David Harvey
A Brief History of
Neoliberalism.

3

The Neoliberal State

The role of the state in neoliberal theory is reasonably easy to define. The practice of neoliberalization has, however, evolved in such a way as to depart significantly from the template that theory provides. The somewhat chaotic evolution and uneven geographical development of state institutions, powers, and functions over the last thirty years suggests, furthermore, that the neoliberal state may be an unstable and contradictory political form.

The Neoliberal State in Theory

According to theory, the neoliberal state should favour strong individual private property rights, the rule of law, and the institutions of freely functioning markets and free trade.[1] These are the institutional arrangements considered essential to guarantee individual freedoms. The legal framework is that of freely negotiated contractual obligations between juridical individuals in the marketplace. The sanctity of contracts and the individual right to freedom of action, expression, and choice must be protected. The state must therefore use its monopoly of the means of violence to preserve these freedoms at all costs. By extension, the freedom of businesses and corporations (legally regarded as individuals) to operate within this institutional framework of free markets and free trade is regarded as a fundamental good. Private enterprise and entrepreneurial initiative are seen as the keys to innovation and wealth creation. Intellectual property rights are protected (for example through patents) so as to encourage technological changes. Continuous increases in productivity should then deliver higher living standards to everyone. Under the assumption that 'a rising tide lifts all boats', or of 'trickle down', neoliberal theory

holds that the elimination of poverty (both domestically and worldwide) can best be secured through free markets and free trade.

Neoliberals are particularly assiduous in seeking the privatization of assets. The absence of clear private property rights—as in many developing countries—is seen as one of the greatest of all institutional barriers to economic development and the improvement of human welfare. Enclosure and the assignment of private property rights is considered the best way to protect against the so-called 'tragedy of the commons' (the tendency for individuals to irresponsibly super-exploit common property resources such as land and water). Sectors formerly run or regulated by the state must be turned over to the private sphere and be deregulated (freed from any state interference). Competition—between individuals, between firms, between territorial entities (cities, regions, nations, regional groupings)—is held to be a primary virtue. The ground-rules for market competition must be properly observed, of course. In situations where such rules are not clearly laid out or where property rights are hard to define, the state must use its power to impose or invent market systems (such as trading in pollution rights). Privatization and deregulation combined with competition, it is claimed, eliminate bureaucratic red tape, increase efficiency and productivity, improve quality, and reduce costs, both directly to the consumer through cheaper commodities and services and indirectly through reduction of the tax burden. The neoliberal state should persistently seek out internal reorganizations and new institutional arrangements that improve its competitive position as an entity vis-à-vis other states in the global market.

While personal and individual freedom in the marketplace is guaranteed, each individual is held responsible and accountable for his or her own actions and well-being. This principle extends into the realms of welfare, education, health care, and even pensions (social security has been privatized in Chile and Slovakia, and proposals exist to do the same in the US). Individual success or failure are interpreted in terms of entrepreneurial virtues or personal failings (such as not investing significantly enough in one's own human capital through education) rather than being attributed to any systemic property (such as the class exclusions usually attributed to capitalism).

The free mobility of capital between sectors, regions, and countries is regarded as crucial. All barriers to that free movement (such as tariffs, punitive taxation arrangements, planning and environmental controls, or other locational impediments) have to be removed, except in those areas crucial to 'the national interest', however that is defined. State sovereignty over commodity and capital movements is willingly surrendered to the global market. International competition is seen as healthy since it improves efficiency and productivity, lowers prices, and thereby controls inflationary tendencies. States should therefore collectively seek and negotiate the reduction of barriers to movement of capital across borders and the opening of markets (for both commodities and capital) to global exchange. Whether or not this applies to labour as a commodity is, however, controversial. To the degree that all states must collaborate to reduce barriers to exchange, so co-ordinating structures such as the group of advanced capitalist nations (the US, Britain, France, Germany, Italy, Canada, and Japan) known as the G7 (now the G8 with the addition of Russia) must arise. International agreements between states guaranteeing the rule of law and freedoms of trade, such as those now incorporated in the World Trade Organization agreements, are critical to the advancement of the neoliberal project on the global stage.

Neoliberal theorists are, however, profoundly suspicious of democracy. Governance by majority rule is seen as a potential threat to individual rights and constitutional liberties. Democracy is viewed as a luxury, only possible under conditions of relative affluence coupled with a strong middle-class presence to guarantee political stability. Neoliberals therefore tend to favour governance by experts and elites. A strong preference exists for government by executive order and by judicial decision rather than democratic and parliamentary decision-making. Neoliberals prefer to insulate key institutions, such as the central bank, from democratic pressures. Given that neoliberal theory centres on the rule of law and a strict interpretation of constitutionality, it follows that conflict and opposition must be mediated through the courts. Solutions and

remedies to any problems have to be sought by individuals through the legal system.

Tensions and Contradictions

There are some shadowy areas as well as points of conflict within the general theory of the neoliberal state. First, there is the problem of how to interpret monopoly power. Competition often results in monopoly or oligopoly, as stronger firms drive out weaker. Most neoliberal theorists consider this unproblematic (it should, they say, maximize efficiency) provided there are no substantial barriers to the entry of competitors (a condition often hard to realize and which the state may therefore have to nurture). The case of so-called 'natural monopolies' is more difficult. It makes no sense to have multiple competing electrical power grids, gas pipelines, water and sewage systems, or rail links between Washington and Boston. State regulation of provision, access, and pricing seems unavoidable in such domains. While partial deregulation may be possible (permitting competing producers to feed electricity into the same grid or run trains on the same tracks, for example) the possibilities for profiteering and abuse, as the California power crisis of 2002 abundantly showed, or for deadly muddle and confusion, as the British rail situation has proven, are very real.

The second major arena of controversy concerns market failure. This arises when individuals and firms avoid paying the full costs attributable to them by shedding their liabilities outside the market (the liabilities are, in technical parlance, 'externalized'). The classic case is that of pollution, where individuals and firms avoid costs by dumping noxious wastes free of charge in the environment. Productive ecosystems may be degraded or destroyed as a result. Exposure to dangerous substances or physical dangers in the workplace may affect human health and even deplete the pool of healthy labourers in the workforce. While neoliberals admit the problem and some concede the case for limited state intervention, others argue for inaction because the cure will almost certainly be worse than the disease. Most would agree, however, that if there are to be interventions these should work through market

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The Rise of Neoliberal Theory

Neoliberalism as a potential antidote to threats to the capitalist social order and as a solution to capitalism's ills had long been lurking in the wings of public policy. A small and exclusive group of passionate advocates—mainly academic economists, historians, and philosophers—had gathered together around the renowned

Austrian political philosopher Friedrich von Hayek to create the Mont Pelerin Society (named after the Swiss spa where they first met) in 1947 (the notables included Ludvig von Mises, the economist Milton Friedman, and even, for a time, the noted philosopher Karl Popper). The founding statement of the society read as follows:

> The central values of civilization are in danger. Over large stretches of the earth's surface the essential conditions of human dignity and freedom have already disappeared. In others they are under constant menace from the development of current tendencies of policy. The position of the individual and the voluntary group are progressively undermined by extensions of arbitrary power. Even that most precious possession of Western Man, freedom of thought and expression, is threatened by the spread of creeds which, claiming the privilege of tolerance when in the position of a minority, seek only to establish a position of power in which they can suppress and obliterate all views but their own.
>
> The group holds that these developments have been fostered by the growth of a view of history which denies all absolute moral standards and by the growth of theories which question the desirability of the rule of law. It holds further that they have been fostered by a decline of belief in private property and the competitive market; for without the diffused power and initiative associated with these institutions it is difficult to imagine a society in which freedom may be effectively preserved.[15]

The group's members depicted themselves as 'liberals' (in the traditional European sense) because of their fundamental commitment to ideals of personal freedom. The neoliberal label signalled their adherence to those free market principles of neoclassical economics that had emerged in the second half of the nineteenth century (thanks to the work of Alfred Marshall, William Stanley Jevons, and Leon Walras) to displace the classical theories of Adam Smith, David Ricardo, and, of course, Karl Marx. Yet they also held to Adam Smith's view that the hidden hand of the market was the best device for mobilizing even the basest of human instincts such as gluttony, greed, and the desire for wealth and power for the benefit of all. Neoliberal doctrine was therefore deeply opposed to state interventionist theories, such as those of John Maynard Keynes, which rose to prominence in the 1930s in

response to the Great Depression. Many policy-makers after the Second World War looked to Keynesian theory to guide them as they sought to keep the business cycle and recessions under control. The neoliberals were even more fiercely opposed to theories of centralized state planning, such as those advanced by Oscar Lange working close to the Marxist tradition. State decisions, they argued, were bound to be politically biased depending upon the strength of the interest groups involved (such as unions, environmentalists, or trade lobbies). State decisions on matters of investment and capital accumulation were bound to be wrong because the information available to the state could not rival that contained in market signals.

This theoretical framework is not, as several commentators have pointed out, entirely coherent.[16] The scientific rigour of its neoclassical economics does not sit easily with its political commitment to ideals of individual freedom, nor does its supposed distrust of all state power fit with the need for a strong and if necessary coercive state that will defend the rights of private property, individual liberties, and entrepreneurial freedoms. The juridical trick of defining corporations as individuals before the law introduces its own biases, rendering ironic John D. Rockefeller's personal credo etched in stone in the Rockefeller Center in New York City, where he places 'the supreme worth of the individual' above all else. And there are, as we shall see, enough contradictions in the neoliberal position to render evolving neoliberal practices (vis-à-vis issues such as monopoly power and market failures) unrecognizable in relation to the seeming purity of neoliberal doctrine. We have to pay careful attention, therefore, to the tension between the theory of neoliberalism and the actual pragmatics of neoliberalization.

Hayek, author of key texts such as *The Constitution of Liberty*, presciently argued that the battle for ideas was key, and that it would probably take at least a generation for that battle to be won, not only against Marxism but against socialism, state planning, and Keynesian interventionism. The Mont Pelerin group garnered financial and political support. In the US in particular, a powerful group of wealthy individuals and corporate leaders who were viscerally opposed to all forms of state intervention and regulation, and even to internationalism sought to organize opposition to what they saw as an emerging consensus for pursuing a mixed economy. Fearful of how the alliance with the Soviet Union and the command economy constructed within the US during the Second World War might play out politically in a post-war setting, they were ready to embrace anything from McCarthyism to neoliberal think-tanks to protect and enhance their power. Yet this movement remained on the margins of both policy and academic influence until the troubled years of the 1970s. At that point it began to move centre-stage, particularly in the US and Britain, nurtured in various well-financed think-tanks (offshoots of the Mont Pelerin Society, such as the Institute of Economic Affairs in London and the Heritage Foundation in Washington), as well as through its growing influence within the academy, particularly at the University of Chicago, where Milton Friedman dominated. Neoliberal theory gained in academic respectability by the award of the Nobel Prize in economics to Hayek in 1974 and Friedman in 1976. This particular prize, though it assumed the aura of Nobel, had nothing to do with the other prizes and was under the tight control of Sweden's banking elite. Neoliberal theory, particularly in its monetarist guise, began to exert practical influence in a variety of policy fields. During the Carter presidency, for example, deregulation of the economy emerged as one of the answers to the chronic state of stagflation that had prevailed in the US throughout the 1970s. But the dramatic consolidation of neoliberalism as a new economic orthodoxy regulating public policy at the state level in the advanced capitalist world occurred in the United States and Britain in 1979.

In May of that year Margaret Thatcher was elected in Britain with a strong mandate to reform the economy. Under the influence of Keith Joseph, a very active and committed publicist and polemicist with strong connections to the neoliberal Institute of Economic Affairs, she accepted that Keynesianism had to be abandoned and that monetarist 'supply-side' solutions were essential to cure the stagflation that had characterized the British economy during the 1970s. She recognized that this meant nothing short of a revolution in fiscal and social policies, and immediately signalled a fierce determination to have done with the institutions and

political ways of the social democratic state that had been consolidated in Britain after 1945. This entailed confronting trade union power, attacking all forms of social solidarity that hindered competitive flexibility (such as those expressed through municipal governance, and including the power of many professionals and their associations), dismantling or rolling back the commitments of the welfare state, the privatization of public enterprises (including social housing), reducing taxes, encouraging entrepreneurial initiative, and creating a favourable business climate to induce a strong inflow of foreign investment (particularly from Japan). There was, she famously declared, 'no such thing as society, only individual men and women'—and, she subsequently added, their families. All forms of social solidarity were to be dissolved in favour of individualism, private property, personal responsibility, and family values. The ideological assault along these lines that flowed from Thatcher's rhetoric was relentless.[17] 'Economics are the method', she said, 'but the object is to change the soul.' And change it she did, though in ways that were by no means comprehensive and complete, let alone free of political costs.

In October 1979 Paul Volcker, chairman of the US Federal Reserve Bank under President Carter, engineered a draconian shift in US monetary policy.[18] The long-standing commitment in the US liberal democratic state to the principles of the New Deal, which meant broadly Keynesian fiscal and monetary policies with full employment as the key objective, was abandoned in favour of a policy designed to quell inflation no matter what the consequences might be for employment. The real rate of interest, which had often been negative during the double-digit inflationary surge of the 1970s, was rendered positive by fiat of the Federal Reserve (Figure 1.5). The nominal rate of interest was raised overnight and, after a few ups and downs, by July 1981 stood close to 20 per cent. Thus began 'a long deep recession that would empty factories and break unions in the US and drive debtor countries to the brink of insolvency, beginning the long era of structural adjustment'.[19] This, Volcker argued, was the only way out of the grumbling crisis of stagflation that had characterized the US and much of the global economy throughout the 1970s.

The Volcker shock, as it has since come to be known, has to be

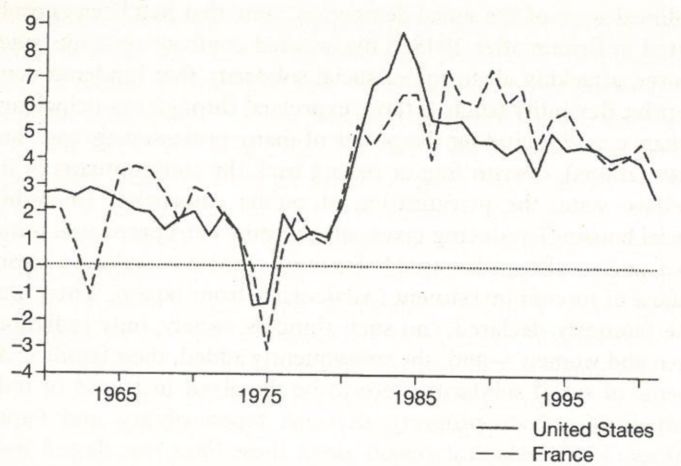

Figure 1.5 The 'Volcker shock': movements in the real rate of interest, US and France, 1960–2001
Source: Duménil and Lévy, *Capital Resurgent*.

interpreted as a necessary but not sufficient condition for neoliberalization. Some central banks had long emphasized anti-inflationary fiscal responsibility and adopted policies that were closer to monetarism than to Keynesian orthodoxy. In the West German case this derived from historical memories of the runaway inflation that had destroyed the Weimar Republic in the 1920s (setting the stage for the rise of fascism) and the equally dangerous inflation that occurred at the end of the Second World War. The IMF had long set itself against excessive debt creation and urged, if not mandated, fiscal restraints and budgetary austerity on client states. But in all these cases this monetarism was paralleled by acceptance of strong union power and a political commitment to build a strong welfare state. The turn to neoliberalism thus depended not only on adopting monetarism but on the unfolding of government policies in many other arenas.

Ronald Reagan's victory over Carter in 1980 proved crucial, even though Carter had shifted uneasily towards deregulation (of airlines and trucking) as a partial solution to the crisis of stagflation. Reagan's advisers were convinced that Volcker's monetarist

'medicine' for a sick and stagnant economy was right on target. Volcker was supported in and reappointed to his position as chair of the Federal Reserve. The Reagan administration then provided the requisite political backing through further deregulation, tax cuts, budget cuts, and attacks on trade union and professional power. Reagan faced down PATCO, the air traffic controllers' union, in a lengthy and bitter strike in 1981. This signalled an all-out assault on the powers of organized labour at the very moment when the Volcker-inspired recession was generating high levels of unemployment (10 per cent or more). But PATCO was more than an ordinary union: it was a white-collar union which had the character of a skilled professional association. It was, therefore, an icon of middle-class rather than working-class unionism. The effect on the condition of labour across the board was dramatic—perhaps best captured by the fact that the Federal minimum wage, which stood on a par with the poverty level in 1980, had fallen to 30 per cent below that level by 1990. The long decline in real wage levels then began in earnest.

Reagan's appointments to positions of power on issues such as environmental regulation, occupational safety, and health, took the

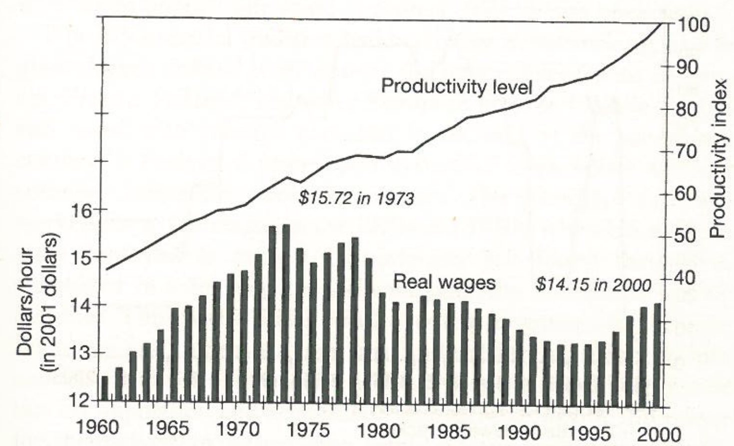

Figure 1.6 The attack on labour: real wages and productivity in the US, 1960–2000
Source: Pollin, *Contours of Descent*.

campaign against big government to ever higher levels. The deregulation of everything from airlines and telecommunications to finance opened up new zones of untrammelled market freedoms for powerful corporate interests. Tax breaks on investment effectively subsidized the movement of capital away from the unionized north-east and midwest and into the non-union and weakly regulated south and west. Finance capital increasingly looked abroad for higher rates of return. Deindustrialization at home and moves to take production abroad became much more common. The market, depicted ideologically as the way to foster competition and innovation, became a vehicle for the consolidation of monopoly power. Corporate taxes were reduced dramatically, and the top personal tax rate was reduced from 70 to 28 per cent in what was billed as 'the largest tax cut in history' (Figure 1.7).

And so began the momentous shift towards greater social inequality and the restoration of economic power to the upper class.

There was, however, one other concomitant shift that also impelled the movement towards neoliberalization during the

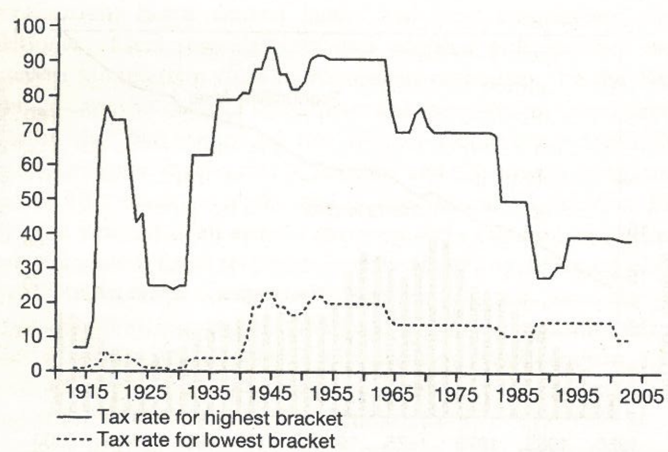

Figure 1.7 The tax revolt of the upper class: US tax rates for higher and lower brackets, 1913–2003

Source: Duménil and Lévy, 'Neoliberal Income Trends'.

1970s. The OPEC oil price hike that came with the oil embargo of 1973 placed vast amounts of financial power at the disposal of the oil-producing states such as Saudi Arabia, Kuwait, and Abu Dhabi. We now know from British intelligence reports that the US was actively preparing to invade these countries in 1973 in order to restore the flow of oil and bring down oil prices. We also know that the Saudis agreed at that time, presumably under military pressure if not open threat from the US, to recycle all of their petrodollars through the New York investment banks.[20] The latter suddenly found themselves in command of massive funds for which they needed to find profitable outlets. The options within the US, given the depressed economic conditions and low rates of return in the mid-1970s, were not good. More profitable opportunities had to be sought out abroad. Governments seemed the safest bet because, as Walter Wriston, head of Citibank, famously put it, governments can't move or disappear. And many governments in the developing world, hitherto starved of funds, were anxious enough to borrow. For this to occur required, however, open entry and reasonably secure conditions for lending. The New York investment banks looked to the US imperial tradition both to prise open new investment opportunities and to protect their foreign operations.

The US imperial tradition had been long in the making, and to great degree defined itself against the imperial traditions of Britain, France, Holland, and other European powers.[21] While the US had toyed with colonial conquest at the end of the nineteenth century, it evolved a more open system of imperialism without colonies during the twentieth century. The paradigm case was worked out in Nicaragua in the 1920s and 1930s, when US marines were deployed to protect US interests but found themselves embroiled in a lengthy and difficult guerrilla insurgency led by Sandino. The answer was to find a local strongman—in this case Somoza—and to provide economic and military assistance to him and his family and immediate allies so that they could repress or buy off opposition and accumulate considerable wealth and power for themselves. In return they would always keep their country open to the operations of US capital and support, and if necessary promote US interests, both in the country and in the region (in the Nicaraguan case, Central America) as a whole. This was the model that was deployed after the Second World War during the phase of global decolonization imposed upon the European powers at US insistence. For example, the CIA engineered the coup that overthrew the democratically elected Mosaddeq government in Iran in 1953 and installed the Shah of Iran, who gave the oil contracts to US companies (and did not return the assets to the British companies that Mossadeq had nationalized). The shah also became one of the key guardians of US interests in the Middle Eastern oil region.

In the post-war period, much of the non-communist world was opened up to US domination by tactics of this sort. This became the method of choice to fight off the threat of communist insurgencies and revolution, entailing an anti-democratic (and even more emphatically anti-populist and anti-socialist/communist) strategy on the part of the US that put the US more and more in alliance with repressive military dictatorships and authoritarian regimes (most spectacularly, of course, throughout Latin America). The stories told in John Perkins's *Confessions of an Economic Hit Man* are full of the ugly and unsavoury details of how this was all too often done. US interests consequently became more rather than less vulnerable in the struggle against international communism. While the consent of local ruling elites could be purchased easily enough, the need to coerce oppositional or social democratic movements (such as Allende's in Chile) associated the US with a long history of largely covert violence against popular movements throughout much of the developing world.

It was in this context that the surplus funds being recycled through the New York investment banks were dispersed throughout the world. Before 1973, most US foreign investment was of the direct sort, mainly concerned with the exploitation of raw material resources (oil, minerals, raw materials, agricultural products) or the cultivation of specific markets (telecommunications, automobiles, etc.) in Europe and Latin America. The New York investment banks had always been active internationally, but after 1973 they became even more so, though now far more focused on lending capital to foreign governments.[22] This required the liberalization of international credit and financial markets, and the US government began actively to promote and support this strategy

globally during the 1970s. Hungry for credit, developing countries were encouraged to borrow heavily, though at rates that were advantageous to the New York bankers.[23] Since the loans were designated in US dollars, however, any modest, let alone precipitous, rise in US interest rates could easily push vulnerable countries into default. The New York investment banks would then be exposed to serious losses.

The first major test case of this came in the wake of the Volcker shock that drove Mexico into default in 1982–4. The Reagan administration, which had seriously thought of withdrawing support for the IMF in its first year in office, found a way to put together the powers of the US Treasury and the IMF to resolve the difficulty by rolling over the debt, but did so in return for neoliberal reforms. This treatment became standard after what Stiglitz refers to as a 'purge' of all Keynesian influences from the IMF in 1982. The IMF and the World Bank thereafter became centres for the propagation and enforcement of 'free market fundamentalism' and neoliberal orthodoxy. In return for debt rescheduling, indebted countries were required to implement institutional reforms, such as cuts in welfare expenditures, more flexible labour market laws, and privatization. Thus was 'structural adjustment' invented. Mexico was one of the first states drawn into what was going to become a growing column of neoliberal state apparatuses worldwide.[24]

What the Mexico case demonstrated, however, was a key difference between liberal and neoliberal practice: under the former, lenders take the losses that arise from bad investment decisions, while under the latter the borrowers are forced by state and international powers to take on board the cost of debt repayment no matter what the consequences for the livelihood and well-being of the local population. If this required the surrender of assets to foreign companies at fire-sale prices, then so be it. This, it turns out, is not consistent with neoliberal theory. One effect, as Duménil and Lévy show, was to permit US owners of capital to extract high rates of return from the rest of the world during the 1980s and 1990s (Figures 1.8 and 1.9).[25] The restoration of power to an economic elite or upper class in the US and elsewhere in the advanced capitalist countries drew heavily on surpluses extracted

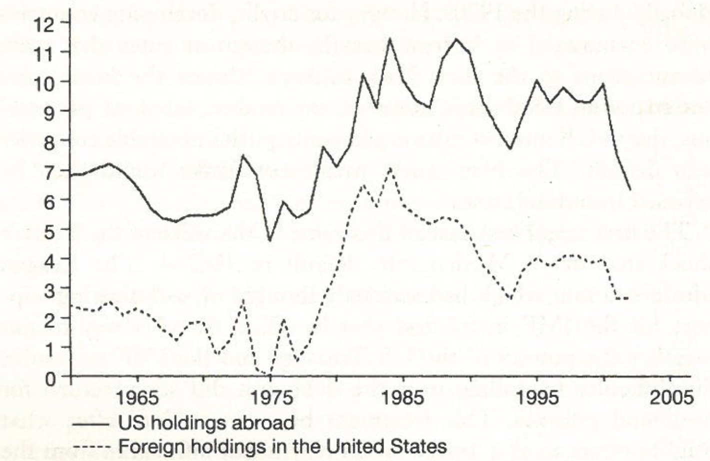

Figure 1.8 Extracting surpluses from abroad: rates of return on foreign and domestic investments in the US, 1960–2002
Source: Duménil and Lévy, 'The Economics of US Imperialism'.

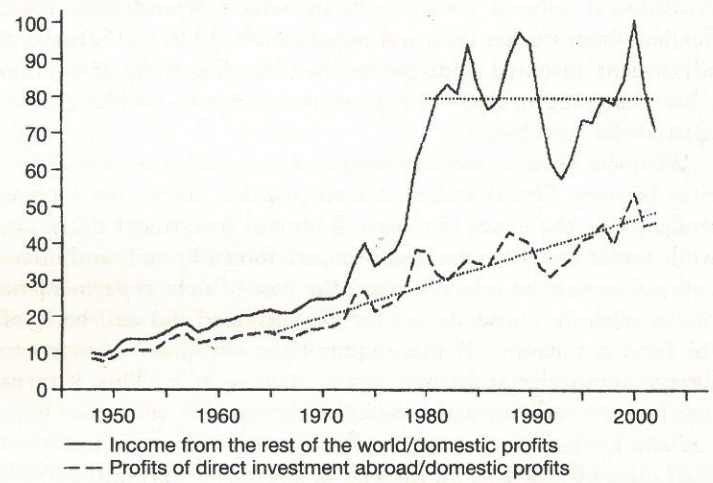

Figure 1.9 The flow of tribute into the US: profits and capital income from the rest of the world in relation to domestic profits
Source: Duménil and Lévy, 'Neoliberal Dynamics: Towards A New Phase?'.

from the rest of the world through international flows and structural adjustment practices.

The Meaning of Class Power

But what exactly is meant here by 'class'? This is always a somewhat shadowy (some would even say dubious) concept. Neoliberalization has, in any case, entailed its redefinition. This poses a problem. If neoliberalization has been a vehicle for the restoration of class power, then we should be able to identify the class forces behind it and those that have benefited from it. But this is difficult to do when 'class' is not a stable social configuration. In some cases 'traditional' strata have managed to hang on to a consistent power base (often organized through family and kinship). But in other instances neoliberalization has been accompanied by a reconfiguration of what constitutes an upper class. Margaret Thatcher, for example, attacked some of the entrenched forms of class power in Britain. She went against the aristocratic tradition that dominated in the military, the judiciary, and the financial elite in the City of London and many segments of industry, and sided with the brash entrepreneurs and the nouveaux riches. She supported, and was usually supported by, this new class of entrepreneurs (such as Richard Branson, Lord Hanson, and George Soros). The traditional wing of her own Conservative Party was appalled. In the US, the rising power and significance of the financiers and the CEOs of large corporations, as well as the immense burst of activity in wholly new sectors (such as computing and the internet, media, and retailing) changed the locus of upper-class economic power significantly. While neoliberalization may have been about the restoration of class power, it has not necessarily meant the restoration of economic power to the same people.

But, as the contrasting cases of the US and Britain illustrate, 'class' means different things in different places, and in some instances (for example in the US) it is often held to have no meaning at all. In addition there have been strong currents of differentiation in terms of class identity formation and re-formation in different parts of the world. In Indonesia, Malaysia, and the Philippines, for example, economic power became strongly