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Contemporary Macroeconomic Outcomes: A Tragedy in Three Acts

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Abstract

The thesis developed in this paper is that contrary to the claims of its proponents, the main supply-side consequence of neoliberalism was to zap labour, institutionalize worker insecurity, and install an ‘incomes policy based on fear’ in the US economy. Like any successful incomes policy, this diminished conflict over shares of real income and so reduced inflationary pressures – but at the cost of decoupling real wage growth from productivity growth. This last outcome fueled rising income inequality and hollowed out the wage-funded, consumption-led core of the demand-generating process. The demand-side weakness of the neoliberal economy was initially concealed by household borrowing that debt-financed increases in autonomous consumption spending. But it has asserted itself in the wake of the Great Recession, following the exhaustion of the household debt accumulation process. The result was a depressed upswing 2009-2019 that addressed none of the fundamental structural weaknesses evident in the US economy prior to the Great Recession. The institutionally entrenched but exhausted neoliberal paradigm left the US unprepared for the onset of recession in 2020, and for the larger social and economic travails of the COVID-19 pandemic with which the initial onset of the 2020 recession was associated.

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1 Introduction

After years of basking in the glow of the ‘Great Moderation’ or NICE (non-inflationary, continuous expansion) era, academics and policy makers alike in the US and UK – the epicenters of the post-Thatcher/Reagan 1990-2007 Neoliberal Boom – were taken aback by the sudden onset and subsequent calamity of the financial crisis and Great Recession in 2007-09. They should not have been. The crisis was, to a substantial extent, the product of two trends in neoliberal capitalism that have already been discussed in this book: financialization and increasing inequality. The link between these trends has already been anticipated in chapter 4, where it was shown that the process of financialization has contributed to rising inequality over the last 3-4 decades. A key focus in this chapter will be the reverse line of causality, according to which increasing inequality contributed to financialization – more specifically, the financialization of the household. Focusing on the US economy, we argue that this sequence of events constituted a ‘three act tragedy’. The much-vaunted supply-side economics promoted in the 1980s (Act I) ‘reformed’ the supply side of the economy, but in a manner that served chiefly to weaken the bargaining power of labour. Apart from suppressing conflict over the distribution of income – an important modification to the dynamics of the Marx-Keynes-Schumpeter (MKS) system that has had implications for the Goodwin pattern – this development also hollowed out the core of the demand-generating mechanism in US capitalism. This it achieved through the (still ongoing) destruction of middle-class incomes that has forced American households into a new era of debt-dependency (Act II). The continuing negative consequences of these developments for macroeconomic performance are evident in the long but relatively weak recovery from the near-depression that was the 2007-09 financial crisis and Great Recession (Act III).

As will already be evident from the foregoing, we view the 2007-09 crisis as a crisis of realization rather than the result of a classical profit squeeze – a situation where, consistent

with the consequences of supply-side economics as intimated above, workers were ultimately ‘too weak’ rather than ‘too strong’. Our analysis in this chapter takes on a distinctly Keynesian flavour, then, the focus throughout being on the recent process of demand formation in capitalist economies. Particular attention is paid to the interplay of growing inequality, emulation effects, the erosion of social provision, household debt accumulation, and the evolution of household consumption spending over the course of the Neoliberal Boom. The unsustainability of these processes was demonstrated by the onset of the financial crisis and Great Recession, but their structural ‘drivers’ remain in place, suggesting that neoliberalism is an exhausted growth regime that nevertheless remains institutionally entrenched. This observation leads directly to our explanation for the problems that have continued to beset the US economy since the end of the Great Recession. Despite appearances to the contrary (seemingly record low levels of unemployment), the US experienced little more than a depressed upswing after 2009, which has addressed none of the fundamental structural weaknesses associated with high and rising inequality that were evident prior to the Great Recession. This left the economy unprepared for the onset of recession in 2020 and for the larger social and economic travails of the COVID-19 pandemic with which the initial onset of the 2020 recession was associated.

A second and perhaps equally self-evident feature of this chapter will be its focus on developments and outcomes in the US economy. Our US focus is justified by the fact that the US economy – together with the UK – is the ‘leading edge’ of neoliberalism, and has been since the Thatcher/Reagan revolutions of the early 1980s. This does not mean that the analysis that follows is of no significance for other economies, however. On the contrary, the recent fate of the US economy provides an indication of what is in store for European economies, and even middle-income economies in Latin America and elsewhere, if they are unable to articulate and adopt a vision of sustainable and inclusive growth. This observation is all the more important given the hegemonic role of the US among advanced capitalist

economies.

The remainder of the chapter is organized as follows. We first take up Act I of the tragedy (neoliberal supply-side economics), which is characterized as a process of ‘zapping labor’ – restructuring the labour market so as to disempower workers – in order to create an ‘incomes policy based on fear’ (Cornwall, 1990).¹ This is shown to have re-structured class conflict in a manner that explains the recent ‘breakdown’ in the Goodwin pattern discussed in chapter 1. Next, the unintended demand-side consequences of neoliberalism are presented as Act II of the tragedy. This involved growing inequality promoting the financialization of households, resulting in both increasing household indebtedness and an unsustainable process of demand formation. Act III brings us to the neoliberal inheritance, or, the macroeconomic consequences of an institutionally entrenched but exhausted growth process – the consequences of which continue to haunt present-day realities. Finally, we relate the account of recent macroeconomic outcomes provided in this chapter to the apparent ‘breakdown’ of the Goodwin pattern discussed in chapter 1, showing that this ‘breakdown’ can be properly explained by the transformation of distributional conflict inherent in the MKS system during the neoliberal phase of growth.

2 Act I – The supply side during the neoliberal era

According to its progenitors, neoliberalism would work by freeing the private sector from the fetters of the state and revitalizing the supply-side of the economy. In particular, the labor market would be made flexible: disincentives to work such as taxes and benefits would be lowered, and impediments to wage adjustment, such as trade unions and minimum wage legislation, would be curtailed or removed. The result, it was promised, would be more jobs,

¹The term ‘zapping labour’ was introduced by Welch (1976) and was used by (Harrison and Bluestone, 1988) to characterize the labour market restructuring processes characteristic of neoliberalism. The details of this restructuring will be outlined below; for a retrospective assessment of (Harrison and Bluestone, 1988), see Peck (2002).

faster growth, and hence a healthier economy overall. Even the increased inequality associated with the initial changes to the structure of taxes and social benefits would eventually be offset as output gains ‘trickled down’ to those at the bottom of the socio-economic scale.

Using standard statistical benchmarks, macroeconomic performance did, in fact, improve in the US after 1990, as compared to the previous two decades. As the first two rows of table 1 make clear, the first full business cycle of the neoliberal era (1990-2000) re-established the low average rates of unemployment and inflation last seen towards the end of the post-war ‘Golden Age’ (represented by the period 1960-73 in the first column of table 1).² This improvement in macroeconomic performance did not occur because of the effects of neoliberalism as envisaged by its progenitors, however. Instead, changes to the supply-side of the economy during the 1980s constituted a process of ‘zapping labor’ (Harrison and Bluestone, 1988). Post-1980 changes in public policy that claimed to make labor markets more flexible, together with various contemporaneous changes in corporate behavior, all succeeded in markedly increasing *worker insecurity*.³

These changes included labor law ‘reforms’ that, among other things, made unionization by workers in the US more difficult and de-unionization by firms easier (Block et al., 1996). The result, not surprisingly, has been a precipitous drop in the rate of unionization in the US, from a post-war peak of about 35% to 20% by the early 1980s to just 10% by 2020.⁴

²Note that the focus in table 1 is on the *transition* to the Neoliberal Boom. The *continuation* of some of the developments brought to light in table 1 during the current millennium is a topic to which we will return in section 6.4 below.

³It is important to note that the institutional changes discussed in what follows are not the only major structural change that has characterized the neoliberal era. Instead, all advanced capitalist economies have witnessed the continuation of longer-term trends towards deindustrialization and the rise of the service sector. Deindustrialization is of significance not only because of its contribution to deunionization (as noted below), but also because of its direct effect on the rise of inequality. Hence the low productivity/(near) zero productivity growth that characterizes so-called ‘stagnant’ service sector industries (Baumol et al., 1989) means that not only are these industries labour-attracting (employment must grow rapidly as output in these industries grows because of the lack of productivity growth), they are also low wage/(near) zero wage growth industries by virtue of their low productivity/(near) zero productivity growth character. The direct contribution of deindustrialization to the growth of inequality will not be discussed further in what follows, but see, for example, Mendieta-Muñoz et al. (2020).

⁴The rate of unionization in the private sector of the US economy dropped to just 6% by 2020, union

Other changes included increases in ‘non-standard’ (i.e, part time and/or temporary) employment, that eroded the post-war norm of employment constituting year-round, full-time work. This gave rise to the phenomenon of ‘involuntary’ part-time/temporary employment (a counterpart to involuntary unemployment) as a form of under-employment. The introduction of periodic ‘downsizing’ exercises by firms, meanwhile, created the credible threat of job loss independently of general economic conditions (Osterman, 1999). Worker insecurity was further enhanced by the emergence of a credible threat (on the part of firms) to relocate production between political jurisdictions. This threat of plant relocation began as a domestic phenomenon that witnessed the migration of industry within the US from traditional industrial areas in the north-east and mid-west to southern and south-western states. It then took on an international dimension thanks to the pro-corporate form of ‘globalization’ encoded in various international trade agreements. The latter contributed to the creation of an international institutional environment that makes little or no reference to labor standards, thus exposing domestic workers to competition from low-wage foreign workers, not only as a result of the internationalization of product markets, but also by enhancing the credibility of the threat of plant relocation. Together, these developments have transformed ‘trade’ from a mid-twentieth century competition between firms, involving product innovations and productivity-enhancing process innovations, into a contemporary competition between *political jurisdictions* to attract footloose corporations, on the basis of tax reductions and denuded environmental and labour standards.

The combined effects of these various facets of the process of zapping labor are dramatically evident in the final row of table 1. This reports an index of worker insecurity based on numerical measures of the various phenomena described above. This index rises precipitously during the 1980s and 1990s, as the institutional architecture of the neoliberal economy first emerged and was then consolidated.⁵

representation in the US being much greater in the public sector.

⁵Details of the calculation of this insecurity index can be found in Setterfield (2005) and Setterfield and

Table 1: US Macroeconomic Performance, 1960-2000

	1960-73	1974-79	1980-89	1990-2000
Unemployment	4.9	6.8	7.3	5.6
Inflation	3.1	9.6	5.6	3.1
Wage share	57.4	59.1	58.4	57.7
Interest rate	4.77	7.67	9.97	5.24
Worker insecurity	N/A	0.21	0.57	0.82

Source: Setterfield (2006)

The process of zapping labor described above made the neoliberal economy work by instituting an ‘incomes policy based on fear’ (Cornwall, 1990) – a ‘model of domination in which conflict is ameliorated essentially by means of coercion and in which the costs of ... [reducing] distributional conflict ... fall squarely on the shoulders of workers’ (Setterfield, 2007, p.144). Workers were first disempowered in the manner described above. This reduced their ability to bargain for nominal wage increases, lessening their capacity to either seek improvements in their standard of living or even increase wages in the face of rising prices in an attempt to protect their existing standard of living – an outcome that, *ceteris paribus*, lowered the real wage and hence the wage share of income.⁶ Since any increase in nominal wages results in an increase in the costs of production that may be passed on in the form of higher prices, the disempowering of workers under the incomes policy based on fear reduced underlying inflationary pressures in the US economy. Not only could workers not *initiate* an

Lovejoy (2006).

⁶In the presence of labour-saving technological change, any failure on the part of workers to bargain for real wage *increases* that keep pace with the rate of increase of productivity will, of course, have a similar effect, lowering the wage share of income. The relationship between the wage share and the rate of productivity growth is analysed in greater detail below.

inflationary process (by bargaining for higher nominal wages despite corporate resistance to increases in the real wage), neither could they *propagate* an inflationary process by seeking to defend their standards of living against price increases resulting from, for example, commodity price ‘shocks’.⁷ These developments are clearly seen in the second and third rows of table 1 where, following their rise during the 1970s, inflation and the wage share fell during the 1980s and 1990s.

By relieving pressure on inflation, the incomes policy based on fear simultaneously reduced the need for the Federal Reserve to perform this function themselves, by using restrictive monetary policy interventions to depress aggregate demand, raise unemployment, and so discipline workers into moderating wage claims. The incomes policy based on fear made this un-necessary: the very *structure* of the labor market created by the process of zapping labor now disciplined workers by creating job and/or income insecurity at any rate of (conventionally measured) unemployment, eliminating the need for high unemployment to perform this disciplinary task.⁸ This freed the Federal Reserve to lower interest rates and allow unemployment to fall (and with it, incomes and hence profits to rise). Again, these developments are evident in table 1 (rows one and four), where marked declines in both interest rates and the rate of unemployment can be seen after 1990. In this way, the neoliberal restitution of Golden Age standards of macroeconomic performance evident in column five of table 1 (rows one, two, and four), where we see the return of a low inflation, low unemployment, and low interest rate environment in the US economy for the first time since the early 1970s, can be explained by the process of zapping labor evident in rows three and five of the same table, and its creation of an incomes policy based on fear. Taken to-

⁷The increases in the price of oil resulting from the US invasion of Iraq in 2003 and the impact of hurricane Katrina on oil refining capacity located on the Gulf of Mexico in 2005 are salient examples of this latter process during the period of the Neoliberal Boom.

⁸Even Alan Greenspan was wise to this effect, referring in Congressional testimony during the mid-1990s to the ‘labor market fear factor’ gripping American workers as a reason for diminished inflation concerns at the Federal Reserve.

gether, these developments describe a process of ‘balancing the macroeconomic books on the backs of workers’ (Setterfield, 2006), wherein the costs of achieving improved macroeconomic performance are borne uniquely by working households.

Central to the account provided above is what amounts to the substitution of *institutional conditions* for *unemployment* as the key ‘worker discipline device’ moderating distributional conflict and hence the wage share of income and/or the accompanying rate of price inflation. To see this in more detail, consider the following system of equations:

$$\hat{w} = \mu(v_W - v) \quad (1)$$

$$\hat{p} = \phi(v - v_F) \quad (2)$$

$$\mu = h(e, I), h_e > 0, \quad h_I < 0 \quad (3)$$

where $\hat{w}$ is the rate of growth of nominal wages, v_W is the target wage share of workers, v is the actual wage share, $\hat{p}$ is the rate of price inflation, v_F is the target wage share of firms, I captures the effects of institutional features of the labour market that create employment and/or income insecurity amongst workers, and the parameters μ and ϕ represent the relative power of workers in the wage bargain and the relative power of firms in product markets, respectively.⁹ Equations (1) and (3) constitute a simplified form of the conflicting-claims model of inflation due to Rowthorn (1977). Hence note that in equation (1), for example (and *ceteris paribus*), workers would need to increase nominal wages at a rate equivalent to $m = \hat{z}$ (the rate of growth of labour productivity) simply in order to maintain the *current* value of the wage share (much less advance it towards the target value, v_W), given that

⁹Note that, for the sake of simplicity, v_W is treated as being independent of e and I even as μ is modelled as being endogenous to these variables. See, however, Setterfield and Lovejoy (2006) for discussion of the endogeneity of workers’ aspirations. Note also that, in what follows, we abstract entirely from changes in ϕ , v_F and v_W in order to highlight the particular importance of changes in the values of μ for the structure and performance of US capitalism over the past thirty years. It is, however, quite possible that changes in ϕ , v_F and/or v_W have contributed to the macroeconomic outcomes analyzed in this chapter.

$v = \frac{\omega}{z} = \frac{w/p}{z}$. This matter is nullified if, for simplicity, we assume that $m = \hat{z} = 0$.¹⁰

It is also possible that workers reference an expected rate of inflation when seeking wage increases in accordance with equation (1) given that *ceteris paribus*, and once again recalling that $v = \frac{w/p}{z}$, they would need to raise nominal wages in tandem with any increase in prices merely in order to maintain the current value of the wage share. Abstracting from these concerns is worthwhile in the current context, however, where our objective is to highlight the role of conflict in the determination of outcomes such as v and $\hat{p}$ and, in particular, the changing influences on this conflict as a result of the transition of US capitalism towards neoliberalism.

The underlying theory in equations (1) and (2) is that workers and firms care about achieving target or ‘fair’ shares of total income (reflected in the targets v_W and v_F), and strive to inflate nominal wages and prices (respectively) in the pursuit of these target shares. Hence $\hat{w}$ is increasing in v_W and decreasing in v in equation (1), while $\hat{p}$ is increasing in v and decreasing in v_F in equation (2). Equations (1) and (2) combine to yield equilibrium values for the rate of inflation ($\hat{p}^*$) and the wage share (v^*) under the equilibrium condition $\hat{w} = \hat{p}$, which is necessary to ensure a constant wage share ($\dot{v} = 0$) under the hypothesized conditions $v = \frac{w/p}{z}$ and $m = \hat{z} = 0$. These equilibria can be written as:

$$\hat{p}^* = \frac{\mu^* \phi (v_W - v_F)}{\mu + \phi} \quad (4)$$

$$v^* = \frac{\mu v_W + \phi v_F}{\mu + \phi} \quad (5)$$

Note that in equation (5), the equilibrium wage share is a weighted average of the distributional targets v_W and v_F : as long as $\mu, \phi \neq 0$, neither workers nor capitalists are able to set v equal to their preferred, target values. Instead, equilibrium price inflation $\hat{p}^*$ emerges as the

¹⁰Note that this simplifying assumption also means that statements about the wage share are equivalent to statements about the value of the real wage and *vice versa*, since with $m = 0$ any variation in ω is reflected in equal-proportional variation in v , and *vice versa*.

residual outcome of the ‘balance of conflicting forces’ that keeps the functional distribution of income constant in equilibrium.

Equation (3) relates the bargaining power of workers directly to the employment rate $e = L^d/L$, and indirectly to the degree of institutionalized worker insecurity, I . This equation captures a trade off between the rate of unemployment ($1 - e$) and the degree of institutionalized worker insecurity necessary to maintain a constant rate of worker bargaining power, μ . As will become clear below, this allows us to model the substitution of institutionalized worker insecurity for unemployment as a worker discipline device under neoliberal capitalism. Note that, when taken together, equations (1) and (3) modify the ‘wage push’ element of traditional Goodwin-type dynamics, as discussed in chapter 2. Specifically, their interplay can be thought of as modifying the $f(e)$ component of the wage growth equation (equation (1)) first introduced in section 2 of chapter 2 – so that the simple conflicting-claims model used in this chapter can be directly connected to (aspects of) the formal models of the Goodwin pattern outlined in chapter 2. This is not altogether surprising, of course, since both are concerned with the contribution of distributional conflict to capitalist macrodynamics.

Referring to equations (3), (4) and (5), consider first the derivatives:

$$\frac{dp^*}{de} = \frac{dp^*}{d\mu} \frac{d\mu}{de} = \frac{\phi^2(v_W - v_F)}{(\mu^* + \phi)^2} h_e > 0 \quad (6)$$

and:

$$\frac{dv^*}{de} = \frac{dv^*}{d\mu} \frac{d\mu}{de} = \frac{\phi(v_W - v_F)}{(\mu^* + \phi)^2} h_e > 0 \quad (7)$$

These results establish the existence of ‘standard’ (price inflation) and wage-share Phillips curves: as the employment rate rises (unemployment rate falls) and the labour market tightens, the rate of inflation and the wage share of income both rise.

Now consider the derivatives:

$$\frac{dp^*}{dI} = \frac{dp^*}{d\mu} \frac{d\mu}{dI} = \frac{\phi^2(v_W - v_F)}{(\mu^* + \phi)^2} h_I < 0 \quad (8)$$

and:

$$\frac{dv^*}{dI} = \frac{dv^*}{d\mu} \frac{d\mu}{dI} = \frac{\phi(v_W - v_F)}{(\mu^* + \phi)^2} h_I < 0 \quad (9)$$

These results demonstrate the capacity of variations in institutionalized worker insecurity to ‘shift’ the standard and wage-share Phillips curves – so that as I rises, both the rate of inflation and the wage share of income fall at any given rate of employment (unemployment).

Finally, consider the total derivatives:

$$dp^* = \frac{\partial p^*}{\partial e} de + \frac{\partial p^*}{\partial I} dI \quad (10)$$

and:

$$dv^* = \frac{\partial v^*}{\partial e} de + \frac{\partial v^*}{\partial I} dI \quad (11)$$

It is clear from inspection that because the partial derivatives in both equations (10) and (11) are of opposing signs, we can find $de, dI > 0$ such that $dp^*, dv^* = 0$. This is the essence of the neoliberal supply side as described earlier and its apparent restitution of Golden Age macroeconomic performance (seen in table 1) through the institution of an incomes policy based on fear ($dI > 0$). The result is illustrated in Figure 1.

Suppose we begin at the equilibrium $v_1, \hat{p}_1$ in the north-east quadrant of Figure 1. This puts the economy at points A and A' (respectively) on the wage-share and standard Phillips curves $WSPC_1$ and SPC_1 in the south-east and north-west quadrants of the Figure. *Ceteris paribus*, a rise in institutionalized worker insecurity I will lower worker bargaining power (to μ_2) and so lower the equilibrium wage share and inflation rate (to v_2 and $\hat{p}_2$, respectively).

Figure 1: Restoring Macroeconomic Performance with an Incomes Policy Based on Fear

But if accompanied by a simultaneous increase in e (and hence decrease in U from U_1 to U_2) sufficient to exactly offset the impact of the change in I on μ , the equilibrium in the north-east quadrant of Figure 1 will be restored to its initial configuration. This will bring the economy to rest at points B and B' (respectively) on the new wage-share and standard Phillips curves $WSPC_2$ and SPC_2 in the south-east and north-west quadrants of the Figure. In the final analysis, macroeconomic performance will have improved by conventional metrics, the economy realizing a lower rate of unemployment at U_2 without any accompanying ‘sacrifice’ in terms of a higher rate of inflation.

In addition to explaining the stylized facts of neoliberalism’s restoration of Golden Age standards of macroeconomic performance, note that Figure 1 also furnishes an explanation for the recent shift in the centre or focus of the Goodwin pattern – a shift of the type that was remarked upon in chapter 1 – brought about by the change in the structure of distributional conflict due to the incomes policy based on fear. Hence as is evident from the bottom-right quadrant of Figure 1, the transition to the Neoliberal Boom facilitated a longer-term rise in the rate of employment without any accompanying rise in the wage share. This same pattern is clearly evident in the data reported in Figure 2 in chapter 1, where, over the course of events from 1982-2000, it is evident that the employment rate rose substantially (by fully 6 percentage points) even as the wage share declined modestly.

The account provided thus far suggests that neoliberalism *worked*, even if not ‘as advertised’. But closer inspection suggests that this was not quite the case. Even as the events described above were unfolding and giving rise to seemingly palatable macroeconomic outcomes during the 1990s and 2000s, some macroeconomists were warning of danger ahead – specifically, concern that:

the incomes policy based on fear during the 1990s has had adverse effects on the aggregate demand generating process in the US economy, the full consequences of which have yet to materialize ... the seemingly dichotomous treatment of the demand and supply sides [in the account above of how neoliberalism works]

... masks the potential for a deeper malaise arising from the *interdependence* of supply and demand, as a result of which the supply-side “solution” to the problem of reconciling low unemployment with low inflation interferes with the process of demand generation so as to ensure that the potential for simultaneous low inflation and unemployment cannot be realized in practice. (Setterfield, 2006, p.61; emphasis added).

These concerns are summarized succinctly by reference in the title of Palley (2002) to ‘economic contradictions coming home to roost’.¹¹ We now turn to provide an account of the problems that gave rise to such consternation.

3 Act II – The demand side during the neoliberal era

The concerns expressed above reflected recognition of a structural flaw on the demand-side of the neoliberal economy, emanating from the *real wage-productivity disconnect*. Figure 2 depicts the compensation of production workers (who make up approximately 80% of the US workforce) as keeping pace (approximately) with the expansion of productivity until the late 1970s. By the 1980s, however, the two series can be seen to have ‘decoupled’; workers’ compensation stagnates even as productivity continues to rise apace. This last development constitutes the real wage-productivity disconnect referred to above.

The significance of this development is evident in the remarks made in section 6.2 about the relationship between the wage share, the real wage, and productivity in the discussion of equation (1). Hence as previously noted, since $v = \frac{\omega}{z}$, we must observe $\hat{\omega} = m = \hat{z}$ simply in order to maintain the value of v over time. If $\hat{\omega} < m$, the result will be a secular decline in v . Referring again to figure 2, we can see that this inequality is exactly the pattern (rising productivity without any accompanying, much less equivalent, rise in the real wage) that was established in the US economy under neoliberalism.

¹¹The same concerns are summarized still more dramatically by the title of Godley and Izurieta (2002): ‘The case for a severe recession’.

Figure 2: Productivity and Hourly Compensation of Production and Non-Supervisory Workers, 1959-2005 (1959 = 100)

Source: Palley (2009, p.8)

As we have already seen, these outcomes were a by-product of neoliberal supply-side economics, properly understood as a process of zapping labor to create an incomes policy based on fear. The resulting disempowerment of workers reduced their ability to bargain for wage increases to such an extent that it facilitated not only the ability to raise the rate of employment without contributing to inflationary pressure (the phenomenon captured by the behaviour of the SPC in the north-west quadrant of figure 1), but also eliminated their ability to so much as increase real wages *at all* – even in the presence of rising productivity that, in principle, facilitates steadily rising real wages without any (potentially conflict-inducing) distributional implications. The result has been the steady decline of the wage share of income since 1980 previously noted in the third row of table 1.

The declining wage share has had devastating budgetary implications for the majority of US households, for the simple reason that most of these households derive most of their income from wages. This is because the ownership of wealth in the US – and especially the ownership of wealth other than owner-occupied housing, that generates monetary incomes for its owners – is extremely unequal. As such, although the functional distribution of income (the division of total income between wages and profits) is not the same as the size distribution of income (that measures the frequency with which households earn incomes of a particular size, regardless of its source), the two distributions are related. Indeed, the wage-income-dependence of the majority of households means that changes in the size distribution of income can be understood as a principle ‘driver’ of changes in the size distribution of income (see, for example, Glyn, 2009; Atkinson, 2009; Piketty, 2014). This is clearly illustrated in figures 3 and 4, which show the growth of household income by income quintiles, together with the growth of income experienced by the top 5% of households in the size distribution of income, prior to and since the advent of the Neoliberal Boom. Figure 3 shows that throughout the post-war era prior to 1979, the growth of incomes was remarkably equal. Consistent with real wages keeping pace with the growth of productivity in figure 2,

thus keeping the functional distribution of income between wages and profits roughly constant, this sufficed to keep the income shares of different quintiles of the size distribution of income (and the share of the top 5%) roughly constant. But figure 4 shows that after 1979 this pattern changed dramatically. Consistent with the real wage productivity growth disconnect that emerged during the neoliberal era, the incomes of households at the top end of the income distribution – and in particular, the incomes of households in the top 20% and especially the top 5% of the distribution, where income-generating-wealth ownership is concentrated – grew much faster than incomes in the bottom 80% of the distribution (where households that depend exclusively on wage income are concentrated). This pattern of unequal growth resulted in ever more income becoming concentrated in the hands of households at the top of the income distribution – in other words, it resulted in the large increases in income inequality and increasing share of total income that accrues to top income earners that have been extensively documented in chapter 3 and elsewhere in the literature (see, for example, Atkinson et al., 2011; Piketty, 2014).

Figure 3: Change in Real Family Income by Quintile (and Top 5%), 1947-79

Source: Korty (2008, p.2)

Figure 4: Change in Real family Income by Quintile (and Top 5%), 1979-2005

Source: Korty (2008, p.1)

The implications of these developments for the demand-side of the economy follow from the fact that current income funds current consumption spending by households, and consumption expenditures make up 70% of total expenditures (aggregate demand) in the US economy. *Ceteris paribus*, slow income growth for the majority of households translates into slow growth of consumption spending by these same households. This is not offset by increased consumption spending arising from the faster income growth experienced by top earners, meanwhile, because much more of these top incomes is *saved* rather than spent.¹² The result is an apparent crisis of demand formation under neoliberalism, as the majority of households need to rein in the growth of their consumption spending in conformity with their diminished income growth.

In fact, a crisis of demand formation was *not* the immediate consequence for the US economy: the structural developments on the demand side outlined above did not fetter the Neoliberal Boom in the US from 1990-2007. This was because ‘other things’ were not ‘equal’

¹²See, for example, Carvalho and Rezai (2016) on the propensity to save of top income earners.

during this growth episode, owing to the new-found willingness and ability of households to accumulate debt to finance consumption spending that they were unable to fund from current income. The increased *willingness* of households to borrow in order to spend can be explained by two factors. First, aspirations grow even if income does not. This is partly a result of the ‘American dream’ (each generation both aspiring and expecting to be better off materially than their parents). During the Neoliberal Boom, this phenomenon was amplified up by a mixture of rapid product innovation (especially in information and communications technology) together with mass-media focus on these new products and the lifestyles of those who used them, coupled with the established phenomenon of ‘keeping up with the Joneses’ – the fact that consumption is a referential, positional, and innately *social* process, rather than something undertaken by ‘atomistic’ individuals acting in isolation (Cynamon and Fazzari, 2008). The second factor was the process of ‘running to stand still’: the need for households to make up for declining public provision by accumulating debt merely to accomplish the same outcomes as previous generations. For example, rising tuition fees in post-secondary education mean that individuals must now accumulate more student loan debt in order to earn a college education.¹³ Meanwhile, the *ability* of households to borrow was facilitated by easier and cheaper credit resulting from various financial sector innovations associated with the process of financialization discussed in chapter 4. These included widespread credit reporting that increased lender confidence in the assessment of credit-worthiness, ‘cash out’ mortgage refinancing, and the securitization and sale of debt (including mortgages and auto loans) that had previously been held by banks, purportedly so as to disperse and diminish risk. Not surprisingly, household debt rose sharply during the neoliberal era, the pace of household debt accumulation even accelerating after 2000 (see figure 5). Figure 5 also makes

¹³It should be noted that not all aspects of social provision fell during the neoliberal era, despite the Thatcher/Reagan emphasis on ‘rolling back the frontiers of the welfare state’. Indeed, the case can be made that from the mid-1990s onwards, some aspects of social provision increased sharply in order to ‘subsidize’ the operation of low-wage-growth neoliberal labor markets (Moos, 2019). The focus here, however, is on aspects of social provision – such as public higher education – that now require a larger private contribution.

clear that much of the increase in household borrowing during the Neoliberal Boom was driven by the accumulation of mortgage debt and was therefore associated, in part, with the bubble in the US housing market prior to 2006. The rise in house prices associated with the latter can therefore be considered an important facilitating factor in the creation of the Neoliberal Boom, providing collateral for additional indebtedness that, for the reasons outlined above, households were both willing and able to accumulate.¹⁴

Figure 5: Household Debt as a Proportion of GDP

Source: Cynamon and Fazzari (2008, p.18)

In short, there was no immediate crisis of demand formation in the US economy to prevent the Neoliberal Boom, because household debt accumulation provided a timely ‘offset’ to the potential demand shortfall arising from the stagnation of real wages (and resultant rising household income inequality) created by neoliberal supply-side economics. At the same time, however, household debt accumulation sowed the seeds of the destruction of the

¹⁴See, for example, Moore and Stockhammer (2018) on the importance of the housing bubble for promoting growth in the US economy during the Neoliberal Boom.

Table 2: Distribution of household debt by income

Household type	Average income	Average debt	Debt to income ratio
$\leq$ \$50,000 (66% of households)	\$23,090	\$68,918	2.98
$>$ \$50,000 (34% of households)	\$112,232	\$157,681	1.40

Source: Palley (2002)

Neoliberal Boom, by creating an economy characterized by increasing financial fragility and risk of collapse. First, and as might be imagined (given that the motivation for household debt accumulation was the stagnation of wage income experienced by all but those at the top of the income distribution), household debt accumulation was not equally distributed. As table 3 demonstrates, while the absolute levels of indebtedness incurred by households in the top third of the income distribution were larger than those incurred by households in the bottom two thirds, it was the latter group (less affluent households) that accumulated the highest debt to income ratios – patterns evident even as early as the year 2000, before the acceleration of household debt accumulation shown in figure 5 occurred. This is significant because while the purpose of debt accumulation by less affluent households was to make up for a lack of income growth (that would otherwise have impaired consumption), debt accumulation imposes a burden on household income because it sets up debt-servicing commitments (interest payments and payments towards principal). So as households – particularly lower-income households – accumulated more debt relative to their total income, the debt servicing claims on what remained of their income steadily increased. This is clearly illustrated in figure 6.

The significance of this last observation – and its relationship to the increasing financial

Figure 6: Debt Service as a Proportion of Disposable Income

Source: Cynamon and Fazzari (2008, p.22)

fragility and risk of collapse alluded to earlier – can be illustrated as follows. First, consider the plight of households that borrow to finance consumption spending that they are unable to fund from current income. This initial act of borrowing results in the accumulation of debt, which in turn results in a debt-servicing commitment in subsequent periods. Debt servicing commitments reduce the amount of disposable income available for consumption, which puts pressure on already indebted households to borrow *more* in order to finance consumption spending. This will, of course, add to total indebtedness, increasing further the debt-servicing obligations of debtor households, further constraining the availability of income for consumption spending, thus increasing borrowing requirements, and so on. The situation has all the makings of a vicious circle.

Now consider the consequences for demand formation of the vicious circle just described. The debt service payments of debtor households are received as income by rentier households – i.e., more affluent households that save a larger part of their total income and thereby act as creditors. As previously noted, these rentier households are more likely to save rather than spend any additional income they earn. In other words, as soon as less affluent households start to borrow in order to finance consumption spending, they inadvertently set up a transfer payment scheme (their debt servicing obligations) that redistributes total income towards more affluent households that are less likely to spend the additional income they earn. In and of itself this redistributive feature of debt accumulation by less affluent households threatens to undermine total consumption spending, and is thus inimical to demand formation. Moreover, should less affluent households continue to accumulate debt as a means of relieving the income constraint on their consumption spending, the resulting debt servicing obligations may eventually become overwhelming, resulting in default. This makes debtor households bad credit risks, constraining their ability to borrow (and hence spend). It also reduces the wealth and confidence of rentier (creditor) households, making them less able

and less inclined to both lend or even, themselves, spend on consumption goods.¹⁵ In the worst case scenario, these events do not just have negative effects on demand formation and hence economic activity, they result in a full-blown financial crisis and the onset of a deep recession or even depression.

In the final analysis, a confluence of factors – including the end of the housing market boom by 2006 and prominent instances of corporate insolvency in the financial sector in 2007 and 2008 – triggered the onset of the 2007-09 financial crisis and Great Recession that, together, brought the Neoliberal Boom to a close. But as has been demonstrated above, the real architect of this crisis was the institutional structure of neoliberalism itself – the institutionalized worker insecurity that not only made the US labour market quiescent for employers, but also hollowed out the core of the demand-formation process, based on steadily rising consumption expenditures funded by steadily rising real wage incomes. In short, the growing inequality first documented in chapter 3 drove the ‘financialization’ of US households documented in chapter 4, resulting in the financially-fragile and innately unsustainable structure of the Neoliberal Boom documented in this chapter.

4 Act III – The neoliberal inheritance

The account of the neoliberal era provided thus far suggests that neoliberal supply-side economics constituted a process of zapping labor so as to construct an incomes policy based on fear. This so tamed the growth of wages as to result in a disconnect between real wages and productivity. The real wage-productivity disconnect created rising income inequality as the wage incomes of the majority of households stagnated, so undermining the process of demand formation – a problem masked by the increasing willingness and ability of US

¹⁵Rentier’s wealth is destroyed because, of course, the financial liabilities of debtor households are the financial assets of creditor households. Default on debts therefore forces creditors to write down or write off some part of the value of their total financial wealth.

households to accumulate debt in order to finance consumption spending. The process so described was, however, unsustainable, giving rise to a financially fragile and crisis-prone form of capitalism even as the neoliberal economy seemingly prospered through 2007. The climax of these events was the 2007-09 financial crisis and Great Recession – a near depression that constituted the most severe downturn in the US economy since the 1930s.

But the Great Recession was not the end of the story. This brings us to Act III: the contemporary experience of the ‘neoliberal inheritance’ during the period since the end of the Great Recession.

4.1 Did the US ‘recover’ from the Great Recession?

The short answer to the question posed in the title of this subsection is ‘no’. On the face of it, just prior to the onset of the recession that began in the spring of 2020, the US economy was booming, experiencing unemployment rates lower than any witnessed since the early 1970s. In reality, the post-Great Recession trade cycle boom that can dated from the third quarter of 2009 through the fourth quarter of 2019 was little more than a long ‘depressed upswing’:¹⁶ persistently weak macroeconomic performance that, even at the peak of the boom, was flattered by reduced estimates of potential output and the fact that much contemporary unemployment is now disguised by pro-cyclical adjustments in labour-force participation associated with the discouraged worker phenomenon and the under-employment of those who work involuntarily on a part-time, temporary, or ‘gig’ basis.

Turning first to the growth record, figures 7 illustrates the timepath of real GDP in the US from 1991-2020. The ‘line of best fit’ depicted in figure 7 plots the predicted values of

¹⁶All business cycle dating referred to in this section is based on the National Bureau of Economic Research’s (NBER) business cycle reference dates. See www.nber.org/cycles.

The astute reader will note that the post-Great recession depressed upswing was brought to an end by the onset of the COVID-19 pandemic – the catalyst for the recession that began during the first quarter of 2020. We will return to the topic of the ‘COVID-19 recession’ and its possible implications and legacy in chapter 8.

real output based on estimation of the equation $y = \beta_1 + \beta_2 t + \beta_3 t^2 + \epsilon$ using quarterly data over the duration of the Neoliberal Boom (1991 QII – 2007 QIV). It serves as a first-pass approximation of the trend path of real output during the Neoliberal Boom, and its out-of-sample extrapolation (using data for the period after 2007 QIV) illustrates the simple fact that in the aftermath of the Great Recession, real GDP growth was never strong enough to restore the US economy to anything like the prior trend path of GDP established during the Neoliberal Boom. Indeed, the real rate of growth of GDP during the expansion since 2009 was lower than that during any previous cyclical upswing since the 1940s (Kotz, 2019, Fig.4, p.534). The basis for reports of a ‘tight’ US economy by the end of the 2009-2019 depressed upswing are revealed in figure 8, which is reproduced from Coibion et al. (2018): closing of the output gap (the difference between potential and actual real output) was achieved by relentless downward revision of the Congressional Budget Office’s (CBO) estimates of potential output, and not by any robust recovery in actual real output.

Whether intentionally or otherwise, figure 8 makes a strong case for the existence of hysteresis in US potential output – or at the very least, hysteresis in *estimates* of US potential output. This last phenomenon – the sensitivity of potential output estimates to actual economic performance over the course of the cycle – is addressed by Tercioglu (2020), who uses a different methodology for estimating potential output in the US economy. Figure 9 reproduces Tercioglu’s estimates of the output gap in the US from 1991-2019. Consistent with what is suggested by figure 7 – and contrary to the impression created by recent CBO estimates of the potential output illustrated in figure 8 – figure 9 reveals a persistent output gap in the US economy throughout the period 2009-2019 which, unlike the behaviour of the output gap during either of the two previous business cycle booms during the Neoliberal Boom, does not come close to disappearing even as the economy reaches its cyclical peak.

The performance of the labour market tells a similar story of persistent slack (even close to the cyclical peak of 2019) during the 2009-2019 depressed upswing in the US economy.

Figure 7: Real GDP in the US, 1991-2020

Source: Authors' calculations based on Federal Reserve Economic Data (FRED).

Figure 8: Revision of Potential Output Growth in the US since 2007

Source: Coibion et al, 2018

Figure 9: Output Gap in the US Economy, 1991-2019

Source: Author's calculations based on Tercioglu (2020).

First, and as is well known, the ‘headline’ unemployment rate reported by the Bureau of Labor Statistics (BLS) – U3, which measures the total number of unemployed persons as a percent of the civilian labor force – understates slack in the labour market. This is because of changes since the mid-twentieth century Golden Age in both the nature of employment (fewer full-time, year round jobs as a proportion of total employment) and attachment to the labour force (the discouraged worker phenomenon). In recognition of these changes, the BLS now reports a broader measure of unemployment, U6, which measures the total number of unemployed persons plus all persons marginally attached to the labor force plus the total number of persons employed part time for economic reasons, as a percent of the civilian labor force plus all persons marginally attached to the labor force.¹⁷ Figure 10 illustrates both measures of unemployment since the onset of the neoliberal era. As is clear from figure 10, U6 was considerably higher than U3 throughout the depressed upswing 2009-2019, remaining as high as 7% even as the peak of the cycle was reached.¹⁸

Of course, what figure 10 also reveals is the fact that U3 has exceeded U6 throughout the neoliberal era: the changes to the labour market that prompted the creation of the U6 measure pre-date the recent depressed upswing.¹⁹ Moreover, the U6 rate of unemployment is no higher in 2019 than it was in either 2000 or 2007, when the two previous business cycle booms reached their peaks. Nevertheless, taking stock of the last three business cycle booms as a whole, there was (on average) a greater amount of slack during the recent depressed

¹⁷The U6 definition of unemployment recalls Marx’s distinction between floating and latent segments of the labour market – the former consisting of regular employment and the latter made up of, for example, part-time and temporary employment – and is, as such, quite consistent with the MKS vision of the economy. See also Flaschel and Luchtenberg (2012, chpt.2).

¹⁸Another potential barometer of labour market slack is the behaviour of wages which, according to the basic dynamics of the Goodwin pattern, should inflate as the unemployment rate drops in such a way as to raise the wage share of income. There is little evidence of this happening during the 2009-2019 depressed upswing – which in and of itself is of a piece with the evidence presented here, which suggests that ‘slack’ in the US labour market has been the subject of chronic underestimation. We will return to the behaviour of the wage share below, on the basis that its behaviour – and the apparent breakdown of the Goodwin pattern that it suggests – signals something still more telling about the structure and functioning of the US economy since the end of the Great Recession.

¹⁹Indeed, they are changes that can be associated with the emergence and onset of neoliberalism itself.

Figure 10: Unemployment in the US Economy 1991-2019

Source: Bureau of Labor Statistics (BLS)

upswing than existed during either of the two previous trade cycle booms that belong to the Neoliberal Boom phase of growth. Focusing on U3 (for which data exists prior to 1991), figure 11 illustrates the ‘time to recovery’ of the US labour market 1991-2000, 2002-2007, and 2009-2019 – that is, the ratio of the current value of U3 to its value at the peak of the preceding trade cycle boom, and hence the number of months that it took for U3 to recover to its value at the peak of the preceding trade cycle boom. Figure 11 reveals that U3 was persistently much higher than its previous business cycle peak value during the recent depressed upswing than during either of the preceding booms, and took longer (15-40 months, depending on which of the two previous booms is used as the basis for comparison) to recover to its value at the peak of the prior boom. In short, the labour market was persistently slacker during the 2009-2019 depressed upswing than during either of the two previous cyclical upturns.

Indeed, the notion that the recent depressed upswing witnessed greater annual average slack in the US economy than preceding booms during the neoliberal era is borne out by *any*

Figure 11: Recovery of Unemployment in the US Economy over Successive Trade Cycle Booms, 1991-2019

measure of macroeconomic slack, whether based on measures of real output or unemployment. Table 3 reports annual average values of U3, U6 and the output gap (due to Terciglu, 2020) for each of the three consecutive trade cycle booms in the US since 1991. As table 3 makes clear, performance during the 2009-2019 depressed upswing was worse than during either of the two previous booms by any of the three measures reported.

4.2 Explanations for the depressed upswing

If the much-lauded macroeconomic performance in the US since the end of the Great Recession was, in fact, relatively weak, then what explains the fact that since 2009 the US economy has witnessed nothing more than a long depressed upswing? Why has the US economy effectively stagnated during this period?²⁰

²⁰Our use of the term ‘stagnation’ here is deliberate: the perspectives outlined in what follows are part of a large literature that interprets recent US macroeconomic performance as consistent with the onset of *secular stagnation*. As originally defined by Hansen (1939, p.4), secular stagnation refers to ‘sick recoveries which die in their infancy and depressions which feed on themselves and leave a hard and seemingly immovable core of unemployment.’ A more general contemporary definition would be a prolonged period of slow growth,

Table 3: Macroeconomic ‘Slack’ in the US Economy over Successive Trade Cycle Booms, 1991-2019

Boom	U3	U6	Output Gap
1991 QI – 2001 QII	5.5	8.8	-3.11
2002 QI – 2007 QIV	5.3	9.1	-1.54
2009 QIII – 2019 QIV	6.4	11.9	-3.30

Source: FRED and Tercioglu (2020)

According to Gordon (2012) (see also Gordon, 2015, 2016), the causes of slow growth in the contemporary US economy are to be found among the supply-side determinants of potential output growth, which is, in turn, understood to be the determinant of actual output growth. The rate of growth of potential output can be decomposed into the sum of labour productivity growth and, assuming constant rates of employment and labour force participation in the long run, population growth.²¹ The focus of Gordon’s analysis thus becomes the rate of productivity growth, which is thought to have slowed down in recent decades because of a drop in the rate of growth of total factor productivity (TFP).²² This, in turn, extending well beyond the duration of a normal business cycle recession, that is not automatically ‘self-correcting’. See Anselmann (2020) for a comprehensive overview of the meaning and theories of secular stagnation.

²¹If we write:

$$Y_p = \frac{Y_p}{eL} \frac{eL}{P} P$$

where Y_p denotes potential output, P is total population, and $e = L^d/L$ here denotes employment consistent with the natural rate of unemployment, then assuming constancy of the latter and the labour force participation rate, L/P , we get:

$$\hat{Y}_p = m + \hat{P}$$

²²In neoclassical growth accounting, potential output can be written as:

$$Y_p = AK^\alpha (QL)^{1-\alpha}$$

is explained by the allegedly diminished prospects for productivity-enhancing innovations arising from the ‘third’ industrial revolution (associated with the recent wave of information and communication technologies) as compared to the previous ‘second’ industrial revolution, that was rooted in the electronics, chemicals and motor vehicle industries.

Gordon’s theory can be subject to a number of criticisms. First, technology ‘optimists’ argue that it is ‘too soon to call’ the innovation-based, productivity-enhancing potential of modern information and communications technologies (Mokyr, 2014; Eichengreen, 2015). Second, because Gordon seeks to explain the behaviour of actual output growth in terms of potential output growth, he overlooks arguments to the effect that actual output growth, in fact, determines potential output growth (Setterfield, 2003). Hence the growth of actual output encourages investment and so stimulates the capital development of the economy, induces greater labour force participation and migratory inflows of labour via its positive effects on the employment rate, and stimulates productivity growth by fostering an environment conducive to research and development and hence process innovations. Third, the secular, supply-side trends emphasized by Gordon – which include not only a decline in the productivity-enhancing potential of ‘new’ industries, but also a steady decline in educational attainment and the adverse effects of an aging population on the size of the labour force – should assert themselves gradually. The onset of post-Great Recession macroeconomic failure in the US has, however, been more sudden. Finally, Gordon’s quintessentially neoclassical analysis, focused on technical features of the supply side, is inconsistent with the MKS vision of capitalist dynamics that, among other things, puts emphasis on the importance of the

where A is total factor productivity, K is the capital stock, Q denotes the quality of labour (as measured by educational attainment, for example) and the rate of employment consistent with the natural rate of unemployment has been normalized to one for simplicity. It follows that:

$$\begin{aligned}\frac{Y_p}{L} &= \frac{AK^\alpha(QL)^{1-\alpha}}{L^\alpha L^{1-\alpha}} = Ak^\alpha Q^{1-\alpha} \\ \Rightarrow \hat{z} = m &= \hat{A} + \alpha\hat{k} + (1-\alpha)\hat{Q}\end{aligned}$$

where k denotes capital intensity.

demand side (drawing on Keynes’s principle of effective demand).

Drawing on this last observation, it is important to note that there do exist demand-side explanations for secular stagnation capable, in principle, of explaining the depressed upswing experienced by the US in the wake of the Great Recession. These demand-side explanations proliferate, however (Anselmann, 2020, chpt. 3), and not all of them are consistent with the MKS vision. Summers (2014b,a, 2015), for example, couches his explanation of a chronic lack of aggregate demand in the US in terms of the loanable funds theory of the real interest rate.²³ According to loanable funds theory, the real interest rate serves as the servo-mechanism that equates investment spending and saving, and so eliminates the possibility of a deficiency of aggregate demand (relative to potential output). But according to Summers (2014b,a, 2015), the equilibrium real rate of interest has turned negative, because of a decrease in investment and/or an increase in saving. Moreover, this negative real rate is unattainable, because of the contemporary coincidence of historically low rates of nominal interest and inflation, coupled with the fact that the nominal interest rate cannot be further reduced because of the zero lower bound.²⁴ The result is a structural state of excess supply: specifically an excess of saving over investment, which translates into a deficiency of aggregate demand, that is not self-correcting because of the impairments that prevent the required fall in the real interest rate.

Although the coincidence of near-zero nominal interest rates and low inflation post-dates the Great Recession – so that Summers’s explanation of chronically deficient aggregate demand can explain the depressed upswing conditions that materialized in the US only after the Great Depression – this explanation is far from universally accepted. First, it is not clear that it fits the data. For example, a prominent feature of the Summers hypothesis

²³See also Krugman (2014). For a critical overview of this essentially New Keynesian position, see Weiszaäcker and Kramer (2021, chpt.7).

²⁴Recall that using the Fisher equation, the real rate of interest can be expressed as the difference between the nominal rate and the rate of inflation.

is the notion that a rise in saving rates, resulting from increased income inequality (that has redistributed income towards affluent households with higher propensities to save) and the aging of the population (which calls for increased saving for retirement), has depressed interest rates.²⁵ However, as noted by Storm (2020, pp.100-102), drawing on Bofinger and Reis (2017), saving rates of households have *declined* significantly since the 1980s in the US (and elsewhere), while the aggregate propensity to save has remained more-or-less constant over the same period – even as real interest rates have fallen considerably. In short, there has been no savings glut – locally (within the US) or globally – that can be held responsible for driving down interest rates. Instead, the observed decline in interest rates to historically low levels is better explained as a central bank *response* to emerging conditions of secular stagnation (rather than an initiating cause of stagnation) – and one that has met with limited success because of traditional Keynesian arguments concerning the interest-inelasticity of investment spending and the dominant role of expectational factors in the determination of autonomous private-sector spending.

Second, central to the Summers hypothesis is the pre-Keynesian loanable funds theory. In this theory, chronic deficient demand is a special case resulting from an unattainable negative real rate of interest (as described above), rather than the general case anticipated by the principle of effective demand.²⁶ This brings us to demand-side explanations for secular stagnation that *do* embody the principle of effective demand and that, as such, are more compatible with the MKS vision of modern capitalism.²⁷ As noted by Di Bucchianico (2020,

²⁵The Summers hypothesis also alludes to a decline in investment as having depressed the real interest rate. A decline in investment spending is harder to explain in the context of loanable funds theory, however – where investment is a purely technical variable determined by the value of the marginal productivity of capital – than in the original ‘fundamentalist Keynesian’ theory of Hansen (1939) (and subsequent Post-Keynesian theory), where investment spending depends on expectations formed under conditions of uncertainty, and varies with confidence in the general state of the economy.

²⁶See, for example, Taylor (2017), Anselmann (2020, pp.84-86), Storm (2020, pp.93-100), and Di Bucchianico (2020) for more extensive Keynesian criticisms of loanable funds theory in the context of the secular stagnation debate.

²⁷These theories also possess other features that are compatible with the MKS vision. For example, they eschew the notion of a natural rate of interest and so leave room for interpretation of the rate of interest

p.295), these provide simpler (and so, by Occam’s razor, more appealing) explanations for chronic deficiencies of aggregate demand, that break free of the special-case contrivances of loanable funds theory. In fact, specific theories of this sort abound (see, *inter alia*, Nakatani and Skott, 2007; Hein, 2016a,b; Petach and Tavani, 2020; Serrano et al., 2020).²⁸ The account of the rise and decline of the Neoliberal Boom in this chapter, which centres on labour market institutions, inequality, and the financialization of households, furnishes one such theory. Hence the post-Great Recession period in the US has witnessed continuation of the worst trends associated with the Neoliberal Boom: worker insecurity and wage stagnation. Specific trends discussed earlier, such as changes to (or reinterpretations of) labour law that are disadvantageous to workers, have continued apace (Stelzner, 2017), with the result that the general decline in worker bargaining power has continued – so much so that it has now (finally) drawn the attention of mainstream macroeconomists (see, for example, Stansbury and Summers, 2020). Indeed, it is now common to refer to a ‘precariat’ among the American working class who occupy part-time, contingent, and benefit-free jobs (Standing, 2014) and whose numbers (as a proportion of all workers) are expanding (Greenstein, 2020).²⁹ Meanwhile, at just 0.8% p.a., real wage growth in the US economy during the 2009-2019 depressed upswing was lower than during either of the two preceding cyclical booms associated with the Neoliberal Boom, when real wage growth averaged 1.6% and 1.0%, respectively (Setterfield, 2021, Table 2, p.29).

In the wake of the financial crisis, however, households have been busy deleveraging rather than borrowing to supplement stagnant income streams. As shown by Kotz (2019, Fig.1, p.526), the debt to personal income ratio of all US households exceeded 130% by the end of the Neoliberal Boom, but fell to 110% by 2012 and has since fallen still further.

as a monetary variable, as in Keynes. They also introduce social classes and the balance of power between classes into the analysis, as in Marx. See Di Bucchianico (2020, pp.295-6).

²⁸See also Anselmann (2020, pp.44-71) on the historical precursors of these theories.

²⁹The growth of the precariat so-defined is frequently associated with the growth of the ‘gig’ economy.

Hence Cynamon and Fazzari (2016, Fig.3, p.383) note that whereas the consumption to income ratio of the bottom 95% of US households rose continuously during the Neoliberal Boom (consistent with the borrowing behaviour described in the previous section), the same ratio has declined steadily during the period since the Great Recession (consistent with household deleveraging). Absent the process of household debt accumulation and debt-financed consumption spending witnessed during the Neoliberal Boom, the latent problems of demand-formation identified earlier – and that can be traced back to the institutional structure of neoliberalism and its ‘reconfiguration’ of distributional conflict discussed in section 2 – have become manifest: the neoliberal US economy has lost its debt-financed, consumption-driven ‘engine’ of growth. The depressed upswing witnessed in the US 2009-2019 was a result of all this – as noted earlier, a period of markedly slower growth than that observed during any previous post-war cyclical boom. In short, the changes to the institutional structure of the labour market identified earlier in this chapter can be seen as a critical contributory factor to the triumvirate of inequality, financialization, and weak macroeconomic performance discussed throughout this section of the book. Moreover, the interaction of inequality, financialization, and weak macroeconomic performance provide not only a theory of structural demand deficiency capable of explaining tendencies towards secular stagnation (on which see also Pariboni et al., 2020, and the references therein), but also the seemingly sudden onset of this problem following the Great Recession – this onset arising from the sudden turn towards deleveraging among indebted households in the wake of the financial crisis.

4.3 Summary

The continuing real wage-productivity disconnect in the US economy, and the resultant hollowing out of the key source of income growth for the majority of US households, meant that in the immediate aftermath of the Great Recession the US economy stood at a cross-

roads: ‘wind up the clock-springs’ of unsustainable household debt accumulation once again; or confront a future of relative stagnation (slow economic growth and persistent slack in the labor market) as a result of the ‘broken’ demand-generating process. The failure of the US economy to rapidly or even completely recover from the Great Recession since 2009 – manifest in the long but weak recovery that characterized the decade following the Great Recession – suggests that this was not, in fact, a choice at all. Instead, by 2007, the neoliberal growth regime fueled by rising household debt was exhausted, leaving in its wake a set of institutions that are still entrenched but are now incapable of fully and properly revitalizing the US economy, as a result of the damage done by supply-side economics to the process of demand formation (see Cynamon and Fazzari, 2013, 2016).³⁰

5 Neoliberalism and the ‘breakdown’ of the Goodwin pattern

In chapter 1, we noted observations in the data consistent with an apparent ‘breakdown’ in the Goodwin pattern (see also Nikiforos, 2017). Figure 12 focuses on the relationship between the wage share and the employment rate in the US since 2000 in an effort to further bear out this observation.³¹ It is clear that during the expansion following the ‘dot-com’ recession in the US in 2000 (leading up to the onset of the Great Recession in 2007), there was no systematic profit squeeze: the wage share *falls* through 2006, and rises only very belatedly (and modestly) during the final year of this boom, from 2006-07. Figure 12 also shows that while the onset of the Great Recession produced a pattern more consistent with the Goodwin pattern (both the employment rate and the wage share falling substantially

³⁰For extensive discussion of neoliberalism’s inertia and entrenchment – institutional and otherwise – see Cahill (2014).

³¹See Setterfield (2021) for a fuller account of the ‘disappearance’ of the Goodwin pattern and the analytical basis for this phenomenon.

from 2007 through 2010), there was once again no obvious profit squeeze during the ensuing depressed upswing. Even as the employment rate rose by fully six percentage points between 2010 and 2019, the wage share remained essentially constant.

Figure 12: The wage share – employment relationship in the US, 2000-2019

The question arises as to how this apparent breakdown in the Goodwin pattern during the late neoliberal era can be explained? As noted earlier in this chapter, ‘headline’ employment/unemployment statistics now systematically understate the true extent of ‘slack’ in the US economy. One possible explanation for the breakdown in the Goodwin pattern, then, might be that there has always been too much slack in the labour market to put pressure on the profit share. But inspection of figure 10 reveals that by any measure, unemployment changes over the course of the business cycle – so on the face of it, there is still more or less slack in the US labour market at any point in time, as a result of which there should (in principle) be less or more pressure on the profit share. The fact that the wage share has now essentially *ceased to respond* to even the substantial rise in the employment rate (6 percentage points) registered during the 2009-2019 depressed upswing suggest that a more *structural* explanation of the events in figure 12 is required.

Drawing on the creation of institutionalized worker insecurity and the incomes policy based on fear as described earlier in this chapter, the answer provided here focuses on modifications to the distributional conflict that is a central feature of the dynamics of the MKS system. First, events from 2000-2007 can be thought of as reflecting the *completion* of the neoliberal project – an extension of the events summarized in Figure 1, with any increase in employment now being *more than* fully offset by increases in institutionalized worker insecurity, resulting in a net decline in the wage share even in the course of a short-cycle boom. Developments since the Great Recession, meanwhile, can be explained by the workings of the ‘complete’ neoliberal project reflected in an ‘institutionally entrenched’ incomes policy based on fear, in which worker bargaining power has been brought so low that we effectively observe $\mu = 0$ at any but the very lowest rates of employment. The result is that tightening of the labour market has virtually no effect on either inflation or the wage share, rendering both the standard and wage-share Phillips curves effectively flat. To see this, suppose we re-write equation (2) as:

$$\hat{p} = \phi(v - v_F) + \varepsilon \quad (12)$$

where $\varepsilon \sim (\bar{\varepsilon}, \sigma_\varepsilon^2)$ captures supply shocks associated primarily with commodity prices, and $\bar{\varepsilon} > 0$. Solving equations (1) and (12) for v^* and $\hat{p}^*$ under the assumption that $\mu = 0$, we now obtain:

$$\hat{p}^* = \bar{\varepsilon} \quad (13)$$

$$v^* = v_F \quad (14)$$

The workings of this modified conflicting-claims system is illustrated in Figure 13. Effectively, employment (unemployment) has been ‘decoupled’ from the dynamics of distributional con-

flict, so that developments in the north-east quadrant now function independently of those in the south-west quadrant. This results in ‘flat’ Phillips curves in both the north-west and south-east quadrants, wherein variations in employment (unemployment) have no effect on inflation or the wage share (respectively), *ceteris paribus*. Both inflation and the wage share are now determined independently of the conventionally-measured ‘tightness’ of the labour market – the rate of inflation depending only on the average rate of growth of commodity prices, $\bar{\varepsilon}$, and the wage share depending only on the pricing decision of firms (whose bargaining power *vis a vis* workers means that their mark up pricing decisions are now the sole determinant of the real wage and hence, given that $m = \hat{z} = 0$ by hypothesis, the wage share of income). It is as a result of this unilateralism in the determination of v – the transformation of an enduring source of conflict into an effective ‘no contest’ by virtue of the institutional structure of neoliberalism – that we observe $v^* = v_F$ in Figure 13. The outcomes just described bear out our previous claim (in chapter 1) that the observed breakdown in the Goodwin pattern evident in the data can be explained in terms of a transformation in the structure of class conflict during a particular phase of growth (neoliberalism), conflict itself remaining central to our account of the patterns evident in the data, as the MKS system suggests, in fact, it should.

6 Conclusions

The advent of neoliberalism in the 1980s has, over the course of the past four decades, forced the US economy to play out a three act tragedy. Ostensibly a supply-side revolution that would free the economy from socio-political fetters and launch a new era of prosperity, the main supply-side consequence of neoliberalism was to zap labour, institutionalize worker insecurity, and so install an ‘incomes policy based on fear’. This diminished conflict over shares of real income and so reduced inflationary pressures, but at the cost of decoupling

Figure 13: The institutionally entrenched incomes policy based on fear

real wage growth from productivity growth, and outcome that fueled rising income inequality and hollowed out the wage-funded, consumption-led core of the demand-generating process. This demand-side weakness was, at first, concealed by household borrowing designed to debt-finance increases in autonomous consumption spending that could not be funded by stagnant real wages. But it has since asserted itself in the wake of the Great Recession, following the exhaustion of this household debt accumulation process. We are still in the midst of act three, and there is no obvious (or easy) end to the performance in sight.

The necessary response to the apparent exhaustion of neoliberalism that was signaled by the 2007-09 financial crisis and Great Recession and its aftermath is, in a sense, straightforward. Starting with the fundamental cause of the malaise – the lack of worker bargaining power and its corrosive effects on the real earnings of the majority of US households – structural reforms are required to supplant neoliberalism and create a foundation for inclusive and sustainable growth. We will return to detailed exploration of this agenda in chapter 8.

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