G.Ü. İ.İ.B.F. Özel Sayısı / Special Issue 2002, 189-210

The Rhetoric And Economics Of Neoliberalism

Mayo TORUNO*

For almost three decades public discourse has been governed by the Neoliberal faith in free markets and limited government. It's a movement whose origins can be traced to the emergence of rightist politics during the mid 1970s in advanced capitalist nations, and formalized with the coming to power of Margaret Thatcher in Great Britain in 1979 and Ronald Reagan in the United States in 1980. Economic stagnation, it was argued, was the result of an over bloated public sector that had prevented free enterprise from achieving its full potential. What was needed was a reduction in the size of government; markets should be deregulated, public services privatized, social safety nets removed, and discretionary fiscal and monetary policy abandoned. The result would be an explosion of entrepreneurial effort generating a rising tide of economic prosperity that would lift all classes of people onto higher levels of affluence. What's more, this would all be achieved through the magic of the free market.

The collapse of the Soviet Union provided further inspiration to this rightist vision. The implosion of the world's largest centrally planned economy came to be interpreted as confirmation of the superiority of free market systems. In the United States, in particular, this event was viewed by its ruling class as validating the presumed historical destiny of America, to serve as the model of a just social order, the beacon light guiding all of humanity into an era of unprecedented freedom and wealth. The new millennium would see the blossoming of political economies that had come to realize the virtues of free markets and its necessary counterpart, the night watchman state.

At the global level this Neoliberal faith was being pushed by an elite group of international institutions, in particular the International Monetary Fund, the World Bank, and the World Trade Organization, that were beholden to American policy elites. While these institutions had originated in a Keynesian context, assuming the

*Prof., California State University, San Bernardino

need for public oversight of market relations, they have evolved, particularly the International Monetary Fund and the World Trade Organization, into the primary instruments through which Neoliberal reforms are imposed on developing nations. The World Trade Organization has become the chief vehicle through which a global free market is to be created, one that unambiguously favors commercial interests at the expense of labor, national sovereignty, and the environment. And the International Monetary Fund has been imposing its vision of Neoliberalism by demanding that nations seeking loans adopt, as a condition of the loans, free market prescriptions - eliminating social safety nets, privatizing public services, and agreeing to austere balanced budgets.

It's against this background that the publication of Joseph Stigletz's most recent book, *Globalization and its Discontents* (2002), comes as a breath of fresh air, underscoring the extent to which the policies of the International Monetary Fund have been driven more by faith, what he calls free market fundamentalism, than by a reasoned understanding of the limitations of markets and the corollary need for a government attentive to the material needs of society. Markets, Stigletz reminds us, are not always right, they can be unstable and inefficient, require a complementary set of cultural, financial, and political institutions, and often need public oversight.

Coming upon the heals of the dramatic demonstrations, over the last few years, against the World Trade Organization, Stigletz's critique suggests that an opening might now exist for the pursuit of policies that negate Neoliberal tenets and acknowledge the importance of collective, democratic, control over economic outcomes. This is a possibility, but one that's dependent on a number of factors not all of which might work out as one would like. Moreover, and more to the point, it's unlikely that, Stigletz notwithstanding, the core of the economics profession, the mainstream, will raise it's voice in protest against the idiocy of free market fundamentalism. What we may instead witness is the emergence of a more vibrant and humane political economy evolving from regions of the globe that are currently in the shadow of America's hegemonic power. By virtue of their distance, culturally, ideologically or geographically, from the center of free market fundamentalism, they're more likely to develop solutions to the eternal problem of social provisioning that are more pragmatic and less doctrinaire than anything currently emerging from the Neoliberal vision. The irony is that it might be the United States that falls behind, blindly insisting on the sanctity of markets, as other nations forge ahead building upon a more reasoned understanding of markets and a richer vision of democracy. In the meantime, whether economics will undergo the kind of paradigmatic shift needed to dislodge the free market ideal from its core depends largely on the extent to which public discourse, and, of necessity, the political economic structures which set limits to that discourse, acknowledges the need for democratic control of economic outcomes.

II

What makes Stigletz's book so refreshing is the fact that, despite coming from impeccably mainstream credentials, having earned the 2001 Nobel Prize in Economics, he doesn't flinch from pointing out the obvious problem with free market fundamentalism; namely, that it doesn't work. The International Monetary Fund's uncritical application of the free market dogma has done more harm than good. Its Neoliberal policies have contributed, over the last twelve years, and in varying degrees, to the economic collapse or stagnation of Argentina, Brazil, Kenya, Russia, and the East Asian countries of Indonesia, the Philippines, Singapore, South Korea, and Thailand. Rather than helping developing nations adjust to economic difficulties by encouraging counter cyclical monetary and fiscal policies, the austerity or balanced budget prescriptions demanded by the International Monetary Fund have exacerbated the problem. And rather than suggest a cautious, case by case, approach to the issue of privatization or market deregulation, the International Monetary Fund adopts a one-size-fits all prescription that imagines free markets to be the universal panacea.

The failure of the Neoliberal program is perhaps most evident in the tragic collapse of the Russian economy during the 1990s as a result of the short-sighted attempt to impose a free market regime upon a formally centrally planned economy. The presumption was that a quick and dramatic dismantling of the bureaucracy of the state, privatizing previously public enterprises and quickly creating a regime of private property, would be sufficient to unleash the magic of the free market. There seemed to be a complete lack of understanding regarding the necessary institutional framework, cultural, legal, and financial, which must be in place before a market system could operate more or less unimpededly. The consequences of that short-sighted policy are well known: in the period from 1990 to 1999, Russia experienced a 54% decline in GDP, a 60% drop in industrial production, a dramatic expansion in wealth and income inequality, rising unemployment and poverty, rising crime and corruption, and social unrest (Stigletz, 143).

But, it isn't just the developing, or momentarily week, nations that have had to endure the blessings of the free market, advanced capitalists nations have also adopted these Neoliberal prescriptions. But, in this case, the prescriptions have seldom been administered with the same zeal demanded of developing nations. In part, this is due to the fact that the advanced capitalist nations, particularly the Western Europeans, already have developed welfare states that, for important political and cultural reasons, are not about to be dismantled. Similarly, there still exist, within these nations, political coalitions that have managed to resist the imposition of a complete Neoliberal program. Additionally, the rightist politicians, despite their breast-beating proclamations in favor of free markets and limited government, and seemingly unaware of the inconsistency, accept as incontrovertible the need to pursue stimulative

policies in the face a deteriorating economy, though it invariably involves elements of military Keynesianism and tax reductions for the rich.

Nevertheless, despite this more timid and hypocritical application of the Neoliberal medicine, the outcomes have been similar. In the case of the United States, the economy performed less dramatically during the last quarter century of Neoliberalism than it had in the quarter century following World War II. To be sure, some of this is due to reasons that have nothing to do with changed policy regimes. Yet, it's undeniable that the fiscal stimulus employed by the United States government during the 1980s and 1990s was less than what would have been the case if a more activist view of government had been dominant; causing, of course, GDP to grow at a slower rate than it could have. In addition, the rightist tax policies of the Neoliberal era, beginning with the Economic Recovery Tax Act of 1981 under President Reagan, were responsible for the growing inequity in the distribution of wealth and income that has characterized the United States during the last two decades (Peterson 1994, pp. 101-127, 264-274; 1996, pp. 604-616). The attack upon organized labor, the reduction in the real minimum wage, and the scaling back of unemployment compensation programs, contributed to the reduction in worker's wages and a higher average level of unemployment. The government's neglect of social infrastructure led to not only a deterioration in such public services as education, highways and parks, but a decline in the productivity of labor as well (Peterson 1994, 178-184). And the deregulatory frenzy of the last two decades contributed to the debacle of the Savings and Loan industry in the late 1980s, the speculative stock market bubble of the 1990s, the recent failure of California's electricity market, and a commercial culture that tolerates fraud, embezzlement, and chicanery, so long as it's cloaked in the language of corporate respectability.

But, it isn't really necessary to review the recent record of Neoliberalism to determine its efficacy; a more direct route has been available all along, namely the economic history of advanced capitalist nations prior to the development of the social welfare state. A quick review of the conditions of people in the United States prior to the New Deal era underscores the extent to which economic instability was much greater at that time than it was in the era of the social welfare state; or even in this new era of Neoliberalism, which has managed to spare itself the worst excesses of its own philosophy by operating within the context of an extant welfare state. Depressions were much steeper, the distribution of wealth and income was more unequal, poverty and unemployment was more extensive, and social security and other social safety nets were non-existent. When the great depression of the 1930s hit, the discontent was sufficiently palpable that many were wondering whether capitalism might survive. As we know it did, but as a result of the creation of the kind of public programs, the welfare state, which Neoliberals now insist on dismantling.

III

At the level of popular political discourse, particularly as voiced by rightist politicians and the business class, the plea for free markets is most often expressed as a demand for unhampered private property and the right to exploit profitable opportunities wherever they might arise. It doesn't necessarily carry with it the presumption that markets be competitive; all it demands is that capital be free to seek out profitable opportunities, regardless of whether these opportunities present themselves in the form of competitive or monopolized markets. It assumes that the interests of capital are coincident with those of society, and that profitability is sufficient proof of its effectiveness as a tool of public policy. And it views government as inefficient and unproductive, a burdensome institution incapable of sustaining itself without siphoning off, through taxation, some of the wealth created by private enterprise.

This combination of sentiments is generally found in varying degrees, and with different emphasis, among the business classes and the broader capitalist culture. It's not a coherent philosophy but rather a lose set of prejudices common to a privileged class of people who make their living by cultivating investment opportunities, controlling labor processes, and haggling in the market. And while it's part of the ideological milieu of capitalist cultures, it's not necessarily the same thing as the argument for free markets one generally encounters among economists. There are, to be sure, family resemblances, and it's this resemblance that accounts, in part, for the legitimacy that's granted free market economists. But, despite the superficial resemblance, the differences are sufficient to explain why it is that even conservative economists are frequently repulsed by the above self-serving expression of this ideology.

The economist's version of the free market differs from this common prejudice by emphasizing the role of competition. The presumption is that economic freedom brings with it sufficient competition to insure that, on the whole, the self serving behavior of any one capitalist is checked by the self serving behavior of all the other capitalists. It's not that capitalists, per se, are good, or that their actions are generally consistent with the interests of society, but rather that competition has the unintended effect of guiding their self-serving actions toward outcomes beneficial to society. What's more, the concept of competition, as used by the economist, is generally different than the version common to the businessperson. The latter invariably has in mind the metaphor of an athletic competition, where the winner is the first one to reach the goal, the one who can outperform, or stay ahead of, the others. But economists, particularly contemporary neoclassical economists, think of competition as a constraint that limits the maneuverability of capitalists. The basic idea is that there are so many agents in the market that each is forced to conform to its dictates. The capitalist's self-interested behavior, while generally not consistent

with the general interest, is made consistent by the constraint that market competition imposes on her/his behavior. In the absence of such a constraint, the profit seeking activity of capitalists will tend to run contrary to the common good.

There are two versions of this idea: the classical version that dominated economic thought during most of the 19th century, echoes of which still exist in contemporary literature; and the neoclassical version that emerged in the last quarter of the 19th century and dominates the interpretation to this day. The classical version, articulated in the work of Adam Smith, David Ricardo and John Stuart Mill, focused on the impact that competition would have on economic growth. Competition, it was thought, was the natural outcome of economic freedom, what Smith called a system of natural liberty. The classical economists were advocating a system of natural liberty and not, necessarily, a system of competitive markets. While competition was thought to be the normal state of economic freedom, the latter would also include the monopolies that were bound to emerge, if only temporarily, in new markets.

The classical argument for economic freedom assumes that the capitalist is forever seeking to capture monopoly profits. In this sense the classical notion of competition is similar to that of the typical businessperson. However, the classicals believed that any monopoly position that might be captured by a capitalist would be short lived. The search for monopoly induces the businessperson to invest his/her capital in new products and services, extending the social division of labor, and increasing the volume of gross domestic output. But the monopoly profits being captured by the first entrants shortly vanish as other capitalists invade that same market in the hope of capturing some of those profits. This process would encourage economic growth while ensuring that market prices tend toward their natural, prices of production, values.

This was a long-term argument intended to explain the beneficial effects of a system of natural liberty over a period of a generation or two. It was not intended as a quick, short-term, fix. The image was that of a large collection of small entrepreneurs scurrying about in search of untapped opportunities and preventing each other, by their shear numbers, from sustaining a monopoly position. And if a monopoly were to persist longer than expected, a period of time that was presumed to be temporary, then government could rectify the situation by either encouraging more competition or controlling its behavior, which could include nationalization. The argument did not claim that all would share equally in the benefits of natural liberty; it assumed a stable class structure that kept the distribution of wealth and income unequal. And, over the long-term, workers would earn just enough to reproduce another generation of workers, but could, in the short-term, rise above or below subsistence, leading to either an era of relative abundance or growing poverty among the working classes.

The neoclassical version of competition, exemplified in the work of Alfred Marshall and Leon Walras, among others, shifted its focus from issues of economic growth to issues of allocative efficiency; not that growth was ignored, but rather that it was subsumed under the broader argument for efficiency. The prime mover of the system was now thought to be the consumer rather than the capitalist, and the latter was reduced to the somewhat passive act, by virtue of being in a competitive market, of meeting consumer demand by efficiently churning into outputs at profit maximizing rates. The basic idea was that competitive markets force firms to produce the amount and variety of goods demanded by consumers at prices that, in the long run, equal the minimum unit cost of production. Firms would be forever adjusting production to the rates set by demand while continually seeking the minimal combination of inputs needed to generate the product. Market prices would quickly respond to demand and supply conditions and every consumer and firm would be a price taker. In the products market, the rising prices and greater than normal profits brought on by excess demand would be met by an inflow of resources causing supply to expand and prices and profits to fall back to their normal level. And in the labor market, an excess supply of labor would be quickly remedied through competitive wage reductions.

In the long run, the economy would achieve a general competitive equilibrium, a situation in which supply would match demand in every market, ensuring the full employment of labor, prices would equal the minimum unit cost of production (including the firm's normal profit as a cost), and consumers would be maximizing utility (profit maximization is implicit in the condition that price equal minimum unit cost). Resources would be allocated so efficiently that an increase in the demand for any one good would require that resources be removed from the production of other goods and shifted toward producing the good in excess demand. In short, the system would be operating in a state of perfect efficiency, otherwise known as a Pareto Optimum. The Neoclassicals understood that such a state was consistent with a highly unequal distribution of wealth and income and situations in which worker's wages were below subsistence. In addition, it was understood that government would maintain a competitive environment by regulating or nationalizing monopolies.

In the short run, a real competitive market system is bound to experience some inefficiency as a result of momentary mismatches between demand and supply, evidenced through either the existence of labor unemployment, shortage or surplus of commodities, or prices that differ from minimum unit cost. If the underlying parameters structuring the system, such as preferences patterns, initial endowments, and technology, were held constant, then the competitive market system would move toward a general equilibrium insuring the achievement of a Pareto Optimal outcome. But, of course, in the real world, the underlying parameters are always

undergoing change, even if gradual and incremental, so that at any one moment in time a real competitive market system will always be in a state of disequilibrium groping its way toward the general equilibrium consistent with the current, or most recent, parameters. So, the neoclassical argument isn't that real competitive market systems are always efficient, in the Pareto Optimal sense, but rather that they are always tending toward a Pareto Optimal state; with the further assumption being that the system is close enough to a Pareto Optimum that it can be achieved rather quickly.

Since a general competitive equilibrium can never be observed, its existence and stability has to be determined through logical proofs. Leon Walras was the first to take up this task, in the 1870s, by developing a linear mathematical model that depicted a perfectly competitive market in a state of general equilibrium. But, as is well known, despite the ingenuity of his work and the clarity he brought to the issue, his existence proof was inadequate and stability was suggested, through a groping process, but never proven. As a result, the Neoclassical claim that competitive market systems move toward a general equilibrium, and thus a Pareto Optimum, remained more of a conviction than a demonstrable truth. There was no guarantee that the on-going dynamics of real market systems, replete with unemployment, shortages or surpluses, and prices above or below unit cost, were indeed tending toward a Pareto Optimum. They could just as easily be moving away from it or in a state of continual turmoil and instability.

It wasn't until 1954, with the work of Kenneth Arrow and Gerard Debreu, that a logical proof of the existence of a general competitive equilibrium was established. But the proof was so abstract and devoid of verisimilitude that it was worthless as a vehicle for the understanding of reality or as a guide to public policy. The existence proof required conditions that do not exist in the real world, such as the universal presence of perfectly competitive markets, the non-existence of increasing returns to scale, consumers with perfect and complete information regarding all commodities and terms of exchange, a futures market for every commodity, and instantaneous production. It was a purely formal exercise that could not be used to say anything substantial regarding the efficiency of real market systems (Koopmans 1957, pp. 146-7). Indeed, to this day existence proofs have been incapable of incorporating assumptions that provide reasonable approximations to reality. What's more, there are no stability theorems that can prove that competitive market systems converge on a general competitive equilibrium without relying on highly restrictive assumptions (Weintraub 1979, pp. 34-35). Yet, despite the inadequate nature of these proofs, Neoclassical economists continue to hold onto the image of the competitive market as an efficient system that, on the whole, insures that self-interested behavior concur with the general interest of society.

IV

Central to these theoretical traditions is the faith that a free market system is self-regulating and does not require the attention of government. The primary objective of these theories is to demonstrate that government should confine itself to a rather limited set of tasks and allow economic activity to be dictated by the free market. So long as the markets are competitive, then government can confine itself to defending private property and adjudicating disputes, providing for the military defense of the nation, and supplying the needed infrastructure, included the provisioning of public goods. This latter condition was sufficiently ambiguous that it could be interpreted to mean the provisioning of commercial infrastructure, such as public highways, transportation systems, and ports, or more broadly to include, in addition to commercial infrastructure, social goods such as public education, health care, and parks. It was assumed that government would regulate, in some fashion, monopolies whose existence seemed to be more than temporary. And the theories were consistent with public policies that sought to lessen the inequities in the distribution of income through various redistributive schemes. It wasn't the absence of government that was being advocated, but rather the existence of a particular type of government, what I have called the night watchman state.

From the beginning, there were problems with this vision. To be sure there were the critiques from the socialist camp, generally arguing that it was unstable and anarchistic and that it relied on a system of private property requiring the exploitation of labor. But, even among those who favored private property and individual initiative there were those who were skeptical of the harmonious or stabilizing properties of a free market system. Jeremy Bentham's position provides the classic example. Bentham did not accept Adam Smith's claim that a system of natural liberty would result in outcomes that are consistent with the general interest of society. As a result, he favored the use of government as a way of nudging the free market system toward more appropriate outcomes. The system would still rely on private property and markets, but government would take a more active role than was generally accepted by Smith (Halevy 1972, p.17).

By the early 1930s a critique of the free market system had emerged among a small but insightful group of neoclassical economists, or economists in the process of breaking away from the neoclassical paradigm, who were skeptical of the presumed efficiency of competitive markets and open to the possibility that government might need to take on more than its classic night watchman functions. Arthur Pigou (1932), for example, was arguing that, because competitive markets are incapable of incorporating the true social costs of production, in the presence of negative externalities such as environmental degradation, government should use its taxing and subsidy powers to ensure that prices reflect total social costs. What's more, he continued, government can improve social welfare by pursing policies that

bring about greater equity in the distribution of income. Piero Sraffa's (1926) critique of Alfred Marshall's belief that external economies maintain competition even in the presence of increasing returns to scale, underscored the extent to which free market systems may not guarantee the maintenance of competitive conditions and that, for a wide range of industries, monopoly is the natural outcome of formerly competitive environments. And Joan Robinson (1933), along with, though independently of, Edward Chamberlin (1933), noted that monopolistic competition, rather than perfect competition, is common in free market economies; implying that most firms are actually price setters rather than price takers, and excess capacity, rather than efficiency, is the norm. The free market, in short, may not possess enough self-correcting features to insure that it remain competitive and forever close to a Pareto Optimum, it might instead have a greater capacity, than previously believed, to encourage the development of monopolies and a rather common form of competition that generates inefficiency.

An opening was presenting itself for the idea that government should take on a greater role in overseeing the market. This opening, which was really more of an inclination than anything else, became a plea for greater government involvement with the publication of John Maynard Keynes's General Theory of Employment, Interest and Money in 1936. The fundamental critique that Keynes introduced was that competitive market systems could not be counted on to bring about full employment, even in the long run. Neoclassical economists accepted the idea that unemployment exists in the short run, but they viewed it as a temporary phenomenon that would vanish in the long run. What made Keynes's critique so dramatic is that he was arguing that unemployment could be a long run equilibrium outcome of a competitive market system. What's more, he was not claiming that unemployment was the result of market imperfections, sticky wages and prices, he was making a more powerful claim, namely that full employment could not be assured even in the presence of perfect competition.

Keynes's critique implied that government would have to be more actively involved in the maintenance of full employment. In the words of Keynes, it implied a "somewhat comprehensive socialisation of investment" (Keynes 1964, 378). His critique and policy recommendations lent support to the growing demand for a government that would provide for the welfare of society through the provisioning of a wide range of public goods, alleviate poverty through the establishment of social safety nets and redistributive schemes, regulate markets injurious to the public, and maintain full employment through macroeconomic policies. In all of this, it's important to note that the plea was not for the overthrow or removal of the market, let alone capitalism, but rather for greater collective, democratic, control of the economy, one that sought to guide the market toward outcomes it might normally not take.

The reactions to these developments were as predictable as they were swift. By the early 1940s, the more radical element of Keynes's message had been expunged through an awkward synthesis of neoclassical and Keynesian ideas. The result was the development of the Keynesian school of thought, the bastardized Keynesians as Joan Robinson called them, that dominated economics in the three decades following World War II. The message that the Keynesians were delivering was less jarring to neoclassical ears than the one which Keynes himself had delivered. Unemployment, they argued, was the result of imperfect competition and or/sticky wages and prices, and not something that would occur in a state of perfect competition. This, of course, rescued the ideal of the competitive market, if only as a logical possibility, while serving as justification for a more cautious approach to macroeconomic management. The government would not have to socialize the investment process, it could simply engage in a more limited policy of fine-tuning.

But even in this form, the argument was too unsavory for free market economists, and, as a result, there emerged a counterrevolution intended to rescue the notion of the free market by focusing on the failures, inefficiencies, and tyrannical tendencies of government. The roots of the Neoliberal perspective can be traced to this reaction, making its first appearance in the 1950s with the emergence of the Monetarist and Libertarian perspectives, and more broadly the Chicago school of economic thought. The Monetarists, under the leadership of Milton Friedman, argued that the free market was sufficiently close to the purely competitive ideal that it didn't really need macroeconomic management, let along the socialization of investment. Indeed, they argued that unemployment and macroeconomic instability was more often than not the result of government itself. Monetary and fiscal policy, rather than nudging the system toward full employment and stable prices, would too often exacerbate the problem or be the cause of it in the first. As a result, they favored fixed rules that constrained government's ability to us discretionary monetary or fiscal policy. Best to leave the economy to the free market.

The Libertarians, in the form of the Public Choice school of thought, as exemplified in the work of James Buchanan and Gordon Tullock, as well as in the work of Friedman and Friedrich Hayek, stepped up their attacks against Keynesian prescriptions and the welfare state by arguing that expanding the functions of government beyond those strictly expected of the night watchman state would inevitably lead to an erosion of political freedom. Quite apart from the question of whether or not the free market leads to efficient outcomes, which they believe anyway, the libertarians view the free market as the foundation for political freedom. Each extension of government must come at the expense of the free market and, consequently, the political freedom it's thought to encourage. What's more, as noted by Buchanan and Tullock, governments, even if they are democratic, are incapable of meeting voter preference without coercion. Unlike the market, which they believe is capable of bringing about unanimity without coercion, government, even

if it is democratic, must use coercion to coordinate the actions of individuals. Democracy is, of necessity, coercive since it forces the minority to conform to the choices of the majority. As a result, freedom is best assured by constraining government through constitutional rules, limiting the range of issues over which it has discretion - such as monetary and fiscal policy, while simultaneously preventing it from becoming a Leviathan inclined to grow at the expense of individual liberty.

The growing dominance of Monetarist and Libertarian thought was aided during the 1980s by the rise of a related school of thought now referred to as New Classical, but which first appeared in the form of Rational Expectations. Like the Monetarists and Libertarians, the New Classicals are leery of government. Since they believe that expectations are formed rationally and that, more importantly, the purely competitive model captures the behavior of real economic systems, counter cyclical government policy can never be successful, unless it somehow manages to fool the people - carrying out policies that are systematically different from those that would be rationally expected. Because of this, government, they argue, should not pursue discretionary policies intended to bring about full employment and stable prices. The free market is capable of doing this on its own. What's more, activist monetary or fiscal policy exacerbates the situation by creating the very instability government is hoping to temper.

This set of arguments, and a few others, most notably R. H. Coase's theorem of property rights, and the Chicago school's belief that private monopolies are preferable to the presumed inefficiencies of public monopolies or government regulation, provide the intellectual foundation for the Neoliberal movement that came to power with the dominance of rightist politics in the early 1980s. What these traditions share in common, and what places them in a different camp than the Keynesians, and even their contemporary incarnations known as New Keynesians, is the belief that the perfectly competitive market model is a reasonable approximation to reality, despite the imperfections of real markets. Because the extant market system is thought to conform, on the whole, to the neoclassical vision of perfect competition, society is better off with a wide unregulated sphere of private enterprise and a limited, night watchman, state. In contrast, the Keynesians, and the New Keynesians, believe that the imperfections of the real world are sufficiently important to make the perfectly competitive model an inappropriate guide to understanding real markets, as a result they see a greater need for public oversight of market outcomes.

V

The thing to note in this brief review is the extent to which economic debate has centered on determining the limits of public authority. When viewed in this light the theory of perfect competition, particularly when expressed as general competitive

equilibrium theory, seems to be less a theory of actual market behavior than a theory of what could be or a theory of the ideal. It has more in common with political philosophy than it does with scientific theories intent on explaining actual, observable, behavior. This is especially apparent when considering the mainstream's reaction to the mathematical proofs of the existence and stability of a general competitive equilibrium.

Prior to the development of such proofs Neoclassical economists were convinced that real competitive market systems were forever converging upon a Pareto Optimum, closer to that ideal than what would be the case if the state were to organize economic activity; a conviction that was sustained by faith rather then empirical confirmation or logical proof. But, more tellingly, that faith remained just as unshaken once logical "proofs" were finally discovered, proofs that were so devoid of empirical referents they could be used in reduction ad absurdum arguments to disprove the very existence of a general competitive equilibrium. What's more, empirical evidence in the form of unemployment, prices that diverge from minimal unit cost, surpluses or shortages, monopoly, oligopoly, increasing returns to scale, price setting firms, imperfect or incomplete information, stagnation, instability, environmental degradation, and poverty, is not enough to dislodge faith in the perfectibility of the free market since they can all be classified as either evidence of disequilibrium or conditions that would not hold in a system of perfect competition. Empirical disproof can never be offered, and empirical proof is always put off until the arrival of the long run, which by its very nature, never arrives.

It is this feature of the theorem, the conviction with which it's held, that suggests it has more in common with political philosophy than with science. Its purpose is to outline the ideal, to explain why society should be organized along free market lines, rather than to explain how free market societies actually operate. It's a theory of justice, in the sense that it offers a positive answer to the question of whether individual self-interested behavior can be compatible with the general interest of society. Indeed, its structure is identical with those political philosophies, such as John Locke's theory of government, that envision the existence of a state of nature wherein rational, self-interested, individuals can interact and engage in exchange, arriving at reasonable outcomes, without the existence of government. Government, from this perspective, emerges because of the occasional inconvenience, transgressions of reasonable behavior, which can arise in a state of nature. But, on the whole, the state of nature can carry on by itself and, ultimately, its purpose is to serve as the criterion by which to assess the legitimacy of government.

The similarity that exists between Lockean theories of a state of nature and the economist's notion of the free competitive market, and in particular a general competitive equilibrium, is not coincidental. The two emerge from the same cultural context. And the suggestion I'm here making is that the mainstream's conviction in

general equilibrium theory is itself part of a broader social project, a cultural system that sees private property and the pursuit of self-interest as core normative beliefs, hard core propositions that serve as the unshakable foundation from which a characteristically bourgeois view of the world emerges. Economics, it must be remembered, evolved with the development of capitalism. And, in particular, it emerged, and was given its most famous expression, from British and Anglo Saxon cultures that had seen the emergence of merchant classes vying to gain a political voice while seeking limits to government behavior. Economics can thus be interpreted as the medium through which such cultures developed arguments intended to legitimize the exercise of private economic power, while setting limits to public power.

Cultures can be viewed as on going hermeneutic systems intent on explaining reality by reference to a core set of values, axiomatic norms, that govern that culture's paradigmatic vision. The socialization and rituals, which are a part of every culture, provide the means through which core values are passed on from one generation to the next, serving as the basis from which the dominant paradigm is used to explain and manipulate reality. Extending Thomas Kuhn's notion of normal science to political communities, allows us to interpret them as cultures that use and adjust their dominant paradigm to explain and deal with the on-going problems, the puzzles, confronting society (Wolin). But unlike the core values of scientific paradigms, the core values of a political culture are normative in the sense that their purpose is to explain how things should be. The purpose of the paradigm is not to explain society as it is actually constituted, but rather to serve as a guide for what should be, to make political reality conform to the ideal. The importance, or legitimacy, of the paradigm is not dependent on the extent to which it explains actual behavior but rather on the extent to which it makes credible the possibility of attaining the values professed by the theory; on the extent to which the individuals living in society believe they can conform to the ideal, even if their actual behavior falls short of it.

The core political values that emerged from Anglo Saxon cultures are those that were formalized in the work of John Lock and which served as the framework from which the political constitutions of Great Britain and the United States developed. The political communities that evolved out of such cultures have their base in the material conditions of merchant and commercial life, and carry with them the ideal of free exchange as first expressed in Locke's notion of a state of nature. This state of nature can be viewed as an expression of the ideal life; individuals endowed with private property, entering into mutually beneficial exchanges that are, on the whole, reasonable and consistent with the common good. Government stays out of these exchanges and has only one justification, namely, the defense of private property. But since the exercise of self-interest and the pursuit of gain might lead to

unreasonable outcomes, preventing some citizens from exercising their right to subsist, government can be justified in interfering with private economic affairs for the purpose of restoring the common good. Its actions, however, must be consistent with the defense of private property and its reasonable use.

The Lockeian vision of a political society is one in which the burden of proof rests upon the state and not the individual citizen. It is the state, not the individual, which needs to justify its actions by reference to the rule of reason and the prior rights of the individual. Moreover, the legitimate exercise of state power is dependent on the extent to which government carries out its mandate to protect property by allowing individuals to carry out their activities in a reasonable fashion, consistent with the right of every other individual to do the same. Clearly, the purpose of such a political philosophy is to lay out the limits of state authority, with the general presumption being that state action is suspect unless a good reason can be supplied for believing otherwise. And since the primary objective of the state is to protect property and the reasonable actions of individuals, reasons that are considered legitimate are those that can protect this right while simultaneously promoting the common good.

Economics can be viewed as the sphere of society that emerged from Anglo Saxon political cultures to provide specificity to this Lockeian vision of society, to serve as the vehicle through which the puzzles confronting these political cultures would be resolved. Much of the history of economics can interpreted as an on-going effort to determine the conditions under which the state of nature can arrive at outcomes consistent with the common good and, by implication, the limits to state authority. The history of economist's theories regarding natural liberty, economic freedom, and perfect competition, can be viewed as the detailed arguments that have been offered to justify the exercise of private economic power. At the same time, of course, those same theories have been offered to explain the limits to government action. And, as with Locke, two broad interpretations exist: those theories that argue that private economic activity tends to coincide with the common good and advocate the night watchman state; and those theories that argue that private economic activity does not always result in the common good, requiring the need for a more activist state.

Both interpretations of this Lockeian vision do not carry equal weight. The image of a free market society sustained by a night watchman state has always been the dominant view and the one most consistent with the business class's political orientation. It's the voice most frequently heard and the one most likely to be funded by business. Within the discipline of economics, models of perfect competition and general equilibrium are the required point of departure for presumably understanding real market behavior. Indeed, textbooks on economic principles invariably start out by assuming the existence of a Pareto Optimum, presented as a

point along a production possibilities frontier, to socialize students into accepting the idea that trade-offs are the inevitable consequence of an economy in which resources are fully and efficiently employed, which, of course, only occurs in a state of general competitive equilibrium.

Kuhn's explanation of the role that exercises, proofs, simulations, and experiments play in a practitioner's socialization into a scientific paradigm is relevant in this regard (Kuhn pp. 46-7). The theoretical approach that economists are socialized into accepting involves methodological individualism and the analytics of equilibrium, which encourages a view of society that emphasizes self-regulatory processes, stability and automatic, non-discretionary, coordination of interests. In a revealing 1959 article, George Stigler [1959] defined most economists as political conservatives inclined to champion free markets, and argued that this bias is a result of their training in the logic of the competitive market model. The habits of thought which emerge from learning that model predisposes the economist to interpret reality from that perspective even though the actual economy may depart considerably from the conditions of the model. Repeated instruction in that mode has the effect of inculcating a preference for, or at the very least increased tolerance of, free market prescriptions. In short, economics does more than generate analytical models of the economy; it socializes students into adopting a worldview that is congenial to the free market.

But, in addition, the schools of thought that are emphasized and deemed worthy of discussion within economics are affected by the broader political culture. There is, in short, an on going dialogue between economics and the political discourse of society. While the dominant theme within the discipline, as well as in the broader political community of Lockeian cultures, has always been that of the free market, it's relative standing has ebbed and flowed depending on the configuration of political forces vying for control of the state. In this regard it's no coincidence that the emergence of the Keynesian school of thought, along with its dominance over macroeconomic analysis in the quarter century following World War II, occurred in the context of the emergence and ascendance of the welfare state. But, it's important to note that the version that took root was precisely the one that did not question the, in principle, validity of a general competitive equilibrium. What made Keynesianism legitimate, as opposed to the economics of Keynes, was the fact that it acknowledged the idea that, at least under idealized conditions, the free market could work.

VI

While Keynesianism reigned during the quarter century following World War II, and coincided with the apex of the welfare state, its dominance was never secure. Indeed, it was challenged from the beginning, as pointed out in section IV above. In the meantime, the welfare state was also subject to a counterrevolution that had been

in effect since its inception but which didn't take hold until the first decade after World War II. The sources of this counterrevolution are manifold and I will only address the more obvious causes that concern the specific case of the United States. First, there's the fact that the welfare state was consolidated in the context of World War II and the subsequent cold war. The expansion of the state that took place during that era was greater than the expansion that occurred in the 1930s with the introduction of the New Deal. But, much of this growth was due to the increased military expenditures the United States incurred upon emerging as a global power during World War II and which it sustained throughout the entire cold war era. As a result, in the United States, the relatively high and growing levels of effective demand were largely nourished through militarism rather than the kind of redistributive, full employment, welfare policies which Keynes had envisioned.

Moreover, this Military Keynesianism was justified by an ideological war that pitted the free market ideas of America against the totalitarian communism of the Soviet Union. The result was an awkward combination of circumstances. On the one hand, the anti-communism of the era, reinforced by America's long standing anti-statist political traditions, kept the strictly social welfare component of the state from developing as robustly as it did in Western Europe and virtually all other advanced capitalist nations. America's welfare state, particularly when compared to the Western Europeans, has always been relatively undernourished and subject to a greater level of antipathy than is common of other capitalist states. On the other hand, the rapid growth rates and low unemployment rates characteristic of the three decades following World War II can be credited, in part, to the military component of the state. In addition, there was the fact that, particularly during the 1950s and 1960s, the United States was able to maintain a dominant position in international trade because of the greater productive capacity that had remained untouched during World War II. This combination of circumstances led to an ideological environment in which the unprecedented growth of the golden age, the quarter century following World War II, was popularly interpreted as an outcome of economic freedom and not the result of the stimulus that Military Keynesianism was administering all along.

A second, and closely related, cause for the decline of America's welfare state, had to do with the anticommunism that was being promoted not just by the state, as already noted, but by private capitalists as well. Elizabeth Fones-Wolf (1994) has argued that, starting in the 1940s, American capitalists consciously set out to sell the ideology of free enterprise in response to the growing tide of "socialism" they saw emerging out of the New Deal, the federal government's "socialistic" planning of World War II, and the growing acceptance of labor unions. To them, it appeared that free enterprise was under attack. In response, capitalists invested heavily in public relations campaigns designed to sell the virtues of free enterprise and the evils of communism.

A third reason that helps to account for the decline of America's welfare state is related to the racist heritage of American culture. The civil rights movement of the 1950s and 1960s, along with the War on Poverty and the affirmative action programs that were first instituted by the federal government in the 1960s, and which did entail an expansion of the social welfare component of the state, led to a rightist backlash among working-class whites. White working class families viewed these programs as providing an unfair advantage to minorities and women. As a result, the welfare state came to be viewed as a promoter of specific, unwarranted interests, rather than as an agency that should provide equal opportunity to all.

Lastly, some of the more important institutions that, in an earlier era, had helped to create America's welfare state and which had been a strong political base for it's continuance, began to deteriorate in the 1960s, and have been declining ever since. The most obvious case here involves the collapse of the labor movement in the United States. While never as strong a presence as in Western European democracies, the labor movement was an important force in American politics from the 1930s to the 1950s but began to decline in the 1960s. Thus, as an example, over 30% of the labor force was unionized during the 1950s, but it now stands at about 13 % of the labor force. In addition, electoral participation rates have been declining in the United States since the early 1960s, with the largest percentage declines occurring among the working classes (Miller and Traugott 1989, 3-4). As a result, the middle and upper classes, more inclined to vote conservatively, and in particular for the Republican party, have a greater relative voice in electoral choice. Moreover, the growing concentration of capital, as witnessed not only in the growing inequity in the distribution of wealth and income but in the growing concentration of mass media ownership, had the effect of narrowing the range of political discourse to rightist prescriptions (Herman and Chomsky 1988, 3-14).

VII

The collapse of the Soviet Union reinforced rightist trends that have been evolving in the United States for quite some time and which have coalesced into the Neoliberal prescriptions being advocated on a world scale. It's the outcome of a confluence of two related processes that are in continual interaction: on the one hand, the rightist discourse of the broader political community intent on dismantling the welfare state; and, on the other hand, the re-emergence, after four decades of Keynesianism, of a conservative economics that's convinced of the beneficial properties of free competitive markets and the ineffectualness of government.

At the level of practical politics, much of Neoliberalism can be viewed as a demand for the kind of self-serving policies outlined at the beginning of the third section of this paper. It carries a myopic vision that confuses the general interest of society with the interest of capital. And it comes, as Adam Smith warned over two

hundred years ago, "from an order of men, whose interest is never exactly the same with that of the public, who have generally an interest to deceive and even to oppress the public, and who accordingly have, upon many occasions, both deceived and oppressed it" (Smith, 250).

At the level of academic economics, Neoliberalism has been pushed by a growing chorus of conservative economists, mostly Monetarists, New Classicals and Public Choice theorists, who are convinced that, despite the existence of all manner of market imperfections, despite the absence of credible existence and stability proofs of a general competitive equilibrium, despite the historical record of free market economies, and despite the existence of credible theories that suggest otherwise, are convinced that free markets work best and that government should be confined to a small set of chores.

The theory of the competitive market has been refined to such an extent that it's devoid of all institutional context. The infatuation with the logical structure of self-interested exchange, in an a-historical, a-social, and a-political context, may have less to do with the needs of mathematical abstraction, than with the need of a political culture intent on developing arguments that claim to prove the limits of public authority. The problem with this is that it has led to two predictable results: one, a view of markets that prevents it's practitioners from understanding the rich institutional environment that must exist before they can be made to work; and, two, a tendency to focus on a simplistic dichotomy between markets and government that prevents the development more practical approaches to the problem of social provisioning.

By elevating the market to an ideal, conservative economists lock themselves into a false dichotomy between markets and freedom on the one hand, and government and coercion on the other. It's a dichotomy that emerges from a political culture that prevents the theorist from viewing markets and government as nothing more than human institutions that can, and should, be manipulated for the sake of the public good. The insistence on free market prescriptions comes from those who believe that markets are somehow natural institutions that will magically burst into existence once the artificial institutions of government have been dismantled or shoved aside. But, the market is no more natural than is government, and the latter is no more artificial than the former. Both institutions are the product of historical forces and both can be changed; though doing so requires paying attention to institutional complexity.

Lastly, much of the antipathy that conservative economists display toward government, particularly economists in the Public Choice tradition, is based on a very poor understanding of democracy (Tilman). The argument they make is that the market does a better job of meeting the unadulterated preferences of consumers than political democracy does in meeting the choices of citizens. The market is

thought to coordinate independent sovereign choices without the need for coercion. In contrast, democracy requires the minority to acquiesce to the choices made by the majority, which inevitably involves an element of coercion. Since government, even democratic government, is coercive, it's thought best to keep its actions limited to a narrow set of rigid rules, preventing it from exercising discretion, and thus coercion over the population. Individual freedom can only come about through the limitation of governmental authority.

The problem with this interpretation is threefold. First, democracy involves much more than simply given expression to the unadulterated choices of citizens. It involves, in the richest sense of the democratic tradition, an on-going public discourse that seeks to find the general interest and give it expression. It doesn't give expression to unadulterated preferences, but rather assumes those preferences will change as a result of the political dialogue which is at the core of a democratic culture. Second, the belief that markets do not require coercion, while majoritarian democracy does, is simply false. Third, the conservative vision of freedom is as stunted as it is uncreative. By imagining that freedom only means the absence of restraint, it's incapable of conceiving of freedom as the opportunity to exercise it, which, in turn, requires the existence of a government intent on providing the political and economic infrastructure that must be in place before freedom can be exercised.

The blind insistence on free market prescriptions that American policy elites have been demanding was bolstered by the belief, encouraged by the collapse of the Soviet Union, that the world was converging on the American view of capitalism. Governments would everywhere be shrinking in size, while free markets would spontaneously emerge from the wreckage of dismantled bureaucracies. This Neoliberal faith was forced upon the Russians, and the formerly socialist republics of Eastern Europe, during the first half of the 1990s and the results, as noted in section II above, were disastrous. Since then, these societies have responded by discarding that approach by building, instead, political economic institutions that take a more pragmatic approach to markets and a more expansive view of government than is common among conservative American economists. Rather than looking to the United States as the model, these societies are instead more interested in the lessons to be learned from the social welfare states of Western Europe and in particular Sweden (Kornai, Haggard, and Kaufman, 2001). In the meantime, the nations that have managed to survive the worst excesses of Neoliberalism, are the ones that have chosen to ignore the counsel of the International Monetary Fund and use government to guide and regulate market activity.

The new millennium may not bring about, as American conceit would have it, a convergence toward Neoliberal states, but rather the emergence of state forms that

have more in common with the social welfare states of Western Europe or the state capitalist societies of China and other east Asian countries. And to the extent that America's relative economic position begins to decline, as other nations forge ahead with a more pragmatic view of markets and government, public discourse might encourage economics to give voice to a more reasoned and less doctrinaire theory of markets and government.

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