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Policy Continuity, Policy Change, and the Political Power of Economic Ideas

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Abstract

Because far-reaching changes in macroeconomic policies are accompanied by the adoption of a new theoretical framework, economic ideas are frequently assumed to have a causal influence on policy innovation. It is argued here that changes in the macropolicy regime are mainly driven by developments in the labour and financial markets, which confront the existing regime with intolerable deflationary or inflationary dynamics. The adoption of new economic ideas in regime changes is primarily driven by the need to provide a justification for exogenously determined changes in policies which are compatible with the particular ideological convictions of the main political groupings. Ideas are argued to exert a causal influence on policies primarily by promoting policy continuity.

1 Introduction

That new economic ideas can profoundly alter the course of macroeconomic management would seem beyond doubt. The last two major revolutions in macroeconomic policy-making in Western Europe seemed to be linked closely to new theoretical developments. The macroeconomic revolution of the Great Depression, when governments came to adopt the view that discretionary demand management is necessary to prevent market economies from getting stuck in an unemployment equilibrium, is inextricably bound up with the name of John Maynard Keynes. Similarly, the turn to macroeconomic austerity of the last two decades drew much inspiration from the work of Chicago economist Milton Friedman and his followers, who argued that Keynesian policies provided at best a short-term remedy for unemployment and merely inflation in the long run.

New ideas, in this perspective, can be seen as discoveries that change policy-makers' conceptions of how the economy works, thereby leading to novel policies. Yet, a closer look at the history of macroeconomic policy and macroeconomic ideas in Europe since the interwar period suggests a different interpretation. This article argues that the view that new economic ideas

determine the character of new policies reverses cause and effect. More specifically, three hypotheses are advanced:

(1) Ideas exert an independent causal influence on policies by providing for continuity rather than change because economic policy-makers cling to the ideas and policies that were adopted in response to a traumatic event, even if the original constellation justifying such policies has long disappeared.

(2) The changes in macroeconomic policy regimes during this century have been driven by the need to correct cumulative price level disturbances. An expansionary macroeconomic strategy aimed at full-employment is only viable if it can rely on financial and labour market institutions to prevent cumulative inflationary pressures. Conversely, a restrictive regime, which uses unemployment as a means to prevent inflation, is only viable as long as financial and labour market institutions are able to stem deflationary pressures. Put differently, a reasonable degree of price stability functions as a selection criterion, that determines the viability of macroeconomic strategies independently of the priorities of policy-makers.

(3) Because the timing and character of a regime change is determined by developments in financial and labour markets, it is largely exogenous to the political system. The role of new economic ideas in regime changes is confined to providing a justification for exogenously determined policies of price stability. This is compatible with the tenet that economic policies strive to promote growth and employment, and with the particular ideological convictions of the main political parties.

The structure of the article is as follows: section two briefly reviews the macroeconomic regime changes in Europe since the end of the First World War. Section three argues that because policy paradigms like Keynesianism or monetarism can be used to justify almost any type of economic policies they are largely irrelevant for the analysis of the role of ideas. Section four argues that ideas cannot be understood as mere cloaks for interests. Section five provides a 'Darwinian' model of the role of ideas in macroeconomic policy-making, centred on the notion of the primacy of price stability. Section six applies this approach to the policy changes in France, Britain, and Sweden during the last two decades. Section seven is the conclusion.

2 Macroeconomic regime changes

Macroeconomic policies are subject to constant change. Most of these changes, however, do not require explanation in terms of ideational factors as they merely involve adjusting policies to new economic developments within a given interpretative framework. It is only in the much less frequent cases of regime changes, when the relation between policies and outcomes is funda-

mentally reinterpreted, that it would seem necessary to invoke economic ideas as an explanatory variable.

Macroeconomic policy regimes can be distinguished by the extent to which monetary and fiscal management are seen to give rise primarily to real or to nominal effects. If macroeconomic management can durably affect real variables then the stabilization of growth and employment around target levels set by the government is an appropriate policy goal. If, in contrast, macroeconomic management can only hope to affect nominal variables, then the stabilization of the price level is the only appropriate goal for such policies.

In the period since the end of the First World War three regime changes can be identified in Western Europe: one during the early twenties, one during the Great Depression, and the most recent one during the seventies and eighties. At the end of World War I the view that discretionary demand management positively affects the economy was dominant amongst West European policy-makers. To provide jobs for the returning soldiers, prevent social upheaval, and facilitate the conversion to a peacetime economy, West European governments pursued cheap monetary policies. Given the enormous drain the war had exerted on the budget, fiscal policies generally aimed at restoring budget balance, although there were some notable exceptions, like Germany and Norway. During the first half of the twenties this regime changed radically. Returning to the fixed exchange rate system of the gold standard now became the overriding priority. Monetary policy was reoriented from domestic concerns to the exchange rate. Except for in a few countries, like France and Belgium, who chose not to restore the pre-war parity, severely restrictive policies were required to depress the price level from its inflated level. Given the threat to the parity that might result from deficits, budget balance became the overriding fiscal policy goal, although deficits frequently proved unavoidable.

The main impetus for the regime change derived from the massive post-war inflation – which in the case of Germany escalated into an unparalleled hyper-inflation – was seen as confirmation of the view that expansionary monetary management only achieves nominal effects. Resurrecting the gold standard then was an attempt to provide an external anchor to monetary policies to prevent a repetition of inflationary finance.

The interwar gold standard was short-lived. Between September 1931 and September 1936, all West European countries abandoned the fixed exchange rate for some form of managed floating. The reorientation of monetary management to domestic goals was followed by cheap monetary policies. In a complete reversal of the doctrine of the twenties, monetary expansion was now seen to play a crucial role in promoting growth and investment. In some cases, like Sweden and Norway, the monetary changes were accompanied by some modest deficit spending. In most countries, the breakthrough of Keynesian

ideas did not occur until after the war, but given the buoyant growth of the post-war decades, there were few occasions for practising deficit spending.

Keynesian deficit spending on a significant scale only occurred after 1973 when the combination of an oil price shock and the restrictive macroeconomic policies of the previous years led to substantially higher unemployment throughout Western Europe. But the first half of the seventies marked the beginning of the end of the regime established during the Great Depression. Beginning with the turn to monetary targetting by the Bundesbank in 1974, more and more governments came to the conclusion that Keynesian policies were bankrupt and that macroeconomic management should be primarily oriented to price stability whereas growth and employment were to be addressed by supply-side policies. The election of Margaret Thatcher in 1979 marked the British conversion to monetarism. Three years later French socialist president Mitterrand abandoned Keynesian expansion in favour of macroeconomic austerity. In 1991, finally, the Swedish social democrats also accepted that monetary policies should be geared to fighting inflation rather than unemployment. Although no policy-maker would ever dream of resurrecting a gold standard type system of exchange rates, and curtailment of deficits rather than 'balancing the budget at all costs' has become the goal in fiscal management, the basic principles informing macroeconomic management in Western Europe at present are in many ways similar to what they were in the 1920s.

3 The irrelevance of policy paradigms

Because regime changes in macroeconomic policies are characterized by the adoption of a different view on the causal relationships between policy instruments and target variables, it might seem as if their explanation would necessarily have to accord a prominent role to economic ideas. As Peter Hall has argued:

> After all, the economy is simply a set of human relationships and material flows that cannot be perceived by the naked eye. It must be interpreted or modelled to be understood and from divergent models follow different prescriptions for policy. (Hall 1992:92)

Yet a closer look suggests that the adaptation of a new model, or policy paradigms, is neither a sufficient nor necessary condition for the adoption of new policies.

First, the explicit formulation of Keynesian and monetarist doctrines was not a necessary condition for the adoption of discretionary demand management, or rule-bound monetary policy because such policies have a

much longer lineage. In Keynes's native Britain the notion of countercyclical spending was already contained in the Development and Road Fund Act of 1909 (Winch 1969: 53-55). Proposals for countercyclical public works were also to be found in the Labour Party's 1918 programme (Skidelsky 1967: 40). In Sweden, to give another example, countercyclical fiscal policy was already being employed several years before the outbreak of the First World War (Steiger 1971: 99-110). In Germany, Chancellor Bismarck had advocated countercyclical fiscal policies as far back as the 1880s. In 1919, the German ministry of economic affairs formulated an explicitly countercyclical spending programme (Held 1982: 98-99). Seven years later, the German government even embarked on deficit spending to alleviate unemployment (Clingan 1994). Similarly, the neoclassical belief that expansionary monetary policies cannot durably affect the level of economic activity but will only create inflation, was formulated long before Friedman's monetarism. The earliest theoretical formulation of the Quantity Theory dates back to the mid-eighteenth century, namely to Hume's essay Of Money. Its first formal representation was given by Irving Fisher in 1911.

Second, and more importantly, different policy paradigms do not necessarily give rise to different policy recommendations. Economic doctrines like Keynesianism and neoclassical theory are formulated on such a level of abstraction that, in order to arrive at a policy recommendation, a host of auxiliary assumptions need to be made concerning the state of the world at that time. Given different auxiliary assumptions, it is very well possible to derive similar policy recommendations from rather different economy doctrines or to arrive at sharply different policies from within the same doctrine.

Keynesians are generally said to advocate discretionary demand management, in particular budget deficits, and cheap money in recessions. In this they allegedly differ sharply from their neoclassical colleagues who instead favour tight money and balanced budgets, while seeking the remedy for unemployment on the supply side, i.e. in eliminating those obstacles that prevent markets from adjusting optimally.

In spite of fundamental theoretical differences between the two approaches, it is possible to derive Keynesian-type policies from neoclassical views and vice versa. Changing the emphasis placed on long-term versus short-term effects is the most common road through which Keynesian policies have been advocated with neoclassical justifications. Neoclassical theory does recognize the existence of rigidities in the real world that prevent markets from adjusting instantaneously. It follows that demand management policies can have short-term effects. Arguing that rigidities are likely to exist for a substantial time and/or that the present situation requires immediate remedies provides a neoclassical justification for Keynesian policies.

The most telling instance of such Keynesian policy prescriptions on the basis of neoclassical theory comes from the Great Depression. Notwithstanding that Keynes's General Theory was written as an indictment of Pigou's views on the causes of unemployment, both adversaries could agree on the need for fiscal expansion during the Great Depression. Pigou judged that the rigidities in the British economy were not likely to disappear soon, yet the economic situation was so severe that immediate measures were called for. As he explained in his testimony to the Macmillan commission in May 1930, wage cuts could in theory get rid of unemployment, yet, given the rigidity of British wages, policies like the public works advocated by Keynes were indeed to be recommended (Clarke 1988:176-80). Moreover, Pigou was certainly no exception amongst neoclassical economists. As Mark Blaug (1986: 245) has pointed out, the overwhelming majority of economists in the UK as well as the USA advocated expansionary macroeconomic policies during the Great Depression, although they differed sharply on the correct theoretical justification.[1]

Keynesians may choose to travel the same road in the opposite direction by arguing that demand-management policies are mainly appropriate for the short-term, and by emphasizing that the relevant problems are of a long-term nature. Yet, such an argument involves accepting that Keynesian theory is merely a special case of a more general neoclassical theory. A more common approach has been to argue that demand management, though in theory superior also in the long run, is unavailable in practice due to the constraints of economic openness. A high degree of trade openness implies that a large portion of a fiscal stimulus will leak abroad. Moreover, it can be argued that international financial investors prefer tight, disinflationary macroeconomic policies (Stewart 1983). To avoid an exodus of capital, restrictive macroeconomic policies will need to be pursued even under conditions of unemployment.

The assumption of openness introduces a microeconomic element in the otherwise macroeconomic Keynesian models. Keynesians accept that one single firm can increase the level of employment by reducing wage costs, but deny that such a recipe can work in the aggregate. By analysing the national economy as part of an international system it is possible for Keynesians to, in a logically correct manner, advocate supply-side policies aimed at cutting (relative) domestic costs as a remedy for unemployment. Hence, policy convergence with the (long-term) neoclassical model is complete: macroeconomic policies need to prioritize price stability, and unemployment is to be tackled by supply-side policies. Historically the most telling instances of such convergence, as we shall see below, are the adoption of macroeconomic austerity by leftist governments during the last two decades.

But, if it is possible to arrive at similar prescriptions from different policy paradigms, and to advocate radically different policies without a change in

paradigm, then the notion of policy paradigms is simply inadequate for the analysis of the impact of ideas on policy change. The crucial policy divide apparently does not run between Keynesians and neoclassics but between those representatives of both camps who hold that macroeconomic instruments should be assigned to the goals of growth and employment, and those who advocate price and/or exchange rate stability as the appropriate goal. The implication is that if the impact of ideas on changes in policy-making is to be examined, the notion of ideas should not refer to the paradigms, as is commonly the case, but to the auxiliary assumptions used to derive specific policy prescriptions from a given paradigm.

4 Ideas and interests

The mere fact that policy-makers who advocate different policies hold different ideas does not warrant the conclusion that ideas have a causal influence. As Goldstein & Keohane (1993:11) have pointed out: "Choices of specific ideas may simply reflect the interest of actors."

To argue that political actors employ ideas instrumentally by cloaking particularistic interests in the language of science, has a strong intuitive appeal because the main macroeconomic approaches do display distinct affinities with specific parts of the political spectrum. Keynesianism tends to be most popular amongst the centre-left. It can be interpreted as corroborating the core tenet of the Left, that free markets are unstable and inefficient and hence need to be complemented by a substantial dose of public intervention. The postulate of demand-determined unemployment allows the Left to protect its trade union clientele from demands for income cuts during times of recession while at the same time satisfying its public sector clientele's preference for increased fiscal spending. In contrast, the neoclassical/monetarist tenet that untrammelled markets will tend towards a Pareto equilibrium and that the observed deviations from this equilibrium must be attributed to market obstruction, is much more amenable to the centre-right of the political spectrum. That unemployment is either voluntary or a function of excessive real wages is obviously an attractive proposition for those who stand to gain directly from lower wage costs and for those who are net contributors to the welfare state.

Yet, the argument that ideas are used as cloaks for interests is unsatisfactory for two reasons:

(1) If ideas do serve merely as cloaks, then they are irrelevant to policy decisions. Actors with different interests will adopt different ideas and will steadfastly refuse to be swayed by competing views. Accordingly decision-making would simply be determined by the relative political strength of the relevant interests.

To retain a role for ideas, some form of elitism must be introduced. Some actors must be able to arrive at a decision concerning their preferred policy on the basis of their interests, whereas the majority of actors must be influenced quite substantially by the ongoing discourse. Yet, in this case, the reference to interests becomes irrelevant. To point out that the policy entrepreneurs' 'true' motives were of a self-serving nature may provide a convenient platform from which to launch moralistic attacks. Yet, because in a democratic polity the viability of a given set of policies depends on the ability of policy entrepreneurs to convince a majority of the electorate, the motivation of those who originally advanced a specific view has little relevance for explaining policy-making. It follows that ideas must play an independent role in policy-making, as intellectual persuasion is crucial for the policy preference formation of the electorate.

(2) More importantly, in the case of uncertainty concerning the effects of policies, it is inadmissible to assume that even political entrepreneurs can derive their preferred policies directly from their interests without any interference from ideas. Especially in the field of fiscal management, many policies do admittedly have a clearly identifiable and immediate impact on particular groups. Yet, in general, the impact on the majority of actors will be uncertain (Bates & Krueger 1993: 455-56). Moreover, even in those cases where the immediate impact on certain actors is beyond doubt, the longer-term impact will commonly be uncertain. Consequently, it is generally not possible to depict the decision-making process concerning macroeconomic policies as determined by the interests of the actors involved.

Consider the example of macroeconomic policies for reducing unemployment. The Keynesian response of increased spending on infrastructure projects will no doubt meet with the approval of businesses and employers in the construction sector. The view of the remaining sectors will depend on the macroeconomic effects of such a policy and hence cannot be determined without recourse to some elements of theory. If deficit spending reignites the economic engine, then it will have favourable effects on most actors. If the neoclassical tenet that fiscal expansion will leave GDP unaltered holds, then infrastructural programmes merely redistribute activity, leaving the remainder of the economy worse off. If fiscal spending disrupts the confidence in the currency, it will provoke monetary and fiscal austerity aimed at restoring confidence. A similar story can be told for monetary management. A policy of cheap money will generally be greeted by creditors. If cheap money indeed serves to stimulate aggregate investment it will be beneficial to the economy as a whole. If instead, as neoclassical theory argues, cheap money will only lead to higher inflation in the long-term, such policies would hardly be attractive to the majority of actors. Again, if cheap money is assumed to undermine the currency it must be considered a self-defeating strategy.

5 A 'Darwinian' theory of economic ideas

The fact that it is generally not possible to derive policy preferences directly from interest, however, only establishes that ideas have an independent influence in static contexts and is insufficient for the analysis of the role of ideas in policy change. If only one policy existed that could safeguard the conditions under which governments can survive, ideas would play no role in the evolution of policies. In such a world, policies would converge towards a single point, as governments, in response to policy failure, changed course or were replaced. Consequently, the historical evolution of policy-making would be independent of the ideas of governments even if each individual policy measure is not. Moreover, in such a case a detailed examination of the communicative process that allowed some ideas to spread from their originators to the level of decision-making would not add to the understanding of why specific policies were pursued, but would merely illustrate that there can be numerous paths to the same outcome.

To establish that ideas play an independent role in bringing about policy *change* it will hence be necessary to address the problem of the adequacy of ideas. Is each policy idea viable in the sense that it can produce the expected outcomes, or must some ideas necessarily fail because they fail to conform to the facts of the real world? Was, for example, Prime Minister James Callaghan's (1987: 426) famous pronouncement at the 1976 Labour Party conference that the option of Keynesian deficit spending no longer existed, an idea with as much intrinsic validity as the opposite view that demand management remained the only appropriate way to combat unemployment? Or did Callaghan's view correspond to a fact in the real world with the implication that the decline of Keynesianism had become inevitable?

The pattern of policy convergence in the early twenties, during the Great Depression, and in the seventies and eighties, irrespective of the domestic political balance of power, and on the basis of different ideas, suggests that at times governments have found only a narrow set of policies viable. The demise of the notion, both during the twenties and since the seventies, that macroeconomic management exerts a powerful influence on growth and employment, proved politically and ideologically costly for leftist governments, as it seemed to seriously weaken the case for the superiority of economic interventionism. During the Great Depression, the recognition by both conservative and liberal governments in turn, that the unemployment problem could not be solved without public intervention, undermined the case for the superiority of market solutions. In the absence of serious problems it is implausible to assume that governments could have been persuaded by new ideas to abandon a regime that seemed to conform closely to their main ideological tenets. Moreover, the fact that the new regimes adopted during

these three periods of change had rather similar views on the proper assignment of macroeconomic instruments to goals suggests that ideas played a rather limited role not only in the decline of the old regime but also in the selection of its successor.[2]

Given that ideational arguments provide an unconvincing explanation for the historical pattern of change in European macroeconomics management, this section will sketch an alternative explanation of a 'Darwinian' nature. The argument is Darwinian to the extent that it suggests that regime changes are not driven by the ideas of policy-makers, as only those practices will prove viable over time which conform to the exogenously given criterion of price stability.

5.1 The problem of reflexivity

The notion that outcomes are uniquely determined by the environment is especially widespread in microeconomics. Neoclassical theory predicts that a pure market will establish a unique equilibrium in which the behaviour of firms is determined exogenously, and is independent of the justification firms may give for such behaviour. As Friedman (1953) and Alchian (1950) pointed out in response to evidence that actual firms do not behave in the maximizing way neoclassical theory seems to imply, the reasons and methods by which individual firms arrive at a specific behaviour are irrelevant because only those firms will survive that behave in accordance with the dictates of the market.

To be convincingly employed for issues of economic policy, however, such Darwinian arguments need to address two problems: (1) How can the social world, where the environment is the creation of the actors, generate a unique environmental selection criterion that is independent of the behaviour of those actors? (2) If governments of different political hues have different economic preferences, how can the conditions for their success depend on a single criterion?

The view that behaviour must conform to exogenously given criteria of adequacy would seem appropriate for the physical world where the environment is independent of the actions of its individual elements. In the social world, where the individual actor faces an environment that is the sum of the actions of the other individuals, the notion of an uncoordinated system tending towards a predetermined position would seem inappropriate. As behaviour changes the environment, the criteria according to which environmental selection could operate must themselves be dependent on the behaviour of the actors. Moreover, in case of a conflict between behaviour and the requirements of the environment, it is always possible, in principle, to purposefully change the environment instead of adjusting behaviour.

Accordingly, the environmental constraints on policy-making can never assume the absolute character enjoyed in the physical world. Darwinian arguments can fruitfully be applied to social science only in the weak sense of analysing the constraints evolving from the institutional features that structure social interaction. The policy-making environment is not in continuous flux but structured by a set of relatively inert institutions. In particular, basic institutions like the market economy and political democracy are extremely costly to change. The Darwinian nature of the argument below hence rests on the assumption that the cost of overturning markets and democracy will generally prove to be so overwhelming that these institutions essentially can be interpreted as providing binding constraints on policy-making.

The first step to understanding the nature of these constraints is to note that, due to the reflexive character of social interaction, environmental selection actually plays a much weaker role than postulated by the Darwinian approach of Alchian, Friedman et al. The notion that a perfectly competitive market will establish a unique and Pareto optimal equilibrium is untenable because the constraints each individual actor faces are shaped by the sum of the action of all other actors. This implies that the equilibrium that may be established is not unique but path-dependent. If actors trade at prices that are not the equilibrium prices of the system, they will thereby change the conditions facing other actors, and therefore also the equilibrium (Hahn 1987).

Neoclassical general equilibrium theory does recognize that the problem of reflexivity implies that a general equilibrium will be established only by pure coincidence (Hahn 1984: 125). For the unique Pareto optimal equilibrium to result, extra market devices of coordination have to be assumed. One such device is perfect foresight, i.e. assuming that each individual is perfectly informed about the actions other individuals will undertake in the future. Apart from being obviously unrealistic, this device is logically questionable to the extent that in order for each individual to decide upon a course of action, the decision of all other individuals must already be known (Robinson 1972: 4). Another device is the so-called auctioneer; a (fictitious) coordinating agent that operates outside the market and is assigned the task of determining the equilibrium vector of prices and making it known to the actors before trade takes place. Neither device, however, exists in the real world.

In sum, because the behaviour an individual market actor faces is largely determined by the behaviour of the other market actors, the case for environmental determination of economic outcomes is much weaker than commonly assumed. But, although the inevitable reflexivity of market interaction accords for a larger role for human agency than generally accepted, it allows at the same time for the identification of binding constraint on policy-making. These constraints mainly arise from two factors: (1) The reflexivity of interaction not only implies the presence of multiple-path, dependent

equilibria but also the possibility of cumulative disequilibria, i.e. the dynamic process by which the adjustments individual actors undertake in response to a disequilibrium aggravates the disequilibrium. (2) Whereas under conditions of perfect foresight money mainly functions as a unit of account and medium of exchange, the inevitable uncertainty that market actors face due to reflexivity accords money an important role as store of value, i.e. as a device for (temporarily) not committing resources to economic activity.[3] Binding constraint on economic policy emerges in situations where cumulative disequilibria lead to a progressive cessation of economic activity.

5.2 Coordination and price stability in a monetary economy

In a world where money serves as a store of value, price flexibility no longer necessarily serves as the device through which markets will quickly return to equilibrium. Instead, excessive changes of the general price level may severely disrupt the willingness to engage in productive activity and hence precipitate rather than mitigate economic crises (Keynes 1963: 168-90; Riese 1986; Tobin 1980).

Consider first the case of deflation, i.e. a falling price level. Incidental deflation is harmless. Expectations of ongoing deflation, on the other hand, will aggravate any crisis because it reduces the demand and supply for investment. For industrial borrowers, investment becomes less attractive because deflation increases their real debt and additionally reduces profitability due to the time that elapses between the purchase of raw materials and the sale of finished goods. Deflation also makes lending less attractive because holding money now earns a yield, and because of the increased risk of debt default. Falling investment, however, implies more unemployment. Since wages are part of flexible costs, generalized wage cuts will depress the price level. If labour market institutions therefore react to higher unemployment with nominal wage cuts, the vicious circle is complete.

As Tobin (1980:18) suggests, inflation is the mirror image of deflation. Tight labour markets will generally result in higher nominal wages and, as long as monetary authorities are committed to full employment, in higher prices. Initially, inflation increases the demand for and supply of investment. Inflation increases profitability because of decreasing real indebtedness and the time lag between the start of production and sales, and makes borrowing more attractive. Similarly, the erosion of the value of money and the reduced risk of debt defaults make lending more attractive as compared to the holding of money. More investment, in turn, means more employment. While inflation will stimulate activity initially, the longer-term result is a flight out of money, whereby all wealth holders try to liquidate their holdings of the continuously

depreciating money and financial assets in favour of real assets. Speculation, at this point, becomes a more promising way of increasing and safeguarding wealth than productive investment.

In sum, because modern market economies require a fair degree of price stability to function properly, but cannot provide it themselves, the goal of price stability must be given priority. While socially disagreeable, mass-unemployment as such poses no threat to the functioning of a market economy. Serious disturbances of price stability, on the other hand, disrupt the coordination mechanism and spark vicious circles that may bring the whole process of market interaction to a standstill. Governments may have a rather different ordering of priorities, but these will only prove viable to the extent that they are compatible with a reasonable degree of price stability.

Notwithstanding the current fixation with economic globalization, whether an economy is (financially) open or closed, does not fundamentally change the dynamics. Curtailing international financial transactions does not allow governments to ignore domestic inflation. Continued inflation in an open economy will most likely prompt a switch to a more stable foreign currency. But such a run on the currency is simply the manifestation of a desire to change portfolio allocation, which will take the form of a speculative flight into domestic debt and real estate in a financially closed system. In the absence of domestic inflationary problems, in contrast, financial openness does not imply a necessity for macroeconomic austerity as expansionary policies as long as the government is willing to allow the currency to float (Oatley 1998: 13-18).

5.3 Policy changes and changing ideas

The political hue of the government exerts a significant influence on economic policies. Differences in the balance of political power do give rise to significant cross-national policy differences. Yet, such power politics operate within clearly defined limits, given by the ability of financial and labour market institutions to assure the compatibility of a given macroeconomic policy programme and the requirement of price stability.

Full-employment is a crucial goal for leftist governments. Mass-unemployment seriously affects the well-being of wage earners and makes financing the welfare state increasingly tenuous. Durable growth and full-employment, however, require an expansionary macroeconomic regime in which the labour market parties are able to contain inflationary pressures. Cumulating inflation will generally also rob leftist governments of support. Trade unions increasingly come to dislike the devaluation of their wage contracts resulting from inflation. Rampant financial speculation leads to calls for restrictive measures, especially from the lower-paid wage earners who do not have the means to speculate in

financial markets. And since it is generally, but mistakenly, believed that disinflation by means of a macroeconomic austerity will only cause a short-lived recession, unions are likely to sooner or later defect from a government that cannot stop a runaway inflation. Increasing inflation will also be regarded as a serious threat by savers and pensioners and others who receive non-automatically indexed money transfers. If the economy is open, runs on the currency may provide additional incentives for an anti-inflation policy.

Yet, even without a significant loss of support, leftist governments will also have sufficient incentives for changing course. Runaway inflation implies the loss of control over financial and labour markets. But if the choice is between losing the ability to steer the economy and regaining control at the price of having to pursue restrictive policies, the latter will commonly be preferred. In the extreme case where the fear of the recessionary consequences of a disinflation preclude any restrictive measures, hyperinflation will develop, with the result that the domestic currency ceases to be accepted and productive investment comes to a standstill. But when this ends in mass-unemployment, the last motivation for tolerating inflation is removed.[4]

Conversely, rightist governments cannot pursue a restrictive macroregime indefinitely if they lack the appropriate institutions to contain deflationary pressures. The unemployment consequences of such a constellation may prompt leftist governments to change policies at an earlier stage. Ultimately, when the flight into money ruins the banking system and brings the real economy to a standstill, the industrial and agricultural sectors will also start to have grave doubts about the wisdom of deflation. This leaves liberal and conservative governments the option of changing their policies or being elected out of office.

When old policies fail to achieve the expected effects, a dynamic process is set in motion of groping for a new regime, which satisfies the criterion of price stability. But, as follows from the discussion in section 3, what the causes of policy failure were is always open to numerous interpretations. Accordingly, actors face a potentially infinite menu of options for justifying the policy change. In practice, nevertheless, two constraints can be identified.

(1) The democratic constitution of the polity requires, as a rule, that political parties, which wish to enlist a political majority, must present an economic policy programme that is said to promote growth and employment. Thus, the new policies should be presented as promoting overall economic prosperity. To break a deflationary constellation governements will have to choose expansionary macroeconomic policies and in doing so they will have to abandon the view that such policies will only have inflationary consequences in the somewhat longer run. In turn, the restrictive policies required to combat inflation will either require a resurrection of this view or some kind of argument which holds that governments, due to forces entirely beyond their

control, are not able to pursue expansionary policies.

(2) Because politicians, like most other people, are reluctant to abandon deeply held beliefs, the justifications for new policy regimes will generally involve only the abandonment of previously held 'auxiliary hypotheses', while retaining the core beliefs. Moreover, successful political competition requires that political parties distinguish themselves from their competitors. They should thus be able to justify economic policy strategies in terms of the general philosophy on which their parties are said to be founded. As a result of both mechanisms, different ideological traditions will generally provide sharply different justifications for what may be rather similar policies.

In general terms, the liberal tradition prefers to accommodate regime changes by switching the emphasis from short-term to long-term considerations (and vice versa) within the framework of the neoclassical model that upholds the superiority of market solutions. The social democratic left shows a preference for changing the emphasis placed on the constraints evolving from economic openness within a Keynesian type model. And the Marxist left tends to accommodate regime changes by altering the importance of the alleged policy imperatives of maintaining capitalist accumulation and political legitimacy, with the latter serving as an 'explanation' for expansionary-interventionist regimes and the former as an 'explanation' for liberal-restrictive regimes.

It is important to note that, because the binding constraints on economic management emerge on the level of preventing deflationary or inflationary spirals, policy convergence does not necessarily extend beyond the macroeconomic field. Consider the case of disinflationary regimes like the ones of the 1920s and the present. The mass-unemployment, which characterizes such regimes, tends to be interpreted by the Right as the result of high wages, taxes, and welfare provisions that depress profitability. For the Left, such an interpretation is unacceptable. Unlike the uncertainties that surround macroeconomic management, a strategy of cutting wages and dismantling the welfare state runs unambiguously counter to the interests of its constituency of private sector blue-collar, and public sector labour. Indeed, liberal microeconomic policies question the legitimacy of institutions like trade unions and the welfare state. Accordingly, leftist and rightist governments may differ sharply in their microeconomic approach. Admittedly, the left is in a weaker position to pursue its preferred policies under a regime of low growth, as budget deficits impose strong constraints on welfare state expansion and continued mass-unemployment may erode the ability of trade unions to prevent their members from accepting wage cuts in an effort to safeguard unemployment. Nevertheless, the microeconomic policies of the Left and Right do not converge under such regimes, as Carles Boix, for example, has shown for the present period (Boix 1998).

5.4 Ideas and policy continuity

Whereas ideas play no significant role in explaining regime changes, they do play an important role in accounting for regime inertia. The events that give rise to a regime change generally constitute a trauma that then determines the interpretative framework of economic policy-makers for a long time to come. The dramatic failures of expansionary macroeconomic management in the early twenties and the seventies generally convinced politicians that we live in a world where expansionary policies will necessarily falter either due to excessive inflation or capital flight. Similarly, the failure of macroeconomic austerity in the Great Depression convinced politicians of the need for discretionary management to avert unemployment.

In a world where economic actors always react identically to the same objective signals, those lessons learned from the past are a reliable guide to the future. In a world, however, where behaviour is determined to a considerable extent by expectations, and expectations are in turn partly shaped by government policy, the lessons from the past do not necessarily provide an appropriate guide to the future.

The higher unemployment that resulted from the tight monetary policies of the twenties, seventies and eighties was generally expected to be short-lived. The Keynesian policy-makers of the sixties and seventies generally held that inflation could only rise in tandem with employment. Both sets of expectations were disappointed, without prompting a change in macroeconomic policy assignments. That the tight monetary policies of the twenties and seventies were followed by prolonged periods of mass-unemployment, could be explained by pointing to the pervasiveness of supply-side imperfections. Similarly, the emergence of rising inflation despite rising unemployment in the late sixties and early seventies did not require Keynesians to conclude that the conditions under which such policies could be pursued successfully had changed fundamentally, but could be explained by special circumstances such as the first oil price shock. In sum, to the extent that ideas do influence the development of macroeconomic management their influence is generally moderate as they tend to perpetuate a given regime even if the conditions which gave rise to that regime have long disappeared.[5]

6 From Keynesianism to disinflation: Britain, France and Sweden

Although Britain, France and Sweden all travelled a similar road, from Keynesianism to disinflation, the reasons commonly given for the policy shifts are contradictory. Britain, where the new regime coincided with a shift from a

Keynesian-inspired Labour government to a Conservative government influenced by monetarist ideas, has come to function as the paradigmatic case for the power of ideas. In France, the regime shift was implemented under the socialist government of President Mitterrand. Mitterrand's U-turn of 1982-83 has become the paradigmatic case for those who argue that Keynesianism must fail due to external constraints. In Sweden, in contrast, the newly-elected social democratic government defended full-employment by means of a major devaluation in October 1982. The social democrats there did not switch to a disinflationary regime until 1991. This switch was also largely justified by a reference to external constraints. But, if external constraints left Mitterand no alternative, then the role of ideas in the British case would seem ephemeral. The Swedish policies of the 1980s indicated, however, that there was an alternative. But, in that case, why would a socialist French government use external constraints to justify macroeconomic austerity?

When confronted with a trade-off, Conservative parties tend to give low inflation priority over full-employment. Since the wave of labour unrest in the late sixties, full-employment has increasingly had inflationary consequences. Consequently, some Conservative parties sought a change in policies to the extent that macroeconomic management would no longer guarantee full employment, irrespective of the wage bargains struck. British Conservative prime minister Edward Heath sought to implement such a programme after he was elected in 1970, as did Raymond Barre in France in 1976. In Barre's view monetary policy was to maintain a fixed exchange rate in the EMS, which would serve to impose discipline on domestic wage bargaining. Unemployment was mainly to be tackled by reducing costs and improving the competitiveness of French industry.

Yet such (proto) monetarist policies were politically stillborn as long as a social democratic opposition existed that claimed to have a strategy for combining full-employment and low inflation. During 1972, British unemployment rose from half a million to one million. Fearful of the electoral consequences, Heath changed course and embarked on a programme of macroeconomic expansion and a floating pound sterling, coupled with statutory incomes policies. British unions were not to cooperate. In 1974 the TUC called a strike against the wage policies, which eventually brought down Heath and returned Labour to power under prime minister Harold Wilson. Raymond Barre did not make a U-turn, but his austerity policy brought the socialists a spectacular election victory in 1981.

For the new regime to become politically acceptable the Left had to demonstrate the bankruptcy of the old regime by exhausting all the alternatives to macroeconomic disinflation. First, Keynesian deficit spending had to fail. Second, it had to be shown that wage moderation by means of incomes policy was unworkable. Third, social democrats had to demonstrate that it was not

feasible to ignore higher inflation by pursuing a soft currency policy.

Keynes advocated deficit spending in the Great Depression as an additional measure to boost business confidence when monetary expansion seemed to have few immediate effects. In the understanding of many post-war policy-makers, deficit spending simply created employment irrespective of profitability or confidence. The first lesson they had to learn was that deficit spending, when failing to restore business confidence, leads to endemic budget and current account deficits.

In Sweden, the Conservative coalition, which ruled from 1976 to 1982, demonstrated that this alternative did not exist. Desperate not to have to preside over a substantial rise in unemployment, the government embarked on a massive programme of fiscal spending. Since most OECD countries had turned to austerity, and Swedish competitiveness deteriorated due to above average inflation rates, substantial current account and budget deficits soon emerged. When the Social Democrats returned to office in 1982, they were convinced that the deficit spending strategy was a dead end. As finance minister Feldt (1991:65) argued: "With an already catastrophically large budget deficit, additional loan-financed public expenditures would drive up interest rates even more and curtail investment." (My translation.)

Mitterrand learned this same lesson during his first few months in office. Private sector profitability had already declined sharply as a result of Barre's policies, and Mitterrand's "redistributive Keynesianism" (Hall 1986:193) did nothing to re-ignite investment, nor did the first devaluation of the franc in October 1981. By the time Mitterrand was considering the second devaluation of June 1982 he had become convinced that improving the profitability of the private sector was a precondition for recovery (Favier & Martin-Roland 1990: 410-38). Having obviously forgotten his Keynesian emphasis on the demand side, Mitterrand now argued: "The French are now starting to understand: it is business that creates wealth, it is business that creates employment, it is business that determines our standard of living and our place in the global hierarchy." (Machin & Wright 1985:3. My translation). British policy-makers had learned this lesson earlier. Heath had already recognized in 1972 that fiscal expansion needed to be combined with depreciation to safeguard the competitiveness of British industry. Harold Wilson took a similar approach when he assumed office in 1974.

The realization that deficit spending was unworkable and that profits needed to be improved did not imply a turn to macroeconomic austerity. On the contrary. Tight monetary policies were feared to have damaging effects on private investment. To the extent that domestic inflation was above average, fixed exchange rates would result in a further loss of competitiveness. Moreover, a fixed exchange rate commitment implied having to accept the restrictive policies of the Bundesbank. As Swedish finance minister Feldt (1991:62)

remarked in 1982, a tight monetary policy to defend the exchange rate "could only mean one thing: an additional drop in production and investment with higher unemployment as the inevitable consequence." (My translation.)

The failure of Keynesianism hence led social democratic policy-makers to strategies for stimulating the business sector, without having recourse to macroeconomic austerity. Such strategies mainly consisted of two elements: (1) intensified attempts to reduce wage growth by means of incomes policies; (2) currency depreciation, either as a defensive strategy to compensate for higher domestic inflation rates or as an offensive strategy to improve competitiveness.

In Britain in 1974-75, the Wilson government allowed the pound sterling to float downward to improve competitiveness while simultaneously trying to reach a so-called Social Contract with the trade unions. Mitterrand's second devaluation (June 1982) was accompanied by a four month freeze on prices and wages and a drastic scaling back of fiscal spending. The new Swedish social democratic government started its term in office in October 1982 with a massive devaluation of 16 per cent, while cutting much of the fiscal expenditure programmes of the previous government. The Swedish devaluation was backed up by wage moderation, and had the hoped for effects: speculation against the krona subsided, growth picked up, and unemployment gradually disappeared. By the late eighties, however, relations between employers, unions and the state had become so conflictual that a policy of voluntary moderation was impossible. Inflation increased, financial speculation was rampant and a current account deficit re-emerged. In the autumn of 1990, the krona came under strong pressure again.

In France, the rate of increase of prices and wages did slow down rather dramatically during the freeze of 1982 but started to accelerate again as soon as the freeze was lifted (Muet & Fonteneau 1990: 255). Moreover, the devaluation did little to reduce pressure on the franc. It soon became clear that a third devaluation would be necessary.

Wilson's government was unable to translate its closer links with the unions into wage moderation. During the bargaining year 1974-75, wages exploded and depreciation was not able to restore confidence in the pound. On the contrary, from the summer of 1975 a run on the pound developed which eventually forced the government to apply for IMF assistance. The IMF crisis marked the beginning of Labour's turn to macroeconomic austerity. If the combination of soft currency polices and an expansionary macroeconomic stance led to exploding inflation and currency crises, then Keynesianism was no longer feasible. In his famous speech at the Blackpool Labour Party congress of September 1976 Prime Minister Callaghan (1987: 427) hence pronounced Keynesianism a failure. "Overcoming unemployment now unambiguously depends on our labour costs being at least comparable with those of our major competitors."

As yet, however, Callaghan and his finance minister Healey were still unwilling to use mass-unemployment to bring down inflation. The IMF crisis brought home to the unions the severity of the crisis, and an effective incomes policy now appeared possible. Yet, the success was short-lived as the incomes policy collapsed in a spectacular manner during the winter of 1978.

Once the soft currency strategies coupled with wage restraint had failed, those who still advocated macroeconomic expansion now had to contend with the counter-argument that it would not only lead to massive inflation, but also to an uncontrollable run on the currency. This would require even more macroeconomic austerity to restore confidence. The only theoretical alternative to disinflation at this point was a socialist one. Strict import and exchange controls would be needed to counter capital outflows and deteriorating competitiveness. In addition, a large degree of economic planning seemed necessary given private business's reluctance to invest. The Labour party adopted such a programme in the early eighties, but only after it had been relieved of government responsibility. Governing social democrats considered such a socialist cure worse than any disease it might cure.

Mitterrand, however, still hesitated. Like Feldt, he feared the consequences of macroeconomic disinflation for business investment. As he remarked in September 1982: "The business sector must manage to escape three current threats: the increasing burden of their costs, high interest rates, and the overload of their financial indebtedness." (Favier & Martin-Roland 1990:445. My translation.) Yet the failure of the previous two devaluations had decisively weakened the option of a soft currency strategy as advocated by some industrialists and the so-called CERES fraction in the socialist party. Advocates of this option now argued themselves that substantial controls over external trade were necessary. Moreover, Mitterrand's advisors came to the conclusion that floating the franc would not be an alternative to austerity but would actually require higher interest rates to prevent a cumulative downward spiral. After the third devaluation of March 1983, Mitterrand embarked on macroeconomic austerity and the *franc fort* policy of defending the exchange rate with the DM became the top priority. Macroeconomic disinflation was now no longer said to have negative consequences for investment. Instead the argument became that by pushing French inflation below the level of its competitors, growth and employment would result.

Sweden pursued a similar policy. Notwithstanding fierce protests from the trade unions, the social democratic government abolished exchange controls and linked the currency to the ECU in 1991. Simultaneously, it declared that unemployment would be allowed to increase to stamp out inflation. A renewed devaluation was not considered feasible. Since wage setting was out of control and financial markets were showing the typical signs of an

inflationary flight into real estate, a policy of floating would only have added an uncontrollable currency to the list of problems. SAP policy-makers saw this not as a policy but rather as an abdication from governing the economy.

Feldt (1991:259) had already warned in 1986 what would happen if wage moderation broke down: "If we fail and push inflation up again we ourselves must bear the consequences – a lower standard of living, less employment, and less space for an active reform policy. In that case we might have to start to travel the same dark road as many other countries in Europe." It was left to his successor Allan Larsson to implement such policies. In the budget proposals for 1991, Larsson announced the end of full-employment policies :

> In the long run it is not possible to safeguard employment in an economy which has a higher inflation rate than the surrounding world. In order to protect employment and prosperity, economic policies during the next few years with all strength will have to aim for a permanent reduction in inflation. This task must take priority over all other ambitions and demands. (Finansdepartementet 1990: 4.)

In all three countries, the new strategies were argued to promote profitability, investment, and competitiveness. Yet, interpretations which ran in terms of improving investment, competitiveness and employment now had to be prefixed with the phrase 'in the long run', because the turn to macroeconomic disinflation accomplished the opposite. Britain and Sweden recorded what were amongst the worst recessions in their history in the early eighties, respectively early nineties. In France, where austerity had already been practised during 1976-78, the recession was more moderate. In all countries, unemployment has remained at a high level since the policy change.

That improving profitability now had to be relegated to the long-term, however, was simply a reflection of the fact that combating inflation needed to be given immediate priority. Soft currency strategies could only work in tandem with controls on nominal wage growth. Once domestic inflation was out of control and any increase in import prices was likely to be passed on to higher wages, depreciation could not restore confidence, but served only as a signal that constraint on domestic price-setting had been relaxed further and that inflation was likely to accelerate. Consequently, depreciation strengthened the incentives to flee the currency, and the strategy of restoring business confidence by means of a soft currency, which had worked so well during the Great Depression and at several instances in the post-war decades, now failed.

The justifications for the new policies differed sharply. The French and Swedish socialists justified the new regime almost entirely in terms of external constraints. French finance minister Jacques Delors had started a refrain back in late 1982 that would be repeated often: "There is an international conspiracy against France. They want to smash our experiment and make us devalue a third time." (Connolly 1995: 28.) After the turn to macroeconomic disinflation

had been completed, socialist prime minister Pierre Mauroy explained that the Mitterrand experiment had failed, not because France had failed to control its own inflation, but because other countries had failed to inflate: "A real left-wing policy can be applied in France only if the other European countries also follow policies of the left. If the French resign themselves to living with an inflation [rate] of 12 per cent, then they should know that, because of our economic interdependence with Germany, we will be led into a situation of imbalance. France must rid herself of this inflationary disease." (Goodman 1992:138.) In Sweden, former finance minister Feldt (1994:40), who in the eighties had still maintained that by means of flexible exchange rate management Sweden could walk a "third way" between neoliberal austerity and Keynesianism, now came to the conclusion that a consequence of financial liberalization was the "obvious fact that a single country cannot determine its monetary and exchange rate policies itself, i.e. the level of its interest rates and the external value of its currency."

Since the IMF crisis of 1975-6, the British Labour government had good arguments to justify such a policy change in terms of external constraints. If Labour had stayed in government this would no doubt have happened.[6] For Margaret Thatcher, however, there was no need to justify a change in course defensively as the result of external pressures. In France and Sweden social democratic parties had to justify a 180 degree turn to a constituency which was hostile to macroeconomic austerity, and in the face of opposition parties that claimed that the social democratic project was fundamentally flawed. For Thatcher instead, the apparent inability of Labour to manage the economy provided the ideal opportunity for an aggressive ideological attack on the opponents. External constraints played no role in Thatcher's discourse whatsoever. Instead, Britain's economic problems were depicted as the outcome of Labour's misguided approach. "No theory of government was ever given a fairer test or a more prolonged experiment in a democratic country than democratic socialism received in Britain. Yet it was a miserable failure in every respect." (Thatcher 1993:7.) Monetarism constituted an ideal ideology for the macroeconomic part of such a programme.

The fact that each country had to realize at different junctions that the attempt to pursue an expansionary macroeconomic regime led to accelerating inflation, runs on the currency, deteriorating competitiveness, and increasingly uncontrollable domestic markets did not imply that such policies would always have those effects. The exchange rate crises of 1992 gave a first indication that the reigning macroeconomic convictions might no longer be appropriate. In September of that year, Italy and Britain were forced to leave the EMS. The peseta and escudo devalued, and Sweden and Finland were forced to abandon their link to the ECU. If it had been correct that the possibility of a soft currency strategy no longer existed, depreciation should have sparked higher inflation

and higher interest rates. Nothing of the sort happened. Inflation did not reappear and depreciation restored rather than undermined confidence in the currency, thereby allowing interest rates to come down.

The French franc managed to avoid any significant depreciation. Yet as some of its main competitors were forced out of the EMS, a serious threat to the policy of competitive disinflation emerged. French policy-makers now bitterly complained that other countries were gaining unfair advantage by depreciating. Yet, much of the argument in favour of a *Franc Fort* policy was based on the assumption that alternatives to a fixed exchange rate policy did not exist.

Apparently, there was policy leeway again in the early nineties. But the exchange rate crises did not give rise to a change in regime. As the dire consequences of depreciation did not materialize in the short-run, it was argued that they would materialize in the long-run, if the basic policy orientation was allowed to change. Hence policy-makers took pains to assure the public that the exchange rate crises had been a mere accident which would not lead to macroeconomic policies, and in particular monetary policy, to assume responsibility for growth again.

7 Conclusion

Ideas matter. They certainly matter more than much of modern economics, which still takes a lot of its methodological cues from physics, is ready to admit. In a social world, where the constraints we face are man-made, ideas are bound to have a profound impact. Hence, the renewed emphasis on ideas in the discipline of political economy is a welcome antidote to the structural determinism that still characterizes much of the field.

Yet one should take care not to throw out the baby with the bathwater. Even a social world is not free of constraints and accordingly not every idea can serve as an appropriate basis for economic policy-making. To argue that ideas played an independent role in the advent of macroeconomic disinflation implies the assumption that at any time alternative policies existed which would have been pursued if they had only managed to convince policy-makers. However, the fact that Swedish social democrats, British Conservatives and French socialists all embraced disinflation as the main priority for macroeconomic management did not arise because such views seemed to be the most reasonable alternative to policy-makers at the time when the void left by Keynesianism had to be filled. Rather, the adoption of macroeconomic disinflation was the result of an institutional failure. As West European countries lost the ability to contain price increases by means of (negotiated) nominal wage moderation, there was no alternative to macroeconomic disinflation. Accordingly advocates of

macroeconomic austerity came to dominate policy-making, just as they had done in a similar situation in the early twenties, when the pursuit of expansionary policies was not matched by an institutional capacity for incomes policy.

Whatever their academic credentials may have been, proposals for macroeconomic disinflation were not politically viable until all other alternatives had failed. Indeed, to the policy-makers in all three countries, a soft currency strategy and not macroeconomic disinflation appeared the most attractive alternative to the failed Keynesianism. Yet, such strategies were only viable as long as the removal of the external constraint on wage bargaining did not prompt escalating inflation. Without the ability to contain nominal wages, continuation of a soft currency strategy implied escalating inflation, a flight out of the currency, and hence also the need for high interest rates. The latter, however, implied that a soft currency strategy had ceased to be an alternative to macroeconomic disinflation.

Britain reached this point between the 1976 IMF crisis and the 1978 winter of discontent. And, it was only during this period that the advocates of macroeconomic disinflation dramatically gained strength in the two main parties. Mitterrand reached this point when the second devaluation of 1982 failed to have the hoped for effects, and it was then that he discovered the theme of external constraints. Sweden had the institutional preconditions to pursue such a strategy during the eighties, and accordingly the argument of external constraints, which most West European social democrats had started to embrace already in the mid-seventies, had no impact, even though in theory it should have applied with full force to this small open economy. Also in Sweden, the breakthrough of the advocates of macroeconomic disinflation only arrived with the collapse of the wage-setting system in the early nineties, which made a soft currency strategy infeasible.

In other words, with the breakdown of the ability to apply nominal wage moderation by means other than macroeconomic, the institutional environment had narrowed down the set of alternatives to just one: macroeconomic disinflation. Accordingly, how policy-makers interpreted this constraint, i.e. whether they were seen to arise from economic internalization or from a fundamental flaw in the Keynesian model, had no causal effect on the broad reorientation of the macroeconomic regime. Those ideas only came to play a causal role in the nineties, when all three countries did their best to cling to the restrictive macroeconomic policies despite the absence of an inflationary threat from the labour markets.

It should be pointed out, however, that the conclusion that ideas serve to perpetuate regimes is a historical rather than a theoretical one. It was by no means inevitable that the restrictive policies, to which there was no alternative in the early twenties, would be pursued for so long as to cause the Great Depression. Similarly, there is no necessity for European governments and the

ECB to persevere with a disinflationary regime at a time when roughly 19 million Europeans are out of work and inflation is non-existent. At present, the 'European co-stagnation zone' is clearly in need of new (old) macroeconomic ideas if it is to solve its unemployment problem.

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Notes

1. For a fuller account of the Keynesian myths concerning Pigou's position see Hutchison 1992, chap.6

2. Most studies on the role of ideas in the macroregime changes of the seventies and eighties employ analytical dichotomy; the decline of Keynesianism is explained with reference to some facts of the real world, whereas the role of ideas is confined to selecting the successor from amongst a host of candidates. See Hall 1992, 1993; McNamara 1998.

3. Since holding money yields no pecuniary return, in the absence of uncertainty, there can not be a demand for money as a store of value. See also Davidson 1994, chap. 6.

4. This was how the German hyperinflation of 1920-23 ended.

5. For similar arguments see Temin 1989 on the Great Depression, and Jonung 1999 on Swedish economic policies since the seventies.

6. Denis Healey, Chancellor of the Exchequer during 1974-79, justified his break with Keynesianism as follows: "[Keynes'] theories had two important weaknesses when applied in postwar Britain. They ignored the economic impact of social institutions, particularly the trade unions … And they ignored the outside world." (Healey 1989: 378-79.)

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Party Policy and Cabinet Portfolios in the Netherlands, 1998: Results from an Expert Survey

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Abstract

This research report gives the results of an expert survey conducted among Dutch political scientists around the time of the 1998 election in the Netherlands. It extends and updates a series of expert surveys on party policy positions and the relative importance of cabinet portfolios in the Netherlands. Building on earlier work by Morgan (1976) and Castles and Mair (1984) this present series began in 1989, when Laver and Hunt conducted expert surveys in 24 countries including the Netherlands (Laver and Hunt 1992). The Dutch expert survey was repeated after the 1994 election. Other updates have taken place in Britain (Laver 1998a), Ireland (Laver 1993, 1998b), and Japan (Laver and Kato 1998). Since the first work by Morgan, and Castle and Mair, data reporting expert locations of political parties have been used in a wide range of applications, including studies of coalition behaviour, of the impact of parties on public policy, and of coherence and congruence within party families and transnational party alliances. The ongoing series of national expert surveys, of which this report forms a part, is therefore intended to both add to and update the resources available to scholars engaged in cross-national analyses in these and other fields.

1 Introduction

Although expert surveys have obvious limitations (Budge forthcoming; Mair 1999), they are seen to enjoy three advantages over alternative approaches to estimating party positions. First, precisely because they reflect the judgements of experts, they acquire a certain weight and legitimacy. In particular, they avoid the danger of popular misconceptions, which is a problem with mass surveys, and that of bias, which is a problem with surveys of political elites. Second, they have the advantage of being 'of the moment'; that is, they allow for a judgement of party position based on what the party is currently doing or saying, rather than being based exclusively on assumptions derived from