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The Strange Survival of 'Embedded Liberalism': National Economic Management and Globalization in Britain from 1944

Abstract

This article examines the fate of national economic management in Britain in the face of the growing economic international interdependence, which initially grew in the context of the 'Bretton Woods institutions', and continued apace up until the crisis of 2007–8. It frames the argument with the concept of 'Embedded Liberalism', which allows to examine in detail the evolution of key elements of the Bretton Woods settlement, their subsequent development, and how far these shifts led to a 'race to the bottom' in national policies. On the basis of arguments about the continuing viability of national economic management, it questions how far we should accept a story of 'the short life of social democracy' as a wholly accurate account of Britain since the 1970s.

Recent wide-ranging discussions of possible narratives of modern British history have re-emphasized the need to integrate the 'national story' with understandings of how Britain was always both affecting and affected by

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diverse international and global forces.[1] This article approaches this problem for Britain since the 1940s, by examining the interplay between the drive to national economic management operating simultaneously with a renewed commitment to internationalization of the economy.

At the close of the Second World War two major forces were at work in framing the post-war period in Britain, both extensively documented in the historiography. The first drive was towards domestic social and economic reform, embedded in national management of the economy, built on war time policies and instruments, and focussed above all on the delivery of full employment in an industrial economy.[2]

Second was the construction of a new architecture of international economic co-operation, leading in particular to the setting-up of the 'Bretton Woods institutions', the IMF, the World Bank and the GATT, dedicated, albeit in qualified fashion, to the creation of greater economic interdependence between nations.[3]

This article examines the fate of national economic management in the face of the growing economic international interdependence, which initially grew in the context of the 'Bretton Woods institutions', and continued apace up until the crisis of 2007–8. It argues that, contrary to much of the literature on 'globalization', national states like Britain have retained considerable capacity to manage their economies, despite major shifts in the international and domestic environment.[4]

The key term 'embedded liberalism', used as a starting point for this essay was coined by the political scientist John Ruggie. Ruggie's terminology derived in turn from Polanyi's *Great Transformation*, and in this framework 'embedded' emphasizes the reassertion of the social context of economic life, after the perceived loss of such embeddedness under the

[1] J. Vernon, 'The History of Britain is Dead; Long Live a Global History of Britain', *History Australia*, 13 (2016), 19–34; D. Edgerton, *The Rise and Fall of the British Nation. A Twentieth Century History* (London, 2018).

[2] P. Addison, *The Road to 1945* (revised edition, London, 1994) remains foundational; A. Cairncross, *Years of Recovery. British Economic Policy 1945-51* (London, 1985); R. Middleton, 'Economic Policy and Management', in R. Floud, J. Humphries and P. Johnson, eds., *The Cambridge Economic History of Modern Britain. Vol. II. 1870 to the Present* (Cambridge, 2014), 488–92. Specifically on the employment issue, see J. Tomlinson, *Employment Policy.The Crucial Years 1939-1955* (Oxford, 1987). On the centrality of industry, Edgerton, *The Rise and Fall*, 281–308.

[3] For a recent survey of this foundational moment, M. Daunton, 'Britain and Globalisation since 1850: III Creating the World of Bretton Woods, 1939-1958', *Transactions of the Royal Historical Society*, 18 (2008), 1–42.

[4] An important pioneer in making the case for the curtailment of state capacity by capital mobility was S. Strange, 'The Limits of Politics', *Government and Opposition* 30 (1995), 291–311. For other arguments, making similar claims from very different ideological viewpoints: J. Gray, *False Dawn: The Delusions of Global Capitalism* (London, 1998); M. Mann, 'Globalization after September 11', *New Left Review* 51 (2001), 51–73.

previous regime of the gold standard and free trade.[5] Ruggie used 'embedded liberalism' to summarize the regime that emerged from the two forces of the 1940s identified above. He defined this term to mean a 'form of multilateralism that is compatible with the requirements of domestic stability'. In this arrangement national governments would 'seek to encourage an international division of labour which, while multilateral in form and reflecting some notion of comparative advantage (and therefore gains from trade), also promised to minimize socially disruptive domestic adjustment costs . . ..' [6]

The discussion begins by summarizing the key elements of both sides of this combination. On one side, the debates over multilateralism, and their eventual institutionalization, especially in the IMF. On the other, the construction in Britain of national policies aimed at securing domestic economic stabilization. It goes on to look at how the world economy moved away from key features of the Bretton Woods model, followed by a discussion of how their demise affected the British capacity to manage their economy. This leads into a discussion of why, despite fears of a 'race to the bottom', growing international capital flows did not undermine the capacity of successive British governments to manage the economy. While 'race to the bottom' arguments can relate to a wide range of state actions, including, for example, labour and environmental regulation, here the focus is on taxation and fiscal capacity. This capacity relates especially to the possibilities of expanding social welfare spending, and conducting active fiscal policies in the face of recession. The final part draws some broad conclusions, drawing especially on arguments about the rise of neo-liberalism and the 'end of social democracy'.

The liberal international regime

The Bretton Woods agreement of 1944, which was at the heart of the new international economic regime, was largely an Anglo-American product, drawing heavily on a centrist liberal understanding of 'what went wrong' in the 1930s.[7] (Development issues, and questions of long term capital for the development of poor countries were not important for the IMF, but were partly addressed by the World Bank).[8] For key decision-makers the

[5] J. Ruggie, 'International Regimes, Transactions and Change: Embedded Liberalism in the Post-war Economic Order', *International Organization*, 36 (1982), 385–92: K. Polanyi, *The Great Transformation* (London, 1944).

[6] Ruggie, 'International Regimes', 399.

[7] B. Eichengreen, *Hall of Mirrors: The Great Depression, the Great Recession, and the Uses-and-Misuses of History* (Oxford, 2016); E. Heillener, 'A Bretton Woods Moment? The 2007-2008 Crisis and the Future of Global Finance', *International Affairs*, 86 (2010), 619–36.

[8] E. Helleiner, *Forgotten Foundations of Bretton Woods.International Development and the Making of the Postwar Order* (Ithaca: NY, 2014). A. Balasubramanian and S. Raghavan, 'Present at the Creation: India, the Global Economy, and the Bretton Woods Conference', *Journal of World History*, 29 (2018), 65–94.

1930s was seen as having been dominated by non-co-operative responses by the major industrial powers to external economic pressures, leading to most nations pursuing self-defeating policies of deflation, competitive devaluation and tariffs. Pressures on countries had manifested themselves especially through loss of export markets and/or capital flight, the second of these seen as resulting from the existence of the evocatively named 'hot money'.[9]

The literature on Bretton Woods is enormous and continuously expanding, though Keynes writings as a key participant in the proceedings remain crucial.[10] The arguments at the conference were multi-faceted and hard fought. Many have seen them as entrenching an American hegemony in the world economic system, built on the unparalleled relative economic strength of the USA as it ended the war.[11] But in the current context what matters is how the conference envisaged balancing the claims of national economic management and those of a revived multilateralism in international trade. The approach to this question, and what was eventually agreed is effectively summarized in the textbook trilemma (Fig. 1).

In this trilemma, countries seeking to manage their economies have to decide which of the two out of three aims indicated in the triangle–fixed exchange rates, free capital flows, and national monetary autonomy–they wish to pursue. Achieving all three is impossible, because free movement of capital will reflect different monetary conditions across countries, and the capital flows which follow these differences will make fixed rates impossible. At Bretton Woods the agreement was absolutely clear that it was the free flow of capital that would be sacrificed, allowing countries to combine monetary autonomy and fixed exchange rates (meaning the policy is captured by point C on the diagram). On capital flows the argument was pungently expressed by Keynes: 'In my view the whole management of the domestic economy depends upon being free to have the appropriate rate of interest without reference to rates prevailing elsewhere in the world. Capital control is a corollary to this.'[12] Fixed exchange rates were seen by most contemporaries as a necessary correction of the instability of

[9] Eichengreen, *Hall of Mirrors*.

[10] John Maynard Keynes, *Collected Writings vol XXVI Activities 1941-1946: Shaping the Post-War World. Bretton Woods* (London, 1971); R. Skidelsky, *John Maynard Keynes. Fighting for Britain 1937-1946* (London, 2000); B. Steil, *The Battle of Bretton Woods: John Maynard Keynes, Harry Dexter White, and the Making of a New World Order* (Princeton, NJ, 2013).

[11] C. Kindleberger, *The World in Depression, 1929-39* (Berkeley, CA: 1973), especially chapters 1 and 14. C. Newton, *The Global Economy 1944-2000: the Limits of Ideology* (London, 2004). For recent work emphasizing the *joint* responsibility of Britain and the USA for the post-war regime, see J. Green, *The Political Economy of the Special Relationship. Anglo-American Development from the Gold Standard to the Financial Crisis* (Princeton, 2020).

[12] Keynes, *Collected Writings* vol. 25, 149.

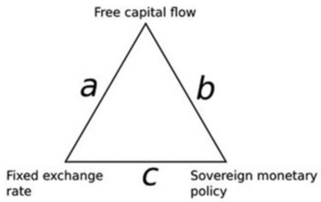

Figure 1.
The monetary trilemma.

such rates in the 1930s, believed to be a key feature of the overall economic instability of that decade.[13]

The basic aim of 'embedded liberalism', to reconcile a revived multilateralism with a large degree of autonomous national economic management, was very clearly at work at Bretton Woods. But the mechanisms put in place to achieve this aim have to be put firmly in a contingent, historical context. Fixed exchange rates and tight restrictions on 'short-term' capital movements made sense to those who looked back to the 1930s for much of their understanding of the problematic features of that 'failed decade', and hence what would have to be different in the future.

The domestic regime

The emergence of national economic management in Britain, can, like the Bretton Woods system, be usefully traced back to the end of the gold standard in the 1930s, specifically in Britain to 1931. As noted above, the origins of Bretton Woods were located in the failure of the 1930s to find a form of international economic co-operation to replace the gold standard, and the 'beggar my neighbour policies' that followed that failure. Conversely, the departure from gold opened-up a space for managing the national economy that adherence to that standard seriously inhibited. In the years after 1931 a managed exchange rate and discriminatory tariffs constructed a specific kind of national economic management, one aimed primarily at raising profits as the route to a private sector recovery.[14]

The management regime that emerged in the mid-1940s was very different from pre-war. Initially it relied a great deal on war-invented controls, on everything from consumer goods to investment to imports.[15] Slowly this regime gave way to a more macroeconomic focus, though many controls lasted well into the 1950s. The two decades that followed

[13] D. Irwin, *The Missing Bretton Woods Debate over Flexible Exchange Rates*, National Bureau of Economic Research WP 23037 (Washington DC, 2017).
[14] A. Booth, 'Britain in the 1930s: a Managed Economy?', *Economic History Review*, 40 (1987), 499–522.
[15] Cairncross, *The Years of Recovery*, 299–322.

were for Britain (and many other countries) a 'Golden Age' of economic stability-of full employment, low inflation and historically high levels of sustained growth.[16] This, of course, is a view from the perspective of the 'longue duree'—at the time, as is perhaps true of all eras, contemporaries saw themselves as living in a world of exceptionally rapid change and uncertainty, rather than one of stability. With the benefit of hindsight we can see that in *some* regards contemporaries were right: economic stability was certainly not the result of any kind of *stasis.* Very importantly, structural change in the economy, especially the rundown of the old 'staple' industries, many of them in the public sector, was exceptionally rapid: 'The generally high rate of expansion and pressure of demand made structural changes less conspicuous and less disturbing than they were in the inter-war period.'[17] In this period, enormous job losses in industries such as coal (where employment contraction peaked in the 1960s) were managed with a significant degree of regard for the prevention of economic and social hardship.[18]

Why was there a golden age? This used to be much argued about, especially the extent to which it was due to a new regime of 'Keynesian' economic policy-making.[19] The narrative of Keynes' ideas spreading from the academy to policy-makers, then being turned into policy aims and instruments, and this new policy regime happily yielding the prosperity of the 1950s and 1960s, is not one that in general convinces.[20] The classic Keynesian instrument of budgetary policy was conservatively used in these years, and the key driver of the post-war boom was private investment—though this investment may have been encouraged by the governmental commitment on employment.[21]

While budgetary policy was used only for 'fine-tuning' in this period, the size of the budget, and therefore its potential to affect the economy

16 M. Chick, *Changing Times. Economics, Policies and Resource Allocation in Britain since 1951* (Oxford, 2020), 2–3. As is well-known, growth was faster in continental Western Europe, especially because in those countries enormous numbers of workers shifted from agriculture into higher productivity jobs in industry, a process that largely occurred in Britain in the nineteenth century. This weaker growth performance, in combination with the unambiguous decline of Britain as great imperial power, led to the enormous literature of failure and economic 'decline'.

17 R. Matthews et al., *British Economic Growth 1956-1973* (Oxford, 1982), 255.

18 J. Phillips, 'Deindustrialization and the Moral Economy of the Scottish Coalfields, 1947 to1991', *International Labour and Working-Class History*, 84 (2013), 99–115; E. Gibbs, 'The Moral Economy of the Scottish Coalfields: Managing Deindustrialization under Nationalization c.1947-1983', *Enterprise and Society*, 19 (2018), 124–52.

19 N. Rollings, 'British Budgetary Policy 1945-1954: A 'Keynesian Revolution"?', *Economic History Review*, 41 (1988), 283–98; A. Booth, *British Economic Policy, 1931-49. Was there a Keynesian Revolution?* (Hemel Hempstead, 1989).

20 R. Lekachman, *The Age of Keynes. A Biographical Study* (New York,1966); M. Stewart, *Keynes and After* (Harmondsworth, 1972).

21 R.C.O. Matthews, 'Why Has Britain had Full Employment since the War?', *Economic Journal*, 78 (1968), 555–69.

was magnified (whether by deliberate action or the effects of automatic stabilizers). Public spending (and taxation levels) grew significantly, especially after the 'austerity welfare state' erected in the 1940s was extended from the early 1960s. But though this expansion is associated with the 'Keynesian' period, the direct link from Keynes' doctrine to state expansion was small. The big drivers of public expenditure growth were political calculation about, especially, the attractiveness of free health provision to voters across the social spectrum, and the parental demand for improved school and eventually university education.[22] Combined with a political commitment to mitigate the effects of deindustrialization, and promote growth, by industrial and regional policies, we can understand why the early 1960s to mid-1970s were to see public spending growth rates unequalled until the splurge of education and health spending of the early 2000s.[23]

In a characteristically astringent account, Alan Milward argued not only that Keynes' specific contribution to domestic policy-making was limited, but also that his ideas were strongly nationalistic, and it was happily the case that he had little influence on international trade policy.[24] More positively, he argued that the key to the post-war boom was the revival of (West) Germany as the key supplier of capital goods for the rest of Europe. In this view the 'Great European Boom' was crucially 'the greatest period of industrial growth in European history', and the 'culmination of western Europe's industrialisation'.[25]

Whatever the causes of the boom, plainly it was not prevented by the international economic regime. That regime only followed the blueprint laid out at Bretton Woods with considerable lags. Much expanded multilateral trade and free convertibility of currencies for current transactions were only achieved well into the 1950s. Fixed exchange rates and limits on short-term capital movements do not seem to have had the importance for the success of this regime envisaged in 1944. Exchange rates were fixed (within narrow bands) but the major effect of this was to put a constraint on inflationary policies, rather than prevent competitive devaluations in the style of the 1930s.[26] We cannot know the answer to the counterfactual question of how far capital controls in this period

[22] On the sustained popular support for the NHS: R. Lowe, *The Welfare State in Britain since 1945* (Basingstoke, 2005), 337–8. On education: P. Mandler, 'Educating the Nation I: Schools', *Transactions of the Royal Historical Society*, 24 (2014), 5–28; Mandler, *The Crisis of the Meritocracy. Britain's Transition to Mass Higher Education since the Second World War* (Oxford, 2020).

[23] See Figure 3 and discussion below.

[24] A. Milward, 'Keynes, Keynesianism and the International Economy', *Proceedings of the British Academy*, 105 (2000), 225–42.

[25] Milward, 'Keynes', 238.

[26] M. Daunton, 'Britain and Globalization since 1850. IV. The Creation of the Washington Consensus', *Transactions of the Royal Historical Society*, 19 (2009), 28.

prevented damaging 'hot money' flows from occurring, but given the underlying context of fast trade growth, low inflation and overall prosperity the likelihood of such flows was much reduced. In fact, such controls were never fully effective (a point returned to in the next section), and where they were evaded most spectacularly was the result of a *political* crisis (the Suez invasion), not the outcome of capital passing adverse judgement on a country's economic management in the classic fashion as occurred in Britain in 1931 or France in 1936–7.[27]

In an important sense national economic management 'had it easy' in the 1950s and 1960s. The structural changes that Milward identified went along with domestic political conditions which made deflationary responses to inflationary or balance of payments pressure much harder to for national governments to pursue, had they been so minded (and fixed exchange rates turned such pressures into a 'crisis'). By broadly encouraging multilateralism and the freeing of exchange controls Bretton Woods provided a benign environment for the operation of expansionary forces, but the specific contribution of fixed rates and (partially) controlled capital movements was arguably much less than the expectations of those involved in those negotiations in 1944 would lead us to believe. In that sense the events of the 1930s were not a useful guide to post-war conditions.[28]

The crises of the 1970s and the 'end of Bretton Woods'

The 1970s saw the 'end of Bretton Woods' in the straightforward sense that by the end of that decade floating exchange rates had become the international norm, and capital flows were on a clear (if not uninterrupted) trend to liberalization. These two changes were of course related, but the trajectory of change was by no means identical. In the case of exchange rates a core problem was that fixed rates, coupled with what was effectively a dollar exchange standard, greatly inhibited any change in the value of the dollar. When inflationary wars and domestic expansionism threatened the US balance of payments in the 1960s, a dollar devaluation was hard to engineer. The result was crisis, eventually resolved by a movement towards floating rates, which gathered pace from 1973 onwards, encouraged further by the inflationary and uneven effects of OPEC1, which left the original pattern of rates unsustainable. In the absence of an alternative grand design, policy on rates became highly *ad hoc*. Attempts at international agreement on the stabilization of rates

[27] J. Boughton, 'From Suez to Tequilla: the IMF as Crisis Manager', *Economic Journal*, 110 (2000), 273–91; P. Williamson, *National Crisis and National Government. British Politics, the Economy and Empire, 1926-1932* (Cambridge, 1992), 255–84; M. Kalecki, 'The Lesson of the Blum Experiment', *Economic Journal*, 48 (1938), 26–41.
[28] A. Milward,' Keynes', 239.

continued, as in the 1980s Plaza Accord, but there could be no return to the *status quo ante*.[29]

Apart from the peculiar, unintended consequences for America economic policy, the stability of rates had come under pressure more generally from the growth of capital movements, especially evident from the late 1960s, but with roots going back to the previous decade.

Why had capital mobility risen despite the unambiguous hostility expressed to such mobility in 1944? Part of the answer was intrinsic to the workings of the post-war international economy. Central to that economy was the rapid growth in trade that Bretton Woods had of course wanted to encourage. But such trade expansion necessarily meant that the distinction between foreign exchange transaction for trade purposes and those for investment purposes eroded. That such a distinction was not hard and fast was recognized in the 1940s, which was why comprehensive forms of exchange control were regarded as necessary to police the boundary. But such policing became harder and harder as with mounting volumes of trade the sums involved in 'leads and lags' in the payment patterns made distinguishing the motives for buying and selling foreign exchange much harder to determine.[30]

But beyond this unintended consequence of the success of Bretton Woods in encouraging trade, controls on capital movements declined because key national governments saw advantages to such a decline.[31] Both the USA and Britain, despite being key architects of the proposals for control, came to see easing capital movements as a policy favourable to their respective financial centres in New York and London. The process began in 1950s with rise of Euro-Dollar market, with London playing a leading role in dealing with 'off-shore' dollar assets.[32] The trajectory was different in the USA, but in the early 1970s decisive measures were taken to resist the Bretton Woods idea that countries should co-operate to control capital flows.[33] There were attempts to increase regulation of these flows in the 1970s and 1980s, with some European counties and Japan resisting what was increasingly driven by both ideological pressure and capital market competition from the USA. There emerged what came to be called the 'Washington Consensus' for which a key principle was liberalization of

[29] Daunton, 'Britain and Globalization. IV. The Creation of the Washington Consensus', 8–18.

[30] J. Chwrieoth, *Capital Ideas. The IMF and the Rise of Financial Liberalization* (Princeton, NJ, 2010), 133–40.

[31] E. Helleiner, Explaining the Globalization of Financial Markets: Bringing States Back In', *Review of International Political Economy*, 2 (1995), 315–41; Chwrieoth, *Capital Ideas*. For an emphasis on the *interplay* between the USA and Britain in shaping these changes, see Green, *The Political Economy.*

[32] C. Schenk, 'The Origins of the Euro-Dollar Market in London: 1955-1963', *Explorations in Economic History*, 35 (1998), 221–38.

[33] Helleiner, 'Explaining', 322–3.

capital markets.[34] Alan Greenspan of the US Federal Reserve explicitly repudiated the terminology of Bretton Woods in 1997 when he said 'We used to describe capital flight as "hot money". But we soon learnt that it was not the money that was "hot" but the place it was running from'.[35]

The transition to capital market liberalization was messy, and followed no 'plan', with the IMF only slowly and reluctantly converted. Liberalization was never incorporated into the IMF Agreements, and the Fund resiled somewhat from its 'one size fits all' stance in the wake of East Asian crisis of 1997 and further after the Crash of 2008.[36] Nevertheless, in the rich countries especially, by the 1990s liberalization had become the new normal.

For our current concerns a key question is how far did the demise of fixed rates allied with the expansion of capital flows prevent effective national economic management? In looking at this question in the British case we of course need to confront the policies leading up to the sterling crisis of 1976. In many accounts (both those lamenting and the celebratory), this crisis stands as a shining example of how national governments can be brought to heel by international capital flows, with the 'hot money' flowing out of the British economy in 1975 triggering the downward pressure on the pound, and the government's eventual recourse to the IMF and a change of domestic economic policy in a more restrictive direction. Green's recent account rightly stresses the key role of the USA in shaping the IMF response to Britain's difficulties, but continues the exaggeration of the external aspect when he writes that 'US disciplinary power played a key part in steering the UK away from a radicalization of Keynesian social democracy . . .'.[37] To see why this is a significant exaggeration we need to look at the events well before the IMF crisis of late 1976.

When Labour came to power in 1974 it inherited a poisoned legacy of a sharply increasing budget deficits, rising inflation and worsening balance of payments, and all this in a context where fixed exchange rates had been abandoned.[38] Despite these huge macroeconomic problems, until the spring of 1975 the pound had not significantly depreciated, partly because of the 'recycling' of the dollar receipts from the new, post—OPEC1 price of oil, into London. While there was certainly nervousness in the foreign exchange market in early 1975, the authorities (Bank of England and

[34] Daunton, 'Britain and Globalization since 1850. IV. The Creation of the Washington Consensus', 2–3.

[35] Cited in Chwrieoth, *Capital Ideas*, 207.

[36] B. Clift, *The IMF and the Politics of Austerity in the Wake of the Global Financial Crisis* (Oxford, 2018).

[37] Green, *The Political Economy*, 190; for a similar conclusion, M. Harmon, *The British Labour Government and the 1976 IMF Crisis* (Basingstoke, 1997), 228–29.

[38] M. Artis and D. Cobham, 'The Background', in Artis and Cobham, eds, *Labour's Economic Policies 1974-79* (Manchester, 1991), 1–5.

Treasury) on balance favoured exchange depreciation as a route to improved competitiveness.[39]

It was in this context that the Chancellor, Dennis Healey, introduced the landmark 1975 budget:

> I fully understand why I have been urged by so many friends both inside and outside the House to treat unemployment as the central problem and to stimulate a further growth in home consumption. Public or private, so as to start getting the rate of unemployment down as fast as possible. I do not believe it would be wise to follow this advice today ... I cannot afford to increase demand further when 5p. in every pound we spend at home has been provided by our creditors abroad and inflation is running at its current rate.[40]

This explicit repudiation of a 'Keynesian' response to the crisis was followed in July by the introduction of an incomes policy, in contradiction of the pledges made by Labour in the 1974 elections. By this time the exchange rate was falling hard. But, as Chris Rogers has argued, this fall, rather than forcing the hand of a reluctant government, provided a powerful argument for Ministers to use to persuade a reluctant party to accept uncongenial policies. 'By-and-large, it is not appropriate to conceive of policy changes as responses to sterling "crises", even if this language was deployed in the public arena. Rather, a planned depreciation in the pound was used to justify policy preferences with reference to apparent necessity.'[41]

In this light we can see the events of 1975 as in important respects parallel to those following the Great Financial Crash of 2007–8 when the Conservatives successfully used the alleged threat of a 'debt crisis' to persuade the electorate to support austerity. On both occasions the claim of compelling 'external forces' was used as a weapon in an ideological struggle over the direction of economic policy—though in 1975 the audience was primarily Labour party and trade union members, rather than the electorate at large as in the run-up to the 2010 election.[42]

A failure to recognize what occurred in 1975 has allowed accounts of the following year's developments, especially Britain's relations with the IMF, to become encrusted with myths. The two primary myths are that: 'The IMF settlement of December 1976 inaugurated the last Labour government's policy of public spending cuts ... and that the IMF forced the

[39] C. Rogers, 'Economic Policy and the Problem of Sterling under Harold Wilson and James Callaghan', *Contemporary British History*, 25 (2011), 345–50.

[40] Parliamentary Debates (Commons), 890 15 April 1975, 282.

[41] Rogers, 'Economic policy'; see also Rogers, 'The Politics of Economic Policy-making in Britain: a Re-assessment of the 1976 IMF Crisis', *Politics and Policy*, 37 (2009), 971–94.

[42] On the 'debt crisis' see Clift, *The IMF*, 154–60; C. Hay, 'Treating the Symptom not the Condition: Crisis Definition, Deficit Reduction and the Search for a New British Growth Model', *British Journal of Politics and International Relations*, 15 (2013), 23–37.

government to abandon the commitment to full employment through demand management.'[43]

Healey's 1975 budget speech, quoted above, included both the repudiation of expansionary fiscal policy and the announcement of future public spending cuts. Though the road to achieving cuts was a tortuous one, it was clearly commenced upon well before the IMF became involved in the debate.[44] The drivers for these cutbacks on public spending were a combination of immediate macroeconomic concerns about inflation and levels of public borrowing, but underpinned by more fundamental worries about whether the social democratic project could be pursued by continuing to increase taxes on the mass of the working class, a trend occurring over much of the post-war period, but which accelerated in the 1970s.[45] A telling statistic in this debate was that the stereotypical 'married man on average earnings' paid one tenth of his income in tax in 1961, but one quarter by 1975.[46]

The claim here is not that capital flows cannot inhibit national economic management in the conduct of fiscal policy. In some cases this seems to have happened, such as Britain in 1931, or France and Sweden in the1980s.[47] But, first, in the case of Britain, that is not what happened in the 1970s. Policy reversal was largely driven by domestic politics, and the role of the IMF was not to force the Labour government onto a wholly different path, but, as Burk and Cairncross put it, to give a 'seal of approval' to pre-existing government policies.[48]

Second, the conditions under which 'hot money' in the post-war world has reacted violently to domestic fiscal policy in OECD countries seem to have been quite specific.[49] Mosley identified such conditions as two-fold: high inflation and the threat of unsustainable public deficits.[50] Her research draws on a wide range of developed countries, including these were both present in the French and Swedish cases.

[43] S. Ludlam, 'The Gnomes of Washington. Four Myths of the 1976 IMF Crisis', *Political Studies*, 40 (1992), 715.

[44] Ludlam, 'The Gnomes', 716–20; P. Ormerod, 'The Economic Record', in N. Bosanquet and P. Townsend, eds, *Labour and Equality: a Fabian Study of Labour in Power* (London, 1980), 31, 48.

[45] R. Whiting, *Labour and Taxation* (Cambridge, 2000), 246–58; M. Daunton, *Just Taxes. The Politics of Taxation in Britain, 1914-1979* (Cambridge, 2002), 328–38.

[46] Whiting, *Labour*, 249.

[47] For some of the complexities of 1931, see J. Morrison, 'Shocking Intellectual Austerity: the Role of Ideas in the Demise of the Gold Standard in Britain', *International Organization*, 70 (2016), 175–207. For France and Sweden, see J. Tomlinson, *Can Governments Manage the Economy?* Fabian Society Pamphlet no. 524 (London, 1988), 10–13.

[48] K. Burk and A. Cairncross, *'Goodbye Great Britain'. The 1976 IMF Crisis* (New Haven, 1992), 215–28.

[49] Capital mobility was undoubtedly a problem of a different order for developing countries: D. Rodrik and A. Subramanian, 'Why did Financial Globalization Disappoint?' *IMF Staff Papers*, 56 (2009) 112–38.

[50] L. Mosley, *Global Capital and National Governments* (Cambridge, 2003).

These are important findings for two reasons. First, as discussed further below, they help to explain how in later years in Britain equally expansionary fiscal policies could be pursued without leading to capital flight. Second, they suggest that as long as these conditions are met governments have a great deal of manoeuvre in their policies, including in determining the levels of both public expenditure and borrowing without having to worry about the response of financial markets.

Taxing and spending: racing to the bottom?

An important way in which the decline in adherence to Bretton Woods norms has been linked to domestic policies is by the idea of a 'race to the bottom', which flows from the same broad mechanisms identified in the previous section. In this account, free movement of capital leads to pressure on national governments to offer favourable tax terms to mobile corporations and individuals, which in turn reduces their tax returns, and forces them to scale back public spending, especially on the welfare state. Fears of such a trajectory were voiced from the 1970s, but were a particularly prominent in the 1990s, when the term 'globalization' was widely adopted to summarize changes in international economic conditions, especially liberalized capital flows. As Helen Thompson pointed out in 1997, 'In recent years it has become a commonplace of both academic and financial discourse that we are living in a new economic and political world in which financial globalization is destroying the economic autonomy of individual states and hence the foundations of the nation-state as the focus of political authority and the possibilities of politics'.[51]

Such loss of autonomy was seen as especially damaging for the prospects of social democracy, with a diagnosis of 'social democracy versus globalization'.[52] This problem was not just a matter of economic debate: on the contrary, we can see the constraints on policy posed by financial globalization (and the explicit use of the 1976 IMF crisis as an example of the dangers) as foundation to New Labour's approach to the economy.[53] From this perspective, establishing credibility with international finance, for example by making the Bank of England independent, was crucial to creating any room for manoeuvre for domestic policy.[54]

[51] H. Thompson, 'The Nation-state and International Capital Flows in Historical Perspective', *Government and Opposition*, 32 (1997), 84.

[52] This discussion is returned to in the final section below. For sceptical views on the conflict, see P. Hirst, 'Has Globalisation Killed Social Democracy?' *Political Quarterly* 70 (1999), 84–96; B. Clift, 'Social Democracy and Globalization: The Cases of France and the UK', *Government and Opposition* 37 (2003), 467–500.

[53] B. Clift and J. Tomlinson, 'Credible Keynesianism? New Labour's Macroeconomic Policy and the Political Economy of Coarse Tuning', *British Journal of Political Science*, 37 (2007), 47–69; C. Hay, *The Political Economy of New Labour* (Manchester, 1999).

[54] B. Clift and J. Tomlinson, 'Negotiating Credibility? Britain and the IMF from 1956 to 1976', *Contemporary European History*, 17 (2008), 545–66.

How far did such political understandings reflect an underlying economic and political reality? In addressing these issues a key empirical question is what has happened to public spending (especially spending on social welfare, which makes up the largest and growing share of total spending) and taxation over the post-war period, and how far have changes in these been determined by international forces (or 'globalization'), notably capital mobility?

The big story for the whole of the OECD world is that public spending on welfare has, on trend, risen persistently in the 'globalized' era since the 1970s. This upward trajectory was interrupted by the austerity after the Great Financial Crash of 2007–8, but then resumed. Britain's trajectory broadly follows that of the OECD, but with a later turning point after the post-2010 austerity period (Fig. 2). On this measure social spending in both the OECD and the UK has increased by a third (from 15 to 20 per cent of GDP) since 1980. This data, showing that Britain has kept pace with rising *average* OECD spending levels, is of course consistent with a falling behind of the levels in the *highest* spending countries of Northern Europe.[55]

This increased social spending has gone along with two other trends: a rise in total public spending, but a decline in that total as a share of GDP. Total public spending, adjusted for inflation, has risen almost continuously in the years since the mid-1970s, and even in the recent (post-2010 but pre-COVID19) era of cuts the absolute level has barely declined. Over the last forty years total spending (adjusted for inflation) has grown around 250 per cent.

However, this absolute increase has gone along with a decline in total spending ('Total Managed Expenditure') relative to National Income. Measured in this way public spending has fluctuated with the economic cycle, but with a downward trend from just under 50 per cent in 1975–6 (the post-war peak) to a low point of 37 per cent in 1999–2000. Thereafter the trend was up, with a sharp increase to around 48 per cent in 2009–10. Post-2010 austerity plans would have taken the figure to around 38 per cent by 2020, but that project ended by the time of the 2019 general election (Fig. 3). The long-term downward trend is a partly accounted for by the very large fall in public investment (not least in housing) which means *current* spending fell by perhaps 6 per cent of GDP over the period from the mid-1970s to the end of the century.[56]

The combination of rising social welfare spending and a falling overall share of spending in GDP has been reconciled by falls elsewhere,

[55] A. Atkinson, *Inequality. What Can Be Done?* (Cambridge, MA, 2015), 269.

[56] A. Jowett and M. Hardie, *Longer-term Trends-Public Sector Finance* (London, ONS, 2014), 14.

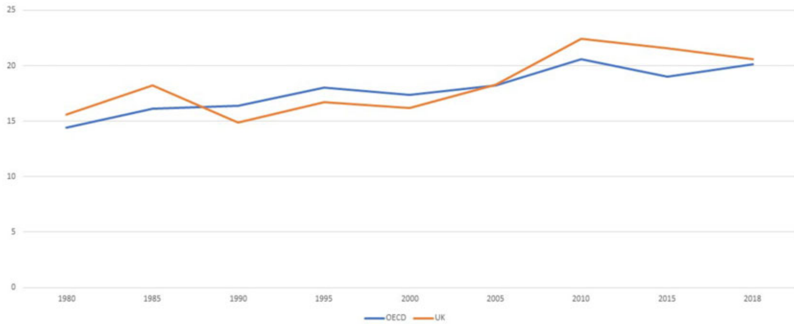

Figure 2.
Public social spending in the OECD and the UK, 1980–2018 (percentage of GDP).

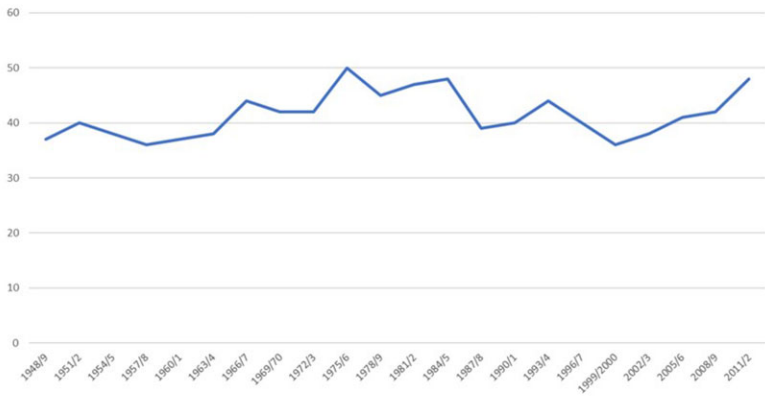

Figure 3.
Public spending in the UK 1948–9 to 2011–12.

especially in military spending but also subsidies to nationalized industries and to the private sector.[57] Table 1 summarizes the major elements.

So overall in the 'neo-liberal era' state spending on welfare has *risen*; we have moved from what David Edgerton called a 'warfare state' in mid twentieth-century Britain to one which, at least in quantitative terms, more than ever deserves the term 'welfare state'.[58]

So it turns out that the historical puzzle is not to explain a 'race to the bottom' in welfare spending, but to explain the persistent upward

[57] Though the story of industrial subsidies is complicated by the rise in disguised subsidies in the form of tax allowances and exemptions. The scale of these, along with direct subsidies, has been calculated to exceed total corporate tax revenues: K. Farnsworth, *Social Versus Corporate Welfare. Competing Needs and Interests within the Welfare State* (London, 2012), 119, 120.
[58] D. Edgerton, *Warfare State. Britain, 1920-1970* (Cambridge, 2006).

Table 1.
Key components of public spending as a share of GDP, 1978–79 to 2017–18

	1978–79	2017–18
Health	4%	7%
Military	4%	1.9%
Social security (pensioners	5%	6%
Social security (non-pensioners)	3%	4.6%

Source: C. Emmerson, T. Pope and B. Zaranko, *Outlook for 2019 Spending Review* (London, IFS, 2019), 5.

movement *despite* globalization. One important argument is that globalization encourages the growth of the welfare state. A pioneering study of the period 1960–75 found the degree of openness of economies by some margin the best explanation of state growth in that period.[59] This argument draws evidence not only from the globalization of the last few decades, but also from the first great globalization in the decades before 1914, when in many countries in Western Europe and the Antipodes greater economic openness was paralleled by the beginnings of substantial public welfare provision.[60] Rodrik emphasizes that this positive relationship between openness and public spending is true for a wide range of countries, and explains it in terms of risk reduction. 'Societies seem to demand (and receive) an expanded government role as the price for accepting larger doses of external risk. In other words, government spending seems to provide social insurance in economies subject to external shocks.'[61]

This kind of 'race to the top' argument provides a persuasive general case, though how exactly higher risk translates into policy changes is less clear. It seems necessary to link these statistical linkages to political arguments and forces to understand more precisely how this translation might take place.[62]

Other political scientists have accepted that increased risk is the key explanation for the rise of state spending, but disputed the claim that this

[59] D. Cameron, 'The Expansion of the Public Economy: a Comparative Analysis', *American Political Science Review*, 72 (1978), 1243–61. This work drew on discussions of the experience of small open economies especially in northern Europe, for example: A. Lindbeck, *Swedish Economic Policy* (Berkeley: CA, 1974).

[60] A. Atkinson, 'Globalization and the European Welfare State at the Opening and the Closing of the Twentieth Century', in H. Kierkowski, ed., *Europe and Globalization* (London, 2002), 249–73; Atkinson, *Inequality*, 264–66.

[61] D. Rodrik, Why do More Open Economies have Larger Governments?', *Journal of Political Economy*, 106 (1998), 998.

[62] G. Garrett, *Partisan Politics in the Global Economy* (Cambridge, 1998); the one case where national legislation on social support has been tied *explicitly* to the impact of international trade is in the USA with 'trade adjustment assistance': K. Baicker and M. Rehavi, 'Policy Watch: Trade Adjustment Assistance', *Journal of Economic Perspectives*, 18 (2004), 239–55.

extra risk is primarily due to globalization. Instead, they argue, it is deindustrialization that is the main causal factor. They point to the way in which this structural change brings job losses, and often, even where a new job is acquired, a shift to a less skilled and less well-paid employment in the service sector.[63] The authors are aware that deindustrialization could itself be caused by globalization, and thus merely be adding a complication to the argument that globalization is the key to welfare expansion. But they refute this view, showing that most of the deindustrialization in their sample of fifteen advanced countries was not linked to global competition.[64] Rather, as many other analysts have suggested the major long run causes of deindustrialization are rapid technological change in industry, combined with relatively low income elasticities of demand for industrial goods, as affluent consumers spend greater proportions of their incomes on services.[65] (This conclusion needs to be qualified, at least for the short term, in looking at the last couple of decades of deindustrialization, especially in the USA, where Chinese competition does appear to have fed into a significant loss of industrial jobs—though such losses have been going on for a much longer period.)[66]

Both globalization and deindustrialization, and responses to them, are an important part of the story about the growth of welfare spending. Deindustrialization, defined as a falling share of industrial as a share of total national employment, is now a global trend, extending even to the 'world's factory', China.[67] But like most global trends, it has been responded to differently in different countries.[68] In Britain's case it has been accompanied by (on trend) a very substantial growth in public sector employment, especially if one take's account of the large number of 'parastate' jobs where finance comes from the state, but the jobs are sub-contracted to the private sector.[69] Much of this growth is the employment dimension of the growth of public spending, especially on health and social care. But this employment growth, whilst offsetting the loss of industrial jobs, has often added to the spread of poorly paid and precarious

63 T. Iversen and T. Cusack, 'The Causes of Welfare State Expansion. Deindustrialization or Globalization?', *World Politics*, 52 (2000), 313–49.

64 Iversen and Cusack, 'The Causes', 339–45.

65 R. Rowthorn and R. Ramaswamy, 'Growth, Trade and Deindustrialization', *IMF Staff Papers*, 6 (1999), 18–41.

66 D. Autor et al., 'The China Syndrome: Local Labor Market Effects of Import Competition in the United States', *American Economic Review*, 103 (2013), 2121–68.

67 <https://data.worldbank.org/indicator/SL.IND.EMPL.ZS> accessed 29 April 2020. The global figure for 2014 was 23.2%, down to 22.8% in 2019, for China 29.4–28.3%; see also D. Rodrik, 'Premature Deindustrialisation', *Journal of Economic Growth*, 21 (2016), 1–33.

68 For more discussion of this, J. Tomlinson, 'De-industrialization not Decline. A New Meta-Narrative for Post-War British History', *Twentieth Century British History*, 27 (2016), 76–99.

69 J. Buchanan et al., *Undisclosed and unsustainable: problems of the UK National Business Model* (Manchester, CRESC, 2009). These calculations are similar to those in Centre for Cities, 'Cities Outlook 2014' (London, 2014).

employment, part of the polarization of the labour market that has accompanied deindustrialization.[70]

This polarization, and the accompanying rise of in-work poverty, has led to much of the growth on non-pensioner social security quantified in Table 1. While support for the unemployed has been very tightly limited, there has been an enormous expansion of in-work benefits, beginning on a very small scale with Family Income Supplement in 1972, and expanding especially rapidly in the form of tax credits in the 1990s and 2000s.[71] There were serious cutbacks after 2010, but this remains a large expenditure which, to emphasize, did not exist in the 1950s and 1960s.[72] The mounting costs of this support help to explain the *volte face* of the Conservative party on a national legal minimum wage, which they strongly opposed when first proposed by the Labour party in the early 1990s, but after it was introduced in 1998, came to embrace it with increasing enthusiasm in the 2000s.[73] It was a way of trying to address in-work poverty which did not require state spending. Expenditure on housing benefits also expanded rapidly from the 1980s, an unintended consequence of the liberalization of house rents, combined with income polarization.[74]

In sum, in the British case, the trend of public spending across a range of headings can be seen to have risen markedly as deindustrialization has persisted. But there have been other factors at work in causing this trend. Most important are demographic changes. Britain has shared with most of the world an ageing population profile, which has translated into higher demand for pensions and for healthcare.[75] Older people tend to have a higher voting propensity, so these demands have been significantly acceded to, leading to substantial growth in pension and health care spending (demand for which rises rapidly in old age).

It is not hard to understand the diverse pressures for higher public spending in modern Britain. But the race to the bottom story would suggest that this demand for spending would be ineffectual because of the

70 M. Goos and A. Manning, 'Lousy and Lovely Jobs: the Rising Polarization of Work in Britain', *Review of Economics and Statistics*, 89 (2007), 118–33.

71 There is excellent discussion of this shift and its historical context in P. Sloman, *The Transfer State. The Idea of a Guaranteed Income and the Politics of Redistribution in Modern Britain* (Oxford, 2019), 174–202. For the reduction in unemployment benefits, Atkinson, *Inequality*, 226.

72 Tax credits were incorporated into Universal Credit: D. Clegg, 'The Demise of Tax Credits', *Political Quarterly*, 86 (2015), 493–99; Sloman, *The Transfer State*, 209–16.

73 By 2005 David Cameron was proclaiming: 'I think the minimum wage has been a success, yes. It turned out much better than people expected.' Cited in J. Waltman, *Minimum Wage Policy in Great Britain and the USA* (New York, 2008), 207.

74 <https://obr.uk/forecasts-in-depth/tax-by-tax-spend-by-spend/welfare-spending-housing-benefit/> (2019) accessed 29 April 2020.

75 R. Disney 'Population Ageing and the Size of the Welfare State: is there a Puzzle to Explain?' *European Journal of Political Economy*, 23 (2007), 542–53.

difficulties national governments would have in expanding their revenue base, in the face of footloose capital (assuming that borrowing could not expand indefinitely to fill such a gap in revenues). But this squeeze from the revenue side has not occurred.

Discussion of this issue focusses on corporate tax, assumed to be most vulnerable to downward pressure as corporations are able to play one country against another in searching for the lowest rates. Such a perception of the forces at work fits well with the public rhetoric of successive Chancellors of the Exchequer in Britain, who to demonstrate that Britain is 'open for business' have consistently cut corporation tax rates, from 52 per cent in the 1970s to 19 per cent in 2019.[76] This, indeed, has been a common pattern across the OECD world, suggesting that corporations have indeed gained the upper hand in bargaining with nation states.[77]

But as so often with tax, headline *rates* are not very informative about the levels of tax revenue. Despite these rate cuts, revenue from corporate tax has been quite buoyant, as a result of two factors. First, alongside rate reductions governments have commonly cutback on a variety of exemptions, deeming them 'distorting', thus raising the effective rate. Second, since the 1980s corporate profits, whilst affected by the economic cycle, have been more buoyant that in the previous decades, so the amount of revenue from a given rate has risen. In 2000 a report by the Institute for Fiscal Studies observed: 'Perhaps the most striking feature of the current regime is that it continues to raise significant revenue, despite concerns that globalisation would lead to a 'race to the bottom' as countries competed with one another to attract businesses by offering lower and lower tax rates.' This conclusion would continue to apply in the early twenty-first century.[78]

In addition, corporate taxes are a quite small proportion of total tax revenues. This was one of the important points made by Andrew Glyn twenty years ago, in his sceptical assessment of the impact of globalization, and the point stands. At that time, he suggested that corporate tax was typically around 8 per cent of revenues in OECD countries, and that figure would still be accurate in the twenty-first century.[79]

This limited contribution of corporate taxes to overall tax revenues is significant in assessing the claims made, especially in the run-up to the Crash of 2007–8, that the financial sector was the 'goose that laid the golden egg', and that therefore the growth of that sector should not be

[76] Under New Labour it fell from 31% in 1997 to 28% in 2010.

[77] <https://stats.oecd.org/Index.aspx?DataSetCode=REV OECD.Stat> *Revenue Statistics.* accessed 1 May 2020.

[78] T. Clark and A. Dilnot, *Long-term Trends in British Taxation and Spending* (London, IFS, 2000), 8.

[79] A. Glyn, 'The Assessment: how far has Globalization gone?' *Oxford Review of Economic Policy*, 20 (2004), 10.

inhibited. Claims to the effect that the financial sector played such a role often ignored both the small proportion of total tax contributed by corporations, and that the manufacturing sector contributed more. At the peak of the pre-Crash boom in the City (2006–7), *total* tax paid by the financial sector was 7.4 per cent of government revenue.[80]

The other tax which is potentially affected by international competition is income tax, where countries might reduce the tax rates, especially on higher incomes in order to attract or hold on to highly-paid individuals.[81] As with corporation tax, we do indeed see a fall in income tax rates over the last forty-odd years, especially at the top end. The process of cutting these rates began dramatically under Thatcher, when the highest rate was cut from 83 to 40 per cent and the standard rate from 35 to 23 per cent. Governments since then have broadly followed the 'low tax' path, with the standard rate falling to 20 per cent. Much more than in the case of corporation tax, the cuts in income tax have gone along with a fall in its share of total revenue, which was around 40 per cent in 1975 but only 26 per cent in 2018. The 'gap' in tax this has left has been made up largely from National Insurance (which most tax analysts would regard as income tax by another name, although the ceiling on contributions makes it much less progressive in impact) and VAT. This has gone along with the tax structure overall becoming less progressive, as more revenue is raised from the less progressive indirect taxes—though the redistributive impact of the British public sector right through the post-1945 period has come more from the pattern of social spending than from the progressivity of taxation.[82]

But the idea that cuts in income tax in Britain since the 1970s have been primarily caused by external competitive pressures appears largely mistaken. Issues of domestic equity and efficiency were the main drivers of the cuts under Thatcher, and have largely shaped tax policy thereafter. In principle high earners might migrate for tax reasons, and tax havens have become popular residences for British billionaires, but the impact of such movement on total revenue is very limited.[83] As Glyn noted 'the share of

[80] I. Erturk et al., 'City State against National Settlement. UK Economic Policy and Politics after the Financial Crisis', Centre for Research on Socio-Cultural Change (Manchester, 2011), 15–16.

[81] As with corporation tax, lower rates have been accompanied by the curtailing of some allowances, most notably Mortgage Interest Relief (MIRA), which was reduced and finally abolished in 2000. At its height MIRA cost the Exchequer £7.7 billion in 1990, more than was spent on *gross* social housing investment (i.e. ignoring receipts from council house sales): D. Mullins and A. Murie, *Housing Policy in the UK* (Basingstoke, 2006), 51.

[82] Whiting, *Labour*, 2; for the significance of this point, J. Tomlinson, 'Social Democracy and the Problem of Equality: Economic Analysis and Political Argument in the United Kingdom', *History of Political Economy*, 52 (2020), 519–38.

[83] The history of tax havens is explored in V. Ogle, ' "Funk Money": The End of Empire, The Expansion of Tax Havens and Decolonization as an Economic and Financial Event', *Past and Present*, 249 (2020), 167–211.

tax paid by the rather few very high earners who are genuinely internationally mobile is pretty small, and it is hard to see this having a major effect on welfare-state financing'.[84]

Doctrine: the limited triumphs of neo-liberalism?

While the prime concern here is the *effects* of the demise of 1940s-style embedded liberalism, the combination of fixed exchange rates and capital controls, it is worth asking *why* both of these had largely disappeared by the end of the 1970s. As these inter-connected changes involved allowing more freedom to market forces it is tempting to see them as a manifestation of the growth of neo-liberal ideas, part of a general trend in that direction often seen as central to post-war economic thinking. Yet such a view needs to be heavily qualified.

First, as regards flexible versus fixed rates, the arguments do not fit readily onto a neo-liberal versus Keynesian spectrum. At Bretton Woods itself there was remarkably little debate about the merits of these alternatives.[85] The pre-disposition to support fixed rates evident amongst most economists drew on a sense of the damage done by floating in the 1920s and 1930s, summed up in the influential League of Nations study which argued 'If there is anything that interwar experience has clearly demonstrated, it is that paper currency exchanges cannot be left free from day to day under the influence of market supply and demand' because speculation would 'play havoc' with them.[86] Key neo-liberal figures such as Hayek and Robbins agreed with this diagnosis of the damage wreaked by flexible rates, and for Hayek the solution was a return to some kind of gold standard.[87] This kind of view was to be re-phrased during the burst of enthusiasm for the benefits of globalization at the end of the century, for example in the rhetoric of Thomas Friedman's 'golden straitjacket'. In this view, positioning a country on point 'A' in Fig. 1 would mean capital flows forcing 'responsible', beneficial behaviour on otherwise badly-behaving national governments.[88]

Conversely, an early critic of the fixed rate regime was the resolutely Keynesian economist, James Meade. Partly drawing on his unhappy experience as economic advisor to the Labour government in 1945 and 1946, Meade believed that a more flexible exchange rate regime would be preferable to what he saw as the excessive controls on British trade. In 1948, while not advocating a depreciation of sterling, he was clear that 'the

[84] A. Glyn, 'The Assessment: how far has Globalization Gone?' *Oxford Review of Economic Policy*, 20 (2004), 10.
[85] Irwin, *Missing Bretton Woods Debate.*
[86] R. Nurske, *International Currency Experience* (Geneva, 1944), cited in Irwin, *Missing Bretton Woods Debate*, 2, 13–14.
[87] Irwin, *Missing Bretton Woods Debate*, 7–8.
[88] T. Friedman, *The Lexus and the Olive Tree* (New York, 2000), 101–11.

method of exchange rate adjustment is to be greatly preferred to that of direct trade controls'.[89] By 1952 he was calling for a fresh round on international economic negotiations to sort out what he called the 'intellectual muddle' of Bretton Woods which had not recognised that you could not have free convertibility of currencies without variable foreign exchange rates, and he advocated frequent and substantial alterations of parities or floating.[90] These arguments were being made, it should be stressed, before the publication of Milton Friedman's famous article on the issue, which is often seen as the foundation stone of economic arguments for floating.[91] As Daunton emphasizes: 'ideas were not the major drivers of change.'[92]

In the event, as already noted above, the driving forces for the breakdown of the fixed rate system were the American dilemmas about reconciling a dollar-based international system with domestic priorities, and accelerating inflation. Even then, there was strong support for fixed rates by those who believed, as was so common in the 1940s, that floating rates would fluctuate hugely and be economically destabilizing.

If we look at the issue if the decline in controls on capital movements, we again see more evidence of the working of calculations of national (and interest group) advantage driving policy than the impact of economic doctrine. In Britain the drive to free capital from these controls came especially from the City of London, emphasizing, for example, the balance of payments benefits from expanding London's 'invisible exports'.[93] The city found a willing ally in the Institute of Economic Affairs, the key contemporary source of neo-liberal thinking, who published a key text from a City figure promoting the role of invisibles.[94]

Just as an early generation of Keynesian economists exaggerated the impact of Keynesian thinking on policy outcomes, so both friends and enemies of neo-liberalism have tended to do the same for the work of

[89] J. Meade, 'Financial Policy and the Balance of Payments', *Economica*, 15 (1948), 110.

[90] J. Meade, 'Bretton Woods, GATT, and the Balance of Payments: A Second Round?' *Three Banks Review*, 16 (1952), 3–22; also, Meade, 'The Case for Variable Exchange Rates', *Three Banks Review*, 27 (1955), 3–27.

[91] M. Friedman, 'The Case for Flexible Exchange Rates', in *Essays in Positive Economics* (Chicago, 1953), 157–203.

[92] Daunton, Britain and globalization IV The Creation of the Washington Consensus', 13.

[93] J. Tomlinson, 'Labour Party and the City 1945-1970', in R. Michie and P. Williamson, eds, *The British Government and the City of London in the Twentieth Century* (Cambridge, 2004), 189; A. Davies, *The City of London and Social Democracy. The Political Economy of Finance in Britain, 1959-1979* (Oxford, 2017), 148–80.

[94] W. Clarke, *The City's Invisible Earnings: how London's Financial Skill Serves the World and Brings Profit to Britain* (London, 1958). The IEA was set up in 1957 (with money from the factory farming of chickens), and most of its early publications focused on the welfare state-its very first pamphlet was on pensions: R. Cockett, *Thinking the Unthinkable.Think-tanks and the Economic Counter-Revolution, 1931-1983* (London, 1994), 141.

thinkers like Hayek and Friedman. As far as flexible exchange rates and the ending of capital controls are concerned these did indeed become causes that neo-liberals supported, but that is far from showing that their doctrinal attitudes were key to policy changes.

The end of social democracy?

Embedded liberalism is a term mostly used by political scientists. Historians of Britain have been more inclined to talk of a 'short-life of social democracy' as describing the years from the 1930s to the mid-1970s.[95] These approaches clearly overlap; both see a major discontinuity in post-war Britain (and elsewhere) in the 1970s, linked to the growth of economic internationalization or 'globalization'. For James Vernon 'Changing global conditions assured that social democracy in Britain had a brief life'.[96] By the 1990s there was 'a conventional wisdom about the demise of leftist alternatives to free market capitalism in the face of internationalization forces'.[97]

So we can look at the issues raised by this article from a slightly different perspective by looking at the fate of social democracy; did the international regime defined by the collapse of fixed exchange rates and the decline of capital controls undermine the viability of social democracy?

Our view of the fate of social democracy will necessarily be affected by our definition of that term. It clearly should not be reduced to one dimension, but linked to its historic evolution in the British context. One view is that 'The propensity to deficit spend is the political economic *sine qua non* of social democracy'.[98] This seems compelling as *one* central component of British social democracy, though, as suggested above, the general buoyancy of the economy meant there was little call for such spending on a large scale before the mid-1970s. But the strength of commitment to the principle of such policies is evident in the anguish on the Left when Healey, in the speech quoted above, proved unwilling to increase the deficit to reduce unemployment. But does Healey's unwillingness tell us that such fiscal expansionism was no longer possible in a 'globalized world'?

Here the evidence is clear. Despite Healey's refusal of that policy path in the mid-1970s, followed by the trauma surrounding the 1981 budget, when the government directly contradicted long standing norms and cut the budget deficit in a recession, these two decisions did not establish a

[95] J. Vernon, *Modern Britain, 1750 to the Present* (Cambridge, 2017), 430–516.
[96] J. Vernon, 'The History of Britain is Dead', 33.
[97] G. Garrett, 'Capital Mobility, Trade and the Domestic Politics of Economic Policy', *International Organization*, 49 (1995), 659.
[98] Garrett, 'Capital Mobility', 682.

'new normal'.[99] In the next depression, in the early 1990s, the Conservative government under Major allowed the 'automatic stabilizers' to work, and the deficit (Public Sector Net Borrowing) peaked in 1993–4 at 7.7 per cent of GDP, actually larger than the 7.0 per cent in 1975/6, about which so much fuss had been made. In 2008–9 in the wake of the financial crisis, the Labour government again pursued standard 'Keynesian' remedies, with the budget deficit rising to almost 14 per cent in 2009–10.[100] It is surely paradoxical that with so much literature proclaiming the 'end of Keynesianism' that public borrowing since the 1990s has varied with the economic cycle at levels significantly *higher* than in the preceding 'Keynesian age'.[101]

To emphasize the broader point: freeing capital markets has put little inhibition on domestic stabilization policy in Britain. All these crises had different characteristics, but just as, in the early 1980s, Thatcher's policies were driven by wholly domestic considerations, the same was true in the early 1990s and in 2008–9, with no constraining adverse reaction from international finance. In the run-up to the 2010 election Labour, like the Conservatives, proposed policies to reduce the budget deficit as the economy recovered, but this was not driven by external financial pressures, and the evidence of the bond market is that Conservative claims of an impending 'Greek-style' sovereign debt storm were spurious.[102]

But 'Keynesian' fiscal policy is only one element of social democracy. Long before the days of fiscal stabilization British social democrats put state spending on welfare at the heart of their agenda.[103] The historical story of public expenditure as outlined above undermines any notion of a simple bifurcation of Britain's post-war history into 'social democratic' and 'neo-liberal' regimes. Thatcher's government was strongly committed to public expenditure cuts, but found them very hard to achieve.[104] Eventually the late 1980s and 1990s did see a clear downward trend in public spending to GDP, but this was reversed early in the new century,

[99] On the 1981 budget see: D. Needham and A. Hotson, eds, *Expansionary Fiscal Contraction. The Thatcher Government's 1981 Budget in Perspective* (Cambridge, 2014). Healey undoubtedly *was* constrained by international pressures and the flight of 'hot money', but this was in highly unusual circumstances similar to those discussed by Mosley; inflation reached a historic peak of 25 per cent *at approximately the same time* as the fiscal deficit was at an unprecedented peacetime high.

[100] ONS Database.

[101] Of course, such recourse to fiscal stabilization has been more necessary, because the economy has been more subject to more shocks in the 'neo-liberal' period.

[102] An *Investors Chronicle* headline of 6 October 2009 summarized the situation well: 'benign bond markets belie political panic'; M. Blyth, *Austerity.The History of a Dangerous Idea* (Oxford, 2013), 71–73.

[103] R. H. Tawney, *Equality* (London, 1931); B. Jackson, *Equality and the British Left* (Oxford, 2007).

[104] J. Tomlinson, 'Britain since the 1970s: a Transition to Neo-liberalism?' in J. Hoppitt, D. Needham and A. Leonard, eds, *Money and Markets. Essays in Honour of Martin Daunton* (Woodbridge, 2019), 181–97.

with unprecedented increases in welfare spending, especially on the NHS (Fig. 3).

The long-standing social democratic focus on welfare spending has derived from a powerful commitment to egalitarianism (albeit often vague in character); rightly or wrongly, ever since Tawney the welfare state has been at the centre of the ambition to achieve greater equality.[105] On inequality, it is clear that the Thatcher years do indeed mark a watershed. Inequality, measured by the Gini Co-efficient, jumped by almost 50 per cent, from 0.23 in 1978 to 0.34 by 1992.[106] This resulted from tax and social security changes, the weakening of trade unions, but also an accelerating shift in the labour market towards a more polarized distribution. After 1990 the Gini Co-efficient fluctuated, without any clear trend, though the very top part of the distribution continued to pull away. Under New Labour poverty was reduced but the overall pattern of inequality changed little.[107] Labour's policies were 'running-up a down escalator' as they sought to counteract the continuing divergence in labour market rewards, driven in large part by deindustrialization.

Clearly in some respects we can proclaim the death of social democracy. Policies plausibly labelled 'neo-liberal' (or 'market fundamentalist'), such as labour market de-regulation (except national minimum wages), anti-trade unionism, and privatization have become the new normal in post-1980s Britain. But if we return to the intertwined question of embedded liberalism and *its* fate the conclusion is more mixed. The domestic political pressures to stabilize the national economy and sustain an expansion of overall welfare spending, whilst simultaneously pursuing enhanced international integration, have remained powerful even as social democracy has weakened. While the precise mechanisms identified to reconcile the two imperatives in the 1940s—fixed exchange rates and capital controls-have disappeared, the key purpose of embedded liberalism has survived. But the context for domestic policy has been greatly altered, above all by deindustrialization and the polarization of the labour market that has followed.

The centrality of deindustrialization to the overall argument here takes us back to the starting point of David Edgerton's arguments about the national and the international in *The Rise and Fall of the British Nation*. In that book he makes a compelling and important case for the centrality of industry to the understanding of the British nation in the mid-twentieth

105 N. Ellison, *Egalitarian Thought and Labour Politics. Retreating Visions* (London, 1994); for an important perspective on this: B. Jackson, 'The Rhetoric of Redistribution', in J. Callaghan, N. Fishman, B. Jackson, and M. McIvor, eds, *In Search of Social Democracy. Responses to Crisis and Modernisation* (Manchester, 2009), 233–51.

106 K. Stewart et al., 'Introduction', in J. Hills, T. Sefton and K. Stewart, eds, *Towards a More Equal Society?* (Bristol, 2009), 3.

107 T. Sefton et al., 'Poverty, Inequality and Redistribution', in Hills et al., eds, *Towards*, 21–45; Chick, *Changing Times*, 114–22.

century. He also charts how towards the end of the twentieth-century large parts of industry became externally owned, and the level of international integration of British-based production made it much harder to talk of a distinctive national *industrial* economy. But the book does not analyse some of the issues arising from the combination of intense 'globalization' in much of manufacturing industry with a *de-globalization* via the development of largely 'unglobalized' public and private services, and a continued growth of significant parts of social welfare spending.

The 'national economy' was always 'imagined', a 'myth' created by a combination of state and political practices which exaggerated the separateness of economic activity from that of other countries.[108] And, *imagined as an industrial economy*, the national economy has, as Edgerton rightly insists, ceased to exist.[109] But it still makes a great deal of sense to talk of a 'national economy', thought of as a distinctive economic 'space' in which the national state remains powerful in its control over (some) resources and (some) effective policy instruments. In that regard we are still in the world of 'embedded liberalism', where despite the progress of globalization, including especially capital mobility,nation states continue to be economic 'communities of fate'.

[108] A. Tooze, 'Imagining National Economies: National and International Economic Statistics, 1900-1950', in G. Cubitt, ed., *Imaging Nations* (Manchester, 1998), 212–28.

[109] Chapter nineteen of *The Rise and Fall* is entitled 'A Nation Lost'.