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Neoliberalism and the State of the Advanced World Economy: Can the Blind Heal the Crippled?

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Crises are an inherent feature of capitalism. Marx knew this only too well; so did Keynes and Minsky. Neoliberals, on the other hand, tend to believe that it is government action that causes market turbulence and economic instability.

Whoever said that economic science is free of ideological bias and political prejudice? Three hundred years of financial and economic crises have meant nothing to die-hard neoliberals, who insist on the existence of the self-regulating market, believe in trickle-down theory, and, until recently, even argued, as Robert Lucas did back in 2003, that the "central problem of depression prevention has been solved."

With so many incorrect assumptions guiding market liberalism, it is no wonder neoliberals have failed to draw the proper lessons from the experience of the Great Depression and turned a blind eye to the real causes of the global financial crisis of 2007–08 and the ensuing recession.

In the case of the global financial crisis, it was an unbound, out-of-control Promethean capitalism that gave rise to wild financial innovation, which in turn led to unsustainable speculation in the US housing market and, in the end, to the subprime mortgage crisis. Failure to regulate credit default swaps and other derivatives was indeed a huge mistake. But the causes of this crisis can be attributed to yet another key variable: namely, to a brutal version of capital accumulation marked by downsizing, wage stagnation, regressive redistribution of income, and the curbing of organized labor—factors that, together, resulted in a wild spiral of borrowing and debt.

Those are two among a number of other key facts about the global financial crisis of 2007–08 that neoliberal economists refuse to even acknowledge.

Neoliberal doctrinaires also downplay the idea that, as in the past, capitalism was saved by none other than the very institution they so despise (when not functioning exclusively at the behest of the rich and powerful): government intervention, which included a wave of nationalization, averted a global financial meltdown, and prevented a second Great Depression through government stimulus programs. Without this last, we would have had an even greater rate of unemployment and a steeper GDP decline.

But the world's advanced economies are not out of the woods yet. On the contrary, there are signs that the risk of a downturn is high and a "double-dip" recession, although certainly not inevitable, is still very much in the picture. Among the signs that the risk of a global recession is high are that the US economy is experiencing a historically unprecedented lack of job growth and growth throughout Europe is slowing down, even in Germany.

The situation in Europe in particular is quite volatile. The austerity measures are having a direct negative effect on economic growth, but Europe's political elite insist on a fiscally conservative attitude. In addition, the Continent's banks are grossly undercapitalized and thus extremely vulnerable. Yet there is no plan for a European approach, and countries are left on their own to take measures to protect their banks. And finally, of course, there is the eurozone's serious debt crisis, which will only get more serious, as EU leaders have essentially opted to kick the can down the road for as long as possible and are oblivious to the fact that the day of reckoning is getting closer.

Common sense, economic theory, and historical experience indicate that the tools for avoiding a global recession lie in the hands of government and its institutions, and not in the invisible hand of the market. This means active government intervention in the marketplace (housing, education, health, energy, infrastructure, et cetera) and expansionary monetary policy. Reducing deficits in the midst of an economic downturn through austerity measures and budget cuts is government intervention in the wrong direction: it is shifting the balance in favor of markets, when it is the markets themselves that are responsible for the economic mess—and thus hardly in a position to stir economic growth and accelerate development.

Neoliberal economic thinking is dangerously flawed. The current state of the advanced world economy has some striking similarities to the conditions that led to the Great Depression, and the spread of neo-Hooverism provides the unsettling sensation of déjà vu. Indeed, expecting the blind to heal the crippled ended in tragedy in 1929. Why would anyone think it would be any different this time around?

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