



policy brief

What next for economic policy and the economy?

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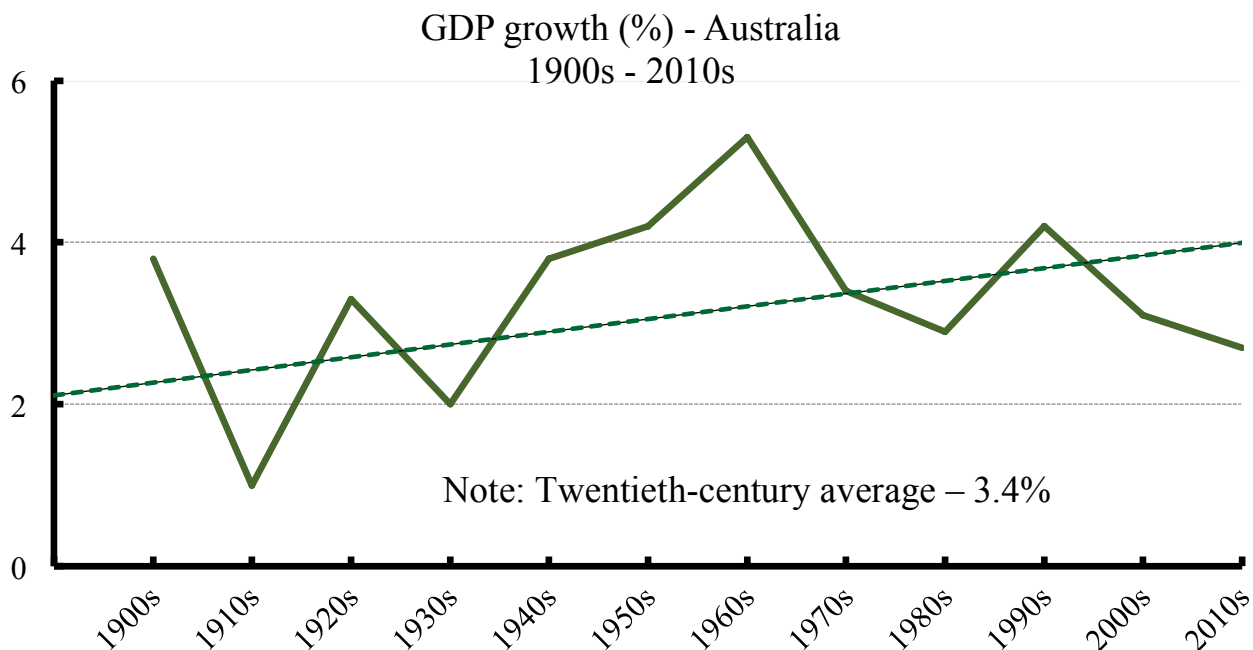
In this age of multiple political uncertainties, there are many tasks for social democrats wanting to reconstitute effective politics. One is to refute common errors about economic growth, unemployment, government spending and taxation. Though social democrats' expectations seem to be in retreat, their actual accomplishments are not – with welfare transfers, political capacities and the role of politics still showing signs of structural advance. Renewed interest in inequalities in wealth and income suggest, too, that political processes can still affect distributive outcomes. While neoliberalism has worsened social conditions in rich and poor countries, it has not produced a viable mode of economic development for the future.

The economics of political opportunities

Any Labor or social-democratic party, prior to formulating policy, needs to refute the fateful fallacies concerning economic growth, employment, taxes, budget deficits and debt that prevail in popular commentary. If uncorrected, these misperceptions rebound, to the detriment of us all. An indication of the discursive aspects of the tasks ahead can be gleaned from comparisons available in the latest *OECD Economic Outlook* (no.99, June 2016).

Contrary to conventional elite and journalistic opinion, economic growth is not and can never be a reliable indicator of success (nor its absence a sign of failure). And in itself, growth can never be

an honourable aspiration. Rich, mature and complex societies do not grow at the rates they once achieved and in fact often retain satisfactory (even enviable) living standards with quite low rates of increase in per capita GDP. Currently (2011-2016) all the wealthy societies experience growth rates below 3 per cent per annum – ranging from 2.6 per cent in Australia to negative rates for Italy and below 1 per cent for Japan, with the OECD average 1.8 per cent. Only in the ‘golden age’ of post-war reconstruction (1945-1974) did annual growth in the most-developed countries exceed 2 per cent (Maddison 2007, p.383). Australian growth has been unusual in recent times, with a 3.4 per cent average over the twentieth century (see chart). For the past two decades annual growth in the OECD has been well below 2 per cent for understandable reasons: no one expects high growth from a high base. Affluence can be achieved and maintained even with growth of less than 2 per cent a year; there is no imperative for rich countries to keep growing. (Even China’s growth rate which for the first decade of this century was over 10 per cent, has now declined to about 6 per cent, for reasons associated with its past success; it has become steadily wealthier.) Proper economic management should embrace these realities – that is, responsible affluence with distributive decency – rather than an unattainable growth chimera.

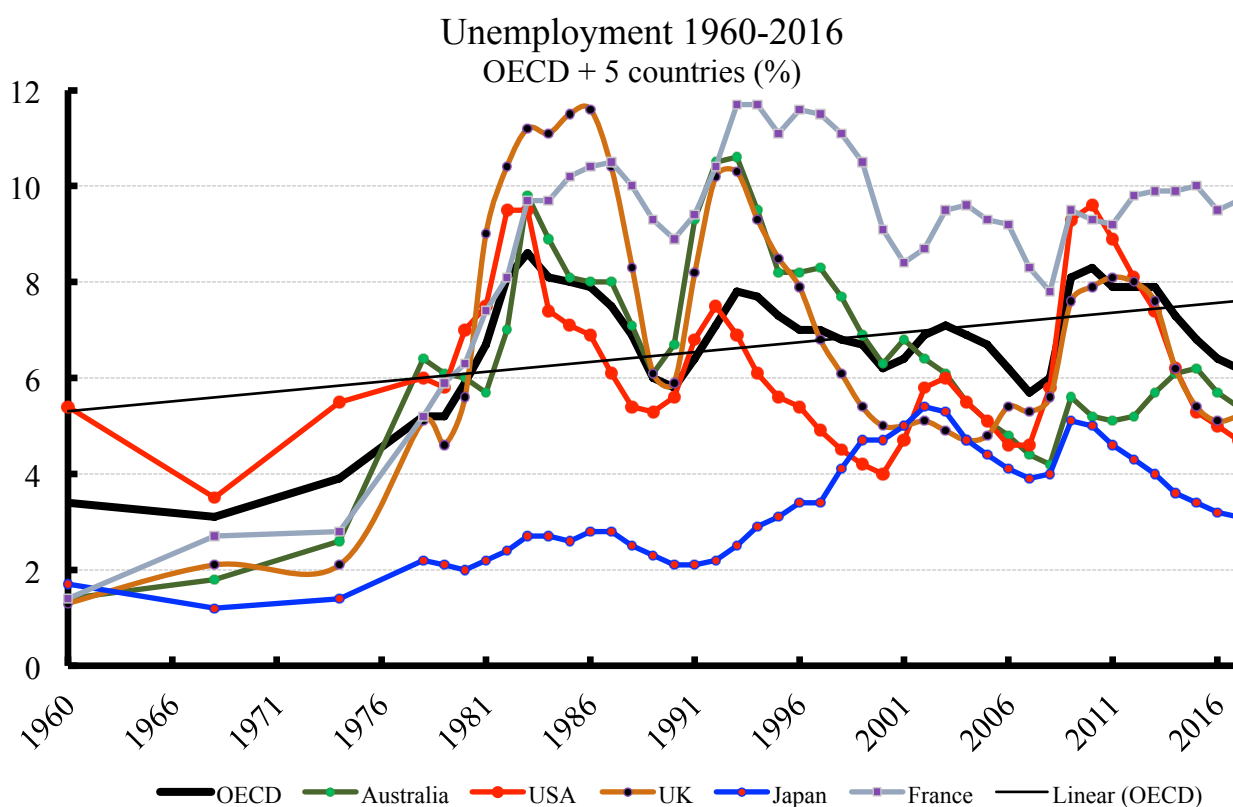


Sources: *Treasury Economic Roundup Centenary Edition 2001*
and *OECD Economic Outlook* no.99, June 2016, p.247.

Unemployment is the paramount gauge of economic policy failure, both because it indicates real, ongoing hardship and because it is a sign of inefficiency (unused labour resources). OECD unemployment (standardized measures for 34 OECD countries) is currently 7.4 per cent (2014, or 6.4 per cent in 2016 on an unstandardized basis). In Australia the figure is slightly lower than the OECD average (6.1 per cent), and close to the levels for the UK and the USA.

Of course all countries have suffered employment and industry-structure jolts since the mid-1970s when the OECD unemployment average was 3.5 per cent. The trajectory still seems to be upwards (see chart), instancing the relinquishment of many of the mixed-economy aspirations of the postwar period. We must remember, however, that for no country does the

presence of high unemployment signify that policy processes are impotent, just that, in an age of neoliberalism, supportive institutional commitments are readily forsaken.



Sources: *OECD Historical Statistics* (various issues), *OECD Economic Outlook* no.99, June 2016, p.269. [unstandardized projections for 2016-2017].

Government spending is an important first indicator of the extent of state intervention. As a proportion of GDP it is still above 40 per cent in the OECD but only 35.5 per cent in Australia. This places Australia near the bottom of the ranking table for comparable (wealthy) economies. Total taxation is commensurately low here, at around 34 per cent of GDP (total taxes at all levels of government as a share of GDP), compared with 38 per cent for the whole OECD. The disparity between

government expenditures and revenues (taxation) has been wide, in fact increasing, for the past four decades everywhere. The downward trajectory, that is, the tendency for receipts to fall short of spending, has rendered budget deficits the normal outcome in the OECD since the early 1970s – the trend line is between -2 and -4 per cent of GDP. As fluctuations in industry and uncertainty in investment are inevitable, and as the spontaneous generation of activity is now insufficient to guarantee full employment, permanent budget deficits may be desirable (Wray 2012, pp.71-72), so the recurrent and shrill expressions of concern with them seem to serve only an ideological (small government) purpose. In an era of very low interest rates internationally, borrowing – for infrastructure or to cover accumulated budget deficits – may be wholly responsible.

Social democrats, informed by heterodox and Keynesian economic ideas, have long recognized that any amount of unemployment can be eliminated by sufficient injections of additional public revenues particularly in the form of public infrastructure spending. This is true even in an age of globalized activity and decision making. But the capacity of public authorities to act effectively to manage structural disruption (and its accompanying unemployment) is clearly weakened by any long period of deficient public revenues (under-taxation), such as has been experienced everywhere since the mid-1970s – albeit often exacerbated by self-inflicted tax reductions in the recent past. In Australia, an initial register of the public revenue shortfall is the disparity between its taxation and the OECD average figure

– 4 per cent of GDP, or close to \$65 bn. If taxes were increased here to close this gap, about \$5000 (on average) in additional revenue from each of Australia’s 12 million taxpayers would be required. As estimates of the cost of a Very Fast Train from Sydney to Melbourne come to the equivalent of about 2 per cent of GDP (with similar costs for a Brisbane to Sydney VFT), the societal costs (poor transport, technological and environmental lags, urban congestion) of the under-resourcing of the public sector can be readily adjudged. Other aspects of state capacity – the ability of governments to do what market processes can or will not – are not always costly, for example, a return to principled and centralized wage fixation. Further, infrastructure improvement does not necessarily imply construction projects – it can include investment in research and education, remediation of land degradation and enhancement of the arts and public amenity. The point of this linking of public funding and public expenditure challenges is, first, to remind ourselves that a significant redress to our conundrum could be made simply by achieving in Australia the currently existing OECD average levels of taxation.

Second, it becomes consequentially clear that fiscal constraints seem far from insurmountable, though political courage is always required to increase political competence. The fiscal and political capacities implied by the above proposal (for that is what it is) amount only to levels reached already in other jurisdictions, including more conservative ones.

The politics of economic opportunities

A social-democratic program therefore envisages more than left-wing government with higher taxes and more expansive government expenditures. It anticipates, as well, a permanent shift in the balance between private and public activity, between individual and collective decisions, between the economy-as-unintended and the economy-as-democratically determined. These shifts have been occurring gradually for a century, not always as a result of conscious politicking by social democrats; and they should nonetheless be seen as both politically desirable and enduring. As citizenship entitlements expand, the rights attaching to property narrow, in some spheres freedom gives way to authority, flexibility cedes to regulation, the commodification of daily life declines in response to decommodifying tendencies, and people's fragmented calculations and expectations wane as institutional competences and capacities assert themselves. Social-democratic and labour movements have long proposed such transformations, and social-democratic principle demands them; even if they have diverse origins. By 2016, almost a quarter of all consumption in the rich societies is attributable to government provision, compared with almost nothing before the first world war.

Comparative data reveal, however, that the social-democratic impulse cannot be content with allowing secular changes in the economy, polity and society to deliver what people want or what will benefit them. Political effort (for example, through specifically designed institutions) is also needed to defend past

democratic and policy achievements, as well as to agitate for new ones. If it seems that, over the past four decades, progressive developments in some areas have stalled, in other spheres, political and institutional commitments and accomplishments have been retained. The most obvious, and damaging, instance of disruption has been with respect to unemployment. In Australia unemployment between 1945 and 1975 was rarely above 3 per cent, and often far below that figure; since 1974 unemployment has rarely been below 6 per cent and often far above it. This abandonment of commitment to full employment is characteristic of the modern age and is perhaps attributable to globalization, to technological change, to structural transformation (away from manufacturing towards finance, in all economies) or to an unlovely combination of many contributors. Most important of all, however, unemployment results from deficiencies in political will, a conscious refusal to marshal the full range of state capacities – national and international – able to ensure that seemingly intractable problems remain subject to human interventions at the political level.

Significant advances – political and intellectual – had been made from 1945 to create institutions capable of implementing the regulatory responsibilities attendant upon the Keynesian and corporatist expectations developed before and during the war. Even where these developments had not been driven by social-democratic sentiment, they relied on the structural (often unintended) shifts in economies and societies that characterized the decades after 1945 – welfare-state protections,

macroeconomic management competences, redistributive taxation regimes, fiscal subsidies and transfers, wage-fixing systems, toleration of corporate power (even restraints on competition), prudential regulation of finance, state enterprises, steady accretion of extra-market provision, policies to control the structural transformation of industry and experiments in tripartite decision-making. Of course, retreats from these commitments after 1974 have been insistent and a disturbing loss to the social-democratic momentum; but as detailed above, they have not disrupted the enduring basis for equality, prosperity and principled politics that social democracy seeks to ensure and to exploit. The return to long-term unemployment, together with well publicized increases in inequality, which usually feeds back into lower levels of economic activity and corrodes civic ambitions, reflect political defeats, not a permanent reversal of propitious possibilities.

So, if the century-long increase in government activity and confidence has not been undone in recent years, it is the otherwise debilitating public and discursive disillusionment (with the idea that politics is able effectively to transform economic processes in the general interest) that has been discredited. The available evidence above indicates that contemporary cynicism is unfounded. Politics, institutions and deliberative processes have not lost their purchase over social and economic outcomes, even if political elites here and elsewhere never understood or have abandoned their purposes. The reconstitution and amplification of postwar democratization intends a more authoritative role for public policy (especially anti-recessionary policy, incomes policy

and public investment policy, via collective capital formation), an emphasis on civic as well as private consumption, a distrust of monetary policy, and the (Keynesian) principle of counter-cyclical investment as an instrument of employment creation (in the context of an economy increasingly disposed to wealth creation rather than to job creation). Unsurprisingly, proponents of globalism and inevitability dare not acknowledge these transformative projects and therefore endorse anti-progressive tendencies.

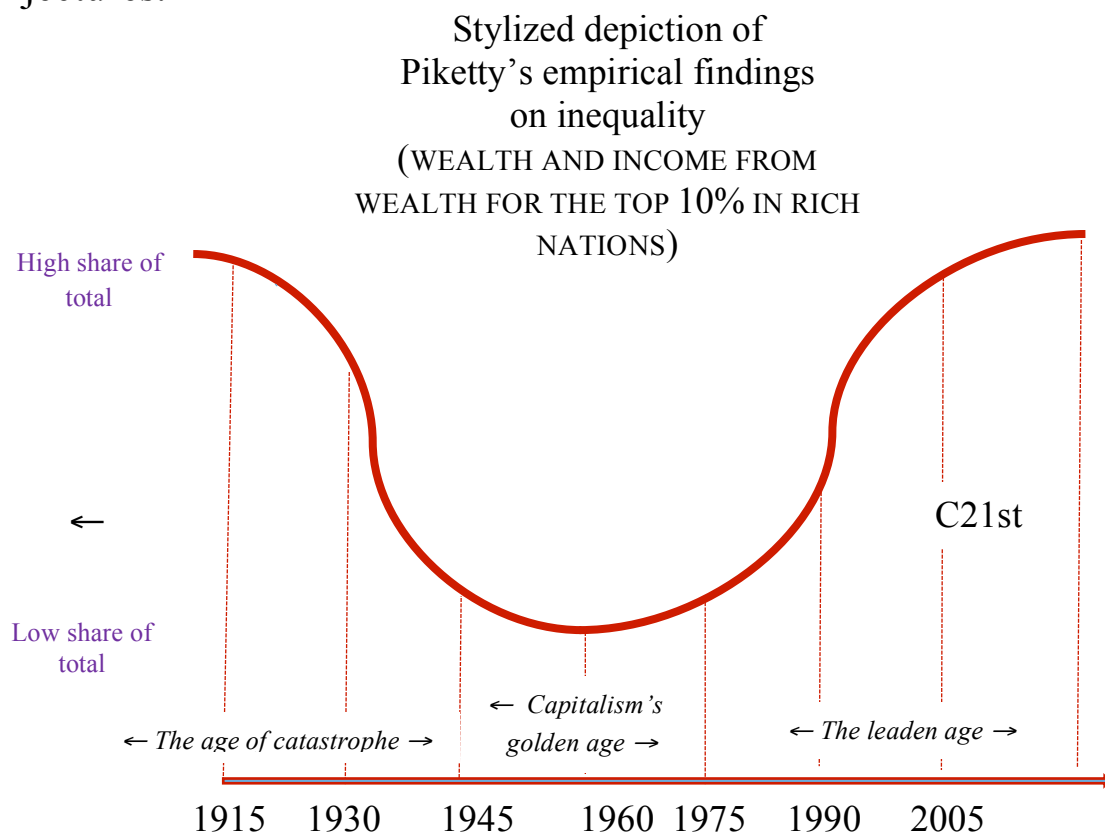
The required transformations are necessitated not just by political aspirations. They're demanded, as well, by unexpected evolutionary transitions we've witnessed in contemporary capitalist economies. These evolutionary opportunities are matters social-democratic thinking must incorporate. And it has proven, thus far, to be well able to do this – as in social democracy's longstanding claims that progress towards economic democracy is necessary to keep the economy running at its full-employment potential. Profit-oriented economic activity does not normally guarantee full utilization of resources, particularly of labour, and changes to decision-making criteria (for example, to mandate more public activity) can ensure interventions that enlarge the general interest. The recognized links between social-welfare (redistributive) aspects of the economy and its productive base, require continual re-affirmation. But, as we also now know, capitalist economies themselves cannot remain viable without them: the shifts already observed – more public spending, more fiscal capacities (taxation revenues), more social-citizenship

transfers and more income security – both confirm social-democratic expectations and provide the material basis for further social-democratic development. As social democrats have often maintained, the conscious erosion of economic liberalism’s fundamental presuppositions and lasting enhancement of economic outcomes are really the same project.

Societal aspects of economic and political possibilities

Productive and redistributive aspects of any economy are linked and benefit from their own powerful discursive traditions. Recently Thomas Piketty’s *Capital in the twenty-first century* has drawn attention to inequalities in the distribution of wealth and income – highlighting particularly the reduction in disparities that began with the ‘age of catastrophe’ (roughly from 1914 until 1945) and continued until about 1974 (when globalization, manufacturing decline, unemployment, economic dislocation, sectoral change, inflation-in-recession, and the ugliest aspects of neoliberalism began to plague societies, economies and polities in the rich countries). The last three decades of this period were otherwise known as the long postwar boom or the ‘golden age’ of capitalism or the emergence of welfare capitalism or even the era of the ‘repression of finance’; whereas the decades since the mid-1970s have been referred to as a ‘leaden age’ of policy abrogation. Social-democratic progress was for a time understood by its adherents as able to lay down the foundations for a new political-economic order – coherent, ever-more transformative, part of an inevitable supremacy of politics over markets. Others,

more sceptical and more pugnacious, saw it as reflecting only temporary and contingent increases in labour's capacities, not enduringly market-displacing, aberrant, fated to be succeeded by a resurgence of capitalism-as-usual. The data, though not the analyses, in Piketty's book broadly affirm either of these conjectures.



Hence a conundrum (intended by Piketty) presents itself: if six decades of optimism has given way to the reversals always anticipated by the pessimists, do the inequalities derive from features inherent in capitalist history (a structural tendency spanning the nineteenth and twenty-first centuries interrupted only briefly)? Or do they denote that the policy-driven progress of the period to 1974 has suffered a setback contingent upon

political defeats with which we have become familiar, implying that egalitarian policies are always possible (though subject to setbacks), but that the ‘long run’ is only a product of sequential happenstance associated with the rise and fall of industries but not with an abiding logic of its own?

Certainly we know that Keynesian and heterodox political economy, including sociological institutionalism, would have foreseen the recorded abatement of inequality for about sixty years – because ‘good times’ (of high employment, enhanced development opportunities and prosperity) necessarily imply less exclusion and a diminution of the more repugnant forms of market conduct. Complemented by stronger trade unions and new or improved state regulatory capacities (for example, in industrial relations, macroeconomic management and extra-market provision) the epoch would have resembled a virtuous circle even without a conscious social-democratic impulse.

We now know, as well, that 1974 ushered in a more-or-less capital-led reaction. As economic activity relocated from the core countries (and core zones within the rich countries) in search of lower costs or more propitious production circumstances, influential forces – notably economic liberals, financiers and internationalists – began their 40-year campaign to dismantle institutional arrangements that had come to characterize post-war growth regimes, so that, even where politicization was not wound back, it lost its regenerative momentum and capacity to galvanize the citizenry. These neoliberal responses have poisoned the popular imagination but they haven’t reconstituted a viable

regime of prosperity for more than an isolated few in the rich nations (such as upwardly mobile and disconnected workers in financial districts). The evidence thus far suggests however that policies and institutions designed to subvert the inegalitarian thrust of the market remain possible.

So, one of the great truths of social-democratic politicking has reasserted itself: the need for full employment to underwrite social civility and the reciprocal dependence of the former on the latter.

Of ongoing importance for social democracy is the need for periodic regeneration of the economy. No polity can presume the structure of economic activity (industry structure) that has delivered affluence in the past will continue to do so in the future. Consequently, political capacities need to be created and maintained that can oversee national or regional decisions adjudicating protectionist versus developmentalist impulses.

The most significant desideratum attending this realization is that political institutions must ensure increasing-return activities, that is, industries or industry segments where disproportionate increases in production result from any increase in inputs (typically manufacturing, based on high wages and high investment). It used to be said that, with manufacturing, even grocers and farmers and non-employees are better off. Such a concern with the preservation of high-value-added activity has long featured in critiques of orthodox liberal policy in both developed and poorer economies. It is an issue that has pitted

heterodox against conventional approaches to political economy for some time (possibly since before capitalist industrialization began about five centuries ago). In any case, this requirement has been referred to as the ‘collusive spread of economic growth’ (Reinert 2007, p.291). It is an imaginable link between material life and the common good, as long as polities ‘get the economic activities right’, including high-end services, and signifying in turn that it has always been political will that has piloted affluence. Weak polities, unable to choose and direct what have rightly been called production-biased ‘regimes of accumulation’ or ‘social structures of accumulation’ leave in place too many incentives for relocation, too many productivity-killing forms of corporate governance, too much consumer sovereignty; and they mistake deregulation and liberalization for the maintenance of a productive economy. This is why the ‘other canon’ (a form of neomercantilism, explained in *How rich countries got rich ... and why poor countries stay poor* and other writings by Erik Reinert) identifies de-industrialization in the wealthy economies as a man-made (policy-induced) crisis. In its demolition of politicized economies, it is a disaster for humanity.

This neomercantilism is clearly contentious and is just as compatible with principled conservatism as with social democracy. It scorns the economic-liberal idea that polities should as a matter of dogma avoid responsibility for the level and content of productive investment. But it sets parameters for the battles of the future.

Conclusion

Controversies in economic policy have always needed to deal with long term issues thrown up by the continual restructuring of industry. Contemporary unemployment is of this type, with the added complication that economic growth – even in Australia, which does well if growth is the arbiter – no longer generates employment as reliably as it generates wealth. Economies have evolved in ways that have made more apparent than previously the determining impact of politics on both overall living standards and on distributive outcomes. Unlike in the post-1945 period, inequality is once again increasing, everywhere, exacerbated by unemployment and the industrial decline of the last four decades. This means that social-democratic and labour-oriented politics will underpin, as well as benefit from, the transitions already evidenced in the rich societies (towards higher taxation, more state responsibility for consumption, and explicit employment-creation efforts that should not be dependent on strictly economic or efficiency criteria). That is why neoliberalism, and other forms of resistance to politics, is proving so destructive; but this is something labour movements and social democrats have long understood.

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