behavioural economics in understanding its habits and propensities. Under the same conditions, most people choose to have more rather than less. That is why it is difficult to alter the logic of economic activity (net revenue/profit maximisation), to make markets internalise externalities that they do not readily perceive, or are forced one way or another to take into account (as when a Pigou tax is imposed). It is not simple either to redefine welfare as a statistical and accounting methodology; markets are used to aggregates of economic activity that increase ceaselessly, as much as possible, even if macroeconomic corrections are often asked for by widening deficits and large debt stocks. All this makes us think that markets do not accept (yet?) that some people might be more content with having less, even though such a mindset might be tantamount to rescuing the human species and a proper surrounding habitat. There is a market myopia judged in a broad sense, which further weakens highly sophisticated models that can be invalidated by non-linearities[11].

Inflation targeting (the monetary policy regime implemented in advanced economies in the past two decades) replaced the control over monetary aggregates, while the focus on price stability appears to have put central banks on autopilot. Inflation targeting uses models that work with output gap (potential GDP) as a key concept that implies a trade-off between inflation and unemployment (see Jordi Galli, Richard Clarida).

The fall of the Berlin Wall, the collapse of communism, augmented a general frame of mind, stimulated globalisation, the belief that the world has come to 'the end of history', as Francis Fukuyama put it (1990). But the less benign side of globalisation and financialization of systems were blatantly overlooked. The deregulation of finance, *the light touch regulation regime* (that started with the Big Bang in the City of London (in 1986) and continued with the rescinding of the Glass Steagall Act in the US in 1999) can be seen as one of the most harmful policy capture in advanced economies, with global repercussions, and which enhanced the Great Recession.

China's awakening: state capitalism and a monolithic political structure

From 1978 onwards, under Deng Xiao Ping's leadership, China embarked on a path of market reforms, which ensured swift and steady economic progress and made the country a global power in a few decades time. Its inhabitants and enormous natural resources, the industrial development of the past decades and a remarkable technological advance have made China a geopolitical rival of the US, of the Western world. Yet, China has stuck to a monolithic political structure and projects an illiberal political model, a form of a broadly based state capitalism, despite the domestic entrepreneurial effervescence and the development of remarkable private companies.

There is an intense ideological competition, pending responses from the US and Europe (the EU). However much some claim that China does not seek to provide an

[11] As was the case with models used by the Long Term Capital Management/LTCM hedge fund; fearing a financial market meltdown, the Fed "coordinated" the bail-out of LTCM in 1998.

alternative, that its model fits its own development needs and not much else (Kishore Mahbubani), a competition is underway as the Asian giant is expanding its interests worldwide, in Europe included. China also seeks to set up a network of international institutions, presumably as an alternative to the Bretton Woods arrangements, that are seen to be too much under western influence. Competition with China is ever broader, be it geopolitical and military (security-related: on the ground, in space, in the oceans), technological, and economic.

In this context, it is easy to see why the European Union aims at achieving an economic and technological 'sovereignty', as a response to a new global geopolitical context – not least also because of the erosion of multilateralism in international economic relations, the decline of globalisation as it has been practiced over the past decades, as well as strains in transatlantic relations. It is to be seen whether the Biden Administration will be able to resuscitate multilateralism, in spite of geopolitical rivalries.

3. The great recession, the coronavirus pandemic, climate change: re-regulating finance, rethinking globalization, resuscitating public policies

The Great Recession, which broke out in 2008, marked a wake-up call and an attempt to return to a regulated financial industry (giving up *light touch regulation*). This was encouraged by insights from the analytical work of Alexandre Lamfalussy, Anat Admati and Martin Hellwig, of other kindred spirits, from rediscovering Hyman Minsky and Charles Kindleberger's analyses[12]. The recourse to quantitative easing (QE) unfroze financial markets and, in the euro area, it rescued (via the ECB) the single currency. But QE is, arguably, a sort of "kicking the can down the road", though arguments noticing a dramatic decrease of "the natural rate of interest" (Knut Wicksell's concept) and, relatedly, of the policy rates of central banks, are to be taken into account: demography, falling productivity gains (Robert Gordon), *secular stagnation* (Larry Summers, who revived the concept used by Alvin Hansen back in 1938), a shortage of *safe assets* (Robert Caballero and Emmanuel Farhi), etc. Olivier Blanchard speaks about a new normal in monetary policy, which would allow the financing of larger public debts (as compared to Kenneth Rogoff and Carmen Reinhart' 90%-of-GDP ceiling). Rogoff advocates even negative nominal interest rates.

This is a time when both theory and practice are in full display of creativity, but also a time of confusion and puzzles mingled with big conundrums and uncertainties; as some say, policies are sailing in uncharted territories. Disconcerting for many is the flattening of the Phillips curve, the persistence of very low inflation with very low unemployment rates.

The Fed has announced a new monetary policy framework, which targets average inflation over time allowing inflation to overshoot the target without a response from the central bank. At the same time, the unemployment rate would not trigger a policy reaction as long as inflationary pressures are not manifest; monetary policy would focus on stability, with income distribution as one of its benchmarks. In a way, it is a return to the Fed's 1946 mandate. The ECB and other central banks are also re-examining their monetary policy frameworks.

A critical policy issue is whether central banks can target several objectives – as

[12] Re-regulation of finance involves also a redeeming of capital controls, especially of capital inflows surges (see also Bilge Erten, Anton Korinek, and Jose Antonio Ocampo, 2021). The IMF, too, changed its views on capital controls acknowledging the destabilizing effects of large capital in- and outflows.

there is also the desire to consider climate change as well. Taking into account climate change has become a stated objective of the ECB. As Isabel Schnabel put it "when markets fail, there is need for collective action" (2020).

But central banks cannot be a factotum, and this is not only because they lack sufficient independent instruments (*the Tinbergen rule*) in pursuing several objectives. Nonetheless, central banks need to be responsive to huge challenges and, in addition, they have to adapt their models and practices in view of flaws that these very models have glaringly revealed[13]. Central banks cannot escape the spectre of commercial banks being increasingly exposed to industries that would fail the acid test of greening themselves. This is why green bonds as collateral are gradually finding their way into central banks' practices. Even the conduct of monetary policy may have to consider climate change.

Some voices raise the issue of central bank independence, not only in virtue of a perceived 'fiscal dominance' that might lead to monetisation of deficits (the *New Monetary Theory* is looming highly in this respect), which is a path riddled with significant risks. For, thinking that high inflation would solve the issue of over-indebtedness opens the door to all sorts of troubles.

Climate change as an existential threat: the spectre of "hydraulic civilizations'

The threat of climate change is not new. Nevertheless, a technology-driven optimism prevailed, with the Club of Rome's messages, decades ago, being light-heartedly put aside and (MIT-based) Jay Forrester's global dynamics models likewise. Public policies remained unmoved even when Nicholas Stern, a British high-ranking official (who served as Chief Economist of the EBRD, then of the World Bank), released a report (2006) that highlighted environmental issues and risks as the most blatant "market failure" in history. The past years' sequence of events, with wildfires, the melting of the ice cap, floods, the dramatically widespread and fast changes in temperature, etc., pinpoint a dangerous future for mankind, with a possible extinction of humans if nothing is done to rescue ourselves.

All this means to change public policies, bolster public budgets that would allow timely interventions in case of emergencies as well as systematic actions that would help face major adverse shocks and increase economic and social systems' resilience and versatility. People's behaviour needs to change (though man's acquisitive nature is a major hurdle), industries need to cut back on their carbon emissions and our relationship with Nature must change. Unless this is done, a spectre of "hydraulic civilizations" (to use Karl Wittfogel's concept), for which access to water resources equates power, would be looming, would encourage authoritarian tendencies.

It is refreshing to see the policy stance of the new European Commission, of the EU institutions in general. The 'Next Generation EU' programme is a step in the right direction and EC President's Ursula von der Leyen speeches in the EU Parliament show that, in Europe, politicians and people at large take climate change very seriously, as do most Americans[14]. The US re-joined the Paris talks on climate change, which is an ominous fact. And the Fed (the US central bank) joined the Network for the Greening of the Financial System (NGFS). The European Central Bank is adamant about the need

[13] A major flaw that these models have revealed is that they focused almost exclusively on price stability; and price stability does not secure financial stability automatically.

[14] Frans Timmermans (EC Vice-president)'s words that he may not be able to look into his children's eyed in the not too distant future unless bold action is taken in order to deal with climate change is pretty telling (Bloomberg interview).

to address climate change, as is the European Investment Bank. Like her counterparts in Europe, Kristalina Georgieva, the head of the IMF, is pretty clear about the need to combat carbon emission and revisit public policies to this end; a carbon tax implemented globally would be a step forward[15]. The global accord on climate change must be underpinned by both the US and China so that fossil fuel dependence be reduced drastically.

COVID-19, the economic crisis, artificial intelligence and labour market redundancies

The healthcare crisis and the partial lockdowns revealed the possibility for many companies, public institutions to continue functioning with a considerable reduction in the number of employees. Homeworking, digitization, new technologies in general, entail sweeping changes to the activity of many firms, leaving their hallmark on the future structure of labour markets. This impact is to be seen in the context of an increasing number of losers due to unrestrained globalization[16].

The economic and healthcare crises are forcing companies to streamline their operations, cut workforce not only temporarily. Automation, artificial intelligence, entail a very severe joint impact on labour markets. Mass redundancies will heighten social issues and structural unemployment. This is why the introduction of minimum guaranteed wages is experimented as a means to prevent social tensions going to the extreme.

The financing of a minimum guaranteed income could be done through a 'taxation of robots' (as some have advocated) which would lead to an income redistribution from businesses that use robotics (and displace human labour) to people who lose their jobs; the more automated a lucrative business is, the more taxed it will be in absolute terms. Such ideas are meaningful as we strive to avoid facing scores of jobless, desperate people on the rise, serious social anomies[17].

4. The return of the state – a one-off or lasting trend?

The COVID-19 public health crisis, the severe economic crisis and a potentially broad-based social crisis in the years to come, all of them seen as major national security concerns, have triggered a tendency for a stronger presence (intervention) of the State in the economy, in a bid to provide safeguards and key public goods: to make healthcare systems (which become national security concerns) more robust/resilient, to promote inclusion, to cope with geopolitical challenges, to promote or support economic 'champions', and, not least, to deal with climate change.

In Europe, more resources in the EU budget are envisaged to be collected via own resources (new taxes – carbon tax, digital tax, a tax on financial transactions, etc.) by fighting tax evasion and tax avoidance. EU Commissioner Paolo Gentiloni is adamant in this respect not only vis-à-vis the abusive, incorrect practices of telecom giants; he claims that those who are the big winners of the health crisis and of implementing new technologies should participate more (a sort of a windfall gains tax) in the joint fight against the coronavirus and mitigate the pains of the economic crisis, have an adequate

[15] Numerous famous economists signed an open letter in favour of a Pigou tax implemented globally in order to combat carbon emission, Wall Street Journal, 18 January, 2019.
[16] David Autor has revealing studies on globalization and the rising number of losers in advanced economies, the decay of industrial cities and why this matters for local and national politics.
[17] See also Anna Case and Angus Deaton: 'Deaths of despair and the Future of Capitalism' (2020).

contribution to Member States' budgets.

COVID-19 and the severe economic crisis have called for massive interventions on the part of both governments and central banks. The tools of this intervention evince a temporary component which shows up in larger budget deficits and central banks' special operations, but some of the new measures are quite likely to stay on geopolitical and security grounds, or as they are motivated by the need to address economic and social issues, to pursue industrial policies and to counteract climate change effects.

Strategic foresight at the macro level will probably acquire higher significance. Commissioner Maros Sefcovic announced that he would recommend Member States to develop strategic foresight capacity – which should not be mistaken for either forecast analyses or policy planning conducted as routine endeavours. France has announced a revival of the 'Plan Commission (Commissariat du Plan), as part of a strategic foresight and guidance of its investment policy[18]. Other countries will probably follow suit, and even the EU will develop such a capacity. This, it makes sense to assume, would collide with the current stance on state aid if the goal of fostering European champions is seen as a means to underpin sectors that promote innovation and technological excellence. It is to be noted here the unhappy experience with the Lisbon Agenda and the 2020 Agenda. The United Kingdom keeps to a similar path, i.e. the last conservative governments announced industrial policy programmes.

New Deal-type measures are gaining currency in the United States against the backdrop of the geopolitical/technological/economic competition with China, the economic competition with the EU.

The 'return of the State' comes, nevertheless, with a risk that ought to be considered: as markets alone can neither solve social issues, nor surmount economic crises, a considerable higher public support will not automatically ensure lasting solutions (rising public debts are a telling evidence in this regard). We need smart states that should address market failures and create public goods on a necessary scale[19]. But, for this to happen, states need robust budgets, higher public revenues. This implies combating tax evasion and tax avoidance resolutely, punishing unethical corporate conduct firmly, revamping fiscal regimes and raising taxes on the wealthier members of society eventually. It also demands diminishing undue rents that some industries extract from the economy/ society. How to achieve this is a big question as vested interests hold immense political clout and swaying power.

We need an agile and smart state that, without unlimited resources, should do more by putting in place policies to get more people out of dependence on social security, to restore dignity for each person and the feeling that he or she is an active player of society, not abandoned by it. There is a need for a pragmatic approach to public policies, for accountability, for rediscovering the middle ground represented by 'community' and 'reciprocity' (mutual rights and obligations), for belonging to more than oneself, loyalty, dignity, respect, moral values in general[20]. It is not simple, yet we need to find the right path and avoid further setbacks.

The world is changing, capitalism is in the throes of major changes by the force of events, and public policies are being adjusted along the road, frequently erratically. We will likely go through a transition period, an inter-regnum with a lot of mayhem

[18] See also Jean Pisani Ferry, 2020.
[19] Mariana Mazucatto argues that we need 'entrepreneurial states' (2013, 2020).
[20] See also Paul Collier, Raghuram Rajan (2020), Jean Tirole, Samuel Bowles, Paul Mason, Martin Sandbu.

and mushrooming tensions – with global governance rules being eroded markedly, with survival of the fittest -type reactions. But capitalism will quite likely change. Academic textbooks will in time capture these developments. Agustín Carstens noted that textbooks had become obsolete when examining macroeconomic policy in emerging economies (2019). The same may hold true, on a much larger scale, for the interpretation of the path of capitalism in the years to come. It is difficult to make predictions in light of extraordinary uncertainties[21]. But avenues of change are looming at the horizon.

5. Which way should capitalism turn?

Challenges for capitalism originate not only in the idiosyncratic inclinations of some leaders and in vested interests, in the sheer struggle for power and geopolitical rivalries; they have deeper roots such as: unrestrained globalisation and *market fundamentalism*, neglect of social aspects (exclusion and lack of fairness), market abuse perpetrated by large players (firms) including massive tax dodging, the lack of proper regulations, disregard of the impact of climate change, inability to reform the EU more substantially[22] etc.

There are stark facts and dynamics underway that will quite likely define capitalism in the years to come, such as:

- governments will be more present in economic life for the sake of providing more public goods; *state presence* is to be seen in conjunction with the need to deal with climate change and pandemics (public health becomes a national security concern).
- industrial policies will be on the rise. In the EU, industrial policies are epitomized by The Plan for Recovery and Resilience, which aims at fostering the 'greening' and digitization of economies;
- tax regimes will likely be revisited to make them more fair. The US Treasury support for a worldwide minimum profit tax rate on international companies is a move in the right direction. It is something the OECD has pleaded for years in order to stop "the race to the bottom", the erosion of the tax base. Together with regulations and public investment, tax policy would have to "incentivise technology to support labour rather than supplant it", as the former governor of the Bank of England, Mark Carney, argues (2021)
- inclusion and fairness will acquire more prominence in public policies
- critical mass of solidarity is crucial at both community/national and international levels in order to cope with common challenges.

As to concrete features of future capitalism it pays to point out some relevant issues.

Is there an ideal model?

The Nordic (Scandinavian) model is eye-catching. This model relies on a very high level of economic and social development, with massive redistribution of resources. The Nordic countries also went through episodes of national crises: Sweden a few decades ago, Finland after the collapse of the Soviet system owing to its high reliance on Eastern markets, then on Nokia. But there were timely responses and clever reform measures, a

[21] What Mervyn King calls 'radical uncertainty' (2016).

[22] In spite of recommendations made by various reports over the years (see The Sapir and the Monti reports, which were preceded by the MacDougall Report).

high degree of adaptability. The Nordic countries (including the Baltic States) are models of excellence in educational systems and innovation. Nordic societies reveal a lot of modesty in politicians' conduct and less corruption as against other societies. But this model is not immune to social tensions, to difficulties in integrating immigrants.

Germany has, besides features of the Nordic model, an impressive industrial and manufacturing power. But there is also fallibility and there are blatant cases of corporate misconduct (Wirecard, the Volkswagen carbon emissions scandal, etc.).The South of the EU is different in many ways, sometimes it seems entrenched in inertial and sclerotic structures, though economic progress has been made over the years.

An EU model?

There is an all-encompassing model epitomized by EU's principles and values, and which is embraced by the political families that are imbued with the liberal spirit in its deepest meaning. From this perspective, Christian Democrats/People's Parties, Social Democrats, The Greens, the parties grouped in the *New Europe* family in the European Parliament, conservatives who accept the checks and balances mechanism and fundamental freedoms, belong to an enlarged political family that supports liberal democracy. But this all-encompassing model has weaknesses that derive from the incompleteness of the EU, of the euro area, and the neo-liberalism that underpins, to a large extent, the Single Market.

The European (EU) model faces big challenges that are reflected by illiberal propensities, by the rise of extremist groups and the assault of demagogues and populists, the crisis of 'social paternalism' and spreading cynicism. How to reform its functioning, how to deal with economic divergence in the euro area, are formidable challenges for European leaders.

Issuing collective bonds in order to fund the Recovery and Resilience plan of 750 Billion euros is a major step forward (some call it a *Hamiltonian moment*), and the ECB proposal to make it permanent has a deeper meaning – as the euro area badly needs a *safe asset* (the euro area needs risk sharing mechanisms, which involve adequate fiscal arrangements).

Markets, States, Community

The debate should be about the form of capitalism, whether markets can be reined in so that inclusion and fairness, income distribution, be met as policy objectives. Mark Carney, Branko Milanovici, Paul Mason, Mariana Mazzucato, Minousche Shafik, Fareed Zakaria, and others are pointing the finger at the need to revamp capitalism, as do Raghuram Rajan, Paul Collier and Martin Sandbu do when they emphasize the need to rediscover the middle ground, *the community*, society, as a matter of fact, as Karl Polanyi would say. Samuel Bowles touches a relevant chord when he says that not only incentives are needed to shape individuals' conduct, that society needs 'good citizens'. This brings us to the issue of ethical conduct, be it in the corporate world or among people at large. This is an issue that Adam Smith pointed out in 'The Theory of Moral Sentiments' and closer to our days, the Nobel laureates Kenneth Arrow and Amartya Sen strongly stress.

Dealing with companies that abuse markets and society

Industries have to be properly regulated and undue rents need to be downsized, if not eliminated. Massive tax evasion and avoidance is a scourge of our times, especially since public budgets are under so much strain and income distribution has gotten so skewed. Tax regimes have to be fair; tax havens should be wound down. A carbon tax is needed both internationally and nationally, as are digital taxes on giant companies (the tech companies) that pay almost nothing in numerous countries where they operate. Conditioning bail-outs on higher future taxes does make sense as the obnoxious cycle of privatizing social benefits and socializing private losses has to be stopped; equity may be taken in companies that are rescued during the current crisis[23].

Finance

Finance needs to continue to reform itself. Banks are larger now and their revenues (that include the pay of management and staff) continue to be disproportionately large. That their net profits are diminished by ECB's QE is a different matter for discussion. Finance will have to change not least because of new technologies, of digitalization. Banks feel the pinch of shadow banking, while capital markets, too, are under the impact of new technologies.

The regulation and supervision of finance will have to consider new systemic risks, those that come from capital markets and the advent of digital currencies. One way or another, financial services will have to cater more to the needs of the real economy.

Central banks consider climate change as an increasing systemic risk and income distribution is also on their radars. To what extent that fits into the traditional mandate of central banks is heavily debated. But there are strong arguments that push central banks to change their policy frameworks.

The social responsibility of the corporate world

When it comes to the corporate world, it has a long way to go to ditch its seemingly still prevailing philosophy: that economic logic is amoral. The shareholder vs. stakeholder distinction should not be a formal one, and what is called *corporate social responsibility* should not be empty rhetoric, a mere object of study in business schools. The American Business Roundtable, that groups some of the largest US firms, has spoken about the need to consider all stakeholders in their operations (in a statement of August 2019). How much this is a candid acknowledgement of the distance between what Big Business claims and what it practices remains to be seen.

Big Pharma needs to be restrained with the prices they charge, not only on moral grounds, but also in view of the funding they get from governments (during the current Pandemic too)– a point strongly made by Mariana Mazzucato (2020).

The threat of climate change may speed up a transformational attitude, as people would be more picky in their preferences. As central banks become so serious about climate change, companies need to heed to it too; if they do not, not a few of them will perish.

Income distribution and fairness

The Brexit and the Trump phenomena in the United States stemmed also from a 'reality denial' of many political leaders. *The Third Way* promoted by Bill Clinton, Tony Blair and Gerhard Schröder, etc, with Anthony Giddens (1998) as the academic guru, was not the way out of the woods. You do not have to share Thomas Piketty, Emmanuel Saez, Gabriel Zucman and others' outlook to see that there is something valid in what they say

[23] See also Mariana Mazzucato (2020).

concerning income distribution and fairness. The increasing attention central banks and IFIs give to income distribution is more than relevant in this regard[24]. But an additional issue is to be highlighted here: “how to design the rules of the market so that the economy generates what most people consider a fair distribution on its own” (Robert Reich, p. 219).

An increasing social problematique; the role of education

A big question is how to stop the jobless from growing in number. Even if a guaranteed minimum income would, supposedly, eliminate the spectre of social riots. Not incidentally, inclusion is a key concept, which is underscored by international financial institutions as well. Education systems are key in this regard. And better public education is a must; for only good private education and healthcare arrangements would deepen social and political fractures. Social and economic dynamics will be more tense if the middle class is increasingly eroded, if new technologies displace large groups of people from the labour market.

An entire society cannot turn into a Silicon Valley. A ‘start-up nation’ is an exciting catchword and one might say that Israel, for instance, would come close to something like this in an inspirational manner (because this country has a density of mathematicians, physicists, engineers hardly seen in the rest of the world). However, it is difficult for economies, societies, to turn into ‘scientific-technological complexes’ (to paraphrase Dwight Eisenhower’s ‘military-industrial complex’ famous formulation); I do not even think this is possible. But it takes sweeping changes in educational systems to provide equal opportunities to the youth, to all citizens.

Public debts and fiscal sustainability

There is also the issue of mounting public debt (massively fuelled by the pandemic-induced economic crisis), of burdening the future generations, which can turn into a clash between generations, with political implications and an impact on public policies. Taxation of property and wealth, as advocated by some economists, may be seen from this perspective, of dwindling chances for many youngsters to have the well-being their parents enjoyed. Climate change adds further anxiety and potential burdens to public budgets and is likely to become the biggest threat to debt sustainability over the longer run.

Public health and education as national security concerns

Public health and education are turning into big national security concerns, calling for higher budgetary resources. Governments all over the world are concerned about finding budgetary resources to deal with present and future challenges. Strategic thinking will be subject to reassessment from this perspective.

Global commons are needed

Global issues should not be underplayed. Not only because there is a geopolitical competition for resources and supremacy, but also because we all face the same global challenges, among which climate change is paramount; other challenges include large disparities in economic and social development around the world, fighting pandemics,

[24] Noticeably, a IMF working paper submits a changed Taylor rule that would include the level of wages among its parameters (Niels Jakob Hansen and Rui Mano, 2020).

cyber threats, averting nuclear disasters. However intense geopolitical rivalries may be, a certain degree of cooperation is badly needed among the main global actors.

Climate change and democracy

How we deal with climate change conditions the future of democracy. For people need basic food and water for their survival. Thousands of years, even hundreds of years ago, the struggle to have basic food available was the paramount worry of most people. Conflicts and wars, small and big, were waged in order to secure life essentials. This is reciprocated in modern times by conflicts and wars for the control of strategic resources as levers of power and economic wellbeing; geopolitics boils down to it ultimately. Among such resources, oil and gas are, ironically, at the roots of our existential conundrum nowadays.

In this context, redefining the GDP (Gross Domestic Product), which includes negative externalities, is also needed. As a matter of fact, GDP, the way it is computed now, can grow while GDW (Gross Domestic Wellbeing) can go down. One needs to rethink economic growth in terms of human and ecological concerns and change its logic. Financial institutions, rating agencies also need to change their performance assessments of countries and companies.

Rediscovering Truth is a must as is the belief in Science

We need to rediscover Truth in our lives, to fight fake news, mass manipulation. We need also to believe in Science; the discovery of vaccines to combat the current Pandemic is more than telling in this respect. Sliding towards an area of debate and battle for power where moral milestones are lost, where truth is perverted by replacing facts with fiction, undermines democracy in the end. Truth is indispensable to democracy, and the tendency to distort, to pervert it, should worry us to the highest degree.

Strategic alliances are needed between those who believe in moral values and what a society can offer, combining economic freedom with the need for public goods, with empathy, compassion, solidarity. Just as markets alone cannot solve the problems of society, an omnipotent state, with an overwhelming public sector, is not the solution for the ills of society.

Final remarks

An in-depth discussion on what the future holds for our societies should not be about capitalism vs. socialism. For this counter-position is a hyper-simplification. The discussion should be about the path of capitalism, of the mixed economy, of democracy, and how we can tackle climate change as an existential threat as well as other big challenges – like pandemics. When to comes to democracy, the crux of the matter is whether the separation of powers, checks and balances, do function properly (see also Levitsky and Ziblatt) in order to avoid the encroachment on power by foes, disguised or not, of democracy. It boils down also to the issue of who shapes the rules and regulations in a market economy, whether these arrangements are fair and serve the majority of citizens.

The avenues to explore in rethinking capitalism would have to combine the virtues of economic freedom, of entrepreneurship with the need to nurture social cohesion and fairness, the *social capital* of society, human being's longing as a social being, as a member of a community (to distinguish it from *collectivism*). An increasing number of social scientists rightly emphasize[25] the need to partake in the community, the social sphere, the civic values, that we need open mindedness, pragmatism in public policies, a rejection of policy fundamentalism. As Yascha Mounk insightfully says, unrestrained markets (market fundamentalism) can bring about their own version of an illiberal society (undemocratic liberalism) –when many people feel that they lose any control on their fate.

The stakes are much higher than a simple battle between political families, political philosophies and schools of thought; it is about the fate of democracy, because, if the number of losers in economic competition is ever higher, extremist groups will gain the upper hand in politics. Rearing its ugly head is the spectre of authoritarianism, of illiberal capitalism. Climate change, unless properly tackled and with an ensuing struggle for basic scarce resources (food and water) would bolster illiberal inclinations.

If we are not lucid, mindful of menacing in-depth trends, if we do not change public policies so that our societies become more fair, skies will fall down upon us, overwhelm us. Xenophobia, chauvinism, growing racism will enhance authoritarian, illiberal tendencies, fuelled by social and political anger, as well as by violence. A "coming anarchy", to paraphrase Robert Kaplan (2000), would not leave the wealthy West untouched. The great, historical stake is, therefore, to save liberalism in its deep sense (which defines democratic parties alike, left and right of the political scene), liberal democracy, checks and balances, human dignity, the rule of law, the belief that good ultimately prevails, that human ingenuity can be guided towards noble ends and save us all, both individuals and the society as a whole.

The assertion that the debate on the future of capitalism is how to save democracy in no way diminishes the overriding challenge of dealing with climate change as an existential threat, as well as preparing us all better to tackle future pandemics and other big challenges. When it comes to global commons, geopolitical rivals need to cooperate, one way or another (see also Richard Haass and Charles Kupchan, 2021).

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[25] Raghuram Rajan says that "if we want to save the state and markets we need to rediscover communities" (2020).

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