# Neoliberalism and its crisis[*].

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## 1 - Introduction

The term "neoliberalism" is now commonly used to refer to the phase of capitalism that began at the transition between the 1970s and 1980s. The functioning of capitalism was thoroughly transformed. Nearly 30 years later, as of 2007, many had already heralded the "end of history". But the first symptoms of the "crisis of neoliberalism" were observed in August 2007.[1] After the meltdown in September and October 2008, most economists came to acknowledge its serious character, a major crisis in the history of capitalism reminiscent of the Great Depression. The lessons of the Depression had been learned, and the corresponding policies were used to dampen the shock, an all-out support to ailing financial institutions and huge deficits of government accounts, the come back of Keynesian policies. In the second quarter of 2009, the trough of the recession had been reached and the same economists began to use the past tense when speaking of the crisis.

As of the fall of 2011, the atmosphere is distinct. The macroeconomies in the United States and Europe did not recover an autonomous capability to grow independently of deficits (despite the return to comparatively elevated growth rates in the peripheries). The analysis of the determinants of the crisis points to structural mechanisms that have not been reversed, basic features of neoliberalism and the disequilibria of the U.S. economy. Will neoliberalism

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[1] A broad used is made of our recent book: G. Duménil, D. Lévy, 2011.

survive the crisis? What new social configurations could, instead, be established? What will be the position of the United States within international hierarchies?

The present study addresses these various issues: the overall periodization of capitalism, in which neoliberalism defines a specific phase (section 2); the nature and methods of neoliberalism (section 3); the two episodes of the crisis, respectively, around 2008, and the crisis of sovereign debts in the United States and Europe in 2011 (section 4); the prospects for the forthcoming decades (section 5). The United States and Europe are central stage in the analysis of the two episodes of the current crisis. But in the discussion of scenarios for the future, a particular attention must be paid to emerging countries, first of all, China.

## 2 - Periodizing capitalism

The following sections make explicit our general historical framework of analysis: (1) modes of production, the establishment of "modern capitalism" at the turn of the 20th century; (2) the structural crises that marked the emergence of modern capitalism and punctuated its history; (3) the social orders separating these crises and their relationship to the transformations of capitalism.

### 2.1 - Capitalism, the revolutions in the ownership of the means of production, and modern capitalism

Central to Marx's interpretation of history is the distinction between various modes of production. Underlying this periodization is the broad historical dynamic of productive forces and relations of production. This dynamic is *permanent*, that is, not interrupted during the course of a specific mode of production, here capitalism. Marx elaborates on the broad notion of the increasing social character of production. This transformation is expressed in the growing sophistication of production and the complexification of the network of interrelations. These relationships are manifest within enterprises (where they reached a high degree of development), as well as at the level of the society as a whole and gradually more, around the globe.

The transformations of enterprises—concerning technology and organization, and correspondingly the size of units of production—and the extension of markets during the 19th century in the United States were preparing radical institutional changes. The institutions in which the ownership of the means of production is expressed were metamorphosed, marking a major break in the history of capitalism, which we denote as the entrance into "modern capitalism". The sudden wave of incorporation around 1900 is known as the corporate revolution. The revolution of financial institutions refers to the emergence of a new banking system (of the Morgans, Rockefellers, and the like) directly involved in the financing of the emerging large corporations, backing the wave of incorporation. The phrase "managerial revolution" is used to denote the third aspect, the transfer of the traditional tasks of the active capitalist to salaried staffs of managerial and clerical/ commercial personnel.

Class patterns were correspondingly transformed. An important outcome was the emergence of a new bourgeoisie at a distance from production, whose ownership of the means of production was supported by the holding of securities, such as stock shares and bonds, giving to this ownership a financial character. In the managerial revolution, a strongly hierarchical division of tasks (a "polarization") occurred, with a concentration of initiative, power, and income among managers, and execution among lower ranking employees. The emergence of these new intermediate classes—managers and other employees—defined the class pattern typical of modern capitalism to the present. We denote capitalist and managerial classes as "upper classes", and clerical/ commercial employees and production workers, as "popular classes".

One of our theses concerning the course of history is that the progress of coordination involved in the three revolutions above commanded the rise of managerial classes. The relationship between capitalist owners and managers, thus, became a central political issue. We even contend that the continuation of the same dynamic could determine the transition to a new managerial mode of production, beyond the rule of capitalist owners.

### 2.2 - Structural crises

The emergence of modern capitalism was the result of continuous underlying trends, but the changes were precipitated by the major crisis that occurred in the United States during the 1890s. This crisis was the first of four successive structural crises. The second, the Great Depression, is better known. The third was the crisis of the 1970s, with the slowing down of accumulation and the wave of inflation. The fourth one is the current crisis of neoliberalism. One can note the periodic character of such breaks, about every 30 or 40 years, although it is difficult to tell the origins of this regular pattern.

Both the crises of the 1890s and 1970s followed periods of declining profit rates. They can be denoted as "profitability crisis", manifest, respectively, in a competitive war and a wave of inflation. The Great Depression and the current crisis are not profitability crises. Capitalist classes dramatically pushed forward basic economic mechanisms—as in financialization and globalization (in both of which deregulation is involved)—in directions supportive of the rise of their income and wealth. They were very successful in this endeavor within a time frame of two or three decades. But, as Marx and Engels had described in the *Manifesto*, they behaved as apprentice "sorcerers", at some point, losing control of their own magic. We denote such crises as "crises of financial hegemony" (in reference to Finance, defined as capitalist classes and financial institutions).

### 2.3 - Social orders

We call "social orders" (or power configurations) a phase of capitalism characterized by the prevailing specific hierarchies of power among classes or fractions of classes, including the compromises among these groups. Social orders can only be defined in reference to a given pattern of class relationships, as prior or after the establishment of modern capitalism. They delineate shorter periods in the history of the mode of production. Only the three social orders in modern capitalism are relevant to the present investigation:

1. *The first financial hegemony.* Beginning with the three revolutions to the Great Depression, capitalist classes enjoyed a situation of hegemony within social relations. The worker movement (with major strikes) was finally curbed under the circumstances created by World War I. A form of social compromise was established with the emerging class of managers, despite the emotion within capitalist classes created by their rising power. Although the Federal Reserve was created in 1913, the resistance remained strong against the central control of the macroeconomy. Liberalism was the doctrine, domestically as well as internationally.

2. *The postwar compromise.* The Great Depression, the New Deal, World War II, and the strength of the worker movement worldwide led to the establishment of a new social compromise after the war. Many of the rules enacted during the New Deal were prolonged, but a milder social compromise was found. Keynesianism was substituted for liberalism, with

a major role of the government (given the dramatic rise of government revenue), monetary and fiscal policies, while the initiative concerning production and investment was left to enterprises. (A more detailed analysis would be required to account for the differences between national policies and the continuing weakness of international coordinations, as envisioned in Bretton Woods.) These years were those of the Welfare State. The compromise was to the Left, between managers and popular classes, while the power and income of upper classes were diminished, with a sharp reduction of inequalities. Important differences were observed among countries, for example, between the United States and Europe (with, notably, the nationalization of important segments of the economy in Europe) and, to an even larger extent, Japan.

The postwar compromise died of its lack of political prospects in combination with: (1) its internal weaknesses (the almost exclusive concern about the prolongation of the progress of purchasing powers); (2) the exhaustion of the favorable features of technical-organizational change inherent in the new efficiency proper to modern capitalism; and (3) the struggle of capitalist classes.

3. *The second financial hegemony*. The crisis of the 1970s and the weakening of the worker movement allowed capitalist classes to recover their earlier hegemony around 1980, the outcome of a class struggle in which popular classes were defeated. Capitalist classes imposed a new discipline on popular and managerial classes. Gradually, however, an alliance was formed among upper classes, between capitalists and managers, that is, to the Right. The overall rearrangement of the economy and society in general was dramatic.

The relationship between the mode of production (given the revolutions introducing to modern capitalism) and social orders is not only that the latter defines a shorter term periodization. The link is dynamical. The social actors active within social orders are determined by the metamorphosis of class patterns associated with the transformation of relations of production—specifically, over the decades considered, the rise of managers that echo the overall process of socialization. The postwar compromise can be interpreted as a first rehearsal of a great historical scenario in which capitalist classes would be set aside, although it was finally reversed. In neoliberalism, capitalist classes attempted to orient the social trends inherent in the dynamics of productive forces and relations of production in directions compatible with the survival of their own hegemony. In some respects, they pushed forward the process of socialization of production, as in neoliberal globalization; in other respects, they worked hard in favor of the limitation of the consequences susceptible of damaging their own hegemony, as in financial deregulation. Overall, they failed to establish or bolster the mechanisms aiming at the stabilization of the course of the economy, nationally or internationally, as manifest in the current crisis, thus, jeopardizing their own privileges.

## 3 - A second hegemony of Finance

Neoliberalism is a class phenomenon.[2] The power and income of Finance, capitalist classes and financial institutions, was restored in a new "social order", in the wake of the social compromise after World War II. The present section also discusses the expansion of neoliberalism around the globe and its limits, notably in reference to China.

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[2] An interpretation that we introduced in the mid-1990s, first published in English in G. Duménil, D. Lévy, 2001.

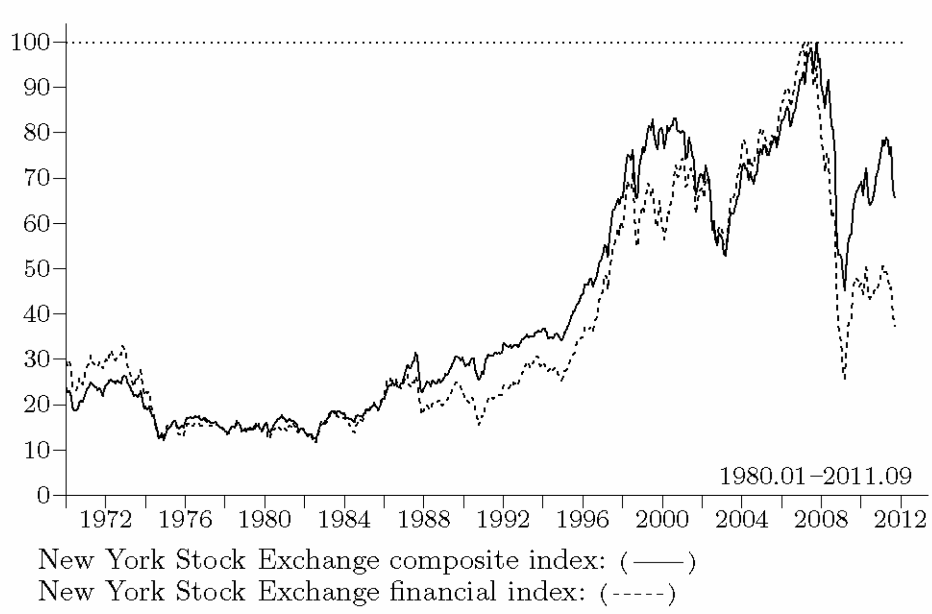
### 3.1 - Finance at the helm

The imposition of neoliberalism meant a thorough redirection of the economy, both nationally and internationally. To this one must add the class offensive concerning politics and ideology.

It is, first, important to recall that, from the early 1980s to the current crisis, the neoliberal endeavor was very successful when assessed according to its own objectives, the income and wealth of upper classes. In other works[3], we presented data testifying to the sharp rise of upper incomes (notably the upper 99-100 income fractile). An additional finding is the unexpected importance of the increase of upper wages. In the progress of income inequality, they played a role about equivalent to capital income (interest, dividends, and capital gains). These high wages are clearly those of managers, notably their upper fractions, while the wages of the bulk of the working population were stagnating or diminishing. To this, one must add that unknown further incomes are garnered and capitalized within tax havens.

An expression of these trends is shown in Figure 1. The variables are New York Stock Exchange indices, corrected for inflation by the deflator of GDP. Clearly apparent are the falls into the crisis of the 1970s, the sharp trends upward in neoliberalism, the declines into the crisis of 2000/1 and the current crisis. In constant dollars, an investment in 1980 was worth about five times its value during the 2000s.

Figure 1. NYSE indices corrected for inflation (max=100)




Besides the new discipline imposed on management and workers to the benefit of capitalist owners (gradually more to the benefit of jointly capitalists and managers), one can mention the new policies tending to the maintenance of price stability to the benefit of lenders. But two major components were *financialization* and *globalization*. The intersect, financial globalization, played a central role. Financial mechanisms exploded, with a significant

[3] Most recently in G. Duménil, D. Lévy, 2011. See also 2004.

acceleration after 2000. On derivative markets, for example, the gross market value of over-the-counter (OTC) interest rates contracts reached $ 20 trillions in 2008, to be compared to $ 14 trillion for U.S. GDP; the loans by all banks worldwide to foreigners were multiplied by about 3 between 2000 and 2008. The imposition of free trade and movements of capitals around the globe opened all regions of the world to the investment of transnational corporations be they nonfinancial or financial. Between 1970 and 2008, the total exports of goods in the world were multiplied by almost 7; during the 2000s, the flows of direct investment abroad were 48 times larger than during the 1970s. As is also well known, globalization placed all workers of the world in a situation of competition. The impact was devastating concerning the purchasing power of popular classes and their access to health care, retirement, and education.

Political life was also thoroughly transformed. As long as the values of the Left were supported by the most educated fractions of the population—linked to what we denote as "managerial classes" including their intellectual components—capitalist classes had to battle (mostly indirectly) with individual and groups well equipped to resist their contentions. Concerning ideology, in close relationship to the above, the two financial hegemonies replayed the old tune of the "liberalism" of the 19th century, as implicit in the notion of a "*neo*liberalism". In this context, "liberalism" denotes the freedom to act of capitalist classes—with possible progressive features within earlier social structures (in the phase of establishment or maturation of capitalism), but outdated in the circumstances created by the maturation of relations of production in the 20th century, not to mention the 21st. In its first formulations, prior to World War II, during the war, and after, neoliberalism was defined in reaction to the so-called "totalitarist" regimes in Nazism and Sovietism, then, explicitly, in reference to social-democracy. Following von Hayek, social-democracy was born to lead, in the short or longer run, to totalitarism.[4] This program is directly aiming at the imposition of a class "democracy", that is, structured to the benefit of upper classes, as in both financial hegemonies.

### 3.2 - A neoliberal globe?

It is important to distinguish between the expansion of neoliberalism to all countries around the globe and neoliberal globalization (free trade and the free international movements of capitals). Several countries in Latin America refused George Bush Junior's offer concerning the broad Free Trade Area for the Americas (FTAA). If the three well-known Andean countries are part of the neoliberal international "division of labor", they domestically broke with a number of the rules of neoliberalism. But the major and more important case for the coming decade is China.

The official phrase "Socialism with Chinese characteristics" is certainly misleading.[5] The Chinese economy and, more generally, society can be described as the combination of a *managerialism*, under the leadership of officials and (usually simultaneously) the members of the Communist party, and a mushrooming *capitalist sector*.

During the 2000s, China followed a very efficient trajectory concerning growth and exports, in which its position within neoliberal globalization was crucial. But this does not mean that the domestic trajectory of the Chinese economy is neoliberal. The intervention of the government remains very strong and at odds with the rules of neoliberalism: (1) The exchange

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[4] F.A. Hayek, 1944. See also P. Mirowski, D. Plehwe, 2009.

[5] A recent summary of these official theses can be found in E. Cheng, X. Xin, 2011.

rate of the renminbi is controlled centrally; (2) The same is true of capital movements, in and out of China (given the role played by Hong Kong); (3) And also true of financial markets, under close scrutiny; (4) The banking system is still basically owned by the government and its action is targeted toward development, with a lax credit policy; (5) The key sectors of the economy are still owned by the government, with a very active industrial policy in favor of development.

In this context, it is difficult to determine the pattern of class alliances in the Chinese society. The government and, first of all, the Communist party traditionally claim to directly represent the interest of the people, but everybody knows that the social situation is more complex.

The recent developments are worth a careful consideration. From the early 2000s, the Hu-Wen course (from Hu Jintao and Wen Jiabao) marks a significant alteration of the trajectory followed during the 1990s (the Jiang Zemin era). The new course strengthened the grasp of central authorities and manifests an increased concern for social unrest. Thus, it tends to extend a number of social benefits (health, retirement) for certain categories of workers. The reference to a "social-democracy" would, however, be misled. Although the purchasing power of managers is increasing rapidly, the conditions of life and work of the bulk of urban and countryside workers (given the flows of migrants) remain very hard, while the inclusion of capitalist classes in the structures of power at the top are progressing. These latter features suggest social alliances at the top of social hierarchies, similar to those prevailing within financial hegemonies in capitalist countries, with the *major difference* that the leadership is in the hand of officials and members of the Communist party. The case of the managers of enterprises is more ambiguous, given the often unclear patterns of ownership of non-state enterprises.

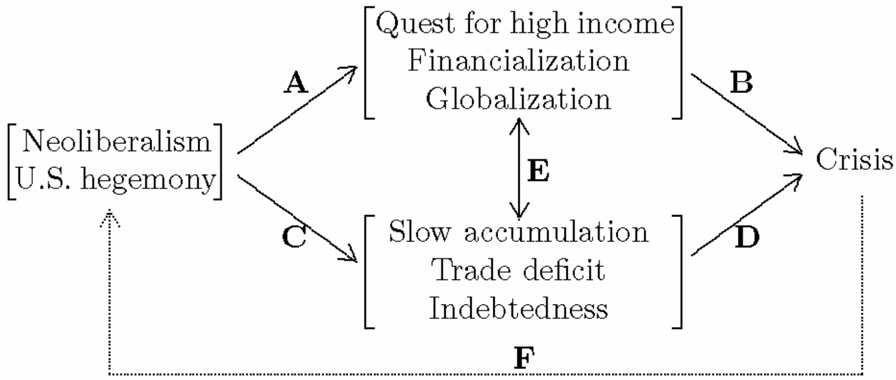
## 4 - Two first steps in the crisis of neoliberalism

As of the fall of 2011, the current crisis clearly entered into a second episode. One can, equivalently, refer to two crises, in 2008 and 2011, but they are tightly connected. The second episode is the crisis in the treatment of the first crisis. The two following sections are successively devoted to each of them.

### 4.1 - Neoliberalism under U.S. hegemony: The crisis of 2008

The determinants of the crisis of 2008 are summarized in diagram 1.[6] *Neoliberalism*, in the left brackets, is at the origin of everything, but in combination with *U.S. hegemony*, as in the phrase "neoliberalism under U.S. hegemony". This second aspect emphasizes the importance of the trajectory of the U.S. macroeconomy, only made possible by the towering international position of the country. The two arrows A and C distinguish between two sets of factors, in the upper and lower brackets. The former refers to general features of neoliberalism shared by all neoliberal countries, although the United States were leading most of these trends. Prior to 2007, with little exception, the factors listed in the lower brackets were only typical of the U.S. economy:

[6] G. Duménil, D. Lévy, 2011, p. 34.




1. *Neoliberalism in general.* These factors are all the expression of the endeavor of Finance aiming at the removal of all barriers to its power and wealth, as in the *Quest for high income*, along the lines already introduced (capital incomes, wages, conditions of labor, policies, etc.). The diagram makes explicit *Financialization* and *Globalization*, including financial globalization, aiming at the same objective. Deregulation was a crucial tool. A huge and unwieldy financial-global structure was created, within each country and internationally. Other countries, such as the United Kingdom, were thoroughly transformed in the directions opened by neoliberal financialization and globalization.

A crucial factor of the crisis was deregulation and the reluctance to reregulate financial mechanisms, given threatening trends, on the part of monetary authorities, notably the Federal Reserve. To this one can add the difficulties met in the conduct of monetary policy in the context of neoliberal globalization, as the Federal Reserve lost the control of long-term interest rates. The blind faith in the self-discipline of financial-global market mechanisms was the root of the meltdown not a "mistake" in the conduct of monetary policy.

2. *The trajectory of the U.S. macroeconomy.* The first factor in the lower brackets is slow accumulation. The United States were not the single economy among advanced countries in which the rates of accumulation were lower than before the neoliberal decades but, in this country, the downward trend of accumulation (with the exception of the high-tech boom during second half of the 1990s) was part of the quite specific combination of three trends: (1) the slowing down of accumulation; (2) the increasing deficit of foreign trade; (3) the growing indebtedness.

Concerning the latter aspect, indebtedness, one must distinguish between the domestic debt and foreign financing:

1. In the present investigation, the domestic debt is defined as the sum of the debts of households and the government. Each can borrow and make financial investment. Depending on the issue considered, either the gross amount of debt (as in the study of financial stability), or the net debt—gross debt minus financial assets—(as in the study of the formation of demand) is relevant. Enterprises also borrow but they make financial investments for approximately the same amount, and it is possible to make abstraction of their net debt in the analysis of demand mechanisms.

2. The rest of the world makes financial investments in the U.S. economy and, reciprocally, U.S. economic agents make financial investments in the rest of the world. Foreign financial investment (or foreign financing) refers to the U.S. assets held by foreigners, securities, loans,

and deposits.[7] The net external debt of the U.S. economy is an important variable in the analysis of the crisis. It is the difference between the U.S. assets held by the rest of the world and the foreign assets held by U.S. agents.

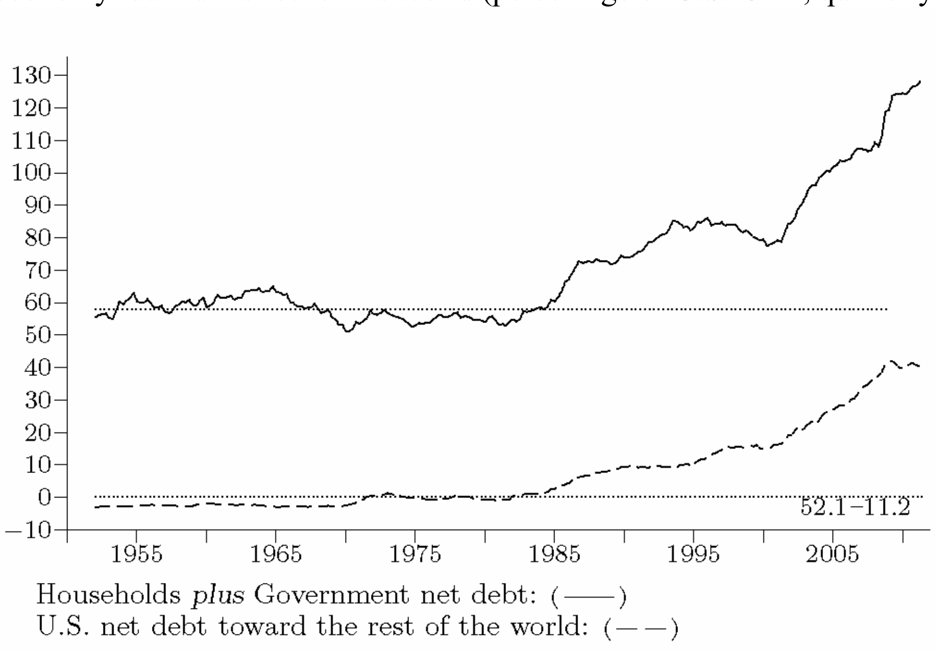
A basic relationship links the net debts (in terms of *variations*, $\Delta$):

$$\Delta\ \textit{Net external debt} \quad = \quad \Delta\ \textit{Net debt of households} \quad + \quad \Delta\ \textit{Net debt of gouvernment}$$

This relationship is illustrated in Figure 2 for credit market instruments exclusively. The variables are amounts outstanding instead of variations nbsp;; thus, the joint variation of the two variables is manifest in the parallelism of the two lines. Two periods are clearly apparent, from the 1950s to the early 1980s, and the following neoliberal decades when the trajectory of disequilibria of the U.S. economy was initiated.

These patterns of variation are the product of the reciprocal causal link between: (1) free trade (at the origin of the deficit of foreign trade in a world of unequal labor cost and technical capabilities, and exchange rates often divorced from purchasing power parities); and (2) the growth of the domestic debt. *The direction of an increasing fraction of demand toward the rest of the world must be compensated by the stimulation of domestic demand to ensure a normal use of productive capacities on the domestic territory.* In addition, part of this stimulation is derived toward the rest of the world, adding to the requirement to stimulate. The rise of the gross debt of households in the United States was all the more dramatic that households were also making financial investment.

Figure 2. Net debts: U.S. households and government considered jointly, and the U.S. economy toward the rest of the world (percentage of U.S. GDP, quarterly)




*The variables are debts in credit market instruments. The rest of the world also purchases stock shares of U.S. corporations (and reciprocally) but these amounts are much smaller.*

[7] Stock shares are part of securities, and should not be referred to as "debts", but is convenient to denote foreign financing as a "foreign debt". Note that direct investments abroad are counted as "financial investment".

3. *Relationships between the two sets of factors.* They are represented by vertical arrow E. An important aspect is that both financialization and globalization made possible the growth of the debt of households. Financial deregulation paved the way to subprime mortgages and other junk bonds, and the proliferation of Mortgage Backed Securities (MBSs) supported by private label securitization, the multiplication of vehicles such as Collateralized Debt Obligations (CDOs), and Credit Default Swaps (CDSs). Financial globalization allowed for the sale of about half of the products of securitization to the rest of the world.

The collapse of the financial-global fragile structure inherent in neoliberalism was triggered by the wave of default on household mortgages that began in 2006 in the United States, and then in the rest of the world.

Europe was well advanced along the neoliberal trajectory, and also subject to the perilous developements listed in the upper brackets in the diagram. It was part of the overall fragile financial structure, which was also destabilized when the original shock came from the United States. (*When considered globally*, Europe was not affected by the same disequilibria as the U.S. economy, only specific countries.)

### 4.2 - Crisis in the treatment of the crisis: The U.S. and European economies in 2011

The present section focuses on the U.S. and European economies as of 2011. In both regions of the world, the treatment of the crisis of 2008 combined loans to the financial sector and very large deficits of governments' accounts.[8] To this, one can add the provision of dollars by the Federal Reserve to foreign central banks. These actions were successful in a given time frame, though with significant limitations:

1. Despite major failures, the loans to financial institutions allowed for the survival of many of those hurt by the crisis. It is important to emphasize, however, that this support did not stop the so-called "credit crunch", notably in the United States. As of the second quarter of 2011, the new loans to households by financial institutions are still inferior to the sums paid back by households. Only the loans to enterprises have been significantly revived.

2. As of 2011, in the United States, the only economic agent at the origin of final demand still financing part of its expenses by new borrowing is the government. The deficits of the budgets in all countries successfully supported the macroeconomy, though with important limitations. First, despite government deficits larger than 10 percent of GDP, the recovery is weak within major countries of the center. In the second quarter of 2011, the U.S. GDP in constant dollars almost reached its pre-crisis level (in the fourth quarter of 2007), but new symptoms of a downturn are apparent. Both in the U.S. and Europe, industrial production indices remain inferior to their peak prior to the crisis (10 percent below in the United States). Second, and most importantly, four years after the first symptoms of the crisis were observed, this stimulation never reignited the *autonomous capability to grow* of the two economies.

The roots of the sovereign-debt crisis, as of 2011, lie in this latter feature of the macroeconomy. The support of the general level of activity of the U.S. economy requires the stimulation of domestic demand by rising indebtedness. Given the levels reached by the debt of households, it is hard to imagine that this supplement could come from households. (Actually, the gross debt of households diminished to a small extent.) Only the deficit of the government can uphold the macroeconomy.

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[8] G. Duménil, D. Lévy, 2011, Part VII.

Prior to the crisis, a considerable fraction of the Treasury securities issued to finance the deficit was purchased by foreigners, an average of 78 percent between 2002 and 2007. The rise of deficits during the crisis posed a major threat on the exchange rate of the dollar. In the last months of 2010, the Federal Reserve began to buy amounts of Treasury securities even larger that the increase of the government debt, in the procedure known as “quantitative easing”. During the first two quarters of 2011, the Federal Reserve, thus, purchased the equivalent of 160 percent of the new securities issued. Correspondingly, during the same period, the share of securities purchased by the rest of the world diminished to 17 percent. Households were simultaneously selling a fraction of the securities they held.

The trade-off is clearly established. Either the deficient demand to producers based on U.S. territory is compensated by the spending of the government, or the macroeconomy plunges. The situation reached such degrees that the contraction of output would be spectacular. The further destruction of a large fraction of productive capacities within industry is implied. The resistance would be sharp. The U.S. manufacturing sector presently only accounts for about 10 percent of GDP (still 25 percent of manufacturing worldwide), but its role is crucial concerning foreign trade. The political agenda in the United States, with the forthcoming elections, is such that the Republicans play the dangerous game of pushing the U.S. economy toward a new recession.

In Europe (the 27 or the 17 of the euro area), no deficit of foreign trade is observed for the entire zone (or is small) and the debt of households did not reach levels similar to U.S. households, a situation substantially distinct from that prevailing in the United States. A pattern similar to that prevailing in the U.S. economy prevails within a number of European countries. The same determination to reduce deficits on the part of governments is observed. This is where the problems lie.

The combination of the two deficits—foreign trade and government like in the U.S. economy—defines the worst possible configuration for a small European economy, in particular if these trends have been established years prior to the crisis, as in Greece. Under such circumstances, the so-called “markets” (financial institutions, notably outside of the European Union) react aggressively to the prevalence of these twin deficits. One can contrast this configuration with the one prevailing in Japan, with a skyrocketing government deficit but a large surplus of foreign trade. Since the surplus of foreign trade creates a flow of financing from the country toward the rest of the world, the financing of government debt is less dramatically dependent on foreign financing and the exchange rate of the currency is not threatened.

One important feature of the debt problem in Europe is, however, that the foreign financing is, to a large extent, provided by European banks. For example, in Greece at the end of 2010, the total claim of foreign banks amounted to 45 percent of the Greek GDP, of which 9 percent are due to banks outside of the euro area and the remaining 36 percent to banks within the zone. For Portugal, the total debt to foreign banks is equal to 93 percent of GDP, that can be broken down, respectively, into 16 percent (outside of the euro zone) and 77 percent (inside). Thus, the problem is mostly European. This does not change, however, the fact that the banks which lent to these countries, in particular to their governments, are now facing a difficult situation. The European Central Bank is confronted to circumstances similar to those that followed the first major shock in late 2008, and is compelled to refinance these banks for considerable amounts, or new mechanisms must be elaborated (as the “euro bonds”). The problem is not, however, simply *liquidity*, but also *solvability*. The own funds of these banks must be increased (and devalued to the extent of incoming losses). Who will recapitalize the banks confronting these pressures? Governments already fighting to curb deficits?

In the case of the euro zone, the crisis revealed the weaknesses inherent in the construction of the European Union and the euro area within neoliberal patterns. There was no "financial European Union", as Europe was immediately inserted within financial globalization, with the free international mobility of capital; "markets" were supposed to discipline countries, not a strong central governance, only blind rules (such as the maximum government deficit at 3 percent of GDP)[9]; the solidarity among countries remained weak. The deterioration of the macroeconomic situation in a number of countries is not a recent development, and nothing was done. Ireland was allowed to practice fiscal dumping, in a pure neoliberal fashion, with considerable advantages in the medium run, but creating a situation whose unsustainable character was revealed by the crisis, again without collective preventive action.

Though under distinct circumstances, the ways out are difficult to imagine both in the United States and Europe. It is, therefore, unlikely that this second episode will be the last in the list, as currencies are under threat. The resistance to change on the part of upper classes is still very strong and the Rights are orchestrating alternatives, which, if they were actually pursued would likely lead to chaos.

## 5 - Beyond neoliberalism: Classes in a new social order

In the analysis of historical trends, it is important to distinguish between various time frames, notably between a form of medium term and longer term prospects. This is the lesson taught by, respectively, the interwar period and the war, on the one hand, and the postwar decades, on the other hand. Concerning historical prospects, we distinguish between three alternative social orders: (1) a third financial hegemony, in continuation of the second but with the required adjustments; (2) neomanagerialism, the continuation of the alliance at the top of social hierarchies, but under the leadership of managerial classes, and (3) a scenario similar to the postwar compromise. In these respects, the present situations in the United States and China appear symmetrical. Concerning political orientations, class struggle will have the last say.

### 5.1 - Crisis preliminary episodes—! Forthcoming social orders

In the discussion of possible options for the coming decades, the comparison with the situation that prevailed during the 1930s, 1940s, and after World War II is telling. The Great Depression led to the establishment of social configurations as diverging as Nazi Germany and the New Deal in the United States (or the Popular Front in France). Political circumstances, including the preparation of the war, played a central role. Both Nazism and the New Deal shared, however, a common feature, the strong intervention of the government. After World War II, a new social order was found in the post-war compromise, with more moderate traits. Despite remaining differences, a convergence was observed within, at least, the United States, Europe, and Japan.

Concerning the current crisis, a possible scenario is that a similar course of events be reproduced. A first period would be marked by strong perturbations and potentially diverging configurations (to the extreme right, the right, or the left). Only later, a new more stable social order would be found. It would match some of the features of the underlying transformation of relations of production, in line with the new degrees and forms of the socialization of

[9] Such rules are reminiscent of the short-lived attempt at the implementation of monetarist procedures in the early 1980s in the United States in place of Keynesian feedback policies.

production, nationally and internationally. For example, new coordinations would be established globally, susceptible of imposing a degree of coherence in the previous wild neoliberal globalization, a combination of limitations to free trade and the free movements of capital internationally, and steps forward in the enhancement of global governance, for example, controls imposed on the expansion of financial mechanisms worldwide. Class struggle would, as after World War II, determine political orientations. When we refer to the establishment of *new social orders*, we point to this type of longer term developments. It is difficult, however, to imagine what type of events, similar to World War II, could command the transition from the preliminary disorderly configurations to such more coherent and stable paths.

As already stated, the postwar compromise was established in the context created by the Depression and the war, given the political conditions resulting from a strong worker movement worldwide. A few decades later, this social order died of the metamorphosis of these circumstances. Despite the violence of the crisis, the present situation is thoroughly distinct. A new social compromise to the Left, grounded in the alliance between popular and managerial classes, is unlikely, although, simultaneously, the present crisis made the demonstration that the trends inherent in the second financial hegemony are unsustainable.

### 5.2 - A third financial hegemony — Neomanagerialism

Considering post-neoliberal social orders at a general level of analysis, two options are opened. Due to the political situation recalled above, the alliance at the top of social hierarchies between capitalist and managers is the most likely scenario. The alternative is between the exercise of the leadership by capitalist or managerial classes. Though to different degrees, a significant break with the rules of the second financial hegemony is implied in both instances:

1. *A third financial hegemony.* Capitalist classes find a way out of the present crisis and show a capability to adjust the power configuration to the advance of productive forces and relations of production, both nationally and internationally. A degree of regulation and collective governance is involved. The freedom to act of capitalist classes is subjected to self-discipline. Manifestations of such concerns are already apparent in the contemporary second financial hegemony. The action of the Federal Reserve intending to stabilize the economy, nationally and internationally, testifies to the prevalence of such trends; it is so in the so-called "Basel Accords" concerning the balance sheets of banks; an important fraction of financial transactions is performed within exchanges, instead of direct OTC procedures; international institutions such as the World Trade Organization (WTO) or International Monetary Fund (IMF) already play important roles. A new social-global arrangement would require the extension of such mechanisms. The role of managers would be technically increased, but the leadership and the income of capitalist classes would not be questioned.

2. *Neomanagerialism.* In the term, there is obviously a wordplay with respect to neoliberalism. As this latter notion was calling for the restoration of some of the features of the liberalism of the 19th century, neomanagerialism points to aspects of managerial capitalism during the postwar decades, basically the leading role of managers and their larger degree of autonomy vis-à-vis capitalist classes. In neomanagerialism, the alliance at the top is also preserved, but the leadership is transferred to managerial classes.

In a potential third financial hegemony, the adjustment to the advance of relations of production would be subjected to the leadership of capitalist classes, as in the control of the stability of trajectories (both concerning the macroeconomy and financial mechanisms, given the tight relationship between the two) and growth performances or, even, industrial policies or forms of protectionism; in neomanagerialism, these trends would be pushed to further degrees; even more importantly, fundamental aspects of social relations would also be involved, notably concerning comparative powers in decision making and income channels (as in wages and bonuses relative to capital income). A degree of "financial repression" would be imposed, but with some moderation since the new social alliance would still be to the right. This would open a path to capitalist families in their gradual transition to the new configuration (a movement whose preliminary forms are already apparent in the second financial hegemony.[10])

In the distinction between the two social orders, one can observe the tight link to the historical progress of productive forces, the transformation of relations of production, and the corresponding class patterns. A third financial hegemony can be viewed as an adjustment of the power of capitalist classes to the progress of relations of production. This is what neoliberalism failed to do and what provoked its crisis. Like the second financial hegemony, the third such hegemony would manifest a resistance to adjustments of a similar historical import, along a road leading to its own structural crisis. In neomanageralism, the adaptation would be much stronger, opening a much more stable historical trajectory. Obviously, the outcome would be distinct from the one—a "social-managerialism"—to which the alliance to the Left would lead, and which we judge unlikely under the present conditions of class struggle. But the two trajectories would share common aspects, those conveyed by the transformation of relations of production.

In the definition of the whole range of outcomes—third financial hegemony, neomanagerialism with the compromise to the right, and social-managerialism with the compromise to the left—there is obviously a matter of degree (how much government intervention, autonomy of managers, financial repression, social protection, etc.) Our interpretation, concerning the past as well as the future of societies, is that such *degrees* are superficial expressions of specific historical configurations of relations of production and class hierarchies of power and compromise, to be distinguished in their *nature*.

## 5.3 - The United States and China: Mirror images?

The present situation in the United States is much more serious than is usually thought. A central thesis in *The crisis of neoliberalism*[11] is that the changes to be undertaken are so dramatic that a third financial hegemony would not measure up to the task and a transition to neomanagerialism is required if U.S. upper classes want to preserve their power and income. This is due to the joint requirement of remedying the unsustainable trends toward financialization and globalization and, simultaneously, correcting the trajectory of disequilibrium of the U.S. macroeconomy. Concerning this latter aspect, it is even difficult to imagine ways out. This is all the more true if one takes account of the requirement to significantly slow down the decline of the international hegemony of the country. Thus, the consciousness of the interest of the country, notably on the part of upper classes—what we denote as the "national factor"—could provide the stimulus in the direction of a new course in neomanagerialism.

Despite obvious differences, the situation in China is in many respects symmetrical. The development of the country is based on the combination of a strong managerial leadership,

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[10] G. Duménil, D. Lévy, 2011, ch. 5.

[11] G. Duménil, D. Lévy, 2011, Part IX.

notably on the part of officials/ members of the Communist party, and an exploding capitalist sector, a combination directly evocative of neomanagerialism. One difference is, however, that the managerial aspect is not “new” with respect to an earlier managerial capitalism, but to the rule of a managerial class in China prior to the reforms (with its bureaucratic aspects). The symmetry with the U.S. society lies in the observation that the Chinese society is now confronted to the continuation of its neomanagerial traits or the transition to financial hegemony.

Overall, the United States must now confront the bifurcation between a third financial hegemony and neomanagerialism, while China faces the same alternative, but coming from the other branch. The situation in Europe is significantly distinct as, in the short run, the main issue seems to be the preservation of the European Union and the euro zone.

Within the dynamics governing such historical bifurcations, the seriousness of the contemporary crisis, its duration and depth, will play a central role. The features of the crisis also command the possible reignition of new bouts of more radical class struggle on the part of popular classes. But one must keep in mind the likely divergences within various regions of the world and, in a form of medium run, the uncertainties surrounding what has been denoted earlier as “crisis episodes”, including far-right endeavors. Crucial will also be the agility of upper classes, in their two components, to react to historical circumstances instead of defending narrowly defined short-term interests.