



Neoliberalism, World Crisis, and The New Pragmatism

By Grzegorz W. Kolodko

The things happen, as they do, because many things happen at the same time.

This sentence, repeated as the guiding principle, is the foundation of what I call the coincidence theory of development and the New Pragmatism¹. It essentially means a comparative and interdisciplinary explanation of the essence and mechanisms of social and economic development as a historical process. But this theory may also be very useful on other occasions, for example, to explain the causes and mechanisms of the great economic crisis of 2008-11. Most frequently the crisis is described in this timeframe, although its roots go back much earlier than 2008, and its consequences are going to be felt well beyond 2011.

It is the most extensive crisis in the post-war period; that is, during the lifetimes of three generations. However, it is an intellectually and politically unacceptable simplification to identify the current crisis with a temporary recession. If it is averaged, which as economists we enjoy doing, in principle the crisis could be deemed to be over, as already in the 4th quarter of 2009 world production was again rising. Unfortunately, the crisis continues, since it goes far beyond the narrowly understood field of production. Someone looking from the side might ask: why so much ado just because in 2009 the production level dropped by only one percent? In the context of the whole decade, during which it increased in total by as much as 40 per cent, it seems to be a trace change of insignificant importance. Someone else stresses that the Dow Jones

index has again risen to over 12,000, so apparently the crisis is over, as the stock exchange quotations rise again. But in fact it is not over yet. Why?

First of all, the quoted indexes refer to the dynamics of GWP presented annually as average values for the whole world. And the world, as we know, is extremely diversified. It is sufficient to mention that in the first three years of the decade, global production increased on average by 3.1 per cent per annum, while for the group of rich countries (i.e., the most developed economies populated by almost one billion people), the index was only 1.6 per cent. In the case of the “developing countries” (in fact, in this context this phrase may be used without the quotation marks) inhabited by 6 billion people, the index was 4.3 per cent. In the period from 2005 to 2007, the indices of dynamics were respectively 2.8 and 7.7 per cent, and during the crisis of 2008-10, the “scissors” open even more: in the former case the dynamics of global production oscillates around minus 0.5 per cent, while in the latter it was as much as plus 4.3 per cent. The global economic order has been changing. And the change has been for the better, since it reduces the enormous discrepancies resulting from the historical development process between the production levels and living standards in the highly developed countries and in those less developed. The crisis accelerates the process of diminishing the gap, which should be deemed favourable. It is worth considering that back in 2000 the GDP *per capita* in China (calculated according to purchasing power parity, PPP) constituted only 6.7 per cent of the American level (respectively they amounted to 2,377 \$PPP and 35,252 \$PPP);

in 2010, this relationship oscillated around 15 per cent (i.e., 7,200 \$PPP and 47,400 \$PPP)².

Secondly, this is the crisis of redistribution rather than of production. The fluctuations, including absolute slumps, of the consumption volume and investments in particular, are much deeper than those of the GDP itself. There are also great differences per region or industry sector. Disturbances affected Western Europe more than North America, and in turn Eastern Europe suffered more than Western Europe. If we refer to the disturbance concerning distribution to the American economy (though not exclusively), the crisis here is much more severe for Wall Street, rather than Main Street: the financial sector, rather than the salaried workers. In other words, in comparison to the past, it has affected the *white collars* relatively more than the *blue collars*. The crisis is definitely more damaging for the automobile industry than food processing. At a large scale, the redistribution effects are greatly diversified, both globally, and at the level of particular countries.

Thirdly, tendencies present in the financial markets, sometimes the positive ones expressed in the increase of stock exchange quotations, are by no means the sign of the economy coming back to “normal” (if we assume that such a condition exists at all). Sometimes it happens the other way round: the speculation on financial markets may be the symptom of irrationality and, by excessive separation of the financial sector from the real economy, they could actually be the symptom of a production crisis, or they may even be one of its causes.

Fourthly, alongside disturbances in production and trade, there is a fall in employment, which is automatically followed by an increase in the unemployment rate. It increases continuously, even during the phase when the global economy starts to emerge from recession. It may be estimated that in 2011, the number of unemployed in the world is 60-80 million higher than three years ago. And the number keeps growing. Despite recovery, in 2009-10 the unemployment was rising in the USA and Germany, as well as in China and India. The unemployment rate in the USA is the highest in the last twenty-five years and, similarly to the European Union, it is close to the psychological threshold of 10 percent. In the case of the USA, if total unemployment includes those people without work but not registered as unemployed and people who are employed part-time, it amounts to over 16 percent. The fluctuations of the employment rate are very chaotic and they severely affect different sectors to a greater degree than the whole economy, in particular industries producing for export, but also the construction and automotive industries. In the labour market one may therefore also observe a far-reaching redistribution process, which affects not only the economic but also the social dimension of the reproduction process.

The fifth, and I believe the most important factor, is that the present crisis is of a fundamental nature. This is the systemic crisis. It is not just another case, no matter how spectacular, which is related to the business cycle. It is a systemic crisis of

modern capitalism, and in particular of its neoliberal mutation, that is the contemporary *laissez faire*. And so it is by no means sufficient to talk about the end of the crisis by merely reversing negative tendencies in production or bouncing back from the bottom of recession and coming back to the growth path.

The question of whether it was possible to avoid the present crisis is frequently asked. Such a general question cannot be answered correctly, since it is necessary to define the time-frame it refers to. In other words, this is a complex question: not really “when”, but “how” was it possible to avoid the crisis of 2008-11? The answer will be different if one asked about such a possibility three years ago, if we were to analyse the period thirteen years ago, and different yet again if we had looked at the future from the perspective of thirty years ago. And such a threefold approach of three, thirteen and thirty year periods emphasizes the essence of the current crisis by revealing its causes, mechanisms and consequences. Above all, it is extremely illuminating from the point of view of proposals for actions to prevent similar disturbances in the future – in three, thirteen and thirty years. It is worth remembering that the present is nothing more than just the future of the past.

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It is obvious that three years ago the world crisis was not possible to avoid. The scale of detachment of the speculative financial sector from the productive real economy, which provides all goods and services necessary for life, as well as for further production, was so great that the required adjustment to level the size of such a detachment could occur only through crisis shock. What politics could not fix *ex ante*, was achieved *ex post* by crisis. It is an extremely expensive way of making adjustments.

Three years ago, the values related to good economic practice were already devastated; even if it had not been the case everywhere, it affected many segments of the economically inter-related world, and particularly its epicentre, which is still in the United States. The devastation was so advanced that within the existing institutions, there were no political powers that would have been able to re-direct the economy to the path of non-crisis development. The imbalance in the world economy was also too large. The characteristic feature of all economies is the lack of external balance, which is expressed in the deficit (more often) or surplus (rarely) of the current account balance. If we pass over any accounting errors and omissions or extraordinary losses, in the planetary scale the surpluses and deficits balance each other and the final result is zero. However, if we sum up the values of all deficits and

all surpluses of current accounts and then if we refer to such an aggregate to the GWP, then in 2008 it oscillated around 6 per cent!³ And how is it possible not to fall at this scale of structural imbalances?

And thirteen years ago? Was it possible to avoid the present crisis? In this case the answer is more complicated. Some attempts were made. There was contentious debate between monetarism (which serves as theoretical basis of neoliberalism) and neo-Keynesianism, which seems to be enjoying rejuvenation in many circles⁴ but as such is not a panacea for contemporary complaints. In particular, there was a major battle between the advocates of far reaching uncontrolled de-regulation on the one hand, and the advocates of justified intervention of the government on the other hand; between the apologists of an unbridled market and supporters of the active role of government. In numerous countries it was possible to resist the neoliberal attack in total – for example, in large China, or in tiny Slovenia. In other countries it was only possible periodically, for example in India or in the largest post-socialist economy of East-Central Europe during the implementation of “The Strategy for Poland” from 1994 to 1997. In several Latin American countries, which trusted the Washington Consensus or allowed its imposition upon them, unorthodox actions were taken and they dominated later on, and not only in Brazil and Argentina. In the USA, attempts were made to create a different concept of development. So it was the case in the UK. However, neither the “Clintonism” inspired by the Democrats, nor the Labourite “Blairism” which was forced (quite unconvincingly and inconsistently) in the UK could manage the neoliberal storm. Hence, at the turn of the century neoliberalism won the *mainstream* position in economics as well as in economic policies. The flight of the moth to the flame was not stopped...

What about thirty years ago? Was it possible to avoid the present multi-layer crisis back then? The answer is of course positive. In the conditions of increasing globalisation, it was easy enough to refrain from following the ruts of neoliberalism, which were quite shallow then, and instead go forward towards the future along the path marked out by the model of the social market economy. The characteristic features of the social market economy include the imperative of social cohesion and economic institutionalisation, which allow for the development of private entrepreneurship while maintaining the State’s supervision over the balanced distribution of the fruits of growing labour productivity and capital efficiency.

However, the world went along a different track – due to aggressive greed and spreading short-sightedness, due to the relatively weak position of the Scandinavian countries on the international arena that enjoyed a social market economy, due to the fact that Germany (united) and Japan (during a structural crisis) were busy managing their own business, due to the gullibility of intellectual and political elites in the countries of the so-called emerging markets (more in the countries of postsocialist transformation than in other parts of the world).

With the benefit of hindsight, it is necessary that we be able to draw conclusions for the future, with intellectual skill and political will.

Thus the source of the crisis lies deeply in neoliberal capitalism.⁵ It could not start in countries with a social market economy, as was the case of Scandinavia, but only in the conditions of the neoliberal Anglo-American model. Such an intense shock could take place only as a result of the coincidence of numerous political, social and economic circumstances (as well as technological, since it would not have been possible without the Internet). The overlapping of these conditions in a specific way, which accumulated the crisis-related phenomena and processes, was possible only in the case of a special combination of values, institutions and politics, typical of neoliberalism.

Such values definitely overestimate individualism. They unnecessarily support greed by elevating this vice to the level of an economy propelling virtue. They neglect the social cohesion aspects of the economy and they do not perceive a human being as the centre of the reproduction process. There is money instead. As far as values are concerned, neoliberalism leads to the translation of almost everything into monetary worth, since according to this doctrine it is possible and worthwhile to trade in everything, which may bring profit, including expectations. And, of course, irrational expectation too.

The purpose of economic policy is sustainable long-term development. It should be sustainable not only economically, but also socially and ecologically.

From the institutional side, neoliberalism converted the State with its regulations into a kind of a public enemy number one. By using (quite brilliantly, one has to admit) media to manipulate public opinion and, unfortunately, by using the opinion-forming capacity of some groups of social sciences experts, particularly of the economists, it imposes the idea of a small (read: weak) State (government) and diminishes its interventions in the spontaneous market processes⁶, while the State, alongside with the market, is the fundamental super-institution of the modern economy.⁷ A far-reaching economic success is possible only due to an intelligent synergy of the power of the invisible hand of the market and the visible head of the government. Institutional intervention is the necessity of contemporary capitalism, which is not accepted by neoliberalism due to its values and, above all, due to its care about the interests of special groups.⁸

As far as neoliberal policy is concerned, it confuses its purposes with its measures, or the ends with the means. The purpose of economic policy is sustainable long-term development. It should be sustainable not only economically, but also socially and ecologically. Low inflation, positive interest rates,



balanced budget, fast privatisation, currency exchange rate either fixed or fluctuating, stock exchange quotation, taxes (low, of course) – these are only instruments and tools of economic policy. It is not possible to subordinate any economic strategy or policy to indices, which only illustrate phenomena and processes from those areas. To improve the financial standing of narrow groups of elites at the expense of the majority of society, neoliberalism uses in policy-making and politics such great liberal ideas as liberty and democracy, private ownership and economic freedom, entrepreneurship and competition. However, supporting such ideas as *pro publico bono* on the one hand, and their usage for the benefit of the rich minority at the expense of the middle-class and poor majority on the other hand, are two totally different faces of economic policy.

On top of that, current disturbances of the world economy are not symptoms of the financial and economic crisis only. The difficulties started with a serious financial crisis, which rapidly advanced to other services and industries. Production dynamics crumpled and in many countries went into the stage of collapse. Now the crisis spreads to the social sphere, from where it slowly starts to have an impact on the political sphere too. As if that were insufficient, the crisis of the fifth sphere, that is the sphere of principles and values, starts to overlap. Therefore, the crisis rolls over five inter-related spheres:

- financial,
- real,
- social,
- political,
- ideological.

It is not, however, a general crisis of capitalism, since this political system has special adaptation capacities. It has been proven on many occasions in the past, and so will be the case in the foreseeable future. Nevertheless, the current crisis is a fundamental breakdown of the neoliberal model. By the time the crisis had become evident, this model managed to function

fairly well, at times even remarkably well, by manipulating public opinion and politics. It was clearly noticeable wherever neoliberal tendencies dominated – from the USA in the times of Reaganomics and in the UK during the primacy of Thatcherism, via Latin American countries which allowed the imposition of the Washington Consensus in the 1990s, to Russia during the Yeltsin's term of office or Poland during the “shock without therapy” in the early 1990s⁹. Now it is important to prevent the neoliberal doctrine, after minor cosmetic changes and insignificant adjustments, from imposing the main trajectory of the world economy again.

The crisis was not caused by the breakdown on the sub-prime loans market in the USA as that was only a fuse of the bomb, whose potential was accumulated as a result of the pathological relationships typical of neoliberalism, which existed for many years. Any interpretation, which shifts the responsibility for the crisis to the crash on the American sub-prime loans market, is either a neoliberal attempt to escape political and intellectual responsibility for bringing the crisis about, or a simplified consideration on the surface of phenomena. It was the gradual weakening of the position of the State and uncontrolled, destructive deregulation that increased the irrationalities in the world economy.

In the short term, the reaction of the immediate policies (fiscal and monetary) to the financial crisis has to be evaluated positively. An increase of the money supply in the conditions of increasingly underutilized production capacities was the right move. Lubricating economies with non-inflation money already brings positive results, from the USA, via Western Europe, to China and Brazil. However, it is only a reaction to the symptoms and consequences of the crisis.

It is indispensable to reach the systemic sources of the crisis. It is not possible to remove its primary causes without modifying the value system, re-orientating institutions (understood in a behavioural way, which means the rules of the market game) and changing the way of conducting policies. In particular, the values have to move more from “to have” towards “to be”, and greater attention must be paid to cultural conditions and social surroundings. The targets of development have to be redefined. It is necessary to introduce fundamental modifications to institutions, within which the global interdependent economy functions. The current international institutional arrangement facilitates chaos, rather than global order. The future requires institutions enabling political coordination on a global scale too. Considering the changing values and new targets, it is necessary to apply a different approach to the manner of conducting politics and its instrumentation. Emphasis must definitely move to the layer of supranational coordination.

Development strategy and economic policy can be efficient only if it is based on a sound economic theory. The coincidence theory of development, in an unorthodox and holistic way, answers the question about mutual dependencies in long-term development processes. The New Pragmatism

implies a normative approach, which demonstrates the possibility of creating a better future by following this theory. There are eight main, constitutive characteristics of the coincidence theory of development:

1. Departure from dogmatism understood as an intellectual corset and a factor that unilaterally influences the search for answers to specific questions;
2. Avoiding blind subordination to any ideology or political line; instead, searching for objective truth without surrendering to conventional wisdom and consensual truth;
3. Abandonment of "all-istic" attempts to create a universal theory of economic growth; instead, paying attention to specific features of phenomena and processes integrally related to macroeconomic reproduction;
4. Interdisciplinary approach enriching economic thinking with considerations from other fields of social sciences, particularly from history, futurology, geography, law, sociology, psychology, management or the web-science;
5. Wide application of the comparative method of economic analysis;
6. Moving in the multi-dimension space comprising essentially historic, geographic, cultural, institutional, political, social and specific problem related substances;
7. Differentiation between targets and measures;
8. Instrumental flexibility open to multidirectional search for remedies fitting a specific and precise situation.

The New Pragmatism points to the need of a new approach to state interventionism. It cannot mean interference in the production and trade, but it must come down to an intelligent regulation of such processes.

Therefore pragmatism is needed. Great pragmatism. As little ideology as possible, but as much pragmatism as possible. It may be easily defined as New Pragmatism, since it has to be based on a new approach resulting from the analytical and theoretical understanding presented above.¹⁰ It is also new because it comprehensively takes into consideration the new conditions of managing the economy, unprecedented in the past, which emerged as a result of globalisation. We are talking here about an unorthodox theory of economics or, in a wider context, a theory of social sciences focused on practice. In the macroeconomic scale, which contemporarily implies the planetary scale, it is a policy or a global development strategy *sensu largo*. The New Pragmatism points as well to the need of a new approach to state interventionism. It cannot mean interference in the production and trade, but it must come down to an intelligent regulation of such processes. That is the fundamental alternative for the neoliberal myopia, which has been discredited so much in the context of the present-day crisis.

About the author

Professor Grzegorz W. Kolodko intellectual and politician, a key architect of Polish reforms, renowned expert on economic development and author of numerous books and research papers published in 25 languages. While Deputy Prime Minister and Minister of Finance (1994-97) he led Poland to the OECD. Holding the same positions in 2002-03, he played an important role in Poland's integration with the European Union. He is Director of TIGER – Transformation, Integration and Globalization Economic Research at Kozminski University in Warsaw. He is a marathon runner and globetrotter.

For more information please visit: www.volatileworld.net
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Notes

1. See Kolodko 2011 (www.volatileworld.net).
2. In the same period, the Chinese GDP per capita (according to PPP) reaches ca. 46 per cent of the Russian level and 39 per cent of the Polish level, while a decade earlier the indices amounted to 31 and 23 per cent respectively. GDP per capita estimates according to the Purchasing Power Parity – World Bank data.
3. It means in the scale of the planet the subtotal of negative and positive current accounts amounted to ca. USD 5 trillion, while GWP was ca. 78 trillion (as calculated in USD according to the current foreign exchange rates).
4. See Skidelsky 2009.
5. On the essence of the neoliberalism read more in the excellent study by Harvey 2005.
6. An advocacy point of view in favor of indeed weak government (yet presented as the argument against "State capitalism") is presented in Brenner 2010.
7. See more on the role of State in modern economy in Fukuyama 2004.
8. See Roubini and Mihm 2010 and Stiglitz 2010.
9. On the issue of postcommunist transformation see more in Kolodko 2000 and Estrin, Kolodko, and Uvalic 2007.
10. See more on this subject in Kolodko 2011.