

The Keynesian Revolution and the Neo-liberal Counter-revolution

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As a result of the depression of the 1920s and 1930s, a new wave of critics tackled the neo-classical creed on a largely pragmatic basis. This new wave was international and involved political leaders and economists from differing backgrounds: enlightened bourgeois thinkers, socialists and Marxists. In a context of mass unemployment and depression, proposals came forward for major public works, for anti-cyclical injections of public money, and even for bank expropriations. Such proposals came from a wide variety of sources: Germany's Doctor Schacht; the Belgian socialist Deman; the founders of the Stockholm School, backed by the Swedish social democrats; Fabian socialists and J.M. Keynes in Britain; J. Tinbergen in the Netherlands; Frisch in Norway; the Groupe X-crise in France; Mexican president Lazaro Cardenas (1935-1940); adepts of Peronism in the Argentina of the 1930s; US president Roosevelt (elected in November 1932) and his New Deal.

*The entire range of proposals and pragmatic policies was partially summed up in Keynes's 1936 work *General Theory of Employment, Interest and Money*.*

The Keynesian revolution

The preparatory work carried out by Keynes (1883-1946), laying the groundwork for the General Theory, was fuelled by the need to find a solution to the spreading crisis of the capitalist system. Moreover, this solution had to be compatible with the continued survival of the system. The work was partially the result of a wide-ranging collective process wherein groups and individuals ended up in different Keynesian camps, often very much at odds with one another. Some leaned more towards Marxist positions, such as the Briton Joan Robinson and the Pole M. Kalecki, who had actually formulated the key components of the General Theory before Keynes. Others grew progressively closer to the very tenets of liberalism and neo-classical economics that Keynes decried.

In one of his works, Keynes pays homage to the English philosopher George Edward Moore, whom he credits with having freed him from the prevailing morality of the day and having 'protected us all from that final reductio ad absurdum of Benthamism known as Marxism'[2].

Keynes had been politically active since the First World War. As an employee of the British Exchequer, he actively participated in negotiations on the Treaty of Versailles, which marked the end of the War in 1918. He resigned from the British delegation in protest against the scale of reparations imposed on Germany. Soon after, he wrote *The economic consequences of the peace* (Keynes, 1919).

In the 1926 pamphlet *The end of laissez-faire*, he writes: 'It is in no way accurate to deduce from the principles of political economy that enlightened personal interest always works in favour of the general interest[3]'.

In the 1920s, Keynes condemned the policies of Winston Churchill's Tory government. He opposed the liberal (neo-classical) policies that provoked the miners' strike, followed by the 1926 general strike.

Thereafter, he called for a policy of major public investment. He supported the Liberal Party while maintaining friendly ties with the Labour Party. In 1929, in the wake of Tory and the liberals' defeat, the new Labour government appointed him to the McMillan Commission on the economic situation. In 1930, he became an advisor to the same government.

The economic crisis deepened following the 1929 Wall Street crash, leading Keynes to produce an analysis of employment, interest and money which strengthened his conviction that there should be increased state intervention. To compensate for the shortfall in demand, the state should increase spending in order to give a boost to the economy and employment.

Thereafter he became involved in a major debate with Hayek. Although, like Keynes, Hayek had come to reject a number of the ideas of Smith, Ricardo, Walras and Jevons, with Ludwig von Mises (1881-1973) he fashioned a set of ultraliberal ideas which fiercely opposed (standing in fierce opposition to) the main tenets of the Keynesian revolution.

Whereas Keynes and his fellow economists were convinced that the Great Depression had been caused by the collapse in investment, Hayek and his supporters saw over-investment rooted in slack monetary policies as the cause. For Keynes, consumption and investment had to be sparked by strong state intervention. For Hayek, state intervention reduced the funds available for private investment. For Keynes, wages had to be increased to stimulate consumption. For Hayek, they had to be lowered to ensure renewed full employment. The debate (polemic) hit the pages of the British press in 1932 (*Times*, 17 and 19 October 1932).

Keynes believed that economic policy should be geared towards reducing the high unemployment rate and distributing revenues in a more egalitarian manner. If the government did not pursue the objectives of full employment and greater equality, he argued, there was a serious danger that either fascism or Bolshevik communism would win the day. Government policy had to be aimed at reducing high interest rates, which channelled vital resources into the financial sector. By lowering interest rates, the aim was to favour the destruction of the rentier class (living on unearned income), the scourge of the capitalist system. At the same time, however, Keynes states quite clearly that the consequences of his theory are 'moderately liberal':

'[...] while it highlights the vital importance of establishing certain central controls in fields that today remain completely in the hands of private initiative, it also leaves a great many fields of activity in private hands [...] It does not actually call for a system of state socialism that would subject most of the community's economic life to its control[4].

Keynes's prescriptions were put into practice in many regions of the world right up until the 1970s. They also strongly influenced a number of economists, such as Samuelson,

Galbraith, Tobin and Prebisch.

Preparing the neo-liberal counter-revolution

There was a swift reaction to the policies of state intervention aimed at boosting demand and moving towards full employment. From the beginning of the 1930s, Hayek and von Mises set out to demolish Keynes's proposals.

'Since 1945, in various academic and business circles, different projects have emerged simultaneously to bring together the qualified defenders of liberalism (neo-classical economics) with the aim of organising a joint response to the advocates of state intervention and socialism. Three centres where this post-War resistance was organised were: the Institut universitaire de hautes études internationales (IUHEI) in Geneva, the London School of Economics (LSE) and the University of Chicago[5]'

At the end of the Second World War, Hayek was teaching at the LSE. In 1947, he and Von Mises founded the Société du Mont-Pèlerin. The first meeting was held in April 1947 and brought together 36 liberal luminaries at the Hôtel du Parc at Mont-Pèlerin near Vevey in Switzerland. The gathering was financed by Swiss bankers and industrialists. Three major US publications (Fortune, Newsweek and Reader's Digest) sent delegates. In fact, Reader's Digest had just run an abridged version of one of Hayek's main works, *The Road to Serfdom*. Among other things, that book said:

'In the past, man's submission to the impersonal forces of the market made possible the development of a civilisation which otherwise would not have emerged. It is through submission that we participate everyday in the building of something much bigger than what we can all fully understand[6]'

Right-wing economists and philosophers from different 'schools of thought' participated in the gathering.

'At the end of the meeting, the Société du Mont-Pèlerin was founded - a kind of neo-liberal Freemasonry, very well organised and devoted to the dissemination of the neo-liberal creed, with regular international gatherings[7]'

Among the organisation's most active members were Hayek, von Mises, Maurice Allais, Karl Popper and Milton Friedman. It became a think tank for the neo-liberal counter-offensive. Many of its members went on to win the Nobel Prize in economics (Hayek in 1974, Friedman in 1976 and Allais in 1988).

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Translated by Vicki Briault, Francesca Denley and Raghu Krishnan.

Notes

[1] The first part of this series ‘A Glance in the Rear View Mirror to Understand the Present’ was posted on the CADTM website on 12 June 2009 under the title ‘Adam Smith is closer to Karl Marx than to those who sing his praise’

<http://www.cadtm.org/spip.php?article4462>;

was posted on June 13th under the title: “Neo-liberal ideology is a hard nut to crack”

<http://www.cadtm.org/spip.php?article4468>

the third part was posted on the 19 June 2009 : "The 1930s to the 1970s: liberalism eclipsed"

<http://www.cadtm.org/spip.php?article4495>;

the fourth part was posted on the 25th June 2009: "The 1970s: Liberal ideology returned with a vengeance"

<http://www.cadtm.org/spip.php?article4508>

[2] Quoted in Beaud and Dostaler, 1995, p.37

[3] Quoted in Beaud and Dostaler, 1995, p.40.

[4] Keynes, 1936, Final Notes, Spanish ed p 362

[5] Udry, 1996

[6] Von Hayek, 1944

[7] Anderson, 1996

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