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MEET THE NEW NORMAL, SAME AS THE OLD NORMAL: THE STATE-MARKET BALANCE AND ECONOMIC POLICY DEBATES AFTER THE PANDEMIC

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Abstract

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The State-Market Balance and Economic Policy Debates After the Pandemic

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1. Introduction

The economic impact of the pandemic of 2020 has been dramatic. Estimates of GDP growth downturns are tentative and varied but there is an overall consistency and they tell a sobering story. For example, the IMF's World Economic Outlook for June 2020[1] says, "Global growth is projected at –4.9 percent in 2020….In 2021 global growth is projected at 5.4 percent. Overall, this would leave 2021 GDP some 6½ percentage points lower than in the pre-COVID-19 projections of January 2020." The recovery from the decline, the shape of the "V" curve, is uncertain, depending on policies. The sharp dislocation will surely change the initial conditions for future trajectories significantly.

The focus of this paper is not, however, on the direct economic impact, but on the consequences of the pandemic for economic policy debates and thinking. Of course, there are many detailed and specific aspects of policy, for example on the efficacy of different types of lockdown, on which lessons are being learnt. But my perspective here is that of a broader canvas, in particular the prediction and the hope that there will be significant and dramatic changes in the balance between state and market, the pandemic having demonstrated the central role of the state in bringing the pandemic under control. Here one cannot help but notice a certain breathlessness in claims that nothing will ever be the same again--the new normal in the economic policy discourse will give a much higher weight to state relative to market.

I wish to argue, both from past experience and from the inherent nature of economic policy debates, that such a dramatic paradigm shift in the balance between state and market is unlikely. My prediction is that once the immediate crisis has passed, these debates, and their resolutions, will settle back into an old pattern of cycling between emphasis on directional moves towards one end or the other of the spectrum without a permanent significant displacement.

The plan of the paper is as follows. Section 2 begins by reviewing some of the claims that the pandemic will, or should, make dramatic changes in the balance between state and market. Section 3 takes a historical perspective and considers the fate of similar claims made in history. It argues that those predictions of major changes did not pan out over the medium term. Section 4 considers why such dramatic and permanent shifts are unlikely in the realm of economic policy and the balance between state and market. Section 5 concludes.

2. New Normal Predictions and Hopes

The pandemic has led to an outburst of predictions and hopes of what the new normal in economic policy might look like in the years to come as we pass through the impacts of the crisis. No doubt, the immediate shock and severity of the crisis has led to this rethink on global futures. I will review here a small selection of these contributions and pronouncements. But before doing that let us consider for a moment the severity of the present crisis compared to previous global crises, to put in historical context the economic basis for these calls to radical reassessment of policy.

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[1] https://www.imf.org/en/Publications/WEO/Issues/2020/06/24/WEOUpdateJune2020

At the time of the last global crisis, the financial crash of 2008-2009, Eichengreen and O'Rourke (2010) quite naturally compared what came to be called the Great Recession to the previous global economic plunge, the Great Depression of the 1930s. The basic conclusion was that the dip in global output was dramatically smaller and less prolonged in the Great Recession than in the Great Depression, thus justifying the nomenclature. In the 1930s, the index of world production fell by close to 40 percent over 35 months before recovery began. In 2008-2009, the same index fell by less than 15 percent and the recovery began within 10 months. The dominant reason for the difference was policy. Fiscal and monetary stimulus brought about a shallower trough and more rapid recovery from the second crash, the lessons of the first crash having been learnt by policy makers.

It is still very early days for a full assessment of the current pandemic shock, but De Grauwe and Ji (2020) have conducted a similar exercise to that of Eichengreen and O'Rourke (2010) using data from US, EU and China. The EU had the sharpest drop in industrial production, of just over 25 percent, but the recovery began only 3 months after the collapse started. For the US and China the drop was less and the "V" shape recovery began after 3 months or less. Six months after the crisis started output is estimated to be around 10 per cent below its pre-crisis level for the US, and the recovery is even stronger for the EU and China.

Thus, despite the immediacy of the difficulties and disruption of daily life, and intense coverage in the media, actual data do not suggest an economic crisis of anything like the severity of the Great Recession, and certainly nothing like that of the Great Depression. Yet there has been no shortage of forecasts of a major rupture to the economic system and of predictions, and hope, of radical realignment in economic policy. I will cite six examples to illustrate the strands in this line of thinking.

In terms of the future of the world economy, Adam Tooze (2020) writes, "the Covid-19 shock has raised globalisation angst to a new pitch. The World Trade Organization (WTO) is predicting that trade may fall by a record 32%. The lockdowns were disruptive enough. But as the economic crisis deepens, 2020 is beginning to look like something worse: a perfect disruptive storm." Indeed, when Tooze looks ahead he sees "the death of globalization," as the result of a number of forces but with the pandemic being the proverbial last nail in the coffin.

Goldberg (2020) continues the theme by stating the attacks that are being mounted on trade and openness in the wake of the crisis: "The COVID-19 crisis has emboldened advocates of protectionism and deglobalization. Familiar concerns about lost manufacturing jobs and rising inequality, or the desire in some circles to "punish" (scapegoat) China with higher tariffs, have now been augmented by an argument against global supply chains. According to this view, widely distributed production has made economies less self-sufficient, and therefore less resilient. The solution is to reshore existing business operations, offshore less in the future, and reduce reliance on trade more generally." Goldberg mounts a defense against these attacks, but their presence shows the nature of debates to come post-pandemic on free trade versus state intervention in international commerce.

That global trends were already problematic before the pandemic, and that the pandemic has merely shone an unforgiving light on them, is the perspective taken by Bouin et. al. (2020). They start by highlighting the paradoxical state of anxiety that existed in the world even before the pandemic, paradoxical because this was despite the enormous progress in economic and social indicators in the world over the past three quarters of a century since the end of the Second World War. The anxiety is the result of key deficits in the patterns of development, among them growing inequality. The issue of inequality would have had to be tackled even without the pandemic, but the unequal impact of the pandemic itself has thrown the issue into sharp relief.

A fourth example of big picture thinking in the wake of the crisis comes in the writings of Dani Rodrik. Rodrik (2020) echoes Tooze (2020) and Goldberg (2020) in saying that there will be a move away from what he calls “hyper-globalization” towards national autonomy, although unlike Goldberg (2020) Rodrik supports such a move. The main thrust of Rodrik’s argument is the prediction that there will be a rebalancing between state and market, towards the state. But such a rebalancing, according to Rodrik, has been building for a while and will merely be accelerated by the pandemic: “There is nothing like a pandemic to highlight markets’ inadequacy in the face of collective-action problems and the importance of state capacity to respond to crises and protect people. The COVID-19 crisis has raised the volume on calls for universal health insurance, stronger labor-market protections (including of gig workers), and protection of domestic supply chains for critical medical equipment.”

Continuing the theme of rebalancing sate and market, Daron Acemoglu (2020) leaves us in no doubt that “Given the nature and scale of the demands being placed on modern states, it is clear that "business as usual" will no longer suffice, even if it remains the easiest option.” He then considers a number of possibilities as alternatives: (1) “China-lite” where “Western democracies would try to emulate China by worrying less about privacy and surveillance, while permitting more state control over private companies.” (2) “Digital Serfdom” where the technology companies would dominate in a world of rising inequality with some redistribution as a palliative. (3) “Welfare State 3.0”, which would follow from the first wave of introduction before and after the second world war, and the retreat of the second wave in the Reagan-Thatcher 1980s. This evolution of the welfare state to version 3.0 would respond to the fact that “many advanced economies need a stronger social safety net, better coordination, smarter regulation, more effective government, a significantly improved public-health system, and, in the US case, more reliable and equitable forms of health insurance.” Acemoglu concedes that this could be “wishful thinking” but holds out the hope that the crisis of the pandemic will mean that this is the path that would be followed.

The above writings of academics and professional economists are of course echoed in the general discourse. A narrative has become established that the previous years of deregulation and weakening of the state explain the poor response to the pandemic in the UK and the USA. Nordic countries, where the state has remained relatively strong, have done much better. Kibasi (2020), for example, views recent experience as confirmation of this thesis: “Among advanced countries, Britain and the United States have had the weakest responses to the pandemic. On both sides of the Atlantic, the state has been maligned and undermined by years of free-market ideology that has long held government to be an obstacle to progress, rather than an engine of it. We are all paying the price of this foolish ideology. Building back better needs to start with jettisoning the notion that problems are best solved individually rather than collectively. All our lives depend on it.” More hope than prediction, but still a call for rebalancing state and market away from a direction that is argued to have gone out of kilter.

3. State and Market: Predicted New Normals in History

It should be clear even to the casual observer that the pandemic has unleashed considerable thinking and writing about the evolution of the world post-pandemic, in particular on economic policy after the crisis. We have seen six illustrative examples in the previous section. Analysts and commentators have combined predictions with hopes on a range of policy issues. The balance between state and market has received a great deal of attention with both prediction and hope that the state would take on a dramatically bigger role relative to the market, emerging from its central role in addressing the pandemic.

There is of course a long history of thinking, writing and prediction on the balance between state and market. Debates on the balance are a constant feature of policy discourse. For example, in his magisterial account of Tudor government in sixteenth century England, Geoffrey Elton discusses the same balance and puts it in the context of the long duree:

"The doctrine of the body politic knit together demanded obedience and assistance from the governed and put upon the government the duty of looking after the welfare of its subjects. It was once thought that this represented typically medieval doctrine with which the *laissez faire* principles that dominated the state from 1660 to 1906 could be usefully contrasted; more recent development has shown that attitudes to the state which regarded it either as a natural protector or an unholy but necessary evil may alternate without regard to the categories of historical development. In fact, the Tudor revolution produced a much more effective example of the paternal state than anything the middle ages knew—something so effective that only the twentieth century has come to eclipse it. The sixteenth century called this sort of thing "commonwealth" or "common weal."" (Elton, 1974, p. 185)

Elton characterizes laissez faire as the dominant doctrine for a long time up to the twentieth century—the old normal. In an extraordinary piece of prescient writing, in 1926 John Maynard Keynes predicted *The End of Laissez Faire*. As interesting, however, is Keynes's account of the rise to prominence of the Laissez Faire doctrine in the eighteenth and nineteenth centuries (Keynes, 1926, pp. 275-276):

"The individualism of political philosophers pointed to laissez-faire. The divine or scientific harmony (as the case might be) between private interest and public advantage pointed to laissez-faire. But above all, the ineptitude of public administrators strongly prejudiced the practical man in favour of laissez-faire—a sentiment which has by no means disappeared. Almost everything which the state did in the eighteenth century in excess of its minimum function was, or seemed, injurious or unsuccessful….Thus the ground was fertile for a doctrine that, whether on divine, natural, or scientific grounds, state action should narrowly be confined and economic life left, unregulated so far as may be, to the skill and good sense of individual citizens actuated by the admirable motive of trying to get on in the world."

However, Keynes wrote that this state of affairs was about to rebalance:

"But a change is in the air. We hear but indistinctly what were once the clearest and most distinguishable voices that have ever instructed mankind. The orchestra of diverse instruments, the chorus of articulate sound, is receding at last into the distance." (Keynes, 1926, p. 272).

Why the predicted change? For Keynes it was that the market system could not address key emerging issues and state intervention was essential:

“Many of the greatest economic evils of our time are the fruits of risk, uncertainty, and ignorance. It is because particular individuals, fortunate in situation or in abilities, are able to take advantage of uncertainty and ignorance, and also because for the same reason big business is often a lottery, that great inequalities of wealth come about; and these same factors are also the cause of the unemployment of labour, or the disappointment of reasonable business expectations, and of the impairment of efficiency and production…..I believe that the cure for these things is partly to be sought in the deliberate control of the currency and of credit by a central institution…My second example relates to savings and investment. I believe that some coordinated act of intelligent judgement is required as to the scale on which it is desirable that the community as a whole should save, the scale on which these savings should go abroad in the form of foreign investments, and whether the present organisation of the investment market distributes savings along the most nationally productive channels. I do not think that these matters should be left entirely to the chances of private judgement and private profits, as they are at present.”(Keynes, 1926, pp.291-292.)

Keynes’s battles with the UK Treasury in the 1930s are well known, and the post war consensus on economic policy has the appellation “Keynesian” with good reason. However, the consensus of the 1950s on a greatly expanded role for the state lasted for only so long. As Acemoglu (2020) noted above, the pendulum began to swing back again in the 1980s—the Reagan-Thatcher era. And at the end of this decade came the fall of the Berlin Wall, an event regarded at the time by observers as cataclysmic in its consequences and implications. Most famously, of course, Fukuyama (1989) pronounced “the end of history”, meaning by this that the big debates of the century were over. Liberal politics and market economics had triumphed. He did not use the term, but he was in effect predicting a new normal, indeed proclaiming that it had arrived.

It was not to be. Writing in 2001, only a decade after the proclamation, I noted, “The end of history lasted for such a short time” (Kanbur, 2001, p. 1083). The disasters of transition to market economies in the previously centrally planned economies, too rapid and too ill planned (I use the term advisedly), highlighted the institutional basis of a functioning market economy. To this was added the equally disastrous “lost decade” of austerity and marketization in Latin America in the 1980s. To cap it all, the financial crisis of 1997, the conditions for which were ripe after the deregulation of financial markets in the 1980s and 1990s, became in effect the first global economic crisis of the emerging century. Towards the end of the 2000s, less than two decades after Fukuyama’s pronouncement of the end of history, the Commission on Growth and Development (2008), headed by two Nobel Prize winners, Robert Solow and Michael Spence, and comprising leading lights of the economic policy making elite of developed and developing countries, concluded as follows:

“In recent decades governments were advised to “stabilize, privatize and liberalize.” There is merit in what lies behind this injunction—governments should not try to do too much, replacing markets or closing the economy off from the rest of the world. But we believe this prescription defines the role of government too narrowly. Just because governments are sometimes clumsy and sometimes errant, does not mean they should be written out of the script. On the contrary, as the economy grows and develops, active, pragmatic governments have crucial roles to play. ” (p.4)

The publication of the Commission’s report coincided with the financial crisis of 2008-2009, the last big global crisis with economic impact comparable to the pandemic--in fact, as we have seen an impact bigger in magnitude than the pandemic. During the crisis, we saw similar writings on the role of the state. “We are all Keynesians in a fox hole” was the adage as central banks loosened monetary policy and governments adopted expansionary fiscal policy. I was among many who wrote that the crisis should be a warning bell of crises to come and that governments should prepare for them by strengthening and expanding social protection (Kanbur, 2010). Again, prediction and hope that the balance of state and market would be pushed towards state by the crisis.

However, the actual outcome was a swing back of the pendulum in the 2010s as government policy, especially in Europe, turned back to austerity and fiscal cuts in the face of worries on the consequences of high levels of public debt. An influential academic paper by Reinhart and Rogoff (2010) argued that high levels of debt above a threshold had a deleterious effect on growth. This paper is among those held to have given the intellectual foundation for austerity policies. In the broader discourse, Greece’s former finance minister and himself an economist, Yanis Varoufakis (2018) gives an insider’s account of the battles of ideology and politics in those times, a battle he considers to have been won by the supporters of austerity and big bank bailouts. Which brings us full circle to the pandemic and a new round of hope and prediction as illustrated in the previous section.

4. Paradigm Shifts and Dialectics[2]

We have seen that the predicted and hoped for shift in state-market balance after the pandemic is part of a cycle of movement in thinking and policy which has been with us for a long time. Rather than a permanent shift in one direction or another (“nothing will ever be the same again”) it is a pendulum that has swung back and forth. If history is any guide, after a reorientation for a few years, perhaps even a decade, we are likely to be back to the old questions of how much state intervention there should be, and a likely swing back to a market-oriented disposition.

But why is this the case? The question was posed in a debate in economics and the history of economic thought that took place after the publication in 1962 of Thomas Kuhn’s book *The Structure of Scientific Revolutions*. Kuhn famously argued that in the natural sciences there were “paradigm shifts”, radical changes in thinking and frameworks as exemplified by the Copernican or Newtonian revolutions—the word revolution being used deliberately:

“Probably the single most prevalent claim advanced by the proponents of a new paradigm is that they can solve the problems that have led the old one to a crisis…. Copernicus thus claimed that he had solved the long-vexing problem of the length of the calendar year, Newton that he had reconciled terrestrial and celestial mechanics, Lavoisier that he had solved the problems of gas-identity and of weight relations, and Einstein that he had make electrodynamics compatible with a revised science of motion.” (Kuhn, 1962, p. 153)

A natural enough question then was whether there had been such revolutions in economic thinking. The conclusion seemed to be that political economy broadly construed did not exhibit such Kuhnian paradigm shifts that swept all before them. Bronfenbrenner (1971, p. 2) offered three possible candidates for the label of revolution:

[2] This section draws on Kanbur (2016)

“The first is a laissez-faire revolution…. A conventional date is 1776, when Adam Smith’s Wealth of Nations was published…. The second possible revolution is the breakup of the classical school which followed Smith, and which was led in turn by David Ricardo and John Stuart Mill. A conventional date for this second, or “utility,” revolution is 1870. The third possible revolution is the breakup of the neoclassical Cambridge School which arose from the utility revolution under the aegis of Alfred Marshall and his successor A. C. Pigou. This revolution occurred during the Great Depression. A conventional date is 1936, the appearance of J. M. Keynes’s General Theory.”

He concluded that none of these had the characteristics to match revolutions in the natural sciences, but were more in the manner of syntheses of doctrines and their contradictions. A Hegelian thesis-antithesis-synthesis dialectic seemed to describe best the evolution of thinking in political economy.

But why, in turn, should the evolution of political economy thinking be one of dialectical process rather than paradigm shifts? Its close, symbiotic, relationship with economic policy may provide an answer. This symbiosis goes back a long way. In 1795, Edmund Burke wrote a long letter to the Prime Minister William Pitt (“Pitt the Younger”) entitled *Thoughts and Details on Scarcity*, arguing against government subsidy of agricultural wages during a time of crisis caused by poor harvests. However, although it was directed to a specific policy issue, the frame of thinking which led to Burke’s conclusions was broader:

“Of all things, an indiscreet tampering with the trade of provisions is the most dangerous, and it is always worst in the time when men are most disposed to it: that is, in the time of scarcity. Because there is nothing on which the passions of men are so violent, and their judgment so weak, and on which there exists such a multitude of ill-founded popular prejudices…. But the throats of the rich ought not to be cut, nor their magazines plundered; because, in their persons they are trustees for those who labour, and their hoards are the banking-houses of these latter. Whether they mean it or not, they do, in effect, execute their trust—some with more, some with less fidelity and judgment. But on the whole, the duty is performed, and every thing returns, deducting some very trifling commission and discount, to the place from whence it arose. When the poor rise to destroy the rich, they act as wisely for their own purposes as when they burn mills, and throw corn into the river, to make bread cheap.” (Kramnick, 1999, p. 195)

It should of course be very clear that the reasons Burke gives for not interfering with the workings of the market are the very reasons that others argued for intervention. Keynes was a follower of Burke in many respects. Indeed he has been called a “Burkean conservative.” But on this he differed with his hero, writing more than a century and a quarter later:

“Let us clear from the ground the metaphysical or general principles upon which, from time to time, laissez-faire has been founded. It is not true that individuals possess a prescriptive “natural liberty” in their economic activities. There is no “compact” conferring perpetual rights on those who Have or on those who Acquire. The world is not so governed from above that private and social interest always coincide. It is not so managed here below that in practice they coincide. It is not a correct deduction from the principles of economics that enlightened self-interest always operates in the public interest. Nor is it true that self-interest generally is enlightened; more often individuals acting separately to promote their own ends are too ignorant or too weak to attain even these. Experience does not show that individuals, when they make up a social unit, are always less clear sighted than when they act separately.” (Keynes 1926, 287-288).

The difference between Keynes and Burke has of course echoed in the political economy discourse and the debate has swung back and forth. But the reason for the debate and the reason for the cycles was well stated by Kramnick, 1999, pp. 195-196):

"It is one of the finest problems in legislation, and what has often engaged my thoughts whilst I followed that profession, "What the State ought to take upon itself to direct by the public wisdom, and what it ought to leave, with as little interference as possible, to individual discretion." Nothing, certainly, can be laid down on the subject that will not admit of exceptions, many permanent, some occasional. But the clearest line of distinction which I could draw, whilst I had my chalk to draw any line, was this: That the State ought to confine itself to what regards the State, or the creatures of the State, namely, the exterior establishment of its religion; its magistracy; its revenue; its military force by sea and land; the corporations that owe their existence to its fiat; in a word, to every thing that is *truly and properly* public, to the public peace, to the public safety, to the public order, to the public prosperity."

Keynes agreed with this characterization when he wrote in *The End of Laissez Faire*:

"The important thing for government is not to do things which individuals are doing already, and to do them a little better or a little worse; but to do those things which at present are not done at all" (Keynes, 196, p. 291)

He further stated that "the chief task of economists at this hour is to distinguish afresh the *Agenda* of government from the *Non Agenda*." In this view, what mattered was what was on the Agenda, and if this changed dramatically then the balance between state and market would shift. Such continuity along the spectrum of state and market does not sit well with the proclamation of *The End of Laissez Faire*, but this inconsistency is not the first in Keynes in his self-proclaimed task of saving capitalism rather than ending it.

Thus at the heart of the evolution of the political economy discourse is Burke's question of "What the State ought to take upon itself to direct by the public wisdom, and what it ought to leave, with as little interference as possible, to individual discretion," and Keynes's call "to distinguish afresh the *Agenda* of government from the *Non Agenda*." As new situations arise the *Agenda* shifts, and then shifts again, sometime involving the state more, sometimes less. Hence the cycles, rather than cataclysmic paradigm shifts.

5. Conclusion

What will happen to economic policy debates after the Pandemic? The majority view seems to be that nothing will ever be the same again. A new normal will be upon us. A combination of prediction and hope points to a major reorientation of the state-market balance towards the state. The last time we had such millennialist thinking was of course after the financial crisis of 2008-2009, when a different sort of contagion spread through the world. Two decades before the great financial crisis, the fall of the Berlin Wall ushered in the new normal claims of that era. Most famously, Fukuyama announced the End of History, the final victory of liberal politics and (neo) liberal economics.

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Of course, the current pandemic will wreak economic havoc and reset at least some of the initial conditions for the global economy. The unsettled times and the proclamations of the new normal will surely be with us for several years. However, if past patterns are anything to go by, at the decade’s end it is as good prediction as any that the new normal will be the same as the old normal.

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