The IMF, the Eurozone and Global Financial Crises, and the Politics of Economic Ideas

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The core European economic policy debates of the last decade, and probably the next, surrounds the wisdom or otherwise fiscal consolidation and other austerity policies, pursued in response to higher public debt and credibility concerns sparked by the Global Financial and Eurozone crises. *The IMF and the Politics of Austerity* charts how the IMF fed into those debates, promoting one prominent set of diagnostic economic ideas about the crisis, and appropriate responses. In the process, the IMF re-evaluated its understanding of financial markets and their relationship to economic stability, and also re-assessed its understandings fiscal policy efficacy for advanced economies it deemed to have ‘fiscal space’. In this contribution I address a range of issue raised in this symposium about austerity, the IMF, and the politics of economic ideas. For European politics scholars, the IMF warrants closer inspection than it often receives. This, as Lagarde put it, is ‘not your grandmother’s IMF’.[1]

Beyond Neoliberalism

[1] http://freakonomics.com/podcast/not-grandmothers-m-f/

I am most grateful to the symposium participants for such searching, thought-provoking and positive critical engagements with my book. It always fascinates me how seeing the way other people see and read your own work makes one think about it afresh. This seems to be all the more true when one has been ploughing a particular furrow for many years.

Although first and foremost a book about the IMF, *The IMF and the Politics of Austerity* is also a statement of intent about how to go about doing ideationally oriented political economy work. As Hodson notes, the book makes the case that, sometimes at least, it makes sense to go beyond (or at least avoid) the broad-brush terminology of neo-liberalism when talking about evolving economic ideas. This term, despite or perhaps because of its imprecision, exerts a tremendously powerful gravitational pull over political economy scholars. One illustration of this that Ban urges my return to it in his critique!

Neo-liberalism as a terminology and as a means to better understand the IMF, has limitations and can be somewhat analytically debilitating. Describing economic ideas as 'neo-liberal' hinders more that it helps because it does not exclude very much, and does not tell us enough about the content of ideas and their policy corollaries. Drilling down into how the politics of economic ideas plays out in more granular detail, as in my book, demonstrates the value of disaggregating beyond the label 'neo-liberal'. Only the can one reveal the more fine-grained contours of evolutions in economic theorising, as well as in IMF policy thinking and practice.

As one digs deeper, one finds a wide range of economic insights in play within this 'neoliberal' institution - including and heterodox elements. There are also complex processes of translation from the underlying doctrinal positions and assumptive foundations, at a high level of abstraction and generality, to their operationalization through particular methods and economic models, and more concrete policy-oriented concepts. None of these important processes are likely to be the focus of attention if one has already resorted to the shorthand of neoliberalism. Conversely, in terms of research practice, side-stepping ‘neo-liberalism’ can open the door to mapping the contours of economic thinking more accurately, using as source material schools of thought in economics. This yields more analytical traction and explanatory purchase over how IMF thinking evolves (see also Chwieroth 2007, 2010). As Hodson puts it in his contribution to this symposium, one payoff of these schools of economic thought is that ‘they map onto the work of specific economists and the views expressed by IMF staff in an altogether more straightforward way than neo-liberalism ever could’ (2018).

Casual allusions to ‘dominant economic orthodoxy’, like those to ‘neoliberalism’, tend to assume doctrinal singularity and homogeneity. The breadth a variety of ideas in play can be overlooked. In fact, almost diametrically opposing views of fiscal policy can be found within the mainstream of ‘New Consensus’ macroeconomics. This breadth, along a wide continuum, of fiscal policy approaches reconcilable to ‘mainstream economic thinking’ means there is no one single ‘lesson from economics’ for policy that policy elites can imbibe. Rather, there is a range of respectable academic economic opinion – a fact that can get overlooked when talking in broad-brush terms about neoliberalism.

The IMF and the Politics of Austerity charts how this breadth and scope within New Consensus Macro was used by IMF ‘bricoleurs’ in the wake of the Global Financial Crisis (GFC) to rehabilitate a positive view towards counter-cyclical fiscal policy as both a crisis-management and a stabilisation tool. For those advanced economies who enjoy fiscal space, the Fund’s repeatedly underscored central insight is how much *more* effective fiscal policy can be under recessionary conditions, where monetary policy is constrained by the zero lower bound. This is particularly so in recessions that follow financial crisis.

But as Ban's contribution to this symposium points out, only a minority of mainstream NCM economists saw the need for or merits of a rethink of models and assumptions on the scale the Fund piloted. The leading macroeconomics journals continue to reproduce what Ban calls 'work with orthodox rational expectations-based models designed as if there had been no crisis'. Many remain in thrall to the same esoteric and somewhat unrealistic 'representative agent with rational expectations' (RARE) underpinnings, derived from New Classical economics, which had formed the assumptive foundations of mainstream econometric modelling in the decade before the crash. Ban puts his finger on the relative autonomy, perhaps even marginality, of the Fund from the centre of gravity of conventional New Consensus economics thinking. This throws into sharper relief both the intellectual work done by Fund economists to bolster their new thinking, and the fact that the Fund has not brought the majority of economists along with them to its more heterodox views.

Indeed, within that continuum of 'mainstream' economic thought, the Fund occupies a somewhat liminal space on issues of macroeconomic stabilisation which tests its credentials as a font of scientific economic policy wisdom. That the Fund's position in the vanguard of a rethink has not been widely taken up within the economics profession perhaps pushes the limits of its intellectual authority which is so crucial for the institution to gain 'traction' in international economic policy debates. If the Fund does have fellow travellers on the road to revising the premises of its models to make them more relevant for post-GFC policy analysis, they are more likely found in central banks than academic economics. Central banks, given their operational remit, constitute a more fruitful hunting ground than some parts of academic economics for the corroboration and authoritative recognition which are so important to new Fund economic ideas gaining ground. Blanchard himself has recognised this difference and distance in modelling ambitions between academic and policy oriented research (2018: 48). Yet how far the Fund is prepared to follow the Bank of England down a path towards accepting the limits of scientifically managing the economy? Could the IMF also embrace different 'rationalities of governance' (Thompson 2017), auguring reduced reliance on and proximity to academic macroeconomics? This seems unlikely, but this is a research proposal waiting to be written.

<u>Policy Paradigms – and Bricolage</u>

In the background of most political economy studies dealing with economic ideas is a notion of ideational change understood in paradigmatic terms (Hall 1993). The book was not written as a critique of the policy paradigm approach, but the more I learned about the Fund, the less helpful a standard paradigm framework proved for understanding its evolutions. The research findings do not indicate ideational change to be anything like so cut and dried as a paradigm shift, nor did paradigm maintenance adequately capture what was going on. Symposium contributors have found the mechanisms of ideational change I delineated useful. Approaching the politics of economic ideas through this lens offers a route out of a paradigm change world-view. They point to the fact that there are kinds of ideational change in economic thinking other than paradigm shift that are important and interesting. For example, it is not the case that the post-GFC IMF advocates a different approach to fiscal policy for all countries at all times under all conditions. The Fund is not looking for a new fiscal policy template. What we are faced with instead is a granular but significant transformation of the centre of gravity of fiscal policy thinking, whose pace and degree can vary – notably according to nationally differentiated assessments of fiscal space.

Ban invites us to see the IMF's evolution as 'translation of the old neoliberal paradigm into a new, revisionist, neoliberal fiscal paradigm'. Leaving to one side the need to know much more about this 'translation' process, such a characterisation – where the pre-crash and post-crash Fund reside comfortably within the same paradigm – pushes beyond the limits of where saying the two positions fall within the same paradigm tells us very much. At the fulcrum of the paradigm framework is a worldview. The IMF shifted from a pre-crash view which accepted, broadly speaking, Ricardian equivalence to a post-crash position where it rejects it. Those are two incommensurable worldviews and fundamentally different understandings of the economy and policy. If this shift remains within a paradigm with the same label, then the concept risks being stretched in ways which limit its analytical purchase.

Contra a paradigm approach, a multiplicity of views are built into the Fund's knowledge bank, standard operating procedures, and policy frameworks, drawn from different paradigmatic homes. A repertoire of acceptable, respectable economic ideas are 'in play' within the Fund, and which come to the fore depends in part on economic conjuncture, and upon who is the recipient of the policy advice, amongst other factors. This tells against the standard paradigm change story fitting the facts in this instance. This broad church of economic thinking – its contours, its policy corollaries – is revealed by the above research practice identifying a range of schools of economic thought and their subcultures of adherents within the Fund.

These characteristics if IMF economic ideas are why bricolage proves so persuasive a concept in this case. Yet it does not commit us, as Hodson fears, to ad hocery where anything goes. Far from it. The need to secure the Fund's reputation, sustain intellectual credibility with its audience, and the importance attached to the coherence of its economic policy message place limits on which ideas the Fund will incorporate, and how. Constructivist Institutionalist analysis of the kind developed in my book is alive to ideational path dependency dynamics. Pre-existing Fund thinking, broadly rooted in the Keynesian/Neo-classical synthesis which underpinned the Fund's financial programming techniques of the 1950s and 1960s, continues to be an important foundation of Fund work today. The Fund's economic policy thinking and recommendation largely remained consistent a short-term Keynesian, long-term neo-classical dichotomy (see e.g. Stockhammer 2011; Romer 1993). This somewhat anachronistic amalgam still forms the bedrock of Fund economic thinking – providing an intellectual anchor to which new ideas must be reconciled.

Nevertheless, as noted by Hodson, the theoretical eclecticism in evidence can require Fund economists to reckon with some contradictions in their thinking. This is one of the most fascinating questions, and spurs to further research, provoked by my findings. Reading inordinate numbers of Fund working papers and flagship publications, and conducting lengthy searching interviews with many Fund economists, all of which were integral to the research process underpinning my book, one is struck that there does seem to be a degree of cognitive dissonance with which IMF economists can work. The Fund incorporates multiple modes of thinking about economic policy, different and even incommensurable understandings of the economy, not only in organisation as a whole but also in one staff economists' head. IMF economists appear comfortable operating with different and even incompatible economic world-views depending on the policy issue and economic conjuncture.

Different Staff economists, depending on training, pre-disposition and experience, will have allegiances to or sympathy with different positions on the above spectrum of respectable economic thinking. Acknowledging the repertoire of IMF ideas, from a range of schools of thought, brings to the fore the *political* role played by the Fund and other actors seeking to shape understandings of sound economic policy conduct. Whilst presenting their line in technocratic terms, the positioning on fiscal policy amounts to a normatively-informed judgement call and a political decision.

In part, the contradictions derived from theoretical eclecticism are dealt with through the mantra of 'when the facts change…', which IMF staff see themselves as guided by. The institution puts very significant resources behind learning the lessons of perceived past mistakes. There is a self-reflexive dimension to Fund thinking and speaking – a self-conscious desire to demonstrate learning. The IMF's Independent Evaluation Office reports have offered some trenchant auto-critique of Fund conduct, both during the East Asian crisis and during the Global Financial crisis. This feeds into internal organisational procedures. For example, Strategy Policy and Review department, what Momani's interviewee memorably terms the Fund 'thought police' (2005:182), in exercising its oversight over and sign-off on all Fund intellectual production, looks for this evidence of learning from past practice. This has been one sources of a slightly more diverse set of economic ideas and pre-dispositions that have been incorporated into the 21st Century Fund.

The contradictions presented by amalgamating divergent economic views become more acute when we consider the ideological underpinnings of all economic analysis. Yet economics as a profession and discipline tends to gloss over its ideological underpinnings beneath a scientific veneer. In a way that reveals what Chwieroth has called the 'productive power of economics' (2010: 33), it is part of the Fund's scientific culture to do likewise. This shaping role of economics informs, as Barnett and Duvall put it, why 'certain "problems" come to be constructed' in the way they are, and why particular bodies of knowledge are 'authorized or legitimated in the construction of those problems' (Barnett & Duvall 2005: 21-22). The IMF narrates its own ideational evolution in terms of practical, pragmatic, policy-oriented 'clinical' economists operating in a Bayesian world of rational updating of their economic ideas in the light of new evidence. Yet this overlooks the fact that economic ideas are always rooted in ideological assumptions about how the economy and policy work.

New information and evidence, presented by the Lehman crash and the Great Recession, has been one source of the fiscal policy shift. Yet what separates the 'expansionary fiscal contraction' position decisively rejected by the Fund from its post-crash view positing high fiscal multipliers is, at root, *a priori* normative pre-suppositions rooted in the principles of political economy. These have divided political economists down the centuries: pre-dispositions regarding fiscal policy efficacy and whether the state can and should intervene in the economy to improve the growth. This is uncomfortable territory for a Fund keen to assert its intellectual authority as a source of scientific, technocratic wisdom on economic policy, and to retain a non-political character removed from such ideological considerations.

Technocracy and Politics

Moschella, in her contribution, puts her finger on the 'complicated dilemmas that the Fund is required to navigate by virtue of its institutional design at the intersection of technocracy and politics'. This should become a wider research programme for European and international politics, extending beyond the IMF to explore similar dynamics amongst financial regulators, central bankers and others. Whilst Fund commentary is cloaked in scientific and technocratic parlance, how economic theory is invoked in economic policy recommendation, by the IMF as by anyone else, is inherently political. The politics of economic ideas pervades what is a selection and framing exercise, choosing which ideas and insights to draw on, which methods to use, and what balance of prioritisation to strike. As one recent study of IMF surveillance put it, 'methodological practices should be examined as a process wherein the illusion of distance between the technical and political is constructed and maintained'. For all the Fund's 'heavy reliance on claims of technical and apolitical authority and expertise' in its surveillance practices and positions have an inevitably political character (Robles 2018: 227).

As Johnston notes, apparently small policy details within economic evaluation – such as size of fiscal multipliers, or the use structural as opposed to nominal measures, can be of cardinal importance in terms of their policy implications and ramifications. These seemingly technical issues can be of huge political economic significance. In order to explore the dilemmas of this fascinating intersection between technocracy and politics, the next wave of political economy work on the Fund and other international economic institutions needs to learn more about the politics of economic methodology (See e.g. Robles 2018; Yarrow 2018).

The Fund's influence rests on its mandate, reputation and track record as a technocratic, scientific source of reputable economic policy wisdom. These scientific and technocratic credentials are crucial for the Fund to retain its political power as it plays the role trying to prick the conscience of what it sees as misguided economic policy-makers. Yet the Fund, including in its methodological choices, and especially in the *selection* of *which* economic ideas and insights are afforded primacy, makes normatively driven interventions in economic policy debates. Sailing close to wind, and risking letting its technocratic apolitical façade slip, the IMF may occasionally enjoy scope to shape and shift the boundaries of what constitutes 'legitimate' policy. This was what the Fund sought to do in the European politics of austerity debate, where the Fund took on the how far? How fast? to pursue fiscal consolidation issue. It is also true of the Fund agenda on tackling inequality.

The horns of another dilemma around technocracy and politics faced by the Fund were revealed in the maelstrom of the GFC. The Fund arguably achieved most 'traction' when it did *not* observe its normal bureaucratic standard operating procedures and scientific norms of internal approval. Strauss-Kahn and Blanchard, at the G20 in November 2008, undertook a back of the envelope assessment of the size of fiscal stimulus that would be politically acceptable to fiscal conservatives, whilst being on a scale sufficient to meet the economic need. The timeliness of the intervention, and the clarity of the message would not have been possible through regular Fund peer review and sign off processes, wherein caveats and rejoinders are attached which can dilute the policy line.

This moment – the Fund's high profile call for a 2% global fiscal stimulus – was key in demonstrating the institution's relevance and helped save its skin. The substantial increase of Fund financial resources from member states, which meant that internal staff cutbacks could be ceased and reversed, followed soon after. Yet this was a judgement call that went through none of the normal internal peer review and sign-off processes which reinforce the institution's scientific norms. It was experienced as a surprise, perhaps even an unwelcome one, by many Fund insiders. In hindsight, most recognised Strauss-Kahn as playing a pivotal role in reviving the Fund's fortunes, as well as in the management of the crisis. Yet this was achieved by departure from how the Fund normally gets done. When the next big crisis hits, will the IMF leadership be able to think outside the box and act swiftly as Strauss-Kahn effectively did?

<u>Fund/Member State Interactions: Traction and Inter-Elite Persuasion</u>

There are, of course, different ways to understand the Fund as a 'political' organisation. One much travelled road is the Fund's relations with its powerful members. Did member states lead and did the Fund follow? The intellectual leadership, and outlier status within mainstream economics, of the IMF's post-crash thinking discussed above tells against the Fund as follower narrative. The Fund's Research Department in particular was in the vanguard of new research on post-crash fiscal policy. More fundamentally, though, it is not clear that the IMF and its member states are as ontologically separable as posing the question in that way implies. The protagonists are all engaged the same economic policy debate. They are part of the same economic policy elite, with revolving recruitment doors and innumerable secondments between national economic policy authorities and the Fund.

Fund relations with its powerful members are, to my mind, best understood as process of attempted 'inter-elite persuasion' (Blyth RIPE 2007). The IMF seeks, as Johnston notes in her contribution to this symposium, to 'change minds behind the scenes' partly by 'finding allies in (national) elite circles that shared similar views on the crisis and how it should be managed.' The Fund can open up policy space for advanced economy policy-elites seeking to bolster growth using macroeconomic policy in ways which retain the Fund's seal of approval as 'sound policy'. Senior Fund members were able, in the wake of the Lehman crash, to 'play onside' Keynesian thinking about fiscal policy. This was partly because it could count on like-minded elites in key capitals to help facilitate the international economic coordination of fiscal stimulus.

The success of the Fund persuasive efforts is intermittent, and often partial – one contribution of *The IMF and the Politics of Austerity,* as contributors here have recognised, it to establish the limits of Fund success, and the conditions of possibility for it. There have been 'victories' including persuading the Commission to accept a slower path towards fiscal adjustment in the context of softening the application of stability and growth pact fiscal targets from 2012 onwards. Not all the avenues the Fund sought to open up were taken up – a notable example being its expansive conception of Banking Union, and the large and more powerful public fiscal backstops the Fund urged upon the EU in the context of the Eurozone crisis. Unstinting hostility to these ideas from Germany in particular put paid to these aspirations. The ways in which the IMF was unsuccessful is a research finding in itself – generative of fresh insights into European, comparative and international political economy.

The IMF and EU Institutions

Hodson's critique that the book does not apply the framework equally to all international organisations within the ambit of the books' focus is well taken. Key institutional factors affecting EU and Eurozone crisis responses are indeed not the main focus of the analysis. Whilst I do note some differentiation and evolution amongst thinking in EU institutions, and delineate differing views of EU governments (differentiating between French and German positions in particular). It would indeed be fruitful to explore EU institutions and actors more systematically through the lens of the book's framework.

The European Stability Mechanism (ESM), as Ban highlights, is a key player in Eurozone crisis resolution, and it perhaps deserved more attention. The ESM developed as the crisis unfolded, often behind the scenes. As Erce has noted (2015), the ESM is the means by which European authorities have been able to take a softer stance towards fiscal and macroeconomic adjustment (through e.g. legthening debt maturities) than comes across in the headline grabbing hawkish discourses of the likes of Trichet, Merkel and Schauble over the last decade. As the ESM took shape the Fund, perhaps underestimating the 'local competition' threat it posed, envisaged a role for it countering the growth sapping and austerity-oriented proclivities of other parts of the EU economic governance landscape. The dynamics of this kind of inter-institutional completion in European crisis management is another research proposal waiting to be written.

The prospects of the Fund exiting the European crisis programmes landscape, envisaged as a feature of Lagarde's second term as Managing director of the IMF, result primarily from the frictions within the Troika over debt restructuring as the Fund defines it. The IMF remains convinced that up front debt restructuring, rather than on the quiet and through the back door, remains a necessary component of European recovery. The Fund's potential withdrawal from European programmes is also, however, a ceding of ground to the 'local competition' from the ESM highlighted by Ban. The same recognition of the IMF's limits may be part of the explanation behind the IMF's positive view of prospective initiatives like the European Monetary Fund championed by Macron and Juncker. Perhaps, as a result of the painful compromises and the discomfiture of the IMF's Troika experience, and frustrations at the limits of the traction it has been able to gain over European policy thinking and policy developments more widely, we may be at the end of an era of the IMF's mission creep into attempting hands-on management of the European political economy.

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