FROM PROSPERITY TO NEOLIBERALISM. EUROPE BEFORE AND AFTER THE STRUCTURAL CRISIS OF THE 1970s

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RÉSUMÉ

DE LA PROSPÉRITÉ AU NÉOLIBÉRALISME.
L'EUROPE AVANT ET APRÈS
LA CRISE STRUCTURELLE DES ANNÉES 1970

ABSTRACT

FROM PROSPERITY TO NEOLIBERALISM.
EUROPE BEFORE AND AFTER
THE STRUCTURAL CRISIS OF THE 1970s

MOTS CLEFS : Néolibéralisme, finance, crise, politique monétaire, taux d'intérêt, classe, Union Européenne.
KEYWORDS : Neoliberalism, finance, crisis, monetary policy, interest rates, class, European Union.
J.E.L. Nomenclature: E6.

Introduction (intro)

It is common in Europe to refer to the period 1945-1974 as 30 years of prosperity, and this assessment can be extended to the United States and Japan. Not without foundations, this is particularly the case in France, where the expression "30 glorious years" (*les trente glorieuses*) has been coined. This reference to three decades of prosperity is probably a rather optimistic description of the course of events which followed World War II, since the first postwar years can be described as a period of reconstruction in Europe and Japan, and the first symptoms of a deterioration were already evident before 1974 in all major capitalist countries. But the basically favorable character of the period is, however, unquestionable.

The decade of the 1970s was quite specific in many respects, and can be caracterized as a period of *structural crisis*, with lower rates of accumulation and growth after 1974, the formation of a wave unemployment, double digit inflation rates, increased macroeconomic instability, deteriorated conditions of technical change and profitability. The recession of 1974 marked a quite significant break in the profiles of growth, technical change, and distribution, introducing to a period of overall deteriorated achievements.

Did the economy of the major capitalist countries recover from this crisis? The assessment is mitigated. The rates of capital accumulation and the growth of labor productivity remained comparatively low, but new upward trends of the productivity of capital and profitability have been asserted; an end has been put to inflation; large unemployment disappeared in the US, but is still an issue in Europe; growth remained slow everywhere, but in particular in Europe; Japan entered into a deep and lasting crisis; countries of the periphery underwent devastating crises, and there is certainly more to come; etc. A new crucial element is the assertion of *neoliberalism* since the early 1980s, and its consequences on the globalizing world economy (box 1).

Thus, concentrating on Europe, the contrast is strong between the first postwar decades and the last decades of the 20th century. In terms of growth, employment, technical change, the prosperity of the first decades appears strikingly. *The purpose of this paper is to discuss the nature and origin of this transformation: from prosperity, before the crisis of the 1970s, to mediocrity after.* Europe is obviously center stage, but none of the features of these periods can be understood independently of the relationships between the US and Europe, and the transformations of capitalism on a world scale.

The overall interpretation underlying the present study is ambitious since its purports to combine both the technical and the institutional components of these transformations, or, in a Marxist formulation, relations of production, class patterns, power configurations, and the historical tendencies of technology and distribution. A double process is at issue:

1. Europe is involved in the broad international movement of the progress of productive forces (independently of any assessement concerning its desirability and forms), with its own chronology and features, notably in relation to the US. In this respect, Europe has been faring rather well, but the general deteriorating trends from the late 1960s and early 1970s are also apparent in Europe. (One specific trait of Europe and Japan, since World War II, was certainly the process of cacthing-up with the US concerning technology and wage,

1 - Neoliberalism and Globalization (neol)

As a preliminary to this investigation, it is important to specify the use that we make of the terms "neoliberalism" and "globalisation".
The term *neoliberalism* is used in this paper to designate the new course of capitalism since the beginning of the 1980s. Important components of neoliberalism were actually implemented during the 1970s, for example the flotation of currencies and the gradual disaggregation of capital controls. The term *monetarism* was originally used to refer to the new course of macro policies: the emphasis on the definition of targeted growth rates of monetary aggregates and the determination to fight inflation at any costs. The complete failure of the first element and the importance of the second, in combination with the tight connection between all the various aspects of the new emerging order, domestically and internationally, suggest to consider the label *monetarism* as a terminological by-product of this chain of events, now outdated.
Neoliberalism and *globalization* are two distinct phenomena. As has been often contended, globalization refers to an old trend in capitalism in the direction of its internationalization. Neoliberalism defines a new configuration, *domestic* as well as international, in which the interests and power of capitalist ownership have been restored: a new discipline of labor and management (or corporate governance); deregulation in some respects (those contributing to the freedom of action of large corporations and capitalists), reregulation in others (with respect to the fight against inflation); the financialization of capitalism (within the "nonfinancial" sector, and as manifest in the rise of financial institutions); a determination to tap profits from workers in general and to pump income from the periphery along new lines. The link between the two notions is that neoliberalism defines a new phase and new forms of globalization (distinct from the old forms such as colonial empires). The crucial features are the *globalization of neoliberalism*, toward Europe (as discussed in this paper), Japan, and the periphery (as evident in the recurrent financial crises of the 1990s), and the new configuration of US hegemony, including its new military component, more than globalization in general.

which was not interrupted by the overall lower performances of the 1970s and following decades.)

2. The initial tolerance toward rather radical alternative frameworks of development (social democracy, macro stimulative policies, intervention of the state...) questioning the preeminence of the capitalist class — the outcome of the specific postwar political conditions (in particular, the context of the coldwar) — were a crucial factor of postwar prosperity but came gradually to an end. This followed from the transformation of these political conditions and the opportunity opened to ruling classes by the crisis of the 1970s to strengthen their grasp on the economy and society in general, leading finally to the consecration of the dominance of the owners of the means of production, within the new neoliberal order, and new patterns of US hegemony. This contemporary configuration of power is not favorable to growth, even more in Europe than in the US.

1 - Outline and summary of the major conclusions (paoutres)

• Section 2 is devoted to growth and the long-term trends of technology and distribution: a description and a first set of interpretations. Three European countries are considered, France, Germany, and the United Kingdom, later abusively designated as "Europe", and generally treated globally in this section. The profiles observed for these countries are compared to similar measurements for the US. Then, these movements are placed in historical perspective, in the context of the secular evolution of the US economy, allowing for the identification of a first set of causes of postwar prosperity. The main conclusions are as follows:

1. Abstracting from the 1950s, when the US grew slowly, the growth rates in Europe and the US remained of similar intensity until the end of the 1970s. During the two decades of neoliberalism, the 1980s and 1990s, the US grew more rapidly. The major phenomenon was the gradual catching-up of Europe with US levels of labor productivity and wages, achieved through an also progressive movement toward about the same levels of mechanization.

2. In spite of this catching-up, the profiles of capital productivity and profit rate appear quite similar in the two zones. The changing trends define a periodization in two stages: a first phase of decline from the 1960s into the early 1980s, and the new upward trends since the early 1980s. The period extending from the second half of the 1970s to the first years of the 1980s, a period of low profitability, was marked by the structural crisis, resulting from the earlier deteriotating performances.

3. The postwar years of prosperity must be understood as the effect of the extension to Europe of the new technological and distributional trends, originating in the US at the transition between the 19th and 20th centuries. They were the expression of the new framework of capitalist relations of production, in particular the *managerial revolution*, which superseded the traditional features *à la Marx* of technical change as in the industrialization of the second half of the 19th century, in which the rise of labor productivity is only obtained at the cost of large investment in fixed capital. The Great Depression and World War II accelerated this transformation in the US. Europe and Japan caught up with these new trends after the war, completely or to a large extent.

4. The favorable effect of the assertion of the new technology and organization — new management in the broad sense — came to an end in the 1960s or 1970s, depending on the countries, industries, or sectors. This occurred when Europe and Japan were well advanced in their catching up. Technical change gradually recovered its typical features, with a declining profit rate, causing the crisis in the 1970s and early 1980s in all major capitalist countries.

5. Since the mid-1980s, new technological trends are underway. The growth rates of labor productivity remain comparatively small, in particular in the US, but the productivity of capital and profit rate are now trended upward. These movements reflect new technical and organizational trends in line with the performances of the first half of the 20th century in the US.

• Section 3 discusses another set of transformations concerning the flows of financial incomes and the financing of accumulation. The focus is on the features of neoliberalism. The followings are noteworthy:

1. The rise of neoliberalism was manifest in the large flows of interest and dividends transferred from enterprises to the wealthiest fractions of the population, whose income had been comparatively diminished during the 1970s. In addition large amounts of interest were paid by the state and a fraction of households in debt to the same groups. Income was pumped from the countries of the periphery.

2. The assertion of new patterns of financing, from the 1980s onward, defines another striking feature of neoliberalism. The main transformation was the reduction of borrowings. The net issuance of shares (shares issued minus shares purchased) remained, and is still, insignificant in the global financing of nonfinancial corporations. Under neoliberalism, investment is self-financed, as has been the case in the US since World War II. The consequences for investment are severe, and explain why the underlying restoration of profit rates before income transfers did not materialize into a large investment.

3. Besides the above explanation of *the poor performances of neoliberalism concerning growth*, these features provide a second crucial interpretation concerning the *nature of neoliberalism*, a system targeted to the income and wealth of ruling classes rather than growth *per se*, or employment.

• Section 4 locates the above observations within the social frameworks which made the prosperity of the postwar decades possible, contributing to the favorable technical and distributional trends already mentioned:

1. The history of capitalism can be viewed as a sequence of power configurations, such as financial hegemony or the postwar social compromise, labeled the *Keynesian compromise*. Neoliberalism is such a configuration, with a new hegemony of finance (box 2).

2. The first decades which followed the Great Depression and World War II can be characterized as periods of broad social compromise. Besides the improved condition of salaried workers, the power of finance was diminished in favor of increased managerial autonomy, in connection to the rising role of state officials. In addition to macro policies, this framework of *managerial capitalism* in the US led, in other major capitalist countries, to alternative frameworks, in which income and financing was channelled toward nonfinancial corporations, with a large state intervention targeted toward a capital allocation favorable to growth (industrial policy) — precisely what neoliberalism reversed. There was an international component to this configuration, inherited from the Bretton Woods agreements. Domestically and internationally, there was a large Keynesian inspiration.

3. The importance of these frameworks is clearly illustrated by the devastating consequences of their destruction, in particular within developing countries. The lack of control on national financial and monetary mechanisms, as a consequence of the globalization of the neoliberal order, prohibits stable development and appears detrimental to development in general.

• Section 5 is devoted to the rise of neoliberalism, globally within major capitalist countries and in Europe in particular. Clearly, the economy provided the economic conditions of a political struggle, in which capitalist owners, managerial classes, and workers were involved. The tensions among the ruling classes of the main capitalist countries were also crucial. The main interpretations are the followings:

1. The 1970s can be viewed as a period of transition, with the dislocation of the Bretton Woods order. A number of economic developments are at issue in the explanation of these events, notably: (1) the partial catching-up of Japan and Europe with the US, and the

2 - Finance (finan)

The notion of *finance* plays a central role in this study. Finance is portrayed as an "actor" in the history of capitalism, whose role was central in the emergence of neoliberalism. Independently of the well-known problems posed by the reference to such a broad social collective force in the analysis of history, an obvious extreme simplification, it is necessary to understand the content we give to this entity.

By finance, we simultaneously mean the upper fraction of the owners of the means of production and the institutions in which the power attached to this property is concentrated. This refers to a specific stage of capitalism in which ownership and management (in particular, the management of nonfinancial corporations) are separated. As a result of this separation, the property of the means of production on a large scale became "financial", at a distance from the firms and materialized in portfolios of securities. In this context, exercising the power of ownership becomes a crucial issue, and financial institutions play a central role in this respect.

Thus, the notion of finance, as used in this study, does not refer to the traditional distinction between a financial and a nonfinancial sector. Financial institutions are, however, a component of finance.

corresponding external deficit in this latter country; (2) the crisis of the 1970s and the wave of inflation. The outcome of the "crisis of the dollar" was the suspension of its convertibility into gold and the flotation of currencies. These first steps were followed by the gradual suppression of capital controls. Internationally, the stage had been set for neoliberalism, and the first act was already in process.

2. In spite of its fundamental nature, this economic perspective appears limited when these events are considered in relation to the political move of finance in direction of the reassertion of its privileges (reduced in the wake of the Great Depression and war). The economy defines the conditions in which this fight for the preservation of the power of capitalist ownership was waged since the late 19th century when modern finance emerged.

3. Considered from this angle, the Bretton Woods order appears restropectively as a crucial but shaky conquest in a battle which was never thoroughly won. This is clearly revealed by a more detailed analysis of the vicissitudes of its implementation and actual functioning. The destruction of capital controls was a decisive element in the reassertion of capitalist power.

4. Europe, as Japan, was a central piece in this complex chain of events. The necessities of the cold war imposed a large tolerance from capitalist classes and the US, now the new unchallenged hegemon. But the situations of each country were significantly distinct, economically and politically, with a large legacy of history:

- In spite of the temporary access to power of the Labour party, Britain remained constantly under the sway of financial interests, with the ambition to restore London as a financial place paving the way for neoliberalism, finally realized by Margaret Thatcher.
- Germany always acted in favor of monetary orthodoxy and price stability. The German mark conquered the position of international transaction and reserve currency, and Germany the status of a financial place. Besides the trauma of the 1920s, and the features of *social market economics*, this attitude probably reflects the characteristics of a country in which capital is basically held as *loan capital*. The temporary practice of controls responded to the desire of protecting the country from world turbulences,

as was the decisive action in favor of the monetary union, without questioning the possible role of Germany in international monetary and financial mechanisms.

- France, traditionally a country of large state interventionism, moved gradually toward the framework of free-market economy in the context of unifying Europe. This movement had been largely performed when Mitterand was elected in 1981, on a program at odds with the new monetarist and neoliberal trends. In complete contradiction with the gradual insertion of the country in Europe and a world deeply involved in the evolution described earlier, France more or less perfunctorily called for the collaboration of Germany and Britain to isolate Europe. It faced a rebuttal, and executed its well-known about-face.

5. The econonomic unification of Europe was gradually realized concerning trade among the various countries in the Union (originally, the Common Market); a monetary union was also developed in a stepwise fashion, culminating in the creation of a common currency, the euro. Conversely, no *financial Europe* was ever established. From its origin, the liberalization of financial mechanisms, the free mobility of capital, was promoted on a world basis — a great victory of European and international finance. In this context, no autonomous policy was possible without facing the sanction of the so-called "markets", and it was consequently impossible to resist the gradual implementation of neoliberalism, despite its specific traits prevailing in Europe (due to the partial success of people resistance to the destruction of social protection).

2 - Postwar prosperity, structural crisis in the 1970s, new trends from the mid-1980s (palt)

Section 2.1 compares the performances of three European countries and the US since the 1960s, concerning growth, technology, and distribution. Then, section 2.2 provides an interpretation of the favorable traits of the earlier postwar decades, the crisis years of the 1970s, and the ensuing limited recovery.

2.1 Growth, technology and distribution (stgrowtech)

2.1.1 Growth. The comparative rise of the US in the 1980s and 1990s (ssgrowth)

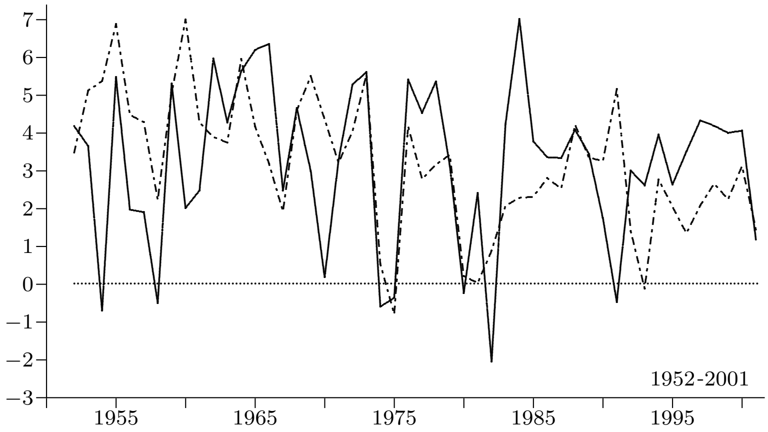
Figure 1 shows the growth rates of the GDP for the aggregate of the three European countries and the US. The US grew at comparatively low rates during the 1950s. One can, then, observe the large average rates prevailing during the 1960s (4.3% in Europe and 4.4% in the US), in line with the previous decade for Europe. The ensuing decline (respectively 3.2% and 3.0% during the 1970s) is also demonstrated. No clear restoration is evident. [*Il faut pousser aussi loin que possible pour voir la rechute aux États-Unis*]

Figure 2 plots the relative size of the three countries in comparison to the US, in the aggregate and for each country taken separately.[1] This figure shows that after 1960, the European product did not increase relatively to the US, fluctuating around 60%. It then declined to 49% in 2000. Only France grew comparatively to the US, culminating in 1975 or 1982 at about 20%, before diminishing. This figure also shows that, abstracting from the German reunification, this relative European decline was prolonged during the two later neoliberal decades, in accordance with the observations in figure 1 of comparatively larger growth rates in the US.

There are obviously other differences between the profiles of output, or patterns of growth in general, among these various countries. For example, the relative importance of the manufacturing sector in Germany is often emphasized. The comparison between the US and Germany in this respect is, however, not easy. Besides the differences in the series available per industry, it is also clear that the division between manufacturing and trade (wholesale and retail trade) signals a distinct division of tasks among sectors rather than actually different proportions of outputs. In the 1990s, the total *manufacturing plus trade* represented similar percentages of about 40% of total output in the two countries, signaling an apparently larger delegation of commercial activity to a specific trade industry in the US. This characteristic of the US economy is probably equally relevant concerning services, with larger fractions of services to business delegated to particular enterprises in the US. It is also often contended that the German economy is oriented toward exportations. A large excedent of trade was, indeed, observed for Germany during the 1980s, while the US suffered a deficit (figure 11). This dramatic positive balance of foreign trade in Germany was, however, quite specific of this decade. As is well known, the actually distinct profiles are characteristic of the US and Japan, since the beginning of the 1980s. Although these

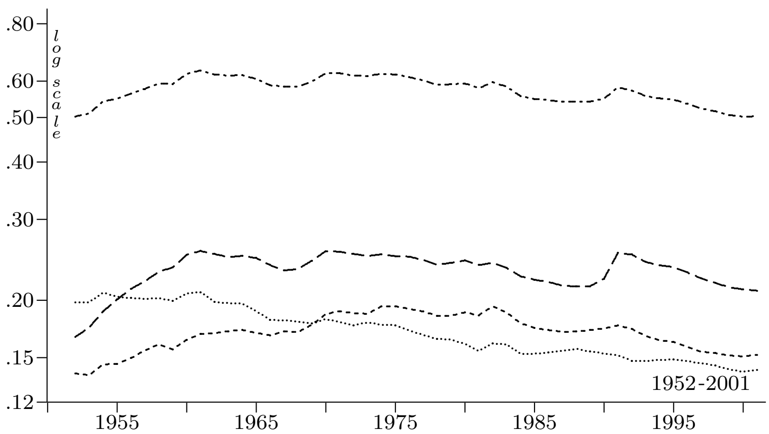
1. In 1929, the three European countries represented 71% of the US economy. At the beginning of the 1950s, they only amounted to 50%.

Figure 1 Growth rates of GDP (%) (pncroib)



Sources: OECD, Economic Outlook, and Angus Maddison.

Figure 2 Ratio of the GDP of each country to that of the US (%) (pntailb)



Europe: (-·–·-); France: (-----); Germany: (— —); United Kingdom: (·········)

In this figure, GDPs are measured using *purchasing power parity* exchange rates (definition in figure 13). A logarithmic scale is used for legibility. The distances between the lines are, thus, proportional to their ratio instead of their difference. The sudden rise in the 1990s for Germany corresponds to the reunification.
Sources: idem.

structural differences certainly matter, their impact should not be overemphasized. As is confirmed by the data in the following section, the similarities between the various countries are strong. This does not prejudge, however, of other differences (concerning financial mechanisms, corporate governance, or state interventions) that will be discussed in section 4.

2.1.2 Technology and distribution. Catching-up (sstech)

The profit rate plays a central role in the dynamics of capitalist countries, and is a crucial variable in the periodization of capitalism. Figure 3 shows the profit rate for the US and Europe. It is the ratio of a broad measure of profits (the Net Domestic Product minus the total compensation of labor) to the stock of fixed capital (net of depreciation). Thus, this measure of profitability abstracts from the payment of taxes and any financial mechanism (in particular, the flows of interest and dividends). The profit rate diminishes into the 1970s and then recovers from about 1983 onward.[2]

One can notice incidentally the decline of the profit rate in the last years in the US. The profit rate culminated in 1998 and 1999; the figures for 2000 and 2001 are lower. (This is the combined effect of the rise of the labor cost and the diminished activity in the recession.)

Despite minor differences, the similarity between the two profiles is striking. This observation is all the more interesting that it concerns several of the variables involved in the determination of the profit rate, r, *i.e.*: the productivities of labor and capital, P_L and P_K, and the real wage (total labor cost), w. Both labor productivity and labor are expressed per hour worked. The relationship is the following:

$$r = \frac{\text{Profits}}{\text{Fixed capital}} = P_K \left(1 - \frac{w}{P_L}\right)$$

Table 1 provides the growth rates of these variables for the US and Europe, before and after the structural crisis. In the computation of the *relative levels*, P_L, w, and K/L, are expressed using *purchasing power parity* exchange rates (definition in figure 13).

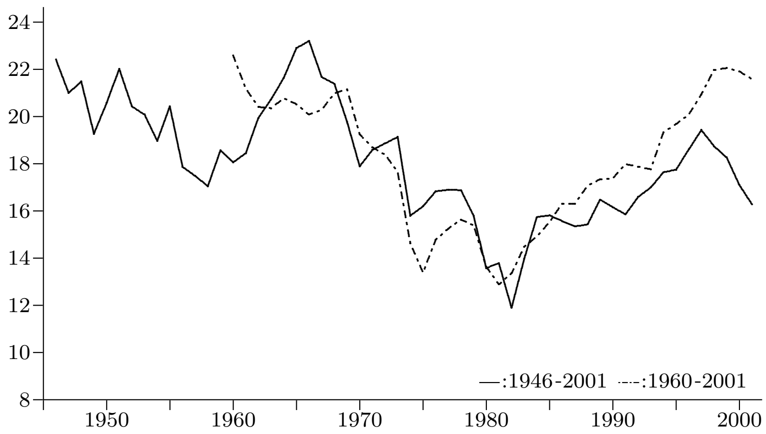
Two types of comments must be made. First, besides the profit rate, the successive decline, prior to the structural crisis, and recovery, after, are evident for the productivity of capital. Second, the profile of evolution of labor productivity and the wage rate is distinct from the above, but similar in each country: The growth of these two variables consistently slowed down, without recovering during the latter period.[3] Thus, the overall profile is similar in the US and Europe, but does not match the pattern in two stages.

Table 1 also displays the ratios of the variables for Europe to their value in the US. At issue is the catching-up. Contrary to what was observed with respect to growth and, therefore, the relative sizes of the various economies, the table reveals a very strong catching-up of Europe with respect to the US concerning the capital-labor ratio, labor productivity, and wages. This process is still going on during the 1980s and 1990s.

A first striking expression of this catching-up is the variation of the comparative levels of labor productivity. In 1960, the hourly productivity of labor in Europe represented 60%

2. G. Duménil, D. Lévy, "The Profit Rate: Where and How Much Did It Fall? Did It Recover? (USA 1948-2000)", *Review of Radical Political Economy*, 34 (2002), p. 437-461.
3. The rise of the growth rate of labor productivity in the US is only apparent since 1995, when productivity is measured per hour, and still quite limited.

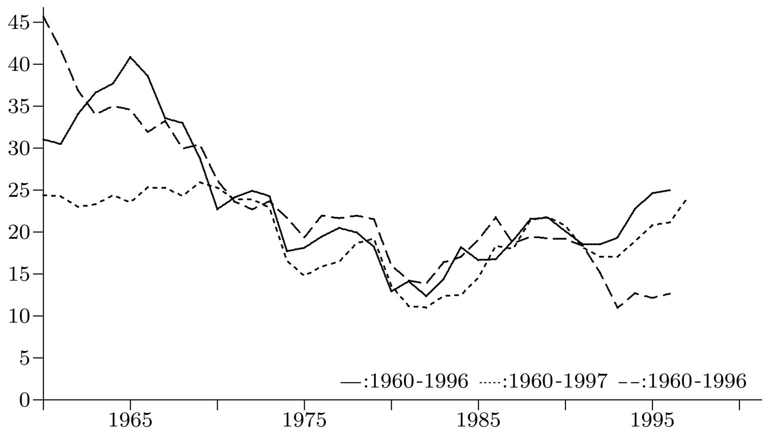
Figure 3 Profit rates in the total private sector (%) (pnrtot)



United States: (——); Europe: (·-·-)

Profit rate = (Net product − Labor compensation)/Fixed capital
Sources: Europe, Various data bases of OECD; US, BEA.

Figure 4 Profit rates within manufacturing industries (%) (pnrman)



United States: (——); France: (-----); Germany: (— —)

Profit rate = (Net product − Labor compensation)/Fixed capital
Source: OECD.

Table 1 (pntech) - Technical and distributional trends
US and Europe, private sector (averages per period)

	US *Growth rates (%)*		Europe *Growth rates (%)*		Europe/US *Relative levels*	
	60-73	*84-98*	*60-73*	*84-98*	*60-73*	*84-98*
P_L	2.90	1.48	5.03	2.35	0.68	1.03
w	2.47	1.17	5.40	1.50	0.33	0.50
P_K	−0.35	0.96	−1.39	1.04	0.89	0.92
K/L	2.56	0.66	6.05	2.42	0.69	1.16
r	−0.08	1.52	−2.27	2.71	0.94	1.06

Sources: Europe, OECD; US, BEA.

of that of US. In 1998, the ratio was 107%. Second, it appears clearly that this was obtained as a result of a strong process of capital investment relatively to labor. In 1960, the capital-labor ratio for Europe represented 53% of its value in the US, to be compared with 129% in 1998.[4] Finally, this third block of the table also shows that the ratio of the profit rates and capital productivity were not significantly altered, despite the transformations of the trends of these two variables.

A more detailed analysis by industries would obviously reveal additional differences between industries and countries. But the similarity among the various patterns of evolution appears very strong, even puzzling. Thus, figure 4 compares the profit rates of the manufacturing industries of the US, Germany, and France in the same definition as in figure 3. Both the levels of the profit rates and the profiles of evolution are very close in the three countries, despite the underlying catching-up process. No country can claim outstanding achievements in this respect. (One can note that France only joined the common trend in 1970 and that Germany significantly declines in the 1990s.)

2.1.3 A common profile. A smaller Europe catches up (ssperiod)

A number of important observations emerge from this analysis:

1. In spite of the technological and wage gap between the two territories, the growth rates in the US and in Europe were comparatively large during the first decades following World War II, as were the profit rates. Then, growth rates and profit rates diminished significantly.

2. Concerning growth the catching-up of Europe with the US appears limited to the 1950s. An opposite process, strengthening the superiority of the US, was characteristic of the 1980s and 1990s. Conversely, Europe gradually adjusted its technical capabilities to those of the US.

3. A periodization in two stages is manifest in the profile of the profit rate and capital productivity, with successively a decline, and a rise of these two variables. This pattern is

4. This very strong figure might be subject to the fact that we use the purchasing power parity exchange rate for the total GDP (instead of a specific rate for capital goods, which would be more appropriate but does not exist).

not apparent concerning labor productivity, wages, and growth, whose growth rates have been rather consistently diminishing.

2.2 Before and after the crisis of the 1970s (stinter)

2.2.1 The postwar boom and the European catching-up in historical perspective (ssboom)

The profit rate is a crucial variable in the interpretation of the long-term movements of capitalist economies, as suggested by Marx more than a century ago. It commands the rhythms of accumulation, since profits are simultaneously the objective and a source of accumulation. The levels and trends of profit rates also influence the stability of the macroeconomy (the succession of overheatings and recessions) since they impact on the decisions of firms.

An analysis of historical trends reveals the existence of periods of actual declines of the profit rate, several decades long. These periods are separated by phases of recovery, of similar duration. Considering the US economy since the Civil War, four such periods can be distinguished. A first phase of decline is observed up to approximately World War I; then a phase of recovery stretches from this war to the first decades following World War II; this phase was apparently interrupted by the Great Depression because profit rates fall in any contraction of the economy as a result of the low utilization of productive capacity, but the depression actually accelerated the elimination of the older, less efficient, fraction of the economy and, thus, contributed to the restoration of the profit rate; in the second half of the 1960s, the profit rate entered the new phase of decline which has been documented in section 2.1.2; then the phase of recovery is observed since the early 1980s.

At a broad level of analysis, and still concentrating on the US, the cause of the prosperity which followed World War II was the large levels of profitability reached after World War II. They were, themselves, the outcome of the favorable pattern of technical change which prevailed during the first half of the 20th century (that the Great Depression only hid). Contrary to the standard profile of evolution of the profit rate that can be labeled *à la Marx*, in which the progress of labor productivity is obtained at the cost of large investment in fixed capital, the rapid gains of labor productivity during the first half of the 20th century only required limited additions to the stock of fixed capital. The typical example of such technical achievements is the assembly line. Although is can be viewed as a strong process of mechanization, the intensive and efficient use of the equipment did not materialize in a sharp rise of the capital-labor ratio; contrary to standard patterns *à la Marx*, the productivity of capital increased instead of declining. The profit rate actually rose in spite of the larger growth rates of the labor cost.[5]

The conditions conducive to this rise of the profit rate in the US are, however, broader than the transformation of technology and organization within the workshop of manufacturing enterprises. They relate to a major change in the dynamics of US capitalism which

5. Contrary to the thesis of the French Regulation school (R. Boyer, *The Regulation School. A Critical Introduction*, New York: Columbia University Press (1989)), we do not see in the rise of wages after World War II a cause of the postwar prosperity, but one of its effects. (The favorable profile of technological change created the *possibility* for the rise of the wage rate, which was demanded by workers, and represented a component of what can be called the *Keynesian compromise*.)

occurred at the transition between the 19th and 20th centuries. The separation between ownership and management in the new framework of capitalist institutions, allowed simultaneously for: (1) the corporate revolution (manifest in the large incorporation and merger wave), (2) the emergence of modern finance (box 2); (3) the managerial revolution (linked to the rise of managerial and clerical personnel). The managerial revolution was manifest in the new organization and technology of firms. It affected all aspects of their activity (production, commercialization, financing...) and spread gradually from transportations and communications to all sectors of the economy. The gradual improvement and diffusion to the entire economy required several decades and was simultaneously a fundamental cause and effect of the Great Depression. Although the exhaustion of the favorable consequences of this transformation occurred rapidly after World War II, profit rates remained large during several decades, as the pattern of technical change progressively returned to its earlier features.

A similar evolution occurred in Europe and Japan with a lag of several decades, possibly half a century. The gradual involvement of these countries in these new forms of organization and technology was a crucial factor in the assertion of similar trends in these countries, manifested in their catching-up with the US. This does not mean, however, that the chronology of the various components of these transformations (the managerial, corporate, and financial revolutions) was identical. As will be contended in section 4, these countries also developed or pursued alternative frameworks, specific patterns of financing, and a large involvement of the state — all developments that were made possible by the international monetary and financial rules of Bretton Woods — and which largely contributed to the postwar achievements.

2.2.2 The crisis of the 1970s (sscrisis)

It is a general feature of the historical dynamics of capitalism that each phase of decline of the profit rate was followed by a period of *structural crisis*: basically, diminished rates of accumulation and larger macroeconomic instability. Following the first phase of decline of the profit rate, two large recessions occurred in the late 19th century, during the 1870s and 1890s (separated in the US by the boom which followed the return to convertibility in 1880). Important financial perturbations were also observed. Abstracting from the Great Depression, that was of a distinct nature, a second similar structural crisis occurred at the end of the second phase of actual decline of the profit rate after World War II, during the 1970s. In combination with diminished rates of accumulation and the corresponding wave of structural unemployment (beginning around 1975), this crisis was manifested in an increased instability of the general level of activity evident from 1970 to the early 1980s. Simultaneously, given other features of the period, inflation soared (figure 12).

The decline of accumulation which resulted from the fall of the profit was of similar amplitude in the US and in Europe. The wave of unemployment was larger and more persistent in Europe in relation to the continuing process of catching-up, with larger increase of the capital-labor ratio and labor productivity in Europe (table 1).[6]

6. Total employment can be written: $L = K/(K/L)$. The rise of the capital-labor ratio, K/L, diminishes the degree in which accumulation, the increase of K, materialises in employment, L.

2.2.3 The new trends and sluggish growth (ssreco)

The last phase, whose most significant expression is the rise of the profit rate as shown in figure 3, is reminiscent of the transformations which occurred at the transition between the 19th and 20th centuries in the US. The growth rate of the capital-labor ratio diminished and the productivity of capital began to rise although labor productivity remained stagnating (table 1).

We interpret this new phase as a revolution in management (in the broad sense in which we use the term, encompassing organization and technology). There is a technical aspect to this revolution, since the new technologies of information and communications are typically the technologies of management itself: the collection, treatment, and circulation of information. This technical aspect must, however, be understood as a component of a more comprehensive transformation, in which organization and the procedures of management themselves are involved. They act in combination with the new discipline of labor: its flexibility, its intensification, and the stagnating or reduced labor compensation. Management itself was subjected to a new discipline.

There is apparently a paradoxical element in the features of this latter phase of capitalism. It is that the new favorable trends of technology (the rising productivity of capital) did not lead to increased rates of accumulation and growth as could have been expected. The crucial point here is that the profit rate presented in figure 3 is measured before taxes and all financial incomes and expenses. Two diverging evolutions are observed in this respect. First, the burden of taxation on the profitability of nonfinancial corporations was gradually diminished (at least in the US); second, neoliberalism considerably modified the channels by which profits are susceptible of stimulating accumulation. In particular, profit rates measured after the payment of interests and dividends did not recover. (The measure of the capital is correspondingly adjusted to the net worth of corporations.) The description of these new financial mechanisms is the object of section 3.

3 - Changing income flows and patterns of financing. What neoliberalism is about (paincfin)

This section discusses the specific traits of the 1980s and 1990s, the two decades of neoliberalism. Neoliberalism upset radically the flows of incomes and the mechanisms which govern the accumulation of capital, in particular the patterns of financing of corporations. The previous section already emphasized the upward trends of the profit rate, in the broad definition of figure 3, and the slow growth of wages. But the focus here will be more on the channels of the incomes deriving from profits in a broad definition, and their aptitude to finance sufficient savings, accumulation, and growth. The *nature* of neoliberalism is directly at issue.

The analysis of these financial mechanisms is particularly difficult and touches the inner features of the various economies considered in their similarity and diversity. The section provides some information and measurements concerning the US, France, and Germany, from which rather strong conclusions are derived given the limitations of our measurements. It is, therefore, important to stress here the provisional and incomplete character of the investigation.

Section 3.1 is devoted to the channels of formation of the income of upper classes, and section 3.2 to the financing of accumulation in this context.

3.1 Distributing corporate profits. Collecting interests from the state and households (stinco)

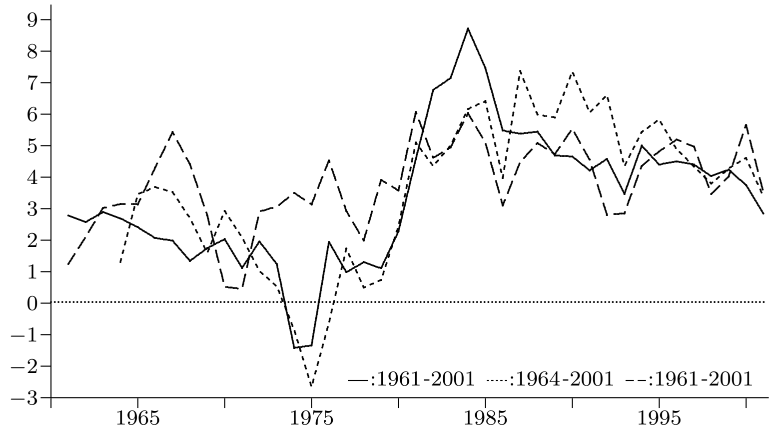
Even before the recovery of profit rates in the mid-1980s, neoliberalism thoroughly modified the formation of incomes to the benefit of upper classes. There are two aspects to this mechanism. First, profits were lavishly distributed to the financial sector and to rich households, *via* the payment of interest and dividends; second, the rise of interest rates also resulted in large payments from the state and households in debt, as well as countries of the periphery, to the benefit of the same agents.

The most conspicuous element in this evolution was the *1979 coup*, when the decision was made by the Federal Reserve to increase interest rates to any levels required to put an end to inflation. This measure proved very efficient, but had devastating consequences, both domestically and internationally.

Figure 5 shows the profile of real interest rates in the US, France, and Germany. A very sharp break is clearly apparent in 1981[7], separating two periods of comparatively low and large real interest rates. In addition, one can observe the distinct profile for Germany during the 1970s. In the US and France, these rates became negative because of the efforts to fight the crisis, resulting in low nominal rates in comparison to inflation. This was not the case in Germany, where prices rose less than in other major capitalist countries (figure 12). This defines a first specific feature of this country.

7. Real interest rates are equal to nominal interest rates minus the inflation rate. The decision to increase interest rates was taken at the end of 1979. The effect on real interest rates is only observable in 1981, because the impact on inflation was not immediate.

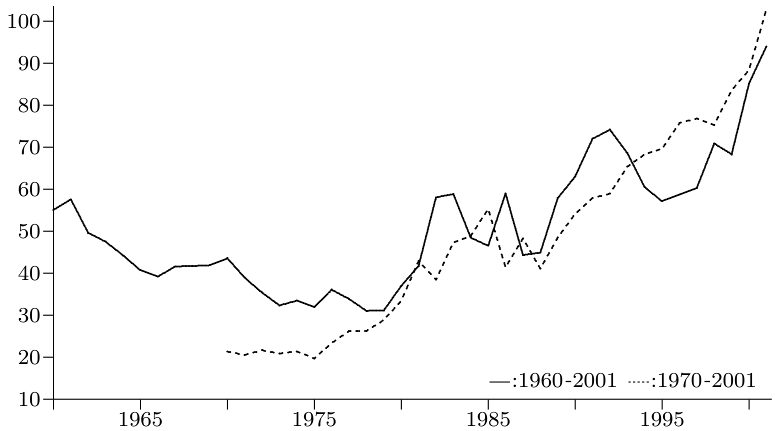
Figure 5 Long-term real interest rates (%) (pnint)



United States: (——); France: (-----); Germany: (— —)

Source: OECD, Economic Outlook.

Figure 6 The share of profits of nonfinancial corporations distributed as dividends (%) (pndiv)



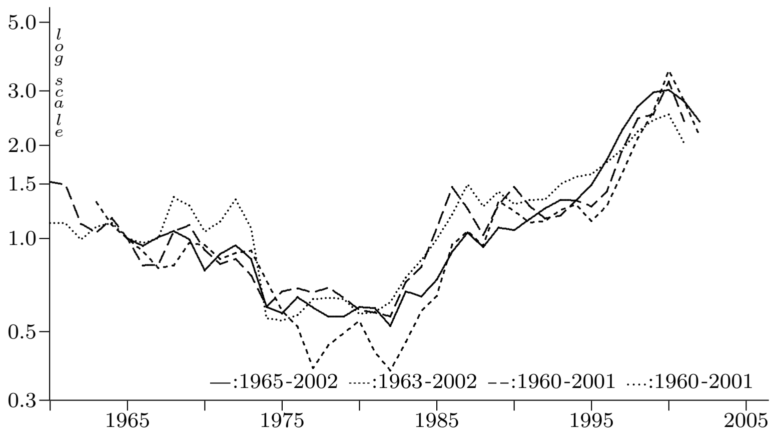
United States: (——); France: (-----)

Profits are measured after the payment of interests and taxes, and taking acccount of the devaluation of the net debt by inflation. This correction is described in the appendix to G. Duménil, D. Lévy, "The Real and Financial Components of Profitability (USA 1948-2000)", *Review of Radical Political Economy*, 36 (2004), p. 82-110
Sources: France, INSEE; US, BEA.

The rise of interest rates rendered the burden of the debt of the state unbearable, creating (in France), or considerably increasing (in the US), the deficits of the budget. These flows of income benefited to all categories of lenders, individuals or institutional. We documented the amplitude of these movements in other works.[8] The transfer of income from Third-World countries was also huge, with the consequences which have often been described.[9]

Simultaneously to the rise of real interest rates, the transformation of corporate governance under neoliberalism (the new discipline of management toward the interest of shareholders) resulted in larger distributions of profits as dividends. This is shown in figure 6 which describes the share of profits (after corporate tax) distributed as dividends, in the US and France. Again the establishment of new income flows appears strikingly.

Figure 7 Indexes of stock market deflated for inflation (1975=1) (pnbou)



United States: (——); France: (-----); Germany: (— —); United Kingdom: (········)

The series are deflated for inflation using the inflation rate in each country. In the US, the level in this measure was 2.74 at the end of the first quarter of 2002.
Source: OECD, Main Economic Indicators.

This new corporate governance targeted to the market value of corporations on the stock market produced the expected result. The price of shares rose to considerable extent. This is clearly demonstrated in figure 7, which shows the stock-market indexes, corrected for inflation in the US, France, Germany, United Kingdom, normalized to 1 in 1965. The similarity in the movements is striking. One can first observe the fall into the crisis of the

8. G. Duménil, D. Lévy, *Crise et sortie de crise. Ordre et désordres néolibéraux*, Paris: Presses Universitaires de France (2000); "Costs and Benefits of Neoliberalism. A class analysis", *Review of International Political Economy*, 8 (2001), p. 578-607.

9. E. Toussaint, *Your Money or Your Life! The Tyranny of Global Finance*, London: Pluto Press (1999). In a recent interview, Volcker confessed that, when the decision was made, there was little concern about its consequences other than domestic (An Interview with Paul Volcker, by Perry Mehrling, Barnard College, Columbia University, New York (2000)). See Helmut Schmidt's comment on Ronald Reagan lack of understanding and concern about these issues (H. Schmidt, *Men and Powers. A Political Retrospective*, New York: Ramdom House (1989), p. 272).

1970s, the rise in the early 1990s, and finally the bubble in the second half of the 1990s, and the ensuing decline.

As can be expected, these new flows of income and capital gains had considerable consequences on the wealth of the richest households. Even before the assertion of the new trends of the profit rate, these transformation restored the privileges of upper classes, which had been eroded during the 1970s.[10]

3.2 Financing accumulation (stfinan)

The proportions in which profits are paid out, in interest and dividends, are not neutral. One could have expected that these sums, once distributed, are then ploughed back within nonfinancial corporations. Actually, it is possible to show that everything, within neoliberalism, and considering the economy globally, happens *as if* this were not the case. These profits, depending on the countries, led to increased savings without domestic investment, or to consumption. Obviously, this consumption is not necessarily or totally that of the recipients. They can be invested within financial institutions, in the country or abroad, and finance or indirectly allow for additional unproductive lending.

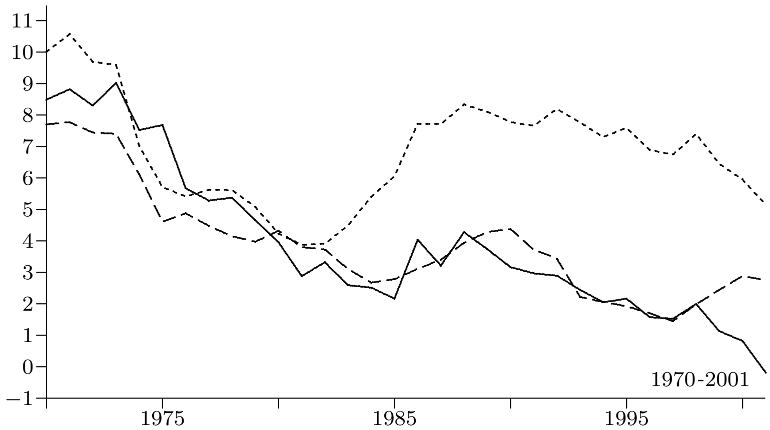
Figure 8 illustrates such puzzling patterns in the case of France. Two profit rates are plotted, both after the payment of taxes (capital is measured as the net worth of corporations). In the first measure (-----), interest and dividends are still included within profits. The large recovery of the profit rate in France is clearly demonstrated. In the second measure (——), net interest and dividends have been subtracted, and most of the recovery disappears as a result of such payments. One can also notice that the growth rate of the stock of fixed capital in real terms, or the rate of accumulation (— —), is closely related to this second measure of the profit rate. The superposition of the two curves until 1985 reflects the rather stable structure of financing; the distance in the following year mirrors the attempt by corporations to get out of debt. Overall, the benefits of the new rising trends of the profit rate, in a measure which abstracts from the two major channels of distribution of profits, have been entirely lost for accumulation following their distribution. The same very stable relationship is observed in the US, from 1960 to 1995.[11]

Figure 9 decomposes the three sources of the financing of gross investment for France: gross retained earnings (— —), the issuance of shares (-----) (issued minus purchased), and the variation of the net debt (——). The succession of the various periods is clearly evident, with an important reliance on borrowings before 1985 and the new pattern of self-financing in the following years. One can even notice the negative rates of self-financing (when the variation of the net debt becomes negative) in the later decade, that testifies of the violence of the efforts to get out of debt. Thus, between 1970 and the early 1980s, firms were resorting to borrowing to finance investment in rather constant proportions: about one third of total investment as shown in figure 9. This favorable patterns disappears during the 1980s and 1990s, until the very last years of the century.

A similar transformation occurred in Germany, a country in which borrowings represented an important component of the financing of the activity of nonfinancial corporations. Figure 10 shows that, from 1965 to 1980, these corporations financed about one third of

10. G. Duménil, D. Lévy, “Costs and Benefits”, *op. cit.* note 8.
11. The recent divergence between (——) and (— —) is even larger in the US than in France. It will be discussed in another work.

Figure 8 Rate of profit abstracting from the flows of interest and dividends, rate of retained profits (considering these flows), and accumulation rate (%): France, nonfinancial corporations (pnracc)



Rate of profit abstracting from interest and dividends: (-----); Rate of retained profits (considering these flows): (——); Accumulation rate: (— —)

Corporations simultaneously receive and pay interest and dividends, although they pay more. The second measure (——) considers the net flows (paid minus received). The burden of interest and dividends payments is measured by the distance between the two series (-----) and (——). Profits, in both definitions of the profit rates, are divided by net worth, and a correction is made for the devaluation of the net debt by inflation. The *accumulation rate* (— —) is the growth rate of the stock of fixed capital, net of depreciation. This figure uses a logarithmic scale on the vertical axis, and the distances between the curves are, thus, proportional to the ratios among the various rates.
Source: INSEE.

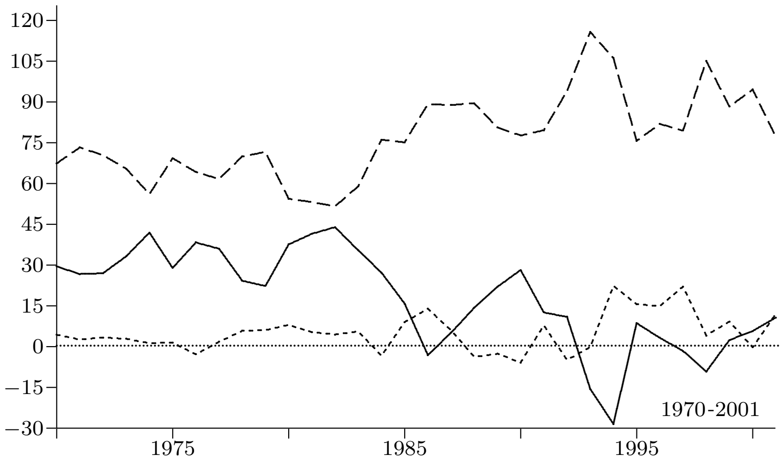
their nonfinancial assets (fixed capital and inventories) by borrowings. The charge of interest (corrected for inflation) amounted in the 1970s to 3.2% of the value of these nonfinancial assets. With neoliberalism, the burden of interest paid by nonfinancial corporations nearly doubled (to about 5% of nonfinancial assets), while the net debt declined from 31% of nonfinancial assets, during the second half of the 1960s, to practically 10% in 1995, as shown in the figure. The date of the transformation (first half of the 1980s) is the same as the case of France, and the amplitude similar. A new step forward was accomplished in the 1990s, again as in France.

It is interesting to compare these new neoliberal patterns of financing to the situation prevailing in the US. In this country, these patterns were not upset by the implementation of neoliberalism since they always prevailed since World War II (investment was consistently self-financed). This is a crucial element in the explanation of the different impacts of neoliberalism in the US and in Europe, more generally in all countries in which borrowings were an important source of financing of real investment. Japan represents an extreme case in this respect.[12]

It is not obvious to understand why *self-financing* represents the traditional US source of financing, and why it constitutes now a pillar of neoliberalism. Considering the economy

12. G. Duménil, D. Lévy, Imposing the Neoliberal Order. Four Historical Configurations (US, Europe, Japan, and Korea), Cepremap, Modem, Paris (2001).

Figure 9 Proportions of the three sources of financing of gross investment in their total (%): France, nonfinancial corporations (pnsour)



Variation of the net debt: (——); Net issuance of shares: (-----); Gross retained earnings: (— —)

Both in *gross investment* and *gross retained earnings*, *gross* means including the depreciation of fixed capital. Corporations simultaneously issue and purchase shares, and borrow and increase their monetary or financial assets. "Net" in this context means *after deducting* the purchase of shares or the increase of monetary or financial assets.
Source: INSEE.

Figure 10 Ratio of net liabilities to nonfinancial assets (%): Germany, nonfinancial corporations (pnndg)

The net liabilities, or net debt, are the excess of real (nonfinancial) assets on the net worth of corporations or, equivalently, the excess of the debt on financial assets.
Source: OECD, Nonfinancial Enterprises Financial Statements.

globally, the issuance of new shares does not contribute significantly to the financing of the economy. Shares are issued, but also purchased by corporations, either their own shares or the shares of other corporations. Overall, and taking account of all these contradictory flows, the contribution is close to zero in the US. It is probably easier to understand why corporations do not want to rely largely on borrowings in the context of large interest rates.[13]

To sum up, in the interpretation of the comparatively low levels of investment, before and under neoliberalism, the decline of the profit rate and the large flows of interest and dividends payed appear as crucial factors (as shown in figure 8). Little is left within corporations for the self-financing of investment. In addition, corporations do not want to resort to borrowings given the large real interest rates, nor do they want to "dilute" the owership, by issuing new shares. The maximizing of the value of the firm on the stock market seems to be at issue. At a broader level of generality, one can contrast to social systems: (1) a first configuration in which profits largely remained within corporations under managerial control, and were generously invested; (2) the neoliberal configuration in which profits are lavishly distributed and management is targeted to the maximizing of the shares of the firm in the stock market (not the total market value of the firm, but the value of individual shares).

3.3 The nature and purpose of neoliberalism (stneol)

The identification of these new flows of income and patterns of financing is a crucial element in the interpretation of neoliberalism. Neoliberalism defines a new course of capitalism, in which the income, wealth, and power of finance has been reasserted. Its purpose is not growth or accumulation of fixed capital *per se*. Even during the worst years of the crisis of the 1970s, new flows of income were directed toward finance, in total contempt for the ensuing consequences concerning growth and employment in the major capitalist countries and in the countries of the periphery. Now that new profitability trends have been asserted, they do not lead to larger growth rates.

Neoliberal propaganda is based on the following sophisms: (1) the US is the country were neoliberalism reaches the highest degree of achievement; (2) this country grew more than other major capitalist countries during the 1990s; (3) other economies must imitate the US. The same line of argument is applied to countries of the periphery hurt by the monetary and financial crises that neoliberalism itself created. The truth is rather: (1) neoliberalism is targeted to the maximizing of the income and wealth of ruling classes; (2) it is not favorable to growth even in the US but hurt less this economy because its basic rules of functioning were less distant from neoliberal patterns than in other countries; (3) the superior achievements of the US in terms of growth during the 1990s, in comparison to others, can be largely imputed to the domination of this economy (in particular the domination of the dollar), and cannot be exported.

The consequences of neoliberalism on major capitalist countries, in particular other than the US, cannot, however, be understood exclusively in relation to patterns of financing. These patterns only represent one expression of the specific features, or "models", which allowed for the growth of these countries during the earlier decades and their catching-up (in terms of technology and wages) with the US. This broadening of the framework of analysis is the object of the following section.

13. The total debt of corporations is large, but not their net debt (debt minus financial assets), because large corporations tend to act more as financial intermediaries, to engage in financial business.

4 - Growth, progress, and power (pagropow)

Besides the various phases marked by the successive trends of technology and distribution, as well as the flows of income and sources of financing, as recalled in the previous sections, it is also possible to detect in the history of capitalism a sequence of configurations, corresponding to the various patterns in which class power is exercised: Who dominates? Which compromises are passed? Etc. Neoliberalism represents such a configuration. The purpose of section 4.1 is to place in historical perspective not only neoliberalism, but also the previous phase often referred to as the *Keynesian compromise*, an expression which does not convey the diversity of its components and variants in various countries. Section 4.2 outlines the main features of these alternative frameworks which preceded neoliberalism, in their domestic and international aspects. Section 4.3 contrasts the conditions in which the catching-up of Europe and Japan were accomplished during the first decades following World War II with the situation of the countries of the periphery presently attempting to adjust their economy and society to the framework of globalizing neoliberalism.

4.1 Historical background (sthistor)

The three "revolutions"—corporate, managerial, and financial—which occurred in the US at the transition between the 19th and 20th centuries led to a first hegemony of *finance*, the major capitalist owners separated from management and the financial institutions in which the power of ownership is embodied (box 2). Although management enjoyed a large autonomy at the beginning of the 20th century, finance reigned with little contest on monetary and financial mechanisms currently expanding at an unprecedented pace. Despite the creation of the Federal Reserve in 1913, the traditional orthodox rules of finance prevailed, with more concern for price stability, the convertibility of fiduciary money, and the stability of financial institutions, than for the actual management of the macroeconomy. The basic framework was that of the *gold standard*, domestically and internationally, although monetary mechanisms were gaining a gradual and irrerversible autonomy from gold.

Already in those years, the US were progressively asserting the foundations of what would become their supremacy over Britain and the rest of the world. Abstracting from the rise of real socialism, other countries were developping along rather specific trajectories (as, for example, Germany or Japan).

As is well known, the Great Depression unsettled the hegemony of finance, in the context of the gradual assertion of new social and political trends, linked to the progress of the labor movement and to the rise of managerial and clerical personnels (a configuration often referred to as the *New Deal Coalition*). These transformations resulted in various frameworks, which can be interpreted as complex combinations of: Keynesianism (the transfer of the control of the macroeconomy to the state); the welfare state and the increased involvement of the state in education and research; social democracy (with a degree of participation of unions and "workers" parties to power); state intervention in industry (including the nationalization of large segments of finance or nonfinancial corporations); new rules governing international monetary and financial mechanisms; etc.

One general feature of these frameworks is that they corresponded to specific class compromises. Capitalist owners were not deprived of their income or power, though their prerogatives were limited; the power of managerial personnel, both private and public, was strengthened; salaried workers acquired a number of guarantees and protections, although their basic relation to capital was not altered. Relevant to the present investigation, is the fact that these post-World War II configurations appear restrospectively favorable to growth and industrialization. The situation was, however, reversed when a new hegemony of finance was imposed, as in neoliberalism, under US leadership.

4.2 Alternative frameworks conducive to industrialization and growth (staltern)

4.2.1 Domestic components (ssdomest)

As recalled in section 2.1, the first decades following World War II coincided with comparatively large growth rates in the major capitalist countries, and the rapid catching-up of Europe and Japan concerning technology and wages. A basic factor was the favorable trends of technical change and the ensuing large values of the profit rate (section 2.2.1), which allowed simultaneously for large accumulation rates and a steady rise of wages. Europe and Japan followed the avenue opened in the US.

Europe and Japan benefited from a considerable autonomy, which allowed them to develop specific institutional and policy frameworks favorable to development:

1. A first trait was the heavy reliance on lending to finance the growth of nonfinancial corporations (documented in section 3.2 for France and Germany). This reliance had two specific characters: (1) a macroeconomic component: loans were provided under favorable conditions, *i.e.*, low rates of interest (in particular low rates of real interest as a result of inflation); (2) an industrial component: states intervened actively in the allocation of capital toward sectors of the activities (energy, public utilities, import substitution, exports, etc.), whose role was judged crucial in the industrialization of these countries and their insertion in the world economy.[14] In some instances, the property of large segments of the economy was transferred to the state. The low cost of credit posed a difficult problem

14. John Zysman's early analysis (*Governments, Markets, and Growth. Financial Systems and the Politics of Industrial Change*, Ithaca: Cornell University Press (1983)) of these frameworks hinges around the relationship between financial systems and the comparative openings for state intervention and their forms. He distinguishes between three frameworks: "Japan, like France, has a credit-based, price-administered financial system [...] Germany is the one example of a credit-based, bank-dominated system [...]. The United States [*and Britain*] [...] has a capital market-based financial system" (p. 233). The degree to which the state can intervene in industry diminishes from the first to the third framework. A strong interference of what Zysman calls the "bureaucracy" is congenial to the first model, where prices are administered, conditioned to the cooperation of large banks in the second, and practically impossible in the third. The singularity of German capitalism is striking, in particular the extremely low fraction of the financial assets of corporations held by households under the form of shares (J. Story, "Globalisation, European Union and German Financial Reform: The Political Economy of "Finanzplatz Deutschand"", *in* G. Underhill (ed.), *The New World Order in International Finance*, New York: St Martin's Press, 1997, p. 245-273). The role of the central bank is well defined in E. Kennedy, *The Bundesbank. Germany's Central Bank in the International Monetary System*, New York: Council of Foreign Relation Press (1991), ch. 3. See also: R. Deeg, *Finance Capital Unveiled. Banks and the German Political Economy*, Ann Arbor: The University of Michigan Press (1999); W. Streeck, K. Yamamura, *The Origins of Nonliberal Capitalism. Germany and Japan in Comparison*, Ithaca: Cornell

concerning the profitability of the banking system[15], which could be nationalized (as in France) or benefit from favorable lending conditions from the central bank (as in Germany). The case of Japan and the MITI has often been discussed.[16] Overall, the features of these systems can be summarized as a large reliance on borrowings at a low cost, supplemented by the accompanying measures required by the functioning of financial institutions; state intervention biased profitability to the advantage of nonfinancial corporations in general, and specific industries in particular (for example, by providing cheap credit or energy).

2. Activity in the economy was encouraged by stimulative macro policies. This stimulation was already a natural consequence of the above frameworks, but could also be conducted independently or in the absence of such devices. Cheap credit and large state expenses tended to stimulate the activity, even to overstimulate it, potentially with inflationary consequences. Exchange rates were periodically readjusted. They were actually maintained at levels favorable to exportations, in spite of the necessity of importing equipment and energy at nonprohibitive costs. This is where the international component of these mechanisms comes into play.[17]

3. The efficiency of these policies was strengthened considerably by active intervention concerning health, education, research, etc., tending to create a broader dynamic of social progress and equality.

4.2.2 The international monetary and financial order of Bretton Woods (ssbrett)

All the above would have been impossible without the Bretton Woods system devised at the end of World War II, and did not survive to the destruction of this framework. A major concern in the project was to avoid a contraction of international trade similar to that which occurred during the 1930s. This required the provision of credit in strong currencies to countries facing a disequilibrium, and a capacity for each country to maintain policies of macroeconomic stimulation.

Capitals tend, however, to flow from one place to another responding to interest rates differentials and in anticipation of modifications of exchange rates, and these movements prohibit independent national macro policies. For this reason, the implementation of strict limits to capital mobility was a crucial component of the Bretton Woods system as envisioned by Keynes. This was clearly stated by Keynes in one of his intervention in the House of Lords in May 1944, where he discussed the Bretton Woods agreements. Keynes linked the "power to control the domestic rate of interest so as to secure cheap money" to

University Press (2001). One can also consult the interesting collection of essays by Michael Loriaux concerning France, Spain, Mexico, Japan, and Korea (*Capital Ungoverned. Liberalizing Finance in Interventionist States*, Ithaca: Cornell University Press (1999)).

15. The computation of the profit rate of the financial sector of the French economy leads to negative values, a situation which was reversed during the neoliberal decades (G. Duménil, D. Lévy, "Costs and Benefits", *op. cit.* note 8).

16. See C. Johnson, *MITI and the Japanese Miracle: The Growth of Industrial Policy, 1925-1975*, Stanford: Stanford University Press (1982).

17. This second point in this list represents the specifically *Keynesian* component of these frameworks. It is important to recall, however, that Keynes put forward a very broad and ambitious program of reforms, which refers to the third aspect below. References are given in James Crotty's informative article: "On Keynes and Capital Flight", *Journal of Economic Literature*, XXI (1983), p. 59-65.

capital controls: "Not merely as a feature of the transition, but as a permanent arrangement, the plan accords to every member government the explicit right to control all capital movements. What used to be a heresy is now endorsed as orthodox".[18]

After heavy amendment, the Bretton Woods agreements acknowledged the principle of the implementation of controls, which were later never fully accepted. Practically, this recognition of controls in the accord and the necessities of the period resulted in a complex structure of such devices, permanent or temporary, reglementary or fiscal.[19] Although, exchange rates were fixed, the various currencies were adjusted recurrently (typically devaluing with respect to the dollar), another prerequisite to the conduct of autonomous macro policies. These adjustments were realized at rather low exchange rates in comparison to the dollar, given comparative price levels (figure 13).

4.3 The devastations caused by globalizing neoliberalism (stperip)

Nothing illustrates more strikingly the benefits of this *de facto* Bretton Woods order than the consequences of its gradual destruction during the 1970s and the rise of neoliberalism during the 1980s. These advantages appear even more conspicuously, negatively so to say, when contrasted with the "development model" that the IMF attempts to impose on countries of the periphery.

Since the early 1980s, most of the countries which followed the recipes of the IMF did not fare well. For example, after the crisis of the debt, the growth rate of Mexico was divided by nearly three and stagnated at this level, with a marked increased instability. It is too early to say if the large growth rates of Korea will be destroyed, or if this country will continue to grow rapidly but suffer a large macroeconomic instability. The damage caused to this economy are, however, unquestionable. Argentina, after stagnating during the 1980s, enjoyed half a decade of growth but entered a wild crisis at the end of the century.

An examination of the major macro variables for these countries shows that the neoliberal order leads them inescapably to crisis. In Argentina, for example, the turn to neoliberal policies (with the currency board established in 1991) proved efficient to fight inflation but at the cost of rising external deficits (as in Mexico), rising interest rates, and the explosion of the external debt — all symptoms of the unsustainable character of the new course. This policy was pursued during a number of years, thanks to the flows of

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18. J.M. Keynes, "Bretton Woods and After, April 1944-March 1946" (1944), *The Collected Writings of John Maynard Keynes, Vol. XXVI*, p. 17, London: Macmillan, St Martin's Press for the Royal Economic Society, 1980. The second part of this extract is cited in E. Helleiner, *States and the Reemergence of Global Finance. From Bretton Woods to the 1990s*, Ithaca: Cornell University Press (1994). Concerning Keynes and the movements of capital, James Crotty ("On Keynes and Capital Flight", *op. cit.* note 17) refers to Keynes' article: J.M. Keynes, *National Self-Sufficiency, The Collected Writings of John Maynard Keynes, Vol. XXI, p. 233-246*, London: Macmillan, St Martin's Press for the Royal Economic Society (1933). The Bretton Woods System is called by the official historian of the IMF, Margaret De Vries, the *par value system* (*The International Monetary Fund, 1972-1978. Cooperation on trial. Volume I: Narrative and Analysis*, Washington: International Monetary Fund (1985)). In a section entitled *How the System Worked*, capital controls are not presented as a key component of the system, only the gradual relaxation of these controls is put forward. This official assessment can be described as the exact opposite of Keynes appreciation.

19. J. Nembhard, *Capital Control, Financial Regulation, and Industrial Policy in South Korea and Brazil*, Westport: Preager (1996), ch. 2, *History and Use of Capital Controls*.

foreign capitals taking advantage of large interest rates and a fixed exchange rate (with the growing "risk premium"), which fed currency reserves otherwise depleted by the deficit of trade. As in all of these countries, these capitals left the countries when the threat of the obviously pending crisis materialized, precipitating its occurrence.

This example demonstrates that a country must keep the control of its currency, be able to adjust its rate of exchange, and not thoroughly rely on volatile flows of capital to replenish its reserves. The difficulties to impose domestic anti-inflationary policies cannot be superseded by the imposition of a drastically overvalued currency. Contrary to what is often contended, the flows of foreign direct investment are not necessarily discouraged by the limitations to capital mobility when basic favorable conditions exist. These flows were very large in Europe during the Bretton Woods years, in spite of such limitations. Conversely, capital flights can be partially discouraged by capital controls.

The liberalization of capital movements within a zone which unites together countries of similar levels of development, or between zones which share common characteristics, is one thing. But no process of development or catching-up, such as the one undertaken by Europe after World War II, can be achieved in the absence of the mechanisms ensuring the control of its currency by a less developed country. Obviously, this condition is not sufficient. (Macro policies are not sufficient to explain how Europe or Japan developed after World War II.)

5 - The rise of neoliberalism. The insertion of Europe in globalizing neoliberalism (parise)

It is difficult to date the emergence of neoliberalism. The 1979 coup represents certainly an emblematic moment in this process, but the gradual dislocation of the Bretton Woods system during the 1970s can be described as a first phase in which many of the new traits emerged.[20] The complexity of this analysis is further increased by the important differences among countries. On one side, the leading role played by the US and Britain is well known. Did Germany's fear of inflation paved the way for neoliberalism in Europe? France had already joined the march toward monetary and financial orthodoxy, when Mitterand was elected at the beginning of the 1980s with a program at odds with the neoliberal agenda. What forces commanded the reversal? What was the role of the Monetary Union?

An important preliminary to this investigation would be the characterization of the specific features of capitalism in each of these countries, economically and politically (as briefly sketched in section 4.2.1). This refers, in particular, to the mechanisms by which the property of the means of production is exercised (the channels such as loans or shares, the degrees and forms of the concentration of securities within financial institutions, their distribution among households...), and the corresponding powers and social compromises (corporate governance, the direction of the action of the state...). In the absence of such a framework, what follows must be considered as directions of research.

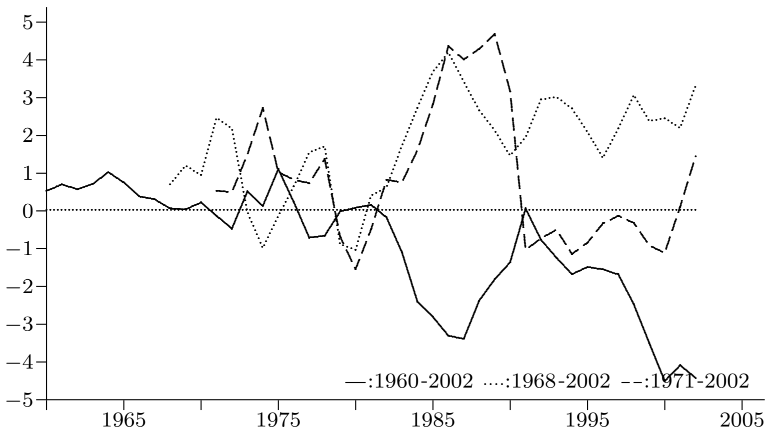
Section 5.1 first locates the rise of neoliberalism in a broad, historical and international, perspective in which Europe tends to be considered as a global entity confronting the US. Section 5.2 focuses on Britain, Germany, and France considered separately. Section 5.3 suggests a few conclusions.

5.1 The US and unifying Europe (sthisint)

The first step in the gradual assertion of neoliberalism was the dislocation of the Bretton Woods framework. At issue is a set of economic conditions, in which the relative position of the US in comparison to other major capitalist countries is central. These events were immediately followed by the deepening of the structural crisis during the 1970s, with the rise of inflation. But these economic circumstances only provided the conditions which made possible the assertion of the new hegemony of finance, a political development that must be understood in the context of the succession of power configurations introduced earlier for the US.

20. The transformations of capitalism in the 1970s led Susan Strange to define the notion of *Casino Capitalism*. See the synthesis in her chapter 1 (*Casino Capitalism*, Oxford: Basil Blackwell (1986)) and the first chapter of the new book (*Mad Money. When Markets Outgrow Governments*, Ann Arbor: The University of Michigan Press (1998)), entitled *The Casino image gone mad*.

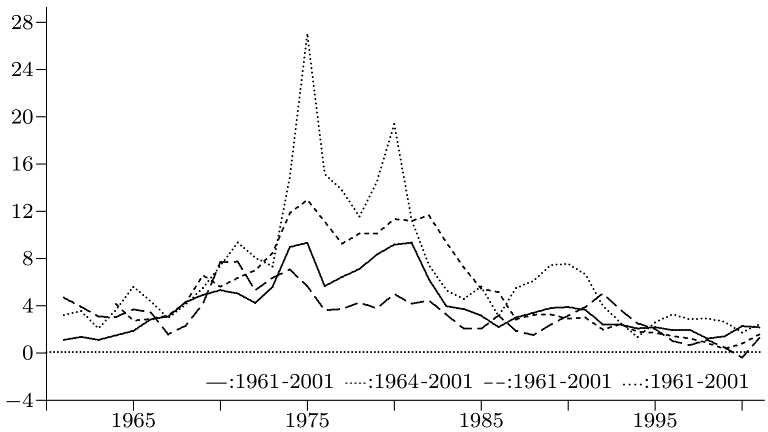
Figure 11 Net exports as a percentage of GDP (%) (pndef)



United States: (——); Japan: (·······); Germany: (— —)

Source: OECD, Economic Outlook.

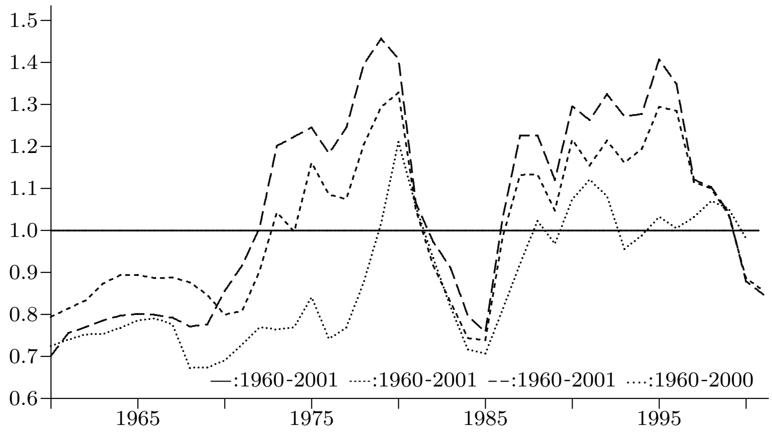
Figure 12 Inflation rates (%) (pninfl)



United States: (——); France: (-----); Germany: (— —); United Kingdom: (·······)

Inflation is measured as the growth rate of the GDP deflator.
Source: idem.

Figure 13 Ratio of actual exchange rate to purchasing power parity exchange rates in comparison to the US (pnexch)



United States: (——); France: (-----); Germany: (— —); United Kingdom: (·········)

This ratio is larger than 1 when a currency is overvalued, and inferior, when it is undervalued. *Purchasing power parity exchanges rates* are fictitious exchanges rates which equalize the price of a same broad bundle of commodities in the two countries.
Source: OECD, Economic Outlook.

5.1.1 The catching-up, the dollar crisis, the structural crisis, and the internationalization of capital (ssecofac)

As shown in figure 11, the US maintained during the 1960s (actually since World War II), an excess of exports over imports.[21] This excess began to diminish during the second half of the 1960s, giving way in 1970 and 1971 to deficits. This new situation was the effect of the gradual catching-up of the main competitors of the US. Retrospectively, these deficits appear quite limited, but the newness of the phenomenon caused considerable emotion. Other countries, such as Japan and Germany, were in the average running surpluses, and the US became an international borrower. Those years were also marked by the first steps of what became in the ensuing years a large wave of inflation (figure 12). During the 1960s, the inflation rate in the US remained low and inferior to that of other major capitalist countries but, at the end of the decade, prices were rising in the US at the same accelerating pace as in most European countries, and faster than in Germany.[22]

Traditionally, Japan and most European countries were adjusting their exchange rates by devaluing their currency, because of inflation rates larger than in the US. The opposite adjustment was now required. The US asked other countries to adjust their currency upward, since a devaluation of the dollar seemed impossible. As they refused this quite unusual correction, some of these countries had to face incoming flows of capital, which were judged inflationary and feared as such. These countries were finally forced to let

21. From the end of the war to 1972, both imports and exports represented about 5% of GDP. This percentage increased suddenly to about 9%, and went on rising afterward up to 14% for exports and 18% for imports.
22. Concerning the role of inflation, domestic and on primary products, see D. Calleo, *The Imperious Economy*, Cambridge: Harvard University Press (1982), ch. 6.

their currency float. As is well known, the result of the crisis was the suspension of the convertibility of the dollar, its flotation and *de facto* devaluation. (A more detailed account of these developments is given in section 5.1.3.)

The amplitude of the adjustment is illustrated in figure 13, which shows an indicator of the relative values of currencies in comparison to the dollar. It is the ratio of actual exchange rates to purchasing power parity exchange rates. (A value above 1 indicates an overvaluation.) The direction and amplitude of the adjustment are clearly depicted in the figure, with the franc and the mark moving suddenly from undervaluation to overvaluation at the beginning of the 1970s[23], the relative value of the pound vis-à-vis the dollar being provisionally conserved. Thus, it appears that the effects of the Smithsonian agreement (December 1971) were short-lived.[24]

One can also notice in the figure the relative stability of these real exchange rates prior to the flotation. (Note that the subsequent movements downward and upward refer to the rise of the dollar in the early 1980s and its ensuing correction in the wake of the Plaza meeting in September 1985.[25])

The floating of currencies represented a first component of what would become neoliberalism. It also signaled, from the origin, the adjustment in favor of the US or, equivalently, the end of the earlier undervaluation of European currencies favorable to the zone. This first development was rapidly followed by the alleviation or suppression of capital controls. In 1974, the US removed the controls it had established during the 1960s.[26] They were followed in by Britain, Germany, and France. The world was entering a new phase with the rise of the new international deregulated financial framework of the *eurocurrencies*, and the rising importance and power of multinational corporations. The surge of inflation and, more generally, the failure of Keynesian policies to confront the problems posed by the structural crisis, created the conditions for a new step forward: the 1979 coup at the end of the decade, accompained by the increased discipline imposed on labor and management (the new corporate governance).

5.1.2 Finance's return to hegemony (ssretheg)

The economy set the stage, in a variety of respects, for a broad transformation of capitalism, but the fundamentally political nature of the rise of neoliberalism is obvious.

Abstracting from differences among countries, and with special relevance for the US and the United Kingdom, the financial repression, which had followed the Great Depression and World War II and led to the establishment of the postwar framework, never meant a complete defeat of financial interests. The Bretton Woods agreements were already the

23. This *de facto* devaluation of the dollar certainly contributed to the size of the recovery of the US economy after the 1974 crisis, significantly larger than in other major capitalist countries.

24. Originally, the US sought an average 12-15% depreciation with respect to other major currency. In the wake of the meeting the fall had been reduced to 8%. But there was more to come, in particular a new devaluation of 10% in February 1973 (J. Odell, *U.S. International Monetary Policy. Markets, Power, and Ideas as Sources of Change*, Princeton: Princeton University Press (1982), ch. 4-5).

25. R. Henning, *Macroeconomic Diplomacy in the 1980s*, London: Croom Helm (1987), ch. IV. Concerning the pressures exercised by business groups on the administration during the rise of the dollar, see I. Destler, R. Henning, *Dollar Politics: Exchange Rate Policymaking in the United States*, Washington: Institute for International Economics (1989), p. 124.

26. J. Hawley, *Dollars and Borders. U.S. Government Attempts to Restrict Capital Flows, 1960-1980*, London: M.E. Sharpe, Inc. (1987), ch. 5.

expression of a rather unstable compromise. New York bankers had strongly opposed the plan, and defended their alternative *key currency plan*, expressing their aversion toward regulations, and their option in favor of the free international mobility of capitals.

The restrictions placed on the international mobility of capital remained a constant object of controversy from the war onward. Subtle distinctions between good and bad capital flows were at issue. Finance, notably in the US, opposed to any type of controls, in particular cooperative controls in which the country affected by the flight of capital and the country receiving these flows were supposed to cooperate; controls were criticized as mechanisms tending to hinder or delay necessary adjustments[27]; etc. A huge debate developed concerning *euromarkets*, that the US (the Federal Reserve)[28] and European countries attempted to regulate in the first phases of their development. Finance was, however, able to impose its view and interests in the last instance, and deregulated financial operations were implemented even on US territory. In the early 1970s, a favorable terrain had already been prepared for the assertion of a new course of events.

All alternative socio-economic frameworks posed a threat on this international strategy of finance. A struggle was fought in the US against the social compromise of the first decades following World War II, following from the depression and the war. But Europe represented another threat, besides Japan and Third World countries. Several European countries were balancing between free-market capitalism and various forms of social-democracy or "socialism". The political conditions were uncertain, and they required a tolerant and patient action. In spite of the features of the various frameworks described in section 4.2.1, the postwar situation was consolidated to the advantage of capitalism. One important exception was the attempt by the French socialists, after the election of Mitterand in 1981, to turn their back to the ongoing process of integration into the neoliberal world, and to strengthen the grasp of the state on the economy and promote policies of demand stimulation. But, in the context of the rise of monetarism and neoliberalism in Britain and the conservative policy of Germany, this attempt was defeated.

The link between business interests and the political arena has been the object of much investigation. In all instances, the states played a crucial role in the emergence of the new global framework of neoliberalism.[29] Several studies also documented the narrow relationship between this fight of finance, on domestic and international grounds, and the new vigor of the old theoretical frameworks which had been temporarily discredited by the Great Depression and the rise of Keynesianism. The convergence became rapidly evident

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27. G. Haberler, "The Case Against Capital Controls for Balance of Payments Reasons", *in* A. Swoboda (ed.), *Capital Movements and their Controls*, Leiden: A.W. Sijthoff, 1976, p. 63-78.
28. J. Hawley, *Dollars and Borders, op. cit.* note 26, ch. 7.
29. In addition to E. Helleiner, *States and the Reemergence, op. cit.* note 18, see J. Hawley, *Dollars and Borders, op. cit.* note 26, ch. 8, entitled *State Policy and Business Interests*; S. Strange, *Casino Capitalism, op. cit.* note 20, ch. 1. At issue is the rivalry or cooperation of the various states, their autonomy and the possible emergence of a type of transnational state, at least representing the interests of the major capitalist countries. This was the content given to the notion of *trilateralism*, that Stephen Gill defines as follows: "For the purposes of this book 'Trilateralism' can be defined as the project of developing an organic (or relatively permanent) alliance between the major capitalist states, with the aim of promoting (or sustaining) a stable form of world order which is congenial to their dominant interests. More specifically, this involves a commitment to a more-or-less liberal international economic order." (*American Hegemony and the Trilateral Commission*, Cambridge: Cambridge University Press (1990), p. 1). Note that US hegemony is now more on the agenda than "trilateralism".

between the efforts of business and academics (the former financing the latter).[30]

At the end of the 1970s, a large convergence of opinions originated, in the US, from the rising doubts concerning the international hegemony of the country: economically, politically, and militarily. Such circumstances paved the way for the election of Ronald Reagan.[31]

5.1.3 US-Europe: A closer look at the fragile order of capital controls (sseurdol)

The fragility of the Bretton Woods[32] order was already apparent during the crisis of 1947. In spite of the signature of the Bretton Woods agreements, the rules of the game were not well established yet. After the war, economic recovery resulted in growing deficits and large flights of capital occurred from Europe toward the US.[33] New York bankers refused to cooperate with European governments to limit these flows and, instead, insisted to obtain a relaxation of controls. Their suggestion was that deflationary policies were the only sane procedure to prevent capital flights! The crisis stopped the efforts of Britain to restore rapidly convertibility. The deficits were at the origin of the *European Recovery Programme*, a US contribution to the reconstruction of Europe.

This first episode acted strongly in favor of the establishment of strong unilateral controls, to which the US government did not oppose, in conformity with the Bretton Woods agreements, and given the fears inspired by real socialism. These events opened a first phase in the Atlantic monetary and financial relations. In the following years, the US did not push in favor of an exceedingly rapid return to convertibility, and when this return was achieved in December 1958 for all major European currencies, it remained partial in its application, and capital controls were not lifted.[34]

A strong movement in favor of liberalization was, however, developing. Only the possibility of the controls had been acknowledged at Bretton Woods and they were never really recognized as a fundamental trait of a system destined to last over decades. The free movement of capitals was already an explicit target of the treaty of Rome in 1957

30. As early as April 1947, Hayek created the *Société du Mont Pélerin*, to which Milton Friedman participated. Hayek had described capital controls as "the decisive advance on the path to totalitarianism and the suppression of individual liberty" or "the complete delivery of the individual to the tyranny of the state, the final suppression of all means of escape — not merely for the rich, but for everybody." (F.A. Hayek, *The Road to Serfdom* (1944), Chicago: The University of Chicago Press (1980)). The sympathy of US finance (in contrast with the rest of business) for a high dollar and the floating of currencies is well known (on this latter issue, see I. Destler, R. Henning, *Dollar Politics, op. cit.* note 25, p. 131).

31. T. Ferguson, *Golden Rule. The Investment Theory of Party Competition and the Logic of Money-Driven Political Systems*, Chicago: The University of Chicago (1995).

32. Concerning Bretton Woods and the movement toward liberalization of capital flows, this study owes a lot to Eric Helleiner's outstanding analysis: *States and the Reemergence, op. cit.* note 18.

33. Alan Milward (*The Reconstruction of Western Europe, 1945-51*, Berkeley: University of California Press (1984)) explains the crisis of 1947 not by the "deteriorating economic situation of the European economies [...]. It was, on the contrary, attributable to the remarkable speed and success of western Europe's economic recovery" (p. 465), which caused the deficits.

34. Actually, the return to external convertibility resulted in large flows of capital, in particular short-term capital. This led to the strengthening or creation of devices to curb these movements. Notably, in september 1964, the US imposed a tax on the purchase by residents of foreign bonds and stocks. In 1965, the tax was extended to bank loans. After 1965, these controls were increased. See M. De Vries, "A Convertible Currency World", *in* K. Horsefield (ed.), *The International Monetary Fund, 1945-1965. Twenty Years of International Monetary Cooperation, Volume II: Analysis*, Washington: International Monetary Fund, 1969, p. 280-296.

establishing the *European Economic Community*. When the OECD was created in 1961, a *Code of Liberalisation of Capital Movements* was defined.[35]

A significant breach in the system was the emergence of *euromarkets*. This represented another important episode in the relationships between US and Europe. The conditions which led to this innovation in the late 1950s in Britain are sketched in section 5.2.1, which recalls that the development of these deregulated markets was a central element in the strategy of Britain to restore its role as international monetary and financial place. It was also viewed by US financiers as a way of escaping *New Deal* regulations, such as reserve requirements and interest rate ceilings.

As early as the 1960s, US officials were encouraging the participation of US financial institutions in these markets, in particular as a way of stabilizing the large balance of dollars accumulating abroad. The Federal Reserve originally opposed to this movement, and various attempts were made to impose controls on euromarkets, in particular during the first stages of the dollar crisis. But they failed[36]. The new trends were now asserting themselves.

The next major development was the crisis of the dollar in the early 1970s, whose circumstances were recalled in section 5.1.1, leading to the suspension of the convertibility of the dollar into gold (August 1971), and forced European governments to let their currency float (provisionally, and then definitively after March 1973).[37] This new monetary and financial configuration, in which US supremacy had been temporarily diminished, thoroughly transformed the attitude of the US toward controls. The establishment of conditions favorable to the development of Europe, and the containment of its deviation from standard capitalist rules, was no longer at issue. The reversal of this attitude was clearly established by Nixon (and Treasury Secretary George Schultz).[38] Freedom of trade and capital movements were placed on the same footing, a clear break with Bretton Woods. The *IMF Articles of Agreement* was amended: "the essential purpose of the international monetary system is to provide a framework that facilitates the exchange of goods, services, *and capital* among countries".[39]

In such an environment of floating exchange rates and international mobility of capital, there was little room for Keynesian demand policy, unless under strict international coordination. During the second half of the 1970s the Carter administration attempted to associate Japan and Germany in a move toward "reflation", but faced a rebuttal, confronting a growing dissatisfaction against the policy conducted by the US.[40] Things were continuing to evolve rapidly in direction of the new trends: for example, the New York

35. OECD, *Introduction to the OECD Codes of Liberalization of Capital Movements and Current Invisible Operations*, Paris: Organization for Economic Co-Operation and development (1995).

36. In 1969, a 10% reserve requirement was imposed on the borrowings of US banks from foreign markets (E. Helleiner, *States and the Reemergence, op. cit.* note 18, p. 118).

37. A detailed narration of these events can be found in M. De Vries, *The International Monetary Fund, I, op. cit.* note 18, and many other studies. In addition to Helleiner's chapter 5, see C. Coombs, *The Arena of International Finance*, New York: John Wiley & Sons (1976), ch. 12; J. Odell, *U.S. International Monetary Policy, op. cit.* note 24, ch. 4-5.

38. Council of Economic Advisers, *Economic Report of the President Transmitted to the Congress*, Washington: Government Printing Office (1973).

39. M. De Vries, *The International Monetary Fund. Volume III: Documents. Index*, Washington: International Monetary Fund (1985), p. 381-382.

40. These events allowed Margaret de Vries to present the "domestic unemployment and lack of freedom to pursue stimulative macroeconomic policies" in the US, as a cause of the fall of the Bretton Woods system (*The International Monetary Fund, I, op. cit.* note 18, p. 114).

Stock Exchange was deregulated in 1975. These events led to various sets of outcomes at the end of the 1970s and the following decade:

1. *The U-turn in economic policy in the US*. At the end of 1978, Carter decided the implementation of an anti-inflation policy, *via* the appointment of Paul Volcker at the head of the Federal Reserve, with the well-known consequences.[41] In 1980, the *Depository Institutions Deregulation and Monetary Control Act* and, in 1982, the *Garn-St Germain Depository Institutions Act* were voted, simultaneously strengthening the power of the Federal Reserve and liberalizing monetary and financial markets. In 1981, the Congress authorized the implementation of euromarkets within the US (known as the *International Banking Facilities*).

2. *Monetary Union in Europe*. European governments began the negotiations which led to the creation of the European Monetary System (EMS) in March 1979, tending to stabilize exchange rates among European countries.[42] Each new step in the construction of the monetary union of Europe was made in the direction of complete free mobility of capital flows. In the *White Book*, in 1985, preparing the *Single European Act*, Jacques Delors stressed the urgence of free capital movements, which was finally approved by the European Community's Council of Ministers in 1988. The Delors' report of 1989 suggested the institution of a central bank, independent and with an unequivocal and single objective: price stability. Following the report, very strict limitations should have been placed on public deficits (the treatise did not go as far as devised by the report).[43] In 1989, the OECD Codes of Liberalization of Capital Movements was extended to all movements, long-term or short-term.

It is interesting to note that the discussion and the sequence of events *did not refer to the dismantling of the barriers to capital mobility within the European Community with continuing limitations toward the outside*, but directly to the liberalization of capital movements on a world basis. This echoes the view that an important motivation for the liberation was the desire to integrate European countries into the international financial system (instead of consecrating the preeminence of the US financial sector). In this context, there was no alternative to neoliberalism in Europe, specifically no way of conducting any autonomous macro policy without facing the sanction of international finance (the withdrawal of capitals).

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41. W. Greider, *Secrets of the Temple: How the Federal Reserve Runs the Country*, New York: Simon and Schuster (1987), ch. 3.

42. The impact of domestic political (electoral) conditions is analyzed in P. Ludlow, *The Making of the European Monetary System. A Case Study of the Politics of the European Community*, London: Butterworth Scientific (1982).

43. For these reasons and others, an ample literature describes Delors's stand as neoliberal. For example: "The Faustian compact enthusiastically entered into by Delors had the aim of accelerating the integration process by giving it to a great extent a neoliberal content. [...] in particular Mrs Thatcher and her cabinet, endorsed the new trend toward competition, liberalisation and deregulation in European affairs" (J. Grahl, *After Maastricht*, London: Laurence and Wishart Limited (1997), p. 108). Note that in France, it is common to describe Delors as a true Keynesian, because of its public work program! Bernard Moss writes: "Dominated by the Germans, council repeatedly denied money for minimalist versions of Delors public works proposal for trans-European energy and transport networks" ("The Single European Currency in National Perspective: A Community in Crisis?", *in* B. Moss, J. Michie (eds.), *The Single European Currency in National Perspective*, London: Macmillan, 1998, p. 8-33, p. 19). It is had to imagine, however, the stimulative impact of public works without budgetary deficits and in the context of restrictive monetary policy.

5.2 Three distinct configurations: Britain, Germany, and France (stneoeur)

The presentation, in the previous section, of the events which led to the assertion of neoliberalism tend to consider Europe globally, confronting the US. European countries played, however, active roles in these developments, with their own specific features and options.

5.2.1 Britain: the financial option (ssbrit)

The attitude of Britain concerning the transformations of monetary and financial international relations was, from the origin, contradictory. On the one hand, this country continued to consider itself as a strong financial place or, at least, was eager to recover such a role (in relation to the US). On the other hand, her position was rather weak after the war, and this ambition difficult to realize. In Britain, as everywhere, financial interests resisted the implementation of controls, but such controls were finally enforced under the pressure of facts, on the behalf of superior class interest and of the requirements of class compromise. *If the US acted in favor of the controls for political reasons (to preserve the basic capitalist order and US hegemony), Britain adopted the same attitude by necessity.*

The Bank of England was the direct alley of New York bankers in their opposition to the creation of an institution such as the International Monetary Fund: It was the responsibility of private finance to handle international monetary flows and credits. But simultaneously, Britain's gold reserves were very low, and this country needed strong capital controls, and was forced to act in this direction.

In the same vein, Britain attempted an early return to convertibility, but was unable to realize it. The "normalization" was performed gradually along the 1950s: the re-opening of exchange markets, the stabilization of the pound, and finally convertibility in 1958 (limited to current account operations[44]). But these results were obtained at the cost of recurrent crises: in 1957, 1961, and 1964-1967. In each case, it was necessary to strengthen exchange controls.

Euromarkets originated from the limitations imposed during the crisis of 1957 in Britain. London bankers discovered that, in spite of the existing regulations, they could use the dollar deposits of their foreign customers to make loans to other customers willing to borrow in dollars. No pounds were involved in these transactions. This practice was encouraged by British authorities.[45]

It is the occurrence of a new crisis in 1976, in a general context of increasing defiance toward Keynesian stimulative policies, which prepared the sudden turn to monetarism and the victory of Margaret Thatcher. As shown in figure 12, inflation was large in Britain. Simultaneously, the pound was *de facto* devalued in the mid-1970s, on the markets where it

44. E. Helleiner, *States and the Reemergence, op. cit.* note 18, p. 51.

45. On these issues, Gary Burn ("The State, the City and the Euromarkets", *Review of International Political Economy*, 6 (1999), p. 225-261) criticizes Helleiner (*States and the Reemergence, op. cit.* note 18), who refers to the role of *state officials* (since Helleiner's thesis is that states played a central role in the emergence of international finance). Burns shows convincingly that the Bank of England, despite its nationalization in 1946, always remained independent, and was directed by people emanating from the major Merchant Banks, the same people being very influential within government circles. Burn basically shows the tight interrelation between business, or capitalists, and the state. We do not see in this demonstration an actual contradiction with Helleiner's analyses, provided that a broad definition of the state is given and its class foundations are acknowledged.

floated, nominally as well as taking account of the relative price level of the country (figure 13), in sharp contrast with the mark and the franc. An austerity plan was on the agenda, supposed to take care of inflation and restore confidence. The US and Germany conditioned their help to the adherence to an IMF stabilization plan by Britain, putting definite limits to the growth of monetary aggregates and cutting public expenses. (Note incidentally, that it is in this context that Tobin suggested the implementation of its now famous tax.) The original plan of the Labour government, the *Alternative Economic Strategy*, included the establishment of stricter capital controls. But a revised form of the IMF plan was accepted by the Chancellor of the Exchequer, Denis Healy, greeted by the international financial community as a true hero.[46] The inability of the Labour party to successfully confront financial interests in Britain reflects the power of finance in this country.[47]

This first step beeing accomplished, the rest of the task was performed by the new Thatcher government, abolishing capital controls in october 1979, and guaranteeing the opening of the London Stock Exchange to foreign securities firms in October 1986 (and other adjustments): the famous *big bang*[48].

5.2.2 Germany: the fear of inflation and monetary union (ssgerm)

There is clearly an aversion for inflation in Germany, and inflation remained actually lower in this country than in others (figure 12). This attitude is generally referred to the trauma of the hyperinflation of the 1920s and the legacy of an alleged late industrialization.[49] There could be, however, an alternative, more compelling explanation. As shown in section 3.2, prior to neoliberalism, the financing of German nonfinancial corporations heavily relied on lending (figure 10); another aspect of the same feature is the large proportion of deposits and loans in the assets of households in this country.[50] *The dominant form of capital in Germany is loan capital.*

As a result of the preeminence of loans in the wealth of German capitalists, the level of real interest rates is even more important than in other countries. Because of the international dependence of interest rates in a world of free capital mobility, it was crucial that inflation remained low in this country, to an even larger extent than in the US or France. An alternative, and not exclusive, explanation is that the balance of power was different (and this is where a better understanding of power relations would be crucial). Anyhow, figure 5 shows that real long-term interest rates in Germany remained positive during the 1970s and in line with the previous years. Then the sudden rise is observed as in other countries, leading to the same transformation of the sources of financing toward the preeminence of self-financing.[51]

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46. W. Keegan, *Mrs Thatcher's Economic Experiment*, Harmondsworth: Penguin Books (1984), ch. 4.
47. This feature of Britain probably goes far beyond the management of the macroeconomy. Zysman links the failure of the Labour party to transform the British industry to the capital market-based financial system in this country (*Goverments, Markets, and Growth, op. cit.* note 14, p. 82).
48. The conservative program was expressed in the manifest al. Maude A. and, *The Right Approach For the Economy*, London: Conservative Central Office (1977).
49. Such an interpretation is put forward in C.S. Allen, "The Underdevelopment of Keynesianism in the Federal Republic of Germany", *in* P. Hall (ed.), *The Political Power of Economic Ideas: Keynesianism across Nations*, Princeton: Princeton University Press, 1989, p. 263-289.
50. J. Story, "Globalisation, European Union and German Financial Reform", *op. cit.* note 14.
51. Concerning the strictly "monetarist" procedures of the Bundesbank to fight inflation, see Von Hagen, "A New Approach to Monetary Policy (1971-8)", *in* Deutsche Bundesbank (ed.), *Fifty Years of the Deutsche Mark*, Oxford: Oxford University Press, 1999, p. 403-425.

It is also important to acknowledge that large inflation rates contributed decisively to the neoliberal coup of 1979. Inflation was the main expression of the failure of Keynesian policies. Had the countries of the *Keynesian compromise* been able to define an alternative less inflationary policy, under German leadership, it is not obvious that the turn to neoliberalism would have been taken. Considering the case from this angle might lead to completely different interpretations.

In any instance, the attitude of Germany was always hostile to inflation, and this country was momentarily against flotation and in favor of capital controls to protect itself from imported inflation[52], *a quite specific attitude*, to be contrasted with those of the US and Britain recalled earlier.

Germany was originally reluctant concerning a new step toward European monetary union as suggested by the Werner plan (October 1970), which initially resulted in the exchange arrangement of April 1972 (the snake in the tunnel). The fall of the dollar during this decade (figure 13) placed an important burden on Germany as the mark tended to become an international currency. The tightening of European cooperation implied commitments to assist countries facing exchange strain, and Germany did not want to underwrite French lack of determination to fight inflation. In this context, it is easy to understand that the German doctrine was that countries should first align their policies, meaning adopt a stricter attitude toward inflation before any new step in the direction of monetary union.[53].

This explains the late support of Germany for the creation of the European Monetary System (whose main component was the Exchange Rate Mechanism), effective in early 1979[54], understood as protection against the flows of dollars from the US. Helmut Schmidt consistently opposed to plans devised to support the currency of countries whose policies were judged laxist, and his commitment to anti-inflation policy was very strong.[55] The closer relationship between France and Germany played a role in the transformation of the German attitude, as Giscard d'Estaing's France was moving toward a more anti-inflationary stance.[56]

5.2.3 France: "Socialism" and neoliberalism (ssmitt)

France, a country of traditionally strong state interventionism, in particular since World War II, grew rapidly up to the mid-1970s: more rapidly than Germany, and considerably faster that Britain. The strongly market-oriented and anti-inflationary policy of Raymond Barre, which became Minister of finance in 1976, coincided with a break in this movement. France began its adjustment on monetary and financial orthodoxy.

The "socialist" experiment after Mitterand's election in 1981 has often been told. Only the implementation of strong capital controls could have allowed the pursuit of the new

52. O. Emminger, *On the Way to a New International Monetary Order*, Washinton: American Institute for Public Policy Research (1976).
53. This doctrine was labeled as the "economist" doctrine, as opposed to the "monetarist" (not to be confused with monetarism), referring to the French support for a rapid monetary unification.
54. Simultaneously, the European Unit of Account was renamed ECU (European Currency Unit).
55. H. Schmidt, *Men and Powers, op. cit.* note 9.
56. On these issues, see the very well documented study, P. Bernholz, "The Bundesbank and the Process of European Monetary Integration", *in* Deutsche Bundesbank (ed.), *Fifty Years of the Deutsche Mark*, Oxford: Oxford University Press, 1999, p. 731-789, and the discussions in H. Kaufmann, *Germany's International Monetary Policy and the European Monetary System*, New York: Brooklin College Press (1985) and J. Grahl, *After Maastricht, op. cit.* note 43.

policy autonomously; a large devaluation might only have relaxed the problem temporarily. Both measures meant either the isolation of France from the rest of Europe and the US, or the alignment of other European countries on similar lines, and strong controls between Europe and the US. This was beyond the determination of the newly elected officials. At issue was not simply, the lost possibility to conduct expansionary demand policies, but the accomplishment of a new step forward in the assertion of the specificity of the French economy and society, at a distance from the neoliberal world.

In the first stages of the experiment, a clear divide appeared between people in favor of a plan similar to that of the Labour party a few years earlier, on the one hand, and others like Jacques Delors advocating orthodoxy. Mitterand asked, if he ever believed in a favorable answer, the governments of other European countries to disconnect Europe from the US, a move which they, of course, refused. Given what was recalled above, the reasons are obvious. In March 1982, after consultation with the IMF, the austerity package was decided.[57] Delors negotiated a devaluation of the franc by 8% and a loan from the European Community, and the austerity program was implemented, signaling the return of France into the globalizing framework of neoliberalism, with a long list of reforms.[58] Given the resistance of the population, the French society was not thoroughly aligned on the US model, and the new framework can still be characterized as *social neoliberalism*, as in other European countries, but the process is still underway and there is more to come. Fortunately, if one may say, the fall of the stock market, besides social resistance, will probably stop the introduction of pension funds in a country such as France.

5.3 The assertion of neoliberalism: The rule of finance (stconcl)

The more detailed analysis of the rise of neoliberalism in this fifth section confirms, in our opinion, the contention in section 4 that the crucial underlying element in the analysis of these events is the constant fight by finance (box 2) to preserve the privileges attached to the ownership of the means of production. The succession of World War II and the Great Depression, in the context of the rise of the former countries of real socialism and of the labor movement worldwide, had created the conditions for a form of social "compromise". The power, income, and wealth of ruling classes was at issue: After a period of repression it was reestablished. Class struggle is the central element in this analysis.

There is also an international component to the interpretation provided in this paper. The rivalry among the ruling classes of various countries remained and *is still* largely significant, despite the internationalization of capital. For this reason, the issue of social dominance was always manifested in a complex network of international rivalry for dominance.

Retrospectively, the international mobility of capital appears as a key element in the reassertion of the preeminence of the owners, ounce the task had been performed at the

57. Bernard Moss's interpretation of the failure of the French "Socialist" program refers to Mitterand's hypocritical maneuver: "Mitterand became the instrument of liberalization and monetary union by outmanoeuvering the Communists, first adopting then vitiating their program" ("The Single European Currency", *op. cit.* note 43, p. 16).

58. D. Singer, *Is Socialism Doomed?*, New York: Oxford University Press (1988); P. Cerny, "The "Little Big Bang" in Paris: Financial Market Deregulation in a Dirigiste System", *European Journal of Political Research*, 17 (1989), p. 169-192; M. Loriaux, *France after Hegemony. International Change and Financial Reform*, Ithaca: Cornell University Press (1991), ch. 8.

center, *i.e.*, in the US. The desire of the main European countries, in particular Britain and Germany but also France, to be part of the international financial place remained basically unscathed (despite the conduct of often daring alternatives). They were the expression of the continuing strength of financial interests in each of these countries, and their international convergence, in Europe and in the US. The Bretton Woods order always remained fragile and at issue. When Europe began to move in earnest toward monetary union, the insertion of the various countries into the rising framework of international finance was already well advanced, and the deregulation of international movements of capitals in Europe and worldwide were fundamentally treated as a single issue. Once this step had been accomplished, there was very little room for alternatives and, in particular, no opportunity for radical transformations as briefly considered in France. World finance was leading the game.

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