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THE MACROECONOMIC FETISH IN ANGLO-AMERICAN ECONOMIES

by

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Abstract

English-speaking economists imagine that the economy is manipulated by policies directed at the macroeconomic level. The microeconomy is supposedly dictated by the market mechanism (and by policies designed to enhance the market's operations). This vision is reinforced in Australia within the syllabus, in the bureaucratic hierarchy, in policy priorities, and in media commentary. Yet the vision is essentially ideological, and historically inept. The intellectual and political origins of this vision are explored; and its distortionary and adverse effects on Australian industry policy are examined.

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# THE MACROECONOMIC FETISH IN ANGLO-AMERICAN ECONOMIES

**Evan Jones**

## 1. THE ENTRENCHED DUALITY OF MACROECONOMICS AND MICROECONOMICS

Economics is characterised by an immutable split between a 'macroeconomic' component and a 'microeconomic' component. It is embedded in the syllabus and in the textbooks. It is immutable because considerations of syllabus reform become involved in endless re-orderings of the two components but no consideration of whether the division itself and its key ingredients might be up for grabs.

The macro-micro split is a peculiarly Anglo-American intellectual phenomenon. Yet the cultural influence of Britain and later the US has seen the export of this phenomenon into the alien environment of both Europe and Asia. Thus we have books on the Japanese economy written by US-educated Japanese nationals with chapter titles like 'fiscal policy, 'monetary policy', etc., which are incongruous with the Japanese policy complex. In this process, it becomes doubly hard to learn about one's own culture when divergent cultures are also interpreted through the same lens (c/f Caves & Krause, 1984, offering a mainstream US view of Australia).

In this macro-micro bifurcation, government policy is located predominantly in the macro compartment. Indeed, behind the macro-micro distinction is a policy-market distinction. The private sector looks after the structure of the economy in which the dynamics of the profit motive is constrained by the social ordering of the impersonal market mechanism. The public sector looks after the aggregate level of the economy - it gets the 'big picture' right so that the market can function at the micro level (Jones, 1987).

This world-view and its distortions was captured succinctly some decades ago by the English economic historian Michael Postan (Postan, 1968), but the sentiments articulated by Postan went unheeded. To quote:

"[that] which concerns us most here is the compulsive preoccupation of economists with aggregates cast on a national scale, and their neglect of the more detailed, more concrete, more ... social problems of the modern economy. ... [The Keynesian entities] are generalised holistic concepts, detached from their local and specific circumstances. Its prescriptions are therefore similarly general and holistic ... . They are meant to be administered to the economy at its centre, so to speak by the mouth, and to be ingested and reacted to by the economic system as a whole. ...

All the painful dilemmas of the economy ... are posed and debated as if they affect in equal measure and in the same way all and every branch of the economy. Similarly, ... restrictions of credit are prescribed as general medicines, expected to work their effects through the system as a whole." (ibid.:43)

There is an evident continuing involvement of policy considerations within the micro compartment. Yet these are devoted to considerations of beating back supposedly unwarranted intrusions on the market mechanism. The key area in this regard has been the regulation of product market competition, but this has recently been augmented by a preoccupation with labour force regulation and with public sector infrastructure.

A large sub-discipline of 'industry economics' has grown up around the study of product market competition. The sub-discipline is confined by narrow and artificially-defined constraints. Its central conceptual focus is the idealisation of the perfectly competitive market, and it is preoccupied with the structure and numbers in the 'industry'.1 As a consequence, policy considerations are also artificially defined.2 There is an impoverished conceptualisation of the dynamics of the competitive process - how firms and industries grow and die; how industries are structured in terms of inter-firm interaction; how firms and industries fit into a larger environment; how the internal structure and culture of business firms influences its behaviour; and the myriad ways in which government policy channels

1. A comparable sub-discipline is in evidence in the field of labour under the rubric of 'labour economics'. Again, the idealised market mechanism is a central focus. It is noteworthy that real-world politically-driven regulation of labour conditions through arbitration, etc., has coincided with 'labour economics' maintaining its idealised conceptual focus at the cost of marginalising its relevance. As a consequence a separate discipline has grown up (industrial relations) to deal with wage labour at a more concrete level. The existence of 'industrial relations' is both a tangible reflection and an indictment of the artificial restraints of economic analysis.
2. There has been a challenge to neoclassical-institutionalist orthodoxy by the 'Austrian' school. This has a different view of competition, emphasising (desirably) process rather than merely structure and numbers. But the abstract character of the reasoning and the libertarian politics of the school has inhibited the prospects that this School could expand intelligently the boundaries of industry economics.



the competitive process. Such real-world considerations cannot be comprehended within the macro-micro bifurcation.

## 2. MACROECONOMICS AND THE POLICY SPECTRUM

### *2.1 The optimal (macro) policy mix*

The macro-micro split as a policy-market split is not purely a textbook phenomenon. It is embodied tangibly in the world-view of the opinion-makers who are important mediators between public opinion and the policy-makers. We are adumbrated interminably with the concept of an 'optimal policy mix'. This is centred on the notion that the public authorities' dominant regulatory vehicles are 'fiscal' policy and 'monetary' policy. Both operate only by influencing aggregate demand. The object is to find the optimal mix so that the degree of stimulus and the availability of credit are in harmony.

In particular, the Hawke Government has been criticised for over-reliance on monetary policy as a restrictive device in 1988-89, and for not using fiscal policy more restrictively. This is a curious notion, as the Labor Government's record since 1985 on fiscal austerity had been impeccable (at least until the recession forced its hand in 1991).

The underlying problem is that macroeconomic policy was incapable of resolving by itself the current economic malaise; indeed, it was exacerbating it. This is vaguely recognised within the conventional wisdom and articulated as the economy requiring 'microeconomic reform'. This general thrust is well-placed, insofar as myriad economic problems are to be found at the structural level, but it is predictably channelled through the usual lens of macro-micro as a policy-market divide. Given this vision, it follows naturally that the object of 'microeconomic reform' must be to free up the market.

### *2.2 The bureaucratic reflection*

The macro-micro split is also tangibly embodied in the bureaucratic hierarchy in Australia. The Departments of Treasury and Finance sit at the top of the hierarchy, both at the federal and state levels. Departments servicing industry

and social services are strictly subordinate to Treasury/Finance.3 The Treasury (coupled with the Central Bank) is the vehicle for macroeconomic policy; that is, policy *per se*.

In the formal policy-market divide, there is no room for industry departments possessing policy roles. Indeed, some might say that there is no room for industry departments at all. The State of NSW, for example, has an industry department (State Development) with an attenuated role and which is on the verge of being abolished. Nothing in the macro-micro conceptual orientation of economists' training prepares them for an active role for industry departments in the bureaucracy.

## 3. THE PECULIAR DISTORTIONS OF HISTORY

The macro-micro conceptual orientation provides a powerful set of spectacles through which to interpret processes in capitalist development across time and space. It is a distorting set of spectacles. Several examples are representative of the distortion, whose implications will be treated below.

The Japanese economy found itself in a boom and bust cycle in the wake of the industrial bonanza which was the Korean War. The monetary authorities instituted a credit squeeze in 1958. By Anglo-American standards, this was a piece of macroeconomic policy-making straight out of the textbooks but Japanese authorities weren't reading those textbooks. They instituted the squeeze in a selective fashion, making credit available selectively to favoured firms to ensure them the liquidity to survive hard times.4 The policy object was *structural*, dictated by the Ministry of International Trade and Industry, to hasten industrial rationalisation (Yamamura, 1967:163). In orthodox language, the policy was micro interventionist and not macro, though using an instrument considered to be in the macroeconomic tool kit. This form of policy is *invisible* when viewed through macro-micro spectacles.

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3. During the 1960s, the federal Department of Trade (sometime Trade and Industry) attempted political parity, but its ambitions were deeply resented. For its sins it has since been emasculated, then abolished.
4. There appears to have been no comparable strategic practice in Australia. There have been selective bail-outs during credit restrictions (e.g. the Commonwealth Bank bailout of building societies in 1974; the Westpac bailout of the Bank of Melbourne in the late 1980s). But these measures are unplanned, and occur within the finance sector to prop up general confidence.



The French, who don't mince words, were involved in the same exercise. Here is the French Planning Commissioner, during a credit squeeze in 1963-4:

> "If the basic conditions for expansion are to be respected, out credit policy must be selective. In particular, as far as medium-term credit is concerned, there is a case for giving privileged treatment to the most dynamic firms serving foreign markets and to sectors especially hard-hit by foreign competition and for giving privileged treatment to the financing of projects for the reorganisation of production." (quoted in Hall, 1984:31).

Across the ocean and the decades, one of the first acts of the Reagan Presidency was to enact a substantial cut in taxes, most notably for the better-off. The second act of the Reagan Presidency was to embark on a major expansion of expenditure on the military. James Tobin, America's foremost Keynesian, has labelled these two acts major exercises in 'Keynesian' pump-priming. Tobin acknowledges that the exercise was "reluctant, belated or inadvertent" and the motivation anti-Keynesian (Tobin, 1986:13). Nevertheless, Tobin can only interpret Reagan's policies through macroeconomic spectacles.

The tax cuts, dressed up as supply-side (macro) incentives, involved an act of wealth redistribution pure and simple. Though there are macroeconomic implications, they are incidental. The military expenditure would be expected to have macroeconomic implications, but its motive was 'national security', its institutional channels were a classic manifestation of sectoral industrial policy, and its major effects were profoundly structural. Reagan's policies were not about 'getting the big picture right'; they were about the fine detail of a preferred form of society. To use the perverted language of economists, Reagan was profoundly *interventionist*.

The Tobin mis-reading of the Reagan years is not an isolated exercise. The Keynesian myth has been mapped onto the whole of the post-1945 long boom, and across a wide range of countries (Wattel, 1986:passim). As the label *Keynesianism* is short-hand for 'macroeconomic', the unspoken thesis is that the greatest period of success in the history of capitalism was a product of macroeconomic fine-tuning, or of aggregate demand management (Jones, 1989).

When the boom ended, some blamed OPEC oil price hikes, but more blamed Keynesianism. Yet most of the right-wing economists who attacked Keynesianism didn't attack the macro perspective; they merely re-appropriated it for their cause.

## 4. THE ORIGINS OF MACRO FETISHISM

The macro-micro split has ensured its appeal because it appears eminently sensible - the complementary duality of the parts and the grand picture. However, the split lacks focus - the parts are not integrated and make no coherent whole. This split is partly historically grounded in specific conditions, of which more below. Yet it has been reproduced in an uncritical and generalised fashion, and now sits on understanding like a dead weight.

The intellectual incoherence has intermittently been confronted from within the ranks of respectable economists. In the late 1960s, Edmund Phelps and others attempted to tie a bastard Keynesian macroeconomics to more stringent micro-foundations, along orthodox microeconomic lines (Phelps et.al., 1970). This paved the way for the rise of the rational expectations school. 'New Classical' economics has attempted to redefine the axioms of macroeconomic theory systematically to ensure compatibility with microeconomic orthodoxy. This development has of course taken the tradition in microeconomics as the standard bearer from which to enforce compatibility. By contrast, post-Keynesian economics has attempted compatibility by redefining the basic axioms of microeconomics; but this unpopular proposal has merely reinforced the marginal status of post-Keynesian economics.

The split remains. It is possible that the split reflects an uneasy compromise, a balance of forces of differing world-views within the profession. These differences are partly ideological. It seems apparent that the split also reflects a theory/policy divide. In spite of the increasing dominance of not merely microeconomics but macroeconomics by a neoclassical perspective (vitiating a 'demand management' role for government), the body of macroeconomic thought retains a large 'pragmatic' element. No doubt this is due to the breadth of personnel and strength of the substantial paraphernalia of the institutional policy apparatus involved in macroeconomic policy-making.

### *4.1 A historical grounding in the peculiarity of British capitalism?*

The historical conditions are peculiarly those of Great Britain, with a unique character of capitalist development embodied in its institutions and its culture. Foremost amongst these is the philosophy of liberalism embedded not merely in



beliefs but in practices. Although not synonymous with the laissez-faire State of contemporary 'new right' fiction, the mid-nineteenth century British State embodied an approximation of the liberal ideal - a State in defense of (bourgeois) liberty (Arblaster, 1984).

The British State was distinguished from other States in the social ruptures associated with capitalist development, in being neither absolutist (the Prussians, Russians, etc), nor particularly *dirigiste* (the French). Yet, unlike the textbook version of rampant individual entrepreneurialism, the British economy had had the good fortune of a previous period of assertive state-building (during the sixteenth and seventeenth centuries) on which it could later rest its liberalist laurels.

The mercantilist State gave British industry a solid foundation by which it came to rule the world. In addition, the peculiar character of the British economy rested on its role as an entrepot of finance and commerce (Ingham, 1984). Three key institutions serviced this role, imperceptibly blending private and public power - the Treasury, the Bank of England, and the finance houses of the City of London. These pinnacles of power were offered infrastructural support by the Imperial bureaucracy and the Royal Navy. The touchstones of this rule became the balanced budget, sound money and free trade.

Of course, there was developing gradually a hydra-headed role for the State in the service of 'the economy', embodied in poor laws, work regulation, union recognition and control, mass education, urban infrastructure, and imperial and colonial policy, especially under Tory rule after the 1870s (Jones, 1991). Yet there is a sense in which these developments remained secondary and unintegrated behind the rule of the 'holy Trinity', even when it was clear by the late nineteenth century that British industry was falling behind other competitors (Newton & Porter, 1988). The strength of the City/Treasury/Bank nexus was reinforced in the decaying 1920s with the return to the Gold Standard in 1926 and the formal enhancement of the power of the Treasury over the rest of the civil service. In spite of various incursions into its pre-eminence by Keynesianism, war, 'planning', etc., the dominance of the nexus survives to this day.

On this material base, there is some meaning in interpreting the policy input into the economy only at the macroeconomic level. The notion that industry runs itself and the authorities merely get the 'big picture right' has some reflection in real practice. Policy was predominantly monetary policy, supported by balanced budget

austerity of the Treasury as the keeper of the public purse. The empire was figuratively off-budget, and as long as everybody conveniently displaced the ruinous costs of war from the demands of empire, the empire paid for itself.

*4.2 The generalisations of academia*

The academic economics profession has compounded in dramatic fashion the impoverished treatment of the role of the State. From the early nineteenth century onwards, the long thrust for both social respectability and analytical elegance has led to the construction of a pseudo-science centred on a mechanical view of economic life (Jones, 1992a). Neoclassical economics is the quintessential product of this tradition.

In this process, economists thought intermittently about the role of the State, though it did not unduly tax their minds (c/f Stigler, 1964), even in the post-1870s period of substantial social turmoil. What they did most successfully was to split their musings on the State from their speculations on 'economic man' - hence the distinction between the 'science' of economics and the 'art' of political economy.5

The 'science' of economics purported to be a theory of social order, resolving the anarchy of action of autonomous 'economic man' via the impersonal market mechanism. As such, it became and remains the *raison d'etre* for the 'micro' part of the macro-micro duality. However, it was based on a metaphor stolen from contemporary physics and garnished with a utilitarian version of liberalism. As such it is devoid of insight into real market processes and their trappings of competition, innovation and decay (certainly in Jevonian or Walrasian versions). This fairy tale quality impedes any possibility that the artificial character of the macro-micro divide could be breached from the microeconomic side.

If the early generations of neoclassical economists dealt with the broader role of the State haphazardly and off camera, they also marginalised the core processes of contemporary policy - the machinations of Treasury, the setting of monetary policy, and the administration of Empire. Although the sphere of monetary policy was a hotbed of debate, it was conceptually a minefield of uncertainty and complexity. As such, it was unsuitable for incorporation into the core of the subject (Deane, 1983).

5. Those who wanted to integrate the story into a more coherent if less elegant whole (such as the English Historical School) were gradually pushed to the margins of the discipline.



The early classical economists (notably Smith) were concerned to paint a coherent picture of the whole. What we would put in the 'macro' box was for them the issue of how order was established over the parts - what one might call the *closure* of the system (c/f Lowe, 1965). Smith not merely attempted coherence; he pursued it widely beyond the 'economic' sphere of life. Smith was a social theorist, coming before the destructive compartmentalisation of human behaviour into non-interacting disciplines. Smith found the (macro) closure of the system partly in this wondrous thing called the market. But he also found it in the trappings of the State and of culture (his 'moral sentiments').

After Ricardo and Malthus, the classical economists looked more narrowly to the 'economic' sphere for the sources of macro closure - the population principle, the wages fund doctrine, declining returns to agriculture, etc. Yet each of these ran into trouble as empirically questionable by mid-century. By 1870, Classical economics was on the ropes. The marginal revolution came to the rescue by diverting attention from the important issues, and macro closure was left to depend upon the thin reed of what came to be called Say's Law.

It was in this context that J.M. Keynes arrived on the provincial English scene. Keynes attacked both the policy elite, centred on Treasury, and his intellectual inheritance, centred on (Marshallian) neoclassical economics. The question of the closure of the system had been put to one side, debated at the margin by monetary economists as a specialty. Keynes and others (especially the Swedes - Wicksell, Myrdal, Lundberg), in trying to integrate the 'monetary' and the 'real' economies, put the question of closure back in the intellectual mainstream. At the political level, Keynes helped to break the unquestioned authority of the 'balanced budget' maxim.

Keynes was probably single-handedly responsible for the creation both of the 'macro' preoccupation of the English-speaking economics discipline and of its character. If this was a great advance for a moribund discipline, it was an advance that was flawed from the beginning.

Keynes was steeped in the tradition of Marshall's Cambridge and carried over most of its micro baggage. This occurred partly because he believed in it, and partly because he wanted to hold the attention of his profession. He carried over the wretched marginal productivity of wage determination. Keynes raged against the

destructive influence of the policy triumvirate (Treasury, Bank, City) on British industry and on the integrity of the British economy, but downplayed the implications in his theory. Keynes ignored the dramatic qualitative structural transformation of the British economy since World War I, with the decline of the 'staple' industries (coal, textiles, ship-building) and the belated development of second generation industries (automobiles, chemicals, electronics, construction) (Lowe, 1965:Ch.8; Newton & Porter, 1988).6 Equally dramatic structural transformations had occurred in the United States. This assumption of constant technique, against the evidence, means that Keynes' short-run theory was distortive, even for the short run (Lowe, 1965).

Thus, Keynes' theoretical work was steeped in intellectual and political compromise. Though he railed constantly against the intellectual and political establishment, he was more in than out of both, and he craved both legitimacy and immediate impact.

What Keynes lost in intellectual coherence, he gained in a following. Thousands of (English-speaking) economists joined the Keynesian bandwagon, and precisely because of its compromised character - one foot on more progressive territory, and one foot on traditional pasture. As one of Keynes' most famous devotees, J.K. Galbraith, noted: "Keynes had a solution without a revolution. It seemed a miracle" (quoted in Skidelsky, 1979:58). In short, the channelling of policy considerations into the macro sphere by Keynes, and by later appropriations of Keynes, was a political and intellectual compromise. Later generations are under no obligation to accept its axioms.

*4.3 The absorption of Keynesianism into the macro bureaucracy*

The compromised impact of Keynes and Keynesianism on the post-1945 environment is exemplified in the administrative arena. The major positive impact of the Keynesian 'revolution' is in its weakening of the 'balanced budget' fixation. This enhanced fiscal flexibility - upwards (financing the war) as well as downwards.7 Thus a 'fiscal policy' bureaucracy was gradually created, with a broader range of

6. It is true that Keynes contemplated the 'comprehensive socialisation of investment', of which must has been made by Keynes' left-of-centre disciples. Yet this was a throw-away line in the final chapter of Keynes' *General Theory....*, and sits uneasily with the bulk of his analysis and of his political philosophy.
7. Though a major victory for downwards fiscal flexibility in the USA was not won until 1963, and then for non-Keynesian reasons.



control instruments. The simultaneous development of national accounting systems and statistics boosted the capabilities of this fiscal policy bureaucracy.

Yet the label 'Keynesian' has been applied too glibly to the ascendant fiscal policy bureaucracy. These bureaucracies had priorities other than merely employment-generating deficit spending. An immediate high priority was the management of the war debt. In addition, from the mid-1950s onwards, the enhanced instruments of macro control were used for traditional 'non-Keynesian' ends, essentially that of deflation. Unemployment persisted (albeit at a low level), but inflationary pressures (again by current standards trivial) put deflation at the top of the demand management agenda (Jones, 1989).

This is not surprising, given that the administrative responsibilities for demand management were within the Treasury departments, the traditional homes of pre-Keynesian orthodoxy, and administrative keepers of the public purse.8 The dual roles of budgetary administration and demand management do not mesh coherently. This apparatus was thus well-positioned to retreat to pre-Keynesian values in a fully-fledged manner by the mid-1970s, when Keynesianism was simultaneously denigrated as intellectual rubbish and blamed for the destruction of the long boom. The era of John Stone in the Australian Treasury of the late 1960s and 1970s reflects the re-establishment of the dominance of the old values (c/f Whitwell, 1986).

In short, (English-speaking) economists, with much help from Keynes, constrained debate and analysis of policy to the macro sphere. In the 1970s and beyond, the ideology and politics of the policy debate could be transformed while still being restricted within the macro sphere. Much energy has been expended in elaborating the claims of the so-called 'expansionists' and 'restrictionists', as if these camps represented the full spectrum of opinion and of practice in economic policy.

*4.4 The rise of macroeconomic social engineering*

In the process, a supplementary institutional development has occurred which deserves scrutiny. The idea has developed that the capitalist economy could be *controlled*. This development was decidedly different from a substantial intellectual tradition which had gained momentum at the turn of the century. This

8. The claim that such bureaucracies experienced a 'Pauline' conversion to Keynesianism (c/f Whitwell, 1986) appears much over-stated.

earlier tradition placed its faith in transcending 'laissez-faire' and in the rationalisation of capitalist institutions for greater economic and social stability. It could be found throughout the English-speaking world and parts of Europe, and was of conservative, Christian socialist or neo-liberal ideological origins.9 Its agenda was fairly comprehensive. It sought to rescue capitalist society from an ascendant socialist camp by eliminating the former's flaws, flaws which were compounded by advocates of laissez-faire. Moreover, it sought to transform capitalist society through a understanding of the organic character of capitalist society and how it might be structurally transformed by conscious action on the multitude of social relations which characterised that society. This intellectual movement was coincident with broad enhancement of the State's role, not least because many individuals participated in both the intellectual and the political arenas (Australia's H.B. Higgins being a prime example).

The post-1945 ambition for control took place *purely at the macroeconomic level*. The idea prevailed in academia, in think tanks and in advisory and research arms of the (English-speaking) bureaucracy. It was predominantly an intellectual movement, detached from the bureaucracies enacting a broad range of structural policies across the capitalist world. The phenomenon was common to an otherwise disparate set of individuals and beliefs, ranging through 'bastard' Keynesians, econometric model-builders, and optimal control theorists.

The analysis and ideology behind this development was of a very strange breed. It was not a product of Keynes himself. Keynes' work exerted a strong indirect influence through disciples such as Lawrence Klein. But Klein's sophisticated pragmatism and lightness of touch were rare qualities which became rapidly marginalised in succeeding generations of macroeconometric model-building. The dominant figure-head appears to have been Walras, and his vision of general equilibrium the most appealing (producing short-term diminishing returns and long-run constant returns). The ideological curiosity is that models with implied libertarian politics (e.g. the prominent Australian ORANI model), share a conceptual structure in common (Walrasian general equilibrium) with the main thrust of the contemporary Swedish model-building tradition, steeped in social democratic politics (c/f Eliasson, 1977).10 In this process, the dominant influence is

9. In so far as such individuals had a collective home, they could be grouped within the English Historical School, the English radical Liberal philosophers, the German Historical School, the American institutionalists, and the Australian liberal-labour political movement at the turn of the century.
10. There exists a possible filial relation between the Swedish model-building tradition and the ORANI model. The development of ORANI was instigated and



technocratic. The sub-discipline was increasingly staffed by refugees from physics and mathematics (c/f Epstein, 1987). There was resurrected the metaphor of the economy as a machine, and the structure of the economy was to be appropriated, at best, through statistical indices of dubious quality.

Thus arose the notion that one could control a capitalist economy purely at the macroeconomic level through the development of sophisticated techniques while simultaneously avoiding a patient examination of detail. The ideological ambiguities of this development may be cause for amusement, but the limited success of the enterprise's agenda is of real political consequence. The recent failure of the federal Treasury to proffer a reasonable approximation to the economy's short-term trajectory has led to public questioning of the relative merits of particular forecasting models and of the merits of macroeconometric model-building in general (c/f Murphy & Wallis, 1992; Mills, 1992). But the peculiar tradition which has produced such anomalies remains unquestioned.

## 5. THE IMPLICATIONS OF THE MACRO-MICRO SPLIT

The macro-micro split has a range of adverse implications, several of which are discussed below. They include:
- a restricted understanding of the intricate relation between 'market' and the State in capitalist economies;
- an inflated expectation of the capacity of central banks by themselves to instil a low-inflation regime;
- a misunderstanding of the character of the annual budgetary process and its capacity to facilitate economic reconstruction;
- a continuing contribution to the disarticulation of structural policies which are enacted by governments, regardless of the antagonism expressed towards them in academic and some business circles.

### *5.1 The hidden nexus: the market and the State as organically intertwined*

financed by the federal Department of Employment and Industrial Relations in the mid-1970s. The Department, whose philosophical centre of gravity was sympathetic to the Swedish social 'model', was fearful of adverse employment effects emanating from the 1973 tariff cuts. The Department sought a 'rigorous' procedure for estimating such policy influences - hence the birth of the ORANI model.

The historical 'market' is a social construct. It is a fragile institution, of necessity because it harnesses forces engaged permanently in the process of pulling it apart. The market is everywhere underpinned by culture and the State (Jones, 1991). The functioning of the market regularly falls apart (popularly called depression/recession) and has to be reconstructed; as does the symbiotic relationship between market and State. As the market is global and the State presides over a spatially and politically constituted national economy, 'competition' has to be understood as occurring in a multidimensional framework between both individual capitals and political entities (most typically nation states).

In this process of economic reconstruction and sustaining of the market in the competitive process, the crucial role of the State takes place at the level of structural detail. The policy workhorse of industrial dynamism is to be found in discriminatory industry policies.11 This point cannot be over-emphasised, because it is so consistently ignored by economists. Structural policies cannot be comprehended within the dominant macro-micro split. If one wants to comprehend the character and evolution of capitalism and the role of the state in that process, the macro-micro bifurcation in its current form has to be abolished.

This phenomenon is no better reflected than in the long boom following 1945, the great success story in the history of capitalism. The grand myth is that the boom was created and sustained by (macro) demand management (Jones, 1989). This is a grand fiction. In so far as there was a big picture, it was put in place by the US State and capitals in the construction of *Pax Americana*. The rest of the story was provided by assertive and systematic discriminatory industry and trade policies. The motive was the relief of the massive distress caused by depression and war, and an electoral mandate existed for such policies. Non-English speaking countries, less constrained by the institutional manifestations of liberalism, were the more assertive in discriminatory policy and the more successful in their industrial dynamism (c/f Shonfield, 1965; Hall, 1984; both compare UK developments with those in West Germany and France).12 Ironically, the USA greatly facilitated this comprehensive industry policy regime both in Europe and in Asia (contrary to its formal liberalist ideology) as a means of providing an economic bulwark against presumed Soviet expansionist tendencies.

11. This case is argued at length, with supportive literature, in Jones (1987) and Jones (1991).
12. Even in the UK, there were developments in industry policy addressed to structural decay. Yet these developments are consistently ignored by economists, and their inhibited implementation consistently ignored by later policy-makers (c/f BBC, 1992).



There has since arisen the view that the role of Government in the post-1945 boom has been universally counter-productive. The structural elements of Government policy, ignored by Keynesians, have ironically been re-discovered but on a selective basis. They are now blamed, along with excessive (macro) pump-priming, as the cause of the end of the long boom. In the Australian case, the erection of 'protection all round' and the range of regulations over the banking sector have been held up as exemplars. It has also been held, especially by mainstream observers of the European experience (notably the OECD), that the dominant role of Governments after the boom's demise was in propping up declining industries.

Both views are erroneous, but they support the libertarian vision that the way out of the post-boom impasse is to get Government out of the way and let the natural cleansing powers of the market mechanism get on with the business of restoring profitability and prosperity. When the world doesn't conform to the view through the macro-micro spectacles, then the world has to be changed to fit the myth.

*5.2 An important case study: the central bank as politicised?*

One particular manifestation of this vision deserves special attention. This concerns the institution of the Central Bank and the presumed political influences on its operation. There is a much-publicised view that the Reserve Bank of Australia is too politicised.13 It is said that the Reserve Bank needs to assume the (presumed) independence of the West German Bundesbank if it is to carry out its first priority, the minimisation of inflation. This view has also become the official policy of the federal opposition coalition parties in their bid for federal office. The draconian 'inflation-first' policy of the central bank of New Zealand has been held up as an exemplar.

This is a peculiarly dangerous view. It harks back to a mythical golden age in the nineteenth century (an undemocratic age) when the Bank of England, with the aid of the gold standard, ruled monetary policy on a short leash. In a sense, the push for an independent central bank has religious overtones - the dream of a universal standard for a monetary regime controlled automatically by impersonal forces. There are two other ingredients in this view.

13. The Sydney Morning Herald columnist, Max Walsh, is representative of this schoolof thought.

The first ingredient is an ill-informed understanding of the real-money nexus in a capitalist economy. The 'central bank independence' line draws on a monetarist-type interpretation of the causal autonomy and primacy of the money supply. By restraining credit, one restrains excess demand, thereby restraining inflation (although there is a grab-bag of possible causal links within the Monetarist camp - c/f Nell, 1984). This conceptual framework is a predictable by-product of economic analysis through 'macro' spectacles. It presumes that the micro-economy works purely through price-driven market-clearing processes. In flesh-and-blood economies, prices are set by a complex mutual interaction between the 'real' and the 'money' sectors of the economy. Amongst economic agents, especially those in the concentrated core of the economy, prices are influenced by strategic considerations and are subject to considerable discretion. The monetary authorities have to make delicate decisions with limited means (the monetary instruments at their disposal) as to the preferred balance of priorities between inflation, employment and the structural composition of the economy. That balance is in turn influenced by the contemporary policies of other Government authorities. Inflation is not a technical problem to be resolved by mechanical means. The bailiwick of central banks involves an innately political exercise - to claim and demand a non-political central bank is nonsensical.

The second ingredient, one infers, is a vested interest in a particular outcome. Finance sector spokespersons have generally preferred low inflation outcomes, and are apparently unconcerned with the effect that a inflation-obsessed central bank will have on employment or on industrial structure. Finance sector spokespersons thus have no interest in an adequate interpretation of the inflationary process.14 To employ macro-econometric language, they are interested in 'reduced form' analysis and solutions. It is noteworthy that these interests should have received substantial uncritical attention - a finance sector world-view (essentially global and libertarian) generally dominates the Australian economic press. John Hewson, whose education and professional experience lies solely within a global finance sector purview, is representative of this world-view.

14. The 'independent central bank' push is also instrinsically anti-democratic. This is consistent with the anti-social implications of the charter. The label 'populist' is consistently used by Max Walsh and other economic columnists to denote broader attempts to ensure accountability of the central bank, with these attempts being consistently decried.



The limitations of this vision are embodied in an ignorance of the sources of dynamism in capitalist economies. Implicit in the vision is a 'scorched earth' interpretation of competition and the appropriate groundwork for innovation. This component is equally ahistorical. Ironically, West Germany itself supports a counter argument. The West German Bundesbank is held by the 'independent central bank' push as the example to follow. The presumption is that it is the Bundesbank's austere credit regime which has produced the German miracle. On the contrary, the miracle has been produced by a combination of forces, not least an underlying material support from *Pax Americana*. Bundesbank austerity has combined with a nation-specific set of private sector institutions and culture (quite different to those prevailing in Australia), and an assertive discriminatory industry policy (c/f Shonfield, 1965: Chs.XI,XII; Hall, 1984).

*5.3 The annual budgetary process: myths and reality*

The long-term elevation of the 'macro' perspective, integrally coupled with inattention to the sources of industrial dynamism, has led to peculiar anomalies at the macro level in Australia. Key economic events have become rituals, the meaning and significance of which are little understood.

Key among the macro rituals is the annual federal budget. The budget is presented, under the rubric of 'fiscal policy', as if its prime object is as an economic *strategy* document. Major emphasis is placed upon the deficit/surplus as a measure of the degree of fiscal stimulus/restraint. Extravagant promises are made by the federal Treasurer of the expected turn-round following the budget's implementation. Yet the budget is a balance sheet (Jones, 1992b). As such, it ought to be delivered by the Minister of Finance. The budget is only indirectly a vehicle for fiscal policy (tacitly understood as the prime vehicle for short-term macro demand management), and even more indirectly the reflection of strategic intent. As a balance sheet, the budget's prime responsibility is the reconciliation of the Government's economic and social priorities with its revenue options.15 There are two predictable confusions in the understanding of the annual budget - financial accounting is confused with demand management; and (macro) demand management is taken as being synonymous with the government's broad responsibility for economic reconstruction.

15. This confusion is classically reflected in the textbook of Parkin & Bade (1986:663) in which they assume that the social welfare policies of several governments are merely a facet of 'fiscal policy' or demand management manipulation.

The budget certainly has complex implications for the prospects of economic revitalisation, as it includes multiple appropriations for various contributory programs - job creation, investment subsidisation, etc. Yet the overall economic impact of the budget is incidental to the main point of the exercise - the gross financial implications of the programs. The incidental relation between the August budget and economic policy is highlighted by the fact that continued economic deterioration has forced the Government to devise policies within a recognisable 'statement' to stem the deterioration of both the real economy and the Government's reputation. Hence the creation of the March 1991 Statement and the February 1992 (*One Nation*) Statement.

These statements, unlike the August budget, are genuinely policy-oriented. It needs to be emphasised that these statements are not mini-budgets, and they are not constructed because the forecasts/predictions from the August budget turned out to be wrong. The *One Nation* statement and its 1991 predecessor are qualitatively different animals. They are strategic documents in that finance is subordinate to policy (the reverse is the case with the annual budget). They are very poor strategic documents, insofar as they are constructed in appalling haste. Moreover, their status in terms of the commitment of the Government to their implementation remains dubious, because much of the relevant negotiations remain to be carried out at the time of delivery. Nevertheless, their status remains qualitatively distinct to that of the annual budget.

The move from the so-called Keynesian age through the monetarist age and beyond has not changed the emphasis on the macro sphere. Indeed, the current anti-Keynesian age has merely appropriated some of the Keynesian conceptual apparatus and all of its policy apparatus. As both were already compromised this was hardly a problem. The macro demand management functions of the 'Keynesian' age were accrued by the pre-Keynesian central departments of national bureaucracies concerned with the budgetary process. In this long pragmatic accretion of new ideas and policy instruments to old institutions, the centrality of the budgetary process itself has remained. The presumption that these old forms were now being used for major deliberations for economic revitalisation has been a long-term delusion.16

16. This ambiguity of purpose is tangibly embodied in the brief of the federal Treasury. The mechanics of the traditional budgetary process have been displaced within the Department of Finance, carved out of Treasury. Yet Treasury's philosophical centre of gravity still remains muddled because it cannot clearly distinguish between the financial aspects of running a public service, and the policy aspects of running an economy.



The limitations of the annual budget generates a messy and costly state of affairs. Predictably, some of this inefficiency is due to the inevitable 'muddling through' that accompanies the policy process in 'democratic' societies. Yet there is something special about the Australian version. Much of the impasse has to do with a preoccupation with the 'macro' economy.

The over-emphasis on macro policy to the neglect of structural policy means that macro policy cannot sustain the demands made upon it. This is transparent in the disastrous effects on the economy of the 1988-9 credit squeeze.17 A discussion of this period merely in terms of an optimal policy mix of macro policy instruments (combined with 'level playing field' micro policies) is analytically limp and politically inept. The British have best exemplified the inadequacies of macro policy by producing a post-1950 period of endless episodes of 'stop-go', with disabling effects on the stability needed for a vibrant industrial culture.

There is inadequate appreciation for the fact that every element of policy addressed at the aggregate (macro) level has structural (micro) effects. No systematic attention is paid to the structural impact of 'macro' policies.18 As soon as the policy-making apparatus steps onto this path, the primacy of the macro level would have to give way before that of the structural level. To quote Postan, referring to the 1960s U.K.:

> "And for many (perhaps most) of these local ailments the morbid causes will be found not in the malfunction of the life processes in the body economic, such as the low rate of savings, or the high level of prices, or the insufficient allocation of national resources to research and development, but to specific failures of its individual cells - management, design, salesmanship, or the behaviour of groups of labour. For these morbid causes systemic medicines are an irrelevant, and sometimes even a harmful, prescription. ...

17. Finance media remonstrations that the problem with monetary policy was not that it was too draconian but that a period of austerity was implemented too late following a softening after the October 1987 crash. This criticism fits entirely within the macro mind-set, and is no more intelligent than the policy it criticises. As the monetarists themselves claim, a discretionary macro policy is bound to fail of necessity. The move to greater dependence on the price of credit rather than its quantity as a rationing device following deregulation enhances the volatility of macro monetary policy and compounds its weakness in dealing with structural crises.
18. This is also a problem for a Marxist analysis which has sought to interpret the State as the embodiment of the interests of collective Capital, when every act of the State involves an interposition between particular capitals (Mandel, 1975:480).

> What [theoretical aggregates] do not and cannot do is to locate the points at which the body ails and to suggest the proper treatment for the ailment. For this a wider range of *expertise* and a wider choice of experts are needed: technicians in industry and in contact with it, industrial consultants, sociologists, and those business men who happen to know their businesses, as well as economists." (Postan, 1968:44)

The emphasis upon macro policy to the neglect of structural detail produces another peculiar effect, a product of the macro 'social engineers'. It requires a dependence on prediction of aggregate indices with little feeling for the components which make up the aggregates. As noted above, the federal Treasury has come in for considerable criticism in the last twelve months because of the poverty of its predictions of the aggregate economy. The task has to be performed, but the innate weakness of the project means that it cannot support the policy demands presently made upon it.

Thus policy in Australia is centred on (macro) control without understanding. In the smart capitalist countries, their orientation is *strategic*: control involves a more flexible adaptation at the point of the problem, and the macro policies (at best complementary) are charged with a lesser responsibility. Their policies are relatively proactive and preemptive rather than passive and reactive.

*5.4 Structural policy as inevitable: under the table or on the agenda?*

The long Anglo-American emphasis on the macro sphere as the sole province for economic policy has not prevented the pursuit of structural policy. It has merely pushed such policy to the margins of the policy-making hierarchy and compounded its tendency to incoherence (Jones, 1987). Bureaucratic opinion-makers constantly rail against structural policy. The economic columnists generally ignore it.19

This gap between the ideal and the reality has been bridged in the USA and the UK by the 'military industrial complex'. Under the guise of national security, in which the normal rules of 'free market' economics were allowed to be broken, US and UK Governments have carried on active and overarching industry policies whose structural effects on their economies have been profound (c/f Markusen, 1991).

19. That is, except when it takes the form of the protective tariff, in which case it takes on a demonic character and any sensible treatment becomes impossible.



In Australia, a significant role in this unheralded phenomenon (the structural policy you have when you're not having a structural policy) was played by the states; and within the states by the public utilities. This major role for the utilities (especially that of the power authorities) produced a certain political autonomy. This autonomy in turn produced the excesses which came home to roost in the 1980s, although the blame must be more widely attributed. The utilities have been the black sheep of the policy family, having to do much of the structural work with little coherent institutional support (and hence control).

Which institutions might replace or supplement the reconstructed utilities in this role is yet to be seen. There is a budding military industrial complex in Australia vying for the position (in particular, the submarine and the frigate projects, and aerospace components), for similar reasons as occurred in the US and the UK. Some of the sectoral plans (steel, heavy engineering) have had positive if constrained effects. The Australian Manufacturing Council is quietly building a more viable constituency in the manufacturing sector.

However, all such developments remain strictly constrained and marginal to the dominant policy focus. Major documents proposing a general policy U-turn have been vilified and subsequently ignored (c/f Metal Trades Unions, 1984). The federal policy 'establishment' and the major economic columnists remain firmly committed to the world-view of the macro-micro split. Indeed, Mr Hewson, the likely next Prime Minister, is formally committed to eliminating the pockets of resistance, and purifying further the traditional vision.

The macro-micro split is a fiction. It is an artifice transformed into a universal construct by which its partial relevance and its ideological roots are lost. Its continuing dominance inhibits our understanding of our society and its changes, and inhibits our ability to control that society for socially-determined ends. The macro-micro split is a key feature of a profession which has ceased to contribute to a humanising ethical tradition (as Keynes for one intended) and is instead contributing to its antithesis.

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