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## Principles of Political Economy Applied to Policy and Governance: Disembedded Economy, Contradictions, Circular Cumulation and Uneven Development

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# Principles of Political Economy Applied to Policy and Governance: Disembedded Economy, Contradictions, Circular Cumulation and Uneven Development

## **Abstract**

The purpose of this paper is to apply some core general principles of political economy to central issues of policy and governance. After a short section explaining the nature of the science of political economy, we start with Polanyi's principle of the disembedded economy, and how this relates to cycles and waves of policy-making concerning the double movement and the relationship between markets, reciprocity and redistribution. Then we go on to scrutinise the principle of contradiction, paying special attention to the importance of capital-labor relations, the finance-industry dichotomy, monopoly versus competition, profit and the environment, plus individual versus society. Thereafter the principle of circular and cumulative causation is linked to social and production aspects of complex systems of political economy. And lastly we examine the principle of uneven development and how crucial this is to policy-making institutions as the world undergoes asymmetries of financial instability, climate change and cycle dynamics. Core principles thus provide a good grounding for general policy purposes when activist governance measures are required to improve human and environmental provisioning.

## **Keywords**

Principles; political economy; policy and governance; disembedded economy; contradictions; circular and cumulative causation; uneven development.

## **Cover Page Footnote**

Acknowledgement This paper was presented at the annual meetings of the Association for Evolutionary Economics (AFEE) at the ASSA, Denver, January 2011. I wish to thank the discussant John Harvey and session organisers John Hall and Janice Peterson, plus the conference participants for comments and suggestions for the rewrite. This paper is dedicated to the intellectual stimulation provided by Paul Dale Bush over several decades in the development of the instrumental theory of institutionalism.

## Introduction

The *Journal of Economic and Social Policy* has included in its analyses over the past seventeen years some key concepts of political economy applied to policy and governance issues. These include the notions of 'vested interests' (Wheelwright, 1997), 'cooperation' (Laurent, 2000), 'Chartalism' (Kadmos and O'Hara, 2000), 'embedded relationships' (Treuren, 2003), 'safety nets' (Mendes, 2004), 'financial fragility' (Lodewijks and Monadjemi, 2004), 'trust, reciprocity, fairness' (Rosenau, 2006), 'social and public capitals' (Dow, 2009) plus 'complex feedback processes' (Courvisanos and Richardson, 2011), to mention only a few. Numerous articles also examine in some detail theoretical and policy concerns of political economy, including post Keynesian, institutional, Schumpeterian, feminist and 'French' Regulation schools.

What is missing from the journal, so as to comprehend these notions, is an article that applies *core general principles of political economy* to issues of *policy and governance*. Hence this paper, which scrutinises four interrelated principles of political economy applied to several contemporary problems, such as waves of policy and performance, conflicts between various groups, the international crisis of 2008-12, and climate change.<sup>1</sup> These general principles of political economy are based on empirical and historical regularities and broad movements of the system in which we live, and governance and policy elements are critical parts of this movement.

We include firstly a section where the principles are linked to the development of political economy. In the next section we examine the *principle of the disembedded economy*, namely, that capitalism tends to undergo a double movement. It tends to stimulate free markets which dislocate money, land and labor from proper social provisioning when taken to the extreme. Major instability periodically emerges, which usually results in state-generated public goods to protect the system from destructive creation. When the state 'goes too far', however, the logic of capital is often disrupted, thus inhibiting reasonable turnover of the circuit of social capital, often leading to a movement back to more deregulated/capital-dominated institutions. Civil society and reciprocity also play core roles in these complex dynamics.

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1. An earlier version of this paper was presented at the Association for Evolutionary Economics (AFEE) meetings of the Allied Social Sciences Associations (ASSA), Denver, Colorado, January 2011. I thank the anonymous referees, Dale Bush, John Hall, and Janice Peterson plus Amanda Shoebridge and the Editor for comments and encouragement.

The disembedded economy is then linked to the *principle of contradiction*, where some balance is required to moderate the conflict between capital and labor, finance and industry, competition and monopoly, core and periphery, and so on. Contradictions link partly to heterogeneous agents, where there are different roles given to the primary agents of change and motion in the political economy. At the broader level there are species, but in relation to humans there are also classes, ethnic groups and genders, as well as different nationalities, and even more specific roles as we explore the institutions in detail. The trade-offs and movements between these realistic oppositions are critical to comprehending political economy processes, including the policy measures required for solutions to problems.

This leads us to two further principles, including the *principle of circular and cumulative causation*, that multiple factors are important and that they tend to magnify each other in the complexity of processes. The *principle of uneven development* is also important, because the world is subject to uneven forces, and policy needs to take into account these forces to properly represent the real forces impacting on the world. Linked to this is the idea of *decentered totality*, which tells us that policy cannot be monolithic but needs to be multifaceted in dealing with the complex problems of the world. The old model of markets versus government must give way to a more realistic model of different institutions, habits as well as individuals. This has profound ramifications for modern policy making.

## **Political Economy Principles and Policy**

We start by discussing the relationship between the four main general principles of political economy.<sup>2</sup> In order to do this, some brief remarks should be made about ‘what is political economy?’ Political economy is a relatively unified general science of the system in which we live through historical time and within institutions. It is about the quality of life for the general populations on Planet Earth, the source of wealth, the general system of the economy, linked into a broader science of economy within society and imbedded in a political, biological, and even cosmological study of the Earth within a wider Universe. Within this context, the Earth is given a cosmological meaning, but the science also seeks to

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2. The current research program of *specifically* scrutinising the ‘*core general* principles of political economy’ started with O’Hara (1993), continuing with O’Hara (2000), and later on advancing through a whole volley of articles, firstly on the theory (O’Hara, 2007a, b; 2008a, 2009a) then on applications to AIDS/HIV, subprime crisis, climate change, institutional regimes of accumulation and Stanfield’s concepts (O’Hara, 2006; 2007; 2009b, c, 2011). See also Brennan (2008), Dugger (1988), Dugger and Peach (2009), Fusfeld (1988), Kalsi (2011) and Stanfield (2011).

be a pragmatic, practical analysis of the economy historically linked to polity, society and geoeological processes on Planet Earth.

During the 1960s through to the 2010s several groups of economists came together at conferences, dinner parties, Universities, and political and social groups in order to foster a broader view of the economy. The reemergence and revitalisation of several schools of Veblenian institutionalists, feminists, neo-radicals, post-Keynesians, progressive Schumpeterians, and evolutionary economists, created an interdisciplinary view of the system in which we live. From this complex process a heterogeneous yet interconnected network of scholars and practitioners sought essentially to provide an alternative vision on the economy. This helped to situate political economy (or 'heterodox economics' as Fred Lee (2009) likes to call it) as a broad science of provisioning for the mass of people and other species within geoeological space and through time. Political economy became a relatively unified science of the study of the production, distribution and exchange of commodities and other goods and services involved in the reproduction of material and immaterial life.

In this *science of provisioning*, institutions became a core part of the process of constructing organisations, norms, knowledge, beliefs and relationships between people and other species. A core part of this complex process is the generation of institutional spheres such as the corporation, the state, finance, family, civil society and World economy. Political economy seeks to stimulate provisioning processes that enhance the broad quality of life, standard of living, happiness, growth and development for the common good, while recognising the conflicting and cooperative interaction within and between classes, genders, ethnic groups, species, institutions, nations and regions.

A study of production and distribution of goods and services within networks of people involved in social and economic life is a core part of the political economy perspective. So is the role of the state in the process of provisioning, including government finance, productive services, safety nets plus health, education and communication processes. This links into the World, regional, national and subnational production networks, commodity chains, ecological circuits, and institutional spheres. One must also examine the role of families, community organisations, not-for-profit groups, worker cooperatives, as well as the linkages between these things through historical time.

Political economists study institutions operating through networks, classes and other groups. They tend to approach the subject of political economy in a *critical manner*; to be explicit about the position of asymmetries in the economy, plus the

conflicts and also cooperative elements involved in this complex system. Often they speak of exploitation, the power of the vested interests, the unequal relationships affecting the life of people and other species set in a geocological space. They usually analyse the 'economic surplus', the way in which it is produced, distributed, exchanged and reproduced through time. They seek to comprehend differential access to the surplus and the forces of competition and cooperation in the pursuit of the surplus within and between classes, genders, ethnic groups, species and regions (Davis, 1992).

They seek also to ascertain the various positive and negative effects of the current system of economic power, including degrees of monopoly, concentration ratios, and rates of profit, accumulation, investment, capital and income. Political economy critically investigates these processes so that one is able to provide assessments of how to improve the state of the economy set in this wide environment. They tend to be influenced by the Physiocrats, the classical economists (including especially Malthus or for some Ricardo), Marx, Veblen, Keynes and Schumpeter, along with a whole host of other scholars such as Nicholas Kaldor, Gunnar Myrdal, Joan Robinson, John Commons, Georgescu-Roegen, Paul Sweezy, Paul Baran, Michal Kalecki, K.W. Kapp, Kenneth Boulding, and Karl Polanyi. Currently they publish in journals such as (the list is more extensive), *Review of Political Economy*, *Journal of Economic Issues*, *Journal of Post Keynesian Economics*, *Review of Radical Political Economics*, *Cambridge Journal of Economics, Politics and Society*, *Review of International Political Economy*, *Feminist Economics*, *World Development*, *Review of African Political Economy*, *Ecological Economics*, *Forum for Social Economics*, *New Political Economy*, *Studies in Political Economy*, *American Journal of Economics and Sociology*, *Journal of Economic and Social Policy* and the *Journal of Australian Political Economy*.

Political economists have come to emphasise the contradictions operating within the social economy. The core contradiction is the disembedded economy, but there are a host of other contradictions affecting the system and its members, such as those between capital and labor, finance and industry, ecology versus business/consumer capital, state and capital, plus individual and society. These contradictions operate within the system and also its dominant institutions and relationships, such as business, finance, state, family and World economy. Historically these contradictions change and adapt to internal pressures within the system and the various sub-systems of the economy, including ecology, polity, geography and society. Complex forms of metamorphosis, evolution and transformation operate through time as various layers of individuals, classes,

groups, institutions, regions and species undergo reproduction and regeneration through historical time.

Change is the product of a complex interactive process of natural selection, adaptation, plus the generation of novelty, niches and ongoing transformations. A core element of this change is circular and cumulative in the sense that the elements interact in a system of complexity, while the process of change is ongoing, usually amplifying or multiplying, so that the process rolls through in phases, business cycles, life cycles, waves and other forms of motion. At the global level there are differential and similar processes involved in generating various forms of convergence and uneven development through time. But the uneven or asymmetric elements of the World economy are of great interest as there are always differential processes impacting the distribution of power, wealth, income, happiness, trust, ecological footprint, and so on. It is within this broad science of political economy that the following four main principles are linked to policy and governance.

### **Principle of the Disembedded Economy**

Karl Polanyi in *The Great Transformation* (1944) developed the principle of the disembedded economy which posits a magisterial idea highly relevant to governance and policy. This principle posits the notion that a purely market economy is not possible because it requires a set of ancillary institutions, social support networks and public goods to protect the system from destructive creation. Being a more balanced version of Schumpeter's creative destruction, Polanyi established an idea that leads directly to major intervention. It posits that, under a predominant market system, policy requires the provision of safety nets to protect individuals from unemployment, on-the-job accidents, family and community breakdown, financial crises, and problems with the commons.<sup>3</sup>

The disembedded economy signifies the core contradiction of the predominantly market system, namely, that it cannot exist; it operates through a whole series of institutions, habits, systems of knowledge, educational and social capitals, infrastructures and housing, plus the rearing of children (see O'Hara, 2010). In other words, markets have to operate in a complicated series of institutions that require resources from the collective wealth of the community, which itself

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3. The disembedded economy is similar—in some respects—to the FTB *notion of minimal dislocation*, namely, that changes in the social economy are required so as to minimise as much as possible the long-term dislocative effects of such changes (Bush, 2001a, pp.736-737). The FTB system needs adjustment though to recognise that disruption is not just caused by instrumental factors but also by the interface of market forces, technological changes and governance.

contributes public goods for the system. Markets have a terrible tendency to become dislocated from the prevailing systems of economy, ecology and society. This contradiction tends to generate (unless unchecked) serious unequal distributions of income/wealth/power, major periodic financial instability, volatile business cycles plus short and long waves, alienation, social dislocation and familial destruction. Being so magisterial in its significance, the contradiction of the disembedded economy predicates all the other significant contradictions discussed in the following sections of this paper.

More generally the disembedded economy states that there are three 'fictitious-commodities' that a market system insufficiently develops. These include labor power, money and common land. The market system fails to adequately reproduce the required amount and quality of labor power because this is a system function or public good largely outside of its jurisdiction. The business cycle, short and long waves, plus technological changes establish varying rates of economic activity, productivity and skills, usually at less than full employment. Thus various accords are required between groups and institutions, along with a sufficiently developed educational system and health apparatus, to contribute to this labor power reproduction outside normal markets.

The second fictitious commodity is 'money'. 'Free banking' systems of monetary arrangements tend towards periodic instability and crisis, according to Polanyi (1944), because the stability mechanisms provided by the market do not operate effectively due to the failure of monetary provision. According to free bankers, purely free markets in money and banking are required, with the main stability mechanisms being too much credit being provided by some banks leading to a decline in specie, with the result of likely illiquidity and decline in reputation of the banks that are reckless with credit. A similar mechanism is said to operate when nations are over-lending inasmuch as they would have an outflow of specie and a similar decline in economic activity.

According to Polanyi (1944), these free banking stability mechanisms are illusory since during most business cycle upswings a pure market system would lead to a general expansion in lending in various markets, increasing the volatility of the business cycle, and leading to periodic crashes, recessions and depressions (especially during long wave downswings). Hence the need for an effective Central Bank to protect the system from these periodic credit over-expansions. The cause of deep instabilities is the generation of over-and-under expansion of debt that follows from the normal workings of the business system for endogenous money and credit through the innovations provided by banks and corporations. Public goods are therefore necessary in the form of lender of last



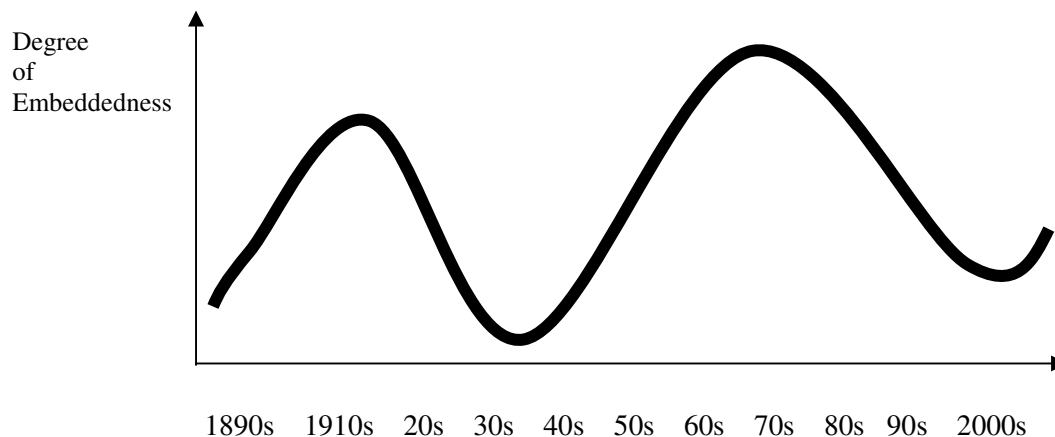
resort facilities, prudential functions, deposit insurance, capital regulations and controls, to protect the system from periodic major instability and crisis.

The third fictitious commodity is 'land' or 'common property'. Polanyi believed that problems of land are not normally solved through the free market, since it produces too many private ownership certificates and fails to provide sufficient public lands. Under the free market, land use would tend to be over-exploited, including the resources, fish stocks and habitats, leading to destruction of critical species, atmospheric processes plus heritage sites and places of natural wonder. He therefore supported policy measures to protect the commons to ensure an adequate supply of natural resources, species and places of beauty for present and future generations.

Closely linked to this fictitious commodity approach to governance is Polanyi's recognition of the instabilities of the business cycle (see Sherman, 1991; Sherman and Kolk, 1996). It is not sufficient to provide adequate and effective monetary policies, but activist fiscal policies are also required. The system-needs for discretionary and automatic fiscal policy led historically to expansion of unemployment relief and demand management techniques. Polanyi (1944) would have accepted Abber Lerner's (1943) rules of functional finance, that demand should be expanded to maximum full employment and that governance should operate in accordance with a counter-cyclical system of conventions. He likely would also have recognised the need to take into account various lags in the system and protect the system from corruption.

The disembedded economy also reveals the 'double movement', which is crucial for understanding the dynamic motion of governance practices. The double movement extricates from history that varying degrees of embeddedness and disembeddedness are historically ingrained in the evolution of state-market relations. Since a fully marketised economy is impossible, some degree of embeddedness is critical for its functioning. Thus, when disembeddedness leads to instability, socio-politico-economic pressures *tend to emerge* for greater levels of embeddedness. The new embeddedness is likely to last perhaps a few decades as the evolutionary contradictions within lead to necessary changes. As these contradictions come into play, along with economic difficulties, through time socioeconomic pressures *tend to emerge* for more disembeddedness (as the old system is 'blamed'), which in turn through time undergoes problems. The double movement of these ongoing waves is inherent in the motion of especially state-capitalist systems of production, distribution, exchange and reproduction.

If such recurring pressures are successful in these differential movements, then short and long waves of disembeddedness tend to be followed by waves of embeddedness followed by waves of disembeddedness, and so on throughout history. This double movement is a powerful explanation for changes in systems of governance throughout the recent history of capitalism. This is related to the *policy wave hypothesis*, as symbolised in Figure 1, below.



**Figure 1:** Policy Waves of Embeddedness and Disembeddedness (Stylised)

Some examples relate to the history of policy since the 1870s to 1890s. In advanced capitalist economies, throughout the 1870s to 1890s there was overproduction in the key sectors, as large-scale industry emerged while competitiveness was fairly strong, leading to low rates of profit and investment. This led to pressure for change, with several institutions emerging during the 1880s to 1910s, including labor unions, banking and accounting institutions, European colonialism and business selling costs (Veblen, 1923), which enhanced effective demand and balanced several contradictions, resulting in higher growth in the core economies during the late-1890s to 1910s (Hobsbawm, 1987). The First World War cut short this wave of growth (van Duijn, 1983) as conflict and later unregulated speculative bubbles and low wages along with problematical policy led to the financial booms and crashes of the 1920s and 1930s, culminating in the Great Depression of the 1930s as disembeddedness became extreme (Hobsbawm, 1994).

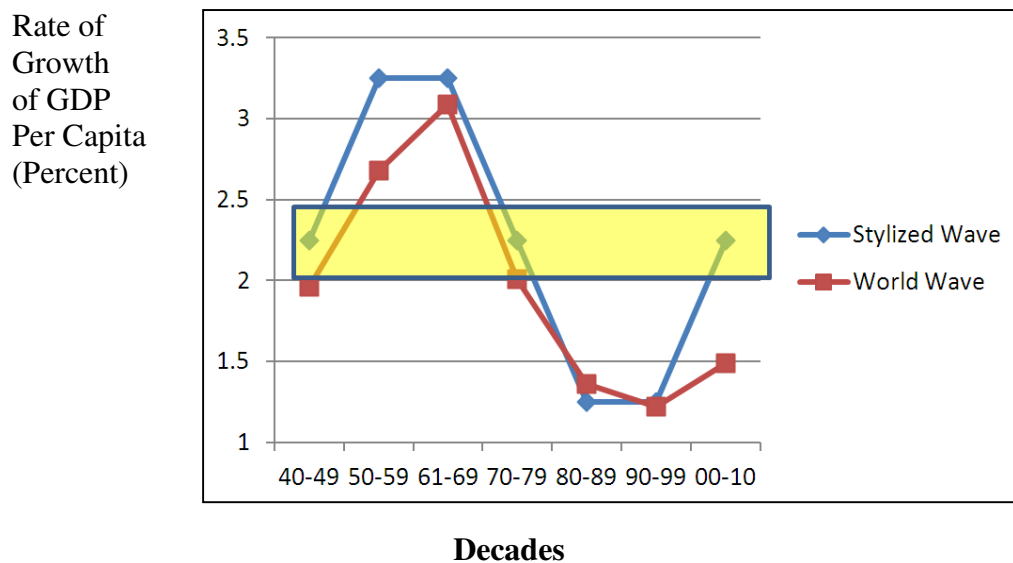
It is well known that out of the Great Depression, Second World War and postwar reconstruction emerged central governments in many (especially Core) nations

with relatively strong financial resources, automatic and discretionary policies, along with a working class mode of consumption that expanded demand. Pressures for change thus emerged, leading to institutions such as Fordism, the Keynesian welfare state (KWS), US hegemony, family formation, and regulated finance, which enhanced demand, socioeconomic reproduction and general embeddedness during the 1950s through to the 1970s. The postwar boom saw long wave upswing in the vast majority of nations for two to three decades until the mid-1970s (Bowles, Gordon and Weisskopf, 1990).

Many see the contradictions of the KWS as representing too many or distorted forms of embeddedness, which contributed to the structural crisis of capitalism that emerged from the mid-1970s onwards (e.g. Claus Offe, 1984). The key contradictions are seen as a heavily bureaucratized state administration, disjointed incrementalism, and decreases in the 'cost of job loss', which contributed to low profit, investment and growth especially during the 1970s (O'Hara, 2000). The KWS was not the only institutional cluster contributing to the anomalous performance. The deteriorating state of Fordism, the capital-labor accord, financial regulation, US hegemony and other institutions also played their role. But both left and right wing economists saw a number of problematic tendencies in the KWS, while their policy reactions were quite different.

Out of the perceived failures of the form that embeddedness took into the 1970s emerged Thatcherism and Reaganomics, supply side economics and rational choice theory, along with the hegemony of neoliberalism into the 1980s to 2000s. This reversion back to a more disembedded form of governance was instituted to contribute to better economic performance. However, it has failed to achieve this objective. Figure 2 compares the Stylized Wave (perfect) with the World Wave of gross domestic product (GDP) per capita growth (decadal annual averages) for the period 1940 to 2010.

The World Wave is almost exactly the same as the (perfect) Stylised Wave. They both start at borderline growth (2.01-2.50 percent) in the 1940s; then undergo twenty years of long wave upswing in the 1950s to 1960s (above 2.50 percent growth); followed by twenty years of long wave downswing (below 2.01 percent growth) in the 1980s and 1990s. The only difference is that in the 2000s the Stylised Wave goes back to borderline—thus completing a Full Wave from borderline-up to borderline-up—whereas the World Wave continues a long wave downswing. The world has thus been suffering from a deteriorating regime of accumulation, including insufficient demand, productivity and growth, through long wave downswing over recent decades.



**Figure 2:** Stylised Wave, World Wave; Gross domestic product (GDP) per Capita, 1940 to 2010 (Decadal AAGR)

Source: Adapted from O'Hara (2012a); based on raw data of Maddison (2007), World Bank (2011) & De Long (1998, p.6).

Note 1: These decadal averages are based on the method of summing individual annual average growth rates for each year and then dividing by the decadal number of years (AAGR; mostly 10 years; sometimes 9 or 11, e.g., 1961-69, 2000-10).

Note 2: The bar in the middle is the area of 'borderline' performance (2.01-2.50% growth) in between upswing and downswing.

Decadal annual average growth rates of GDP per capita are shown in Table 1, below; and then short, long and secular wave phases and periodicities are mapped in Table 2, for the World and its various continents/regions:

**Table 1:** Real GDP Growth Per Capita (Decadal AAGR), World, Continents: 1950–2010

	<b>World</b>	<b>NA</b>	<b>WE</b>	<b>CEE</b>	<b>LACA</b>	<b>MENA</b>	<b>SSA</b>	<b>Asia</b>
1940-49	1.96	3.55	□-0.71	1.24	2.06	n.a.	n.a.	-3.33
1950-59	2.68	2.09	4.03	3.68	2.03	3.49	1.82	3.82
1961-69	3.09	3.21	4.03	3.68	2.59	3.90	2.09	3.77
1970-79	2.01	2.60	2.94	3.26	3.19	5.77	1.30	3.39
1980-89	1.36	2.06	1.99	0.22	0.19	-1.63	-0.68	2.96
1990-99	1.22	1.91	1.88	-0.70	1.18	2.07	-0.60	2.87
2000-10	1.49	1.08	1.18	4.46*	2.35	2.42	2.34	4.32

Source: Adapted from O'Hara (2012a, p. 6); based on raw data from Maddison (2007), World Bank (2011) & De Long (1998, p. 6)

\* Based on growth for CEE5 (Russia, Hungary, Poland, Bulgaria, Czech Republic; population weighted).

NOTE: AAGR=annual average growth rates; CEE=Central & Eastern Europe; GDP=gross domestic product; LACA=Latin America & Caribbean; MENA=Middle East & North Africa; n.a.=not available; NA=North America; SSA=Sub-Saharan Africa; WE=Western Europe.

**Table 2:** ‘Map’ of Short, Long and Secular Wave Phases (Decadal GDP AAGR) World, Continents/Regions: 1940–2010: Upswing, Borderline, Downswing

	<b>World</b>	<b>WE</b>	<b>NA</b>	<b>CEE</b>	<b>MENA</b>	<b>LACA</b>	<b>SSA</b>	<b>Asia</b>
1940-49	B	SWD	SWU	SWD	n.a.	B	n.a.	SWD
1951-59	LWU	LWU	B	LWU	LWU		SWD	LWD
1961-69			LWU			B		
1970-79	B		LWU			B		
1980-89	LWD	LWD	B	LWD	SWD	LWD		
1990-99			LWD **		LWD		B-LW	
2000-10			LWD **	SWU	B	B		

Source: Adapted from O’Hara (2012b, p. 4). Based on Table 1.

\*\* Main areas of Great International Crisis of 2008-2012.

Note: AAGR=annual average growth rates; B=Borderline; CEE=Central & Eastern Europe; GDP=gross domestic product; LACA=Latin America & Caribbean; LWD=long wave downswing; LWU=long wave upswing; MENA=Middle East & North Africa; n.a.=not available; NA=North America; SECWU=secular wave upswing; SSA=Sub-Saharan Africa; SWD=short wave downswing; SWU=short wave upswing; WE=Western Europe.

Neoliberal-neoclassical dominance of theory and policy over the past thirty years has been unsuccessful in restoring performance to upswing for the World economy and its major economies. The World and its Core, especially Western Europe and North America, have been undergoing long wave downswing over the past 20-30 years, culminating in the great international crisis and recession of 2008 to 2012, which affected mainly this Core. All the other areas of the World, mostly those deviating substantially from the neoliberal model, show some optimistic developments. These include borderline results in Latin America, Middle East and North Africa, and Sub-Saharan Africa; short wave upswing in Central and Eastern Europe; and secular long wave upswing (upswing for 40 years or more) for the past sixty years in Asia. However, it should be stressed that economic performance is strongly linked to other institutions besides the state (and neoliberalism), including also the decline of the capital-labor accord, US hegemony and the industrial strength of the advanced capitalist economies (Core relative to Semi-Periphery) (O'Hara, 2006; Raffer, 2011).<sup>4</sup>

There are three critical lessons for policy from these waves of embeddedness—disembeddedness and economic performance. The first is that governance structures—and the economy as a whole (World, continental, national and sub-national)—do tend to move from waves of varying levels of disembedded to more embedded and then onto more disembedded waves through time; as well as waves of high and low growth (plus other indicators). The wave hypothesis must be incorporated into practical policy analysis because there are wave-like changes in the social economy that impact on government budgets, funding needs, social stability, financial crises, growth potential, labor supply issues, ecological changes and similar socio-politico-economic issues.

Secondly, it is useful to have different policy ideologies evolving at the same time to provide a foundation for changing levels of embeddedness, depending on the flow of institutions at the time. Many people have wondered why economists often have so very different ideas about how to organise the economic system. The double movement indicates that, without this pluralism and ideological diversity, necessary reforms into the future would perhaps be difficult. Complicated systems of belief and ideology are required for public life and policy

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4. Decadal GDP growth rates per capita for Australia are 1.68 percent (1950-59), 2.95 percent (1961-69), 1.67 percent (1970-79), 1.87 percent (1980-89), 2.07 percent (1990-99) and 1.66 percent (2000-10). Australia thus underwent (short?) wave downswing in the 1950s; short wave upswing in the 1960s; long wave downswing in the 1970s to 1980s; a borderline wave in the 1990s; and short wave downswing in the 2000s (Maddison, 2006, World Bank, 2011.) This is a similar story to that of the World, and the Core areas of North America and Western Europe, which are *also* undergoing a regime of accumulation anomalies (see O'Hara, 2008b for the Australian situation).

structures for any required changes to be instigated or evolved through time. The stock of knowledge in political economy needs to be fairly wide in scope given the complexity of the real world, and also since pressures long into the future can benefit from this variety as a stock of potential strategies, synergies and principles of action or inaction.

And thirdly, the double movement provides a useful lesson that we must transcend simplistic dichotomies of state and market to analyse socioeconomic waves of motion. As we see later, state and market need to be supplemented by other institutions such as civil society, family, corporation, plus of course the system of production and the world economy. The institutional structure and dynamics of capitalism or advanced societies are necessarily complex and therefore policy processes need to be developed accordingly. The more advanced the society the more complex the structure and dynamics are likely to be. Policies and governance processes must be cognisant of the diversity of social and ecological arrangements in the real world, and that markets are necessarily imbued with safety nets to protect the populations inhabiting and surrounding them.

This notion of the disembedded economy has been the fulcrum of numerous political economy movements. Institutional economists such as Walter (Terry) Neale (1976) and James Ronald Stanfield (1986) spearheaded linkages with the Polanyian movement. International political economists have been researching the disembedded economy in relation to international and regional institutions such as the European Union, International Monetary Fund (IMF), World Bank, World Trade Organisation (WTO), plus production networks and commodity chains, to mention just a few. Feminists, cultural economists and radical political economists have also been using the concept to advance awareness of the need for embeddedness in the social economy.<sup>5</sup>

## **Principle of Contradiction**

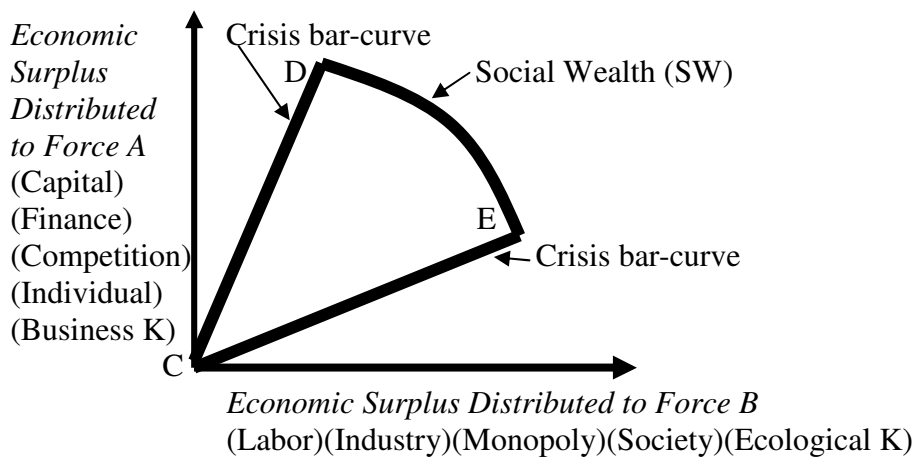
The disembedded economy is the prime contradiction of capitalism, but there are others that affect the lives and fortunes of many. Contradictions are the prime

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5. Literature on the disembedded economy, embedded liberalism and related themes is substantial. The Karl Polanyi Institute of Political Economy in Canada has advanced such knowledge (e.g. Cangiani & Maucourant, 2008). International political economists have researched the concepts in journals such as the *Review of International Political Economy*, *International Organization* and the *Journal of World-Systems Research* (see, e.g. Ruggie, 1982; Dale, 2010). Social structures of accumulation scholars have also analysed the disembedded economy and the double movement (e.g. O'Hara, 2000; Wolfson, 2003).



movers of societies, the forces that generate motion, dualities that promote potential conflict (and require cooperation). They generate endogenous sources of change and metamorphosis. The key thing is to bring out their *concrete forms*, rather than delving into the realm of abstraction and uniformities. Contradictions need to be *brought down to the ground* and linked to the historical genesis of capitalism (and other systems). They have to do with opportunity costs or trade-offs between various forces, as indicated below in Figure 3.



**Figure 3:** Trade-Offs Between Contradictory Pairs

Source: Adapted from O'Hara (1999, p. 134).

In figure 3 the DE bar-curve represents the social wealth of the community; the economic surplus, being a product of the skills, capabilities, institutions, capital structures and effective demands of the community. Economic surplus is variously distributed to capital or labor; finance or industry; competitive or monopoly forces; individuals or society; business or environment. If too much is distributed towards any of the forces, combined or collectively, then this tends to generate systemic crises and deep recessions, including major financial crises. During such crises the *destruction of social wealth* occurs (the SW curve moves inwards) along either extreme bar-curves, CD or CE, as variously financial, economic, ecological and social instability, dislocation and fragmentation periodically become more extreme. Ideally these crisis bars are quite thick, due to problems with knowledge and also indeterminacy. The further the SW curve

moves inward (reflecting destroyed social wealth) along the periodic/structural crisis curves (CD, CE) the greater the depth of crises.

The core contradiction is that between capital and labor. Historically, the relationship between workers and business has been a prime factor involved in the determination of production, distribution and exchange. This association has been at the forefront of the determination of wages and the rate of profit, influencing the lives and standards of living of families and communities. Capital represents the interests of business, including the means of production of machinery, buildings, implements, as well as the flow of finance into enterprises and the stock of inventories moving into shops and warehouses. The people who control these business assets may be called capitalists, usually comprising CEOs, managers, small traders, financiers, and members of the Board of Directors. The people who work for these people, in return for a wage or salary, are the workers, those who depend upon their skills (or lack of) for a wage and have little controlling interest in business. Some of the workers may be deemed part of the Middle Class, which appears to be diminishing in relative numbers in the Core, plus the Lower Classes, including those working part-time, those in declining sectors, and the informal sector. Below these are the unemployed, the sick, and the homeless.<sup>6</sup>

Historically, the institutions associated with capital and labor have been a critical part of policy-making. The difficulties of establishing a viable wage level, appropriate skills, cooperation in industrial relations, the free flow of commodities, and workplace conditions are at the core of policy-making. The capital-labor accord in the US (and many other Core nations), for instance, in the 1950s to 1970s was a system of full employment based on agreements between capital, labor and the state. The rise of Thatcherism and Reaganomics, along with neoliberalism, into the 1980s to 2010s was seen as a policy shift towards deregulating industrial relations, and increasing the power of capital vis-à-vis labor. The union movement has been in retreat over the past several decades, which is part of the trend for credit to substitute for wages in the financing of consumer durables. Workplace agreements and on-the-job decisions have changed the focus of the debate somewhat to more decentralised institutions.

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6. The debates on class in political economy are very extensive, such as delineating class on the basis of property, power or surplus value. The major debates relate to the literature of John E. Roemer (1982), Stephen Resnick and Richard D. Wolff (1987), plus Samuel Bowles, Richard Edwards and Frank Roosevelt (2005), and extensions of these perspectives. Resnick and Wolff, for instance, do not see classes as specific groups of people, but rather as multiple class positions based on the relationship to the production, distribution and exchange of surplus value (including households). See also the work of Steven Pressman (2007) on the global decline in the Middle Class.

However, there are major problems when capital dominates labor, such as over the past thirty years in the Core nations and many others. These problems manifest themselves in major inequality between the high income achievers and the rest of the population. The dominance of capital over labor was influenced by the very structures of competition and uneven industrial development operating on a global and region scale. Lower real wages lead to more cyclical conditions due to financial instability, leading to greater financial crises through increases in debt for the middle and working classes, along with business, while increasing conspicuous consumption and waste of resources.

A society based on consumption and position in the social stratum is ceremonial in that it increases competition between persons and also increases the level of stress to keep up with the Joneses (Veblen, 1899; Perez-Truglia, 2012). Typically political economists would advocate trying to moderate these contradictions between capital and labor through the implementation of accords, worker cooperatives, efficiency wages, social wages, worker participation programs, extended human capital schemes, community development initiatives and similar projects. These schemes seek to promote embeddedness and, if their provisions become extreme, may contribute to systemic crises for capitalism and/or help to generate the roots of a new communitarian system.

The contradiction between monopoly and competition is another core issue of policy. Schumpeterian economists have established this dichotomy as a key area of analysis (Cantwell and Santangelo, 2000). For them the ability of modern capitalism to generate ongoing innovations provides a foundation for short-term monopoly profit, followed by greater competition, further innovation and sectoral change, in an ongoing process of creative destruction. If this process proceeds unimpeded, it is said to generate continual growth and accumulation, employment and prosperity. The ability to reduce the incidence of patents and copyright somewhat is an important part of this process, as protecting vested interests is said to reduce the flow of innovation and competition through time, if they last too long.

'French' Regulation and social structure of accumulation scholars (SSA) (e.g. Bowles et al., 2005) have a modified version of this process whereby an evolutionary balance is required between monopoly and competition for the profit, accumulation and growth equation to operate effectively. For them, too much competition produces too few profits and therefore insufficient accumulation and growth. A dynamic adjustment process of reasonable monopoly profits for a time is said to balance the destructive powers of competition, without destroying it altogether. For instance, the postwar era of Fordism was

characterised by this balance, whereas neoliberal globalisation (with higher levels of competition) has been characterised by insufficient profit and accumulation. The differences between these schools (Schumpeterian, SSA) provide a fertile environment for active policy inquiry into the empirical evidence and how this dialectic relates specifically to industry policy (Elsner, 2003), competition policy and the use of tariffs and subsidies, as the economy moves through varying degrees of imbeddedness and disembeddedness.

Recently another contradiction (linked also to the capital-labor contradiction, above) has come to the fore in the form of the industry versus finance conflict. Industry is the generation of knowledge, productivity, innovation and research and development. Finance is the provision of money, credit, bonds, equity, foreign exchange and other relatively liquid assets and liabilities. Closely linked to finance are the speculative sectors of domestic and commercial real estate. Often industry and finance work in cooperation, especially during the recovery and medium-boom of short cycles. This is also the case when finance is moderately regulated, such as during the postwar boom of the 1950s through to the early 1970s, especially in the Core nations. Some level of dynamic balance seems to be required for finance to support the interests of industry and society. When deregulation becomes too extreme, financial crises tend to become quite entrenched during long wave downswings. Such was the case in the 1920s and 1930s as well as during the 1980s to 2000s when finance has dominated industry.

As argued above, during the 1910s to 1920s finance was deregulated as it contributed to the speculative bubbles and crashes of the 1920s and 1930s. Regulators then introduced more effective central bank activities, including lender of last resort facilities, separation of investment and commercial banking, interest rate controls and qualitative directives during the 1930s through to the 1950s (and beyond into the early 1970s). The (re)emergence of deregulation into the mid- to late-1970s onwards saw the development of severe financial crises/recessions, including the early 1980s crises, the late 1980s/early 1990s stock market crashes and recessions, and the corporate crises and recessions of the early 2000s. The most recent crisis manifesting in the international subprime debacle and deep recession, which has impacted negatively especially on the Core economies of Europe and the US during 2008 to 2012, is the most obvious example of instability closely linked to deregulation and greater disembeddedness.

The current crisis has brought to the fore problems of deregulation through 'innovations' that increase systemic risk through the distancing of mortgage arrangements from securitised mortgage bonds with increasing proportions of subprime assets in the portfolio. The deregulated environment failed to self-

regulate as individual assessments of risk were often fraudulent and failed to recognise rising systemic uncertainty during the cycle boom of 2005 to 2007. The circuit of money capital was thus subject to major dislocation of an uneven nature throughout the world, especially in the Core nations, as differential yet relatively deep levels of uncertainty, liquidity preference and recession prevailed over recent years.

To prevent major depression on a global scale, governments have seen the need for massive bailouts, in the form of trillions of dollars of lender of last resort bailouts, large interest rate discounts, bank nationalisations, increases in deposit insurance, and even bailouts of manufacturing companies (O'Hara, 2011b). Heads of many governments (e.g. USA, Australia) have announced the official end of the neoliberal and deregulation experiment. The first counter to neoliberalism was the Asian crisis of the late 1990s, when the IMF initiated major reforms such as quasi-lender of last resort facilities and protecting innocent bystanders (poverty relief), after deregulation in the early 1980s. The second was the corporate crisis of the early 2000s when the Sarbanes-Oxley Act took effect to counter corporate self-regulation. This third crisis, mostly blamed on deregulation, is *possibly* (though unlikely) the start of a concerted embedded tendency for capitalism, which may institute a type of balance between industry and finance (especially in the USA), although Europe especially seems to be tightening the power of markets in response to debt crises and potential or actual contagion. In this context, recent years have seen evidence that increasing inequality in several nations, regions and continents is adversely impacting socioeconomic performance as disembeddedness became more extreme (see Rohit, 2011; Whalen, 2011).

A fourth contradiction that has recently become more obvious is that *between ecological capital and durable fixed capital*. Global ecological capital has declined over the past quarter of a century by around thirty percent while greenhouse gasses (GHG) have expanded by 15 percent (stocks) or 100 percent (flows). This inverse relationship between ecological resources and business/consumer capital (along with human populations) illustrates the contradictions at play between human activities and their destructive effect on the natural environment. The major sources of this expansion of GHG are industry (19%), transport and building (21%), agriculture and forestry (31%), energy (26%) and wastes (3%) (IPCC, 2007). The desire for business profit and gluttonous consumption (along with expanding human settlements) have been the major factors responsible for the climate change phenomenon.

It seems 2007 to 2008 has been a critical period when most of the major players agreed on the magnitude of the problem. Certainly the core reports (IPCC, 2007; Stern, 2007, UNHD, 2007; Garnaut, 2008) that have been commissioned by major governments, and the responses thereof, indicate broad agreement about the need for more embeddedness to restore ecological/environmental balance and diversity. While being rather late in the day for agreement, it is not too late for changes. Unless GHG stocks are stabilised in the long term at about 300-350ppm, global temperatures are going to increase more than 2°C (above preindustrial levels) leading to major tipping point catastrophes. These include destruction of the Arctic sea ice, melting of the Greenland ice sheet, separation of the West Antarctic ice sheet from the bedrock, moderation of the Gulf Stream, expansion of the El-Nino phenomenon, and deforestation of the Amazon rainforest (Lenton, 2008). These tipping points are the major catastrophes in store for us if the world fails in its efforts to moderate the climate change phenomenon.

Policy-makers will have a difficult time responding to these challenges since major reductions in GHG emissions (flows) are required to reduce the high level of GHG stocks (major lags are involved). The first thing required is global accord, following on from the Kyoto Protocol, but being more widespread in appeal and scope, and more diligent in addressing the problem. This is especially problematic in the face of the current crisis, European debt crisis, national interests, terrorism, and global discord. The second thing needed is a price on carbon that is higher than market price, and if the EU and US experience is any indication then this is not going to happen any time soon. Several national and regional initiatives are likely required before any effective regime possibly emerges to reduce global GHG emissions to appropriate levels.

The third thing needed is changes in technology, especially in reducing carbon emissions. Sequestration is a likely candidate but questions still remain about storage problems. China has to play a leading role here, which will impact on their growth into the future. The key thing is to place an emphasis on profit or production per unit of GHG emissions to internalise the social cost. Vested interests, such as various national concerns, businesses and consumers, continue to be the main opponents of change. The culture-institutions-habits nexus is a constraint on change. If there is success with these anti-GHG emission technologies, accords and changing habits and institutions, alternative long waves of development and policy may emerge that are more ecologically embedded than the current regime of institutions.

Clearly these contradictions are at the forefront of policy-making and governance issues. They involve various opportunity costs and trade-offs, which need to be

balanced by accords, agreements, new institutions/systems/habits rather than purely market forces.<sup>7</sup> Institutions, markets, governments, individuals, families and civil societies are important in the ongoing and temporary resolution of contradictions. They are always ongoing and being modified as history changes relationships and sudden metamorphoses emerge from time to time through varying degrees of embeddedness and disembeddedness.

### **Principle of Circular and Cumulative Causation**

Probably the major challenge for any governance program is that the core problems of the world tend to be multi-causal. Rather than having singular origins they are complex, involving numerous interacting variables, and often cumulating multiplier impacts. Hence the orthodox idea of having one (or even two) instruments for each target seems very simplistic. Equilibrium models and *ceteris paribus* assumptions are hardly ever useful for investigating the causes and solutions to complex problems. Instead, the more realistic model of circular and cumulative causation (CCC) can usefully be employed in governance issues. This model was developed by Gunnar Myrdal and Nicholas Kaldor variously to centre on policy issues originating from monetary problems, ethnic issues, development possibilities, and growth potentialities. It has since been used by many others to study urban and regional problems, AIDS and HIV, terrorism, subprime crisis, and a host of other policy issues (Berger, 2009). At the higher reaches of theory/empirics CCC has evolved into complexity analysis and emergence (see Arthur, 2007).

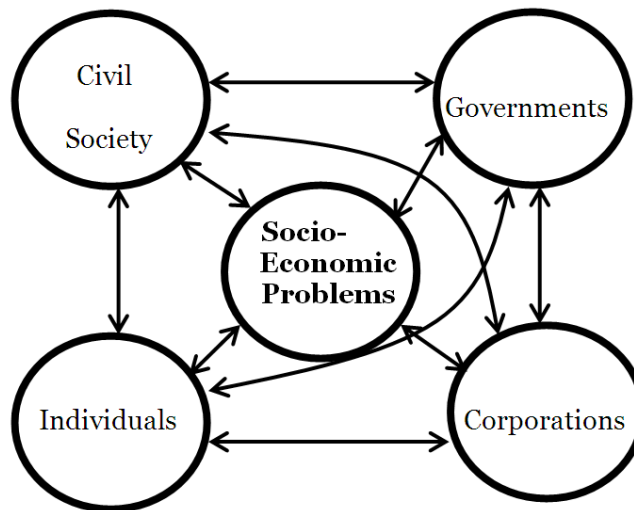
CCC includes five main features. The first is that the whole social system needs to be examined in relation to the problem at hand, or at least micro questions need to be linked into a macro, regional, and/or global framework. The second is that there is a degree of interdependency between variables, in the sense that most socioeconomic problems have a relatively large number of co-factors, usually of both a qualitative and quantitative nature. The third is that the variables tend to operate in a cumulative manner; that there is a multiplier effect with feedback processes involved. There may in fact be multiple cumulative effects, with some operating in different directions. The fourth is that there are contradictions

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7. These contradictions, when viewed as imbalance caused by the often-dominant forces of capital, finance, competition, individual and business capital, embody much of what Fagg Foster and Dale Bush—in a broad Marc Tool-type model of instrumental valuation—(FTB) scrutinise in the principle of ceremonial encapsulation, where progressive change is inhibited by ceremonial dominance of instrumental processes (Bush, 2001b, pp. 80-82). i.e. the *invidious use of power or knowledge* by the market system, capital or labor, finance or industry, monopoly or competition, core-periphery forces, and so on.

(discussed above) usually operating as well, where there are various trade-offs and opportunity costs negatively impacting on the system. These contradictions may either counter some of the cumulative impacts or impose dual cumulative movements (some in different directions). And finally, a core factor often intervenes into the complex mosaic: for Myrdal (1944, 1968) it was education; for Kaldor (1966, 1972) demand; for Amartya Sen (1999) capabilities and freedom; and for Dale Bush (1987), technological change (broadly conceived to include skills, knowledge and communication).

CCC models link well with modern perspectives in recognising that governance is much more than simply 'government' or the 'state' (departments, executive, legislature and judiciary). Governance has more to do with the general provision of adequate levels of embedding processes that provide system-functions or public goods necessary to solve complex problems. The amount and nature of these embedded goods depend on the desired process of reform, whether social capitalism or a more communitarian system is considered proper in the current or future environment. Polanyi recognised that various institutions and individuals can potentially provide embedded goods that prevent or reduce the extent of problems, as indicated below in Figure 4:



**Figure 4:** Quadratic Elements of Governance

This figure illustrates that all the dominant social institutions and groups as well as individuals influence the problem at hand; whatever it is, subprime crisis, climate change, terrorism, AIDS-HIV, growth and development, and so on. Political economy and now some modern progressive schools of governance



believe that all sectors of society have a *responsibility* to provide goods that protect the system from crisis and instability. There tend to be waves of uncertainty that have broadly followed the embedded—disembedded wave dynamic, due to three interrelated processes.

These include, firstly, lack of information, understanding, skills, knowledge, organisation, capabilities and trust within core elements of the complex process by which people interact in social life. Secondly, there is asymmetric distribution of information, understanding, organisation, skills, knowledge, capabilities and trust between people in these activities. And thirdly, there are differing geopolitical and socioeconomic distributions of powerful systems of production, distribution and exchange throughout the World. Changes in these three variables through long historical time reveal waves of socioeconomic performance and phases of evolution. It is critical both to advance this theory and also to promote empirical inquiry into these areas for a proper system of governance and policy to emerge.

A core idea of political economists is that all of the dominant sectors and agents have a role to play in balancing the conflicts involved in provisioning. Indeed, the critical need is to inculcate into the dominant institutions, including individuals, a belief and commitment to a wider vision, a social view of interaction - 'recognised interdependence' (Bush, 1987). Corporations need to see themselves in a wider context, as do governments, civil society groups and individuals. The degree to which they seek a wider context for collective action is likely to be an indication of potential solutions to social problems.

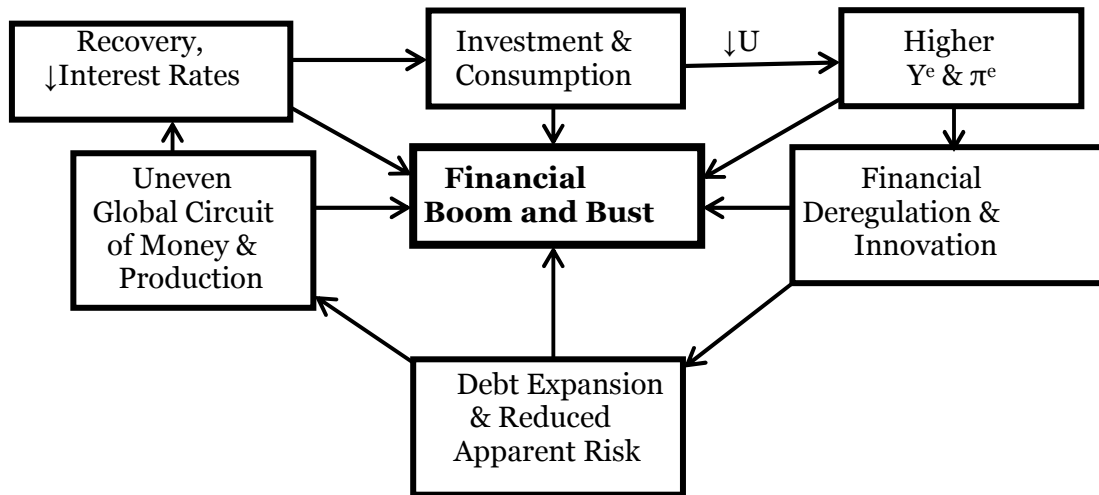
This wider vision of political economy governance views corporations as having a social responsibility to moderate their own negative externalities; individuals and civil society groups to see beyond their narrow domain to the whole community and linkages to other communities; governments able to balance short- and long-term objectives in the interests of the common good, including beyond its electoral, nation state, and local dynamics; and all segments of society interacting with a view to comprehending and improving the functioning of the provisioning process.

Socioeconomic problems are thus caused by the inability of institutions and individuals to see beyond their own short-term vision to communicate and meaningfully seek resolution of ongoing problems with other groups and individuals. The extent to which they isolate themselves to their own functioning and ignore linkages and associations with other segments and individuals is likely to be positively associated with socioeconomic problems, or an inability to

resolve them in a timely fashion. True democracy, in a political economy perspective, is not simply electing governments in every electoral cycle, but having people involved in matters that affect both themselves and the community as a whole. This decentralised form of political economy reveals the true anarchistic or 'republican' origins of its advocates and the underpinnings of its beliefs (Vanek, 1975; Tool, 2001). But still quite often we are left in the situation where rapid changes and asymmetric distributions of resources and knowledge lead to greater disembeddedness, and in this context the state is periodically under greater pressure to intervene where other processes have failed.

The quadratic elements of governance represent a useful model not only for comprehending the ideological and policy beliefs of political economists, but also for understanding the sources of problems. In this model, governments are not only seen as a possible solution to the problem, but also as one of its causes. In like measure, the tendency in various quarters to blame governments for problems, either because they intervene when they should not, or because they fail to intervene when they should, seems a rather narrow view of governance. Political economists tend not to assume that all critical problems should be solved by government, but they do believe governments can play a very useful role in a wider quadratic context.

Consider the example of the current (2008 to 2012) uneven international financial and economic crisis, and the factors that have impinged on its inception and development, as illustrated in Figure 5, below. The factors involved are multifarious (see O'Hara, 2009b for details). In the United States, the initial recovery of aggregate demand from the early 2000s recession, lower official interest rates and less uncertainty eventually stimulated investment and consumption spending. The government is possibly implicated through lowering interest rates too low for too long and increasing them too much too quickly. This contributed to a period of optimism, lower unemployment, eventually expanding the share market, expected income ( $Y^e$ ) and profits ( $\pi^e$ ) over 2004 to 2006. For instance, in the US the eight month recession of March to November 2001 was followed by six years of (slow) recovery and then boom. Many nations of the world followed a similar pattern.



**Figure 5:** Circular and Cumulative Causation (CCC) vis-à-vis Great Crisis of 2008 to 2012

Source: Adapted from O'Hara (2009b)

NOTE:  $Y^e$ =expected income;  $\pi^e$ =expected profits; U=uncertainty

As a result of activist central bankers, financial deregulation and innovation, credit over-expanded dangerously in relation to income, because euphoric conditions enhanced expected income and profitability much greater than actual long-term income growth. This higher level of debt, including the democratisation of debt and predatory lending/debt, contributed to the boom and fragility. In an environment of uncertainty, where prospective yield is associated with long-term conditions, the prevailing business climate is often used as a proxy for future conditions. Hence during good times this leads to expanded credit as investment conditions improve. During the recent era of neoliberalism, finance has become more deregulated, which has expanded credit access. This has been an uneven process globally. For instance, debt to income ratios have increased considerably over the past fifteen years, especially in advanced capitalist economies (Mizen, 2008), a fact that Steve Keen has, for instance, been reiterating in several media over recent years.

Debt escalation was especially notable in the major neoliberal economies, such as the US, UK, Iceland and continental Europe, where the economy had been earlier

deregulated and turned neoliberal. The expansion of credit went hand-in-hand with a decline in quality of loans, as the boom led to bubbles in the major markets of housing and equities, financed through different forms of credit arrangements. This is linked to the expected income—credit—investment transmission mechanism of boom and then crash through financial crises. First, a decline in uncertainty through an optimistic business climate generates greater investment and consumption. This expansion of euphoria, credit and investment beyond fundamentals occurs to a much greater extent when there is wholesale deregulation of the financial sector, and central bank generation of excessive interest rate fluctuations.

Hyman Minsky's (1982) '*short memory hypothesis*' is relevant here, since agents tend to forget about past recessions and financial crises and set up expectations based on the *prevailing business climate*. Also, much of the so-called investment is misallocated during eras of wholesale financial deregulation as the public good of stability declines. It is especially misallocated to the relatively cyclical and speculative sectors such as the secondary stock market, the property market and the foreign exchange market.

Financial innovation and deregulation, including disintermediation and securitisation of mortgage market securities, enhanced the boom and fragility. The financial innovation of securitising subprime mortgages led to problems of lack of available market information about who had the mortgages, what was the quality of the collateral, and what would happen if the boom in housing and equality markets faltered. The *complexity* of the securitised mortgage bonds as well as the collateralised debt obligations (CDOs) was an especially critical problem leading to informational and social capital anomalies.

Rating agencies and institutional mis-pricing of risk played a role. There has been a conflict of interest between ratings agencies such as Moody's and Standard and Poor's, providing ratings for companies and also providing financial advice. The lack of suitable information exchange between borrower and broker, broker and originator, issuer and originator, trustee and issuer, asset fund and trustee, plus investors and asset manager followed through to credit rating agencies. Appropriate ratings depend mainly on the quality and quantity of information, and rating agencies and others failed to incorporate appropriate *systemic risk* into their calculative models. These ratings agencies provided financial advice on how the buyer of the risk assessment might organise its bond offerings, which depends in part on the risk assessment provided. They were thus unlikely to criticise their own risk assessment in advising how to offer the bonds. The risk models also were highly contingent on continuing rising housing prices, for instance, so

alternative risk assessment scenarios (stress testing) would have helped a great deal (O'Hara, 2009).

These multiple factors accentuated the housing boom, which in turn enhanced aggregate demand and the circular and cumulative process ran through several runs. All of the factors contributed to the bubble and hence fragility and subprime crisis. Debt overexpanded based on euphoric expectations and bubbles in the housing and equity markets. The government perhaps contributed to volatility through the use of interest rate adjustments (from very low to much higher rates). All this happened while agents assumed risk was relatively low, while systemic risk was rising especially since midway through the boom (after 2004 to 2005). Eventually agents realised their calculative models of risk were wrong and they escalated risk assessments *suddenly* to reflect high levels of uncertainty (2007 to 2008). While this was happening housing prices declined, demand for securitised bonds evaporated, and equity markets went into freefall, as the credit crunch started to take hold (2008 to 2009).

Problems in the US led to liquidity problems elsewhere in the global economy in close proportion to the extent that financial institutions and agents were buying US securitised bonds. Close global linkages between financial institutions in the circuit of money capital led to chains of bankruptcy in the financial institutions, especially in Iceland, the UK, Europe, and Japan; but there were some flow-on effects to numerous other nations and problematic global growth and investment (O'Hara, 2012b). Three aspects of policy helped to moderate the subprime crisis somewhat. The first was lender of last resort, where the state offered massive credit to financial institutions to increase liquidity; this was also linked to lower interest rates to enhance confidence.<sup>8</sup> The second was a massive fiscal stimulus to generate demand through both the private and public sectors. And the third was some moderate assistance to mortgage holders to reduce the rate of foreclosure. None of these have, however, solved the long-standing problems associated with rising inequality, financial dominance of industry and the changing geopolitical, socioeconomic and sectoral distribution of power (especially between Core and Semi-Periphery).

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8. The contradictions associated with low/high interest rate policy are intriguing. On the one hand, reserve banks (especially in the US and Europe) tended to push interest rates down to low levels to stimulate recovery in the early/mid 2000s (2001 to 2005), followed by much higher interest rates when inflation pressures were starting to impinge in the mid-late 2000s (2005 to 2007); the same policy reaction, to reduce rates during the crisis and even much later (2007 to 2012), while seen as absolutely necessary for economic survival, may in the long term destabilise investment and markets. Austrian and post-Keynesian scholars tend to recognise these potentially destabilizing aspects of monetary policy.

Currently Europe is undergoing their worst crisis and recession since the Great Depression as 'debt crises' (as they are called) lead to further neoliberal policies, while the US is undergoing the very tentative first step to what may be recovery of sorts. All this as Australia managed to lessen the negative impact of the 2008 to 2012 international crisis through being only moderately involved in the holding of US mortgage-backed bonds and CDOs; having proactive discretionary policy at the onset; and having close sectoral linkages to the Asian (especially Chinese) expansion. This Great International Crisis is better viewed through the lens of a non-equilibrium approach such as CCC set in a context of contradictions, disembedded tendencies and uneven developments.

### **Principle of Uneven Development**

The principle of uneven development has been a core principle of political economy for decades now. It has its roots in the desire to be realistic and follow the empirical process of growth and development throughout the global, regional, national and subnational political economies. Much of its edifice came from regional, development and international segments of the transdiscipline. Key scholars contributing to the principle have been Stephen Hymer, Samir Amin, Immanuel Wallerstein, Andre Gunder Frank, Amitava Krishna Dutt and many others. Institutionalists have followed through on this work with contributions by (among others) Thorstein Veblen, James Street, Dilmus James, James Dietz and James Cypher. The core idea is that the orthodox emphasis on convergence of nations towards the leading economies is highly abstract and not found in much of the empirical evidence. Some convergence trends operate, but often the divergences are more interesting and conspicuous. Therefore, governance theory and practices need to recognise this fact and incorporate it into the decision-making conventions and institutions.

There are many reasons for a combination of convergence and divergence, with critical elements of uneven development occurring in the regional and global economies. The first is that while knowledge is a public good and is difficult to privatise it can also be embedded in institutions, cultures, organisations and conventions that can prevent it from being distributed freely and widely. As Dale Bush (2001b) recognised, knowledge can be ceremonially encapsulated by the vested interests, being also used to protect their power and authority from competition and open access. Hence the knowledge of the leading technological processes, technical solutions to specific problems and organisational ways of enhancing markets and sales are not open to use by the general population. They tend to be privatised through patents, copyright, inside information, tacit knowledge, and organisational capabilities.

The second is that knowledge that is easily bought and sold is subject to distribution through various commodity chains and production networks. These chains and networks are based on various forms of organisation and communication within and between businesses mainly through the leading markets and economies. For instance, the consumer-oriented value chains of leading sports shoes tend to operate between Asian producers and European and US consumers and distributors via transnational alliances. The producer value chains of mass production vehicles is based on Japanese and advanced capitalist economies linking to parts manufacturers in Asia and Central Europe plus consumers in the advanced economies. These productive, distributive, exchange and financial networks are very powerful modes of authority and business with cultural and organisational overtones (Dickens, 2009.)

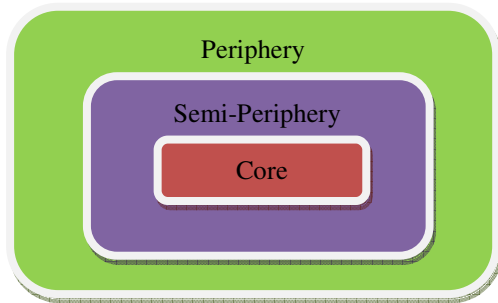
Social networks are also important to the uneven distribution of social, cultural and human capital. Recent research has shown that economic development in the Core economies is not only based on physical capital but also intangible relationships underlying trust, institutions, organisations, and community relations (O'Hara, 2001). Social capital has come to the fore as a crucial element in the development equation, since it is based on bonding and bridging within and between people and social groups. Bonding is important for communication and trust within small groups, but bridging is perhaps more critical in linking various groups together for core objectives. Often these forms of trust and sociality emerge within and between class, ethnic, gender, national and political groupings and networks.

For instance, historically in the US, the upper class mentoring and learning of subtle etiquette associated with the leading families and educational institutions of Harvard, Yale, Columbia, Stanford, Princeton and Cornell helped to create an elite group of powerful leaders of business and politics. John O'Hara in a whole series of novels, especially *Ten North Frederick* (1955, winner of the National Book Award), detailed the subtle nuances necessary for membership in these groups. In the UK a similar grouping of families was oriented around Cambridge and Oxford. Networks of relationships were linked to culture and knowledge in the protection of vested interests and class prestige. Veblen studied the distribution of power and institutional configuration of an earlier era of capitalism (1890s to 1920s), while C.W. Mills (1940s to 1960s) and later J.K. Galbraith (1950s to 1990s) continued this tradition of scrutinising the relationships between culture and power in the social institutions of capitalism.

In this context, political economy has an important subprinciple of *heterogeneous agents*, wherein there are several layers of roles that impinge on socioeconomic

and policy processes (O'Hara, 2007a). At the most general level are roles played according to groupings of species, ethnicities, classes and genders. These are the key groupings, but there are several others as well, such as nationalities (linked to ethnicities to some degree), tribes, political alliances, families and interest groups. Within various institutions there are more micro groups such as within the economy there are different gradations of industrialists, bankers, traders, segmented workers, welfare recipients, politicians, civil servants and the unemployed. At a more micro level within the financial system there are layers of borrowers, lenders, speculators, underwriters, financial analysts, brokers, institutions and central bankers. These different roles are crucial to policy theory and practice. Political economy is thus in this wider sense a pragmatic science of provisioning and policy-making, where real people and other species are situated in groups in geopolitical, business, social and ecological environments.<sup>9</sup>

At the global, regional, national and subnational levels, Core–Periphery–Semi-Periphery (CPSP) changes lead to varying margins of disparity between areas, especially between the advanced nations and sub-Saharan Africa, and to a lesser extent Latin America, Middle East, and parts of South Asia. As Figure 6, below, indicates, there are various barriers due to a myriad of forces inhibiting certain areas and nations from moving from one level to another, such as from Periphery to Semi-Periphery and from Semi-Periphery to Core.



**Figure 6:** Model of Core, Periphery, Semi-Periphery (CPSP)

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9. For instance, in the area of class the issue of cultural capital has helped to make the issue more practical and penetrable (Bourdieu, 1986), as class relations are set in an institutional and habitual framework of the reproduction of relationships, objects and commodities; Irish social policy, for instance, has made advances here, despite their current terrible economic situation.



While over several recent decades, numerous nations in East Asia have managed to move from the Periphery towards the Semi-Periphery, eventually (for some nations) moving towards the Core, less success has been made by Sub-Saharan African (SSA) [mostly Peripheral] and Latin American (LA) [Semi-Peripheral and Peripheral] nations. As indicated in Table 1, above, in SSA and LA the 1980s to 1990s were decades of inadequate performance as structural adjustment policies and high US interest rates generated debt crises and deteriorating socioeconomic conditions. AIDS contributed to malaise in SSA throughout the 1990s, while a whole series of financial crises emerged in Latin America in the 1990s and 2000s, and Eastern Europe underwent institutional destruction which set them back by decades in the 1990s.

Recent adjustments to the Human Development Index (HDI) have lessened the apparent degree of the crisis in SSA, but still their GDP levels are the lowest in the world, while their HDI levels are even worse, indicating major insufficiencies of human, organisational and health capital. The Middle East managed respectable growth rates in the 1950s through to the 1970s, while in the 1980s growth rates dived in the light of declining oil prices and other contradictions; the last two decades have seen stable if relatively mediocre rates. The ability of especially Middle Eastern nations to productively invest their oil and economic surpluses has been especially disappointing in many cases, due to the emergence of several authoritarian or partially pre-capitalist Kingdoms subject to many inefficiencies in the production, distribution and exchange of the surplus (O'Hara, 2011b).

Even within continents unevenness prevails, such as in Latin America where the failure of neoliberal governments to stem the tide of bad performance, financial instability and increasing inequality has seen a whole series of successes of leftist or centre-left regimes into the 2000s. Increasing chasms within and between classes and regions led the electorate to experiment with radical proposals, such as social revolution through the mediation of Chavez in Venezuela, and much more moderate programs in Bolivia, Brazil and Chile. These programs have brought to the fore the need to promote the financial interests of the poor to enhance their role in society, to increase prudential regulation of finance to stabilise the economy, and to increase the stock of infrastructure, education and health capitals to enhance social provisioning (Kadmos and O'Hara, 2000). Echoes of Polanyi's double movement reemerge as post-neoliberal regimes increasingly become the norm in the region in an attempt to improve embeddedness.

The real challenge, however, is Sub-Saharan Africa, where problems have seemed irresolvable for some time now. The core problems have been a colonial heritage

where artificial borders, unnatural elites, insufficient public social infrastructure, corruption and ethnic conflicts have proliferated. The colonial masters and their political offspring failed to provide an institutional order for the great mass of people. Power was held in the hands of colonial classes even after independence, and few successful transfers of power have occurred (Mensah, 1997). Brain drain has played a crucial role in this equation (Ghosh and Ghosh, 2001). Some apparent successes, such as Botswana and to a lesser extent Mozambique and Uganda, look promising in GDP growth terms, but their HDI demonstrate inadequacies. Problem nations, such as Zimbabwe, seem caught in a contradiction between the need for land reform and the minimal productiveness of the present mostly white property magnates. For SSA the millennium development goals seem appropriate yet impossibly difficult to achieve, despite some progress in performance during the 2000s.

Perhaps the greatest challenge of uneven development is environmental. As the major climate change reports noticed (e.g. UNDP, 2007; IPCC, 2007), the prime contradiction affecting the world is that the major GHG generators will be minimally affected while those generating least GHG emissions are majorly impacted by climate change. This will likely exacerbate uneven global development by reducing agricultural productivity, income and health in the Periphery and Semi-Periphery, while perhaps minimally promoting it in the Core. Climate change is predicted to impact majorly on tropical and subtropical areas (mostly underdeveloped nations) and minimally on temperate and colder regions (mostly developed nations). The reasons for this are closely associated with the disembedded economy; firstly, the pattern of anomalous climate processes at play in tropical and subtropical regions and, secondly, the relative inability of underdeveloped nations to cope with the rising temperatures and sea levels and declining rainfall. The major difficulty in constructing a viable new environmental regime is that there are structural linkages between the differential impacts of climate change between Core, Semi-Periphery and Periphery, which are ignored in the official reports. In short, the costs of climate change in the Periphery are closely linked to the lower costs in the Core due to the structure of production and trade between the regions (O'Hara, 2009c).

These issues reinforce the *subprinciple of recognised interdependence and responsibility*, namely that political economies should be evaluated, at least in part, on the extent to which heterogeneous agents, groupings, institutions and nations are able to place their own position in a wider framework, including the World, continental, national, subnational, community, suburban and household levels (depending on the problem at hand and given the limited capacities of the human brain). This is crucial to governance and represents a thoroughgoing

critique of the tendency in many policy structures and theories to emphasise the purely national economy or the national interest, and by other agents, institutions and groupings to emphasise their own personal or collective interests. All classes and segments have a responsibility not only to their own livelihood but also to that of other people, institutions, groupings and species in a wider equation of goodwill, good governance and the common good.

## **Conclusion**

The purpose of this paper has been to present some salient features of a political economy view of governance, by applying some core principles of political economy to contemporary issues of policy. This has never *specifically* been attempted before, despite the revival of political economy over the past several decades. We started by recognising the centrality of the principle of the disembedded economy to political economy governance. Recognising the need to balance various markets with governments, civil society groups and other potentially embedding agents in the double movement helps to explain waves of governance/performance and different policy prescriptions.

The principle of contradiction includes the disembedded economy as well as a series of related processes affecting socioeconomic performance. The degree of conflict and cooperation between capital and labor, monopoly and competition, industry and finance, and ecological capital versus durable fixed capital, help to understand some of the most important problems of our day. The principle of circular and cumulative causation helps to comprehend the complexity of socioeconomic problems as well as the multifarious sources of governance required for stability and provisioning. Lastly, the principle of uneven development emphasises that converging tendencies must be linked with diverging trends on the global, regional and local levels. Uneven development is critical to the differential performance of nations and regions as well as the climate change problem that is besetting the world.

Political economy has acquired a sophisticated yet subtle edifice of theory and policy-making that can assist citizens and institutions in improving the state of the world. It is a broad science dedicated to generating socioeconomic stability and ultimately provisioning for the common people, but also for stimulating innovation and knowledge that generates solutions to complex problems such as climate change and financial instability. The core general principles are central to understanding governance in the contemporary environment, and for activating policy measures into the future. Indeed, without them the process of provisioning

for the people of the world and the ecological environment are both likely to suffer as a result.

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