After privatised Keynesianism*

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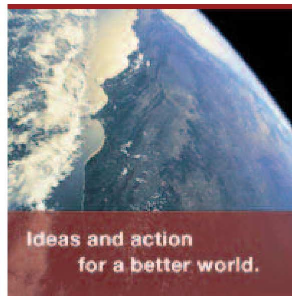

After privatised Keynesianism*

Colin Crouch

Both its supporters and its opponents are proclaiming that we are 'going back to Keynesianism' as the UK government turns to major public borrowing on spending on infrastructure projects to try to prevent the looming recession turning into a slump. But history never turns 'back'; ideas might exist in a timeless world, but the social forces that move them usually change irreversibly.

To consider the likelihood of an enduring return to Keynesian policies requires consideration of the interests that are in a position to move and shake the times. Also, if we seem on the threshold of a major shift in public policy paradigms, we need clearly to understand the nature of the one from which we may be shifting. It is commonly described, again by its supporters and opponents alike, as neo-liberalism. The financial crisis that has brought it to its knees reveals however that it has really been something rather different, and which can best be termed 'privatised Keynesianism'.

Under original Keynesianism it was governments that took on debt to stimulate the economy. Under the privatised form individuals, particularly poor ones, took on that role by incurring debt on the market. The main motors were the near-constant rise in the value of owner-occupied houses and apartments alongside an extraordinary growth in markets in risk. This regime collapsed, partly during a repetition of energy and other commodity inflation, but largely because of certain internal contradictions. Both regimes tried to manage two important tensions produced by the insecurity and uncertainty in ordinary people's lives that capitalist markets create as they adapt to shocks. The first is with the need for democratic politics to respond to citizens' demands for security and predictability in their lives. The second is with advanced capitalism's own needs for mass consumers on whose confidence firms can depend when planning their production.

The first answer to the second tension came in the early 20th century from the mass production system of manufacture associated initially with the Ford Motor Company in the USA. Technology and work organisation could enhance the productivity of low-skilled workers, enabling goods to be produced more cheaply and workers' wages to rise, so that they could afford more of the goods. The mass consumer became a reality. However, as the Wall Street crash of 1929, coming just a few years after the launch of the Fordist model, showed, the problem of reconciling the instability of the market with consumer-voters' need for stability remained unresolved.

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This is where what became known as the Keynesian model, introduced in Scandinavia in the 1930s, and in the UK and some other countries after World war II, played its part. In times of recession, when confidence was low, governments would go into debt in order to stimulate the economy with their own spending. In times of inflation, when demand was excessive, they would reduce their spending, pay off their debts, and reduce aggregate demand. The model implied large state budgets, to ensure that changes within them would have an adequate macro-economic effect. This required the social spending of the new, growing welfare state.

Working people were at last protected from major fluctuations of the market, enabling them gradually to become confident mass consumers of the products of a therefore confident mass production industry. Unemployment was reduced to very low levels. The welfare state not only provided instruments of demand management for governments, but also brought real services in areas of major importance to people outside the framework of the market: more stability. Arms-length demand management plus the welfare state protected the rest of the capitalist economy from both major shocks to confidence and attacks from hostile forces. It was a true social compromise.

Karl Marx famously wrote that at particular moments of historical crisis particular social classes were in a position where their particular interests coincided with the general interest of society. Such classes triumphed in the revolutions in which the crises ended. Marx's error was to believe that when the class concerned became the international proletariat there would be an end to the process, because the proletariat was the generality of society and not just a particular interest within it. But the Keynesian model did represent a temporary coincidence between the interests of the industrial working class in the global north-west and a general interest of the politico-economic system. This was the class likely to threaten political and social order. It was also potentially the class whose mass consumption, if facilitated and made secure, could fuel economic growth of a kind unprecedented in human history. It had also produced political parties, trade unions and other organisations, as well as associated intellectuals, to shape and press its demands.

Conservative critics had warned that it would prove easier to increase public spending in recessions than to reduce it in

periods of expansion, imparting an inflationary ratchet effect to the model. This became clear during the inflationary shocks unleashed by the general rise in commodity prices during the 1970s, particularly the oil price rises of 1973 and 1978. Belief in the Keynesian approach was virtually destroyed.

Privatised Keynesianism

An intellectual challenge to Keynesianism had long been ready. The advocates of a return to 'real' markets required an historical moment to justify the paradigm shift. The 1970s inflationary crisis provided this. Within a decade or so such ideas as the absolute priority of near-zero inflation at whatever cost in terms of unemployment, the withdrawal of state assistance to firms and industries in difficulties, the priority of competition, the predominance of a shareholder maximisation as opposed to a multiple stakeholder model of the corporation, the deregulation of markets and the liberalisation of global capital flows had become orthodoxy.

A further change that had taken place was the declining autonomy of the nation state. The post-war political economy had been founded on the basis of governments that could exercise considerable discretion in how they managed their economies. By the 1980s globalisation, both a producer and a product of the deregulation of financial markets, had eroded much of that autonomy. The only actors capable of rapid action at global level were transnational corporations, who preferred their own private regulation over that by governments. This both advanced and even rendered necessary the new model. Just as a class can be seen as the bearer of Keynesianism, so we can identify a class whose particular interests seemed to embody the general interest in the new model: the class of finance capitalists, geographically grounded in the USA and the UK but extending across the globe. If the world was to gain from the liberation of productive forces and enterprise that the spread of free markets would bring, the class of those who dealt in the unregulated finance that massaged and helped those markets to grow would benefit particularly. Whereas the tight labour markets and regulated capitalism of the Keynesian period had seen a gradual reduction in inequalities of wealth in all advanced countries, the following period was to see a sharp reversal of these trends, with extraordinary rewards (at least in the western world) going to those working in and owning financial institutions.

Meanwhile the class of Keynesianism, the manual working class of manufacturing industry, was declining in size as a result of rising productivity and the globalisation of production. Workers in the main growth sectors of the new economy, private services, were usually not organised and had developed no autonomous political agenda, no organisations to articulate their specific grievances. In the regime of largely unregulated international finance that was instituted during the 1980s, governments were far more worried about capital movements than labour movements: positively, in that they wanted to attract investment from free-floating capital with short time horizons; negatively in that they feared that such capital would move away if they did not provide conditions in which it was happy.

But the need among capitalists themselves for stable mass consumption in domestic markets, as well as workers' political demands for stable lives, remained. In the advanced economies this dependence intensified rather than weakened. As the industries making many of the products bought in mass markets moved to new producing countries, or, if it remained became dependent on less and less labour, employment growth depended on markets in personally delivered services, which are not so subject to globalisation. So the puzzle remains: if the instability of free markets had to be overcome to usher in the mass consumption economy, how did the latter survive the return of the former?

During the 1980s and early 1990s the answer appeared to be that it would not, as rising unemployment and continuing recession became the dominant experience. Then things changed. By the end of the 20th century the UK and the US in particular were demonstrating declining unemployment and strong growth. Did neo-liberalism finally deliver the perfect market economy?

No. As we now know, two things came together to rescue the neo-liberal model from the instability that would otherwise have been its fate: the growth of credit markets for poor and middle-income people, and of derivatives and futures markets among the very wealthy. This combination produced a model of privatised Keynesianism that occurred initially by chance, but which gradually became a matter for public policy so important as to threaten the entire neo-liberal project itself. Instead of governments taking on debt to stimulate the economy, individuals did so. In addition to the housing market there was an extraordinary growth in opportunities for bank loans and credit card debt.

This explains the great puzzle of the period: how did moderately paid American workers, who have little legal security against instant dismissal from their jobs, and salaries that might remain static for several years, maintain consumer confidence, when European workers with more or less secure jobs and annually rising incomes were bringing their economies to a halt by their unwillingness to spend? Europeans were told by experts that the answer to their economic problems lay in producing more and more labour insecurity and cutting back on their welfare states. They eventually obeyed, but found few positive results. No-one told them that these insecure workers would need to be enabled to take on unsecured debt in order to sustain consumer confidence. The growth in private personal services that powered the Anglo-American growth engine was therefore far slower.

In Anglo-America the anti-inflation bias of public policy further encouraged the model. Anti-inflationary policy bears down on the prices of goods and services that lose their value as they are consumed. Producers of food, material goods and services like restaurants or health centres confront an environment hostile to rises in their prices. This is not the case with assets, things that do not lose their value in this ways: real property, financial holdings, some art objects. A rise in their price is simultaneously a rise in their value, and does not contribute to inflation. Therefore assets, and earnings based on assets, have not been the objects of neo-liberal counter-inflation policy. Anything that could be switched from prices and wages derived from the sale of normal goods and services to an asset base therefore did very well. This applied to proportions of salaries paid as share options and to spending funded by extended mortgages rather than by rises in salaries and wages. The dependence of the capitalist system on rising wages, a welfare state and government demand management that had seemed essential for mass consumer confidence in the second half of the 20th century, had been abolished.

Eventually governments began to incorporate privatised Keynesianism into their public policy thinking, though the phrase did not occur to them. There had been an initial implicit public policy boost to the model back in the 1980s when the privatisation of council housing enabled large numbers of people on moderate incomes to take on mortgages and, later, to explore the scope for extended mortgages. But it gradually became clear that government was expected to act through fiscal or other means to ensure that the prices of houses and flats kept rising, until the massive interventions into housing finance and the banking sector in general during 2007 and 2008.
Most of this debt was necessarily unsecured; that was the only way in which privatised Keynesianism could have the same counter-cyclical stimulant effect as the original variety. Prudential borrowing against specified collateral certainly would not have helped the moderate-income groups who had to keep spending despite the insecurity of their labour market positions. The possibility of prolonged, widespread unsecured debt was in turn made possible through innovations that had taken place in financial markets, innovations which for a long time had seemed to be an excellent example of how, left to themselves, market actors hit on creative solutions. Through markets in derivatives and futures the great Anglo-American finance houses learned how to trade in risk. They found they could buy and sell risky holdings provided only that purchasers were confident that they could find further purchasers in turn; and that depended on the same confidence. Provided markets were free from regulation and capable of extensive reach, these trades enabled a very widespread sharing of risk, which made it possible for people to invest in many ventures that would otherwise have seemed unwise.

The fall of privatised Keynesianism

However, while all theories of market economics depend on the assumption that market actors are perfectly informed, privatised Keynesianism depended on what were presumed to be the very smartest actors concerned, the financial institutions, having highly defective knowledge. This is the Achilles' heel of this model, corresponding to the inflationary ratchet of original Keynesianism. Banks and other financial operators believed that each other had studied and calculated the risks in which they were trading. But during autumn 2008 it became clear that had they done so they would not have entered into many of the transactions they undertook. The only calculations made were that there was a good chance that someone else would buy a share in the risk. Bad debts were funding bad debts, and so on in an exponentially growing mountain.

Some people became extremely wealthy in the process, but they continued to be the class whose particular interests represented the general interest, because we all benefited from the growing purchasing power that this system generated. Once privatised Keynesianism had become a model of general economic importance, it became a curious kind of collective good. Given that necessary to it, powering it, was irresponsible behaviour by banks in failing to examine their asset bundles, that very irresponsibility became a collective good. This in itself explains why governments had to bail out the firms involved, nationalising privatised Keynesianism.

And so a second regime to reconcile stable mass consumption with the market economy ended. Both Keynesianism and its privatised mutant lasted 30 years. As regimes in a rapidly changing world go, that is probably as good as it can get. But the question arises: how are capitalism and democracy to be reconciled now? Also, how will the enormous moral hazard established by governments' recognition of financial irresponsibility as a collective good now be managed? The public policy response has not been 'now stop all this', but 'please carry on borrowing and lending, but a little bit more carefully'. It has to be so; otherwise there will be a danger of real systemic collapse.

Options after the fall

As ever, one can see right, left and a 'third way' political response. One can see elements of the first emerging from Conservative commentators and some emerging Conservative party stances. Hard times are coming, so we must maximise money in people's pockets. This means lower taxes, less welfare, fewer employment and social rights, an end to long-term concerns like the environment and climate change. This would mark a return to original Thatcherism. It is unlikely to be at the forefront of public presentation by a party that has seen its electoral fortunes recover as it is believed to have jettisoned that kind of politics. It is however likely to figure in the post-election approach of a new Conservative government. Since it would require a rejection of any return to Keynesianism, it would have little choice but to depend on a resurgence of irresponsible private

Keynesianism to solve the puzzle of reconciling neo-liberalism with consumer confidence. These possibilities make the prospects of a return of a Conservative government even more depressing than they were already.

For the centre left (I do not discuss the hard left, as this remains a broken force) there are in principle many opportunities. Neo-liberalism, held out to us as a triumphant opponent for a quarter of a century, has been shown to have depended on a thoroughly flawed and indefensible financial system. This has implications across all policy fields, not just macro-economic policy itself. Privatisation, marketisation, public-private finance initiatives, the imposition of new public management, have all been premised on the superior performance of the private sector, of which the great Anglo-American financial institutions were seen as the quintessential and supremely successful examples. Even the use of school league tables based on children's test performances were based on analogies of how share prices provided investors with straightforward quantitative indicators that ensured optimal decision-making.

It was coincidence that the government abolished one of the school SATS tests during the height of the financial crisis, but it need not have been, as SATS tests are part of that aping of markets. One used to complain about these market imitations that approaches could not be so easily transferred from one field to another. It is now clear however that the use of indicators had the same defect in its own heartland as in the hapless public services on whom it was imposed. When indicators become the basis of incentives, they replace, distort and become detached from the things they are supposed to measure. This is now seen to be as true of the performance of companies as it is of schools and hospitals.

This should therefore be a time when the storehouse of alternatives to, or intelligent adaptations of, markets that have been gathering in the publications of groups like Compass and in the practices of some of the smaller countries of western Europe, like Denmark and the Netherlands, stand a chance of being taken seriously. However, once again we search for the historical carrier, the class the imperatives of whose interests will drive a new agenda. But where do we find it. The new working classes of post-industrial society have still not developed an autonomous political voice. Sadly, a governing Labour Party has done nothing to help them develop one.

A remarkable feature of recent weeks has been the expression of real popular anger against the new super-rich, whether in the financial sector itself or among more publicly accessible groups like extravagantly paid footballers and media celebrities. But it has been the unfocussed, transitory anger of the kind shown by rick-burners and other discontented folk in the late 18th century. After 100 years of a Labour Party and a decade of continuous Labour government, popular discontent is back where it was a quarter of a millennium ago.

Will this now change? Current leading figures of the Labour Party are still burned with the experience of the extreme left of the early 1980s, and so seems to be the cadet generation that acquired its political learning at their metaphorical knees. Will this new generation, or an even younger one, now receive their own burning from the crisis of 2008, and can we ensure that even now they do not turn even further towards neo-liberalism? There must and will now be attempts to press these arguments within the party, but it is very risky for a party in government to risk courting new ideas and policy paths. The bearers of new thinking cannot show that they have a wider public support without being accused of causing disunity.

Efforts made within the party to take advantage of the changed situation will need support from ever more energy being poured into the social movements, cause groups and civil society activists that exist outside party nut which have been the bright spots on the depressing political scene of the past decade. Only they can try to create a public opinion that really challenges orthodoxies that continue to rule even while they are in decline.

A new third way?

But there is a third route out of the present crisis, which offers different nuances from adapted right or left strategies – which does not mean that I advocate it except with very mixed feelings; I suspect it will be found attractive by both labour and Conservative leaderships. Economic prosperity continues to depend on supplies of capital through efficient markets. The most likely new model is therefore one that works closely with the leading financial corporations.

There has always been a tension at the centre of neo-liberalism: is it about markets or about giant firms? They are far from being the same: the more that a sector is dominated by giant firms, the less it resembles the pure market that in principle lies behind nearly most of today's public policy. There may well be intense competition among giant firms, but it is not the competition of the pure market. The recent banking crisis has seen, on both sides of the Atlantic, governments supporting, and gaining the support of competition authorities for, mergers and acquisitions that considerably reduce competition and choice, strengthening the market dominance of the truly giant financial firms that are the toughened survivors of the crisis.

The financial markets failed when the fundamental criterion of complete knowledge and transparency ceased to characterise banks' relations with each other. If we now add to that a sector with considerably reduced competition, as well as extended guarantees of support from the state in the event of irresponsible behaviour, we have a potentially serious problem of system legitimacy. At the same time, we remain dependent on the financial system to resume privatised

Keynesianism if capitalism's need for confident consumers is to be fulfilled without a new form of 'real' Keynesianism. In the coming months we are likely initially to see a new burst of statutory regulation of this system, but there will soon be complaints from the sector that enterprise is being stifled. How can the derivatives markets get to work in supporting high levels of borrowing if they are to be subject to rules that make much of that borrowing more difficult? Low- and medium-wage, insecure workers will not be able to carry on spending unless they can get their hands on unsecured credit, even if at less maniac levels than had been occurring. One assumes that the government does not intend to hold on to the banks that it is nationalising; the fact that big banks operate internationally will itself be a disincentive to that. It is however also unlikely that these banks will be privatised through general public share issues. They will most likely be levered into the hands of a small number of leading existing firms deemed responsible enough to run them in good order.

For all these reasons there will gradually be a slip towards a more negotiated, voluntary regulatory system, managed by a small number of firms in close contact with government. To predict this is hardly crystal-ball gazing: it is a general trend in government-firm relations right across the economy. Sharing neo-liberal prejudices against government as such, frightened at the impact of regulation on growth, and believing in the superiority of corporate directors over themselves at nearly everything, politicians increasingly rely on corporate social responsibility for the achievement of several policy goals.

This will be the third way approach. It will be a system far less legitimated in terms of the market, freedom of choice and an absence of government involvement. Rather, there will be partnership between government and firms, or autonomous actions by firms commended by governments, with largely informal outcomes attempts to reconstruct trust. The firms will be the dominant partners, as the new model will be limited to nation-state (just possibly EU) level, to which level governments' competence is limited, while the firms remain global and retain a capacity to regime-shop.
Such a development strengthens even further the need for and the possibilities of current trends towards a displacement of political activity from parties to civil society organisations and social movements. The new model brings firms to prominence, not just as lobbies of governments, but as makers of public policy, either alongside or instead of governments. It will be firms that decide the terms of their codes of behaviour and responsible practices. Firms therefore become political subjects and objects in their own right, ending the sharp separation between governments and private firms that is the hallmark of both neo-liberal and social democratic politics. At the same time, as governments of all parties have to make similar deals with firms, and equally fear for their country's ability to attract liquid capital if they are too demanding of them, differences among parties on core economic policies will shrink even further than they have already.

It is already the case that for nearly every major corporation there is a web site revealing details of its conduct, assessing its fulfilment of its social responsibility claims. As this remains a no-go area for party conflict, it will grow in importance in civil society politics. It will have the major advantage that it will not be so trapped at the nation state level as party politics; many of these groups are transnational.

Against that, it is unable to co-ordinate and prioritise issues in the way that parties can. It also lacks the formal citizenship egalitarianism of electoral democracy, while retaining many of the bad habits of parties. Activist groups are capable of grabbing attention with exaggerated claims or (in contrast) cuddling up to corporations in exchange for various resources just as much as are parties. It will also be a highly unequal struggle between them and the corporations. It is not a regime that either neo-liberals or social democrats want; but it is what we are all likely to get; and it may well reconcile again the capitalism economy and the democratic polity.
Some will argue that the victory of Barack Obama in the US presidential elections has seen a rejuvenation of party politics for the centre left, and that we need worry less about the viability of social movement politics. But the new politics created around Obama is as much about movements and causes as about parties. In the US parties are in any case rarely adequate vehicles for causes unless these also have a separate organisational base, and the generation and social groups that Obama has inspired are predominantly active in that way. It is unlikely that all that activity will now disappear into the Democratic Party; it will retain its strong presence within civil society, pressing that party and being very concerned to stay close to it, but retaining a life outside it. It is to strengthening that kind of politics that we must now all look.

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> Compass is the democratic left pressure group, whose goal is to debate and develop the ideas for a more equal and democratic world, then campaign and organise to help ensure they become reality.

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