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Roundtable

The British economy: a crisis of Anglo-liberal capitalism?

Colin Hay's book, The Failure of Anglo-Liberal Capitalism (2013), offers a powerful account of the origins and implications of Britain's current economic malaise. Hay argues that the roots of the recent economic crisis lie in Britain's complicity in the rise of an unstable Anglo-American model of capitalism that sustained consumption and economic growth via the acquisition of private debt. Critical of British governments of all parties, Hay outlines a new economic agenda for a more sustainable and inclusive model of growth. Renewal gathers here four reflections on the book, and a response from Colin Hay.

The right central premise

Nicola Smith, Head of the Economic and Social Affairs Department of the TUC

The starting premise of Colin Hay's analysis is that the roots of the financial crisis can be found in the years preceding the crash. This is a presumption that few in the current government would disagree with, although their assessment would likely be different to Hay's. While the Coalition narrative presents our current fiscal challenges as a consequence of years of irresponsible public sector over-expenditure, Hay's assessment is that without significant change in the composition of UK growth we face on-going future economic risks.

There is much to agree with in this headline analysis, and while my own assessment contains shades of difference to Hay's, his central premise that the crisis revealed the need for significant change in the UK economy is surely the right one.

A crisis of credit?

In brief, the starting point of Hay's argument is that those countries where consumption relied to the greatest extent upon rising household debt were first affected by the crisis, which, given the global nature of both financial markets and trade, then went on to impact on other nations.

In part, this analysis is accurate. As credit markets froze and recession began, consumers with high debt obligations reigned in their spending or found they could no longer access the loans that were funding their purchases. On-going uncertainty meant others reduced their inclination to borrow.

But Hay's position is arguably also partial in so far as it places insufficient focus on the extent to which high levels of private debt were indicative of out of control financial sectors, and on the relationship between the size and nature of nations' financial services industries and the consequent impacts of the crisis on their economies. In the UK, for example, banks' balance sheets tripled in size over the five years from 2002. Capital buffers were low, and new funds tended to be short-term in nature rather than new deposits. The assets of RBS were worth (on paper) 150 per cent of UK GDP (*Economist*, 2013). The high leverage, short-term funding and limited regulation that characterised the sector (all of which had acted to support the consumer borrowing boom) meant that the financial crisis hit the UK hard.

The impacts of the crisis were also perhaps wider ranging than Hay's analysis acknowledges. As banks' balance sheets disintegrated, both consumer and business lending were squeezed (and with the latter having shown barely no recovery since 2008 this sharp fall in business finance is still having a significant impact on the UK's economic prospects). Investment, consumption and confidence plummeted and as trade was so far from able to make up the gap (even before the rest of the world had entered recession) the downturn took hold.

Hay is right to draw attention to the UK's dependence on consumer debt, but a broader approach to analysing the causes of the crash, and its multiple and on-going impacts, would strengthen his analysis.

On-going risks

But Hay is undoubtedly right that high private debt remains a substantial downside risk for the UK economy. The latest Bank of England financial stability report (2012) suggests that 40 per cent of the UK's outstanding mortgages are now interest only (a proportion that rises to 50 per cent in some regions) and that around three quarters of interest only mortgage holders are reliant upon the sale of the home as their repayment plan. While household debt ratios have fallen in the UK since the financial crisis, rates remain significantly higher than a decade ago, and well above 150 per cent of income. The Bank concludes that 'an unexpected rise in interest rates would increase debt-servicing burdens and might induce a fall in property prices', which underlines the fragility of our recovery.

Hay is also right to point out that the UK's over inflated housing market remains an on-going challenge. In the years running up to 2008 the rate of house price growth in the UK outpaced many other developed economies, and undersupply seems to have been the most significant factor in preventing a crash of the sort that the US market has suffered. With prices still so far removed from incomes, the potential for further price falls (at least outside of London) remains real, with clear potential implications for household financial health.

However, Hay's assessment neglects to mention a key part of the puzzle – the extent to which rising reliance on debt financed expenditure has been a consequence not only of a house price boom, and unrestricted access to credit, but also of stagnating household incomes driven primarily by declining real wages and now considered by the ONS to be a key factor contributing to current slow growth in household spending.

In recent research from the IMF research department Michael Kumhof and Romain Ranciere (2010) found that financial liberalisation helps workers smooth consumption, but at the cost of higher household debt and larger current account deficits (as savings ratios are low). But crucially, when looking across different countries, they also identify rising income inequality as a key driver of these trends, and point to the need to distribute the rewards of growth more fairly as a prerequisite for stronger future outcomes. Stronger and fairer wage growth is central to their suggested solutions.

The UK is a perfect case study for this analysis. The wages of middle income Britain grew by an average of just 56 per cent between 1978 and 2008, despite GDP increasing by 108 per cent over the same period, and for some workers real income growth was far less (Lansley, 2011). The reasons behind this concerning trend are complex, reflecting both growing pay inequalities and slowing rates of real pay increases for workers on lower and middle incomes, along with occupational change across the UK jobs market (put simply, a rise in lower paid jobs in parts of the service sector accompanied by a fall in better paid middle income jobs in areas including manufacturing and administration). But its impacts are clear: stagnant living standards where spending is more likely to be supported by lending and equity release rather than rising real incomes.

Hay could therefore strengthen his critique of the sustainability of UK consumption if he focused as much on the poor state of real pay growth as on the extent to which spending has been supported by rising house prices and wider borrowing.

A fair assessment of Labour's performance

While Hay is right that it may well have been economically convenient for all governments to hope the bust was never going to come, he is perhaps too harsh when he claims that the previous administration actively pursued a strategy of asking house prices to fill the gap left by a residualised welfare state. While single unemployed people certainly saw little improvement in their real incomes (as Hay's analysis of benefit replacement ratios shows), some groups (most significantly families with children) saw real benefits from the introduction of tax credits, and the Pensions Commission's recommendations paved the way for some strengthening of provision in retirement. A fairer critique would be that the policy community experienced a collective failure to see the risks inherent in the bubble (and in the UK's growing wealth and income disparities), rather than presenting the government as having overseen an explicit strategy to replace social security with property equity.

On the other hand, Hay is perhaps too optimistic in saying that Labour have 'avoided the blame' for the crash. The challenge of presenting the electorate with a compelling vision of a new economy which both meets public concerns and can be delivered in straightened financial times is significant, and public trust that any political party can deliver substantial economic change, while also getting the public finances back on track, is low. While things could undoubtedly be worse for progressives, there is little room for complacency about public opinion.

Where next for the UK economy?

Hay concludes that we face a number of significant medium-term risks, and that moves towards a new economy will be difficult. He's right, particularly given the current government's aspirations to secure increased private saving and to improve Britain's trade and investment performance appear to have been abandoned. Instead, while real household incomes continue to plummet, austerity Britain is pinning its growth expectations on another house price boom.

But again perhaps the focus of Hay's conclusions is too narrow. He is right that we need to recognise that growth is the best way to get the deficit down and that we need an internationally co-ordinated stimulus. And he's also correct that banks need to lend more (the lack of net lending targets was a significant government mistake) and that there's a case for both greater public investment and national and regional banking structures to more effectively channel private investment into the real economy.

But, as he acknowledges, these changes are far from sufficient. The substantial shifts that we need to see in the overall investment share of the economy will need banking, corporate governance, and public sector reform working in combination. Raising living standards will need policies that deliver both faster rates of real pay growth along with the creation of more jobs in higher value sectors and the closure of the employment rate gaps that characterised the last decade. If we want less income inequality, redistribution will need to continue to play a vital role, which means we may need to think again about tax.

And there are also areas where Hay's conclusions do seem to risk leading us in the wrong direction. His assumption that financial sector regulation may serve to reduce our potential capacity and limit short-term growth does seem to risk undermining much of the rest of his critique. While he is right that bank lending to business needs to rise if investment is to grow I do not believe that this objective conflicts with the aim of securing a safer and more responsible financial services sector. The UK will always need a strong financial services sector but if progressives are serious about a new economy then it also needs to be very different from what has come before, both because of the economic catastrophe which could ensue if we don't better manage risk and because ballooning markets in property and financial products risk squeezing out the productive investment, export and wage growth that we need if there's to be any hope of building a fairer and stronger economy in the medium-term.

Similarly, Hay's conclusion that there has been too much focus on high pay seems counter-intuitive. Excessive executive bonuses and the growing income inequality they represent were a key cause of the crisis, and if we don't address them (through both taxation and sectoral rebalancing as well as regulation), and achieve a fairer income distribution over the medium-term, we're unlikely to be much closer to a better economic model for the future.

But overall Hay's broad assumptions are right – in key areas our pre-crisis economy was failing to deliver, and our future economic health depends on making sure we don't repeat the same mistakes again.

We need a new variety of British capitalism

Tony Dolphin, Senior Economist and Associate Director for Economic Policy at the IPPR

It is more than five years since the UK economy went into recession as a result of the financial crisis, yet real GDP is still over two per cent below its peak level before the recession and unemployment is one million higher than it was at the beginning of 2008. Despite this appalling record, there is little evidence that Britain's economic model – Anglo-liberalism as Colin Hay calls it – is about to be thrown out and replaced by a new variety of capitalism. This will seem odd to many, but it is understandable for a number of reasons.

First, economic paradigm shifts are extremely rare. There have only been two in Britain in the last century: the 'Keynesian revolution' in the 1940s and its replacement by 'Anglo-liberalism' in the 1970s/80s. Second, when shifts do occur, they do not come immediately after the crisis that triggers them: Keynesianism was a response to the Great Depression of the 1930s; Anglo-liberalism a response to the stagflation of the early 1970s. And third, neither the Coalition nor the Labour Party has yet articulated a coherent alternative to Anglo-liberalism.

As Colin Hay also points out, the Coalition has in effect defended Anglo-liberalism by framing Britain's economic problem as a debt crisis rather than a growth crisis. This has enabled it to fight the debate about policy in the short-term on the ground of its choosing. Platitudes such as 'you cannot borrow your way out of a debt crisis' may be bad economics, but they strike such a chord with the public that the Labour leadership is reluctant to whole-heartedly adopt the more sensible alternative, as espoused by Paul Krugman and others, of using fiscal policy to support the economy while private demand is weak and monetary policy ineffectual. As a result, they give the impression of not having a coherent policy for the economy. How different it would be if Labour was willing to argue unreservedly that the UK's problem was not an excess of public debt but a deficiency of growth and that 'you cannot cut your way out of a growth crisis'.

However, this growth crisis has not just emerged in the last few years; it was there well before the recession began, hidden by an unsustainable build-up in household and financial sector debt. Regrettably, although Labour accepts growth was over-reliant on financial services, it is reluctant to acknowledge fully the role of debt in supporting growth during this period because to do so would undermine its ability to take credit for the seemingly good performance of the economy during its first two and a half terms in office. Until it does so, however, it cannot begin to develop a serious alternative to Anglo-liberalism.

The starting point for a new variety of British capitalism has to be a sustained attack on the deficiencies of the Anglo-liberal model, combined with a realistic assessment of the structural pressures likely to be placed on the economy in coming years. It needs, therefore, to show how the financialisation of the British economy, and the strong pound that accompanied it, crowded out investment and growth in the rest of the economy and accelerated the decline in manufacturing; it needs to argue that an economy which has recorded current account deficits in every one of the last thirty years is not a successful one; it needs to make the case that Britain will never be a strong economy

while inequalities between its regions continue to increase; it needs to attack the growing inequalities in income and wealth that built up over the last 30 years and it needs to understand why over four million people were still claiming out-of-work benefits in 2007 after fifteen years of uninterrupted economic growth. It should also re-examine the role of the inflation target, given the absence of any trade-off between unemployment and inflation over the last two decades. And it needs to understand how technological change and globalisation are reshaping the British economy and why private sector firms are unable to adjust rapidly enough to maintain output growth close to its historical trend rate.

If anything sums up the need for an alternative to Anglo-liberalism, it is the failure of the Coalition to deliver on its promise to rebalance the economy. A 25 per cent devaluation of sterling was supposed to deliver growth led by exports, which would in turn lead to stronger investment spending and so reduce the need for growth to rely on debt and consumer spending. However, exports have not grown more strongly over the last few years. This has been blamed on the crisis in the eurozone, but that is only part of the problem. Despite the devaluation and big increases in exports to countries like China, Britain is not winning market share in emerging economies and British firms are not taking an increased share of their domestic market at the expense of importers. Under Anglo-liberalism, Britain's industrial base was allowed to shrink to the point that it no longer has the capacity to compete effectively, even when given a big boost to its competitiveness. And the Coalition is so devoid of ideas to rectify the situation that it is now prepared fall back on mortgage debt as a source of growth: risking a repeat of the worst mistakes of the Labour years with its Help to Buy scheme.

Some of the elements of a new variety of British capitalism should, therefore, be clear. Unemployment should be given an equal weight with inflation in the determination of monetary policy, not just for the next year or two, but on a permanent basis. Rather than pump-priming the mortgage market and encouraging another increase in household debt, more houses should be built. Financial markets should be more heavily regulated, in particular to introduce more competition into banking and to stop the extraction of rents from the rest of the economy. Labour market policies should be designed to increase significantly the employment rates of those who have traditionally been disadvantaged in the labour market: the young and the old, the disabled, certain ethnic groups, and those with no or only low level qualifications. Industrial policies should be unashamedly focused on supporting exporters and potential exporters and on helping the private sector to respond to the effects of globalisation and technological change, in particular in the regions. And there should be a greater role for alternatives to shareholder capitalism, in the form of mutuals and cooperatives, so that employees have a greater say in the running of companies.

The Keynesian revolution heralded a different way of conducting fiscal policy in order to maintain low unemployment. It was also associated with nationalisation and a corporatist approach to the economy. The Anglo-liberal revolution involved a shift to using monetary policy to control inflation. It then introduced privatisation, liberalisation, deregulation and heavy reliance on the financial sector for growth, and under Labour governments combined these with tax and spend policies to redistribute the proceeds of growth. A third revolution, to replace Anglo-liberalism, is now needed and may

emerge over the next decade. It should involve another shift in the focus of macroeconomic policy, giving less weight to inflation and more to unemployment. There should also be a more active role for government in the economy. Rather than standing to one side and leaving the private sector to cope with deindustrialisation, Britain needs the government to work in collaboration with industry to produce more sustainable growth and a more equal sharing of increased prosperity.

Mobilising politically against Anglo-liberalism

Peter Taylor-Gooby, Professor of Social Policy at the University of Kent

Colin Hay's essay sets out a clear account of the economic crisis as a crisis of privatised Keynesianism, set in the context of the inherent instability of the Anglo-liberal 'privatised Keynesian' growth model, and triggered by the failure of the financial system to sustain the required level of borrowing. The cure is not resuscitation of this system, as the policies promoted by the Coalition and by the European Central Bank, IMF and the OECD imply, but its replacement with a growth model that rests on real production. This involves recognising that the crisis is not at root a crisis of debt, which needs to be squeezed out of the system by cutting spending and clearing space for a private sector led recovery, but a crisis inherent in a growth-model that depended to a considerable extent on consumption fuelled by debt. This leads to an alternative analysis that suggests a growth model in which the state leads investment in productive enterprises and in which deficit reduction plays a secondary role, to be achieved in line with real growth in the productive economy.

It is one thing to develop a better analysis of the crisis and its solution and another to generate a feasible strategy for securing electoral support so that the new policies can be implemented. The Coalition's approach is two-pronged: cuts to reduce the deficit, and a wholesale restructuring of virtually every aspect of the public sector. The restructuring is presented in terms of promoting competitiveness and cost-efficiencies and allowing a wider range of providers to contribute. The *Open Public Services White Paper* says: 'wherever possible, public services should be open to a range of providers' (Cabinet Office, 2011, 9). One effect of the reforms, intended or not, may be to create circumstances in which the cuts can be permanently embedded and in which the political climate of the UK can be shifted permanently in a neo-liberal direction (see Taylor-Gooby, 2013, for more detailed discussion of the evidence).

The restructuring programme is large. It includes competitive tendering with competition effectively on price across much of public services: the commissioning budget that makes up some two-thirds of NHS spending; most of social care services; large areas of local government provision, almost all the employment service; the prison service and in other areas. These reforms have the effect of undermining the social institutions which represented successful collectivism, notably the NHS and to some extent care services. The privatisations typically achieve savings by using non-unionised staff. The capacity of professionals to organise on their own behalf or on behalf of service users is weakened. Accountability for local services through local government is also damaged. Combined with this are major reforms to benefits which will have the effect of cutting

rates for those on low wages or in poor housing, and linking entitlement to job-seeking behaviour for the unemployed and many sick and disabled people.

These changes reinforce general tendencies towards a more liberal political climate in which it is the individual's own responsibility to seize such opportunities as are available and in which outcomes are seen more as a matter of individual blame or praise. They go hand in hand with acceptance of the rapid growth of inequality during the last three decades, in which the UK has moved from a European to a US pattern of income distribution. They follow the stigmatisation of the poor as work-shy, responsible for their own circumstances.

In this context liberal market solutions occupy the lead position as the natural framework within which most people think about public policy and citizenship and which sets parameters for political debate. New policy directions must defeat the neo-liberal account at an analytic level. They must also help build the institutions which will direct people's understanding of their social lives and interests towards collective solutions.

Current proposals developed on the left include:

- Greater transparency, so that the fact that 59 per cent of those in poverty live in working households and only one in eight of them are unemployed, replace the assumptions of welfare scrounging prevalent in the media and in political rhetoric; similarly the reality of inequality, the speed with which it has grown, and the low taxes and limited social contribution of many of the wealthy can be pressed home;
- Citizenship welfare, restructured to stress the contribution that individuals make as former or potential workers, as carers and as voluntary workers (Horton and Gregory, 2009);
- The importance of investment not only through the kind of public investment into productive industry that is stressed by the critique of the Anglo-liberal model, but in social investment which would put resources into such areas as childcare that releases mothers for paid work, training to enhance productivity, and care for older people, where there is evidence that properly designed programmes can generate a real return to society in growth and to the Treasury in taxation and benefits saved (Ben-Galim, 2011; Pickard, 2012);
- Recognition of the importance of adequate wages, through the Living Wage programme and making the case for 'predistribution' (Pennycook, 2012).

Putting new ideas into practice requires the identification of a social force that will push through the necessary changes. One possibility in the struggle against Anglo-liberalism is the emerging politics of New Social Risks. The institutions of traditional social democracy were shaped by the class struggles of post-war industrialism and included state intervention to meet the needs that male workers could not address through trade union politics, their own market incomes, and the dependent unwaged labour of women in families as wives and mothers – health care, pensions and education. These remain the core services of modern welfare states and are highly popular.

The transition to post-industrialism and the decline of the family-wage manufacturing sector, the greater instability of working lives, the normalisation of paid work for

women, and the further pressures of globalisation lead to the emergence of New Social Risks. These concern access to adequate care services (child and elder care) to substitute for informal labour; training and retraining that will help people get into the labour market and maintain a position; and decent wages and conditions of work in the face of global competition. New Social Risks impact on people's lives across a range of social classes and across gender, ethnic, and regional divides. The new insecurities and the capacity of the state as the only agency capable of addressing them may form the basis for a new post-industrial collectivism. It is only by reforms that build such collectivism that the political support necessarily for a decisive break with the Anglo-liberal tradition can be developed. This requires determination and political leadership.

There is no silver bullet

Hopi Sen, writer and blogger at www.hopisen.com

First questions

Colin Hay poses a provocative series of questions. To what extent is there a 'decidedly and distinctive Anglo-Liberal' conception of capitalism, and if there is, is this model 'complicit and culpable' in our recent economic travails? If the answer to these questions is yes, then what can be done about it? Hay argues that only by recognising the extent of the systemic flaws in the 'Anglo-Liberal' growth model can we come to terms with the full extent of what is broken and understand what can be fixed.

Oddly, I dissent entirely from the diagnosis, which seems to seek to fit the facts rather uncomfortably and unconvincingly to the theory, but largely agree with the proposed cures, which represent a theoretical coming to terms with the practical limitations faced by governments in the face of larger tides than mere ideological will, and displays a sympathy for the difficult future which is rather absent from his analysis of the easy past.

Naming of parts

What exactly is the 'excessively liberalised Anglo-American form of capitalism'? Hay sets out a nine-fold definition: assertive neo-liberalism; an elite policy community; deregulation and privatisation; dependence on cheap fuel; debt; risk; the absence of 'a coherent theory of society' (incoherent theories of society presumably being plentiful); the embedding of inequalities; and a limited view of global governance. He then argues that these characteristics were pursued in their purest form in the USA and UK.

My first objection is to the absence of other anglophone countries from the 'Anglo-liberal' model. What do Canada, Australia, and New Zealand have to do to get our attention? If any country embraced 'Anglo-liberalism' with true passion, it was New Zealand, while the Canadian and Australian governments broadly pursued the same agenda as their British and American colleagues, but with subtle and important differences. That none of these culturally 'anglo' and economically 'liberal' economies are stranded in the growthless 'recovery' Britain and the eurozone are enduring might

suggest that an 'Anglo-liberal model' is neither as definitively broken nor as clearly defined as it first seems.

If the proposed definition is not so much culturally 'anglo' and more ideologically 'liberal', I confess I don't fully understand from the nine points what uniquely sets the 'Anglo-liberal model' apart from other global, and specifically European, economies. Was the price of oil more economically significant to Ireland than Italy? Are the products of the French *grandes écoles* more or less elitist than those of Oxbridge? Did mortgage debt rise as a share of income faster in America than in Sweden? Is the theory of society less coherent in Australia than China?

Further, it's not at all clear that the model of Anglo-liberal governments exporting their orthodoxy (or spreading the contagion) to European countries is the whole story. When it comes to financial sector liberalisation, for example, Germany's financial sector was more liberal in the early seventies than that of either the US or Britain (see Williamson and Mahar, 1998). Who exactly was following who? More recently, If New Labour's 'orthodox neo-monetarist' decision to hand operational independence to the Bank of England in 1997 was Anglo-liberal in character, what should we say about the Bundesbank, or the independence of the French central bank in 1994?

It's not all about us

This may seem petty, but defining what precisely represents a 'decided and distinctive' Anglo-liberal model becomes important when deciding to what extent this model is broken. Perhaps one way to do this would be to develop a scoring system to identify Anglo-liberalism. We could begin by examining the methods of the most enthusiastic free market champions. Who do the neo-liberals themselves praise? Each year, America's Heritage Foundation produces an 'Index of Economic Freedom'. 'Anglo-liberal' countries regularly come close to the top, including Australia, New Zealand, Ireland, Canada, the US and Great Britain. So perhaps there is an 'Anglo-liberal' model. However, the anglophone countries are usually rated below small open trading economies like Hong Kong, Singapore and Switzerland, and moreover are bunched closely with such welfare state economies as Sweden, Denmark, the Netherlands, and Finland. A similar ranking is produced by the Fraser Institute. If Sweden is almost as neo-liberal as Hong Kong, then perhaps the definition needs more work!

These models have several flaws, but even granting Hay's theory of Anglo-American particularism, it's not clear whether the Anglo-liberal economies were the most egregious offenders against sound policy in the boom years. As Hay notes, in the years to 2007, America's ratio of residential mortgage debt to GDP increased by less than almost every other major economy, while Britain's increase in outstanding household debt was on a par with the Netherlands and Finland, and our increase in house prices was similar to France. If the Anglo-liberal economies were culpable, then so was almost everyone else.

An alternative explanation might be that for the decade after the creation of the euro (and the end of the communist East), Europe saw a radical reduction in the cost of borrowing in the European periphery compared to the core, leading to a surge in debt and housing investment in countries as varied as Estonia, Latvia, Lithuania, Hungary, Ireland, Spain, Italy and Portugal. The extent to which private debt increased in these

countries was directly related to the increased 'gain' from falling interest rates and expectations for future growth (Higgins and Klitgaard, 2011).

Arguably, the exposure of the Baltic, central European and periphery nations to a seizing of financial markets was less a result of Anglo-liberal contagion and more due to a European boom, which had precious little to do with Anglo-anything. If there was 'house price Keynesianism', it was more a result of the euro than Anglo-liberalism.

Alongside this, and at the same time, Western economies generally enjoyed a decade of low inflation and low interest rates, driven by a combination of structural and supply-side reforms, manageable fuel costs, technological and productivity advances, and so on. This model explains the idea of the 'NICE' (non-inflationary consistently expansionary) decade.

Under this model, the obvious German exceptionalism becomes less an expression of Teutonic restraint versus Anglo-Saxon freedom and more a result of the interplay of complex economic factors. After all, if euro-integration meant lower interest rates for the periphery, it also meant a change in Germany's economic relationship with the periphery.

How then to explain the eventual bust? I agree with Hay's account of a combination of low interest rates for an extended period, leading to a boom in property hot-spots, the worst risks of which were disguised by the increasingly complex underpinnings of an emerging global financial system. As Hay describes, when interest rate increases hit the US residential property market, the players in this market, who were found all around the West, found they didn't know what cards they were holding, what they were worth, or who was going to get landed with the Queen of Spades.

The limits of politics

Whether Anglo-liberal or not, Hay suggests the fault lies not in the regulation and management of the system, but in the decisions by 'Anglo-liberal' empowered central bankers to hold interest rates low across the late nineties and noughties. If this is right, it becomes important to explain how a different, more political, system would have delivered a better outcome.

British history, at least, is not helpful here. Under both Barber and Lawson, interest rates were used to stoke a boom, which then had to have the brakes applied harshly when inflationary pressures got out of hand. Even under the 'Ken and Eddie' show, the politician was consistently the voice for lower interest rates. Labour's record was not much better, though Labour Chancellors tended to confront balance of payments and devaluation crises.

In Britain, the evidence is not that politicians would have pushed virtuously for increased interest rates. Instead, they may even have held them lower when politically convenient then pushed them up rapidly in response to the crisis, provoking the sort of tipping point 'boom and bust' crisis we'd seen so often before.

But what if interest rates had been higher? Last year, in his, perhaps self-justificatory, reflection on the crisis, Mervyn King imagined what the British economy would have looked like if the Bank of England had increased interest rates during his tenure at the Bank, in an attempt to restrain asset price inflation. He argued that the view of the

majority of the MPC was consistently that 'higher interest rates would have moderated domestic credit growth and asset prices, but only at the expense of slower output growth, rising unemployment and a prolonged undershoot of the inflation target' (King, 2012). King's solution to this was increased leverage caps, macro-prudential regulation of the finance sector, and a greater willingness to undershoot inflation targets and lower short run output growth in order to avoid asset bubbles.

Worthwhile Canadian initiative

At this point, my analysis and Hay's, having diverged greatly, begin to converge once more. It's all horrendously complex. There may or may not be a big Anglo-liberal bad infecting everyone else. If there is, extricating yourself from such is awkward. If there isn't, one cannot simply resolve the problem by no longer being so foolishly anglo, or idiotically liberal. So where did we go wrong, and how can we put it right?

First, there is the question of how to deal with the possibility of asset price inflation due to sustained low interest rates. If it is possible to find a technical or regulatory solution to the very real issue of extended low interest rates leading to housing price bubbles in economies of all sorts, then perhaps it is here we should direct our attention. I confess I am left confused by Hay's advice here. On the one hand, he seems to be arguing that the error of the past was overly liberal financial services policies, which led to excessive willingness among banks to accept higher risk mortgage customers, turbo charging an unsustainable asset price boom whose continuing fragility remains a severe risk to the UK economy.

On the other hand he identifies 'a step-level increase in the cost of borrowing in Britain that has too often gone unnoticed', and seems to regard the high relative cost of mortgage borrowing while banks display (or are forced into displaying) risk aversion as a *bad thing* (Hay, 2013, 53). Yet on the same page, he argues that the Bank of England has overthrown its mandate by not increasing the base interest rates to squeeze inflation. As far as I can tell, the overall position seems to be that the Bank should increase base rates to squeeze out inflation, while at the same time banks should reduce their spreads to encourage consumer and commercial demand. These proposals seem to act against each other.

This perhaps highlights Hay's point that it is hard to find a non-complex solution to our relationship with mortgages and housing. One option might be to examine the rather more successful Anglo-liberal economies. Canada combines a classically liberal economy with low interest rates with much tougher conditions for mortgage lending and a greater provision of housing for rent, both of which have the effect of reducing exposure to housing price inflation in periods of extended low interest rates. The Canadian system regulates the loan to value level of a mortgage at 80 per cent, and expects that if a bank wishes to lend more than this level, it must seek insurance from the state or other private providers (Kiff, 2009).

This won't solve our current problem, but might help prevent a similar reoccurrence in future. It is, however, a regulatory and technical solution to a specific problem, rather than an assault on either linguistic tendencies or an economic ideology. Canada, after all, is mostly anglo and mostly economically liberal.

This isn't to say introducing such a system to the UK in the 1980s or 1990s would have been politically possible. I find it hard to picture a politician of any party deciding that it would be electorally useful or economically advisable to intervene in a growing economy in order to limit the availability of mortgages to working people on low to middle incomes. The Canadian system works, in part, because it is now organic, having been developed to meet housing needs after the Second World War. Grafting it onto another model may well be easier now, when there is limited mortgage availability anyway, than when it would have represented the state stepping in to crush people's dreams of home-ownership.

Next, Hay suggests a gradual shift from private to public investment, or rather, an increase in public investment alongside and supporting an increase in private investment in targeted areas of commercial activity. Here I have great sympathy with his case. It is clear that current borrowing is cheap, and it would be relatively simple to finance extra infrastructure investment, especially if future income streams were identified to support such activity, while measures like an industrial bank, loan insurance, support for innovation and R&D spending will all help encourage private investment.

I also agree with Hay on the value of 'a far more selective and strategic channeling of the supply of credit ... into new sources of growth (in manufacturing and services). That entails ... a focused assault on interest rate spreads in areas identified as targets for investment in the new growth model' (Hay, 2013, 60), though I see the most effective mechanism for this less as a political assault on lenders and more as the creation of an institutional framework of lenders, risk insurance, and innovation investment that will reduce the effective risk, cost and difficulty for borrowers in key growth areas. (Think Sparkassen, the US SBIR, KfW reinsurance, and so on).

These measures, however, cost money, and while in the short-term they could be supported by borrowing, as growth returns the Keynesian counter-cyclicity that works for state expansion at the moment begins to call for steady deficit reduction and eventual debt repayment. Hay's call for conditional deficit reduction is sensible and right, and follows the steps made by governments like Chile and Sweden in setting up robust fiscal institutions to police the sort of rule he discusses. However, this will mean significant pain elsewhere, and the left will need to come to terms with this.

Further, while I agree with Hay that international co-ordination of deficit strategy is vital (I'd add a revenue strategy too; the continuing failure to develop a common European corporation tax regime being one obvious example – see Lannoo, 2013 for the long and boring history of this effort), we should not be starry-eyed about what this would produce. As a nation on the edge of Europe, the obvious co-ordination would be with European policy, and I am unsure if this would be an improvement even on the current administration!

Eventually, though, growth will return at a non-negligible level. At that point a combination of the need for Keynesian counter-cyclical deficit reduction and the long-term fiscal pressures on the state mean it will be exceedingly difficult to provide extra industrial and investment incentives over a sustained period without a strategic withdrawal by the state elsewhere or a substantial increase in taxation revenue, or both. (The OBR currently projects that if policy is unchanged, debt as a share of GDP will not fall below 60 per cent before rising again).

In the short-term, creating the space to invest might involve front loading industrial or capital programmes from future tax increases for pensioners and savings on welfare, as the Social Market Foundation have proposed (Mulheim, 2012). However, a short-term policy will not be enough. A long-term shift toward public and industrial investment might require a policy of limited pay and employment increases in the public sector, real terms reductions in services budgets, increased co-payment for services, welfare conditionality and broad-based tax increases.

As you might guess, this is not an agenda politicians are likely to embrace with delight unless they feel there is either no alternative or a public willingness to take unpleasant medicine. On the left especially, such a programme would need to be clearly couched in terms of creating employment, raising skills and earning capacity, and lifting incomes for the many.

So what can we on the left do? For me, one useful step would be to abjure entirely the idea of a single, dramatic intervention. The economy is weak, our resources are limited, and the situation is fragile. To get to a better place requires a step by step, gradual reform of institutions, policies and regulations that will eventually take us to a better place, one that will, in many ways look a lot like Britain does now, just as Canada, Australia and New Zealand feel instinctively familiar, but will at the same time feel very different.

The other useful role we on the left can play is to re-accustom ourselves to the idea of shared sacrifice. The changes we need to make will not be easy, or straightforward. They will involve pain and dismay and the abandonment of treasured salients for a more defensible line from which to advance. This will be especially difficult for those of us who see the value in social spending, in the active state, and the fair distribution of reward.

However, the final lesson of history is that if the left is unwilling to undertake painful but needed structural reform, the right will eventually do so in a far more harmful and divisive way. So the task falls to us, and it is vital we do not avoid it in favour of either hunting phantom villains or sketching idealised utopias that can never come to pass. It is in these last points, and on the value of wrestling with the world as it is, that Hay leaves us with the strongest of his insights.

Getting Anglo-liberal capitalism right... and putting its pathologies right

Colin Hay, Professor of Politics at the University of Sheffield and Sciences Po, Paris

I should start by thanking Ben Jackson and *Renewal* for first proposing and then organising and hosting this debate on my little book, *The Failure of Anglo-Liberal Capitalism*. Whatever one thinks about the content and analysis I offer, the debate is a crucial one to have – and this is a vital time to be having it. That said, my interest in this debate is of course not simply that these issues and, more specifically, my ideas about the failure of Anglo-liberal capitalism, are discussed. So I am both relieved and delighted to find so much common ground with such a distinguished and influential group of commentators. And that relief and delight is as much political as it is intellectual – for it is only if, as and when we can agree on what is broken that we can start to put it right. That, in the end, is what counts.

While there is much common ground between us, the four contributions are in fact very different in character from one another. Peter Taylor-Gooby builds from many of the same premises to extend the analysis I present in *The Failure of Anglo-Liberal Capitalism* to consider, quite rightly, how a wider political coalition might be built for the kind of alternative growth model I propose (and that we are both committed to). Tony Dolphin also extends the analysis of the book, examining in a little more detail the implications for the balance between inflation and unemployment in monetary policy and how the long-term structural weakness of the manufacturing sector might be addressed in building a more sustainable and export-oriented growth model. Hopi Sen and Nicola Smith are ostensibly more critical. Though accepting the case for many of the substantive policy reforms I propose, the former takes issue with my attempt to characterise the contemporary British political and economic affliction as a crisis of a specifically 'Anglo-liberal' growth model. The latter seeks to identify a number of issues which she sees as slipping too easily through the net of my analysis, suggesting how each might give a subtly different inflection to the general case for reform that I present. In what follows I seek to respond briefly to each in turn, perhaps inevitably concentrating a little more on the more critical engagements of Sen and Smith in the hope of clarifying some ambiguities, resolving some misinterpretations, and establishing what, if anything, still divides us.

Peter Taylor-Gooby: combining a new growth model with a new social model

Peter Taylor-Gooby is (characteristically) generous in accepting: (i) my characterisation of the crisis as one of a 'privatised Keynesian' or 'Anglo-liberal' growth model based on consumption fuelled by credit; (ii) the need for a new alternative growth model that can deliver a steady and stable supply of credit to growth- and job-creating sectors; and (iii) the need to relegate deficit reduction to a secondary role – something to be achieved with (a portion of) the proceeds of growth, not itself a condition of economic good health or growth (and certainly not a priority trumping growth).

His concern, quite appropriately, is with the building of popular support for such a new growth model and his anxiety is that, in the absence of this, we are mired in a situation in which permanent austerity serves in effect to lock in and further institutionalise proposed and already achieved cuts in public services. This would indeed reinforce an already deeply embedded neo-liberalism which has developed hand-in-hand with an aggressively liberal political culture in which, as he rightly points out, individuals are increasingly seen to bear responsibility for the advantage they take from the limited opportunities available to them such that outcomes are 'a matter of individual blame or praise'. This, he suggests, characterises the emerging politics of new social risk. But it also provides opportunities for a social democratic alternative based on a return to a more collective view of how such risks might be managed more collectively (see also Taylor-Gooby, 2013).

There is very little here with which I disagree. Taylor-Gooby's analysis, though in no sense a direct implication of the account of the crisis I offer, is deeply compatible with it and, indeed, builds upon it. It addresses a supremely important set of concerns about the political conditions of existence of the transition to the kind of new growth model

that I propose and it reminds us, in a most timely manner, that the left does not merely have to win the *economic* battle of ideas if it is to have the chance to preside over that transition. And, above all, it shows us how a new economic growth model can and must be aligned with a new social model if it is to prove politically sustainable.

Given that we agree on so much, I confine myself merely to one point, by way of an observation and a warning. What concerns me is that the Labour opposition (the most obvious and perhaps the only possible carrier of such a new growth and new social model) is in danger, even at this point, of precluding such a transition. For if, as now seems likely, it enters the 2015 General Election campaign committed to the (presumably) outgoing Coalition's spending commitments for even the first two years of its parliamentary term, then it will be Labour, rather than the Coalition, that will preside over the much-vaunted but still largely deferred public austerity we have been threatened with for so long. That would, of course, be a most tragic irony.

Tony Dolphin: 'you can't cut your way out of a growth crisis'

Like Peter Taylor-Gooby, Tony Dolphin very generously couches his important intervention in this debate in terms consistent with and familiar from *The Failure of Anglo-Liberal Capitalism*. As such, we too agree on a very great deal here. The old, broken, economic model – Anglo-liberalism – he argues remains strangely unthreatened by the crisis. Though it is (in the absence of the growth on which it relied) hardly in the rudest of health, it nonetheless remains in place. The reasons for this are three-fold. First, paradigm shifts are exceedingly rare; there have only been two in the entire post-war period. Second, neither the Coalition nor Labour has advocated a coherent alternative to Anglo-liberalism, with both confining their thoughts on how to respond to the crisis to the parameters of the existing paradigm. And, third, this has been reinforced by the framing of the crisis as one of debt, not of growth.

As he crisply points out, platitudes such as 'you can't borrow your way out of a recession' may well be very poor economics, but they remain strongly resonant – and they continue to exert a powerful hold over public opinion. But I think he is also right to suggest that this is at least in part because there has been far too little attempt to find an alternative, equally compelling, public narrative based on rather better economic thinking. The mantra he offers, a truism of at least progressive economics, strikes me as an excellent starting point: 'you cannot cut your way out of a growth crisis'.

Dolphin goes on by developing an analysis again consistent with my own but by no means confined by it, to argue that Labour must now accept its own culpability, in office, for both the build-up of unsustainable private (consumer, commercial and financial) debt and for the increasing dependence of growth upon it. It is not difficult to understand why it might be reluctant to make such a public concession. But it needs to show that it understands the nature of the crisis if it is credibly to commit to its resolution, even if that means casting a retrospective shadow over its economic tenure since 1997.

This brings us to the crux of Dolphin's powerfully compelling argument in his demonstration of the need for a sustained attack on the deficiencies of the Anglo-liberal model of capitalism which long pre-date the crisis. As he so correctly points out, the

most eloquent case for an alternative is the palpable failure of the Coalition to deliver the much vaunted rebalancing of the domestic economy we were promised: and this despite a near 25 per cent devaluation of the currency and the associated stimulus to export markets. What this reveals, as he again makes clear, is that, under consecutive administrations, 'Britain's industrial base was allowed to shrink to the point that it no longer has the capacity to compete effectively, even when given a big boost to its competitiveness'. The effect has been that, in its ever more anxious and frenetic attempt to find some growth before the election, the Coalition has found itself resorting to the pump priming of mortgage-debt. This, it need hardly be pointed out, is a most desperate and dangerous move – with lots of downstream risk and very little, if any, substantive gain to date or in prospect. This is privatised Keynesianism mark II.

So what can be done? Here, again, we are in complete agreement. Dolphin draws out five key implications of what is, in effect, a shared analysis: (i) that unemployment be given an equal footing with inflation management in a revised mandate for the Bank of England – and that this be backed by appropriate labour-market reforms to promote improved access to employment for the most socially and economically marginalised; (ii) that house building replace demand-stimulation targeted on the mortgage market; (iii) that we regulate the financial sector in such a way as to prevent the crowding out of credit and investment by bank recapitalisation; (iv) that we pursue, clearly, unapologetically and explicitly, an export-oriented industrial policy; and (v) that we promote mutualisation and re-mutualisation as a popular alternative to shareholder capitalism.

Hopi Sen: what's Anglo and what's liberal about Anglo-liberal capitalism?

Of the four commentaries, Hopi Sen's is by far the most difficult to respond to. As a response, it is the most extensive and perhaps the most detailed and its charge-sheet (if I can call it that) is certainly the longest. And, on the surface, it would appear as though we disagree about quite a lot. That said, appearances can be deceptive – and to some extent they may well be so here. Sen argues that whilst I largely get the solution to the crisis right, I do so whilst getting the analysis of the underlying affliction wrong – since this is not, for him, a crisis of 'Anglo-liberal' capitalism in any meaningful sense. I could, of course, console myself with the thought that it is far better to agree on what needs to be done and to disagree on why than the converse. But I suspect there is more to this than that. Indeed, I hope to show briefly in what follows that much, though by no means all, of the ostensible difference between us is semantic rather than substantive.

His comments remind me, in a way, that small books are dangerous things – they can focus the mind (hopefully of the reader as much as the author), but they also tend to be characterised by the kind of simplifying devices and tropes which might not be tolerated in a more extended discussion of the same topic. In part, then, his challenge might be seen as a posing of the question of how far I can go and how far I am prepared to go in defending one such simplifying trope – the concept of Anglo-liberal capitalism.

The crux of the case against *The Failure of Anglo-Liberal Capitalism* that he presents is that this can't really be a crisis of Anglo-liberalism since other self-evidently Anglo-liberal cases – notably Australia (where I sit as I write this), New Zealand and

Canada – have not suffered Britain’s fate. This is an interesting and penetrating observation and there would seem, on the face of it, to be something to it. But it is far from unproblematic. A number of points might (briefly) be made.

First, *The Failure of Anglo-Liberal Capitalism* is part of a wider argument, set out in its fullest form in *The Political Economy of European Welfare Capitalism* (Hay and Wincott, 2012) and in a series of comparative articles (Hay and Smith 2013a, 2013b) about the nature of the crisis. Thus, the labelling of this as an ‘Anglo-liberal’ crisis is, in fact, a comparative claim – just one not set out so clearly as such in the (little) book in question, with its more limited focus on the British case. Second, and rather more significantly, in that wider argument ‘Anglo-liberalism’ is not solely an attribute of country cases which are both ‘Anglo’ and ‘liberal’, but rather (as in much of the wider comparative political economy literature) a label or marker for a series of policy dispositions (as Sen himself concedes at the start of his response). Thus, Anglo-liberalising tendencies have been present, even prevalent, in a number of European and other political economies at various points in time since the 1980s – and there are invariably counter-tendencies to them, even in obviously ‘Anglo-liberal’ cases such as Britain or Ireland.

The argument that I was seeking to make, then, is not that we should expect to see evidence of the same pathologies in all political economies in which economic liberalism is ascendant and English is the principal language – there is no expectation here that Australia or Canada should inevitably suffer Britain’s fate; nor that France or Spain should escape it. No, the argument is rather different; though it is clearly one that Hopi Sen has missed (despite my attempts to be very clear about it in the text). Let me restate it as simply as I can. It is that, at each and every significant point in the establishment of the economic and political preconditions of Britain’s unsustainable growth model, the core decisions made reveal a profound Anglo-liberal market disposition. This is as true of Ireland as it is of Britain, and I suspect it is true of the eurozone too.

And what of Canada, Australia and New Zealand? Well, my argument here is also relatively straight forward. In a way, Canada’s good fortune was that its Anglo-liberalism had not gone (quite) so far (by the onset of the crisis) as to unleash the ultimately unsustainable ‘privatised Keynesian’ growth dynamic that I detect in, say, the Irish or British cases. That said, there is a certain irony here – in that much of the (Anglo-liberal) financial and mortgage-market deregulation which would have made this possible was in the process of being implemented as the crisis hit. Canada was spared, in effect, by ‘late-onset’ Anglo-liberalisation. The Australian and New Zealand cases are rather different – for they, too, inflated potentially unsustainable housing and asset-price bubbles in their economies in a typically ‘Anglo-liberal’ vein, but they did so on the back of, and whilst enjoying the proceeds of, a rather more complex growth model – in which exports of raw materials to China and East Asia played, as they continue to play, a crucial role. In short, these economies were spared the crisis (despite their Anglo-liberalism) by their parasitism on Chinese growth. This, I hope, goes some way both to explaining my continued use of the term ‘Anglo-liberal’ here and to defending my characterisation of this as, at heart, a profoundly ‘Anglo-liberal’ crisis.

In a sense, our other ostensible disagreements are quite modest and can hopefully be dealt with more briefly still. There are essentially two of these. The first is that, according to Sen’s reading of my argument, I would have liked to see the Bank of

England respond in a manner more consistent with its formal mandate before the crisis (and particularly from 2006) in continuing to raise interest rates to control inflation (including house-price inflation). This, Sen contends (echoing Mervyn King), might well have led to less of an asset-price bubble, but would also have produced slower growth, rising unemployment, and ultimately the prospect of a prolonged undershoot in the inflation target.

In fact I agree with almost all of this. My point is not that the Bank of England behaved irresponsibly, but that, given the unsustainable growth model Britain had at the time, it had little choice but to continue to inflate the bubble until it burst (ignoring its formal mandate in the process). The problem was not the conduct of the Monetary Policy Committee, nor even the Bank's remit, but the inherent unsustainability of the growth model itself.

Finally, Sen suggests that my views on current interest rate spreads and contemporary monetary policy are contradictory, in that I argue for concerted downward pressure on commercial and consumer interest rate spreads (which would reduce the cost of borrowing) whilst at the same time suggesting that the government and Bank are being irresponsible in seeking to pump-prime the mortgage market. In fact there is no contradiction here. My point is again a simple one, though one intended to reveal something of a paradox. The point is that an unprecedentedly low base rate does not, in and of itself, deliver low borrowing costs at a time when the banks are recapitalising – and using consumer and commercial interest rate spreads to do so. This is bad for growth in the short to medium-term, regardless of whether that growth takes the form of a (dangerous) resuscitation of the old growth model (to which I am opposed) or the move, through the more targeted supply of credit, to a new growth model (which I favour). But, as I see it, there is no contradiction in advocating concerted political pressure (from the government and the Bank) on the banks to reduce their interest rate spreads.

This may still make it sound as though we disagree about quite a lot. But I think that is wrong. For I find myself in almost total agreement with Sen's conclusions. I agree whole-heartedly with the need to think of the transition to a new and alternative model of growth in terms of gradualism, even incrementalism. That said, it is vitally important that we retain throughout this process a clear sense of purpose, of where we are and where we need to be headed. I agree, too, that we need to prepare ourselves for the pain we must endure if we are to make that kind of transition. And finally, I agree that in being prepared to endure that pain we should be bolstered by the certain knowledge that if this not achieved in a socially conscious and collectively just manner something far, far worse – in terms of both economic performance and social equity is likely to befall us.

Nicola Smith: putting what went wrong right

Nicola Smith's careful and perceptive commentary also raises a series of important points. Her intervention is perhaps closest to that of Tony Dolphin, in that it proceeds largely from a shared diagnosis of Britain's current political and economic affliction and how we got here. I agree with very much of it – even on a number of points where, I suspect, she sees more of a difference between us.

She presents essentially six objections to aspects of the argument I present or the political implications I draw from it. I will attempt to deal with each in turn. First, she suggests that I give insufficient emphasis to the structural imbalance in the economy, particularly that between a bloated financial services sector and the rest. She points out, quite rightly, that high leverage, short-term funding and limited regulation, combined with the sheer size of the sector, exacerbated Britain's exposure to the crisis. In fact I agree with all of this and that it is not crystal clear from the book that I wrote is a presentational error on my part – for that is certainly how I see it. Again, these points are perhaps more clearly made in the kind of comparative context I set out with Daniel Wincott in *The Political Economy of European Welfare Capitalism* (2012), but I would hope that they are at least implicit in *The Failure of Anglo-Liberal Capitalism*.

Her second point is of a similar kind, namely that I give insufficient attention to the impact of the crisis in the banking sector on business lending. Again, insofar as this is a warranted criticism, I accept it. I had certainly hoped to make this point more clearly. In a way, it is difficult to make too much of it, as it is terribly, terribly important. Indeed, this is precisely why a targeted assault on interest rate spreads on commercial lending (particularly where such lending might contribute to building export-market share generating capacity) is so high on my list of necessary reforms. Once again, we are in almost complete agreement.

A third point is, in a sense, a further implication of the argument I present – and, again, one I would accept without reservation. Smith points to the potential fragility of the kind of recovery that we might well be experiencing at the moment – and she is right to do so. For if growth returns to the US economy and if, as today, growth is higher in the US than in Britain, there is a grave danger that it will fuel (quite literally) an increase in the demand for oil and escalate oil prices (denominated in dollars) at the same time as the dollar strengthens against sterling. This, of course, can only prove inflationary and hence a likely source of interest rate rises which are bound to threaten those already struggling to service interest-only mortgage debt. As this suggests, house price deflation is never far off and, ironically, it might well be precipitated by the partial recovery of the US economy that may already be underway.

A fourth point is crucial – and a very welcome further development of the argument I make. It is one that I have referred to before, but it is one that arguably should have featured more prominently in *The Failure of Anglo-Liberal Capitalism*. It is that another key determinant of the appeal of the Anglo-liberal growth model has been stagnating household income and declining real wages. This I think is a very important point and one that is arguably central to explaining the appeal to so many households of placing one's financial eggs in the housing market basket in the hope of fuelling consumption (immediate or deferred) through assumed equity release.

Thus far we are in near complete agreement. But on the final two points we part company at least a little. The first of these issues concerns asset-based welfare and the extent to which the governments of Blair and Brown sought, quite consciously, to stoke house-price inflation and other forms of asset-appreciation as a means of compensating workers for stagnant wages and growing and projected welfare residualism (even whilst welfare spending was growing). Smith suggests that the evidence for this is not especially compelling; I must confess that I remain unconvinced. Whilst I think she is right to

point to the real improvement in the incomes of families with children, and the role of tax credits, for instance, in this, I simply do not see this as a reason for refuting the idea that Labour in office had, from around 2000, a conscious strategy for promoting asset-based welfare. I see these as separate, not related, claims.

Finally, and perhaps most significantly, there remains some (blue, red or green) water between us on the question of financial market re-regulation. But the question here is one of political strategy, rather than a more substantive disagreement about the pathologies of the British financial sector. My concern (in the passages she sees as too soft on financial market actors) was that we should not be distracted from the significant task at hand by indulging ourselves in a frenzy of 'banker bashing' to the exclusion of other more important reforms. However cathartic, the targeting of bankers and the bonus culture they have indulged is no solution to our problems. That said, and if only out of a sense of responsibility for the damage inflicted by the model of capitalism we have built and the global contagion of the crisis it has spawned, we do need a profound re-regulation of our banking sector – on that there is no dispute. But we need to proceed with some caution. For a rapid assault on the banking sector is actually likely to make the return to growth a more difficult proposition in the short- to medium-term and that perhaps suggests that we have to proceed with more deftness and more incrementally than we might wish. In a manner analogous to the idea that we make deficit reduction and ultimately debt repayment conditional on growth, we should perhaps think of domestic financial market reform and re-regulation as conditional on the slow weaning of ourselves off our old unsustainable growth model. As this suggests, we agree on where we need to get to and we agree, I think, that it can only take a long time. My point is simply that in our understandable eagerness to put in place the basis for a longer-term and more sustainable growth model we don't rush headlong into those parts of the necessary reforms that might most hinder the short-term prospects of a partial economic recovery on which we can build.

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