[ *Joseph E. Stiglitz* ]

# Foreword

It is a pleasure to write this foreword to Karl Polanyi's classic book describing the great transformation of European civilization from the preindustrial world to the era of industrialization, and the shifts in ideas, ideologies, and social and economic policies accompanying it. Because the transformation of European civilization is analogous to the transformation confronting developing countries around the world today, it often seems as if Polanyi is speaking directly to present-day issues. His arguments—and his concerns—are consonant with the issues raised by the rioters and marchers who took to the streets in Seattle and Prague in 1999 and 2000 to oppose the international financial institutions. In his introduction to the 1944 first edition, written when the IMF, the World Bank, and the United Nations existed only on paper, R. M. Maclver displayed a similar prescience, noting, "Of primary importance today is the lesson it carries for the makers of the coming international organization." How much better the policies they advocated might have been had they read, and taken seriously, the lessons of this book!

It is hard, and probably wrong even to attempt to summarize a book of such complexity and subtlety in a few lines. While there are aspects of the language and economics of a book written a half century ago that may make it less accessible today, the issues and perspectives Polanyi raises have not lost their salience. Among his central theses are the ideas that self-regulating markets never work; their deficiencies, not only in their internal workings but also in their consequences (e.g., for the poor), are so great that government intervention becomes necessary; and that the pace of change is of central importance in determining these consequences. Polanyi's analysis makes it clear that popular doctrines of trickle-down economics—that all, including the poor, benefit from growth—have little historical support. He also clarifies the interplay between ideologies and particular interests: how free market ideology was the handmaiden for new industrial interests, and how those interests used that ideology selectively, calling upon government intervention when needed to pursue their own interests.

Polanyi wrote *The Great Transformation* before modern economists clarified the limitations of self-regulating markets. Today, there is no respectable intellectual support for the proposition that markets, by themselves, lead to efficient, let alone equitable outcomes. Whenever information is imperfect or markets are incomplete—that is, essentially always—interventions exist that *in principle* could improve the efficiency of resource allocation. We have moved, by and large, to a more balanced position, one that recognizes both the power and the limitations of markets, and the necessity that government play a large role in the economy, though the bounds of that role remain in dispute. There is general consensus about the importance, for instance, of government regulation of financial markets, but not about the best way this should be done.

There is also plenty of evidence from the modern era supporting historical experience: growth may lead to an increase in poverty. But we also know that growth can bring enormous benefits to most segments in society, as it has in some of the more enlightened advanced industrial countries.

Polanyi stresses the interrelatedness of the doctrines of free labor markets, free trade, and the self-regulating monetary mechanism of the gold standard. His work was thus a precursor to today's dominant systemic approach (and in turn was foreshadowed by the work of general equilibrium economists at the turn of the century). There are still a few economists who adhere to the doctrines of the gold standard, and who see the modern economy's problems as having arisen from a departure from that system, but this presents advocates of the self-regulating market mechanism with an even greater challenge. Flexible exchange rates are the order of the day, and one might argue that this would strengthen the position of those who believe in self-regulation. After all, why should foreign exchange markets be governed by principles that differ from those that determine any other market? But it is also here that the weak underbelly of the doctrines of the self-regulating markets are exposed (at least to those who pay no attention to the *social* consequences of the doctrines)! For there is ample evidence that such markets (like many other asset markets) exhibit excess volatility, that is, greater volatility than can be explained by changes in the underlying fundamentals. There is also ample evidence that seemingly excessive changes in these prices, and investor expectations more broadly, can wreak havoc on an economy. The most recent global financial crisis reminded the current generation of the lessons that their grandparents had learned in the Great Depression: the self-regulating economy does not always work as well as its proponents would like us to believe. Not even the U.S. Treasury (under Republican or Democratic administrations) or the IMF, those institutional bastions of belief in the free market system, believe that governments should *not* intervene in the exchange rate, though they have never presented a coherent and compelling explanation of why this market should be treated differently from other markets.

The IMF's inconsistencies—while professing belief in the free market system, it is a *public* organization that regularly intervenes in exchange rate markets, providing funds to bail out foreign creditors while pushing for usurious interest rates that bankrupt domestic firms—were foreshadowed in the ideological debates of the nineteenth century. Truly free markets for labor or goods have never existed. The irony is that today few even advocate the free flow of labor, and while the advanced industrial countries lecture the less developed countries on the vices of protectionism and government subsidies, they have been more adamant in opening up markets in developing countries than in opening their own markets to the goods and services that represent the developing world's comparative advantage.

Today, however, the battle lines are drawn at a far different place than when Polanyi was writing. As I observed earlier, only diehards would argue for the self-regulating economy, at the one extreme, or for a government run economy, at the other. Everyone is aware of the power of markets, all pay obeisance to its limitations. But with that said, there are important differences among economists' views. Some are easy to dispense with: ideology and special interests masquerading as economic science and good policy. The recent push for financial and capital market liberalization in developing countries (spearheaded by the IMF and the U.S. Treasury) is a case in point. Again, there was little disagreement that many countries had regulations that neither strengthened their financial system nor promoted economic growth, and it was clear that these should be stripped away. But the "free marketeers" went further, with disastrous consequences for countries that followed their advice, as evidenced in the recent global financial crisis. But even before these most recent episodes there was ample evidence that such liberalization could impose enormous risks on a country, and that those risks were borne disproportionately by the poor, while the evidence that such liberalization promoted growth was scanty at best. But there are other issues where the conclusions are far from clear. Free international trade allows a country to take advantage of its comparative advantage, increasing incomes on average, though it may cost some individuals their jobs. But in developing countries with high levels of unemployment, the job destruction that results from trade liberalization may be more evident than the job creation, and this is especially the case in IMF "reform" packages that combine trade liberalization with high interest rates, making job and enterprise creation virtually impossible. No one should have claimed that moving workers from low-productivity jobs to unemployment would either reduce poverty or increase national incomes. Believers in self-regulating markets implicitly believed in a kind of Say's law, that the supply of labor would create its own demand. For capitalists who thrive off of low wages, the high unemployment may even be a benefit, as it puts downward pressure on workers' wage demands. But for economists, the unemployed workers demonstrate a malfunctioning economy, and in all too many countries we see overwhelming evidence of this and other malfunctions. Some advocates of the self-regulating economy put part of the blame for these malfunctions on government itself; but whether this is true or not, the point is that the myth of the self-regulating economy is, today, *virtually* dead.

But Polanyi stresses a particular defect in the self-regulating economy that only recently has been brought back into discussions. It involves the relationship between the economy and society, with how economic systems, or reforms, can affect how individuals relate to one another. Again, as the importance of social relations has increasingly become recognized, the vocabulary has changed. We now talk, for instance, about social capital. We recognize that the extended periods of unemployment, the persistent high levels of inequality, and the pervasive poverty and squalor in much of Latin America has had a disastrous effect on social cohesion, and been a contributing force to the high and rising levels of violence there. We recognize that the manner in which and the speed with which reforms were put into place in Russia eroded social relations, destroyed social capital, and led to the ereation and perhaps the dominance of the Russian Mafia. We recognize that the IMF's elimination of food subsidies in Indonesia, just as wages were plummeting and unemployment rates were soaring, led to predictable (and predicted) political and social turmoil, a possibility that should have been especially apparent given the country's history. In each of these cases, not only did economic policies contribute to a breakdown in long-standing (albeit in some cases, fragile) social relations: the breakdown in social relations itself had very adverse economic effects. Investors were wary about putting their money into countries where social tensions seemed so high, and many within those countries took their money out, thereby creating a negative dynamic.

Most societies have evolved ways of caring for their poor, for their disadvantaged. The industrial age made it increasingly difficult for individuals to take full responsibility for themselves. To be sure, a farmer might lose his crop, and a subsistence farmer has a hard time putting aside money for a rainy day (or more accurately a drought season). But he never lacks for gainful employment. In the modern industrial age, individuals are buffeted by forces beyond their control. If unemployment is high, as it was in the Great Depression, and as it is today in many developing countries, there is little individuals can do. They may or may not buy into lectures from free marketeers about the importance of wage flexibility (code words for accepting being laid off without compensation, or accepting with alacrity a lowering of wages), but they themselves can do little to promote such reforms, even if they had the desired promised effects of full employment. And it is simply not the case that individuals could, by offering to work for a lower wage, immediately obtain employment. Efficiency wage theories, insider-outsider theories, and a host of other theories have provided cogent explanations of why labor markets do not work in the manner that advocates of the self-regulating market suggested. But whatever the explanation, the fact of the matter is that unemployment is not a phantasm, modern societies need ways of dealing with it, and the self-regulating market economy has not done so, at least in ways that are socially acceptable. (There are even explanations for this, but this would draw me too far away from my main themes.) Rapid transformation destroys old coping mechanisms, old safety nets, while it creates a new set of demands, *before new coping mechanisms are developed.* This lesson from the nineteenth century has, unfortunately, all too often been forgotten by the advocates of the Washington consensus, the modern-day version of the liberal orthodoxy

The failure of these social coping mechanisms has, in turn, contributed to the erosion of what I referred to earlier as social capital. The last decade has seen two dramatic instances. I already referred to the disaster in Indonesia, part of the East Asia crisis. During that crisis, the IMF, the U.S. Treasury, and other advocates of the neoliberal doctrines resisted what should have been an important part of the solution: default. The loans were, for the most part, private sector loans to private borrowers; there is a standard way of dealing with situations where borrowers cannot pay what is due: bankruptcy. Bankruptcy is a central part of modern capitalism. But the IMF said no, that bankruptcy would be a violation of the sanctity of contracts. But they had no qualms at all about violating an even more important contract, the social contract. They preferred to provide funds to governments to bail out foreign creditors, who had failed to engage in due diligence in lending. At the same time, the IMF pushed policies with huge costs on innocent bystanders, the workers and small businesses who had no role in the advent of the crisis in the first place.

Even more dramatic were the failures in Russia. The country that had already been the victim of one experiment—communism—was made the subject of a new experiment, that of putting into place the notion of a self-regulating market economy, before *government* had had a chance to put into place the necessary legal and institutional infrastructure. Just as some seventy years earlier, the Bolsheviks had forced a rapid transformation of society, the neoliberals now forced another rapid transformation, with disastrous results. The people of the country had been promised that once market forces were unleashed, the economy would boom: the inefficient system of central planning, that distorted resource allocation, with its absence of incentives from social ownership, would be replaced with decentralization, liberalization, and privatization.

There was no boom. The economy shrank by almost half, and the fraction of those in poverty (on a four-dollar-a-day standard) increased from 2 percent to close to 50 percent. While privatization led a few oligarchs to become billionaires, the government did not even have the money to pay poor pensioners their due—all this in a country rich with natural resources. Capital market liberalization was supposed to signal to the world that this was an attractive place to invest;

but it was a one-way door. Capital left in droves, and not surprisingly. Given the illegitimacy of the privatization process, there was no social consensus behind it. Those who left their money in Russia had every right to fear that they might lose it once a new government was installed. Even apart from these political problems, it is obvious why a rational investor would put his money in the booming U.S. stock market instead of a country in a veritable depression. The doctrines of capital market liberalization provided an open invitation for the oligarchs to take their ill-begotten wealth out of the country. Now, albeit too late, the consequences of those mistaken policies are being realized; but it will be all but impossible to entice the capital that has fled back into the country, except by providing assurances that, regardless of how the wealth is acquired, it can be retained, and doing so would imply, indeed necessitate, the preservation of the oligarchy itself.

Economic science and economic history have come to recognize the validity of Polanyi's key contentions. But public policy—particularly as reflected in the Washington consensus doctrines concerning how the developing world and the economies in transition should make *their* great transformations—seems all too often not to have done so. As I have already noted, Polanyi exposes the *myth* of the free market: there never was a truly free, self-regulating market system. In *their* transformations, the governments of today's industrialized countries took an active role, not only in protecting their industries through tariffs, but also in promoting new technologies. In the United States, the first telegraph line was financed by the federal government in 1842, and the burst of productivity in agriculture that provided the basis of industrialization rested on the government's research, teaching, and extension services. Western Europe maintained capital restrictions until quite recently. Even today, protectionism and government interventions are alive and well: the U.S. government threatens Europe with trade sanctions unless it opens up its markets to bananas owned by American corporations in the Caribbean. While sometimes these interventions are justified as necessary to countervail other governments' interventions, there are numerous instances of truly unabashed protectionism and subsidization, such as those in agriculture. While serving as chairman of the Council of Economic Advisers, I saw case after case—from Mexican tomatoes and avocados to Japanese film to Ukrainian women's cloth coats to Russian uranium. Hong Kong was long held up as the bastion of the free market, but when

Hong Kong saw New York speculators trying to devastate their economy by simultaneously speculating on the stock and currency markets, it intervened massively in both. The American government protested loudly, saying that this was an abrogation of free market principles. Yet Hong Kong's intervention paid off—it managed to stabilize both markets, warding off future threats on its currency, and making large amounts of money on the deals to boot.

The advocates of the neoliberal Washington consensus emphasize that it is government interventions that are the source of the problem; the key to transformation is "getting prices right" and getting the government out of the economy through privatization and liberalization. In this view, development is little more than the accumulation of capital and improvements in the efficiency with which resources are allocated—purely technical matters. This ideology misunderstands the nature of the transformation itself—a transformation of society, not just of the economy, and a transformation of the economy that is far more profound that their simple prescriptions would suggest. Their perspective represents a misreading of history, as Polanyi effectively argues.

If he were writing today, additional evidence would have supported his conclusions. For example, in East Asia, the part of the world that has had the most successful development, governments took an unabashedly central role, and explicitly and implicitly recognized the value of preserving social cohesion, and not only protected social and human capital but enhanced it. Throughout the region, there was not only rapid economic growth, but also marked reductions in poverty. If the failure of communism provided dramatic evidence of the superiority of the market system over socialism, the success of East Asia provided equally dramatic evidence of the superiority of an economy in which government takes an active role to the self-regulating market. It was precisely for this reason that market ideologues appeared almost gleeful during the East Asian crisis, which they felt exposed the active government model's fundamental weaknesses. While, to be sure, their lectures included references to the need for better regulated financial systems, they took this opportunity to push for more market flexibility: code words for eliminating the kind of social contracts that provided an economic security that had enhanced social and political stability—a stability that was the sine qua non of the East Asian miracle.

In truth, of course, the East Asian crisis was the most dramatic illustration of the failure of the self-regulating market: it was the liberalization of the short-term capital flows, the billions of dollars sloshing around the world looking for the highest return, subject to the quick rational and irrational changes in sentiment, that lay at the root of the crisis.

Let me conclude this foreword by returning to two of Polanyi's central themes. The first concerns the complex intertwining of politics and economics. Fascism and communism were not only alternative economic systems; they represented important departures from liberal political traditions. But as Polanyi notes, "Fascism, like socialism, was rooted in a market society that refused to function." The heyday of the neoliberal doctrines was probably 1990—97, after the fall of the Berlin Wall and before the global financial crisis. Some might argue that the end of communism marked the triumph of the market economy, and the belief in the self-regulated market. But that interpretation would, I believe, be wrong. After all, within the developed countries themselves, this period was marked almost everywhere by a rejection of these doctrines, the Reagan-Thatcher free market doctrines, in favor of "New Democrat" or "New Labor" policies. A more convincing interpretation is that during the Cold War, the advanced industrialized countries simply could not risk imposing these policies, which risked hurting the poor so much. These countries had a choice; they were being wooed by the West and the East, and demonstrated failures in the West's prescription risked turning them to the other side. With the fall of the Berlin Wall, these countries had nowhere to go. Risky doctrines could be imposed on them with impunity. But this perspective is not only uncaring; it is also unenlightened: for there are myriad unsavory forms that the rejection of a market economy that does not work at least for the majority, or a large minority, can take. A so-called self-regulating market economy may evolve into Mafia capitalism—and a Mafia political system—a concern that has unfortunately become all too real in some parts of the world.

Polanyi saw the market as part of the broader economy, and the broader economy as part of a still broader society. He saw the market economy not as an end in itself, but as means to more fundamental ends. All too often privatization, liberalization, and even macro-stabilization have been treated as the objectives of reform. Scorecards were kept on how fast different countries were privatizing—never mind that privatization is really easy: all one has to do is give away the assets to one's friends, expecting a kickback in return. But all too often no scorecard was kept on the number of individuals who were pushed into poverty, or the number of jobs destroyed versus those created, or on the increase in violence, or on the increase in the sense of insecurity or the feeling of powerlessness. Polanyi talked about more basic values. The disjunction between these more basic values and the ideology of the self-regulated market is as clear today as it was at the time he wrote. We tell developing countries about the importance of democracy, but then, when it comes to the issues they are most concerned with, those that affect their livelihoods, the economy, they are told: the iron laws of economics give you little or no choice; and since you (through your democratic political process) are likely to mess things up, you must cede key economic decisions, say concerning macroeconomic policy, to an independent central bank, almost always dominated by representatives of the financial community; and to ensure that you act in the interests of the financial community, you are told to focus exclusively on inflation—never mind jobs or growth; and to make sure that you do just that, you are told to impose on the central bank rules, such as expanding the money supply at a constant rate; and when one rule fails to work as had been hoped, another rule is brought out, such as inflation targeting. In short, as we seemingly empower individuals in the former colonies through democracy with one hand, we take it away with the other.

Polanyi ends his book, quite fittingly, with a discussion of freedom in a complex society. Franklin Deleano Roosevelt said, in the midst of the Great Depression, "We have nothing to fear but fear itself." He talked about the importance not only of the classical freedoms (free speech, free press, freedom of assemblage, freedom of religion), but also of freedom from fear and from hunger. Regulations may take away someone's freedom, but in doing so they may enhance another's. The freedom to move capital in and out of a country at will is a freedom that some exercise, at enormous cost to others. (In the economists' jargon, there are large externalities.) Unfortunately, the myth of the self-regulating economy, in either the old guise of laissez-faire or in the new clothing of the Washington consensus, does not represent a balancing of these freedoms, for the poor face a greater sense of insecurity than everyone else, and in some places, such as Russia, the absolute number of those in poverty has soared and living standards have fallen. For these, there is less freedom, less freedom from hunger, less freedom from fear. Were he writing today, I am sure Polanyi would suggest that the challenge facing the global community today is whether it can redress these imbalances—before it is too late.

[ *Fred Block* ]

# Introduction

Xn eminent economic historian, reviewing the reception and influence over the years of *The Great Transformation,* remarked that "some books refuse to go away." It is an apt statement. Although written in the early 1940s, the relevance and importance of Karl Polanyi's work has continued to grow. Although few books these days have a shelf life of more than a few months or years, after more than a half a century *The Great Transformation* remains fresh in many ways. Indeed, it is indispensable for understanding the dilemmas facing global society at the beginning of the twenty-first century.

There is a good explanation for this durability. *The Great Transformation* provides the most powerful critique yet produced of market liberalism—the belief that both national societies and the global economy can and should be organized through self-regulating markets. Since the 1980s, and particularly with the end of the Cold War in the early 1990s, this doctrine of market liberalism—under the labels of Thatcherism, Reaganism, neoliberalism, and "the Washington Con-

I have incurred significant debts in preparing this introduction. The greatest is to Kari Polanyi Levitt, who provided extensive and detailed comments, both substantive and editorial, on several drafts of the introduction. It has been a rare privilege to work with her. Michael Flota, Miriam Joffe-Block, Marguerite Mendell, and Margaret Somers also gave me valuable feedback. Margaret Somers has helped me to understand Polanyi's thought for close to thirty years; much of what I have written reflects her thinking. In addition, Michael Flota provided assistance in the preparation of the introduction and in the larger task of preparing this new edition.

I also owe a considerable debt to Kari Polanyi Levitt and Marguerite Mendell in their roles as the co -directors of the Karl Polanyi Institute of Political Economy, located at Concordia University in Montreal, Quebec. My understanding of Polanyi's thought has been deeply shaped by their collegiality and by the archive they maintain of Polanyi's papers. Readers who want to learn more about Polanyi's thought and the international community of scholars working in this tradition should contact the Karl Polanyi Institute and consult the important series of books, *Critical Perspectives on Historic Issues,* published with Black Rose Press in Montreal.

sensus"—has come to dominate global politics. But shortly after the work was first published in 1944, the Cold War between the United States and the Soviet Union intensified, obscuring the importance of Polanyi's contribution. In the highly polarized debates between the defenders of capitalism and the defenders of Soviet-style socialism, there was little room for Polanyi's nuanced and complex arguments. Hence there is a certain justice that with the ending of the Cold War era, Polanyi's work is beginning to gain the visibility it deserves.

The core debate of this post-Cold War period has been over globalization. Neoliberals have insisted that the new technologies of communications and transportation make it both inevitable and desirable that the world economy be tightly integrated through expanded trade and capital flows and the acceptance of the Anglo-American model of free market capitalism. A variety of movements and theorists around the world have attacked this vision of globalization from different political perspectives—some resisting on the basis of ethnic, religious, national, or regional identities; others upholding alternative visions of global coordination and cooperation. Those on all sides of the debate have much to learn from reading *The Great Transformation;* both neoliberals and their critics will obtain a deeper grasp of the history of market liberalism and an understanding of the tragic consequences of earlier projects of economic globalization.

## Polanyi's Life and Work

Karl Polanyi (1886-1964) was raised in Budapest, in a family remarkable for its social engagement and intellectual achievements.[1] His brother Michael became an important philosopher of science whose work is still widely read. Polanyi himself had been an influential personality in Hungarian student and intellectual circles before World War I. In Vienna, in the 1920s, Polanyi worked as a senior editor

1. A full biography of Polanyi does not yet exist, but much of the relevant material is covered in Marguerite Mendell and Kari Polanyi Levitt, "Karl Polanyi—His Life and *Times" Studies in Political Economy,* no. 22 (spring 1987): 7-39. See also Levitt, ed., *Life and Work of Karl Polanyi* (Montreal: Black Rose Press, 1990); and her essay, "Karl Polanyi as Socialist," in Kenneth McRobbie, ed., *Humanity, Society, and Commitment: On Karl Polanyi* (Montreal: Black Rose Press, 1994). Extensive biographical material is also available in Kenneth McRobbie and Kari Polanyi Levitt, eds., *Karl Polanyi in Vienna* (Montreal: BlackRose Press, 2000). Peter Drucker, the management theorist who knew the Polanyi family in Vienna, has written an amusing account in his memoir *Adventures of a Bystander* (New York: John Wiley, 1994), but many of the specific facts—including some of the names of Polanyi's siblings—are inaccurate.

for the premier economic and financial weekly of Central Europe, *Der Osterreichische Volkswirt.* During this time he first encountered the arguments of Ludwig von Mises and Mises's famous student, Friedrich Hayek. Mises and Hayek were attempting to restore the intellectual legitimacy of market liberalism, which had been badly shaken by the First World War, the Russian Revolution, and the appeal of socialism.[2] In the short term, Mises and Hayek had little influence. From the mid-1930's through the 1960's, Keynesian economic ideas legitimating active government management of economies dominated national policies in the West.[3] But after the Second World War, Mises and Hayek were tireless proponents for market liberalism in the United States and the United Kingdom, and they directly inspired such influential followers as Milton Friedman. Hayek lived until 1992, long enough to feel vindicated by the collapse of the Soviet Union. By the time of his death, he was widely celebrated as the father of neoliberalism—the person who had inspired both Margaret Thatcher and Ronald Reagan to pursue policies of deregulation, liberalization, and privatization. As early as the 1920s, however, Polanyi directly challenged Mises's arguments, and the critique of the market liberals continued as his central theoret-ical concern.

During his tenure at *Der Osterreichische Volkswirt,* Polanyi witnessed the U.S. stock market crash in 1929, the failure of the Vienna Kreditanstalt in 1931, which precipitated the Great Depression, and the rise of fascism. But with Hitler's ascent to power in 1933, Polanyi's socialist views became problematic, and he was asked to resign from the weekly. He left for England, where he worked as a lecturer for the Workers' Educational Association, the extramural outreach arm of the Universities of Oxford and London.[4] Developing his courses led

2. For an account of Ludwig von Mises and Friedrich Hayek from the 1920s through the 1990s, see Richard Cockett, *Thinking the Unthinkable: Think Tanks and the Economic Counter-Revolution, 1931-1983* (London: Fontana Press, 1995). Cockett stresses the irony that England, who invented market liberalism, had to reimport it from Vienna.

3. By coincidence, Polanyi's book was first published in the same year that Hayek published his most famous book, *The Road to Serfdom* (Chicago: University of Chicago Press, 1944). While Polanyi's work celebrated the New Deal in the United States precisely because it placed limits on the influence of market forces, *Hayek's* book insisted that the New Deal reforms placed the United States on a slippery slope that would lead both to economic ruin and a totalitarian regime.

4. Marguerite Mendell, "Karl Polanyi and Socialist Education," in Kenneth McRobbie, ed., *Humanity, Society, and Commitment: On Karl Polanyi* (Montreal: Black Rose Press, 1994), pp. 25-42.

Polanyi to immerse himself in the materials of English social and economic history. In *The Great Transformation*, Polanyi fused these historical materials to his critique of Mises and Hayek's now extraordinarily influential views.

The actual writing of the book was done while Polanyi was a visiting scholar at Bennington College in Vermont in the early 1940s.[5] With the support of a fellowship, he could devote all of his time to writing, and the change of surroundings helped Polanyi synthesize the different strands of his argument. In fact, one of the book's enduring contributions—its focus on the institutions that regulate the global economy—was directly linked to Polanyi's multiple exiles. His moves from Budapest to Vienna to England and then to the United States, combined with a deep sense of moral responsibility, made Polanyi a kind of world citizen. Toward the end of his life he wrote to an old friend: "My life was a 'world' life—I lived the life of the human world.... My work is for Asia, for Africa, for the new peoples."[6] While he retained a deep attachment to his native Hungary, Polanyi transcended a Eurocentric view and grasped the ways that aggressive forms of nationalism had been fostered and supported by a certain set of global economic arrangements.

In the years after World War II, Polanyi taught at Columbia University in New York City, where he and his students engaged in anthropological research on money, trade, and markets in precapitalist societies. With Conrad M. Arensberg and Harry W Pearson, he published *Trade and Market in the Early Empires;* later, his students prepared for publication posthumous volumes based on Polanyi's work of this period. Abraham Rotstein assisted with the publication of *Dahomey and the Slave Trade;* George Dalton edited a collection of previously published essays, including excerpts from *The Great Transformation*, in *Primitive, Archaic, and Modern Economies: Essays of Karl Polanyi;* and Pearson also compiled *The Livelihood of Man* from Polanyi's Columbia lecture notes.[7]

5. Polanyi wrote the book in English; he had been fluent in the language since childhood.

6. Letter to Be de Waard, January 6,1958, cited by Ilona Duczynska Polanyi, "I First Met Karl Polanyi in 1920 .. .," in Kenneth McRobbie and Kari Polanyi Levitt, eds., *Karl Polanyiin Vienna* (Montreal: Black Rose Press, 2000), pp. 313,302-15.

7. Karl Polanyi, Conrad M. Arensberg, and Harry W. Pearson, eds., *Trade and Market in the Early Empires: Economies in History and Theory* (Glencoe, 111.: Free Press, 1957); Polanyi, *Dahomey and the Slave Trade: An Analysis of an Archaic Economy* (Seattle: University of Washington, 1966); George Dalton, ed., *Primitive, Archaic, and Mod-*

## Polanyi's Argument: Structure and Theory

*The Great Transformation* is organized into three parts. Parts One and Three focus on the immediate circumstances that produced the First World War, the Great Depression, the rise of fascism in Continental Europe, the New Deal in the United States, and the first five-year plan in the Soviet Union. In these introductory and concluding chapters, Polanyi sets up a puzzle: Why did a prolonged period of relative peace and prosperity in Europe, lasting from 1815 to 1914, suddenly give way to a world war followed by an economic collapse? Part Two—the core of the book—provides Polanyi's solution to the puzzle. Going back to the English Industrial Revolution, in the first years of the nineteenth century, Polanyi shows how English thinkers responded to the disruptions of early industrialization by developing the theory of market liberalism, with its core belief that human society should be subordinated to self-regulating markets. As a result of England's leading role as "workshop of the world," he explains, these beliefs became the organizing principle for the world economy. In the second half of Part Two, chapters 11 through 18, Polanyi argues that market liberalism produced an inevitable response—concerted efforts to protect society from the market. These efforts meant that market liberalism could not work as intended, and the institutions governing the global economy created increasing tensions within and among nations. Polanyi traces the collapse of peace that led to World War I and shows the collapse of economic order that led to the Great Depression to be the direct consequence of attempting to organize the global economy on the basis of market liberalism. The second "great transformation"—the rise of fascism—is a result of the first one—the rise of market liberalism.

In making his argument, Polanyi draws on his vast reading of history, anthropology, and social theory.[8] *The Great Transformation* has important things to say on historical events from the fifteenth century to World War II; it also makes original contributions on topics as diverse as the role of reciprocity and redistribution in premodern societies, the limitations of classical economic thought, and the dangers of

*em Economics: Essays of Karl Polyani* (1968; reprint, Boston: Beacon Press, 1971); and Harry W. Pearson, ed., *The Livelihood of Man* (New York: Academic Press, 1977).

8. For an analysis of some of Polanyi's key sources, see Margaret Somers, "Karl Polanyi's Intellectual Legacy," in Kari Polanyi Levitt, ed., *Life and Work of Karl Polanyi* (Montreal: BlackRose Press, 1990), pp. 152-58.

commodifying nature. Many contemporary social scientists—anthropologists, political scientists, sociologists, historians, and economists—have found theoretical inspiration from Polanyi's arguments. Today a growing number of books and articles are framed around key quotations from *The Great Transformation.*

Because of the very richness of this book, it is futile to try to summarize it; the best that can be done here is to elaborate some of the main strands of Polanyi's argument. But doing this first requires recognizing the originality of his theoretical position. Polanyi does not fit easily into standard mappings of the political landscape; although he agreed with much of Keynes's critique of market liberalism, he was hardly a Keynesian. He identified throughout his life as a socialist, but he had profound differences with economic determinism of all varieties, including mainstream Marxism.[9] His very definition of capitalism and socialism diverges from customary understandings of those concepts.

## POLANYI'S CONCEPT OF EMBEDDEDNESS

The logical starting point for explaining Polanyi's thinking is his concept of embeddedness. Perhaps his most famous contribution to social thought, this concept has also been a source of enormous confusion. Polanyi starts by emphasizing that the entire tradition of modern economic thought, continuing up to the present moment, rests on the concept of the economy as an interlocking system of markets that automatically adjusts supply and demand through the price mechanism. Even when economists acknowledge that the market system sometimes need help from government to overcome market failure, they still rely on this concept of the economy as an equilibrating system of integrated markets. Polanyi's intent is to show how sharply this concept differs from the reality of human societies throughout recorded human history. Before the nineteenth century, he insists, the human economy was always embedded in society.

The term "embeddedness" expresses the idea that the economy is

9. Polanyi's relationship to Marxism is one of the most complex and debated issues in the literature. See Mendell and Polanyi Levitt, "Karl Polanyi—His Life and Times"; Fred Block and Margaret Somers, "Beyond the Economistic Fallacy: The Holistic Social Science of Karl Polanyi," in Theda Skocpol, ed., *Vision and Method in Historical Sociology* (Cambridge: Cambridge University Press, 1984), pp. 47-84; Rhoda H. Haperin, *Cultural Economies: Past and Present* (Austin: University of Texas Press, 1994).

not autonomous, as it must be in economic theory, but subordinated to politics, religion, and social relations.[10] Polanyi's use of the term suggests more than the now familiar idea that market transactions depend on trust, mutual understanding, and legal enforcement of contracts. He uses the concept to highlight how radical a break the classical economists, especially Malthus and Ricardo, made with previous thinkers. Instead of the historically normal pattern of subordinating the economy to society, their system of self-regulating markets required subordinating society to the logic of the market: He writes in Part One: "Ultimately that is why the control of the economic system by the market is of overwhelming consequence to the whole organization of society: it means no less than the running of society as an adjunct to the market. Instead of economy being embedded in social relations, social relations are embedded in the economic system." Yet this and similar passages lend themselves to a misreading of Polanyi's argument. Polanyi is often mistakenly understood to be saying that with the rise of capitalism in the nineteenth century, the economy was successfully disembedded from society and came to dominate it.[11]

This misreading obscures the originality and theoretical richness of Polanyi's argument. Polanyi does say that the classical economists wanted to create a society in which the economy had been effectively disembedded, and they encouraged politicians to pursue this objective. Yet he also insists that they *did not* and *could not* achieve this goal. In fact, Polanyi repeatedly says that the goal of a disembedded, fully self-regulating market economy is a Utopian project; it is something that cannot exist. On the opening page of Part One, for example, he writes: "Our thesis is that the idea of a self-adjusting market implied a

10. Polanyi's concept of embeddedness has been borrowed and elaborated on by important contemporary scholars, including John Ruggie, "International Regimes, Transactions, and Change: Embedded Liberalism in the Postwar Economic Order," *International Organization* 36 (spring 1982): 379-415; Mark Granovetter, "Economic Action and Social Structure: The Problem of Embeddedness," *American Journal of Sociology* 91 (November 1985): 481-510; and Peter Evans, *Embedded Autonomy: States and Industrial Transformation* (Princeton, N.J.: Princeton University Press, 1995). The precise inspiration for the coinage is not known, but it seems plausible that Polanyi drew the metaphor from coal mining. In researching English economic history, he read extensively on the history and technologies of the English mining industry that faced the task of extracting coal that was embedded in the rock walls of the mine.

11. No less a figure than the great French historian Fernand Braudel reads Polanyi in this way. See Braudel, *Civilization and Capitalism Fifteenth-Eighteenth Century,* vol. 2, *The Wheels of Commerce,* trans. Sian Reynolds (Berkeley: University of California Press, 1992), pp. 225-29.

stark Utopia. Such an institution could not exist for any length of time without annihilating the human and natural substance of society; it would have physcially destroyed man and transformed his surroundings into a wilderness."

WHY DISEMBEDDING CANNOT BE SUCCESSFUL

Polanyi argues that creating a fully self-regulating market economy requires that human beings and the natural environment be turned into pure commodities, which assures the destruction of both society and the natural environment. In his view the theorists of self-regulating markets and their allies are constantly pushing human societies to the edge of a precipice. But as the consequences of unrestrained markets become apparent, people resist; they refuse to act like lemmings marching over a cliff to their own destruction. Instead, they retreat from the tenets of market self-regulation to save society and nature from destruction. In this sense one might say that disembedding the market is similar to stretching a giant elastic band. Efforts to bring about greater autonomy of the market increase the tension level. With further stretching, either the band will snap—representing social disintegration—or the economy will revert to a more embedded position.

The logic underlying this argument rests on Polanyi's distinction between real and fictitious commodities. For Polanyi the definition of a commodity is something that has been produced for sale on a market. By this definition land, labor, and money are fictitious commodities because they were not originally produced to be sold on a market. Labor is simply the activity of human beings, land is subdivided nature, and the supply of money and credit in modern societies is necessarily shaped by governmental policies. Modern economics starts by pretending that these fictitious commodities will behave in the same way as real commodities, but Polanyi insists that this sleight of hand has fatal consequences. It means that economic theorizing is based on a lie, and this lie places human society at risk.

There are two levels to Polanyi's argument. The first is a moral argument that it is simply wrong to treat nature and human beings as objects whose price will be determined entirely by the market. Such a concept violates the principles that have governed societies for centuries: nature and human life have almost always been recognized as having a sacred dimension. It is impossible to reconcile this sacred dimension with the subordination of labor and nature to the market. In his objection to the treatment of nature as a commodity, Polanyi anticipates many of the arguments of contemporary environmentalists.[12]

The second level of Polanyi's argument centers on the state's role in the economy[13] Even though the economy is supposed to be self-regulating, the state *must* play the ongoing role of adjusting the supply of money and credit to avoid the twin dangers of inflation and deflation. Similarly, the state has to manage shifting demand for employees by providing relief in periods of unemployment, by educating and training future workers, and by seeking to influence migration flows. In the case of land, governments have sought to maintain continuity in food production by a variety of devices that insulate farmers from the pressures of fluctuating harvests and volatile prices. In urban areas governments manage the use of the existing land through both environmental and land-use regulations. In short, the role of managing fictitious commodities places the state inside three of the most important markets; it becomes utterly impossible to sustain market liberalism's view that the state is "outside" of the economy.[14]

The fictitious commodities explain the impossibility of disembedding the economy. Real market societies *need* the state to play an active role in managing markets, and that role requires political decision making; it cannot be reduced to some kind of technical or administrative function.[15] When state policies move in the direction of disem-

12. For an indication of his influence on environmental economics, see Herman E. Daly and John B. Cobb Jr., *For the Common Good: Redirecting the Economy toward Community, theEnvironment, and a Sustainable Future* (Boston: Beacon Press, 1989).

13. Implicit in Polanyi's argument is a more specific critique of the market as a self-regulating mechanism. In the case of manufactured commodities, a falling price for an abundant commodity restores equilibrium by both encouraging increased consumption *and* by discouraging new production. In the case of fictitious commodities, the effectiveness of the price mechanism is reduced because automatic increases or decreases in supply cannot be assumed.

14. For many other commodities as well, government involvement is a precondition for market competition. See the aptly titled book by Steven Vogel, *Freer Markets, More Rules: Regulatory Reform in Advanced Industrial Countries* (Ithaca, N.Y.: Cornell University Press, 1996).

15. Monetarists have tried repeatedly without success to establish a fixed rule for managing the growth of the money supply that would eliminate the discretion of central bankers. In the absence of such a formula, the next recourse is to obscure the political role of central bankers by attributing to them quasi-religious and oracular author-

bedding through placing greater reliance on market self-regulation, ordinary people are forced to bear higher costs. Workers and their families are made more vulnerable to unemployment, farmers are exposed to greater competition from imports, and both groups are required to get by with reduced entitlements to assistance. It often takes *greater* state efforts to assure that these groups will bear these increased costs without engaging in disruptive political actions. This is part of what Polanyi means by his claim that "laissez-faire was planned"; it requires statecraft and repression to impose the logic of the market and its attendant risks on ordinary people.[16]

## THE CONSEQUENCES OF IMPOSSIBILITY

The efforts of free market theorists to disembed the economy from society are doomed to fail. But the very utopianism of market liberalism is a source of its extraordinary intellectual resilience. Because societies invariably draw back from the brink of full-scale experimentation with market self-regulation, its theorists can always claim that any failures were not the result of the design but of a lack of political will in its implementation. The creed of market self-regulation thus cannot be discredited by historical experiences; its advocates have an airtight excuse for its failures. This has occurred most recently in the effort to impose market capitalism on the former Soviet Union through "shock therapy." Although the failure of this effort is obvious for all to see, defenders of "shock therapy" continue to blame the failure on politicians who caved too quickly to political pressures; had they only persisted, the promised benefits of a rapid shift to the market would have been realized.[17]

ity. See William Greider, *Secrets of the Temple: How the Federal Reserve Runs the Country* (New York: Simon & Schuster, 1987).

16. This is Polanyi's central point in his account of the New Poor Law in England; the creation of a labor market required a dramatic increase in the state's repressive powers. On this point Polanyi's interpretation has been supported by later scholars, especially Karel Williams, *From Pauperism to Poverty* (London: Routledge, 1981). On Speenhamland, a number of Polanyi's arguments have been called into question. Two important but conflicting accounts of the Old Poor Law are provided in K. D. M. Snell, *Annals of the Labouring Poor: Social Change and Agrarian England, 1660-1900* (Cambridge: Cambridge University Press, 1985); and George Boyer, *An Economic History of the English Poor Law, 1/50-1850* (Cambridge: Cambridge University Press, 1990).

17. For explicitly Polanyian discussions of the transition in Eastern Europe and the former Soviet Union, see Maurice Glasman, *Unnecessary Suffering: Managing Market*

Polanyi's extreme skepticism about disembedding the economy is also the source of his powerful argument about the "double movement." Because efforts to disembed the economy from society inevitably encounter resistance, Polanyi argues that market societies are constituted by two opposing movements—the laissez-faire movement to expand the scope of the market, and the protective countermovement that emerges to resist the disembedding of the economy. Although the working-class movement has been a key part of the protective countermovement, Polanyi explicitly states that all groups in society have participated in this project. When periodic economic downturns destroyed the banking system, for example, business groups insisted that central banking be strengthened to insulate the domestic supply of credit from the pressures of the global market.[18] In a word even capitalists periodically resist the uncertainty and fluctuations that market self-regulation produces and participate in efforts to increase stability and predictability through forms of protection.

Polanyi is insistent that "laissez-faire was planned; planning was not." He explicitly attacks market liberals who blamed a "collectivist conspiracy" for erecting protective barriers against the working of global markets. He argues, instead, that this creation of barriers was a spontaneous and unplanned response by all groups in society against the impossible pressures of a self-regulating market system. The protective countermovement *had* to happen to prevent the disaster of a disembedded economy. Polanyi suggests that movement toward a laissez-faire economy needs the countermovement to create stability. When, for example, the movement for laissez-faire is too powerful, as in the 1920s (or the 1990s) in the United States, speculative excesses and growing inequality destroy the foundations for continuing prosperity. And although Polanyi's sympathies are generally with the protective countermovement, he also recognizes that it can sometimes create a dangerous political-economic stalemate. His analysis of the rise of fascism in Europe acknowledges that when neither movement was able to impose its solution to the crisis, tensions increased until

*Utopia* (London: Verso, 1996); John Gray, *False Dawn: The Delusions of Global Capitalism* (London: Granta Books, 1998); and David Woodruff, *Money Unmade: Barter and tlteFate of Russian Capitalism* (Ithaca, N.Y.: Cornell University Press, 1999).

18. Polanyi writes in chapter 16: "Modern central banking, in effect, was essentially a device developed for the purpose of offering protection without which the market would have destroyed its own children, the business enterprises of all kinds."

fascism gained the strength to seize power and break with both laissez-faire and democracy.[19]

Polanyi's thesis of the double movement contrasts strongly with both market liberalism and orthodox Marxism in the range of possibilities that are imagined at any particular moment. Both market liberalism and Marxism argue that societies have only two real choices: there can be market capitalism or socialism. Although they have opposing preferences, the two positions agree in excluding any other alternatives. Polanyi, in contrast, insists that free market capitalism is not a real choice; it is only a Utopian vision. Moreover, in chapter 19 he defines socialism as "the tendency inherent in an industrial civilization to transcend the self-regulating market by consciously subordinating it to a democratic society." This definition allows for a continuing role for markets within socialist societies. Polanyi suggests that there are different possibilities available at any historical moment, since markets can be embedded in many different ways. To be sure, some of these forms will be more efficient in their ability to expand output and foster innovation, and some will be more "socialist" in subordinating the market to democratic direction, but Polanyi implies that alternatives that are both efficient and democratic were available both in the nineteenth and twentieth centuries.[20]

## THE CENTRALITY OF THE GLOBAL REGIME

Yet Polanyi is far too sophisticated a thinker to imagine that individual countries are free to choose the particular way in which they want to reconcile the two sides of the double movement. On the contrary, Polanyi's argument is relevant to the current global situation precisely because he places the rules governing the world economy at the center of his framework. His argument about the rise of fascism in the interwar period pivots on the role of the international gold stan-

19. Polanyi addresses fascism in "The Essence of Fascism" in J. Lewis, K. Polanyi, andD. K. Kitchin, eds., *Christianity and the Social Revolution* (London: Gollanz, 1935), PP- 359-94-

20. Polanyi inspired a school of thought that flowered in the 1980s and 1990s that has analyzed the "varieties of capitalism," showing the very significant differences in the ways that markets are embedded in the United States as compared with France, Germany, Japan, and other nations. See Rogers Hollingsworth and Robert Boyer, eds., *Contemporary Capitalism: The Embeddedness of Institutions* (Cambridge: Cambridge University Press, 1997); and Colin Crouch and Wolfgang Streeck, *Political Economy of Modern Capitalism: Mapping Convergence and Diversity* (Thousand Oaks, Calif: Sage, 1997)-

dard in constraining the political options that were available to actors within countries. To understand this part of Polanyi's argument requires a brief excursion into the logic of the gold standard, but this excursion is hardly a digression, because the underlying purposes of the gold standard continue to exert a powerful influence on contemporary market liberals. Polanyi saw the gold standard as an extraordinary intellectual achievement;[21] it was an institutional innovation that put the theory of self-regulating markets into practice, and once in place it had the power to make self-regulating markets appear to be natural.

Market liberals wanted to create a world with maximal opportunities to extend the scope of markets internationally, but they had to find a way that people in different countries with different currencies could freely engage in transactions with each other. They reasoned that if every country conformed to three simple rules, the global economy would have the perfect mechanism for global self-regulation. First, each country would set the value of its currency in relation to a fixed amount of gold and would commit to buying and selling gold at that price. Second, each country would base its domestic money supply on the quantity of gold that it held in its reserves, its circulating currency would be backed by gold. Third, each country would endeavor to give its residents maximal freedom to engage in international economic transactions.

The gold standard put a fantastic machinery of global self-regulation into place. Firms in England were able to export goods and invest in all parts of the world, confident that the currencies they earned would be as "good as gold." In theory, if a country is in a deficit position in a given year because its citizens spent more abroad than they earned, gold flows out of that country's reserves to clear payments due to foreigners.[22] The domestic supply of money and credit auto-

21. The idea was first elaborated by Isaac Gervaise and David Hume in the eighteenth century. Frank Fetter, *Development of British Monetary Orthodoxy, 1797-18/5* (Cambridge: Harvard University Press, 1965), p. 4.

22. The mechanism by which the gold would flow out is equally ingenious and requires no governmental action. Because people in the deficit nation are spending more abroad than they are taking in, their currency—being in greater supply—will fall in value relative to other currencies. When that value falls below a certain level called the gold point, it will be profitable for international bankers to trade that currency for gold and ship the gold abroad where it will bring a higher price. In this way gold will move from deficit countries to surplus countries.

matically shrinks, interest rates rise, prices and wages fall, demand for imports declines, and exports become more competitive. The country's deficit would therefore be self-liquidating. Without the heavy hand of government, each nation's international accounts would reach a balance. The globe would be unified into a single market place without the need for some kind of world government or global financial authority; sovereignty would remain divided among many nation-states whose self-interest would lead them to adopt the gold standard rules voluntarily.

## CONSEQUENCES OF THE GOLD STANDARD

The gold standard was intended to create an integrated global marketplace that reduced the role of national units and national governments, but its consequences were exactly the opposite.[23] Polanyi shows that when it was widely adopted in the 1870s, it had the ironic effect of intensifying the importance of the nation as a unified entity. Although market liberals dreamed of a pacified world in which the only international struggles would be those of individuals and firms to outperform their competitors, their efforts to realize these dreams through the gold standard produced two horrific world wars.

The reality was that the simple rules of the gold standard imposed on people economic costs that were literally unbearable. When a nation's internal price structure diverged from international price levels, the *only* legitimate means for that country to adjust to the drain of gold reserves was by deflation. This meant allowing its economy to contract until declining wages reduced consumption enough to restore external balance. This implied dramatic declines in wages and farm income, increases in unemployment, and a sharp rise in business and bank failures.

It was not just workers and farmers who found the costs of this type of adjustment to be high. The business community itself could not tolerate the resulting uncertainty and instability. Hence, almost as soon as the gold standard mechanism was in place, entire societies began to collude in trying to offset its impact. A first recourse was for countries to increase their use of protective tariffs for both agricul-

23. As Polanyi knew, in practice the operation of the gold standard diverged considerably from theory. See Barry Eichengreen, *Globalizing Capital: A History of the International Monetary System* (Princeton, N.J.: Princeton University Press, 1996).

tural and manufactured goods.[24] By making trade flows less sensitive to price changes, countries could gain some degree of greater predictability in their international transactions and be less vulnerable to sudden and unanticipated gold outflows.

A further expedient was the rush by the major European powers, the United States, and Japan to establish formal colonies in the last quarter of the nineteenth century. The logic of free trade had been strongly anticolonial, because the costs of empire would not be offset by corresponding benefits if all traders had access to the same markets and investment opportunities. But with the rise of protectionism in international trade, this calculation was reversed. Newly acquired colonies would be protected by the imperial powers' tariffs, and the colonizers' traders would have privileged access to the colonies' markets and raw materials. The "rush to empire" of this period intensified the political, military, and economic rivalry between England and Germany that culminated in the First World War.[25]

For Polanyi the imperialist impulse cannot be found somewhere in the genetic code of nations; rather, it materializes as nations struggle to find some way to protect themselves from the relentless pressures of the gold standard system. The flow of resources from a lucrative colony might save the nation from a wrenching crisis caused by a sudden outflow of gold, and the exploitation of the overseas populations might help keep domestic class relations from becoming even more explosive.

Polanyi argues that the utopianism of the market liberals led them to invent the gold standard as a mechanism that would bring a borderless world of growing prosperity. Instead, the relentless shocks of the gold standard forced nations to consolidate themselves around heightened national and then imperial boundaries. The gold standard continued to exert disciplinary pressure on nations, but its functioning was effectively undermined by the rise of various forms of protec-

24. Peter Gourevitch, *Politics in Hard Times: Comparative Responses to International Economic Crises* (Ithaca, N.Y.: Cornell University Press, 1986), chap. 3; Christopher Chase-Dunn, Yukio Kawano, and Benjamin Brewer, "Trade Globalization since 1795: Waves of Integration in the World-System" *American Sociological Review* 65 (February 2000): 77-95.

25. Polanyi's argument is quite different from Lenin's thesis that intensifying interimperialist conflicts are a product of the growth of finance capital in the final stage of capitalist development. Polanyi takes pains to argue that financial capitalists can be a major force for preventing war.

tionism, from tariff barriers to empires. And yet even when this entire contradictory system came crashing down with the First World War, the gold standard was so taken for granted that statesmen mobilized to restore it. The whole drama was tragically played out again in the 1920s and 1930s, as nations were forced to choose between protecting the exchange rate and protecting their citizens. It was out of this stalemate that fascism emerged. In Polanyi's view the fascist impulse—to protect society from the market by sacrificing human freedom—was universal, but local contingencies determined where fascist regimes were successful in taking power.

## Contemporary Relevance

Polanyi's arguments are so important for contemporary debates about globalization because neoliberals embrace the same Utopian vision that inspired the gold standard. Since the end of the Cold War, they have insisted that the integration of the global economy is making national boundaries obsolete and is laying the basis for a new era of global peace. Once nations recognize the logic of the global marketplace and open their economies to free movement of goods and capital, international conflict will be replaced by benign competition to produce ever more exciting goods and services. As did their predecessors, neoliberals insist that all nations have to do is trust in the effectiveness of self-regulating markets.

To be sure, the current global financial system is quite different from the gold standard. Exchange rates and national currencies are no longer fixed in relation to gold; most currencies are allowed to fluctuate in value on the foreign exchange markets. There are also powerful international financial institutions, such as the International Monetary Fund and the World Bank, that play a major role in managing the global system. But behind these important differences there lies a fundamental commonality—the belief that if individuals and firms are given maximum freedom to pursue their economic self-interest, the global marketplace will make everyone better off.

This fundamental belief lies behind the systematic efforts of neoliberals to dismantle restraints on trade and capital flows and to reduce governmental "interference" in the organization of economic life. Thomas Friedman, an influential defender of globalization, writes: "When your country recognizes... the rules of the free market in today's global economy, and decides to abide by them, it puts on what I call 'the Golden Straitjacket.' The Golden Straitjacket is the defining polical-economic garment of this globalization era. The Cold War had the Mao suit, the Nehru j acket, the Russian fur. Globalization has only the Golden Straitjacket. If your country has not been fitted for one, it will be soon."[26] Friedman goes on to say that the "golden straitjacket" requires shrinking the state, removing restrictions on trade and capital movements, and deregulating capital markets. Moreover, he cheerfully describe how the constraints of this garment are enforced by the "electronic herd" of international traders on foreign exchange and financial markets.

Polanyi's analysis of the three fictitious commodities teaches that this neoliberal vision of automatic market adjustment at the global level is a dangerous fantasy. Just as national economies depend on an active governmental role, so too does the global economy need strong regulatory institutions, including a lender of last resort. Without such institutions particular economies—and perhaps the entire global economy—will suffer crippling economic crises.

But the more fundamental point learned from Polanyi is that market liberalism makes demands on ordinary people that are simply not sustainable. Workers, farmers, and small business people will not tolerate for any length of time a pattern of economic organization in which they are subject to periodic dramatic fluctuations in their daily economic circumstances. In short, the neoliberal Utopia of a borderless and peaceful globe requires that millions of ordinary people throughout the world have the flexibility to tolerate—perhaps as often as every five or ten years—a prolonged spell in which they must survive on half or less of what they previously earned. Polanyi believes that to expect that kind of flexibility is both morally wrong and deeply unrealistic. To him it is inevitable that people will mobilize to protect themselves from these economic shocks.

Moreover, the recent period of ascendant neoliberalism has already witnessed widespread protests occurring around the world where people attempt to resist the economic disruptions of globalization.[27] As such dissatisfactions intensify, social order becomes more problematic and the danger increases that political leaders will seek to

26. Thomas Friedman, *The Lexus and the Olive Tree* (New York: Farrar, Strauss, 1999), p. 86.

27. John Walton and David Seddon, *Free Markets and Food Riots: The Politics of Global Adjustment* (Cambridge, Mass.: Blackwell, 1994).

divert discontent by scapegoating internal or external enemies. This is how the Utopian vision of neoliberals leads not to peace but to intensified conflict. In many parts of Africa, for example, the devastating effects of structural adjustment policies have disintegrated societies and produced famine and civil war. Elsewhere, the post-Cold War period has seen the emergence of militantly nationalist regimes with aggressive intentions toward neighbors and their own ethnic minorities.[28] Furthermore, in every corner of the globe militant movements—often intermixed with religious fundamentalism—are poised to take advantage of the economic and social shocks of globalization. If Polanyi is right, these signs of disorder are harbingers of even more dangerous circumstances in the future.

## Democratic Alternatives

Although he wrote *The Great Transformation* during World War II, Polanyi remained optimistic about the future; he thought the cycle of international conflict could be broken. The key step was to overturn the belief that social life should be subordinated to the market mechanism. Once free of this "obsolete market mentality," the path would be open to subordinate both national economies and the global economy to democratic politics.[29] Polanyi saw Roosevelt's New Deal as a model of these future possibilities. Roosevelt's reforms meant that the U.S. economy continued to be organized around markets and market activity, but a new set of regulatory mechanisms now made it possible to buffer both human beings and nature from the pressures of market forces.[30] Through democratic politics, people decided that the elderly should be protected from the need to earn income through Social Security. Similarly, democratic politics expanded the rights of working people to form effective unions through the National Labor Relations Act. Polanyi saw these initiatives as the start of a process by which soci-

28. For an argument that many recent examples of global turmoil can be traced to the international economic regime, see Michel Cossudovsky, *The Globalisation of Poverty: Impacts of IMF and World Bank Reforms* (Penang, Malaysia: Third World Network, 1997).

29. "Obsolete Market Mentality" is the title that Polanyi gave to an important 1947 essay that is reprinted in Dalton, *Primitive, Archaic, and Modern Economies.*

30. The New Deal actually did little to protect the environment. Nevertheless, when environmentalists later gained the political strength to win reforms, agencies such as the Environmental Protection Agency followed the New Deal's regulatory model.

ety would decide through democratic means to protect individuals and nature from certain economic dangers.

At the global level Polanyi anticipated an international economic order with high levels of international trade and cooperation. He did not lay out a set of blueprints, but he was clear on the principles:

> However, with the disappearance of the automatic mechanism of the gold standard, governments will find it possible to drop the most obstructive features of absolute sovereignty, the refusal to collaborate in international economics. At the same time it will become possible to tolerate willingly that other nations shape their domestic institutions according to their inclinations, thus transcending the pernicious nineteenth-century dogma of the necessary uniformity of domestic regimes within the orbit of world economy.

In other words collaboration among governments would produce a set of agreements to facilitate high levels of international trade, but societies would have multiple means to buffer themselves from the pressures of the global economy. Moreover, with an end to a single economic model, developing nations would have expanded opportunities to improve the welfare of their people. This vision also assumes a set of global regulatory structures that would place limits on the play of market forces.[31]

Polanyi's vision depends on expanding the role of government both domestically and internationally. He challenges the now fashionable view that more government will inevitably lead to both bad economic results and excessive state control of social life. For him a substantial governmental role is indispensable for managing the fictitious commodities, so there is no reason to take seriously the market liberal axiom that governments are by definition ineffectual. But he also explicitly refutes the claim that the expansion of government would necessarily take an oppressive form. Polanyi argues instead that "the passing of market economy can become the beginning of an era of unprecedented freedom. Juridical and actual freedom can be made wider and more general than ever before; regulation and control can achieve freedom not only for the few, but for all." But the concept of freedom that he outlines goes beyond a reduction of economic and so-

31. **For** a recent effort to concretize this vision, see John Eatwell and Lance Taylor, *Global Finance at Risk: The Case for International Regulation* (New York: New Press, 2000).

cial injustice; he also calls for an expansion of civil liberties, stressing that "in an established society, the right to nonconformity must be institutionally protected. The individual must be free to follow his conscience without fear of the powers that happen to be entrusted with administrative tasks in some of the fields of social life."

Polanyi ends the book with these eloquent words: "As long as [man] is true to his task of creating more abundant freedom for all, he need not fear that either power or planning will turn against him and destroy the freedom he is building by their instrumentality. This is the meaning of freedom in a complex society; it gives us all the certainty that we need."[32] Of course, Polanyi's optimism about the immediate post-World War II era was not justified by the actual course of events. The coming of the Cold War meant that the New Deal was the end of reform in the United States, not the beginning. Planned global economic cooperation gave way relatively quickly to new initiatives to expand the global role of markets. To be sure, the considerable achievements of European social democratic governments, particularly in Scandinavia, from the 1940s through the 1980s provides concrete evidence that Polanyi's vision was both powerful and realistic. But in the larger countries, Polanyi's vision was orphaned, and the opposing views of market liberals like Hayek steadily gained strength, triumphing in the 1980s and 1990s.

Yet now that the Cold War is history, Polanyi's initial optimism might finally be vindicated. There is a possible alternative to the scenario in which the unsustainability of market liberalism produces economic crises and the reemergence of authoritarian and aggressive regimes. The alternative is that ordinary people in nations around the globe engage in a common effort to subordinate the economy to democratic politics and rebuild the global economy on the basis of international cooperation. Indeed, there were clear signs in the last years of the 1990s that such a transnational social movement to reshape the global economy is now more than a theoretical possibility.[33] Activists in both the developed and developing countries have organized mili-

32. Polanyi believes that a complex society requires the state to exercise a monopoly on violence: "Power and compulsion are part of that reality [of human society]; an ideal that would ban them from society must be invalid."

33. See Peter Evans, "Fighting Marginalization with Transnational Networks: Counter-Hegemonic Globalization," *Contemporary Sociology 29* (January 2000): 230-4i-

tant protests against the international institutions—the World Trade Organization, the International Monetary Fund, and the World Bank—that enforce the rules of neoliberalism. Groups around the world have begun an intense global dialogue over the reconstruction of the global financial order.[34]

This nascent movement faces enormous obstacles; it will not be easy to forge a durable alliance that reconciles the often conflicting interests of people in the global South with those in the global North. Furthermore, the more successful such a movement is, the more formidable will be the strategic challenges it faces. It remains highly uncertain whether the global order can be reformed from below without plunging the world economy into the kind of crisis that occurs when investors panic. Nevertheless, it is of enormous significance that for the first time in history, the governance structure of the global economy has become the central target of transnational social movement activity.

This transnational movement is an indication of the continuing vitality and practicality of Polanyi's vision. For Polanyi the deepest flaw in market liberalism is that it subordinates human purposes to the logic of an impersonal market mechanism. He argues instead that human beings should use the instruments of democratic governance to control and direct the economy to meet our individual and collective needs. Polanyi shows that the failure to take up this challenge produced enormous suffering in the past century. His prophecy for the new century could not be clearer.

34. For a North American perspective on these discussions and a useful guide to additional resources, see Sarah Anderson and John Cavanaugh, with Thea Lee, *Field Guide to the Global Economy* (New York: New Press, 2000).