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NEOLIBERALISM

A Very Short Introduction

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Chapter 1
What's 'neo' about liberalism?

Liberalism old and new

Delivering his 2009 Inaugural Address in the throes of the worst economic crisis since the Great Depression of the 1930s, Barack Obama minced no words as he pointed his finger at what he considered to be the chief culprits of the global financial disaster: greed and irresponsibility on the part of some, and people's collective failure to make hard choices and prepare themselves for a new age. Expanding his argument, the youthful President insisted that the key question today was no longer whether government was too big or too small, but whether it worked. Then, looking straight into cameras that projected his stern image onto countless TV and computer screens around the world, the American leader took issue with the reigning economic paradigm of the last 30 years:

> Nor is the question before us whether the market is a force for good or ill. Its power to generate wealth and expand freedom is unmatched. But this crisis has reminded us that without a watchful eye, the market can spin out of control.

The reaction from news pundits was swift and unambiguous: Obama's address was a clear indication that the age of 'neoliberalism' might be coming to an end.

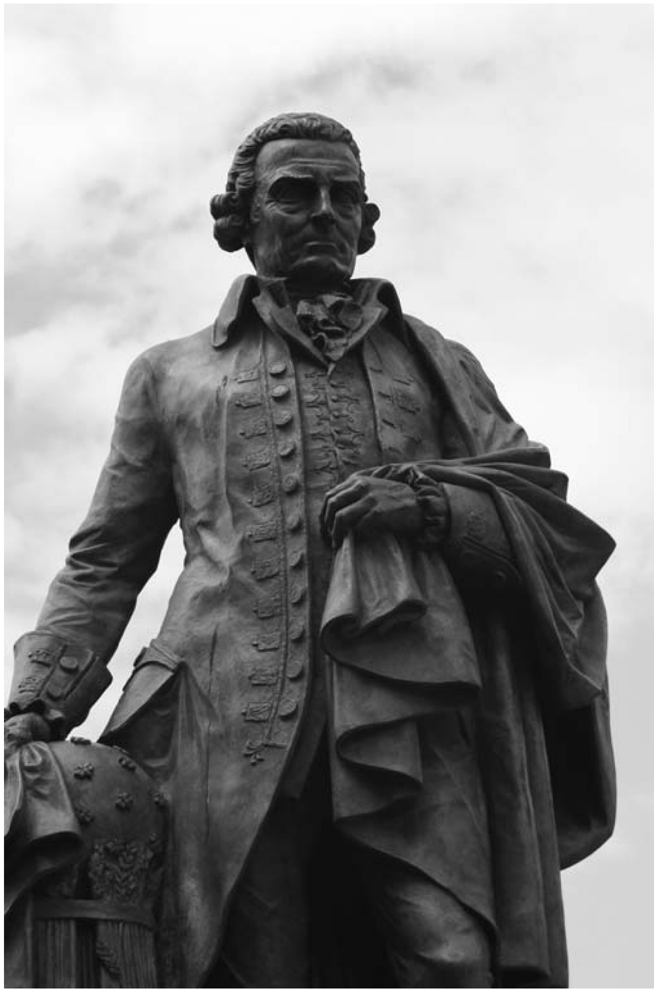
1. President Barack Obama delivering his 2009 Inaugural Address

To be sure, the object of the President's criticism – the neoliberal ideal of the 'self-regulating market' as the main engine powering the individual's rational pursuit of wealth – had been a core tenet of economists since the late 18th century. Opposed to the mercantilism of monarchs who exercised almost total control over the economy in their efforts to amass large quantities of gold for largely bellicose purposes, 'classical liberals' like Adam Smith and David Ricardo preached the virtues of the 'free market' and '*laissez-faire*' economics. Smith is credited with creating the Scottish Enlightenment image of *homo economicus* – the view that people are isolated individuals whose actions reflect mostly their material

self-interests. According to this view, economic and political matters are largely separable, with economics claiming a superior status because it operates best without government interference under a harmonious system of natural laws. Thus, the state is to refrain from 'interfering' with the economic activities of self-interested citizens and instead use its power to guarantee open economic exchange.

Ricardo's theory of 'comparative advantage' became the gospel of modern free traders. He argued that free trade amounted to a win–win situation for all trading partners involved, because it allowed each country to specialize in the production of those commodities for which it had a comparative advantage. For example, if Italy could produce wine more cheaply than England, and England could produce cloth more cheaply than Italy, then both countries would benefit from specialization and trade. In fact, Ricardo even went so far as to suggest that benefits from specialization and trade would accrue even if one country had an absolute advantage in producing all of the products traded. Politically, Ricardo's theory amounted to a powerful argument against government interference with trade and was used by 19th-century liberals like Richard Cobden as a formidable ideological weapon in the struggle to repeal the protectionist Corn Laws in England.

For classical liberals, producers were the servants of consumers who pursued their material needs and wants as they saw fit. Dedicated to the protection of private property and the legal enforcement of contracts, classical liberals argued that the 'invisible hand' of the market ensured the most efficient and effective allocation of resources while facilitating peaceful commercial intercourse among nations. Their ideas proved to be a potent force in fomenting the great 18th-century revolutions that toppled royal dynasties, separated church and state, and shattered the dogmas of mercantilism. For most of the 19th century, the heirs of classical liberalism sought to convince people that bad economic times always reflected some form of 'government failure' – usually too much state interference resulting in distorted price signals.



2. Adam Smith (1723–90)

Classical liberalism and the Enlightenment

Classical liberalism arose in tandem with the Enlightenment movement of the late 17th and the 18th centuries which proclaimed reason as the foundation of individual freedom. Enlightenment thinkers like John Locke (1632–1704) argued that in the 'state of nature', all men were free and equal, therefore possessing inalienable rights independent of the laws of any government or authority. Naturally endowed with the right to life, liberty, and property, humans could legitimately establish only *limited* governments whose chief task consisted of securing and protecting these individual rights, especially private property.

How could there be such a thing as 'market failure', they reasoned, if markets – properly shielded from the meddling state – were by nature incapable of 'failing'?

But the turbulent 20th century soon cast a dark cloud on these 'truths' of classical liberalism. It wasn't until the 1980s that 'neoliberals' managed to bring back some of these quaint ideas – albeit dressed in new garments. So what happened in the intervening period? The story is well known. The fury and longevity of the Great Depression convinced leading economic thinkers like John Maynard Keynes and Karl Polanyi that government was much more than a mere 'night watchman' – the role assigned to the state by classical liberals. At the same time, however, Keynes and his new breed of 'egalitarian liberals' disagreed with Marxists who saw the persistence of economic crises as evidence for the coming collapse of capitalism and the victory of a 'revolutionary proletariat' that had seen through the 'ideological distortions' of the 'ruling bourgeoisie': never again would workers fall into the clever trap of accepting their own exploitation in the name of high-sounding liberal ideals like 'freedom', 'opportunity', and 'hard work'. Seeking to prevent revolution by means of economic reform, egalitarian liberals like Prime Minister Clement Atlee and President Franklin D. Roosevelt remained staunch defenders of individual autonomy and property rights. And yet, they criticized classical liberalism for its inability to recognize that modern capitalism had to be subjected to certain regulations and controls by a strong secular state.

Keynes, in particular, advocated massive government spending in a time of economic crisis to create new jobs and lift consumer spending. Thus, he challenged classical liberal beliefs that the market mechanism would naturally correct itself in the event of an economic crisis and return to an equilibrium at full employment. Keynes linked unemployment to a shortage of private capital investment and spending in the economy. For this shortfall, he blamed short-sighted and avaricious investors, whose speculative investments had destabilized the market. Committed to the market principle but opposed to the 'free market', 'Keynesianism' even called for some state ownership of crucial national enterprises like railroads or energy companies.

Keynes led the British delegation at the 1944 Bretton Woods Conference in the United States, which established the post-war international economic order and its international economic institutions. The International Monetary Fund (IMF) was created to administer the international monetary system. The International Bank for Reconstruction and Development, later known as the World Bank, was initially designed to provide loans for Europe's postwar reconstruction. During the 1950s, however, its purpose was expanded to fund various industrial projects in developing countries around the world. Finally, the General Agreement on Tariffs and Trade (GATT) was established in 1947 as a global trade organization charged with fashioning and enforcing multilateral trade agreements. In 1995, the World Trade Organization (WTO) was founded as the successor organization to GATT and subsequently became the

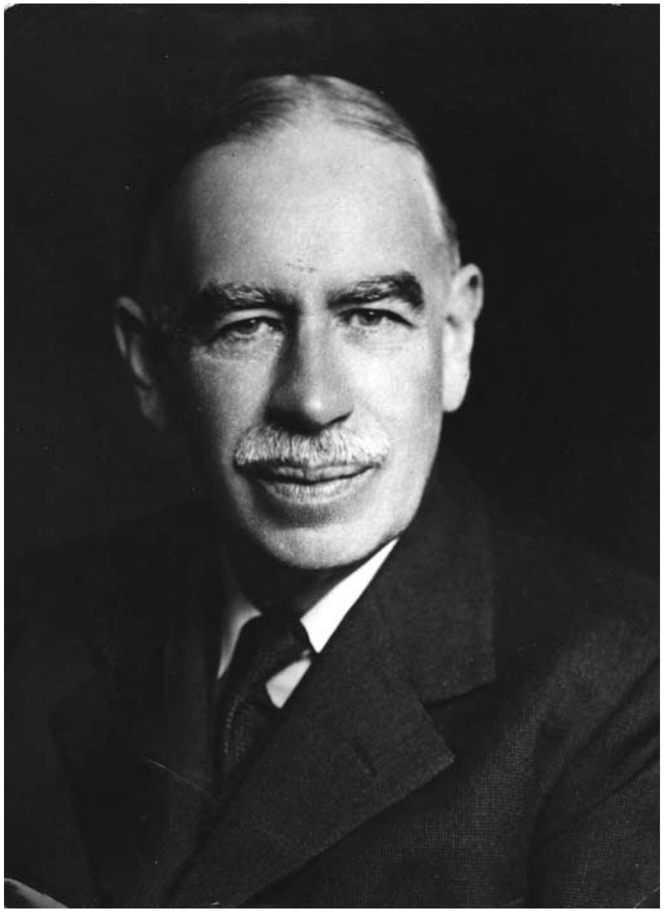
focal point of intense public controversy over its neoliberal design of free trade agreements.

The political applications of Keynesian ideas inspired what some economists called the 'golden age of controlled capitalism', which lasted roughly from 1945 to 1975. The American 'New Deal' and 'Great Society' programmes spearheaded by FDR and President Lyndon Johnson, the much admired model of Swedish social democracy, and the British version of 'welfarism' launched in 1945 reflected a broad political consensus among Western nations that led some pundits to proclaim the 'end of ideology'. National governments controlled money flows in and out of their territories. High taxation on wealthy individuals and profitable corporations led to the expansion of the welfare state. Rising wages and increased social services in the wealthy countries of the global North offered workers entry into the middle class.

The golden age of controlled capitalism in the United States

The economy was based on mass production. Mass production was profitable because a large middle class had enough money to purchase what could be mass produced. The middle class had the money because the profits from mass production were divided up between giant corporations and their suppliers, retailers, and employees. The bargaining power of this latter group was enhanced and enforced by government action. Almost a third of the workforce belonged to a union. Economic benefits were also spread across the nation – to farmers, veterans, smaller towns, and small business – through regulation (of railroads, telephones, utilities, and small business) and subsidy (price supports, highways, federal loans).

Source: Robert B. Reich, *Supercapitalism: The Transformation of Business, Democracy, and Everyday Life* (New York: Knopf, 2008), p. 17



3. **John Maynard Keynes (1883–1946)**

Even US President Richard Nixon, a conservative Republican, proclaimed as late as 1970 that 'we are all Keynesians now'. It was the Keynesian advocacy of an interventionist state and regulated markets that gave 'liberalism' its modern economic meaning: a doctrine favouring a large, active government, regulation of

Keynesian macroeconomics

John Maynard Keynes's literary masterpiece, *The General Theory of Employment, Interest and Money*, was published in 1936 at the height of the Great Depression. The book gained instant prominence because it successfully challenged classical liberal ideas about how modern economies worked. Keynesian ideas proved to be crucial in the development of the theoretical framework of 'macroeconomics'. This new field proclaimed that it was possible for national governments to aggregate data and predict economic crises in advance of their occurrence, thus proposing the use of various policies to intervene in and make adjustments to the economy. Specifically, governments were to increase public spending during economic recessions in order to spur growth, and reduce spending during periods of boom in order to keep inflation in check. Keynesian ideas dominated macroeconomics until the rise of neoliberal doctrines in the early 1970s.

industry, high taxes for the rich, and extensive social welfare programmes for all.

In the three decades following World War II, modern egalitarian liberalism delivered spectacular economic growth rates, high wages, low inflation, and unprecedented levels of material wellbeing and social security. But this golden age of controlled capitalism ground to a halt with the severe economic crises of the 1970s. In response to such unprecedented calamities as 'oil shocks' that quadrupled the price of petrol overnight, the simultaneous occurrence of runaway inflation and rising unemployment ('stagflation'), and falling corporate profits, an entirely new breed of liberals sought a way forward by reviving the old doctrine of classical liberalism under the novel conditions of globalization.

These 'neoliberals' subscribed to a common set of ideological and political principles dedicated to the worldwide spread of an economic model emphasizing free markets and free trade. And yet, they emphasized different parts of their theory according to their particular social contexts. Worshipped by their followers and detested by the Keynesians, neoliberals succeeded in the early 1980s in setting the world's economic and political agenda for the next quarter century. As we shall discuss in Chapters 2 and 3, they argued that crippling government regulation, exorbitant public spending, and high tariff barriers to international trade had been responsible for creating conditions that led to high inflation and poor economic growth throughout the industrial countries in the 1970s. Once this premise became widely accepted, it was the logical next step to claim that these factors remained the major impediment to successful economic development in the global South. Thus was born a global neoliberal development agenda based primarily on so-called 'structural adjustment programmes' and international free-trade agreements. As we shall see in Chapters 4 and 5, powerful economic institutions like the International Monetary Fund and the World Bank imposed their neoliberal agenda on heavily indebted developing countries in return for much-needed loans. The 1991 demise of the Soviet Union and the acceleration of market-oriented reforms in communist China led to the unprecedented dominance of the neoliberal model in the 1990s.

During the last decade, however, neoliberalism has come under a series of criticisms. The global economic crisis of 2008–9 is only the latest in a series of challenges to the still dominant free-market paradigm. But before we can appreciate the full magnitude of the threat facing neoliberalism, we must familiarize ourselves with its various dimensions, varieties, and policy applications. So let us commence our journey with a brief consideration of its core ideas and principles.

The three dimensions of neoliberalism

'Neoliberalism' is a rather broad and general concept referring to an economic model or 'paradigm' that rose to prominence in the 1980s. Built upon the classical liberal ideal of the self-regulating market, neoliberalism comes in several strands and variations. Perhaps the best way to conceptualize neoliberalism is to think of it as three intertwined manifestations: (1) an ideology; (2) a mode of governance; (3) a policy package. Let us carefully unpack these fundamental dimensions.

Ideologies are systems of widely shared ideas and patterned beliefs that are accepted as truth by significant groups in society. Such 'isms' serve as indispensable conceptual maps because they guide people through the complexity of their political worlds. They not only offer a more or less coherent picture of the world as it is, but also as it ought to be. In doing so, ideologies organize their core ideas into fairly simple truth-claims that encourage people to act in certain ways. These claims are assembled by codifiers of ideologies to legitimize certain political interests and to defend or challenge dominant power structures. The codifiers of neoliberalism are global power elites that include managers and executives of large transnational corporations, corporate lobbyists, influential journalists and public-relations specialists, intellectuals writing for a large public audience, celebrities and top entertainers, state bureaucrats, and politicians.

Serving as the chief advocates of neoliberalism, these individuals saturate the public discourse with idealized images of a consumerist, free-market world. Skilfully interacting with the media to sell their preferred version of a single global marketplace to the public, they portray globalizing markets in a positive light as an indispensable tool for the realization of a better world. Such market visions of globalization pervade public opinion and political choices in many parts of the world. Indeed, neoliberal decision-makers function as expert designers of an attractive ideological container for their market-friendly political agenda. Their ideological claims are laced with references to global economic interdependence rooted in the principles of free-market capitalism: global trade and financial markets, worldwide flows of goods, services, and labour, transnational corporations, offshore financial centres, and so on. For this reason, it makes sense to think of neoliberalism as a rather economistic ideology, which, not unlike its archrival Marxism, puts the production and exchange of material goods at the heart of the human experience.

The second dimension of neoliberalism refers to what the French social thinker Michel Foucault called 'governmentalities' – certain modes of governance based on particular premises, logics, and power relations. A neoliberal governmentality is rooted in entrepreneurial values such as competitiveness, self-interest, and decentralization. It celebrates individual empowerment and the devolution of central state power to smaller localized units. Such a neoliberal mode of governance adopts the self-regulating free market as *the* model for proper government. Rather than operating along more traditional lines of pursuing the public good (rather than profits) by enhancing civil society and social justice, neoliberals call for the employment of governmental technologies that are taken from the world of business and commerce: mandatory development of 'strategic plans' and 'risk-management' schemes oriented toward the creation of 'surpluses'; cost–benefit analyses and other efficiency calculations; the shrinking of political governance (so-called 'best-practice governance'); the setting of quantitative targets; the close monitoring of outcomes; the creation of highly individualized, performance-based work plans; and the introduction of 'rational choice' models that internalize and thus normalize market-oriented behaviour. Neoliberal modes of governance encourage the transformation of bureaucratic mentalities into entrepreneurial identities where government workers see themselves no longer as public servants and guardians of a qualitatively defined 'public good' but as self-interested actors

responsible to the market and contributing to the monetary success of slimmed-down state 'enterprises'.

In the early 1980s, a novel model of public administration known as 'new public management' took the world's state bureaucracies by storm. Operationalizing the neoliberal mode of governance for public servants, it redefined citizens as 'customers' or 'clients' and encouraged administrators to cultivate an 'entrepreneurial spirit'. If private enterprises must nurture innovation and enhance productivity in order to survive in the competitive marketplace, why shouldn't government workers embrace neoliberal ideals to

Neoliberalism as new public management: ten government objectives

1. Catalytic Government: Steering Rather than Rowing
2. Community-Owned Government: Empowering Rather than Serving
3. Competitive Government: Injecting Competition into Service
4. Mission-Driven Government: Transforming Rule-Driven Organizations
5. Results-Oriented Government: Funding Outcomes, Not Inputs
6. Customer-Driven Government: Meeting the Needs of the Customer, Not the Bureaucracy
7. Enterprising Government: Earning Rather than Spending
8. Anticipatory Government: Prevention Rather than Cure
9. Decentralized Government: From Hierarchy to Participation and Teamwork
10. Market-Oriented Government: Leveraging Change through the Market

Source: David Osborne and Ted Gaebler, *Reinventing Government* (1992), cited in Robert B. Denhardt, *Theories of Public Organization*, 5th edn. (Wadsworth, 2007), pp. 145–6 improve the public sector? Based on this neoliberal governmentality, US Vice-President Al Gore famously utilized new public management principles in the 1990s to subject various government agencies to a 'National Performance Review' whose declared objective was to cut 'government waste' and increase administrative efficiency, effectiveness, and accountability.

Third, neoliberalism manifests itself as a concrete set of public policies expressed in what we like to call the 'D-L-P Formula': (1) **d**eregulation (of the economy); (2) **l**iberalization (of trade and industry); and (3) **p**rivatization (of state-owned enterprises). Related policy measures include massive tax cuts (especially for businesses and high-income earners); reduction of social services and welfare programmes; replacing welfare with 'workfare'; use of interest rates by independent central banks to keep inflation in check (even at the risk of increasing unemployment); the downsizing of government; tax havens for domestic and foreign corporations willing to invest in designated economic zones; new commercial urban spaces shaped by market imperatives; anti-unionization drives in the name of enhancing productivity and 'labour flexibility'; removal of controls on global financial and trade flows; regional and global integration of national economies; and the creation of new political institutions, think tanks, and practices designed to reproduce the neoliberal paradigm. As we shall see in later chapters, so-called 'neoconservative' initiatives often supported the neoliberal policy agenda in pursuit of shared political objectives. In turn, many neoliberals embraced conservative values, especially 'family values', tough law enforcement, and a strong military. The nearly universal adoption of at least some parts of this policy package in the 1990s reflected the global power of the ideological claims of neoliberalism.

As we noted in the preface, the ensuing chapters of this book will pay special attention to the connection between the ideological and policy dimensions of neoliberalism by examining concrete policy applications in different settings around the world. But let us first complete our clarification of conceptual matters with a brief review

of the major economic theories that fuelled the rise of neoliberalism in the late 1970s.

The intellectual origins of neoliberalism

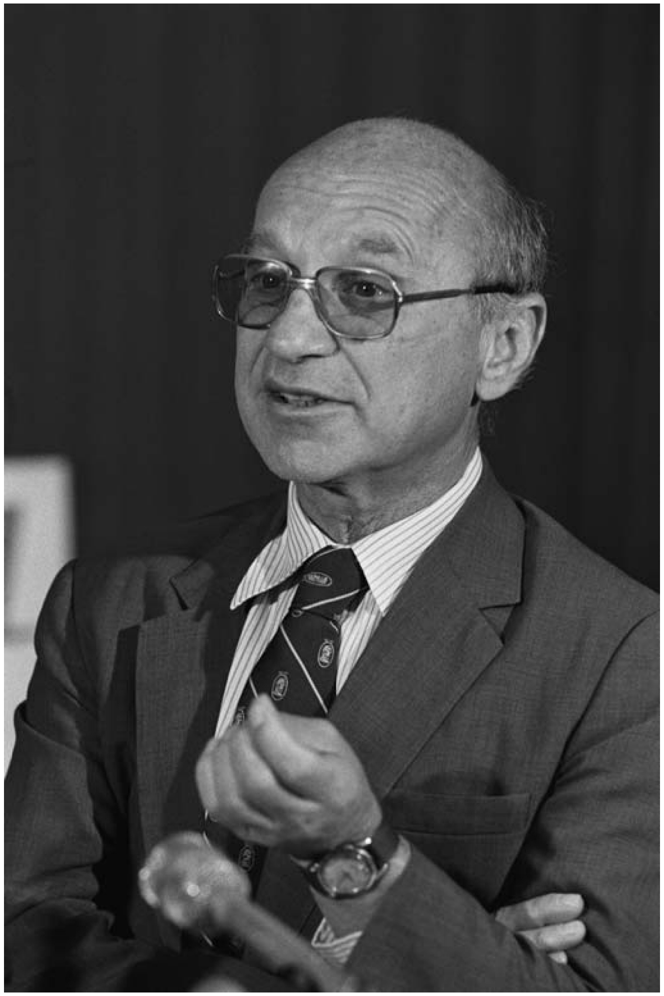
Although neoliberalism comes in several varieties, one can find the first systematic formulation of its economic principles in the Mont Pelerin Society. Founded in 1947 by Friedrich August von Hayek, an influential member of the early 20th-century Austrian School of Economics, the Society attracted like-minded intellectuals committed to strengthening the principles and practice of a 'free society' by studying the workings and virtues of market-oriented economic systems. Vowing to stem what they saw as the 'rising tide of collectivism' – be it Marxism or even less radical forms of state-centred planning – Hayek and his colleagues sought to revive classical liberalism in their attempt to challenge the dominance of Keynesian ideas. A great believer in the free market's spontaneous ability to function as a self-regulating and knowledge-generating engine of human freedom and ingenuity, Hayek considered most forms of state intervention in the economy as ominous milestones on the 'road to serfdom' leading to new forms of government-engineered despotism. His economic theory was anchored in the notion of 'undistorted price mechanisms' that were said to serve to share and synchronize local and personal knowledge, thus allowing individual members of society to achieve diverse ends without state interference. For Hayek, economic freedom could never be subordinated to political liberty and confined to the narrow sphere of material production. Rather, it was a profoundly political and moral force that shaped all other aspects of a free and open society. Surprisingly, however, the members of the Mont Pelerin Society occasionally strayed into conservative ideological territory by emphasizing the limits of human rationality and the importance of time-honoured values and traditions in the constitution of human societies.

4. **Friedrich August von Hayek (1899–1992)**

Libertarianism

Often associated with the economic doctrines of Friedrich von Hayek and Milton Friedman, libertarianism is a political creed hostile to government intervention. While sharing general agreement with mainstream liberalism on the primacy of individual liberty, most libertarians are strictly opposed to other liberal values such as equality, solidarity, and social responsibility. Rejecting modern governments as illegitimate for their use of 'coercive' policies, many libertarians subscribe to the utopian ideal of a loose 'society' of autonomous individuals engaged in strictly voluntary forms of exchange. Indeed, some libertarians go even so far as to demand the wholesale abolition of the state.

The neoliberal principles advocated by Hayek's Mont Pelerin Society greatly influenced the American economist Milton Friedman, winner of the 1976 Nobel Prize. The charismatic leader of the Chicago School of Economics (based at the University of Chicago), Friedman had an influential hand in guiding neoliberalism from constituting a mere minority view in the 1950s to becoming the ruling economic orthodoxy in the 1990s. Focusing on inflation as the most dangerous economic outcome of state interference – such as price controls imposed by Keynesian governments to guarantee low-income earners access to basic commodities – Friedman developed his theory of monetarism. It posited that only the self-regulating free market allowed for the right number of goods at correct prices produced by workers paid at wage levels determined by the free market. By the early 1980s, monetarists like Friedman insisted that slaying the dragon of inflation required that central banks like the US Federal Reserve pursue anti-inflationary policies that kept the supply and demand for money at equilibrium. In short, monetary policies should take precedence over fiscal policy (taxation and redistribution policies) devised by 'big government'.



5. **Milton Friedman (1912–2006)**

As we shall see in ensuing chapters, neoliberalism soon spread to other parts of the world – often by means of so-called 'shock therapies' devised by prominent neoliberal economists. Examples include Chile after General Augusto Pinochet's 1973 CIA-supported coup, the economic transformation of formerly communist Eastern Europe, and post-Apartheid South Africa. In some cases, domestic elites, educated in elite universities abroad, embraced neoliberalism enthusiastically. Others adopted it only grudgingly because they felt that they had no choice but to swallow the bitter pill of structural adjustment demands that inevitably accompanied much-needed IMF or World Bank loan offers. Although Chicago School economists like Friedman disliked the 1940s Keynesian regulatory framework under which the IMF

The Washington Consensus

The 'Washington Consensus' is often viewed as synonymous with 'neoliberalism'. Coined in the 1980s by the free-market economist John Williamson, the term refers to the 'lowest common denominator of policy advice' directed at mostly Latin American countries by the IMF, the World Bank, and other Washington-based international economic institutions and think tanks. In the 1990s, it became the global framework for 'proper' economic development. In exchange for much-needed loans and debt-restructuring schemes, governments in the global South were required to adhere to the Washington Consensus by following its ten-point programme:

1. A guarantee of fiscal discipline, and a curb to budget deficit
2. A reduction of public expenditure, particularly in the military and public administration
3. Tax reform, aiming at the creation of a system with a broad base and with effective enforcement
4. Financial liberalization, with interest rates determined by the market

5. Competitive exchange rates, to assist export-led growth
6. Trade liberalization, coupled with the abolition of import licensing and a reduction of tariffs
7. Promotion of foreign direct investment
8. Privatization of state enterprises, leading to efficient management and improved performance
9. Deregulation of the economy
10. Protection of property rights

and World Bank had originally been devised, their neoliberal ideological descendants in the 1990s managed to capture the upper echelons of power in these international economic institutions. With the support of the world's sole remaining superpower, they eagerly exported the 'Washington Consensus' to the rest of the world.

Let us now examine in more detail the concrete ideological and policy manifestations of neoliberalism across countries, regions, and regimes. Its various strands sometimes diverge on issues such as the precise role and appropriate size of government or take different positions on policy priorities and prescriptions. But most neoliberals share broadly similar ideological positions regarding the superiority of self-regulating market mechanisms over state intervention in producing sustained economic growth. They also agree on policies promoting individual entrepreneurial growth and productivity. Finally, they are united in their view that maintaining low levels of inflation is more important than achieving full employment. We begin our journey through the landscapes of neoliberalism by exploring two of its earliest and most spectacular strands: Reaganomics and Thatcherism.