CRISES AND RECESSION AS THE NORM

John Quiggin

The coronavirus pandemic has been described as a ‘once in a hundred years crisis’, and, in a literal sense this is true. The last comparable disease outbreak was the influenza pandemic of 1919, commonly referred to as the ‘Spanish flu’ though it was actually spread among, and by, the armies of the Great War, first in trenches and field hospitals and then on their return home.

The reality, however, is that economic crises are part and parcel of capitalism. Since the resurgence of neoliberalism in the mid-1970s, events described as crises, crashes or recessions include the mining boom and bust in Australia (1979-83), its ‘banana republic’ crisis (1986), the stock exchange crash of 1987, the ‘recession we had to have’ (1989-91, with effects persisting into the mid-1990s), the Asian financial crisis (1997), the dotcom bubble and bust (1999-2001), the Global Financial Crisis (2008-9, with effects continuing to the present), and now the pandemic.

Despite this record, neoliberal economic policy relies critically on the assumption that capitalist economies are inherently stable. In this sense, classical/neoliberal economic management is like the way Australia historically approached drought (and the National Party still approaches it). Rather than seeing drought as part of the inherent variability of the Australian climate, the possibility of drought was disregarded in ‘normal’ times, and presented as an unforeseeable natural disaster when it occurred. The result was to encourage unsustainable practices such as overstocking. When the inevitable drought occurred, images of starving and dying animals produced an emergency response which effectively rewarded poor management.

The same is true of neoliberal economic policy. Institutions such as financial markets, and policies such as privatisation, are evaluated on the

Quiggin, J. (2020)
‘Crises and Recession as the Norm’
Journal of Australian Political Economy
No. 85, pp. 39-43.

basis of whether they can outperform the public sector under ideal conditions of full employment and economic stability. The fact that they regularly require bailouts in times of crisis is ignored. As a result, they pursue policies that make them, and the economy, even more vulnerable, on the assumption that governments will pick up the pieces when something goes wrong.

In all of the crises of the past 50 years, governments and central banks have acted to mitigate the impact of the crisis, sometimes successfully and sometimes not. As soon as the economy recovered, however, the dominant assumption the crisis represented a once-off shock and that the recovery was a return to normality. Indeed, in the early 2000s, future US Federal Reserve chairman Ben Bernanke popularised the idea of a 'Great Moderation', representing a reduction in the variability of economic growth and unemployment. This idea generated a stream of research articles and opinion pieces, growing in volume of confidence until it was rudely interrupted by the GFC.

This pattern of regular crisis is not specific to the era of market liberalism (or neoliberalism) that began in the late 1970s. Rather, with the exception of the three decades after 1945 (to be discussed below), recessions and crises have been the norm, and sustained periods of stable growth the exception.

Monitoring crises

The most consistent set of data on economic crises is that of the National Bureau of Economic Research, originally established in the 1920s to study business cycles. Although the NBER as a whole has long been absorbed into mainstream economics, its Business Cycle Dating Committee continues to monitor the fluctuations of the US economy, announcing (with some time lag) the beginning and end of US business cycles.

The NBER estimates go back to 1854, and may usefully be divided into three parts: the period 1854-1939; the Keynesian period from World War II to the end of the Bretton Woods system of fixed exchange rates in 1972, and the period of neoliberalism from 1973 to the precent

In the 1854-1939 period, 'classical' economic policies based on budget balance and the gold standard prevailed until the catastrophe of the Great Depression brought them to an end. According to the NBER estimates, contractions and expansions were about equally long, so that the economy was in recession a little under half the time.

However, this classification is, in critical respects, an underestimate. In deep depressions, economic weakness persists long after the end of the contraction phase. At least from the perspective of labor markets, it would make more sense to treat the recession as continuing until the economy returns to full employment and the pre-crisis growth path. On this basis, we derive the common sense that the whole of the Great Depression should be treated as a recession, which implies that the US economy was in recession for more than half the years from 1854 to 1939.

Although there is no comparable data series for Australia, it seems clear that the same result would hold true for the period from the late 19th century (when industrial capitalism was first established) to 1939. From the crisis of the 1890s, which led to the establishment of the Australian Labor Party, to the outbreak of war in 1939, depressed conditions were the norm rather than the exception.

The only period of sustained economic stability and widely-shared prosperity in the economic history of the United States and other leading capitalist countries came during the three decades after 1945, when a combination of Keynesian macroeconomics, social democratic domestic policies and the Bretton Woods system of fixed exchange rates prevailed.

At that time, the causal relationship seemed clear. Keynesian economics had, it seemed, not only provided a theoretical explanation for the instability of capitalist economics, but had shown that this instability could be remedied through government policies based on the maintenance of full employment.

It took only a single economic crisis to see this analysis abandoned in favour of a return to classical economics, initially in the form of the monetarist theory advanced by Milton Friedman. From the late 1960s onwards, inflation accelerated, while unemployment rose to 9 per cent in the United States, and 6 per cent in Australia. These rates were considered catastrophic at the time, but have regularly been surpassed in the era of market liberalism. For the US, unemployment exceeded 10 per cent in the early 1980s, in the aftermath of the GFC and again with the onset of the pandemic.

The resurgence of market liberalism in the late 1970s was followed my major global economic crises in the 1980s and 1990s. These events were treated as after-effects of the presumed failure of Keynesianism and as part of the process of adjustment to a newly liberalized economy. Similarly, the developing country crises of the 1990s were blamed on inadequate liberalization and crony capitalism.

These assumptions were dramatically falsified when the Global Financial Crisis emerged from Wall Street, home of the most sophisticated financial markets in the world, where state-of-the-art regulation was supposed to prevent cronyism and corruption. There was a brief attempt to reimpose some regulation through legislation such as the Oxley-Sarbanes Act and stress testing of financial institutions, but nothing fundamental was changed.

Worse still, as soon as the crisis was past, policy switched to austerity measures, with cuts in education, health care and other services. Among the cuts were the abandonment of seemingly non-urgent expenditures such as preparedness for pandemics. The deeper the cuts, the worse has been the impact of the pandemic.

What's different this time?

While the GFC was generated within the financial system, the coronavirus pandemic has been an externally generated shock. If the GFC demonstrated the potential of financial markets to generate economic crises, the pandemic has demonstrated their irrelevance in resolving them. Financial markets are supposed to be forward looking, with highly skilled professionals paid to assess the future prospects of assets of all kinds. Yet long after the coronavirus was front-page news, financial markets took no account of their likely impact outside China. The US Standard and Poors index reached an all-time high on 21 February 2020, before losing nearly a third of its value. Massive handouts to business have revived share prices, but done little or nothing for the US economy.

As Krugman (2020) observes,

> We've learned that advanced economies are much less stable, much more subject to periodic crises, than almost anyone believed possible.

Yet this 'learning' has had hardly any effect on stock market valuations. The crucial lesson here is not simply, as Krugman puts it that 'stock markets are not the economy', but that any economic policy that relies on these markets to guide investment is doomed to disaster. Yet reliance on financial markets is central to the market liberal ideology that has held sway since the 1970s.

The repeated crises of the 21st century have demonstrated that it is democratic governments, and not markets, on which we ultimately rely for our security and prosperity. A radical change in economic policy was needed after the GFC. It is needed even more now. Attempting a snapback to the *status quo ante* would be a recipe for disaster.

The starting point for these changes should be a renewal of the public commitment to full employment and financial stability that prevailed in the era of Keynesian social democracy. This entails a drastic reduction in the size, influence and profitability of the financial sector, which should be returned to the status of a dull and stable public utility.

Looking to the future, the resetting of economic activity due to the pandemic gives us a chance to return to the path that seemed to lie before us in the middle decades of last century, a path in which we could be free of the incessant demands of the market, while still enjoying a comfortable and prosperous life. I've described some ideas along these lines in various writings, such as Quiggin (2019). Steps along the way would include reductions in working hours, broadening the social welfare system with the aim of providing everyone with a 'participation income', and an end to gross inequalities of all kinds.

John Quiggin is Professor in the School of Economics, The University of Queensland.

j.quiggin@uq.edu.au

References

Krugman, P. (2020), 'Crashing Economy, Rising Stocks: What's Going On?, *New York Times*, 30 April, *https://www.nytimes.com/2020/04/30/opinion/economy-stock-market-coronavirus.html.*

Quiggin, J (2019) Socialist utopia 2050: what could life in Australia be like after the failure of capitalism? *Guardian 17 Jan* https://www.theguardian.com/politics/2019/jan/17/socialist-utopia-2050-what-could-life-in-australia-be-like-after-the-failure-of-capitalism.