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Punctuated Equilibrium or the Orthodox Cycle? Change and Continuity in UK Macroeconomic Policymaking

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Abstract

This thesis provides a study of United Kingdom (UK) macroeconomic policy and economic ideas. Specifically, the thesis seeks to explore the reasons when and why UK macroeconomic policy and economic ideas exhibits change or continuity. The central contention of this thesis is that the model of punctuated equilibrium provides a flawed understanding and explanation of when and why policies and idea exhibit continuity and change in UK macroeconomic policymaking. In particular, the thesis seeks to fill two gaps in our existing knowledge of UK economic policymaking, which emerge from critical literature reviews. The first gap pertains to the need for greater specificity in our understanding and definition of orthodox UK macroeconomic policy. The second gap relates to the need for a superior understanding of when and why UK macroeconomic policy and economic ideas exhibits change and continuity.

The original contribution of this thesis to the literature on UK economic policymaking arises from the two research findings generated in Chapters Three and Four, which are then tested in a series of case-study chapters in the second half of the thesis. The first research finding is the provision of greater precision in our understanding and definition of orthodox macroeconomic policy. The second research finding is the identification of a historical pattern in UK macroeconomic policymaking, which is named the orthodox cycle. The orthodox cycle utilises the new understanding and definition of orthodox macroeconomic policy to show the continuity of orthodox policy and ideas in UK macroeconomic policymaking, through a series of distinct phases, in the aftermath of crises and changes in government.

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Chapter 1

Introduction

This thesis provides a study of United Kingdom (UK) macroeconomic policy and economic ideas. Specifically, the thesis seeks to explore the reasons when and why UK macroeconomic policy and economic ideas exhibits change or continuity. The central contention of this thesis is that the model of punctuated equilibrium provides a flawed understanding and explanation of when and why policies and idea exhibit change and continuity in UK macroeconomic policymaking. In particular, the thesis seeks to fill two gaps in our existing knowledge of UK economic policymaking, which emerge from critical literature reviews. The first gap pertains to the need for greater specificity in our understanding and definition of orthodox UK macroeconomic policy. The second gap relates to the need for a superior understanding of when and why UK macroeconomic policy and economic ideas exhibits change and continuity. In order to address these limitations in our current comprehension of UK economic policymaking and to make an original contribution to the literature, the thesis has two aims and two objectives.

The first aim is to acknowledge that policy scholars and political economists often explain radical change in UK economic policy and economic ideas through the model of punctuated equilibrium. The second aim is to demonstrate that punctuated equilibrium presents a misleading explanation of when and why UK macroeconomic policy and ideas change. The first objective is to develop a new and more precise understanding and definition of orthodox UK macroeconomic policy. The second objective is to construct a new conceptual framework of UK macroeconomic

policymaking, which provides a superior understanding of when and why macroeconomic policy exhibits change or continuity.

The first half of the thesis presents a series of critical literature reviews and historiography of UK economic policymaking in response to major economic crises in the Twentieth century. The opening chapters of the thesis recognise that policy scholars and political economists often explain radical change in UK economic policy and economic ideas through the model of punctuated equilibrium. Accordingly, radical policy and ideational change in UK economic policymaking is often conceived of as a discontinuous process caused by exogenous or endogenous shocks to the policymaking process. Exogenous shocks are conceptualised as economic or financial crises, war or natural disasters. Meanwhile, endogenous shocks include events such as a change in government. The historiography in Chapters Three and Four provides the first demonstration in the thesis that punctuated equilibrium presents a misleading explanation of when and why UK macroeconomic policy and ideas change.

The second half of the thesis presents a series of case-studies of change and continuity in UK macroeconomic policymaking from the 2nd May 1997 to the 13th July 2016, which begins with the election of Tony Blair, Prime Minister (1997-2007), and ends with the resignation of David Cameron, Prime Minister (2010-2016), in the aftermath of the UK referendum vote on leaving the European Union. The breadth of these case-studies of UK macroeconomic policymaking includes periods in government for the three historic major British political parties of the Conservatives, Labour and Liberal Democrats and the Global Financial Crisis of 2007-2009, which was the first major economic crisis of the Twenty-First century.

Summary of Research Findings

The original contribution of this thesis to the literature on UK economic policymaking arises from the two research findings generated in Chapters Three and

Four, which are then tested in the case-study chapters in the second half of the thesis. The first research finding is the provision of greater precision in our understanding and definition of orthodox macroeconomic policy. The second research finding is the identification of a historical pattern in UK macroeconomic policymaking, which is named the orthodox cycle. The orthodox cycle utilises the new understanding and definition of orthodox macroeconomic policy to show the continuity of orthodox policy and ideas in UK macroeconomic policymaking through a series of distinct phases in the aftermath of crises and changes in government. Thus, the orthodox cycle exposes the flaws in punctuated equilibrium and seeks to provide a superior understanding of the reasons for continuity and change in UK macroeconomic policymaking. This thesis concludes that the orthodox cycle does provide a superior understanding of when and why continuity and change occurs in UK macroeconomic policy and economic ideas. The need for a future research agenda is also discussed in the conclusion and at various junctures throughout the thesis.

Thesis Organisation

Chapter Two reviews the literature of different theoretical models of public and economic policymaking. The chapter demonstrates that punctuated equilibrium is often invoked by policy scholars to explain that radical policy and ideational change in UK economic policymaking occurs as a discontinuous process in reaction to exogenous and endogenous shocks such as economic crises or changes in government. However, the chapter identifies that this explanation of policy change is problematic. For instance, policy scholars in recent years have begun to question the relationship between economic crises and radical policy and ideational change. Thus, Chapter Two identifies a gap in our current knowledge of UK economic policymaking for a superior understanding of when and why UK economic policy and ideas exhibit change or continuity.

Chapter Three reviews the literature and provides a historiography of UK economic policymaking and economic performance between November 1918 and December 1934. The sections of this chapter, which provide a critical literature review, identify two gaps in our knowledge of UK economic policymaking. The first gap in our knowledge relates to the need for greater clarity in our understanding and definition of orthodox UK macroeconomic policy. The second gap in our knowledge is identified more narrowly than in Chapter Two as the need for greater comprehension of the reasons for when and why change and continuity occurs in UK macroeconomic policy and economic ideas.

The historiography in Chapter Three supports the central contention of the thesis that existing literature, which explains radical policy and ideational change in UK macroeconomic policymaking via the theoretical model of punctuated equilibrium, are flawed. Indeed, the historiography in Chapter Three presents analysis that demonstrates punctuated equilibrium provides a misleading explanation of when and why UK macroeconomic policy exhibits change or continuity. Furthermore, Chapter Three generates two research findings, which seek to fill the gaps in our existing comprehension of UK economic policymaking. First, a new understanding and definition of orthodox UK macroeconomic policy is advanced. Second, a historical pattern is identified in UK macroeconomic policymaking whereby, rather than radical policy and ideational change in the aftermath of economic crises, continuity of orthodox macroeconomic policy is evident through a series of distinct phases.

Chapter Four reviews the literature and provides a historiography of UK economic policymaking and economic performance between April 1975 and April 1997. The critical literature reviews in this chapter identify the same two gaps in our knowledge of UK economic policymaking as those acknowledged in Chapter Three. Furthermore, the historiography in Chapter Four supports the central contention of the thesis that existing literature, which explains UK economic policy change by reference to punctuated equilibrium, is flawed. Indeed, rather than the radical policy and ideational change that is usually assigned to the myriad of exogenous shocks and endogenous shocks of the 1970s, Chapter Four finds continuity of orthodox

macroeconomic policy and ideas in this period. Thus, the historiography in Chapter Four strengthens the two research findings of the previous chapter, which fill the gaps in our existing comprehension of UK economic policymaking and provide an original contribution to our knowledge.

Chapter Five provides an outline of the methodology adopted by this thesis and specifies the research question, which subsequent case-study chapters will answer. The chapter begins by setting out the two research findings from the historiography in Chapters Three and Four. The chapter then establishes the methodology and methods of the thesis, which includes discussion of inductive reasoning, research design, data collection and data analysis. The chapter also explains why the discussion of methodology has been placed at this juncture of the thesis structure.

Chapter Six provides a case-study of UK macroeconomic policymaking from the 1st May 1997 to the 6th June 2001, which witnessed the end of eighteen years of Conservative government and the election of New Labour. The purpose of the case-study is to see whether the orthodox cycle provides a superior understanding and explanation of change and continuity in UK macroeconomic policy than that furnished by punctuated equilibrium. The chapter draws two conclusions. First, the orthodox cycle allows us to locate a significant event, which initiated an orthodoxy phase in UK macroeconomic policymaking. Second, the orthodox cycle enables us to identify that the new institutional framework for macroeconomic policymaking created after the election of New Labour, rather than leading to radical change in policy and ideas, served to institutionalise orthodox macroeconomic policy in the policymaking process. Consequently, the 1997-2001 Parliament saw a return to the full framework of orthodox macroeconomic policy, which accords to what we should expect in the orthodoxy phase of the orthodox cycle.

Chapter Seven provides a case-study of United Kingdom (UK) macroeconomic policymaking from the 7th June 2001 to the 26th June 2007, which encompasses a period that begins with the victory of New Labour at the 2001 general election and ends with Tony Blair's resignation as Prime Minister at a specially

convened Labour Party Conference. The purpose of the case-study is to see whether the orthodox cycle provides a superior understanding and explanation of change and continuity in UK macroeconomic policy than that furnished by punctuated equilibrium. The chapter draws two conclusions. First, in terms of monetary policymaking, the superiority of the orthodox cycle in this case-study arises from the identification of continuity in orthodox monetary policy rather than continuity in the new radical policy equilibrium expected by punctuated equilibrium after the election of New Labour on the 1st May 1997. Second, neither the orthodox cycle nor punctuated equilibrium can explain the change in fiscal policy that occurred at the 2002 Budget.

Chapter Eight provides a case-study of United Kingdom (UK) macroeconomic policy during the government of Gordon Brown, Prime Minister (2007-2010), from the 27th June 2007 to the 5th May 2010 and the Global Financial Crisis of 2007-2009. The purpose of this case-study is to see whether the orthodox cycle provides a superior understanding and explanation of change and continuity in UK macroeconomic policy than that furnished by punctuated equilibrium. The chapter draws four conclusions. First, the orthodox cycle provides exactitude in the initiation of a crisis phase. Second, the orthodox cycle explains that the Global Financial Crisis did not lead to radical and permanent monetary policy change as expected by punctuated equilibrium, but rather the continuity of orthodox monetary policy as monetary policymaking entered a consolidation phase of the orthodox cycle. Third, change in fiscal policy and economic ideas did occur in response to the Global Financial Crisis. However, the orthodox cycle explains that, rather than leading to new policy equilibrium, change occurred only temporarily. Fourth, fiscal policy reverted back towards orthodoxy before the 2010 general election when fiscal policymaking entered the consolidation phase of the orthodox cycle at the 2009 Pre-Budget Statement.

Chapter Nine provides a case-study of UK macroeconomic policy during the David Cameron, Prime Minister (2010-2016), and Nick Clegg, Deputy Prime Minister (2010-2015) government of the 12th May 2010 to the 7th May 2015 and the Cameron government from the 8th May 2015 to the 13th July 2016. The purpose of

the case-study is to see whether the orthodox cycle provides a superior understanding and explanation of change and continuity in UK macroeconomic policy than that furnished by punctuated equilibrium. The chapter draws two conclusions. First, the orthodox cycle explains that the Global Financial Crisis and the formation of the Cameron-Clegg government did not lead to radical monetary policy change, but rather to the continuity of orthodox monetary policy as monetary policymaking remained in the consolidation phase. Second, the orthodox cycle expounds that the Global Financial Crisis and the formation of the Cameron-Clegg government did not lead to radical fiscal policy change. Instead, it led to the continuity of orthodox fiscal policy as George Osborne, Chancellor of the Exchequer (2010-2016), and the Treasury initiated the orthodoxy phase of the orthodox cycle at the 'Emergency' Budget of the 22nd June 2010. Chapter Ten provides a conclusion and discussion of a future research agenda.

Chapter 2

Understanding Why Policies Change in Models of Public and Economic Policymaking

Introduction

This chapter reviews the literature on models of public and economic policymaking. In particular, it examines how they understand the process through which policy decisions are formulated and implemented, when and why policies change and how interests influence policy outcomes. The chapter acknowledges the contribution made by punctuated equilibrium to studies of UK economic policymaking and its explanation of radical policy change as a discontinuous process that occurs in reaction to exogenous or endogenous shocks. Ultimately, however, this account of policy change is found to be problematic in the context of contemporary UK economic policymaking. Specifically, this chapter will identify that policy scholars, in light of the recent Global Financial Crisis, have begun to question the relationship between economic crises and radical policy and ideational change. Indeed, as subsequent chapters will demonstrate, the model of punctuated equilibrium presents a misleading explanation of when and why UK macroeconomic policy exhibits change or continuity since 1914.

This chapter will be organised as follows. The next section provides a definition of key terms before going on to discuss the various models of public and economic policymaking. This chapter pays initial attention to the models of incrementalism and punctuated equilibrium, which provide explanations of when and why policies exhibit change or continuity, before proceeding to introduce and

evaluate leading models of public and economic policymaking from the rational choice, pluralism, elite theory and constructivism perspectives. The chapter will argue that these models' reliance on punctuated equilibrium to explain when and why policies change is problematic. Consequently, it is the problems associated with punctuated equilibrium highlighted by contemporary policy scholars, which presents us with a gap in our current knowledge of UK economic policymaking. In particular, for analysis that seeks to provide a superior understanding of when and why change or continuity occurs in economic policy and ideas.

Our Current Understanding of Public Policy

This chapter begins with a discussion of our contemporary understanding of public policy studies within the field of political science and also discusses the definitions of key terms and words. Hill (2014:4-6) contends that studies of public policy can be structured into two broad categories that provide either an analysis *for* policy or analysis *of* policy. Here, analysis *for* policy supplies scrutiny of policy outcomes. Often these works centre on the quality of public policy and contain normative elements, which suggest that alternative policies could have secured superior collective benefits. Thus, they are studies about the ends of the policymaking process. Meanwhile, an analysis *of* policy is centred on the processes by which policy decisions are made and policy outcomes are generated. Consequently, they are studies of the means by which policymaking occurs. In this chapter, our attention will focus solely on the literature that provides analytical contributions to the analysis *of* policy.

A simple definition of public policy study has been provided by Weible and Norhstedt (2013:125) who claim that it is 'the study of public policy over time and the surrounding actors, context and events'. Thus, Smith and Larimer (2013:47) declare that 'at a fundamental level, public policy is the study of decision-making. Public policies... represent choices backed by the coercive power of the state. Who

makes these decisions and why they make the decisions they do have always been important research questions for policy scholars'. Later, Smith and Larimer (2013:73) claim that 'the heart of the study of policy process…. [is] the study of how public policy is made. This includes the means by which problems are identified and brought to the attention of governments as well as how solutions are formulated and decided upon'. They conclude the study of public policy making is the study of political power (Smith & Larimer, 2013:74-75).

The importance of politics to public policy studies, however, sits uneasily with existing English definitions of the terms 'public policy' and 'policy'. For instance, Hill (2014:18) notes the difference between the English definition of the word 'policy' and the French and Italian definitions, which do not make a clear distinction between the words 'policy' and 'politics'. As a consequence, in the English language the 'objective distinction between politics and policy is actually likely to be deeply political in its own right', which is criticised as a 'technocratic illusion [of] rational policy' (Jenkins, 2007:27 cited in Hill,2014:18). This criticism is echoed by Hill (2014:18) who argues that the English definition of 'policy' presupposes a rational policymaking process.

In his linguistic analysis and historiography of existing definitions of the terms 'public policy' and 'policy', Hill (2014:14-18) refuses to provide a specific definition of the words, having noted that no precise or universal definition exists. However, Hill (2014:15-17) does point out several implications of existing definitions, two of which are particularly apposite to our understanding of the political nature of policymaking. First, that 'policy' does not represent just one decision but involves webs of decisions and courses of action, which when taken together comprise a more or less common understanding of what policy is. Second, non-decisions or inaction are equally as important when considering what constitutes 'policy'. Therefore, Smith and Larimer (2013:73) claim that the generally accepted definition of public policy is 'a deliberative action (or non-action) undertaken by government to achieve some desired end'. Consequently, the role of politics is of vital importance to any research pertaining to public policy study because

policymaking 'is essentially a political process… in which there are many actors' (Hill,2014:4).

Models of Public and Economic Policymaking

For many academics, policy change defines modern public policy scholarship (Hogwood & Peters,1983;John,1998;Orion & Steinmo,2010). For example, Capano (2013:451) states that change must be the primary analytical focus of public policy studies because 'change is the normal status of public policy-making, whereas stability is simply contingent upon human agency (through rules, institutions, social norms, ideas etc)'. Consequently, emphasis in this section of the chapter will be placed on how models of public and economic policymaking seek to elucidate when and why policy change occurs. Accordingly, our literature review will start by introducing two models whose central objective is to construct explanations pertaining to policy change.

Incrementalism has its origins in the work of Lindbolm (1959) and contends that instead of being rational, policy makers 'muddle through' policy decisions. Typically, policy makers will address each new problem from the perspective of what has been done in the past rather than seek a fresh solution. Consequently, policy change is characterised by small incremental adjustments to existing policies and incrementalism accepts that 'limitations in... [policymakers] ability to consider all possible policy goals or alternatives lead to a heavy and necessary reliance on past decisions, mental heuristics and institutional rules' (Smith & Larimer, 2013:52).

Consequently, incrementalism is heavily influenced by the concept of bounded rationality, which was developed by Simon (1948) in his work on administrative behaviour in the United States (US). Here, it is claimed that individuals are not comprehensively rational and nor do they make decisions on the basis of complete information, but rather are limited by cognitive and environmental

constraints. Thus, whilst policymakers may intend to act rationally they often compromise and make the best decision they can based on their limited resources. This process involves the reliance of policymakers on cognitive heuristics (shortcuts) when processing information, which means that policymakers often draw upon existing policies when faced with a new problem (Cairney,2013c;Smith & Larimer,2013:47-50). For example, Martin Carstensen (2011) argues that policymakers use of cognitive shortcuts takes the form of bricolage, which results in policymakers combining bits and pieces of existing ideational and institutional legacies in new forms. As a result, contemporary incrementalism literature emphasises that change, which can eventually produce major policy and institutional transformation, occurs on a continuous but incremental basis during periods of economic and political stability. Alternatively, it is periods of instability that produces continuity in policy and institutions (Cappocia & Keleman,2007;Djelic & Quack,2003;Streek & Thelan,2005;Thelen,2003).

Meanwhile, punctuated equilibrium has its origins in the work of Baumgartner and Jones (1993) on US politics, which is inspired by evolutionary theories in biology that suggested evolution of species occurred from short bursts of frenetic change (Gould & Eldridge,1972). Punctuated equilibrium stresses that in periods of stability change in policy, ideas and institutions, if it occurs at all, is likely to occur on an incremental basis. This arises from two impulses in policymaking. First, policymakers lack the time, resources or incentive to produce radical policy solutions. Second, stability in policymaking has allowed a policy monopoly to emerge[1]. Here, established interests benefit from the policy continuity of the status quo, and, thus, have few incentives to seek policy and institutional change. Calls for reform are often offset by minor or superficial policy adjustments and continuity in policy is the norm. Consequently, policy is claimed to be in equilibrium (Cairney,2013).

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[1] Baumgartner and Jones (1993:5-7) and Cairney (2013) consider a policy monopoly to be a policymaking process that has a definable institutional structure, is dominated by a single or group of interests and supported by powerful ideas and images.

In contrast to incrementalism, punctuated equilibrium explains policy, ideational and institutional change as the result of economic and political instability, which, through the introduction of conflict and new actors to the policymaking process, punctuates the previous policy equilibrium. For example, Gofas and Hay (2010:4) note that instability in punctuated equilibrium is commonly conceptualised as an exogenously induced critical juncture. A critical juncture is claimed to consist of 'crisis, ideational change and radical policy change', which occur because crises 'create the environment where change agents contest extant ideas and the policies based upon them' (Donnelly & Hogan,2012:324-325)

Boushey (2013:143) identifies that punctuation to policy equilibrium can also be ascribed to endogenous shocks, which include the election of a new government, change in tone of media coverage or policy entrepreneurs influencing the perception of a policy problem. Meanwhile, exogenous shocks are those that arise from outside of the policymaking process and include wars, natural disasters, economic or financial crises. These shocks are claimed to introduce uncertainty to the policymaking process, galvanise political attention on an issue area and reveal a critical policy problem that requires policy intervention. Consequently, punctuated equilibrium explains policy, ideational and institutional change as a discontinuous process that occurs as a result of exogenous or endogenous shocks to the policymaking process. These changes then form the basis of the next policy equilibrium, which exists until it is punctuated by the next exogenous or endogenous shock.

The chapter will now proceed to introduce and evaluate the stages model, evidence-based policymaking (EBP) and state-centric models of public policymaking, which are based upon the rational choice theory of human agency. Rational choice theory has its origins in the 19th century marginal revolution in the field of political economy associated with Jevons (1971/1965), Walras (1871/1950) and Menger (1874/1954). The marginal revolution and the subsequent development of the field of economics was constructed upon a utilitarian philosophy of human agency, which was cast as revolving around three interlocking propositions. First, individuals have rational preferences amongst outcomes. Second, individuals

maximise utility (firms maximise profit). Third, individuals act on the basis of full and relevant information (Weintraub,1999). Thus, the conceit of the stages model, EBP and state-centric model is that policymakers are considered to behave in accordance with the notions of comprehensive rationality and complete information, which allows them to maximise the benefits of policy to society in much the same way as an individual maximises their own utility (Cairney,2013c).

The stages model of public policy has its origins in the post-Second World War period (Easton,1965). Here, public policy is claimed to move through clear cut and ordered stages (Cairney,2013c), which include agenda-formation, formulation, decision-making, implementation and evaluation. In the stages model, policy makers are cast as neutral technocrats or managers acting within neutral institutions. Consequently, the stimulus for policy change resides in technocrats and experts who, following systematic methods, identify problems and the effective means to solve them (Howlett & Geist, 2013:20).

EBP has its origins in the works of Ancient Greek philosophers such as Aristotle (Ehrenberg,1999; Flyvbjerg,2001). Parsons (2002:45) argues that EBP is predicated on the belief that it is 'possible and desirable to move policy-making out of the realm of muddling through to a new firm ground where policy could be driven by evidence, rather than political ideology and prejudice' and that 'better policy-making [is] predicated on improvements to instrumental rationality' (Ibid:45). Consequently, Sutcliffe and Court (2005:iii) contend that EBP is based on the premise that policy decisions should be better informed by available evidence and should include rational analysis'. Thus, Howlett and Geist (2013:20) purport that EBP assumes that policymakers act 'in the classical rational style' through the application of 'systematic evaluative rationality' to policy problems. As a result, the impetus for policy change arises from the creation and rational evaluation of new knowledge by technocrats.

The state-centric framework of public policy has its contemporary origin in the 1980s and concerted efforts 'to bring the state back in' to political science (Evans et al,1985). The state-centric framework emphasises the power of the state and its

institutions in policymaking, which are claimed to formulate and implement policy according to their own policy preferences. Thus, the state is conceived as acting as an autonomous rational actor with considerable independence from societal pressure (Jarvis,2013). A classic example of the state-centric approach is provided by Krasner (1978) who argued that policymakers implement policy in the pursuit of national interest. Therefore, the state-centric analysis claims that policy change occurs from shifting strategies implemented by elites and technocrats located within the state.

The application of the state-centric model has also been advanced in a UK context via the Westminster model of government. The origin of the Westminster model lay in constitutionalist doctrine advanced in the late nineteenth century (Dicey,1885 cited in Gamble,1990a:405). In the Westminster model of government, policymaking is conducted within the institutions of the UK state, such as the House of Commons, and significant power is invested in individuals through the office of the Prime Minister or Chancellor of the Exchequer. For instance, Cairney (2013b) notes how the Westminster model of government is often used by scholars as an ideal-type of system in which power in public policymaking is centralised in the hands of elites within government and state.

A central criticism of these models of public policy lay in their use of rational choice theory of human agency to understand when and why policies change. For instance, rational choice theory of human agency has been strenuously challenged from a number of different fields including psychology (Kahneman & Taversky,1981;1984), international relations (Van Evra,1984) and within branches of economics, which reject the notion of complete information (Greenwald & Stiglitz,1988;1990). Consequently, Cairney (2013d) concludes that bounded rationality provides a superior understanding of policymakers cognitive abilities because they make important decisions in the face of uncertainty (lack of information), ambiguity (lack of knowledge) and conflict (politics).

Gofas and Hay (2010a:24) have argued, for example, that the notion that individuals have complete information when making decisions is a ‘convenient fiction’ that should be dispensed with. Specifically, because the absence of complete

information means that individuals can never act in a rational manner and nor can they ever really know what their material interests are. Hence, what matters when understanding individual or collective agency is not material interests per se, which is just one of several cognitive filters, but actor's perception of their individual and collective interest, the processes by which they come to construct that perception and how they act on the basis of such perception (Gofas & Hay,2010a:24-26,49-51).

Consequently, Gofas and Hay (2010a:24-26) find a flaw in punctuated equilibrium, particularly, in its explanation of radical change in policy, ideas and institutions as the product of exogenous and endogenous shocks that introduce uncertainty to the policymaking process. Here, the authors claim that this understanding of when and why policy change occurs condemns punctuated equilibrium to the assumption that policy continuity during periods of political and economic stability is predicated upon policymakers acting in the context of complete information. However, if complete information is nothing but a convenient fiction then 'a more consistent and fruitful conceptualisation... construes uncertainty as both a universal human condition and a discursive regime that imposes distinct dispositional logics upon actors. Understood in such terms, the appeal to uncertainty is as much as anything else a political and discursive device in the process of enlisting subjects to alternative visions of change' (Gofas & Hay,2010a:26).

A further problem with the adoption of rationalist theories of human agency by various models of public policymaking is that it leads to an apolitical conception of the process through which policy decisions are formulated and implemented. For instance, a Cabinet Office (Campbell et al,2007) review into UK policymaking, which interviewed members of the UK civil service in various Whitehall departments, found that EBP 'contrasted with the reality of policymaking/delivery, which was described as messy and unpredictable' (Campbell et al,2007:6). Consequently, evidence was found to be just one factor that civil servants took into account when making policy alongside 'political imperative[s] and response to media and world events' (Ibid:6). Thus, Sutcliffe and Court (2005:iii) dismiss EBP because 'policymaking is neither objective nor neutral; it is an inherently political process'. The tension between politics and evidence has also been articulated by Parsons

(2002:57), who acknowledges that within policymaking not all evidence is given equal validity. Consequently, the big questions that proponents of EBP must ask are: whose evidence is being used? And what counts as evidence? At the fundamental level, Parsons (Ibid:57) argues that 'use of the word evidence means whatever… [politicians] want it to mean'.

These criticisms of the apolitical nature of models of public and economic policymaking based on a rational theory of human agency also correspond with criticism directed at the stages model concerning its ordered, legalistic and technocratic view of the public policy making process (Sabatier,1990:7). Indeed, the stages model is criticised for excluding investigation of the number, type and motivation of actors involved in the process of formulating policy (Howlett & Geist,2013:17). Consequently, the stages model is claimed to advance 'a potentially distorting framework' because it suggests an understanding of 'policy processes... which might only apply to a new annexed Desert Island where nothing had been done before' (Hill,2013:143).

The same apolitical criticism can also be ascribed to the state-centric model of public and economic policymaking. For instance, Jarvis (2013:61) notes that states cannot always act autonomously and enforce its will such as during periods of rebellion or civil disobedience. Moreover, even the most autocratic of governments make some attempt to respond to public will and democracy and politics ensures that most states can never act in the autonomous manner that is ascribed to them. Similarly, Cairney (2013d) critiques the Westminster model of government as an overly simplistic account of public policymaking, which in reality is far more complex and involves a greater number of actors. For example, the Westminster model of government does not include examination of the role of interests and institutions outside of the realm of the state and their influence on policymaking is absent. Similarly, the proposition that an individual's motivation in policymaking stems from ideas are excluded from the Westminster model of government understanding of the policymaking process.

These challenges to rational choice theory of human agency have profound implications for the stages model, EBP and state-centric frameworks and their explanation of when and why policies change. Ultimately, the claim that policies change as the result of rational analysis by technocrats operating within state institutions is unconvincing due to its implausible account of human agency and its dismissal of the role of politics or ideas in decision-making. For example, Hall (1993:275) criticises state-centric scholars because they fail to explain the process by which national interest comes to be defined in the first place or when and why the states perception of the national interest comes to change. As a result, when applied to models of economic policymaking, state-centric accounts have had to introduce the model of punctuated equilibrium to understand when and why policies change.

This was evident in the comparative study of economic policymaking in the United Kingdom (UK), Europe and the United States (US) during the interwar and post-war period conducted by Weir and Skocpol (1985). In order to explain why some nation-states pursued economic policy change in response to the Great Depression in the early 1930s, whilst others exhibited economic policy continuity, the authors deployed the model of punctuated equilibrium. Here, the authors located power in economic policymaking as residing in institutions of the nation-state. Consequently, the divergence of economic policy responses to the great depression was explained as the product of the openness of state institutions to new ideas. For those nation-states with institutions that were characterised by openness, the exogenous shock of a substantial economic crisis in the interwar period was sufficient to lead to radical policy and ideational change. Consequently, policy and ideational change is conceived as a discontinuous process akin to that described by the model of punctuated equilibrium. However, for those nation-states with institutions that were closed to new ideas, economic policy was guided by the substantial policy legacies of the past, which produced continuity in economic policy outcomes.

The use of punctuated equilibrium to understand when and why policies change was also evident in a later work by Weir (1989), which focused on interwar and post-war UK economic policymaking. Here, the author argued that UK

economic policy outcomes in the interwar period demonstrated significant continuity because of the powerful role played by the Treasury, which was administered by a closed and hierarchal civil service. Consequently, economic policy was guided by the economic policy legacies of the nineteenth century. However, to explain the discontinuous nature of economic policy change of the post-war era, Weir deployed the model of punctuated equilibrium. Thus, the Second World War was presented as an exogenous shock, which opened up the Treasury to new economic ideas and provided the stimulus for the creation of new institutions, which formed the basis for radical economic policy change and the Keynesian policy equilibrium that existed in the post-war years.

The chapter will now proceed to consider pluralist conceptions of public policymaking through the evaluation of three of its more well-developed frameworks: public choice, policy networks and the advocacy coalition framework (ACF). Pluralist frameworks of public policy have their contemporary origin in the concept of ‘issue-networks’ (Heclo, 1978). Hill (2014:26-30) and Smith and Larimer (2013:75) note that in pluralist frameworks power within the policymaking process is considered to be more fragmented, decentralised and openly contested than within the state-centric framework. Indeed, policy making is characterised as a political process of competition in which different organisations or interest groups outside of the state try to secure influence and the implementation of their policy preferences. Consequently, Howlett and Geist (2013: 19) purport that a key aspect of pluralist frameworks of public policy making is to identify the key actors involved, their motivations, methods of interaction and what effect these interactions have on policy development.

Public choice has its origins in the post-Second World War period (Arrow,1951;Downs,1957;Buchanan & Tullock,1962). Public choice frameworks adopt the individualist methodological assumptions of rational choice theory and assume that individuals and state bureaucrats are self-interested and engage in utility-maximisation (Whitford,2013). Therefore, Smith and Larimer (2013:54-62) contend that public choice theory is the transference of the logic of the market to politics in which governments and politicians are claimed to compete to win electoral support

and interests compete to gain policy concessions in a political marketplace. For example, in public choice frameworks, policy change is understood to arise from the actions of self-interested utility-maximising individuals, both public and private, via the democratic process. For that reason, at the very core of public choice are the weaknesses of the rational theory of human agency previously identified.

The emergence of the policy network framework of analysis has its origins in the US and UK policy studies (Knoke,1990;Knoke et al,1996;Lauman & Knoke, 1987;Marsh & Rhodes,1992;Rhodes,1994;1997). Wu and Knoke (2013:153-154) claim the overarching objective of policy network analysis centres on how the relationships between actors help to determine policy decisions. Therefore, the crux of policy network analysis is the identification of different types of social and political interaction that occurs between actors in public institutions such as political parties, labour unions and business organisation and state institutions such as executive agencies and ministries. Thus, Wu and Knoke (2013:155-156) characterise the policymaking process as one of competition between opposing policy networks, which are brought together in order to influence the policymaking process so as to secure policy change to reflect their preferences.

Several studies of UK economic policymaking have utilised the concept of policy networks. Here, three influential examples are provided. First, Katzenstein (1978) developed a proto-policy network analysis in his comparative study of foreign economic policy making in nation-states in Western Europe and the US. In this work, coalitions of public and private interests are claimed to find their institutional expression in the form of distinct policy networks, which seek to influence the formulation and implementation of foreign policy. Consequently, a state's foreign economic policy is presented as the product of the organised support it receives from key societal groups.

Gourevitch (1986) also used a comparative study of economic policymaking in advanced industrial countries, which included the UK, to argue that economic policy is predicated on the mobilisation and retention of political support in favour of change or continuity. For example, Gourevitch (1986:20) argues 'politicians have to

construct agreement from among officeholders, civil servants, party and interest group leaders and economic actors in society' on the formulation and implementation of economic policy. Consequently, Gourevitch (1989) argues that the adoption of Keynesian economic policies and ideas in the interwar period was predicated on the capacity of politicians to construct new coalitions of support in favour of change.

Finally, Hall (1986) also adopted a pluralist framework in his comparative study of UK and French economic policymaking in the interwar and post-war eras. Here, Hall stresses that economic policy is heavily influenced by market and societal institutions. First, because it is through these institutions that an actor can bring to bear pressure and influence on economic policymaking process. Second, because the position of an actor within the institutional structure determines their perception of individual interest, political behaviour and policy preferences.

The ACF has its origins in the late 1980s and early 1990s (Sabatier & Jenkins-Smith,1988;1993). Like policy networks, advocacy coalitions are said to consist of a range of public and private actors seeking to influence the policymaking process. The major difference between ACF and policy networks is the role of beliefs and ideas. Therefore, Sabatier and Jenkins-Smith (1988:139) define advocacy coalitions as groups of actors who 'share a particular belief system' and 'who show a non-trivial degree of coordinated activity over time'. Consequently, Weible and Norhstedt (2013:127-128) consider policy to be the translation of the beliefs of a victorious coalition into policy. In the ACF, the policymaking process is understood as a political competition between various advocacy coalitions as 'alliances [seek] to translate their beliefs into actual policies before actors with different belief systems can do the same' (Ibid:128). Accordingly, opposition coalitions fight over available resources, access to venues (in which to communicate their beliefs) and influence over the formulation of public policy. Here, Weible and Norhstedt (2013:129) identify six key resources which are important both in forming and maintaining advocacy coalition and provide influence in the policymaking process, which are formal legal authority over policy implementation, public opinion, information, personnel, finance and leadership.

Policy network models of public and economic policymaking can be criticised, however, for failing to provide an inadequate exploration of the reasons behind when and why policies change (Dowding,1995), which has been accepted by some policy network scholars (Marsh & Rhodes,1992:Chp.11;Pemberton,2000:789). For example, policy network analysis does not explain when and why certain policy networks are more successful in securing economic policy change than alternative competing policy networks. Despite being leading practitioners of the ACF, Weible and Norhstedt (2013:133-134) indicate this very weakness when they consider the gaps in our current understanding of ACF's. First, they identify that within the ACF there is little understanding about different pathways that lead to policy change or continuity in outcomes. Second, they identify that the ACF in its current form does not explain the conditions under which dominant coalition members to seek to preserve policy continuity or agitate for policy change.

Hill (2014:67) also highlights a further problem with policy network analysis in that it fails to adequately explain how policy networks actually influence the policymaking process. When policy network analysis does attempt to explain how policy networks influence policymaking, it is often ascribed to the technical expertise and scientific data of the actors within the policy network. However, this leads policy network analysis towards the technocratic explanations of policy change evident in the stages model and other rational models of policymaking. This has lead John (1998:85-86) to argue that policy networks are 'hard to use as the foundation for an explanation [of policymaking] unless the investigator incorporate other factors, such as the interests, ideas and institutions, which determine how networks function'.

The inability of policy network analysis to explain when and why policies change was evident in the work of Gourevitch (1986:Chp.1), which was introduced earlier in the chapter. In order to explain the stimulus for the formation of new political coalitions necessary to produce change in economic outcomes, Gourevitch (1986) deployed the model of punctuated equilibrium. Consequently, the process of policy change was conceived as a discontinuous process that arose from the exogenous shock of severe economic crises in the interwar period. For instance, Gourevitch (Ibid) argued that it was the economic crises of the interwar period that

caused the disintegration of political coalitions that supported continuity in economic policy. In their place, new coalitions of interest formed in favour of economic policy change. These new coalitions of interests then drove the economic policy and institutional change in the interwar period that formed a new economic policy equilibrium in the post-war era.

A further pluralist account of UK economic policymaking was provided by Hall (1993) in his work on social learning and policy paradigms. Hall (1993:279) defines policy paradigms as 'a framework of ideas and standards that specifies not only the goals of policy and kind of instruments used to attain them, but also the very nature of the problems they are meant to be addressing'. Furthermore, policy paradigms are embedded in communication and are influential because it is taken for granted in policymaking. Meanwhile, Hall (1993:278) defines social learning as the 'deliberate attempt to adjust the goal or techniques of policy in response to past experience and new information. Learning is indicated when policy changes as the result'.

The aim of Hall's (1993) work was to distinguish the different learning processes that provoked simple and radical policy changes. Here, Hall evaluated policy outcomes into objectives, policy instruments and settings. Similarly, Greenaway and Shaw (1988:Chp. 17) argue that macroeconomic policy can be evaluated in three steps. The first step is to determine policy objectives. Here, the policy scholar must determine the priority objective assigned to macroeconomic policy in times of policy conflicts. For example, is the priority objective price stability or full employment? The second step is the formulation of policy. Here, the policy scholar should determine whether policy instruments are logically consistent with the attainment of the prioritised macroeconomic objective. The third step relates to the cost-benefit evaluation of policy effectiveness, which involved analysis *for* policy and does not concern us in this chapter.

In order to distinguish between simple and radical policy change, Hall (1993) broke down the policymaking process into the notion of first, second and third order change. First order changes are based on new experiences or knowledge and involve

changes in policy settings. For instance, first order change would include raising or lowering interest-rates. Second order change is based on dissatisfaction with previous experience and involves changes in policy instruments. Third order changes involve the transition to new economic policy objectives, which includes ideological transformation that extends ‘well beyond the boundaries of the state to involve the media, outside interests and contending political parties’ (Hall,1993:288). Consequently, third order change involves the institutionalisation of a new economic policy paradigm as its supporters secure positions of authority in politics and policymaking.

Hall (1993:279) characterises first and second order changes as normal policymaking ‘that adjusts policy without challenging the overall terms of a given policy paradigm’ and preserves broad continuities in policy. However, third order change is a more disjunctive process that is associated with policy discontinuity. In order to explain the process through which normal policymaking transforms into fundamental policy and ideational change, Hall introduces the notion of crisis. Thus, third order change is dependent upon the accumulation of policy anomalies. For example, an exogenous shock, such as economic crisis, or an endogenous shock, such as a change in government, serves to undermine the existing paradigm. This leads to experimentation with new policies. The resultant failure of policy experimentation causes further endogenous shock as the locus of authority over economic policy fragments and new actors with different economic ideas from the existing policy paradigm enter the political arena. It was through this process of first, second and third order change, according to Hall (1993), which led to the transition in policy paradigms in UK economic policymaking during the 1970s from Keynesianism to monetarism.

Consequently, Hall used the model of punctuated equilibrium to explain when and why changes occur in economic policy and ideas. For example, Hall (1993:280) recognises that policy paradigms ‘generate long periods of [policy] continuity punctuated occasionally by the disjunctive experience of a paradigm shift’. Thus, policy change is conceptualised as discontinuous process arising from an exogenous or endogenous shock. Furthermore, subsequent attempts to refine the

application of social learning and policy paradigms to UK economic policymaking have continued to utilise the model of punctuated equilibrium to explain when and why economic policy and ideas change. For example, Greener (2001), Oliver and Pemberton (2004) and Pemberton (2009) all emphasised that the institutionalisation of a new policy paradigm requires a powerful exogenous shock – or shocks – sufficient to undermine the previous policy paradigm. These shocks, it is claimed, lead to the introduction of policy anomalies, the failure of policy experimentation and render the policymaking process susceptible to new ideas. Therefore, Greener (2001:133) accepts that social learning and policy paradigm explanation of economic policymaking 'comes to resemble a process of punctuated equilibrium with substantial periods of apparent stability followed by fairly sudden change'.

The chapter will now proceed to examine constructivism explanations of policymaking, which has its origins in the re-emergence of the interest in the role of ideas and discourse analysis in political science in the 1990s. Constructivism literature argues that social and political world is a construction. For example, discursive strategies in politics seek to construct what is social and economic reality, transmit what is considered acceptable behaviour, communicate favoured assumptions and values, obscure the role of vested interests and constrict contestation from alternative policy and ideas (Wiggans,2014:384). Three explanations of the relationship between discourse and policymaking are available in the literature: frames (Druckman,2010), narratives (Stone, 1989) and causal stories (Blyth,2002:39). Here, Rochefort and Donnelly (2013:194-200) note that frames and narratives are very closely aligned as frameworks, both being used as devices in political discourse to bring order and meaning to situations, to make sense of reality and to heighten the impact of a particular message. Thus, narratives are deployed for political purposes in an effort to present facts or explanations of events that identify a problem and legitimise policy solutions (Campbell,1998:385;Campbell,2002:27-28; Van der Pas,2014:45).

One area where a constructivist analysis has been often applied is to the impact of globalisation on public and economic policymaking. For instance, Hay (2002:258) articulates that 'whether the globalisation thesis is true or not may matter

less than whether it is deemed to be true – or, quite possibly, just useful – by those employing it'. Therefore, globalisation 'may provide a most convenient alibi, allowing politicians to escape the responsibility... [for policies that] would otherwise be rather difficult to legitimate' (Hay,2002:259). Here, Hill (2014:48) notes that active agents (policymakers) are understood to operate within a structure (globalisation) but the structure is not all determining, rather, it is how that structure is perceived or used by agents that determine policy outcomes. Subsequently, a plethora of academic literature arose in the 1990s suggesting that globalisation was being used by governments as a discursive weapon, which was used to justify the implementation of neoliberal economic policies (Bourdieu,1998;Krugman,1994; 1994a). For instance, Watson and Hay (2003) argue that globalisation was presented in political discourse by the New Labour government after May 1997 as a non-negotiable external economic constraint, which rendered contingent policy choices as necessity.

Henderson (1986) provides an interesting account of the role of ideas in UK economic policymaking, which was based on his experience as an economist at the Treasury in the 1960s. In his experience, Henderson found ideas to be important in policy decision-making, however, the ideas that were important were not those of his fellow professional economists. Indeed, Henderson (1986:3) encountered ideas about economic policy, 'which owe[d] little or nothing to the economic profession' or 'the elaborate systems of thought which occupy the minds of trained economists'. Instead, Henderson (Ibid) found that the ideas brought to bear on UK economic policymaking were the 'intuitive ideas of lay people', which he termed do-it-yourself-economics. Furthermore, Henderson (1986: 10) found these economic ideas had been constructed within Whitehall, which was a 'self-contained world, generating its own information and ideas'.

One scholar from the constructivism perspective who has been particularly influential in giving ideas a central role in our understanding of when and why policies change is Blyth (1997;2002) For example, Blyth (1997:246) cast economic ideas as both the facilitator and prerequisite of radical policy change. Subsequently, Blyth (2002) argued that economic ideas were central to the 'great transformation' of

economic policy and institutions in the United States and Sweden during the interwar period. However, in order to explain why economic ideas are so important in instigating radical policy change, Blyth (Ibid) had to import the model of punctuated equilibrium into his analysis.

In Blyth's (2002:9-11,18,35-37) explanation of when and why a 'great transformation' in US and Swedish economic policy and institutions occurred during the interwar period the great depression is introduced as an exogenous shock, which introduced a period of radical uncertainty that disrupted the existing ideational, institutional and policy equilibrium. This uncertainty led to a battle of ideas, which consisted of actors drawing on economic ideas to reduce uncertainty through the provision of narratives that attempted to make sense of the crisis and allow collective action to form around policy solutions. Here, the crucial interplay between economic ideas and discourse becomes much clearer because ideas allow actors to interpret events, designate when a crisis is a crisis, reduce uncertainty and provide the policy solutions, which lead to 'great transformations' in policy and institutions. Indeed, Hay (1996:255) identifies that power in policymaking 'resides not only in the ability to respond to crisis. But to identify, define and constitute crisis in the first place'.

The notion of 'shock' and 'crisis' is fundamental to discussion of the model of punctuated equilibrium. However, until recently there had been little interest in establishing precisely what has been meant by 'crisis', which has been rectified by the constructivism literature. For example, Gamble (2009:38-40) provided a linguistic analysis of what is meant by 'crisis', which has been alternatively defined at different points of history as a 'turning point', 'opportunity', 'impasse', 'event' and 'emergency'. Here, Gamble (2009:39) identified that the most widespread use of the term 'crisis' is synonymous with a critical event, which causes a political emergency that requires immediate action. The notion of crisis as an event has also been deployed by Claessans, Kose and Terrones (2013:3) whom describe economic and financial crises as an 'amalgam of events… driven by a variety of factors'. Thus, Gamble (2009:38) notes that for 'much of the history of capitalism, crises were considered to be more natural events than political events, brought about by economic laws rather than by political actions'.

Gamble (Ibid) posits that during the development of the modern capitalist economy, however, this perception of 'crisis' began to change. Thus, our current understanding of 'crisis' is not one of a 'natural event, but a social event', which 'is always socially constructed and highly political. The narratives that are used to designate an event or period as a crisis imply certain courses of action, and privilege some responses over others'. Consequently, constructivism argues that crises are endogenous constructions (Widmaier et al,2007) through ideas, which are deployed in political discourse (Hay,2006). Thus, Gamble (2009:39) contends that 'crises are constructed by particular narratives and interpretations of events, which legitimate particular ways of resolving them. In this view an economic crisis is not just something that impinges upon us with the force of a natural event. It is something we construct for ourselves'. This provides us with an operational definition of 'crisis' throughout the remainder of the thesis.

The Global Financial Crisis of 2007-2009 has spawned a wide and voluminous academic literature. Specifically, we are interested in what this literature tells us about the consequence of the Global Financial Crisis for when and why policies and ideas change. Several scholars used the model of punctuated equilibrium – the notion that crises lead to radical policy, ideational and institutional change – to forecast the impact of the Global Financial Crisis on the capitalist system, governance and politics. For example, Bresser-Pereira (2010) and Kotz (2009) argued that the global financial crisis would lead to the development of new forms of capitalism and democracy, which would involve major restructuring of current economic and political systems. Several scholars also predicted that the global financial crisis would lead to a paradigm shift in global financial governance and regulation of the financial markets (Crouch,2008;Mackintosh,2014;2015; Nesevetailova & Palan,2010). Furthermore, in the context of UK politics and economic policymaking, Marsh (2009) claimed that the global financial crisis would lead to a 'severe questioning' of the 'neoliberal orthodoxy'.

The reliance on punctuated equilibrium to explain when and why policy and ideas change, however, has become increasingly problematic in recent years. Indeed, Gamble (2009:9) warned in 2009 that the history crises of capitalism demonstrates

that crisis need not lead to change, but actually can be used by political forces to re-assert and strengthen the pre-crisis economic and political order. Similarly, historical analysis of the development of capitalism from the late eighteenth century onwards led Kaletsky (2010) to argue that crises lead to the evolution and reinvention of stronger forms of the capitalist model. Here, Kaletsky contended that the collapse of Lehman Brothers on the 15th September 2008 marked a 'turning point' for the fourth major systemic transformation in capitalism's history. Finally, Klein (2008) offered a repudiation of punctuated equilibrium in her 2008 book *The Shock Doctrine*, which argued that developed countries had exploited national crises, such as disasters and war, to deepen the economic and political project of neoliberalism through the implementation of controversial economic and public policies.

Several scholars in the contemporary period therefore have started to question the assumption contained in punctuated equilibrium that exogenous shocks such as the Global Financial Crisis leads to radical policy, ideational or institutional change. For example, Blyth (2013) used historiography to document the continuity of post-crisis fiscal policy strategies of 'austerity' in different historical periods among the advanced industrial nations. In another work, Blyth (2013a) noted that the institutionalisation of a new policy and ideational paradigm in the global economy is conspicuous by its absence in the aftermath of the Global Financial Crisis. Moreover, Crouch (2011) and Schmidt and Thatcher (2013) have identified that neoliberal economic ideas have emerged from the global financial crisis more political powerful than they had been prior. Finally, several scholars argue that global financial governance and financial regulation is marked more by pre-crisis continuity than radical change (Helleiner,2014;Mugge,2014;Tsingou,2014). Continuity in pre-crisis policy has also been found in studies of US public policy (Wilson, 2012) and European trade policy (De Ville & Orbie, 2014).

Since the Global Financial Crisis there has been a multitude of literature that has provided excellent narration of the political context of UK economic policymaking and the economic policy response. This literature broadly identifies that the Global Financial Crisis caused a 'change' in UK macroeconomic policy and economic ideas through the implementation of 'unconventional' monetary policy and

fiscal policy stimulus inspired by the ideas and theories of Keynes to counteract the deleterious impact of crisis on UK economic performance. In turn, this literature acknowledges that the formation of the Conservative-Liberal Democrat Coalition Government on the 11th May 2010 and the resultant 'Emergency Budget' in June 2010 saw policy change from fiscal stimulus to the implementation of an 'orthodox' strategy of austerity, which was mirrored among the states of the G20 (Blyth,2013:ix).

Questions of the applicability of punctuated equilibrium therefore have been asked in the context of contemporary UK economic policymaking since the Global Financial Crisis. For example, Froud (2010) and his fellow authors have suggested that the 'crisis is being wasted' in that the global financial crisis failed to stimulate radical reforms to UK financial regulation or the creation of a new political economy that would redistribute the wealth of the City of London to the rest of the economy. Similarly, Sukhdev (2012) and colleagues claimed that the Global Financial Crisis has failed to instigate change in UK politics and governing system, which has seen a reassertion of power by traditional elites who have stymied political and policy change. Subsequently, UK studies have found continuity of pre-crisis policy in areas such as regulation (Lodge, 2014), social and unemployment policy (Chung & Thewissen,2011) and welfare reform (Mabbett,2013).

The observation of continuity has also extended to UK economic policy and economic growth model. For example, recent literature has found that, in contrast to the 'rebalancing' rhetoric of the UK Coalition government formed on the 11th May 2010, economic policy has supported and re-built the pre-crisis economic growth model (Berry & Hay,2016;Hay,2011). Indeed, Crouch (2009) forecast that a likely consequence of the crisis for UK economic policymaking was the re-creation of the policy regime of 'privatised Keynesianism'. Similarly, Hodson and Mabett (2009) posit that the development of economic policy post-crisis does not show signs of developing into a new and radical economic policy regime. Furthermore, Dunleavy (2010;2010a) identifies a post-crisis resurgence of neoliberal economic ideas – particularly in neoliberal attitudes to the state - in UK economic policymaking and Macartney (2011:193) argues that neoliberal ideas and policy are 'being invoked as

the solution to the ongoing crisis facing the British economy'. Cumulatively, Hay (2013: 23-24) claims that the lack of transition to a new policy paradigm in UK economic policy in response to the recent global financial crisis challenges the common assumption within the policy studies literature that crises lead to change in policy and ideas.

The challenge to punctuated equilibrium through the identification of continuity in UK economic policy in the aftermath of economic crises, however, is not unique to the contemporary era. For example, Booth (1982) charts a historical relationship in UK economic policy between crisis and continuity of 'orthodox' economic policy. Here, Booth argues that the consequence of each international unemployment crisis (1919-1922, 1930-1933 & 1976-1981) has been widespread support in the UK for the 'orthodox' doctrines of economic liberalism, which are implemented as 'crisis solution' policies. Indeed, Booth applied a proto-constructivist analysis to explain the relationship between crisis and 'orthodoxy' claiming that vested interests used their influence in discourse and economic policymaking to legitimise 'orthodox' policy preferences as the policy solution to crises. Consequently, Booth (1982:215) concludes that 'in each case [of crisis], the mass electorate has given substantial support to political parties promising to pursue an 'orthodox' solution to mounting economic problems... pledged to restore the soundness of currency, enforce reductions in real wages, and concentrate economic policy making in its own hands by terminating corporatist initiatives'.

Ingham (1984) also identifies the existence of UK economic policy 'orthodoxy', which was a product of the core institutional nexus at the heart of the UK state and economic policymaking. Here, Ingham (1984:131) argues that the emergence of financial, monetary and commercial policy 'orthodoxy' in the nineteenth century was predicated on the role of the City of London-Bank of England-Treasury within the British state. For example, Ingham (1984:131,142) contends that this core institutional nexus forms a 'centre of power' within the state that is predicated on an 'ingrained system of interdependencies'. These interdependencies include the 'mutual interest they have in the production of stable money forms' and because the perpetuation of 'orthodoxy' forms 'independent

sources of power for the Bank and Treasury in their own respective domains' of the banking system and state bureaucracy (Ingham,1984:9). Consequently, Ingham (1984:142) highlights that the core institutional nexus 'have proved to be effective political resources in repelling industrially based moves to adopt economic policy which, by implication, would have challenged the City's position'. According to Ingham, this has ensured the continuity of 'orthodoxy' in UK economic policymaking.

These accounts of continuity in UK economic policy present a challenge to the model of punctuated equilibrium. However, whilst contemporary scholars have identified continuity in policy and ideas, unlike Booth and Ingham, they do not seek to draw wider judgements as to when or why that continuity occurs. For example, the closest explanation we have on this issue in the contemporary literature is provided by Hay (2013:23-24) who argues that a 'debt crisis' narrative in UK politics proved to be 'paradigm-reinforcing rather than paradigm-threatening'. Furthermore, contemporary accounts of continuity in UK economic policy and ideas have been shorn of historical context and are limited to comparative analysis immediately before and after the global financial crisis. Thus, the chance to draw wider judgements on the reasons for change and continuity during earlier historical periods is lost. This thesis will provide a corrective to this problem by presenting a historiography of UK economic policymaking in response to major economic crises in the Twentieth century with particular focus placed on macroeconomic policy[2]. A

[2] Here, it is worth highlighting that this thesis uses historiography in a different way than that currently available in the contemporary literature, which has deployed historiography in two ways. First, historiography has been utilised to place the causes and consequences of the Global Financial Crisis within a historical context. For instance, see Bordo and Landon-Lane (2010), Bordo and Meissener (2012), Boyer (2013), Claessens, Kose and Terrones (2010), D'Arista (2009), Eichengreen and Temin (2010), Gamble (2009), Graeber (2011), Grossman and Meissner (2010), Krugman (2008), McNally (2009), Perez (2009), Reinhart and Rogoff (2008; 2009;2009a;2011;2011a;2013;2014), Reinhart, Reinhart and Rogoff (2012), Schularick and Taylor (2012) and Wray (2009). Second, historiography has been deployed as part of the fiscal stimulus vs. austerity debate in order to draw policy lessons for contemporary policymakers. For instance, see Almunia, Benetrix, Eichengreen, O'Rourke and Ria (2010), Blyth (2013), Bordo and Landon-Lane (2010a), Crafts and Fearon (2010), Ferguson (2010;2010a;2015), Fishback (2010),

result of these problems in the contemporary literature is that we are presented with a gap in our current knowledge of UK economic policymaking for analysis that seeks to provide a superior understanding of when and why change or continuity occurs in economic policy and ideas. Consequently, this thesis will provide analysis *of* policy of the type described at the opening of the Chapter.

There are certain areas however that subsequent historiography and case-study chapters will not address because they are not immediately pertinent to the examination of change and continuity in UK economic policymaking or because they have already been the subject of intense study in the literature. For example, there are now many exemplary accounts, which provide detailed narration of the major events of the Global Financial Crisis and present three key themes of explanation pertaining to its causes[3]. Thus, subsequent chapters will only provide a brief overview of the

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Grossman and Meissner (2010), Hatton and Thomas (2010), Jorda, Schularick and Taylor (2011), Kregel (2009), Krugman (2008;2012), Middleton (2010) and Trefargne (2012).

[3] The three key themes of explanation as to the origin of the Global Financial Crisis are those that blame the crisis on the financial markets, the state or political economy. Those that claim the origins of the crisis arose in the financial markets emphasise the role of complex credit instruments and their distribution through the financial system due to flawed business models of financial institutions. For example, see Akerlof and Schiller (2009), Archarya and Richardson (2009), Archarya, Phillipon and Richardson (2009), Brunnermeier (2009), Cassidy (2010: Part Three), Claessens, Dell'Arriccia, Igan and Laeven (2010:272-275), Gambacorta and Marques-Ibanez (2011), Kacpercyzk and Schnabl (2010), Keys, Mukherjee, Seru and Vig (2010), Loutskina (2011), Mishkin (2011:49-58), Naduald and Sherlund (2013), Purnanandam (2011), Pym and Kochan (2008), Schleifer and Bishny (2010), Shiller (2012), Shin (2009), Stiglitz (2010), Tett (2010) and Thakor (2012). Those that claim that state is to blame for the crisis cite growing macroeconomic imbalances between the US, China and the Far East and the 'loose' monetary policy of the Federal Reserve, which created a 'search for yield' in financial markets during the 2000s. For instance, see Carmassi, Gros & Micossi (2009), Cechetti (2009), Morgan (2009), Obstfeld and Rogoff (2009) and Wade (2009). Finally, those that argue the crisis was a problem of political economy identify the financialisation of domestic economic growth models, particularly in the US and UK, which lead to housing booms and inadequate regulation of domestic and global financial markets. Here, see Alp (2013), Baker (2010), Bellamy Foster & Magdoff (2009), Bishop and Green (2011:Part One), Brummer (2009), Cable (2010), Crotty (2009), Demyanyk & Van Hemert (2009), Elliott and Atkinson (2009), Gamble (2009), Goetzmann, Peng and Yen (2012), Martin (2011), Mason (2010), Mian and Sufi (2011), Mullard (2012), Pagano and Rossi (2009), Palma (2009) and Wainright (2009).

events and causes of the numerous economic crises to have plagued the UK economy since 1914. Indeed, due to our operational definition of 'crisis', what matters in this thesis are not economic events or emergencies themselves, but rather how crises have been constructed through narratives and how those narratives have influenced change and continuity in UK macroeconomic policy.

As the focus of this thesis is placed on analysis *of* policy, subsequent chapters will not conduct analysis *for* policy, which would include normative or subjective scrutiny of whether the economic policy implemented across different historical periods were the best available policies to secure outcomes such as economic stability, growth, employment or a more equal distribution of income and wealth. This area of analysis is another example of a literature that is already well served and has been added to in the contemporary era by the vociferous debate as to the relative merits and weakness of macroeconomic strategies of fiscal stimulus or 'austerity'[4]. Furthermore, subsequent chapters will not expound upon the role of institutions in the formulation and implementation of policy except to note that, in specific instances, change and continuity is supported by the creation of new institutions and operational changes to the governance of macroeconomic policymaking. Moreover,

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[4] Those who supported the implementation of austerity deemed it necessary to reduce government borrowing and national debt in order to placate financial markets and insulate the domestic economy from the spread of the sovereign debt crisis. For example, see Barro (2009), Booth and Shackleton (2011;2011a), Cochrane (2009;2011;2011a), Fama (2010), Harrison (2011), Fender (2012) and Thompson (2009;2013). Furthermore, the notion that public spending cuts would lead to economic growth – otherwise known as expansionary fiscal consolidation - had been developed during the 1990s. For instance, see Alesina and Ardagna (1998), Alesina and Perotti (1995;1997), Barry and Devereux (2003), Bertola and Drazen (1993) and Giavazzi and Pagano (1990). Meanwhile, those who criticised the implementation of austerity did so on the grounds that it was self-defeating. Here, it was claimed that austerity would lead economic growth to contract, which would cause higher government borrowing and national debt due to a rise in unemployment. Consequently, it was argued that global and domestic economic conditions required further fiscal policy stimulus to maintain demand and support economic activity. For example, see Brittan (2011), Chick and Pettifor (2010), Delong and Summers (2012), Jorda and Taylor (2013), Krugman (2008;2012), Mishkin (2011:63-64), Mitchell (2013), Pettifor (2012), Pettifor and Coe (2012), Sawyer (2012), Skidelsky (2009;2011;2011), Stiglitz (2010a;2010b;2010c;2012;2013;2014), Summers (2012;2012a;2012b;2013;2013a;2014), Weeks (2011) and Wren-Lewis (2011).

following chapters will not explain how established interests influence the policymaking process and policy outcomes. The analysis *of* policy provided by this thesis is focused narrowly on the when and why of change and continuity in UK economic policymaking, rather, than the process through which policy decisions are taken or how established influence policy outcomes. Finally, further discussion of the historiography and case-study research design of this thesis and the methods deployed in data collection and analysis is provided in Chapter Five; the justification for the placing of the methodology chapter at this juncture of the thesis structure is provided in that chapter.

Conclusion

This chapter has reviewed the literature on models of public and economic policymaking and examined how they understood the process through which policy decisions are formulated and implemented, when and why policies change and how interests and ideas influence policy outcomes. The chapter has argued that these models' reliance on punctuated equilibrium to explain when and why policies change is problematic. Specifically, contemporary policy scholars have begun to question the explanation provided by punctuated equilibrium that economic crises leads to radical policy and ideational change. The resultant gap in our knowledge of UK economic policymaking requires an alternative analysis capable of providing a superior understanding of when and why change or continuity occurs in economic policy and ideas. Indeed, as forthcoming chapters will demonstrate, the model of punctuated equilibrium presents a misleading explanation of when and why UK macroeconomic policy exhibits change and continuity since 1914. The next chapter will review the literature on UK economic policymaking and economic performance during the interwar years between November 1918 and December 1934.

Chapter 3

Change and Continuity in UK Economic Policymaking during the Interwar Years

Introduction

This chapter reviews literature and provides a historiography on United Kingdom (UK) economic policymaking and economic performance between November 1918 and December 1934. Existing explanations for interwar policy change are rooted in the notion of punctuated equilibrium, which asserts that policy change in the 1930s derives from exogenous shocks of economic crises such as the 1929 Wall Street Crash, Great Depression and 1931 Global Financial Crisis. This chapter exposes the flaws in this position and highlights two gaps in our current knowledge of UK economic policymaking. First, that greater specificity is required in our understanding and definition of 'orthodox' macroeconomic policy. Second, that there is a need for a superior understanding of when and why UK macroeconomic policy and ideas exhibit change and continuity.

Historiography in this chapter generates two research findings that fill these gaps in our existing comprehension of UK economic policymaking and provide an original contribution to our knowledge. First, greater clarity is provided in our understanding of 'orthodox' macroeconomic policy and ideas. The specification of 'orthodox' macroeconomic policy includes the identification of 'orthodox' economic ideas, an 'orthodox' policy objective and 'orthodox' policy instruments. In addition, the chapter identifies an 'orthodox' hierarchy between policy instruments and 'orthodox' fiscal policy outcomes. Second, a superior understanding of change and

continuity in UK macroeconomic policy and ideas is developed. Here, a historical pattern is discerned, which sees the continuity of 'orthodox' macroeconomic policy in the aftermath of crises through a series of distinct phases of crisis, temporary deviation, consolidation and orthodoxy in macroeconomic policymaking.

The remainder of the chapter will be organised as follows. The next section will outline how existing literature on interwar UK economic policymaking understands and defines 'orthodox' economic policy. The chapter will then examine how existing literature documents the return to 'orthodox' economic policy and 'orthodox' economic ideas in the aftermath of the 1914 financial crisis, First World War and the recession of 1919-1921. The chapter proceeds to demonstrate that the existing literature explains policy change in the 1930s by recourse to punctuated equilibrium. The final section of the chapter exposes the flaws in this explanation through analysis of UK economic policy in the aftermath of the economic crises of 1929-31, which shows that macroeconomic policy during the 1930s was marked by continuity of 'orthodox' macroeconomic policy and ideas.

Our Current Understanding of 'orthodox' Economic Policy in the Interwar Period

The literature on UK economic policymaking during the interwar period does not offer a definition of what is meant by 'orthodox' or 'orthodoxy'. Consequently, the dictionary definition is deployed as an operational definition of 'orthodox' and 'orthodoxy' for the remainder of the thesis. Thus, 'orthodox' is taken to mean 'following or conforming to the traditional or generally accepted rules or beliefs of a religion, philosophy, or practice' whilst 'orthodoxy' is understood as a 'generally accepted theory, doctrine, or practice'. Despite this lack of definition, 'Orthodox' and 'orthodoxy' are used liberally as a noun within the literature on UK economic policymaking in the interwar era. For example, the fiscal policy of the balanced budget and national debt reduction is alternatively described within the literature as

'budgetary orthodoxy', 'orthodox financial principles', 'financial orthodoxy', 'orthodox deflation' and 'Treasury orthodoxy'[5].

'Orthodox' and 'orthodoxy' are also used in conjunction with monetary and commercial policies, economic theory and ideas. Reflecting uncertainty in use of the terms, Booth (1982) variously labels economic liberalism, sound money and monetarism as 'orthodox' economic policies[6]. Furthermore, the Gold Standard is classed by several scholars as an 'orthodox' economic policy[7], whilst Howson and Winch (1977:162) designate free-trade as part of the interwar 'orthodox package'· Meanwhile, Glynn and Booth (1983:348;1996:134), Stewart (1967) and Winch (1969) argue that UK nineteenth century and interwar economic policy adhered to 'orthodox' neoclassical economy theory, which viewed the economy as a self-regulatory system producing full employment of labour. Similarly, Middleton (1996:181) and Peden (1991:2) posit that 'orthodox' economic policy was predicated on a belief in economic ideas of classical liberal political economy, which manifested itself in the desire to protect the free-market order. Therefore, the policy paradigm emerging from Victorian political economy of the balanced budget and national debt reduction, Gold Standard and free-trade provides us with our best understanding of' 'orthodox' UK economy policy in the post-war era (Ingham,1984:127;Middleton, 1996:54,181,355;2010:421;Peden,1991:1-6; Tomlinson,1990:14,40-41,98,Chp. 2)[8].

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[5] This description of the balanced budget and national debt reduction as 'orthodoxy' can be found in Booth (1983;1987), Glynn and Booth (1996:133.135), Gourevitch (1984:99-100), Howson and Winch (1977), Middleton (1981:272,274,278,284,286; 1982:51,53,59,72-73;1985;2010), Peden (1991:88), Stewart (1967:68), Tomlinson (1990:67,76-78, 95) and Winch (1969).

[6] Booth (1982) also discusses the importance of deflationary economic policies, consisting of public expenditure cuts and wage reductions, in order to increase competitiveness to interwar UK economic policymaking. However, unlike those policies and ideas stated above, the author never explicitly states these as 'orthodox' economic policies.

[7] The classification of the Gold Standard as an orthodox economic policy can be found in Eichengreen and Temin (2000:2010), Peden (1991:78), Pollard (1970) and Tomlinson (1990:28,66).

[8] Here, there is a problem with Middleton's classification of balanced budgets, Gold Standard and free trade as both policy instruments and policy objectives. The definition of an instrument is 'a tool or implement, especially one for precision work', whilst the definition of an objective is 'a thing aimed at or sought; a goal'.

The general ambiguity in our current understanding of 'orthodox' macroeconomic policy during the interwar period highlights a gap in our current knowledge of UK economic policymaking for greater specificity in our understanding and definition of 'orthodox' macroeconomic policy, which this chapter will provide. In this endeavour, the works of three scholars have been particularly influential. First, is the definition of policy paradigms provided by Peter Hall (1993), which were defined as a framework of economic ideas, policy objectives and policy instruments. Second, are the evaluative steps for the study of macroeconomic policy provided by Greenaway and Shaw (1988:Chp.17), which included determination of the prioritised objective of macroeconomic policy and the policy instruments implemented to achieve it. Consequently, this chapter advances an understanding of 'orthodox' macroeconomic policy as an interlocking framework of 'orthodox' economic ideas, an 'orthodox' policy objective, 'orthodox' policy instruments, hierarchy between those policy instruments and 'orthodox' fiscal policy outcomes.

UK Economic Policymaking in Response to the 1914 Financial Crisis, First World War and the Recession of 1919-1921

The assassination of the Austrian Archduke Franz Ferdinand in Serbia on the 28th June 1914 sparked a diplomatic crisis among the nations of Europe that precipitated a series of events and emergencies in global financial markets. The Global Financial Crisis of 1914 had a particularly severe impact on the City of London, which was the premier centre of global finance. In order to halt financial crisis, the Bank of England launched an unprecedented financial rescue of financial institutions in the City of London. Financial interventionism to save the City was conducted through a series of open market operations (OMOs) by the Bank of England, financed by the Treasury,

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Thus, by definition an instrument and an objective cannot be one and the same thing because a policy instrument serves the purpose of meeting policy objectives.

with the Bank purchasing bills of exchange from City financial institutions in an attempt to provide liquidity to then illiquid City financial markets. Indeed, such was the scale of financial interventionism, that by the end of the 1914 financial crisis, the Bank of England owned one third of the global market for Sterling denominated bills of exchange (Roberts,2013;2015:233-240).

This was not the first time in UK economic history; however, that financial crisis in the City of London had necessitated a significant financial bailout by the Bank of England. Indeed, Alan Greenspan (2002), Chairman of the United States Federal Reserve (1986-2006), identified in a speech on the 25th September 2002 that the Bank of England has a long history of performing "one of the main responsibilities of modern central banks: ensuring financial stability by serving as the lender of last resort" adding that "it was the Bank of England that established the concept during the financial crises of the nineteenth century". For example, Greenspan (Ibid) noted that the Bank of England had bailed out the City during the 1866 financial crisis, which was triggered by the failure of a prominent City discount house. This led the Bank of England to extend to the City a substantial portion of its currency reserves in an effort to "ensure that panic did not spread" (Greenspan,2002).

The diplomatic crisis that sparked the 1914 Global Financial Crisis was followed quickly by global conflict. The First World War was a new type of conflict for the nations of Europe and the demands of industrial and mechanized warfare caused a series of emergencies and events, which cumulatively served to produce another phase of crisis within UK economic policymaking. For example, 1915 saw an economic failure of production that led to a chronic shortage of shells on the Western Front. This failure of production in the UK economy led to an institutional crisis as the pre-war structure of capitalist production seemed incapable of producing and allocation the resources necessary to prosecute a global conflict. Furthermore, this institutional crisis led to a political crisis and the formation of a National Coalition government under the Liberal Prime Minister Lloyd George (1916-1922).

The reaction to these events and emergencies in economic policymaking was to implement change from the macroeconomic policies identified as 'orthodox' by the existing literature. For example, the economic demands of the conflict led to the effective suspension of the Gold Standard and departure from the 'orthodoxy' of balanced budgets and public expenditure and the fiscal deficit rose exponentially[9]. In turn, the First World War was interpreted by politicians and economic policymakers to have caused economic crises of inflation[10], government borrowing and national debt[11] (Peden,1991:37-43; Tomlinson,1990:43,51). Moreover, these 'emergencies' in macroeconomic performance were followed by a sharp recession in the UK economy from 1919-21, which saw unemployment rise above the 1million mark for the first time in UK economic history[12]. Finally, it was feared that the First World War had caused New York to usurp the City's position as the premier centre of global finance (Burk,1979).

Of vital importance in explaining developments in economic policy after the cessation of hostilities on 11th November 1918 is to understand that the First World War did not engender an ideational crisis. Here, Milward (1984:46-47) documents that change in economic policy during the First World War was not sanctioned politically due to the desirability of new economic ideas or theories, rather, economic policy change had arisen out of the necessity of prosecuting a new type of mechanised conflict. Similarly, Tawney (1943) notes that within politics, business, media and the Treasury there existed no support for war-time economic policies, which were viewed purely as a necessary expedient. The failure of the First World War to bring about ideational change meant that the parameters of policy formulation

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[9] UK membership of the Gold Standard was not formally ended until the Gold & Silver (Export Control) Act of 1920. However, the 1915 Defence of the Realm Act placed significant controls on the movement of gold meaning a de facto suspension of the Gold Standard (Moggridge,1972:16).
[10] 1914-1918 prices rose at an average of 19.45% per annum (Twigger,1999:13).
[11] The fiscal deficit had risen to £1989million by 1917-18 (Morgan,1952:98). Meanwhile, total national debt stood at £7830million and annual debt interest payments had risen to £325million from £20million in 1913 (Pollard,1992:97).
[12] By 1921, the number of persons unemployed had risen to 16.9%. Although this percentage fluctuated over the rest of the 1920s, it never fell below 10%. In 1914, the unemployment rate had been 4.2% (Garside,1990:4).

had not changed and the economic policy implemented during the conflict would only form a temporary deviation from the macroeconomic 'orthodoxy' identified by the existing literature. This is in contrast to what we should expect according to punctuated equilibrium, where exogenous shocks, such as war, are expected to lead to subsequent radical policy and ideational change.

A vital role in ensuring the return to macroeconomic policy 'orthodoxy' after the war was played by the Cunliffe Committee, which provided not only the intellectual justification for the return to 'orthodoxy', but also a narrative to legitimise the return to 'orthodox' macroeconomic policy. For example, the Cunliffe Committee, established before the end of the war, argued that economic recovery and prosperity in the post-war era depended upon the restoration of the Gold Standard at the pre-war parity of $4.86. Furthermore, the Cunliffe Committee recommend severe public expenditure reductions to ensure the fiscal budget was balanced and national debt reduction should take place (Committee on Currency and Foreign Exchanges,1918). Consequently, several scholars determine that economic policy after 11th November 1918 was predicated on the evident desire of policymakers to re-establish the pre-1914 economic world[13]. In terms of macroeconomic policy, scholars are united in agreement that for politicians, Treasury and Bank of England, the re-establishment of the pre-1914 economic world meant a return to the 'orthodox' macroeconomic policies of the Gold Standard, balanced budget and national debt reduction[14].

In terms of economic performance, the consolidation of fiscal policy towards 'orthodoxy' after the First World War is evident in Table One. Here, Morgan (1952:95-98,115-121) demonstrates that consolidation of the public finances

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[13] For example, the desire of policymakers to re-establish the pre-1914 economic world has been noted by Glynn and Booth (1996:125-128), Howson (1975:14), Robinson (1975:123), Sayers (1967:52), Tomlinson (1990:40) and Williams (1959).

[14] This argument has been made by many scholars on UK economic policymaking. For example, see Boyce (1987:Chps.1-2), Glynn and Booth (1996:128-133), Howson (1975: 14,23-29,Chp.3), Moggridge (1972:Chps.1-3,Chp.6), Peden (1991:Chp.4), Pollard (1992: 105-111), Tomlinson (1990:Chp.3) and Winch (1969:75-78,Chp.4,5,6).

consisted of reductions in public expenditure. The objective of this consolidation was to secure the conditions in the UK public finances, which would bring the budget to be brought back into balance and provide for the redemption of national debt. Indeed, from 1920-21 onwards, Table One shows that Her Majesty's Treasury secured significant fiscal surpluses in the public finances, which Tomlinson (1990:51-52) claims arose almost exclusively through public expenditure reductions.

Furthermore, the consolidation of fiscal policy towards 'orthodoxy' after the First World War was supported by the creation of the Geddes Committee, a new institution, albeit temporary, in fiscal policymaking. However, rather than forming the basis for radical fiscal policy change, this institution was created to ensure the consolidation of public finances to the 'orthodox' outcome of balanced budget. For instance, infamous in the drive to reduce public expenditure in the early 1920s was the 'Geddes Axe' of 1922. Appointed by Lloyd George in 1921, the Geddes Committee released three reports in total making recommendations that public expenditure cuts should amount to £87million[15].

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[15] The National government did not implement all of the public expenditure reductions recommended by the Geddes Committee, however, the scale of public expenditure reductions was still large. For example, total defence spending fell from £189.5million in 1921-22 to £111million in 1922-23. Total social expenditure fell from £205.8million in 1920-21 to £175.5million in 1923-24 (Peden,2000:169).

<u>Table One: Economic Performance of Fiscal and Monetary Policy, 1919-1924</u>

<u>Year</u>	**<u>Budgetary Stance</u>** (£millions) *(- = Deficit / + = Surplus)*	**<u>Inflation Rate</u>** (Annual Percentage Change)	**Bank Rate** (Average Annual Rate)
1918-1919	-1693	+22%	
1919-1920	-326.2	+10.1%	
1920–1921	+230.6	+15.4%	6.7%
1921–1922	+45.8	-8.6%	6.1%
1922–1923	+101.5	-14%	3.7%
1923–1924	+48.4	-6%	3.5%
1924–1925	+3.6	-0.7%	4%

(**Source:** Howson,1975:50;Morgan,1952:98;Twigger,1999:13)

Meanwhile, monetary policy did not return to the 'orthodoxy' of the Gold Standard until Winston Churchill's (1925) 1925 Budget Statement on the 28th April. However, this was not due to change in monetary policy, rather, monetary policymaking underwent a period of consolidation towards 'orthodoxy'. The purpose of this phase of consolidation in monetary policy was to provoke the deflationary economic conditions necessary to return to the Gold Standard at the pre-war parity of $4.86, which is demonstrated in Table One and began in 1920 when the Bank of England increased the Bank Rate to 7% (Howson,1973;1974). Consequently, the return to the Gold Standard can be considered the moment that politicians and economic policymakers secured the return to 'orthodox' macroeconomic policy and achieved their desire to re-establish the pre-1914 economic world.

The chapter has highlighted a pattern in UK macroeconomic policymaking from 1914 onwards, which saw macroeconomic policy return to 'orthodoxy' through a series of distinct phases in policymaking of crisis, temporary deviation and consolidation. Cumulatively, these phases begin the process by which we can begin to improve our understanding of when and why UK macroeconomic policy exhibits change and continuity. Furthermore, if we briefly consider macroeconomic policymaking in the eighteenth and nineteenth centuries, we discover a firm historical precedence for these phases in other historical eras.

Buchanan (1978:31-37) and Peacock and Wiseman (1961:41), for example, both determine that wars in the nineteenth century led to the suspension of the balance budget rule in fiscal policymaking as public expenditure and national debt increased. However, deviation from 'orthodoxy' would only be temporary as, in the aftermath of these conflicts, measures were taken to consolidate the public finances via the implementation of public expenditure cuts in order to return to the fiscal 'orthodoxy' of the balanced budget and reduce national debt. Indeed, Bordo and White (1990:4-5) have shown that this relationship between war, temporary deviation, consolidation and return to fiscal 'orthodoxy' in the public finances dates from the 1688 Glorious Revolution. Furthermore, the same relationship between war, temporary deviation, consolidation and return to 'orthodoxy' is also evident in nineteenth century monetary policy. For example, the only interruption to the UK's membership of the Gold Standard, of which it had been a member, de facto or de jure since 1717, occurred during the French Revolutionary and Napoleonic wars (1792-1815). In response to these conflicts, the Bank of England ended specie convertibility in February 1797. Convertibility was not reinstated until 1821[16].

The chapter has also highlighted several policy instruments and policy outcomes that provide greater clarity to our understanding of 'orthodox' macroeconomic policy. In terms of fiscal policy, 'orthodox' fiscal policy instruments include public expenditure reductions. Meanwhile, the 'orthodox' fiscal policy outcome was the balanced budget and national debt reduction. In terms of monetary

[16] For more information on this period of UK monetary policy, see Capie and Wood (1994:241), Eichengreen and Temin (2000:189-190) and Moggridge (1972:3).

policy, ‘orthodox’ monetary policy instruments include the Bank Rate. The specification of these policy instruments and policy outcomes as ‘orthodox’ will be confirmed by subsequent analysis of UK economic policy in the 1930s. However, greater exactitude in our understanding of ‘orthodox’ macroeconomic policy requires a challenge to established explanations of the role of the Gold Standard.

The literature on UK economic policy in the interwar period tends to describe the Gold Standard as a fixed exchange-rate system. Thus, the importance of the Gold Standard to 1920s economic policymaking often leads scholars to argue that the primary objective of UK macroeconomic policy was exchange-rate stability. For example, Winch (1969: 90) argues that ‘‘primacy was given to one aim of policy – stability of the exchanges – above all others’. Consequently, a typical criticism of economic policy in the 1920s was that whilst ‘Keynes concentrated on the problem of domestic stability,... the defenders of the Gold Standard policy were more interested in the stability of the exchange rate’ (Winch,1969:85). However, the literature allows us to challenge this traditional emphasis and construct an alternative explanation of the role of the Gold Standard in UK monetary policy. Here, the importance of the Gold Standard to exchange-rate stability is not ignored, rather, it is emphasised that within monetary policymaking, the Gold Standard gave the UK membership of an institution of global economic governance in order to secure international credibility and domestic anti-inflationary discipline (Rogers,2015:2-4). Consequently, whilst the Gold Standard evidently provided a global fixed exchange-rate system, it also performed an integral function as a system of domestic monetary management.

This assertion can be supported via the work of some scholars on the interwar period. For example, Dewey (1997:84) and Middleton (2010:240) note the twin objectives of the Gold Standard. First, the explicit objective of the Gold Standard was the fixed exchange-rate. Second, the implicit objective of the Gold Standard was to achieve internal price stability. Even Winch (1969:89), who explains the Gold Standard as a fixed exchange-rate system, highlights that the Treasury and Bank of England ‘considered the Gold Standard to be the only effective way of protecting internal stability and integrity of the currency’. Furthermore, Tomlinson (1990:14-

18,43) identifies that the attraction of the Gold Standard in Her Majesty's Treasury and Bank of England was three-fold. First, the Gold Standard allowed the City of London to be the premier centre of global finance. Second, the Gold Standard provided a defence against inflation[17]. Third, the Gold Standard was believed to act as an automatic mechanism of adjustment free from political interference. It was upon this mechanism that the anti-inflationary credentials of the Gold Standard rested as inflation was perceived to be the consequence of the role of politicians in domestic credit markets[18].

Consequently, the suggestion that the exchange-rate was the primary objective of macroeconomic policy in the early 1920s can be challenged, which allows us to provide greater specificity to our understanding of 'orthodox' macroeconomic policy. Indeed, it would be more accurate to suggest that internal price stability was the priority 'orthodox' objective of UK macroeconomic policy. This challenge to the accepted notion is evident from primary sources, which show that the fixed exchange-rate was considered the means by which the end of internal price stability would be secured. For example, Winston Churchill (1925), Chancellor of the Exchequer (1924-1929), in his Budget Statement to the House of Commons on the 28th April 1925, which announced the return of the UK to the Gold Standard, stressed that the Gold Standard provided anti-inflationary discipline and allowed a return to domestic price stability[19].

That the priority objective of macroeconomic policy was price stability is further accentuated when we consider the fear politicians and policymakers had of

[17] The defence against inflation provided by the Gold Standard has also been identified by Middleton (1996:217), Peden (1991:59-60) and Tomlinson (1990:43).

[18] Moggridge (1972:86) illustrates that both the Treasury and Bank of England thought that 'managed money', as advocated by Keynes among others, was a weak barrier to inflation and that the Gold Standard was 'knave-proof'. For instance, Ralph Hawtrey (1919:365), Director of Financial Enquiries within the Finance Division at the Treasury (1919-1945), wrote that the Gold Standard was 'a bulwark against inflationism, that insidious financial vice'.

[19] Churchill emphasised repeatedly in statements to the House of Commons that the Gold Standard provided anti-inflationary discipline and would secure price stability (1925,1925a;1925b;1929). Surprisingly, given the description of his work earlier in the chapter, Winch (1969:89) also provides the same analysis Winston Churchill's statement to the House of Commons on the 28th April 1925.

the inflationary potential of public expenditure and government borrowing in the 1920s[20]. Thus, Middleton (1985:86) posits that the fear of inflation 'influenc[ed] many of the policy decisions of the period, in particular, the return of the Gold Standard and the heroic attempts made to remain on gold in 1931'. Furthermore, Peden (1988:12) highlights that the Treasury thought itself responsible not only for controlling public expenditure in terms of broad aggregates but also from the perspective of controlling the value of money. Here, we can also provide greater exactitude in our understanding of 'orthodox' macroeconomic policy by discerning a hierarchy between 'orthodox' fiscal policy and the 'orthodox' objective of price stability. Specifically, reducing public expenditure in order to achieve the balanced budget was considered integral to the pursuit of price stability.

It is also possible to provide greater specificity in our understanding of the economic ideas associated with 'orthodoxy' in this period. As demonstrated at the opening of our chapter, the economic ideas classed as 'orthodox' are only considered in the broadest of fashion, designated as those of classical liberal political economy or neoclassical economic theory. Our understanding of economic ideas in 'orthodox' macroeconomic policy is influenced by Henderson (1986), which was introduced in Chapter Two and provided an account of how economic ideas were interpreted and constructed in UK economic policymaking from his first-hand experience of having worked as an economist at the Treasury. Henderson (Ibid) found that Whitehall generated its own information and economic ideas in the formulation of policy, which he termed do-it-yourself-economics, that were far removed from economic ideas as understood by economists. Consequently, subsequent analysis will seek to determine how economic ideas were interpreted and politically constructed by actors involved in interwar UK economic policymaking. Furthermore, analysis will document how these interpretations and have been used to formulate macroeconomic policy.

[20] The fear of the inflationary potential of public expenditure and government borrowing in interwar UK economic policymaking process has been highlighted by Howson (1975), Middleton (1985:6,37-38,85-88,91-92,175), Peden (1979:76,80-81), Tomlinson (1990: 61) and Winch (1969:89-90).

The literature suggests two specific impacts of economic ideas on the formulation of interwar economic policymaking. First, 'orthodox' interpretations of economic ideas provided actors with a 'world view'[21]. These world views allowed actors to select 'orthodox' policy objectives and policy instruments and determine the appropriate relationship between them. Second, 'orthodox' interpretations of economic ideas allowed actors to construct crisis and policy narrative that sought to provide an interpretation of economic events and emergencies and legitimise macroeconomic policy 'orthodoxy' as the solution.

The first economic idea that can be identified within the literature as particularly influential on the formulation of UK economic policymaking in the aftermath of the First World War was internationalism. For example, Skidelsky (1975:96-98) highlights two complementary 'orthodox' interpretations of the economic idea of internationalism in interwar economic policymaking. First, that the UK economy was a 'subordinate and integrated part of the system of world economy'. Second, that politicians and policymakers believed that economic prosperity was derived from the interaction and integration of the domestic and global economy. Similarly, Middleton (1996:216-217) posits that, during the nineteenth century, UK economic policy became determined by the growing interconnection of the domestic and global economy. Accordingly, Middleton (Ibid) notes that internationalism ensured the promotion of policy objectives such as a vibrant export sector, free-trade, an international role for Sterling and the City of London, stringent domestic financial policies to stabilise the exchange-rate, stringent domestic financial policies to stabilise prices and policies to ensure the free mobility for capital and labour.

Middleton (1987:111-112) also identifies that internationalism led politicians and policymakers to place considerable importance on the maintenance of confidence in the UK economy. Here, confidence would be maintained through policymaking and necessitated a return to 'orthodox' macroeconomic policy after the

[21] 'World view' ideas provide actors with an overarching understanding of how the world works. In turn, they allow actors to understand how political institutions and policy instruments should be organised in order to achieve policy objectives (Campbell,2002:22-23).

First World War[22]. For example, a predominant fear held by policymakers was that the adoption of large scale schemes of public-works, which threatened departure from fiscal 'orthodoxy' and price stability through an increase in government borrowing, risked a loss of confidence in financial markets and cause capital flight from the UK economy. Furthermore, internationalism played a critical role in the return to the Gold Standard. For instance, Moggridge (1972:Chp.3) illustrates how the Bank of England and the Treasury, when providing advice to the Chancellor Winston Churchill on the return to the Gold Standard, accentuated that a failure to return to the Gold Standard threatened confidence, inflation and the position of the City of London as the premier centre of global finance. Many scholars also note that the decision to return to the Gold Standard at the pre-war parity rate of $4.86 was in order to project confidence in the financial markets as the issue was a matter of prestige for the City of London[23].

The issue of confidence was also prevalent in the political defence of balanced budget 'orthodoxy', which was articulated in the infamous 1929 Treasury View. Peden (1984:169) states that 'any attempt to construct a logical argument about the Treasury View… is liable to founder on ambiguity[24]. However, the ambiguity of the Treasury View can be crystallized by stressing its key ideational aspect: crowding-out. In his defence of the Treasury View in his 1929 Budget Statement of the 15th April, Churchill (1929) emphasised two aspects of crowding-out. First, that 'the 'orthodox' treasury view… is that when the government borrows in the money market it becomes a new competitor with industry and engrosses to itself resources which would otherwise have been employed by private enterprise'

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[22] Hawtrey (1919:154-156) stressed that maintaining confidence in the UK economy was a paramount concern of policymaking because of the position of the City of London in global financial markets.

[23] The importance of the prestige of the City of London in the return to the Gold Standard has been identified by Brown (1929/1970:45), Pollard (1970), Pugh (1994:164) and Thomas (1994). Furthermore, the Treasury official, Ralph Hawtrey (1919a:434) argued that returning to the Gold Standard at any parity other than $4.86 would lead to a loss of confidence.

[24] For instance, Middleton (1982;1983) argues that administrative and political concerns regarding the feasibility of carrying out schemes of public-works was a prominent part of the Treasury View.

(Churchill,1929:c.53). Second, that ‘in the process it raises the rent of money to all who have need of it’ (Ibid:c.53).

Middleton (1985:92-95,161-163;1987:113-117) posits accordingly that two interpretations of crowding-out existed within the 1929 Treasury View: financial and psychological. Financial crowding-out refers to the belief that schemes of public works financed by government borrowing have little effect on long-term employment. This occurs because the sales of bonds to finance the deficit will increase market interest-rates, which by raising the cost of credit will depress private investment and consumption. Psychological crowding-out relates again to the issue of confidence. Here, fiscal deficits are claimed to lead to the loss of economic confidence of domestic and global economic actors. This results in higher interest-rates, which crowds out the private sector and consumers from the market. However, this did not mean that public works were not pursued; rather, they would only be implemented within certain parameters (Middleton,1985:155). For instance, Churchill (1929:c.53) argued that public works would be pursued by government in cases of national security or in instances of market failure. However, public-works projects must be remunerative in an accounting sense and not contribute to an increase in national debt (Middleton,1996:192;Peden,1980:5).

These two interpretations of the economic idea of crowding-out had a particular impact on the formulation of interwar macroeconomic policy through the relationship between price stability and policy instruments. Specifically, crowding-out allowed policymakers to identify that fiscal policy should play a supportive role to monetary policy. At this juncture, it is worth remembering the fear that policymakers held in this period regarding the inflationary potential of public expenditure and government borrowing. Thus, fiscal ‘orthodoxy’ had a monetary function in macroeconomic policymaking and supported monetary policy in the pursuit of the ‘orthodox’ objective of price stability. The supportive role played by monetary policy is further evidenced when we consider the ‘orthodox’ economic idea of crowding-out in the final section of the chapter. Furthermore, fiscal ‘orthodoxy’ ensured that the structure of market interest-rates and the cost of credit in the UK economy reflected not the level of government borrowing and associated loss of

confidence, but rather the operational decisions on the Bank Rate taken by the Bank of England. This argument is strengthened in the next section of the chapter in the discussion of the Bank of England's management of the Gold Standard.

Economic ideas were also crucial in how politicians and policymaking in the 1920s viewed the problem of unemployment. Here, Middleton (1985: 154) states that the Treasury, Bank of England and successive governments held a 'structural' analysis of unemployment, which posited that employment creation was the job not of macroeconomic policy but microeconomic policy (Howson & Winch,1977:162). As a result, the Treasury, Ministry of Labour and other government departments held the position that schemes of public works pursued on a substantial scale distorted 'normal' channels of economic activity and hinder industrial competitiveness by delaying what was considered a proper economic recovery through private-sector investment (Middleton,1985:Chp.8;Stewart,1967:75)[25]. Consequently, crowding-out was critical to the rejection of fiscal policy strategies based on the introduction of schemes of public-works to alleviate unemployment.

Furthermore, it is in the 'structural' analysis that interpretations of other economic ideas, such as economic liberalism and competitiveness, in the formulation of economic policy become clearer. For instance, Glynn and Booth (1996:94) noted the belief that unemployment was a product of market imperfections pervaded politics, Whitehall and City of London in the 1920s[26]. Accordingly, unemployment was attributed to institutions that hindered market exchange and price signals,

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[25] For example, Churchill (1929:c.55) stated in his 1929 Budget Statement that public-works 'for the purpose of curing unemployment the results have certainly been disappointing. They are, in fact, so meagre as to lend considerable colour to the orthodox Treasury doctrine which has steadfastly held that, whatever might be the political or social advantages, very little additional employment or no permanent additional employment can be in fact and as a general rule be created by state borrowing or state expenditure'. Meanwhile, a report by the Industrial Transference Board (1928:Chp.1) argued that deficit-financed public-works created 'artificial employment'.

[26] An example of this can be found in a series of newspaper articles written in 1930 by Winston Churchill (1930;1930a) and Sir Arthur Maitland (1930;1930a;1930b), who served as Minister for Labour (1924-1929).

notably the state and trade unions. Thus, activities undertaken by the state and trade unions, such as unemployment insurance and collective bargaining, were claimed to price persons out of employment by keeping wages higher than the demand for labour. Moreover, these institutions were blamed for causing inflexible labour markets and welfare dependency, which reduced the impetus to seek employment (Cannan,1930;1932; Clay,1929;Pigou,1913).

Youngson (1960:241-247) also notes the prevalence of the 'structural' analysis of unemployment and competitiveness in the evidence provided to the Macmillan Committee in 1930. The interpretation of competitiveness in 1920s economic policymaking related to the ability of UK firms to sell and export goods in world markets. Having rejected domestic based schemes of economic expansion and employment creation through public-works, microeconomic policy was deployed to improve the competitive position of UK industry. One prominent microeconomic policy implemented in the 1920s was rationalisation. For example, the 1929 Balfour report stated that UK industry needed to rationalise so as 'to restore the competitive power of British industry and trade.... and enable British exporters to place their produces in external markets' (Committee on Industry and Trade,1929:297)[27]. Rationalisation improved the competitive position of UK industry in export markets; it was claimed, through the elimination of excess industrial capacity and the reduction unit-costs of UK industry (Howson & Winch,1977:162).

Economic ideas were also important in the formulation of policy, however, because they also provided actors with the tools required to construct a narrative of economic events and emergencies, particularly the growing unemployment problem of the 1920s. Consequently, unemployment was claimed to be the result of turbulence in the world economy, which had led to a dislocation and reduction in world trade exacerbated by a loss of competitiveness in UK industry and exports (Geddes,1919;Glynn,1987:169;Winch,1969)[28]. This internationalist and

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[27] Middleton (1996:358) highlights that the Balfour report was primarily interested in the restoration of United Kingdom industries non-price competitiveness in global markets.

[28] Auckland Geddes served as President of the Board of Trade (1919-1920).

competitiveness narrative was used to legitimise the implementation of macroeconomic policy 'orthodoxy' and the restoration of the pre-1914 economic world as the policy solution to unemployment, which was evident in the arguments made by politicians and policymakers in favour of the return to the Gold Standard. Thus, Moggridge (1969:48;1972:Chp.3) and Winch (1969:84) note that the Treasury and Bank of England believed that the Gold Standard and the fixed exchange-rate system would rebuild the shattered global economy, restore London to the centre of global finance and create the condition necessary for a revival of trade, exports and employment. The positive relationship between the Gold Standard and the revival of trade was articulated in several House of Commons Statements made by the Chancellor Winston Churchill (1925;1925a;1929)[29].

Change and Continuity in UK Economic Policymaking in the 1930s

In the context of a literature that stresses the existence of an economic policy 'orthodoxy' in the 1920s, it could be forgiven to assume that literature on UK economic policymaking in the 1930s would emphasise the continuity of economic policy in the interwar period. On the contrary, the 1930s is portrayed as a decade of radical change in macroeconomic policy as it departed from the established 'orthodoxy'. For example, Beer (1965:279) contends that it was in the 1930s that 'government decisions... endowed Britain with a pattern of economic policy that was comprehensive and radically different from that of previous generations'. Meanwhile, other scholars describe the characteristics of 1930s economic policy as a mixture of 'orthodoxy' and innovation (Glynn and Booth,1996:121; Gourevitch,1984:118-121;Peden,1991:88). Finally, Ingham (1984:244,Chp.8,App.C)

[29] For example, in his 1925 Budget Statement, which announced the return to the Gold Standard, Churchill (1925:cc.58-59) stated that "I believe that the establishment of this great area of common arrangement will facilitate the revival of international trade and of inter-Imperial trade".

stands alone in arguing that 1930s economic policy was based on 'persistent orthodoxy'.

Radical change in 1930s economic policy is ascribed to both monetary and commercial policy. Here, three economic policies implemented in the early 1930s are commonly presented as evidence of radical change from 'orthodox' economic policy. The first of these was the monetary policy of 'cheap money', which was implemented in the spring of 1932 when the Bank Rate was reduced to 2% (Glynn,1987:170;Howson, 1975:90-95). The second example of economic policy change is said to have occurred with the introduction of the Exchange Equalisation Act (EEA) at the 19th April 1932 Budget, which introduced a managed exchange-rate as opposed to the fixed exchange-rate system of the Gold Standard (Middleton,1985:174)[30]. The final claim to economic policy change in the 1930s was the replacement of free-trade with the imposition of a general tariff on 4th February 1932 (Beer,1965:279)[31].

Cumulatively, these changes in economic policy are presented in the literature as heralding the demise of the 'orthodoxy' of the Gold Standard and free-trade[32]. For instance, it is claimed that 'purely domestic considerations appear to have taken precedence over international concerns in 1930s economic policymaking' (Glynn & Booth,1996:135). This led to the implementation of new economic policies, which challenged free-trade and open capital markets and included the implementation of capital controls on the City of London (Tomlinson,1990:131) and interventionism in microeconomic policy (Booth,1978;1987). Several scholars also suggest there was change in economic policy objectives during the 1930s. For

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[30] The EEA was established in April 1932. Under the EEA, the Treasury provided the Bank of England with a fund of £175million to counteract, through purchases and sale of Sterling and foreign currency, temporary divergences from a stable exchange-rate.

[31] The 1932 Import Duties Act introduced a general tariff of 10%, with the exception of some foodstuffs and raw materials, and the creation of the Import Duties Advisory Committee. This committee also introduced a sliding tariff rate of 15%-33% depending on the import.

[32] This argument can be seen in the work of Aldcroft (1970:335-336), Dimsdale (1981: 336), Eichengreen (1981:1), Pollard (1992:92-94), Pugh (1994:172-174), Solomou (1996: 112) and Thomas (1994:358).

example, Middleton (1996:218) suggests that the policy of 'cheap money' introduced a new macroeconomic stabilisation objective to UK economic policy. Similarily, Howson (1975:89,Chp.4,Chp.5) posits that 'cheap money' and the EEA were policies implemented in order to secure the objective of economic recovery.

Absent so far from our discussion has been an examination of the explanation in the literature as to why economic policy changed during the 1930s. Here, Glynn (1987: 170) observes that the 'policy departures' of this decade are explained as 'the products of economic crises'. For instance, Tomlinson (1981:116) argues that it was the Global Financial Crisis of the summer of 1931 that forced UK to leave the Gold Standard, which 'affected a fundamental severance in economic policy. Domestic policies could be pursued, the economy could be managed'. This explanation of when and why economic policy changed in this period is evident in the work of many scholars on UK interwar economic policymaking[33]. Thus, the when and why of economic policy change is explained via the model of punctuated equilibrium. Consequently, economic policy change in the 1930s is depicted as a discontinuous process and the consequence of the exogenous shock of economic crises that lead to the UK leaving the Gold Standard, which punctuated the previous 'orthodox' policy equilibrium and led to radical change in economic policy.

The remainder of this chapter will expose the flaws in this explanation of when and why economic policy changed in the aftermath of the economic crises of 1929-31. Indeed, this section of the chapter will demonstrate that macroeconomic policymaking during the 1930s was marked by continuity of 'orthodox' policy and ideas. Consequently, a gap emerges in our current understanding of UK economic policymaking. Specifically, of the need for a superior understanding of when and why UK macroeconomic policy and ideas exhibit change and continuity. Here, the chapter will show that macroeconomic policy returned to 'orthodoxy' via the series of distinct phases in policymaking identified earlier in the chapter.

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[33] For example, it is evident in the work of Baines (1994:194-195), Beer (1965:279), Eichengreen and Temin (2000), Glynn & Booth (1996:121-22), Middleton (2010:422-423; 2011:10), Peden (1988:34), Solomou (1996:48-49) and Thomas (1994:350-351).

UK Economic Policymaking in Response to the Economic Crises of 1929-1931

The economic events and emergencies of 1929-1931 saw UK economic policymaking descend into another phase of crisis. The point of origin for this phase of crisis emanated from the Wall Street Crash of October 1929, which marked the end of a global economic boom and culminated in a Great Depression in the global economy. The economic impact of the Great Depression on the UK economy included a sharp contraction of 5.4% GDP (Middleton,2010:416), collapse in exports[34], deterioration in the balance of payments[35] and a significant increase in unemployment[36].

The summer of 1931 also saw the onset of a global liquidity crisis in financial markets, which had its origins in the Austrian and German banking systems. The collapse of Austrian and German banks caused panic in the global financial markets as global investors recalled their overseas capital to their domestic markets. This particularly impacted upon the UK economy due to the position of the City of London as a global hub of finance. By July 1931, gold was flowing out of the UK economy at a rate of £12-15million per week and the gold reserve had reduced to just £133million (Stewart,1967:70). Furthermore, the City of London feared that the fiscal deficit, which had risen since 1929, threatened the international position of the Sterling as a global reserve currency. Consequently, a crisis narrative emerged that

[34] UK export volumes fell from £729million in 1929 to £365million in1932 (Sayers, 1967:55).

[35] The current balance fell from a £124million surplus in 1928 to a deficit of £100million by 1931 (Tomlinson,1990:74).

[36] Unemployment in the insured workforce stood at approximately 3million (22%) between autumn 1931 and spring 1933. Also, unemployment in the uninsured and unregistered workforce is estimated to have risen to 750,000 by late 1932. Furthermore, as in the 1920s, unemployment was a regional phenomenon clustered around the export industries in northern England, Wales and Scotland (Miller,1976:455). The 1930s also saw the increasing incidence of long-term unemployment, which caused poverty and deterioration of physical and psychological health for those unemployed (Pilgrim Trust, 1938:5–25).

economic events was a crisis of government borrowing, which was a sign of the lack of probity of the incumbent Labour government. This narrative was also treated, on the part of the United States Federal Reserve and the Bank of France, as a reason to decline financial aid to the Bank of England that was necessary to keep UK on the Gold Standard. Consequently, with the Bank of England's financial resources exhausted, the 21st September 1931 saw the UK leave the Gold Standard (Tomlinson,1990:74,80).

The Labour government (1929-1931) of Ramsey McDonald, Prime Minister (1929-1935), and Phillip Snowden, Chancellor of the Exchequer (1929-1931) was elected on the 5th June 1929. Their election coincided with the onset of the crisis phase for UK economic policymaking, which the Labour government did not survive. The socialist rhetoric of the Labour Party in this period, combined with a significant economic crisis, should have created the possibility for radical economic policy change. However, the reality of macroeconomic policymaking after 1930 is that it followed a similar pattern discerned in UK macroeconomic policymaking after the First World War. The response of macroeconomic policy did differ slightly than in the 1920s, rather than enter a phase of temporary deviation in response to a crisis; macroeconomic policymaking immediately entered a phase of consolidation. As in the 1920s, however, this consolidation phase consisted of the deployment of 'orthodox' policy instruments in order to create the economic conditions necessary to return to the 'orthodox' fiscal policy outcome of the balanced budget and the 'orthodox' objective of price stability.

The consolidation phase is not immediately apparent in fiscal policymaking. For example, the series of events and emergencies in the global and domestic economy after 1929 caused the fiscal deficit to increase substantially. However, when we consider the constant employment balance, which cyclically-adjusts the UK public finances to remove increases in public expenditure caused by higher employment, we can begin to derive the true stance of fiscal policy under the Labour government. Indeed, as Table Two demonstrates from 1930-31 onwards the Labour government was securing ever higher fiscal surpluses through public expenditure reductions and increases in direct taxation as the Labour government strived to

balance the budget (Middleton,1981;2011:12; Tomlinson,1990:77)[37]. Here, we can provide greater exactitude to our understanding of 'orthodox' macroeconomic policy and add increases in taxation to our list of 'orthodox' fiscal policy instruments.

Table Two: Economic Performance of Fiscal Policy, 1929-1932

Years	**Budgetary Stance** (£millions) *(- = deficit / + = surplus)*	**Budgetary Stance** (% GDP) *(- = deficit / + = surplus)*	**Constant Employment Budget** (£millions) *(- = deficit / + = surplus)*	**Constant Employment Budget** (% GDP) *(- = deficit / + = surplus)*
1929/30	+ 17.4	+ 0.4	+ 17.4	+ 0.4
1930/31	- 24.2	- 0.6	+ 47.1	+ 1.1
1931/32	- 45.7	- 1.2	+ 106.7	+ 2.5
1932/33	- 50.2	-1.3	+ 124.5	+ 3.0

(Source: Tomlinson,1990:78)

The continued agitation surrounding the burden of public expenditure and fiscal deficit reached its peak during the 1931 Global Financial Crisis. At this juncture, another similarity between the consolidation phase in the 1920s and 1930s becomes apparent, particularly, the creation of a new temporary institution in fiscal policymaking to assist the return to fiscal policy 'orthodoxy'. This occurred with the

[37] Tomlinson (1990:66-67) also highlights the profound juxtaposition of the Labour party in this period between its socialist ideology and rhetoric and the economic conservatism of MacDonald and Snowden. Under their leadership, the Labour Party adopted economic 'orthodoxy as a deliberate electoral strategy to illustrate fitness to govern.

establishment of the May Committee in the summer of 1931, whose report was described by Winch (1969:119) as a 'symbol of 'orthodox' finance', which called for public expenditure cuts of £97million including cuts to unemployment benefit of 20% (Committee on National Expenditure,1931;Tomlinson,1990:77). The recommendations of the May Committee led to a political crisis inside the Labour Party as nine cabinet members threatened to resign if the cuts to unemployment benefit were implemented. This culminated in a split within the Labour party and the formation of a National government comprising of Labour, Conservative and Liberal Members of Parliament on the 24th August 1931.

In terms of fiscal policy performance, Table Three demonstrates that the National government (1931-1939) continued the consolidation phase in fiscal policymaking and secured the return of fiscal policy 'orthodoxy' when the budget returned surplus in 1933-1934[38]. Thus, Middleton (1985:114) describes Neville Chamberlain, Chancellor of the Exchequer (1931-1937), as a man 'wedded' to fiscal 'orthodoxy'. Furthermore, Middleton (1981:282) contends that the National Government's September 1931 Budget, which implemented public expenditure cuts and increased taxation amounting to £76million, was the most deflationary budget of the entire interwar period. Indeed, Middleton (1981;2010:415) found that budgets through the interwar period had a deflationary bias, with policymakers being prepared to override the automatic stabilisers in order to achieve a balanced budget until 1937.

[38] That the public finances returned to balance in 1993-1934 has also been noted by Alford (1972), (Broadberry (1986:155), Eichengreen (1981:311), Miller (1976:460-465) and Tomlinson (1990:112-113).

Table Three: Economic Performance of Fiscal Policy, 1932-1936

Years	**Budgetary Stance** (£millions) *(- = deficit / + = surplus)*	**Constant Employment Budget** (£millions) *(- = deficit / + = surplus)*
1933/34	+ 33.3	+ 141.2
1934/35	+ 25.8	+ 112.2
1935/36	+ 16	+ 69.8
1936/37	+ 14.7	+ 22.7

(**Source:**Aldcroft,1970:304-305;Broadberry,1986:151)**.**

In order to demonstrate the continuity of 'orthodox' monetary policy during the 1930s, however, it is necessary to make a further challenge to our understanding of the role of the Gold Standard in UK macroeconomic policymaking. Initially, it is important to highlight that Tomlinson (1990:15,18) notes the classical Gold Standard (1860-1914) operated to the benefit of the UK economy because of the City of London's dominance in global financial markets. Specifically, the role played by the City in global short-term money markets meant that the Gold Standard operated not as an autonomous mechanism of adjustment as claimed by policymakers, but rather had been a monetary system that had been actively managed by the Bank of England.

The Bank of England managed the Gold Standard in the nineteenth century (1870-1914) and interwar (1925-1931) periods through the implementation of two monetary policy instruments, which strengthens our understanding of 'orthodox' macroeconomic policy. These 'orthodox' monetary policy instruments were the

Bank Rate and OMOs, which gave the Bank of England a direct influence on the structure of short-term market interest-rates within the banking system and credit conditions in the UK economy[39]. The Bank of England managed the Gold Standard through these policy instruments in the following manner[40]. If the economy was suffering an undesired outflow of gold, which the Bank of England wished to halt, the Bank increased the Bank Rate and restricted the volume of OMOs it conducted with the banking system. This reduced liquidity in the banking system and increased the level of short-term market interest-rates. With a higher level of interest on offer, the UK financial system as a depository for gold and capital was more attractive, this would usually be enough for the Bank of England to stem an undesired outflow of gold. If the economy was receiving an undesired inflow of gold, the Bank of England would operate the Bank Rate and OMOs in the opposite direction, which would lower the rate of interest on offer and reduce the attractiveness of the UK financial system.

Now that it has been established that the Gold Standard was a managed monetary system through the monetary policy instruments of the Bank Rate and OMOs, we can turn to our final challenge to our understanding of the Gold Standard. The Gold Standard provided the UK with membership of an institution of global economic governance, which exerted anti-inflationary discipline on the domestic economy. This argument is strengthened when we consider the importance of the quantity theory of money to the operation of the Gold Standard, which allowed the Bank of England to use 'orthodox' monetary policy instruments of the Bank Rate

[39] The Bank Rate is the official interest rate set by the Bank of England. In the interwar period, the Bank Rate sets the price at which the Bank of England supplied banknotes to the domestic banking system, which it provided through OMOs. This allowed the Bank Rate influenced the level and structure of market interest-rates in the domestic banking system (Bank of England,2016). This relationship between the Bank Rate, OMOs and market interest-rates is discussed in all forthcoming chapters, barring Chapter Five.

[40] The role of the Bank Rate and OMOs in the management of the Gold Standard has also identified by Ford (1981), Howson (1975:36), Ingham (1984:132-133), McCloskey (1981), Middleton (1996:217), Moggridge (1972:9-10,13,147-153,169-176), Peden (1991:64), Sayers (1957) and Whale (1937).

and OMOs to determine prices in the UK economy[41]. However, this also allows us to highlight a further role the Gold Standard played in monetary policymaking. Namely, the Gold Standard acted as a monetary framework, which allowed monetary policymakers to understand prevailing monetary conditions and guide the implementation of the 'orthodox' monetary policy instruments of the Bank Rate and OMOs in pursuit of the 'orthodox' macroeconomic policy objective of price stability.

This new understanding of the Gold Standard as a monetary framework allows us to question the claims made by scholars that 'cheap money' was an example of change from monetary policy 'orthodoxy'. For example, the purpose of 'cheap money' was to achieve precisely what it describes, it was an attempt by policymakers to make the price of money cheaper by reducing the cost of credit. However, the monetary policy instruments used to reduce the cost of credit in the UK banking system were the same 'orthodox' monetary policy instruments of the Bank Rate and OMOs, which the Bank of England had used to manage the Gold Standard (Richardson,1967:182-183). Thus, the Bank Rate was reduced to 2% in order to alter the level and structure of short-term market interest-rates. Consequently, Middleton (1996:358) states that 'in terms of money supply control and interest rates, the [interwar] period saw few new instruments of control save some technical devices such as sales of government debt to the public departments when there was insufficient take-up by the non-banking sector'.

[41] David Hume's (1748/1832) quantity theory of money argues that the price level is determined by the quantity of money in circulation. Increases in the quantity of money leads to higher prices. Decreases in the quantity of money causes lower prices. Meanwhile, Hume's (1752/1963:Part 2) price specie flow mechanism considers the effects of international transactions in a Gold Standard. Here, gold would flow into an economy which had a balance of payments surplus as deficit countries paid for imports. This would cause the money supply to increase and prices to rise. Concurrently, the gold outflow from deficit countries would cause prices to decrease as the money supply contracted. These alterations in price level would lead to an adjustment of competitiveness in global trade and ensure a return to balance-of-payments equilibrium. It was through this link between the Gold and the money supply that the Bank of England could manage the Gold Standard through the orthodox monetary policy instruments of the Bank Rate and OMOs.

Furthermore, the novelty of ‘cheap money’ as a response to economic downturn can also be challenged. For example, Stewart (1967:63) labelled the implementation of ‘cheap money’ in response to an economic downturn as an ‘‘orthodox’ and time-honoured step’ in UK monetary policy. Similarly, Middleton (1996:355) claims that ‘cheap money’ had historical antecedents in UK monetary policymaking and was thus ‘a traditional response to depression pursued with perhaps a new vigour’. For example, scholars identify that the Bank of England reduced Bank Rate in response to economic downturn in 1894-1895 (Peden,1984:172) and 1908 (Middleton,1996:218)[42].

Howson (1975:66) also identifies that the immediate Bank of England response to the 1929 Wall Street Crash was to implement a policy of ‘cheap money’. For example, from October 1929 to May 1931 the Bank of England reduced the Bank Rate from 6% to 2.5%. On this monetary policy response, Sayers (1956:147) comments that the Bank of England implemented ‘cheap money’ policy ‘partly as the classical reaction to the relaxation of the strain upon the supply of money, and partly as a deliberate effort to reverse the world-wide slump’. The phase of ‘cheap money’ was interrupted by the Global Financial Crisis of the summer of 1931 when the Bank of England increased the Bank of Rate to 4% in an attempt to halt the flood of gold and capital from the City of London.

Our new understanding of the development of monetary policy after the UK left the Gold Standard also allows us to challenge claims that the introduction of the EEA 1932 was an example of radical policy change from monetary policy ‘orthodoxy’. For example, intervention in foreign exchange markets through the purchase and sale of Sterling and foreign currency is an OMO, which was confirmed by a recent study by the Bank of International Settlements that found that exchange-rate intervention was the most common type of OMOs (Borio and Disytat,2009).

[42] The Bank of England lowered the Bank Rate in successive stages from 5% in August 1893 to 2% in February 1894. The Bank Rate was then held at 2% for two years and seven months until a 0.5% increase in September 1896. The Bank of England did the same in 1908-1909 when it lowered the Bank Rate in successive stages from 7% in November 1907 to 2.5% in May 1908. The Bank Rate was then held between a range of 2.5% to 3% between May 1908 and October 1909 (Bank of England,2016a).

Thus, the EEA created a new permanent institution within macroeconomic policymaking located in the Bank of England, but financed by the Treasury, which underpinned in statutory legislation intervention in foreign exchange markets through the ‘orthodox’ monetary policy instruments of OMOs.

This was not the first time that the Bank of England had managed the exchange-rate. We have already noted that the Gold Standard was a managed monetary system rather than an autonomous mechanism of adjustment. However, Moggridge (1972:176-196) highlights that the Bank of England also managed the exchange policy during the First World War and in the years before the return to the Gold Standard. For instance, Burk (1979:240) posits that the Treasury had gone to dramatic lengths during the First World War to manage the Sterling exchange-rate, which had been pegged at an exchange-rate parity of $4.76 and required committing between $25-40million per week in US foreign exchange markets. Finally, in a speech given by the Governor of the Bank of England (1973-1983), Gordon Richardson (1977) claimed that the genesis of the EEA lay in a 17th century agreement, pre-dating the Act of Union and Gold Standard, between London and Edinburgh to prevent fluctuations in exchange-rates. Consequently, rather than an example of policy change, the EEA is a further example of the rich historical pedigree that OMOs as an ‘orthodox’ monetary policy instrument.

There is also no reason to suggest that the objective of macroeconomic policy changed as a consequence of the economic crises of 1929-1931[43]. Indeed, the ‘orthodox’ objective of macroeconomic policy continued to be price stability as it was during the 1920s. This observation is evident from the evidence provided by the Treasury official Ralph Hawtrey to the 1930 Macmillan committee. Here, Hawtrey (Committee on Finance & Trade,273-295;Peden 1984:164-168) argued that the primary objective of macroeconomic policy must be to maintain price stability. This meant that monetary policy should ensure, through the Bank Rate and OMOs, the relaxation of credit, increasing the supply of money, when prices fell, and the

[43] The Treasury official, Ralph Hawtrey (Committee on Finance & Trade:para.51), stated in his evidence to the 1930 Macmillan committee that the ‘only innovation called for [in use of the Bank Rate to mitigate economic downturns] is that appropriate action should be taken earlier than in the pre-war days’.

restriction of credit, decreasing the supply of money, when prices rise. Similarly, the Treasury official Frederick Phillips is recorded as stating that when the price level threatened inflation, the bank rate should be increased so that the money supply contracts (Howson and Winch,1977:143)[44].

The argument that the priority macroeconomic policy objective continued to be price stability in the 1930s is strengthened when we examine in more detail the Treasury policy of 'rising prices'. Here, in the absence of a downward adjustment of the cost of labour, the Treasury hoped to increase the profit margins of industry through an increase in prices. However, several scholars (Booth,1987:509-510; Glynn,1987:183; Tomlinson,1990:116-117) note that the policy was carefully controlled due to 'orthodox' concerns regarding the potential for inflation. Furthermore, the fear of inflation was still a primary determinate in Her Majesty's Treasury fiscal policy decisions in the 1930s[45]. Indeed, Booth (1987), Howson (1975:86,90) and Peden (1991:88) contended that the Treasury policy of 'rising prices' was intended only to return the price level to its pre-depression level.

'Cheap money' and ''rising prices'' allowed policymakers therefore to combat the deflationary economic conditions that had occurred as a result of the 1929-1931 crises and create the economic conditions necessary to return to the orthodox objective of price stability. Minford (2006:83-84) argues, for example, that deflationary conditions in the early 1930s meant expansionary monetary policy could be implemented without threatening price stability. Furthermore, Howson and Winch (1977:162) argue that the policies of 'cheap money' and 'rising prices' pursued during deflationary economic conditions suggest that Treasury officials were monetarist. Consequently, 'orthodox' macroeconomic policy is not synonymous with deflation. Indeed, the historical prevalence of 'cheap money', perhaps pursued with extra vigour during the 1930s, demonstrates that the Treasury and the Bank of

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[44] Frederick Phillips held several posts within the Treasury during the interwar years including Principal Assistant Secretary (1927–1931), Deputy Controller (1931) and Under Secretary (1932–1939).

[45] This has been highlighted by Booth (1987:509), Middleton (1985:119-120,162,175), Peden (1979:75-76,79-81) and Thomas (1983:553).

England were quite prepared to provide reflationary finance provided that the source of that finance came from monetary policy rather than fiscal policy.

That the objective of macroeconomic policy continued to be price stability is also evident from primary sources in 1930s economic policymaking. For instance, Neville Chamberlain (1931a) stated in the House of Commons on the 10th December 1931 that 'the [National] government will pursue its policy of maintaining as steadily as possible the internal purchasing power of the pound'. Furthermore, when explaining the National government's economic strategy to the House of Commons in 1931 and 1933, Chamberlain (1931;1931a;1933) declared that it intended to achieve price stability, balanced budgets and the revival of trade. As Table Four demonstrates, Chamberlain, Treasury and the Bank of England were remarkably successful in using 'cheap money' and 'rising prices' to counteract deflationary economic conditions and achieve the 'orthodox' macroeconomic policy objective of price stability.

Table Four: Economic Performance of Monetary Policy, 1931-1936

Year	**Inflation Rate** (Average Percentage Change)
1931	-4.3%
1932	-2.6%
1933	-2.1%
1934	0.0%
1935	0.7%
1936	0.7%

(**Source:**Twigger,1999:13).

Consequently, whilst the abandonment of the Gold Standard may have led to an operational change in the formulation of monetary policy via the adoption of 'cheap money' this change served to restore monetary policy 'orthodoxy', rather, than implement radical policy change. Thus, 'cheap money' ensured monetary policy entered a period of consolidation back towards 'orthodoxy' during which 'orthodox' monetary policy instruments of the Bank Rate and OMOs were implemented to secure 'rising prices' and return economic performance to the 'orthodox' objective of price stability. The 'orthodox' objective of price stability was achieved in 1934, which, alongside the return of the balanced budget, ensured the return of UK macroeconomic policy to 'orthodoxy'. In the aftermath of the crises of 1929-31, macroeconomic policy objectives, instruments and outcomes the continuity of 'orthodoxy' after the 1929-1931 economic crisis is more evident than examples of macroeconomic policy change.

The remaining task of this chapter is to delineate how 'orthodox' interpretations of economic ideas, such as those identified in 1920s economic policymaking, continued to provide UK politicians and policymakers with world views that influenced the formulation of policy in the 1930s. Indeed, when we include these 'orthodox' interpretations of economic ideas in our understanding of interwar UK macroeconomic policy 'orthodoxy', we further strengthen our argument that macroeconomic policy 'orthodoxy' endured the economic and financial crises of 1929-1931. For example, the 'orthodox' interpretation of internationalism continued to maintain that economic prosperity was the product of the subordinate and integrated position of the UK economy within the world economy. This was evident from the persistent prominence placed on the issue of confidence in the formulation of policy (Peden,1984:177-178; 1991:98-99). For example, Howson (1975:92) contends that the maintenance of confidence and fear of inflation was still a central determinate within the Treasury in favour of the 'orthodox' fiscal policy outcome of the balanced budget.

The 'orthodox' interpretation of internationalism was evident in a range of public comments made in the 1930s by Treasury officials, the Chancellor of the Exchequer and the National Government. For example, Chamberlain (1932:c.262)

claimed in a House of Commons Statement on the 8th November 1932 that "all the things… [the National government]… have been doing during the past 12 months has been directed to putting the country back into a position when confidence might be restored and when trade could again revive". Furthermore, internationalism continued to be used by policymakers to select fiscal policy 'orthodoxy' as the means to secure confidence in financial markets. This was confirmed in a National government (1935:36) cabinet paper produced in 1935, which stated that 'confidence in the future remains firm and well founded. To maintain that confidence by the pursuance of a steady policy of sound finance.... is the most essential task of government'. Meanwhile, Richard Hopkins, a senior official at the Treasury, observed that the role of Sterling in world markets limited the Treasury's choices in fiscal policymaking lest it cause a loss of confidence and flight from Sterling (Hopkins cited in Peden, 1984:179) [46]. Similarly, Frederick Phillips, also an official within the Treasury, stated that 'to create any impression [abroad] that this country was committed to inflation would be dangerous as the stability of Sterling and its use as a great medium of international exchange depend very largely on the general conviction that this country does not intend to resort to inflationary measures' (Phillips cited in Howson,1975:92).

'Orthodox' interpretations of crowding-out are less easily discernible in 1930s UK economic policymaking, which was probably a reaction to the political battle that surrounded the articulation of the 1929 Treasury View. However, evidence of continued adherence to the 'orthodox' interpretations of crowding-out is available. For example, the relationship between fiscal 'orthodoxy' and 'cheap money' could be presented as evidence of the adherence to psychological crowding-out in the formulation of macroeconomic policy. For example, Middleton (1985:114) notes that the adoption of 'cheap money' reinforced the commitment to 'orthodox budgetary policy' in fiscal policymaking. Similarly, Glynn (1987:167) and Peden (1988:35) argue that Chamberlain and the Treasury secured a balanced budget in the public finances precisely because fiscal 'orthodoxy' maintained the confidence of finance

[46] Sir Richard Hopkins served in a number of positions within the Treasury including Controller of finance and supply services (1927-1932); Second Secretary (1932-1942); and Permanent Secretary (1942-1945).

and business interests, which allowed the Bank Rate to remain low and money cheap. Consequently, schemes of public-works as the route to economic recovery were rejected because they threatened 'cheap money' through a loss of economic confidence, which would lead to higher interest-rates (Tomlinson,1990:112,114-115)[47] meaning fiscal policy continued to play a supportive role to monetary policy in pursuit of the 'orthodox' objective of price stability.

As a result, Middleton (1985:165) highlights that both the Labour (1929-1931) and National government (1931-1940) continued to believe that employment creation from public-works were poor, that public-works should be funded out of current revenue, rather, than deficit-financed and if public-works were to be financed by government borrowing the scheme should be remunerative in an accounting sense (future revenue stream from the public-work should cover the increase in government borrowing to finance its creation)[48]. Thus, successive interwar scholars have indicated that the Treasury had not adopted Keynesian fiscal policy positions prior to the Second World War[49]. Indeed, as late as April 1939, the Treasury official Frederick Phillips wrote that 'that the real stimulus comes from reflationary finance

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[47] Keynes (1933/1972;1936/2007;1937/1982) built upon his work of the 1920s to provide an ideational challenge to neoclassical economics and policy challenge to fiscal 'orthodoxy'. This challenge reached its epitome in Keynes' *General Theory of Money, Interest and Employment* in 1936. In this book, Keynes provided a theoretical justification for his belief that governments should implement interventionist policies to overcome a recession and alleviate unemployment. Consequently, Keynes' *General Theory* formally challenged the belief of neoclassical economists that free-markets provided for full employment equilibrium. In contrast to neoclassicism, The *General Theory* argued that it was demand, not supply, that governed economic activity. During an economic downturn, Keynes argued, it was necessary for governments to stimulate aggregate demand through counter-cyclical fiscal policy consisting of deficit-financed public expenditure on public-works, otherwise, an economy risked becoming trapped in low employment equilibrium as economic activity grinds to a halt due to the lack of investment and consumption.

[48] This was articulated in House of Commons Statements Phillip Snowden (1930;1931;1931a) and Neville Chamberlain (1937;1937a) when they were Chancellor of the Exchequer.

[49] The continued rejection of Keynesian policy position on public-works by the Treasury, prior to the Second World War, has been identified by Booth (1983), Middleton (1985:170-173;1987:121), Peden (1980;1983;1987:105-108;1988:38), Skidelsky (1975), Weir and Skocpol (1985:109) and Youngson (1960:252).

[provided by ‘cheap money’]. If there was no reflationary finance, the government works tend merely to replace private works without much effect on unemployment. But this is the famous or infamous Treasury view, still a most bitter subject of controversy which it would be great mistake to raise’ (Phillips cited in Peden, 1980:6).

‘Orthodox’ interpretations of economic liberalism and competitiveness were also evident in the formulation of ‘cheap money’ and rejection of public-works. For example, both Howson (1975:91) and Peden (1991:88) indicate that ‘cheap money’ was adopted because it was believed to encourage economic recovery to emerge from natural sources of private investment, rather than government expenditure on public works, which would misallocate economic resources and lead to a loss of confidence. Thus, Peden (1991:89) highlights that Whitehall departments in the 1930s still believed ‘that private investment in industry was superior to public works from the points of view of wealth creation and international competitiveness’.

Furthermore, these economic ideas allowed politicians and policymakers to develop a narrative of the economic problem of unemployment during the 1930s, which legitimised ‘orthodox’ macroeconomic policy as the solution and was similar to that evident in UK politics and economic policymaking in the 1920s. Thus, unemployment was portrayed as the result of dislocation of global trade and a loss of competitiveness in the industrial base. For example, Chamberlain (1932:c.259) told the House of Commons on the 8th November 1932 that “only full, complete and satisfactory solution of this problem of unemployment is to provide an increase of the ordinary operations of trade” and that “the increase in unemployment is not due so much to the falling off in public works as it is to the loss of our export trade” (Chamberlain,1933:c. 388). Similarly, the National government (1935:7) claimed in an internal Cabinet Paper that it had inherited three tasks to promote economic recovery; to restore shattered confidence, to develop home markets whilst world markets were closed and to prepare the nation for the eventual revival of international trade. Consequently, Booth (1987:503) suggests the Treasury’s policy reaction to the crisis of 1929-1931 was to implement fiscal ‘orthodoxy’ and promote

supply-side policies to increase 'the competitive power of British industry and... profitability'.

Conclusion

This chapter has reviewed the literature on UK economic policymaking and economic performance during the interwar years between November 1918 and December 1934. The chapter has highlighted two gaps in our current knowledge of UK economic policymaking. First, that greater specificity is required in our understanding and definition of 'orthodox' macroeconomic policy. Second, that there is a need for a superior understanding of when and why UK macroeconomic policy and ideas exhibit change and continuity. Moreover, the chapter has exposed the flaws of existing explanations for policy change in the 1930s rooted in the notion of punctuated equilibrium.

Meanwhile, the historiography in this chapter has also generated two research findings, which fill the gaps in our existing comprehension of UK economic policymaking and provide an original contribution to our knowledge. The first is through the provision of greater clarity in our understanding and definition of 'orthodox' macroeconomic policy. The 'orthodox' objective of macroeconomic policy is price stability. The 'orthodox' monetary policy instruments are those of the Bank Rate and Open Market Operations (OMOs), which are implemented to alter credit conditions in the UK economy through the management of short-term interest-rates. The 'orthodox' fiscal policy instruments are those of public expenditure reductions and/or tax increases, which are implemented to achieve the 'orthodox' fiscal policy outcome of a balanced or surplus budget and national debt reduction. Finally, an 'orthodox' hierarchy between policy instruments existed in macroeconomic policy, which sees fiscal policy play a supportive role to monetary policy in the pursuit of the 'orthodox' objective of price stability.

The chapter has also provided greater precision to our understanding of 'orthodox' economic ideas and their role in the formulation of policy. For example, the world views of actors involved in interwar macroeconomic policymaking were dominated by 'orthodox' interpretations of the economic ideas of internationalism, crowding-out, competitiveness and economic liberalism. These world views meant economic ideas are used to formulate macroeconomic policy. First, they were invoked by actors to justify the selection of 'orthodox' macroeconomic policy over alternative policy options. Second, they allowed actors to develop policy narratives, which interpreted economic events in such a way that legitimised the return to macroeconomic policy 'orthodoxy'. Consequently, the new understanding of 'orthodox' macroeconomic policy advanced in this chapter has consisted of an interlocking framework of economic ideas, policy objectives, policy instruments, hierarchy between those policy instruments and policy outcomes.

The second original contribution to our existing knowledge of UK economic policy in this chapter has been the development of a superior understanding of change and continuity in UK macroeconomic policy. Here, the chapter identified a historical pattern in UK macroeconomic policymaking, which sees macroeconomic policy return to 'orthodoxy' in the aftermath of crises through a series of distinct phases of crisis, temporary deviation, consolidation and 'orthodoxy'. This historical cycle in UK macroeconomic policymaking and the dynamics of each phase are delineated in full in Chapter Five. The basic outline of the observed pattern in this chapter is provided below.

The crisis phase consists of a series of economic events and emergencies, which are designated as crises by narratives. Dependent on the macroeconomic policy response to the crisis phase, macroeconomic policymaking will either enter a phase of temporary deviation or consolidation. If the macroeconomic policy response consists of a deviation from 'orthodox' objectives, policy instruments and policy outcomes, then macroeconomic policymaking will have entered the phase of temporary deviation. However, the deviation from 'orthodox' policy is only temporary and does not form the basis of permanent radical policy change. Meanwhile, the consolidation phase arises either immediately in response to the

crisis phase, or after the phase of temporary deviation. The consolidation phase consists of the use of 'orthodox' macroeconomic policy instruments to create the economic conditions necessary to secure the return to the 'orthodox' objective of price stability and 'orthodox' fiscal policy outcome of the balanced budget and national debt reduction. The consolidation phase will also see the deployment of a policy narrative that seeks to legitimise 'orthodox' policy instruments as the solution. Finally, the orthodoxy phase consists of a full return to 'orthodox' macroeconomic policy, which is legitimised by the deployment of a policy narrative.

Chapter 4

Change and Continuity in UK Economic Policymaking from April 1975 to April 1997

Introduction

This chapter reviews the literature and provides a historiography on United Kingdom (UK) economic policymaking and economic performance from April 1975 to April 1997. This chapter supports the thesis' central contention that existing literature, which explains economic policy change by reference to punctuated equilibrium, is flawed. Indeed, rather than the radical policy changes normally ascribed to exogenous shocks, such as the 1976 International Monetary Fund (IMF) Loan Crisis, and endogenous shocks, such as the 1979 General Election, this chapter finds significant continuity of 'orthodox' macroeconomic policy and ideas in this period. Consequently, this chapter reiterates the gaps in our current knowledge of UK economic policymaking previously identified. First, that greater specificity is required in our understanding and definition of 'orthodox' macroeconomic policy. Second, that there is a need for a superior understanding of when and why UK macroeconomic policy and ideas exhibit change and continuity.

The analysis in this chapter strengthens the two research findings of the previous chapter, which fill the gaps in our existing comprehension of UK economic policymaking and provide an original contribution to our knowledge. First, the chapter corroborates the new understanding and definition of 'orthodox' macroeconomic policy and ideas identified in Chapter Three. Furthermore, in certain areas, the chapter establishes even greater exactitude. Second, the chapter

demonstrates that the historical pattern in interwar macroeconomic policy highlighted in Chapter Three, which sees the continuity of ‘orthodoxy’ in the aftermath of crises through a series of distinct phases in macroeconomic policymaking of crisis, temporary deviation, consolidation and orthodoxy, is also discernible in macroeconomic policymaking between April 1975 and April 1997.

The remainder of the chapter will be organised as follows. The next section will show that punctuated equilibrium provides the dominant explanation of change in UK economic policy during the 1970s and 1980s. The chapter then continues to explore our current understanding of ‘orthodox’ economic policy in the 1980s. The chapter proceeds to examine the UK’s economic policy response to the economic upheavals of the 1970s, including the two oil price shocks (1973 and 1979), a global recession (1975), three significant domestic recessions (1973-74, 1975 and 1980-81), a secondary banking crisis (1973-75), rising unemployment, inflation and labour unrest. The chapter then turns to examine the economic policy response to the economic crises of the early 1990s, which included recession in the UK economy and a Sterling crisis that precipitated ejection from the European Exchange-Rate Mechanism (ERM).

Change and Continuity in UK Economic Policymaking in the 1970s and 1980s

Two primary explanations of change in UK economic policy in the 1970s are available in the literature. The first explanation centres on the 1979 general election victory by the Conservative party, which is viewed as an epoch defining moment for economic policy in the UK. Here, the election of a Conservative government is portrayed as heralding significant change in economic policy and ideas, which caused the demise of the post-war consensus (Bale,2012:204-206;Booth,1982:216;Dutton,1997;Hay,2001;Jessop, 2002;2003:5). Consequently, the

1979 general election is often presented as an example of a paradigmatic shift in UK economic policy as new ideas, objectives and policy instruments were institutionalised within UK economic policymaking (Hall,1993; Hickson,2005;Oliver & Pemberton,2004;Pemberton,2009). Indeed, the scale of political, economic and social change after 1979 described as 'revolutionary' by scholars from opposite ends of the political spectrum (Harvey,2011:1;Roy & Clarke,2005)[50].

The second explanation of economic policy change is as a consequence of the IMF loan crisis in the summer of 1976. Here, the IMF loan crisis is portrayed as a 'turning point' in UK economic policy, which led to the demise of the post-war consensus, the abandonment of full employment and the emergence of inflation as the primary objective of economic policy[51]. For instance, Burk and Caincross (1992:129) conclude that the IMF loan crisis was 'a turning point in the philosophical basis of economic policy and in the thinking of the Treasury about economic management'. Consequently, Glynn (1991:130-131) argues that economic policy after 1979 was built upon 'the ground... prepared by [previous] Labour governments which undermined belief in collective action, cut areas of public spending, established targets for money supply, and abandoned the traditional approach to full employment in the face of economic crisis'.

These explanations of economic policy change in the 1970s and 1980s therefore are predicated upon the model of punctuated equilibrium. For example, in both explanations, economic policy change is conceived of as a discontinuous process. In the first explanation, the 1979 general election is presented as an endogenous shock, which punctuated the economic policy equilibrium of the post-war consensus and led to radical policy change. In the second explanation, the 1976

[50] Britton (1991:4), Greenaway and Shaw (1988:388) and Pemberton (2009) also described the changes in UK economic policy after the election of the Conservative government in 1979 as 'revolutionary'.
[51] Booth (1982:209,212), Burk & Caincross (1992), Peden (1991:210) and Ridley (2014:57-60) all identified the 1976 IMF loan crisis as a 'turning point' for UK economic policymaking.

IMF loan crisis is presented as an exogenous shock, which punctuated the economic policy equilibrium of the post-war consensus and led to radical policy change.

Subsequent analysis will expose the flaws in this explanation of when and why economic policy changed in the 1970s and 1980s. Indeed, this chapter will demonstrate significant continuity in 'orthodox' macroeconomic policy and ideas. Here, the chapter strengthens the research finding pertaining to the historical pattern in macroeconomic policymaking, which emerged from Chapter Three and explains that macroeconomic policy returned to 'orthodoxy' from the 1975 Budget onwards via the same series of distinct phases in macroeconomic policymaking that was evident in the interwar period. Consequently, the chapter identifies a gap in our knowledge of UK economic policymaking for a superior understanding of when and why UK macroeconomic policy exhibits change and continuity.

Our Current Understanding of 'orthodox' Economic Policy in the 1970s and 1980s

Not all explanations of UK economic policy during this period, however, rely upon the model of punctuated equilibrium. Indeed, several scholars' analysis of interwar economic policymaking has led to them to draw parallels and identify continuities with UK economic policy in the 1970s and 1980s[52]. One of the fullest expression of this proposition was provided by Middleton (1985:182-187). For example, Middleton (1985:182) posits that 'without suggesting any essential similarity between the two ages, we can nevertheless identify certain recurrent themes in Twentieth century UK economic policy; what we might term the diuturnity of 'orthodoxy'.

[52] For example, Booth (1982), Gamble (1979), Glynn (1991:129-131), Howson & Winch (1977:162), Miller (1981:60) and Tomlinson (2012:63-64) all highlight continuities between UK economic policy in the interwar period and in the 1970s and 1980s.

The recurrent themes identified by Middleton included inflation: the fear of it in the interwar period and the reality of it in the 1970s and 1980s. Moreover, in both eras, Middleton (1985:183) notes the 'continued appeal of budgetary orthodoxy' as the 1980s saw a re-emergence of the 'balanced budget doctrine'. Furthermore, Middleton (1985: 186-187) contends that there were similar attitudes towards public expenditure in both periods. For instance, the 1980s saw a return to a view of public expenditure as a 'luxury good' and a belief that government spending to create employment created illusory employment due to the crowding-out of effects of deficit-finance on the private sector. The final recurrent theme identified by Middleton (1985:187) is the moral dimension in economic policy, which was most evident in the use of language in policy statements and speeches. Indeed, Middleton (Ibid) suggests that 'we could continue, almost indefinitely, with such parallels' between economic policy in the two historical periods.

The parallels drawn by scholars between economic policies in the interwar period and 1980s identifies a further gap in our existing knowledge of UK economic policymaking for greater specificity in our understanding and definition of 'orthodox' macroeconomic policy, which would allow us to chart the continuities in macroeconomic policy across the two historical periods with greater specificity. The remainder of this chapter re-emphasises the new understanding and definition of 'orthodox' macroeconomic policy and ideas, which was identified in Chapter Three. Consequently, the chapter highlights that macroeconomic policy between April 1975 and April 1997 exhibits significant continuity of 'orthodoxy'.

UK Economic Policymaking in Response to the Economic Crises of the 1970s

The 1970s was beset by a series of major economic and political events and emergencies, which plunged UK economic policymaking into a phase of crisis and are widely portrayed as contributing or accelerating a longer standing process of UK

economic decline (Crafts,1996;Copley & Woodford,1996:8-10). The events and emergencies that plagued UK economic policy in the 1970s were both global and domestic. At the global level, the global economy suffered a recession (1974-1975), two major oil price shocks (1973 & 1979) and the onset of a global inflationary problem (Peden,1991:197-199). At the domestic level, the 'Barber boom' of the early 1970s saw the emergence of a housing bubble within the UK economy. When this bubble burst across 1973-1975, the dramatic crash in house prices caused a secondary banking crisis that threatened a number of smaller lending banks with bankruptcy necessitating financial intervention by the Bank of England (Reid,1982). This would not be the last time that the Bank of England was forced to intervene to protect a financial institution from the folly of its own speculative investments. In 1984, the Bank of England was forced to nationalise Johnson Matthey Bankers in order to prevent panic spreading through the rest of the UK banking system.

The consequence of these events and emergencies for UK economic performance included a trebling of inflation, rising unemployment and reduced economic growth (Copley & Woodward,1996:2-3). Furthermore, the failure to rectify deteriorating economic performance in the 1970s led to an institutional crisis within Whitehall. For instance, Her Majesty's Treasury belief in the efficacy of demand management was significantly shaken by events of the 1970s (Hall,1993:285-286; Middleton,1996:346). The period is also often presented as a decade of rising labour unrest and trade union militancy epitomised by the Winter of Discontent (1978-1979), which gave rise to the fear that the UK was becoming politically and economically ungovernable (Copley & Woodford,1996:1-2;Hay,1996;Tomlinson,2012:65).

The first challenge to established explanations of UK economic policy in this chapter relates to the question of when economic policy began to change from the post-war consensus of demand management and full employment in reaction to these events and emergencies. For example, several scholars argue that the Labour government (1974-1979) under Harold Wilson, Prime Minister (1964-1970 & 1974-1976), and James Callaghan, Prime Minister (1976-1979), had already jettisoned the economic policy objective of full employment for the defeat of inflation prior to

1976[53]. Similarly, Porter (1996:50-51) argues that the Labour government abandoned Keynesianism in 1975 when it introduced monetary targets for growth in the money supply. Finally, Tomlinson (1984:260) highlights that only briefly in the Budget of April 1974 did the Labour government take the view that the global economic recession, caused by the 1973 oil price shock, could be off-set by expansionary fiscal policy.

As a result, Hickson (2004:41) argues that change in UK economic policy during the 1970s, for example, cannot be reduced to the IMF loan crisis because 'many of the reforms said to have originated with the intervention of the IMF in late 1976 were in fact introduced much earlier'. Indeed, it is the 1975 Budget statement of Denis Healey (1975), Chancellor of the Exchequer (1974-1979), which should be considered the seminal moment in UK macroeconomic policymaking in the 1970s. Specifically, because it was the 1975 Budget that Healey rejected the use of fiscal policy as an instrument to manage demand in the UK economy. Consequently, the 1975 Budget saw fiscal policymaking enter a phase of consolidation, which included the implementation of 'orthodox' fiscal policy instruments to reduce the public sector borrowing requirement (PSBR) [54].

The claim that fiscal policymaking entered a phase of consolidation in 1975 is given greater credence when we consider the account of UK macroeconomic policymaking during this period provided by Douglas Wass, Permanent Secretary to the Treasury (1974-1983). For example, Wass (2008:Chp.2) highlights that Treasury advice to the incoming Labour government in 1974 had included the need for control of public expenditure as part of efforts to rebalance the UK economy. However, Wass (2008:90,Chp.3) identifies that it was in 1975 that the Treasury came to recognise that 'a significant shift of policy required involving a sharp break in hitherto established practice', which involved a 'big improvement in public finances'

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[53] The claim that the Labour government jettisoned the economic policy objective of full employment before the 1976 IMF loan crisis is also available in Clift and Tomlinson (2008), Needham (2014:19) and Tomlinson (2004:60-61).

[54] The PSBR was the name given to government borrowing during this period. The PSBR was the amount the government had to borrow each financial year when expenditure exceeded taxation.

and a ‘determined attack on inflation’. Thus, Wass (2008:91) indicates that whilst the 1974 November Autumn Statement had proposed a reflationary fiscal policy response to the global economic slump, the 1975 Budget was ‘judged… the most opportune moment for a policy change’, which included a ‘new approach to policymaking’ and a ‘significant change in direction’. This chapter demonstrates that far from policy change, the 1975 Budget saw the consolidation of macroeconomic policy towards ‘orthodoxy’.

In his 1975 Budget statement of the 15th April, for example, Healey (1975:c. 282) stated that “the budget judgement is conventionally seen as an estimate of the amount of demand which the government should put into the economy or take out of it in order to achieve the optimum use of resources in the short term. For many reasons I do not propose to adopt that approach today”. Furthermore, Healey used his Budget Statement to claim that two weaknesses in UK economic performance that had to be addressed were the high level of public borrowing and inflation, not the full employment of labour. Thus, Healey (1975:c.283) specified that it was his aim was “to establish a strategy which will enable us to achieve a very substantial improvement in our current account deficit in the next two years and to eliminate the deficit entirely as rapidly as possible thereafter”, which included a reduction in the PSBR of £1billion in 1975-76 and £3billion in 1976-77. Henceforth, Callaghan (1976), Healey (1976b) and Gordon Richardson (1975;1975a;1976;1978;1979), Governor of the Bank of England (1973-1983) repeatedly make clear that the macroeconomic policy strategy was based on a reduction of government borrowing, the introduction of monetary targets and an incomes policy[55]. Additionally, the Labour government would make the primary objective of macroeconomic policy reduction in the rate of inflation (Callaghan,1976a:c.1458;Healey,1976c:c.1176;HM Treasury,1975;1976;1977).

Consequently, by the time of the 1976 IMF loan crisis, the direction of travel in macroeconomic policymaking had already been established by Healey and the

[55] Part of the ‘social contract’, agreed between the Labour government and Trade Unions, was the implementation of a voluntary income policy, which included Trade Unions acceptance of wage restraint as a means of reducing inflation.

Treasury. This is demonstrated in Table One, which provides data on the economic performance of the public finances during the Labour governments of Harold Wilson and James Callaghan. Here, the consolidation towards 'orthodoxy' is evident in the columns for Public Sector Net Borrowing and Public Sector Net Debt, which were on a downward trajectory until 1978. In his memoir, Healey (1989:433) recalls that he could loosen fiscal policy in 1978-79 because he had achieved a larger reduction of the PSBR in preceding years than had been agreed with the IMF in December 1976.

Table One: Economic Performance of Fiscal Policy, 1974-1979

Years	**Public Sector Net Borrowing** (£billions) *(2014/15 Prices)*	**Public Sector Net Borrowing** *(% of GDP)* *(+ = Deficit)*	**Cyclically-Adjusted Net Borrowing** *(% of GDP)* *(+ = Deficit)*	**Public Sector Net Debt** *(% of GDP)*
1974-75	£46.0	+6%	+8.8%	50.3%
1975-76	£50.7	+6.7%	+6.4%	52.2%
1976-77	£40.9	+5.2%	+4.6%	50.6%
1977-78	£33.0	+4.1%	+3.7%	47.1%
1978-79	£40.3	+4.8%	+5.5%	44.9%

(Source:OBR,2016**)**

Table Two presents further data on the economic performance of the public finances under the Labour governments of Harold Wilson and James Callaghan, which shows

that Healey and the Treasury achieved the reduction in the PSBR and national debt through decisions taken on public expenditure. In particular, there was considerable public spending restraint in public sector current expenditure after 1975, which served to reduce public sector current expenditure as a percentage of GDP. Here, the success of public spending restraint had been greatly aided by an operational change to the formulation of fiscal policy with the introduction of cash limits – a fixed annual limit on departmental spending across Whitehall – in 1976 (HM Treasury,1976a). Furthermore, significant expenditure reductions in public sector net investment were implemented. Cumulatively, this meant that Healey and the Treasury secured a slight reduction in total managed expenditure (TME) after the 1975 Budget, which secured a more significant public expenditure reduction as a percentage of GDP. Thus, we can provide greater exactitude to our understanding of 'orthodox' fiscal policy instruments and add public expenditure restraint.

Table Two: Economic Performance of Public Expenditure, 1974-1979

Years	**Public Sector Current Expenditure** (£billions) *(2014/15 prices)*	**Public Sector Current Expenditure** *(% of GDP)*	**Public Sector Net Investment** (£billions) *(2014/15 prices)*	**Public Sector Net Investment** *(% of GDP)*	**Total Managed Expenditure** (£billions) *(2014/15 prices)*	**Total Managed Expenditure** *(% of GDP)*
1974-75	£280.8	36.6%	£44.9	5.8%	£361.1	47%
1975-76	£290.6	38.3%	£44.7	5.9%	£371.5	48.9%
1976-77	£299.3	38.2%	£37.6	4.8%	£374.4	47.8%
1977-78	£295.9	36.7%	£27.0	3.3%	£360.8	44.8%
1978-79	£306.7	36.6%	£24.2	2.9%	£369.7	44.1%

(Source:OBR,2016)

The demonstration that monetary policy also returned to 'orthodoxy' in the 1970s requires the first challenge to our understanding of the role of monetary targets and 'monetarism' in monetary policymaking. For example, Needham (2014:Chps.1-2) finds that the Treasury and Bank of England had begun experimentation with targets for the growth of the money supply in the aftermath of the 1967 devaluation crisis in an effort to reduce the rate of inflation. The result of this experimentation was an operational change in the formulation of monetary policy with the introduction of

Competition and Credit Control monetary management (CCC) (1971-1973) in 1971. Needham (2014:Ix) describes the CCC as 'the most radical overhaul of UK monetary policy since the Second World War' because it abandoned the panoply of quantitative and qualitative restriction on bank lending that had been placed on banks since the 1960s to control credit conditions and replaced them with the 'interest-rate weapon' (Needham,2014:3).

The CCC was only radical, however, in the context of monetary policymaking during the post-war era. Instead, the introduction of the CCC heralded the beginning of a phase of consolidation in monetary policymaking, which saw the implementation of 'orthodox' policy instruments of the Bank Rate[56] and Open Market Operations (OMOs) to reduce domestic inflation (Greenaway & Shaw,1988:124-129). For example, Charles Goodhart (2014:1), Chief Advisor in the Bank of England (1969-1985), notes that 'the intention [of the CCC] was… to achieve the monetary authorities objectives of policy via the operation of market mechanisms, notably adjustments in interest rates and open market operations (OMOs)'. It was through these 'orthodox' monetary policy instruments that policymakers aimed for targets for growth in the money supply. However, as in the interwar period, the Bank Rate and OMOs provided policymakers with indirect control over the money supply through short-term market interest-rates and credit conditions.

Needham (2014:3) identifies, however, that in terms of control of the money supply the CCC came to be considered a failure. Indeed, by December 1973 £M3 money had risen by 72% above target. The apparent failure of the CCC to curtail the

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[56] The Bank Rate was replaced by the MLR on the 13th October 1972. The MLR set a minimum rate at which the Bank of England was prepared to charge on loans and advances to the banking system against a range of securities. The MLR was suspended on the 20th August 1981 and replaced by Band Dealing Rates and then the Repo Rate. However, these developments in monetary policy were only a change in nomenclature, as the MLR, Band Dealing Rates and the Repo Rate provided the same function as the Bank Rate had previously. Thus, they set the price at which the Bank of England provided liquidity to the banking system in an effort to manage the level short-term market interest-rates (Bank of England,2016). In order to avoid confusion, this chapter will merely refer to the Bank Rate.

money supply led the Bank of England to consider that £M3 was a defective measure of monetary growth and the Bank of England implemented the supplementary special deposits scheme (or corset), which penalised banks that grew interest-bearing liabilities above a published level that itself was derived from unpublished £M3 targets for monetary growth. Nevertheless, Goodhart (2014:1) comments that the corset represented only ‘a partial reversion towards a partial direct control system’ pursued after the Second World War and thus continued ‘the direction of travel towards a more liberal, market based system’ (Goodhart,2014:1). Meanwhile, Her Majesty’s Treasury fell back on incomes policy.

The importance of the 1975 Budget is further highlighted when we examine the impact it had on the relationship between fiscal and monetary policy in macroeconomic policymaking. In an echo of the interwar period, the 1970s saw the growing fear among politicians and policymakers of the inflationary potential of public expenditure. For example, officials within the Treasury and the Bank of England began to consider government borrowing as a source of domestic inflation, which contributed to inflation via expansion of the money supply. Consequently, monetary considerations pertaining to the reduction of inflation was an important determinant in the decision to adopt a fiscal policy strategy based on control of public expenditure and reduction in the PSBR (Thain,2005:34). This ensured that fiscal policy played a supportive role to monetary policy in the defeat of inflation, which conformed to the ‘orthodox’ hierarchy between macroeconomic policy instruments evident in the interwar years.

The 1975 Budget heralds a consolidation towards ‘orthodoxy’ in UK macroeconomic policymaking, however, and not an outright return to macroeconomic policy ‘orthodoxy’ for two reasons. First, the macroeconomic policy response of the Labour government, Treasury and Bank of England included policy instruments that can be classed as ‘unorthodox’, which included the aforementioned incomes policy and the supplementary special deposits scheme, which saw a partial return to direct control over bank lending and monetary growth. Second, the macroeconomic policy objective was to defeat and achieve low inflation, which does not necessarily equate with price stability. Third, economic policy

performance was far from exhibiting ‘orthodox’ objectives or outcomes. For example, Table One demonstrates the still significant level of government borrowing by the time of the 1979 general election. Similarly, whilst significant strides had been made towards the macroeconomic policy objective of low inflation, prices had fallen from 24.2% in 1975 to 8.3% in 1978; prices were still far from stable (Twigger,1999:14).

The Conservative government that was elected on 3rd May 1979 under the leadership of Margaret Thatcher, Prime Minister (1979-1990), and Geoffrey Howe, Chancellor of the Exchequer (1979-1983) inherited a UK macroeconomic policymaking process lodged in a phase of consolidation. However, rather than provoking radical change in UK macroeconomic policy, the Conservative government, Treasury and Bank of England continued the consolidation phase in UK macroeconomic policy until the 1981 Budget. This was noted recently by Howe (2014:xi-xii), although he is wrong about the start date of consolidation in UK macroeconomic policymaking, when he stated that the medium-term financial strategy (MTFS) was ‘invaluable in re-orientating radically the broad lines of UK economic policy; or perhaps I should say in consolidating the earlier reorientation initiated in 1976’.

The Conservative government had been in office for only seven and a half weeks when the Oil Producing Exporting Countries increased the price of oil by 15% on the 28th June 1979. This second oil price shock of the decade served to provide further turbulence to an already volatile global economy. Furthermore, weakness in the global economy coincided with the onset of a severe recession in the UK as GDP fell by 5.9% between Q2 1979 to Q1 1981 (Chamberlin,2010:52). The Conservative government also inherited an unemployment rate standing at 5.4% and despite the end of recession in 1981 the unemployment rate did not peak until 1984 at 11.8% (ONS,2016).

The Conservative government’s macroeconomic policy strategy was enshrined in the medium-term financial strategy (MTFS), which was introduced in the 26th March 1980 Budget (HM Treasury,1980) and was the first in a series of

revised MTFS' published at each subsequent Budgets. These MTFS' provided an operational change to the formulation of macroeconomic policy that served to institutionalise monetary targets in monetary policymaking and the 'orthodox' outcome of the balanced budget in fiscal policymaking. The central objective of the MTFS was to 'reduce inflation... [and] progressively reduce the growth of the money stock' (HM Treasury,1980:16), which would be achieved through monetary targets for the growth of £M3 and projections for successive reductions in the PSBR. The eventual aim for the PSBR was for it to reach 0%, which would return the budget to balance. The priority macroeconomic policy objective of the MTFS was the 'orthodox' macroeconomic objective of price stability (Britton,1991:209)[57].

The MTFS also confirmed that the relationship between macroeconomic policy instruments would continue to be organised according to the 'orthodox' hierarchy, which saw fiscal policy play a supportive role to monetary policy in the pursuit of the 'orthodox' objective of price stability. For example, the Treasury (1979:1) argued in its 1979 Budget Report that reduction in the PSBR was necessary to reduce inflation because government borrowing was a main determinant in monetary growth and complicated the task of controlling the money supply. Similarly, in its 1980 Budget Report, the Treasury (1980:16) claimed that the PSBR was a direct cause of excessive growth in the money supply. As a result, the 1979 general election saw a continuation of the belief that public expenditure and fiscal deficits contributed to domestic inflation, which had re-emerged during the earlier part of the decade (Lawson,1982:3-4;Thatcher,2010:97).

The determination of the new Conservative government to reduce public expenditure and government borrowing, however, was complicated by the increasing severity of domestic economic conditions. The contraction in GDP growth caused by the recession of 1979-81 caused upward pressure on public expenditure as public spending unemployment benefits increased. Thus, Table Three demonstrates that public expenditure, TME and the public sector net borrowing all rose after 1979, although, particular attention should be focused on the primary balance, which

[57] Howe (1979a:1) and Lawson (1983;1984) both stated in public speeches that the primary objective of the MTFS was price stability.

calculates government net borrowing excluding interest payments on national debt. Here, the Conservative government were able to secure fiscal tightening amounting to 2.7% GDP between 1980-81 and 1981-82. It was in this context for the UK public finances that Howe (1981:c.771-778) and the Treasury implemented the infamous 10th March 1981 Budget, which sought to override the automatic stabilisers in the UK public finances by introducing significant tax increases in the midst of recession. Here, Gamble (1994:111) notes that the determination of the 1981 budget to see a reduction in government borrowing meant that 'in the midst of the deepest recession since 1945 the government made progress towards fiscal balance its priority rather than attempting to counteract the fall in demand'.

Table Three: Economic Performance of Fiscal Policy, 1979-1983

Years	**Public Sector Current Expenditure** (% of GDP)	**Total Managed Expenditure** (% of GDP)	**Public Sector Net Borrowing** (% of GDP)	**Primary Balance** (% of GDP) *(- = deficit / + = surplus)*
1979-80	36.5%	43.7%	3.9%	-0.1%
1980-81	38.8%	46%	4.6%	-0.6%
1981-82	40.1%	46.4%	2.2%	+2.1%
1982-83	40.3%	46.9%	2.8%	+1.1%

(Source:OBR,2016)

Table Four presents a series of data on public finances, which are cyclically-adjusted and consequently excludes increased public expenditure arising from welfare

payments to the unemployed. Once the public finances have been cyclically-adjusted, we can begin to see the magnitude of fiscal tightening that was implemented by Howe and Her Majesty's Treasury after the 1979 election. Furthermore, we can see that fiscal policy since 1979 had consistently sought to override the automatic stabilisers in public finances. For example, 1979-80 to 1981-82 saw a 4.3% GDP reduction in cyclically-adjusted public sector net borrowing, 3% GDP reduction in the cyclically-adjusted current budget deficit and 4.5% GDP reduction in cyclically-adjusted primary balance. This significant fiscal tightening in the public finances – achieved via the 'orthodox' fiscal policy instruments of public expenditure reductions and tax increases - meant a return to a balanced budget in cyclically-adjusted terms. This included a surplus of 1.5% GDP in the cyclically-adjusted current budget and 4.2% GDP surplus in cyclically-adjusted primary balance. Cumulatively, Table Three and Four allow us to identify that the Conservative government's fiscal policy reaction to the 1979-81 recession was a continuation of the consolidation in the public finances enacted since the 1975 Budget of the previous Labour government.

Table Four: Economic Performance of Fiscal Policy in Cyclically-Adjusted Terms, 1979-1983

Years	**Cyclically-Adjusted Public Sector Net Borrowing** (% of GDP) *(+ = Deficit / - = Surplus)*	**Cyclically-Adjusted Current Budget Deficit** (% of GDP) *(+ = Deficit / - = Surplus)*	**Cyclically-Adjusted Primary Balance** (% of GDP) *(- = Deficit / + = Surplus)*
1979-80	+4.3%	+1.5%	-0.3%
1980-81	+3.2%	+0.9%	+0.8%
1981-82	0%	-1.5%	+4.2%
1982-83	+0.8%	-1.2%	+3.2%

(**Source:**OBR,2016)

The 1981 Budget was still a significant event in UK macroeconomic policymaking, however, for one specific reason, namely, because it was the 1981 Budget, rather than the 1980 MTFS that fully institutionalised the restoration of 'orthodoxy' within the macroeconomic policymaking process. This return to macroeconomic policy 'orthodoxy' occurred despite economic performance not yet returning to the orthodox objective of price stability or the orthodox fiscal policy outcome of the balanced budget and national debt reduction. The scale of fiscal tightening implemented after the 1979 election had been masked from view by rising TME, public sector current expenditure and government borrowing due to rising unemployment during the 1979-81 recession. Furthermore, fiscal consolidation in the 1981 Budget was implemented during a period of significant political conflict over

the relationship between monetary policy, recession and rising unemployment. In the context of this political conflict, the decision to prioritise the reduction of government borrowing in pursuit of the 'orthodox' objective of price stability forcefully communicated the end of the era of demand management to those who had not identified its demise at the 1975 Budget. Consequently, the 1981 Budget considerably altered the psyche of UK macroeconomic policymaking. This was evident in the now infamous letter to the Sunday Times signed by 365 economists, which denounced the fiscal strategy of the 1981 Budget. Henceforth, macroeconomic policymaking under the Conservative government of Margaret Thatcher would be conducted according to the dictates of 'orthodoxy'.

The claim that macroeconomic policy returned to 'orthodoxy', however, necessitates a further challenge to our accepted notion of the role of 'monetarism' in monetary policymaking after 1979. Once again, this challenge focuses on the role of monetary policy objective and instruments, particularly, the implementation of 'orthodox' monetary policy instruments of the Bank Rate and OMOs to target the money supply, which had originally been brought to the fore by 1971 CCC (Hotson,2014:126;Riddell, 1983:57-65). For example, analysis by Needham (2014;2014b) clearly demonstrates the key importance of the Bank Rate as a monetary policy instrument within 'monetarism' and its role in attempts to limit growth in the money supply. Here, Needham (2014:1-2, Chp.5) identifies the 1981 Budget as critical in our understanding of monetary policymaking after 1979. First, because the 1981 Budget confirmed the importance of the Bank Rate. Second, because the 1981 Budget signalled a U-turn in monetary policy, which Needham (2014b:179) claims signalled the end of 'monetarism'.

Needham (2014:1-2,Chp.5) highlights the critical role played by the monetary policy instrument of the Bank Rate, for example, in the 'monetarism' of the Conservative government in the months after their 1979 general election, which had been raised by Howe and the Treasury in successive stages to 17% by November 1979 in an attempt to control the rate of £M3 growth. Thus, Howe and the Treasury sought to slow growth in the money supply and meet its monetary target through the Bank Rate and its impact on credit conditions and short-term market interest-rates.

However, within four months of the introduction of the MTFS in the 1980 Budget, the Treasury had reduced the Bank Rate by 1%. A decision that Needham (Ibid) argues has no underpinning in 'monetarism' given that the Treasury had lost control of £M3 growth, which was overshooting the monetary targets established in the MTFS. In response, rather than increase the Bank Rate in order to control the money supply, the Bank Rate was reduced in successive stages by a further 4% to stand at 12% by March 1981.

The purpose of these reductions in the Bank Rate was to ease the liquidity problem in the UK economy, which was particularly afflicting manufacturing, and reduce short-term market interest-rates and thus the cost of credit. Consequently, albeit within the context of a high profile for the Bank Rate, the Conservative government responded to the 1979-1981 recession through attempts to provide limited reflationary finance to the UK economy through reductions in the Bank Rate. Furthermore, the reduction in the Bank Rate across 1980-1981 further strengthens the argument that fiscal policy played a supportive role to monetary policy in the Conservative government's macroeconomic policymaking. Here, fiscal 'orthodoxy' was believed to create the monetary conditions that would allow the Treasury to cut the Bank Rate and ease the liquidity squeeze in the UK economy. For instance, Lankester (2014) noted that a major incentive for the imposition of deflationary fiscal policy in the 1981 Budget was to secure further reductions in the Bank Rate, which would also allow Sterling to deprecate[58]. Accordingly, Needham (2014:1) suggests that the 'lady was for turning' after all.

The use of the Bank Rate to target the money supply led Milton Friedman to argue, in his submission to the Treasury and Civil Service Committee (1980:55-61) memorandum on monetary policy, that the Conservative government were not monetarists. This was the case, Friedman (Ibid) argued, because the Bank Rate and public expenditure reductions were an alternative, not a complement, to direct

[58] Tim Lankester served as Private Secretary to Prime Ministers James Callaghan and Margaret Thatcher. On the relationship between the 1981 Budget and the Bank Rate, see Hotson, (2014) and the Treasury and Civil Service Select Committee (1981a:42,Q. 188).

control of the monetary base. Thus, Friedman (Ibid) noted that market interest-rates reflects the price of credit, not money, and claimed that using the Bank Rate to alter credit conditions had only a highly erratic and undependable influence on the money supply. According to Friedman (Ibid), the Bank Rate was given primacy as a policy instrument because of a long-standing confusion between money and credit in UK macroeconomic policymaking, which had its origin in the Bank of England's management of the Gold Standard during the nineteenth century and led to the development of a historical tradition in monetary policymaking of exercising indirect control of the money supply via the Bank Rate and credit conditions. The force of Friedman's oral evidence to the Treasury and Civil Service Committee was to illustrate the continuity in UK macroeconomic policy between the Gold Standard and 'monetarism'.

The historical antecedents to Conservative economic policy after 1979 were not lost on Nigel Lawson. For example, Lawson (1980) claimed that the Thatcher government's economic strategy stood in the broad historical tradition of Conservatism and UK economic policymaking. Thus, Lawson (1980:3) argued that 'to the extent that new conservatives turn to new sages – such as Hayek and Friedman – this is partly because what those writers are doing is avowedly reinterpreting the traditional political and economic wisdom of Hume, Burke and Adam Smith' (Lawson,1980:3) and that 'what we are witnessing is the reversion to an older tradition in the light of the failure of what might be termed the new enlightenment [of Keynesian social democracy]' (Ibid: 3). Consequently, Lawson (1980:12-13;1982:2-4) emphasised that the MTFS was the contemporary version of the Gold Standard and balanced budget rule of the interwar and nineteenth century and that 'monetarism' was merely the contemporary reassertion of David Hume's quantity theory of money.

The continuities between monetary policy in these two eras is further apparent when we consider the implementation of the 'orthodox' policy instruments of OMOs after the 1979 general election. The Bank of England conducted daily OMOs to supply liquidity, through the provision of banknotes, to the UK banking system. The Bank of England supplied banknotes through offer of purchase, either

outright or on repo (sale and repurchase agreements), of Treasury bills, eligible local government bills and bank bills from discount houses. The discount houses would then compete to sell bills to the Bank of England at their own choice of rates. The Bank of England would use this process of OMOs to influence market interest-rates. If Discount Houses offer of securities were at a rate that conflicted with the need for higher market interest-rates, then these offers could be rejected in whole or in part, which would force the discount houses to deal at a lending rate that was consistent with the level of market interest-rates it wanted to establish (Bank of England,2016).

In the 1980s, OMOs were also implemented as part of Bank of England's public debt policy (Nelson,2013:97-98). Here, the Bank of England used OMOs to pursue a policy of 'overfunding' government borrowing through the sale of more Treasury bills than was necessary to cover the PSBR, which allowed the Bank of England to elongate the structure of UK national debt. The Governor of the Bank of England, Gordon Richardson, in evidence to the Treasury and Civil Service Committee (1982:42,Q.268-269) gave two reasons as to why the Bank of England had overfunded the PSBR. First, that it allowed the government to make a negative contribution to monetary growth. Second, that the purchase of commercial bills from the financial system allowed the Bank of England to provide relief against the credit squeeze in the UK economy.

The continuity of 'orthodox' monetary policy between the Gold Standard period and the introduction of the 1971 CCC makes it legitimate to claim that the Conservative government, the Treasury and the Bank of England were monetarist in rhetoric only. For example, Treasury documents (1980a:ii-iii), Treasury and Civil Service Committee reports (1981a:vix,para.25-27;1982:v-vi,para.5-7) and memoirs (Lawson,1992:47) make clear that as early as the winter of 1979 £M3 was no longer the main target variable within the MTFS and other indicators of monetary conditions were being used in the formulation of monetary policy. Consequently, 'monetarism' and monetary targets played the same role in monetary policymaking as had the Gold Standard. Specifically, 'monetarism' provided policymakers with a monetary framework with which to understand prevailing monetary conditions and

guide their implementation of the 'orthodox' monetary policy instruments of the Bank Rate and OMOs in pursuit of the 'orthodox' policy objective of price stability.

The literature on UK economic policy in the 1970s to 1990s also allows us to identify the re-emergence of 'orthodox' economic ideas in the formulation of UK economic policy. Indeed, it becomes clear that the same 'orthodox' interpretations of economic ideas from the interwar period continued to provide policymakers and politicians with a world view, which allowed them to interpret events and determine the appropriate relationship between macroeconomic policy objectives and instruments. For example, Margaret Thatcher (1986) articulated that she considered the UK economy as a subordinate part of the world economy in her 1986 Conservative party conference speech when she stated that the "the whole industrial world, not just Britain, is seeing change at a speed that our forebears never contemplated, much of it due to new technology. Old industries are declining. New ones are taking their place....it would be… foolish to pretend that a country like Britain, which is so heavily dependent on trade with other countries, can somehow ignore that is happening in the rest of the world". A visible example the influence of internationalism on the formulation of policy was the importance placed on the maintenance of confidence in the UK economy[59]. For instance, in a collection of essays offering a retrospective of the 1974-1979 Labour government, Roy Hattersley (2004:274), Secretary of State for Prices and Consumer Protection (1976-1979), claimed that after the 1976 IMF Loan Crisis 'high levels of public expenditure… were accepted as incompatible with the essential maintenance of international confidence'.

The 1970s and 1980s also saw the re-emergence of the 'orthodox' economic idea of crowding-out in the formulation of macroeconomic policy, in both the

[59] For example, Healey (1976b:c.236;1976e:c.709;1989:411-413,427) and Richardson (1977a:461) all identified that macroeconomic policy after 1975 was implemented to secure confidence in global financial markets. Moreover, Major (1999:663), and Thatcher (1975) also asserted that economic policymaking must secure confidence in the UK economy.

financial and psychological versions described in the previous chapter[60]. Indeed, Greenaway and Shaw (1988:8) argue that the return of crowding-out amounted to an affirmation of the 1929 Treasury View. For example, the financial version of crowding-out was articulated by Bacon and Eltis (1976) who argued that the UK's economic woes lay in the size of the non-productive public sector in comparison to the productive private sector. Specifically, because 'the great increase in non-industrial employment and the accompanying increase in non-industrial investment' had taken 'resources away from the balance of payments and industrial investment' (Bacon & Eltis,1976:18). The return of the financial version of crowding-out has led Hotson (2014:124) to suggest that the Conservative governments of the 1980s were early believers in theories of expansionary fiscal contraction.

Meanwhile, the psychological version of crowding-out was articulated in the 1980 Budget Statement by Howe (1980a:c. 1444) who declared that "relaxed monetary and budgetary policies might bring higher output – even higher living standards – in the very short run, though even that is questionable, but in reality they would simply fuel fresh inflation. Such policies would inevitably undermine the confidence of financial markets, industry and consumers. The action that would then be necessary to deal with the ensuing crisis would, equally, certainly, destroy jobs and cut living standards further". As a result, Middleton (1985:185) argues that the content of Howe's 1980 Budget statement differs little from the defence of the Treasury View provided by the Treasury official Richard Hopkins in his evidence to the Macmillan Committee in 1930.

The return of the 'orthodox' economic idea of crowding-out also led to the affirmation of interwar attitudes towards public-works, or, what in contemporary discourse would be termed capital or infrastructure investment. Comparable to the interwar period, capital investment became something that could be accepted at an

[60] The re-emergence of the economic idea of crowding-out in its financial and psychological conceptions was evident from the public speeches and statements of politicians and HM Treasury documents, see Healey (1975:201;1976a:231,para.7), HM Treasury (1979:1) and Joseph (1979:1). The return of the economic idea of crowding-out during the Chancellorship of Dennis Healey has also been identified by Hickson (2005),

individual level within the context of controlled public expenditure (Howe,1981b:c.902), rather, than as part of a macroeconomic strategy of demand management. Furthermore, the concept once again re-emerged that capital investment must be remunerative and not contribute to an increase in national debt (Howe,1981a;c.99;Lawson,1984b.c.785).

The 1970s and 1980s also saw the economic idea of economic liberalism become important in the formulation of economic policy. For example, the development of the natural rate of unemployment 'represent[ed] a… refinement of the classical view', which viewed unemployment as a microeconomic and voluntary phenomena (Glynn & Booth,1996:95)[61]. Similarly, Gamble (1979:19) argues that the natural rate of unemployment represented a reassertion of a liberal political economy of the 1920s and 1930s, which posited that unemployment as primarily determined by market imperfections. Specifically, adherents of the natural rate argued that unemployment could not be solved by policies of demand management, which would lead to inflation and, ultimately, higher unemployment. Instead, unemployment must be solved through microeconomic policy, which reduces the role of institutions, such as the welfare state and Trade Unions, in the economy that inhibited free market exchange, price signals and priced persons out of employment[62].

Consequently, Conservative governments after 1979 would embark upon economic liberal inspired microeconomic reform, which aimed to "remove the impediments to the efficient working of the economy by allowing markets to work

[61] The natural rate of unemployment is the level of unemployment within an economy at which prices remain stable. The natural rate contends that if policymakers attempt to hold the unemployment rate below the natural level, through expansionary fiscal or monetary policies, inflation will rise. For this reason, the natural rate is often referred to as the non-accelerating inflation rate of unemployment (NAIRU) (Farmer, 2013: 248).

[62] The claim that the welfare state and Trade Unions represented a market imperfection, which hindered market exchange, price signals and priced persons out of employment were made repeatedly after 1975, see Clarke (1996:cc.28-29; 1996a:c.446;1997), Dorey (1999), Healey (1976e:c.717-719;1977:174; 1977a:c. 1730;), Hill (1999), Joseph (1978:8-9;1979b:c.711;1980:c.1886;1980a:c.189), Lamont (1991a:c.1196;1992a;1993), Lawson (1984c:c.790; 1984d:c.1196), Prior (1978) and Thatcher (1978).

better and by the creation of conditions conducive to growth and employment" (Lawson,1984a:c.1180). Here, government microeconomic policy was directed at reducing market imperfections and included economic policies such as de-regulation, trade union reform, privatisation, liberalisation, tax cuts and competition, which Lawson (Ibid) claimed would create the conditions for "new enterprise and new jobs" through the provision of open, competitive and flexible markets.

The 1970s also saw the return of 'orthodox' interpretations pertaining to competitiveness in the formulation of economic policy. Thus, it was reiterated that UK firms' ability to export goods and services was subject to global competition. For example, Healey (1975:c.275,c.281;1976d:c.281) reminded the House of Commons whilst he was Chancellor that UK industry was competing against foreign counterparts, especially those emerging from the Far East. After the 1979 general election, the Department of Trade and Industry (1982;1994;1996) published several reports on competitiveness strategies for the UK economy, which were predicated on the 'orthodox' interpretation of economic liberalism. Indeed, it was posited that the economic liberal microeconomic policies implemented by successive Conservative governments after 1979 aided competitiveness of the UK economy by reducing unit and non-unit costs to UK firms. Thus, John Major (1994), Chancellor of the Exchequer (1989-90) and Prime Minister (1990-97) declared in a speech on the 24th May 1994 that "it is becoming a truism to say that the world is becoming more competitive than ever before…technology and free trade have created a global environment, there is a global market place". Similarly, Kenneth Clarke (1994:2), Chancellor of the Exchequer (1994-1997), stated in a speech on the 12th July 1994 that in "an ever more competitive world… we have to move still further to improve the supply-side performance of the UK economy... it will mean containing the size and costs of the state so that growth of public expenditure can be restrained and marginal rates of taxation can be reduced for individuals and business. It will mean more deregulation and private finance".

These economic ideas played a critical role in the formulation of policy and led to the rejection of macroeconomic strategies of demand management to secure full employment. Instead, the selection of the 'orthodox' objective of price stability.

For example, in his 1984 Mais Lecture, Nigel Lawson (1984) emphatically stated that the era of demand management was over because “it is the conquest of inflation and not the pursuit of growth and employment, which is or should be the objective of macroeconomic policy”. Furthermore, Lawson (Ibid) claimed that the firm monetary and fiscal discipline of the government’s macroeconomic strategy, alongside the freedom given to markets by economic liberal microeconomic policy, formed a ‘British experiment’ in economic policy. In this ‘British experiment’ the role of macroeconomic policy was to secure economic stability. Meanwhile, the role of microeconomic policy was to create the domestic economic conditions, which would allow entrepreneurs and businesses to improve economic performance in growth, employment and competitiveness in world markets (Joseph,1976;1978)[63].

The rejection of demand management was also evident in the Treasury policy documents. For example, a Treasury submission to the Treasury and Civil Service Committee (1980:8) 1980 memorandum on monetary policy, stated that ‘it is now abundantly clear.... that governments themselves cannot ensure high employment.... governments create the conditions in which it can be achieved’ and any ‘attempt to meet... [full employment] by expansionary fiscal and monetary policies would result in higher inflation, and in the end be disastrous for output, growth and employment’, which echoed the sentiment of the infamous 1976 Labour party conference speech by James Callaghan (1976).

Finally, these economic ideas were important because they allowed actors in UK politics to construct a narrative of the crises of the 1970s. The dominant narrative portrayed the events and emergencies of the 1970s as a symptom of post-war economic decline, which had been caused by two aspects of post-war economic policy. First, the implementation of Keynesian demand management and full employment, which caused government borrowing and inflation. Second, the post-war development of the welfare state and industrial policy had inhibited the dynamism and efficiency of free exchange in private markets.

[63] Keith Joseph served as Secretary of State for Industry 1979-1981 and Secretary of State for Education and Science 1981-1986.

This narrative was driven in politics by the Conservative Party under Margaret Thatcher. For example, in her 1975 Conservative party conference speech, Thatcher (1975) would designate the events of the emergencies of the 1970s not as "a crisis of capitalism, but of socialism. No country can flourish if its economic and social life is dominated by nationalisation and state control". Likewise, Keith Joseph (1979a) would state that the 1979 general election represented the chance to transform an economy in which "growth has virtually been eliminated by a combination of union enforced luddism and overmanning, punitive taxation, excessive state borrowing and spending, excessive legislation and bureaucracy and excessive state interference, control and ownership". Consequently, the purpose of the 'crisis of socialism' narrative was to designate events and emergencies as a product of the state. In turn, this narrative sought to legitimise a macroeconomic policy strategy that prioritised price stability over full employment and implementation of significant reductions in public expenditure.

The Phase of Orthodoxy in Macroeconomic Policy after the 1981 Budget, the Lawson Boom and UK Economic Policymaking in Response to the ERM Crisis and Recession of 1990-1992

Fiscal and monetary policy both remained 'orthodox' after the 1981 Budget. For example, significant public spending restraint during the 1980s ensured that TME and public sector current expenditure fell from their peak of 46.9% GDP and 40.3% GDP in 1982-83 to 37.4% GDP and 32.9% GDP respectively by 1990-91 (OBR,2016). Subsequently, spending restraint, alongside the proceeds from privatisation of nationalised industries, meant the Conservative government returned the public finances to 'orthodox' fiscal policy outcomes. First, the public finances returned to surplus in 1988-89 and 1990-1991. Second, national debt continued to

decline and stood at just 23.6% GDP in 1990. Consequently, Margaret Thatcher (2010:297) claimed that her Conservative government had "set [the] standard of sound finance not seen for two generations. At last there has been a return to 'orthodox' finance... we have done more than balance the books". In his 15th March 1988 Budget statement, Lawson (1988a:c.996) claimed that "henceforth a zero PSBR will be the norm. This provides a clear and simple rule, with a good historical pedigree".

Table Five: Economic Performance of Fiscal Policy, 1987-1991

Years	**Public Sector Net Borrowing** (% of GDP) *(+ = deficit / - = surplus)*	**Current Budget Deficit** (% of GDP) *(+ = deficit / - = surplus)*	**Public Sector Net Debt** (% of GDP)
1987-88	+1.0%	0.0%	33.6%
1988-89	-1.1%	-1.9%	27.8%
1989-90	-0.1%	-1.7%	25%
1990-91	+1.0%	-0.6%	23.6%

(**Source:**OBR,2016)

Meanwhile, developments in monetary policy after the 1981 Budget would seem to indicate significant policy change, rather than the continuity of 'orthodoxy'. For example, in her memoirs, Thatcher (1993:689-690,694-699) stated that the 1987 Budget marked the death knell of 'monetarism'. Thatcher (1993:690) made this assessment of the 1987 Budget because, she argued, 'if the exchange-rate becomes an objective in itself, as opposed to one indicator among others for monetary policy, monetarism itself has been abandoned'. Therefore, Thatcher's claims about the end

of ‘monetarism’ in monetary policymaking relates to the Treasury policy of ‘Shadowing the Deutschmark’.

The failure of experimentation with monetarism as a monetary framework had led policymakers in Her Majesty’s Treasury and the Bank of England to search for a new framework for the operational conduct of monetary policy, which would aid the fight against inflation and led Lawson to favour entry to the European Exchange-Rate Mechanism (ERM). Indeed, in his memoirs, Lawson (1992:111) claimed that he had been persuaded since 1981 of the case for making the ERM the prime determinant of monetary policy in the battle against inflation[64]. However, Lawson was unable to persuade Margaret Thatcher, who remained opposed to fixed exchange-rates, to back UK membership. In this political context, Lawson began to unofficially peg Sterling to the Deutschmark between a rate of DM2.90 and DM3.00 (Stewart,1993:55). Lawson was replaced as Chancellor of the Exchequer by John Major who, alongside others in Cabinet would persuade Thatcher to join the ERM, which the UK did on the 8th October 1990 at a rate of DM2.95.

The policies of ‘Shadowing the Deutschmark’ and the ERM played the same role in monetary policymaking as had the gold standard. Both policies provided, unofficially or officially, monetary policymaking membership of an institution of economic governance, this time regional rather than global, which provided a system of domestic monetary management to maintain domestic anti-inflationary discipline and instil credibility in macroeconomic policy. For example, the key purpose of ‘Shadowing the Deutschmark’ and the membership of the ERM was the desire of the Treasury and Conservative politicians to import the historical success of the German Bundesbank in sustaining price stability[65]. Consequently, the fixed exchange-rate

[64] The ERM was introduced by the European Economic Community on the 13th March 1979 in order to reduce exchange-rate fluctuation between member’s currencies and achieve monetary stability. Each currency that joined the ERM would do so at a fixed exchange-rate, which allowed for 6% margin of fluctuation around that rate. Membership of the ERM forced governments to take monetary policy action to keep its currency within that fixed band of movement.

[65] Lamont (2000:386) and Major (1990;1990a;1999:152-154,662) made it clear that the motivation for joining the ERM was the success the German Bundesbank had in

element of ‘Shadowing the Deutschmark’ and the ERM was considered the means to secure the ‘orthodox’ macroeconomic policy objective of price stability, which was the same function played by the fixed-exchange rate element of the Gold Standard. Indeed, the similarity between the Gold Standard and the ERM was not lost on Nigel Lawson (1988:14) who noted that both included a dual responsibility for internal and external values of the currency as the route to defeating inflation.

It also becomes clear that ‘Shadowing the Deutschmark’ and the ERM also demonstrated a further similarity with the Gold Standard. Specifically, ‘Shadowing the Deutschmark’ and the ERM played the role of a monetary framework, which allowed monetary policymakers to make sense of prevailing monetary conditions and guide the implementation of the ‘orthodox’ monetary policy instruments of the Bank Rate and OMOs in pursuit of the ‘orthodox’ macroeconomic policy objective of price stability. Consequently, much like the return to the Gold Standard in 1925, ‘Shadowing the Deutschmark’ and the ERM were examples of institutional and operational changes to monetary policymaking that, rather than form the basis of radical policy change, served to ensure the continuity of ‘orthodoxy’ within macroeconomic policymaking.

The ‘orthodox’ monetary policy instruments of OMOs, for example, played a significant role in allowing Sterling to ‘shadow the Deutschmark’ and remain a member of the ERM. Here, OMOs continued to play their role in providing liquidity to the UK banking system ensuring the level of short-term market interest-rates reflected the Bank Rate. However, they also played a further role, which was reminiscent of the use of OMOs in 1930s monetary policymaking. Namely, the Treasury and the Bank of England conducted OMOs in foreign exchange markets. For instance, whilst Sterling was ‘Shadowing the Deutschmark’, upward pressure on the value of Sterling meant it necessary for the Bank of England to undergo significant sales of Sterling via OMOs in order to bring down its value and keep it under the upper DM3.00 limit (Stewart,1993:56).

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securing domestic price stability. It was believed that membership of the ERM would allow monetary policymaking to import this success to the UK economy.

The use of OMOs was noted by the Treasury and Civil Service Committee (1988:para.61-62,xv-xviii) report on the 1988 Budget, which highlighted increasing intervention in foreign exchange markets in 1987. Similarly, the Treasury and Civil Service Committee (1989:para.102-103,xxiii) report on the 1989 Autumn Statement found that significant intervention in foreign exchange markets had occurred in 1988 in order to sustain a firm exchange-rate. Furthermore, the Treasury and Civil Service Committee (1989:para.103,xxiiii) contended that the express purpose of these day-to-day interventions in foreign exchange markets via OMOs were intended to 'buck the market' and maintained Sterling at an artificial exchange-rate with the Deutschmark.

The argument that 'Shadowing the Deutschmark' and the ERM acted as a monetary framework within monetary policymaking is strengthened when we consider the role of the Bank Rate. For example, the speculative upward pressure on Sterling, which had led to increasing intervention in foreign exchange markets, also led to a significant reduction in the Bank Rate from 10% to 7% by May 1988 (Bank of England, 2016a) in order to reduce the attractiveness of Sterling on global markets. Similarly, when Sterling began to deprecate, monetary policy was tightened and the Bank Rate was increased to 15% in October 1989 and encourage the purchase of Sterling in global markets and raise its price in relation to foreign currencies. The higher Bank Rate was also designed to help counter the resurgence of inflation in the UK economy as a result of the 'Lawson Boom'. The Bank Rate stayed at 15% for a full year until October 1990, which saw a reduction in the Bank Rate to 14% (Ibid).

The latter stages of this phase of 'orthodoxy' in UK macroeconomic policymaking, however, also saw the emergence of a number of economic weaknesses, which would contribute to the next phase of crisis. 1987-88 saw a significant expansion of in the GDP growth in the economy, which became known as the 'Lawson Boom'. Cumulatively, the economy posted economic growth worth 12.2% GDP between Q4 1986 and Q4 1988 and 4% of that GDP growth came in Q2 and Q3 1987 (ONS,2016). However, by 1989, the 'Lawson Boom' had begun to dissipate and the economy grew by just 1.1% GDP, which included an economic quarter (Q4) of flat growth at 0%. Furthermore, the 'Lawson Boom' had allowed a

resurgence of inflation in the UK economy. Prices rose steadily in 1987 and 1988 before rising significantly to 7.8% in 1989 and 9.5% in 1990 (Twigger,1999:16-17). The causes of the 'Lawson Boom' were plentiful, chief among them was the deregulation and liberalisation of UK financial markets during the 1980s, which led to a credit boom within the UK economy. This expansion of credit drove an upsurge of private sector debt. For example, the household debt to disposable income ratio, which stood at 50% in 1984 had risen to over 90% in 1990 (Dunn & Smith,1994:84).

In evidence to the Treasury and Civil Service Committee (1989:32,Q.197), John Major stated that the 'Lawson boom' of 1987-88 had been caused by excessive private sector demand exacerbated by policy errors. Britton (1991: 205-206) identified that these policy errors included fiscal policymaking. For instance, the five most contractionary fiscal Budgets in the period 1974-1990 were all implemented in the recession years of 1974, 1975 and 1979-1981. Meanwhile, Britton (Ibid) found that the most expansionary fiscal budget in this period was provided in the 1987 Budget of the 17th March, which occurred during the 'Lawson Boom'. The contribution of macroeconomic policy to the economic boom of the late 1980s was also noted by the Treasury and Civil Service Committee (1989:xv,para.58-59), which reported that fiscal and exchange-rate policy had contributed to an emergence of an economic boom in the late 1980s. Here, the Treasury and Civil Service Committee (Ibid) highlighted that 'little attention was paid to the inflation warning signalled by the expansion of domestic credit[66]. Furthermore, this report by the Treasury and Civil Service Committee (1989:xv-xvi,para.58-59) stated, despite the return to 'orthodox' fiscal policy outcomes of the balanced budget and national debt reduction, that the 1988 Budget 'may have contributed to the enormous expansions of credit by generating euphoria at a time of financial liberalisation'. The 1988 Budget famous for the announcement of a series of tax cuts, which included the reduction of the top rate of tax to 40% (Lawson,1992:Chp. 66).

[66] The role of credit expansion in the 'Lawson Boom' was also highlighted by Treasury and Civil Service Select Committee (1988a:xv, para.49) in its report on the 1988 Autumn Statement.

Successive increases in the Bank Rate, which rose from 7% to 15% in the five months from May to October 1988 (Bank of England,2016a) put an end to the 'Lawson Boom' and UK economic policymaking entered another phase of crisis. As market interest-rates rose, businesses and households found it increasingly difficult to access credit. This led to a rising level of bankruptcies and house repossessions as firms and individuals in the heavily indebted UK economy found it increasingly difficult to service their debts. In Q2 1990, the UK economy entered recession, which lasted for eight consecutive quarters until Q2 1992 and saw an economic contraction amounting to 2.5% GDP (Chamberlin,2010:52). Furthermore, unemployment rose by 876,000 persons to peak at 2.929million in 1993 (ONS,2015). The onset of recession coincided with the emergence of civil disobedience in public life, which culminated in a 200,000 strong protests in central London against the imposition of the poll tax on the 31st March 1990. The scale of political opposition to the poll tax, which had been introduced at the behest of Margaret Thatcher, led to disquiet among the Conservative Cabinet and triggered a leadership contest within the Conservative Party. On the 22nd November 1990, Conservative Cabinet members forced Margaret Thatcher to resign as Prime Minister. She was replaced by John Major and Norman Lamont (1990-1993) became Chancellor of the Exchequer.

The Major government were immediately beset by recession in the domestic economy, which was exacerbated by the monetary policies necessary to maintain Sterling within the ERM. For example, Chancellor of the Exchequer (1990-1993), Norman Lamont (2000:150,387-390) posited in his memoir that the UK's membership of the ERM necessitated keeping the Bank Rate at a high level in defence of the DM.295 exchange-rate. Thus, whilst Lamont and Her Majesty's Treasury had been able to reduce the Bank Rate from 15% in October 1990, it still stood at 10% in May 1992 (Bank of England,2016a). The conflict between membership of the ERM and the needs of the domestic economy arose from speculative pressure on Sterling arising from global financial markets. It came to be considered in financial markets that the UK had joined the ERM with an overvalued exchange-rate. Consequently, significant pressure was placed on Sterling within

financial markets, as global investors began to speculate that the UK would be unable to maintain its membership of the ERM at the DM2.95 parity rate.

The speculative pressure placed on Sterling from global investors reached its conclusion on the 16th September 1992, which has become known in UK economic history as 'Black Wednesday'. A flood of Sterling onto the global financial markets, which was led by the Quantum Fund managed by George Soros, threatened to depreciate Sterling below the lower bound permitted by its ERM membership. In response, Lamont authorised the Bank of England to prop up the value of Sterling, which took the form of OMOs to buy Sterling from the global financial markets. Furthermore, Lamont and the Treasury increased the Bank Rate to 15% in an effort to tempt global investors to buy Sterling currency and increase its value. By the end of the 16th September, Lamont was forced to concede defeat and the UK left the ERM.

The remainder of this chapter will show that UK macroeconomic policymaking in the early 1990s conforms to the historical pattern that has been identified in macroeconomic policymaking in the nineteenth century, interwar period, 1970s and 1980s. In these periods, UK macroeconomic policymaking responded to crises through a phase of temporary deviation or consolidation. Chapter Three identified that the temporary deviation phase in macroeconomic policymaking involves the implementation of a macroeconomic strategy that departs from 'orthodoxy'. Chapter Three also identified that the phase of consolidation in UK macroeconomic policymaking consisted of the use of 'orthodox' macroeconomic policy instruments to create the economic conditions necessary for a return to 'orthodox' objectives and outcomes. In response to the crisis phase in the early 1990s, fiscal and monetary policy can be seen to take two divergent paths and operate at different speeds through these phases.

The Major government's fiscal policy response to the recession in the UK economy was to implement a fiscal policy strategy that departed from 'orthodox' fiscal policy outcomes and fiscal policy instruments. This fiscal policy strategy was implemented at the 1991 Budget. For example, in his Budget Statement, Lamont

(1991) argued that rising government borrowing since 1990 had been the result of the cyclical downturn in the UK economy, which had caused declining tax revenue and increased upward pressure on public expenditure. Furthermore, Lamont (1991) would claim that these "cyclical swings in the budget balance can play a useful role in offsetting the swings in private sector borrowing and in stabilising the economy", which meant there would only be a "gradual return to budget balance". Consequently, Lamont sought to legitimise the departure from the 'orthodox' fiscal policy outcome of the balanced budget through a policy narrative, which appealed to economic growth. For example, in his 1991 Autumn Statement of the 6th November, Lamont (1991b:c.449) stated he had "judged it right to allow expenditure to rise to meet the unavoidable consequences of weaker economic activity. Our priority.... [is] to maintain the expenditure of programmes which contribute most to the long-term strength of the economy".

The development of this policy narrative is made more complicated, however, when we consider that Lamont attempted to legitimise his decision to allow government borrowing and public expenditure to increase to counteract deterioration in UK domestic economic performance through appeals to the fiscal policymaking of previous Conservative Chancellors. For example, in oral evidence provided to the Treasury and Civil Service Committee (1991:53,Q.345) on the 27th November 1991, Lamont defended his decision to allow the unimpeded operation of the automatic stabilisers to support economic activity by suggesting that this had been the policy of Geoffrey Howe and Nigel Lawson. Thus, the policy narrative sought to cast the fiscal policy strategy introduced at the 1991 Budget as a continuation of 'orthodoxy' pursued since 1979. Lawson (1981:12) had indeed argued, in a pamphlet written in 1981, that during a recession it was appropriate to allow the PSBR to be allowed to rise above the medium term trend line even though this was not the course of action pursued in the notorious 1981 Budget. However, Lawson (Ibid:12) added that this did not mean 'that the brakes are off. It does not mean... that discretionary action to boost the budget deficit over and above the natural increase brought about by recession is either sensible or desirable'.

The use of automatic stabilisers, however, can be considered an orthodox fiscal policy response to crises for two reasons. First, the use of the automatic stabilisers has only a cyclical impact on the UK public finances, which arises without policy intervention. Thus, it is a non-discretionary fiscal policy response that does not involve an increase in public expenditure, government borrowing and national debt beyond that caused by higher welfare spending on unemployment and lower taxation revenue. Consequently, the automatic stabilisers do not stimulate domestic demand so much as provide a floor beneath which it cannot fall. Second, because the automatic stabilisers have only a non-discretionary cyclical impact on the public finances, the public finances also return to orthodoxy fiscal orthodoxy without policy intervention once employment and taxation revenue recover. The only circumstances this will not occur are if the downturn in the domestic economy is large enough to reduce the pre-crisis growth rate. In such circumstances, the public finances would need to be brought back to orthodoxy through a consolidation phase in fiscal policymaking involving the use of orthodox fiscal policy instruments. Consequently, for fiscal policymaking to deviate from orthodoxy it requires the implementation of fiscal policy strategy that involves discretionary fiscal policy, which aims to stimulate domestic demand via a purposeful increase in public expenditure, government borrowing and national debt beyond that provided by the automatic stabilisers.

Fiscal policymaking entered a phase of temporary deviation at the 1991 Budget because, notwithstanding its limited scale, it involved the implementation of discretionary fiscal policy. For instance, the Treasury and Civil Service Committee (1991:xi-xii,para.28) report on the 1991 Autumn Statement found that the Conservative government had engaged in discretionary spending, albeit at a modest level. Furthermore, in his memoirs, Major (1999:664-665,677-678) credited the deficit to a combination of falling revenue, rising expenditure, discretionary spending and decreases in inflation. Similarly, in the memoirs of Nigel Lamont (2000: 47,95-97,101-102,160-165,334-357) the fiscal deficit was credited to the automatic stabilisers and political pressures inside Cabinet to increase expenditure. Indeed,

Lamont (2000:306-307) provided extra expenditure of £1.65billion on health and £1.4billion on transport in his 1991 Autumn Statement.

Table Six presents a range of data on the economic performance of the public finances, which demonstrates the temporary deviation phase in fiscal policymaking. Instead of adopting an 'orthodox' fiscal policy response to the recession of 1990-92 through the implementation of 'orthodox' fiscal policy instruments of public expenditure cuts, spending restraint or tax increases to balance the budget, the Major government purposefully allowed public expenditure and government borrowing to rise through the use of the automatic stabilisers and discretionary fiscal policy. For example, TME and public sector current expenditure rose significantly between 1990-91 and 1993-94 as a percentage of GDP. Meanwhile, public sector net borrowing, current budget deficit and primary balance all went into a significant deficit in both real and cyclically-adjusted terms. Finally, public sector net investment was increased by 0.5%GDP in response to the recession, which demonstrates the deployment of a discretionary public spending.

Table Six: Economic Performance of the Public Finances, 1990-1994

Years	**Total Managed Expenditure** (% of GDP)	**Public Sector Current Expenditure** (% of GDP)	**Public Sector Net Investment** (% of GDP)	**Public Sector Net Borrowing** (% of GDP) *(+ = deficit)*	**Cyclically-Adjusted Public Sector Net Borrowing** (% of GDP) *(+ = deficit)*	**Current Budget Deficit** (% of GDP) *(+ = deficit / - = surplus)*	**Cyclically-Adjusted Current Budget Deficit** (% of GDP) *(+ = deficit / - = surplus)*	**Primary Balance** (% of GDP) *(= = deficit / + = surplus)*	**Cyclically-Adjusted Primary Balance** (% of GDP) *(= = deficit / + = surplus)*
1990-91	37.6%	33.3%	1.6%	+1.0%	+0.8%	-0.6%	-0.9%	+1.2%	+1.4%
1991-92	39.6%	35.2%	2.0%	+3.5%	+2.1%	+1.5%	+0.1%	-1.6%	-0.2%
1992-93	41.4%	37.1%	2.1%	+6.9%	+5.3%	4.9%	+3.2%	-4.9%	-3.2%
1993-94	40.8*	37.0%	1.7%	+7.2%	+5.9%	5.5%	+4.2%	-4.9%	-3.6%

(Source:OBR,2016)

Whilst fiscal policymaking responded to the recession of 1990-92 with a phase of temporary deviation, membership of the ERM constrained monetary policy choices. This meant that the response of monetary policymaking to the economic crises of the early 1990s was slower to that seen in fiscal policymaking. Indeed, when monetary policymaking did respond to the UK's ejection from the ERM, it did so not through temporary deviation but through immediate consolidation towards 'orthodox' monetary policy via the introduction of the inflation target system. The operational change from the ERM to the inflation target system of monetary management was introduced in a letter sent by Lamont to the Chair of the Treasury and Civil Service Committee on the 8th October 1992. In this letter, Lamont (1992:2) explained that monetary policy would, henceforth, target an inflation rate of 1-4% RPIX over the remainder of the Parliament, which corresponded with a long-term

inflation rate of 2%[67]. This was then changed to an inflation target of "2.5 per cent or below" in the 1995 Budget of Kenneth Clarke (1995), Chancellor of the Exchequer (1993-1997).

That the inflation target system represented the latest incarnation of monetary policy 'orthodoxy' relies upon our understanding of 'orthodox' monetary policy to consist of an 'orthodox' policy objective of price stability and monetary policy instruments of the Bank Rate and OMOs. At the very heart of the inflation target system was the objective of price stability. Indeed, the Bank of England (1993:3) Inflation Report of February 1993 noted that the 'commitment to price stability [is] embodied [in] the inflation target'[68]. Consequently, monetary policy would directly target the rate of inflation, which provided for stable prices. Furthermore, both Lamont (1992b:7) and Clarke (1994a), Chancellor of the Exchequer (1993-1997), confirmed that the primary monetary policy instrument in the new inflation target system was the Bank Rate.

The second monetary policy instrument in the new inflation target system was OMOs, which were used in the same manner within monetary policymaking since 1971[69]. This was confirmed by the Bank of England (1997) in a paper published in March 1997, which was entitled *Reform of the Bank of England Operations in the Sterling Money Markets*. In this paper, the Bank of England (Ibid) set out the purpose of its daily OMOs, which were conducted to ensure that the banking system was supplied with liquidity at an interest-rate selected by the Bank of England. The Bank of England also set out how it conducted its OMOs, which were

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[67] RPIX stands for Retail Prices Index excluding mortgage payments.

[68] The Bank of England (1993a:59;1993c;345;1995b:221) also noted that the objective of price stability was embodied in the inflation target in a series of *Quarterly Bulletins* published after October 1992.

[69] The Bank of England (1993a:61-65;1993b:204-211;1993c:347-349;1993d:464-466; 1994:8-9;1994a:108-110;1994b:206-207;1994c:303-305;1995:8-14;1995a:130-135; 1995b:225-227;1995c:319-322;1996:7;1996b;133;1996c:249-250;1996d:366-368; 1997a:9-12;1997c:131-137) provided a regular update on the role of OMOs in monetary policymaking in their *Quarterly Bulletin* publications. Here, the Bank of England explained that they brought market interest-rates into line with the Bank Rate through the price at which it provided liquidity to the banking system through OMOs.

performed daily in order to ensure that market interest-rates reflected the Bank Rate through outright purchases and repo agreements for gilt repos, Treasury bills, eligible local authority bills, and bank bills.

Monetary policymaking was joined by fiscal policymaking in the consolidation phase of UK macroeconomic policymaking in 1994. Here, Portes (2012) argues that the Conservative government under Major implemented a 'textbook response to the recession of the early 1990s' as the Major government only started to implement spending cuts and tax increases to close the deficit once economic recovery had taken hold. For example, the 1993 Budget, whilst announcing tax increases and tight restrictions on public spending, suspended their introduction until 1994-1995 when GDP growth was near 4% per annum (Lamont,1993). This is demonstrated in Table Seven, which shows that public expenditure and government borrowing on a downward trajectory as a percentage of GDP as Clarke and the Treasury held public spending in restraint, reduced public sector net investment and increased taxation.

Table Seven: Economic Performance of Fiscal Policy, 1994-1997

Years	Total Managed Expenditure (% of GDP)	Total Managed Expenditure (£billions) *(2014/15 Prices)*	Public Sector Current Expenditure (% of GDP)	Public Sector Current Expenditure (£billions) *(2014/15 Prices)*	Public Sector Net Investment (% of GDP)	Public Sector Net Borrowing (% of GDP) *(+ = deficit)*	Current Budget Deficit (% of GDP) *(+ = deficit)*	Primary Balance (% of GDP) *(- = deficit)*
1994-95	40.4%	£487.1	36.7%	£442.5	1.6%	+5.8%	+4.2%	-3.2%
1995-96	40.1%	£494.3	36.6%	£450.6	1.6%	+4.4%	+2.9%	-1.6%
1996-97	38.1%	£481.3	35.3%	£446.2	1.6%	+3.3%	+2.3%	-0.5%

(**Source:**OBR,2016)

Conclusion

This chapter has reviewed the literature and provided a historiography on UK economic policymaking and economic performance from April 1975 to April 1997. The chapter has supported the thesis' central contention that existing literature, which explains economic policy change by reference to punctuated equilibrium, is flawed. Instead, the chapter has found significant continuity of 'orthodox' macroeconomic policy and ideas between April 1975 and April 1997. Furthermore, this chapter has highlighted the same two gaps in our current knowledge of UK economic policymaking identified in previous chapters. First, that greater specificity

is required in our understanding and definition of 'orthodox' macroeconomic policy. Second, that there is a need for a superior understanding of when and why UK macroeconomic policy and ideas exhibit change and continuity.

Analysis in this chapter has also strengthened the two research findings established in Chapter Three, which fill these gaps in our existing comprehension of UK economic policymaking and provide an original contribution to our knowledge. The first original contribution is through the provision of greater clarity in our understanding and definition of 'orthodox' macroeconomic policy. Here, the chapter has allowed us to provide even greater exactitude to our understanding and definition of 'orthodox' macroeconomic policy and ideas. For instance, the chapter has showed that public expenditure restraint should be added to our understanding of 'orthodox' fiscal policy instruments.

The second original contribution to our existing knowledge of UK economic policy is the development of a superior understanding of change and continuity in UK macroeconomic policy. Chapter Three highlighted a historical pattern in UK macroeconomic policymaking, which saw macroeconomic policy return to 'orthodoxy' in the aftermath of crises through a series of distinct phases in macroeconomic policymaking of crisis, temporary deviation, consolidation and orthodoxy. This chapter has found that these distinct phases were also evident in macroeconomic policymaking between April 1975 and April 1997. This historical cycle in UK macroeconomic policymaking and the dynamics of each phase are delineated in full in the next chapter, which will also discuss methodology and specify the research question that subsequent case-study chapters will seek to answer.

Chapter 5

Methodology

Introduction

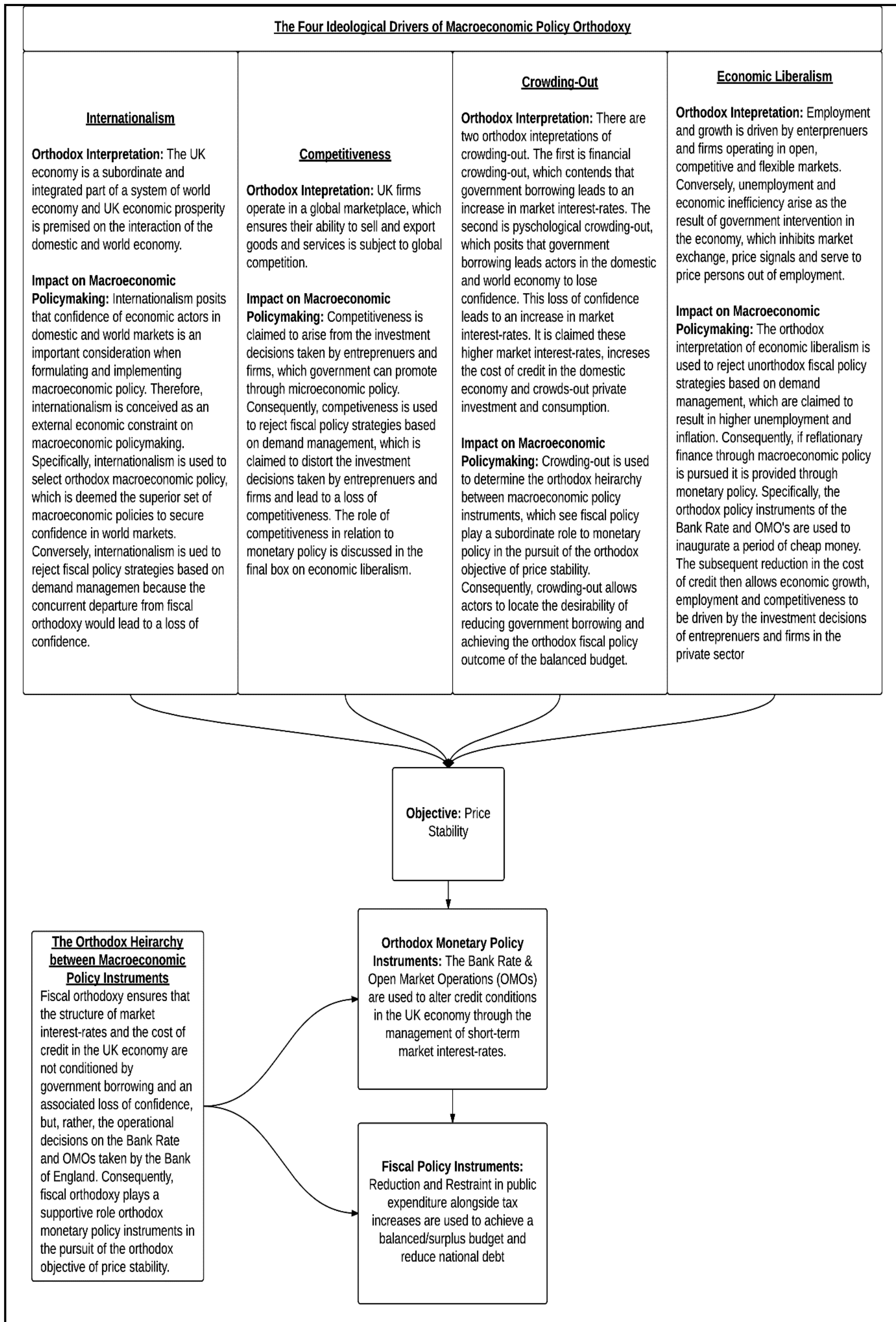
This chapter will outline the methodology employed by this thesis and specify the research question, which the following case-study chapters will answer. The research question is: Does the conceptual framework of the orthodox cycle provide an understanding and explanation superior to that furnished by punctuated equilibrium of the reasons for change and continuity in macroeconomic policymaking in the United Kingdom since the 1997 General Election? The thesis will aim to answer this question by testing the conceptual framework of the orthodox cycle via a series of case-studies of change and continuity in UK macroeconomic policymaking from the 1st May 1997 to the 13th July 2016, which includes the tenure of the Blair, Brown, Cameron-Clegg Coalition and Cameron governments. The remainder of the chapter will be organised as follows. The chapter will begin by setting out the two research findings from the historiography in Chapters Three and Four. The chapter will then continue to outline the methodology employed by this thesis, research design and methods utilised in the collection and analysis of data.

The New Understanding of Orthodox UK Macroeconomic Policymaking

The critical literature reviews in the opening chapters of this thesis established two gaps in our current knowledge of UK economic policymaking. The first of these gaps

pertains to the need for greater specificity in our understanding and definition of orthodox macroeconomic policy. The precise specification of orthodox UK macroeconomic policy advanced in this thesis was influenced by Hall's (1993) work on policy paradigms, which is defined as a framework of ideas, policy objectives and policy instruments. The specification of orthodox UK macroeconomic policy was also influenced by Greenaway and Shaw's (1988: Chp. 17) evaluative steps for the study of macroeconomic policy. Here, the first step involved the determination of prioritised objective/s for macroeconomic policy in times of policy conflict. The second step involved the identification of policy instruments that are logically consistent with the achievement of the prioritised objective. The historiography conducted in Chapters Three and Four identified several additions that had to be made to these basic frameworks, which allowed for the provision of greater clarity and exactitude in our understanding and definition of orthodox macroeconomic policy. Consequently, our new understanding of orthodox UK macroeconomic policy is presented as an interlocking framework of economic ideas, policy objectives, policy instruments, hierarchy between those policy instruments and policy outcomes. Orthodox macroeconomic policy is demonstrated in Figure One.

Figure One: UK Macroeconomic Policy Orthodoxy



The role of economic ideas in orthodox macroeconomic policy has been influenced by Henderson's (1986) first-hand experience of UK economic policymaking. During his time as an economist at the Treasury, Henderson (Ibid) found that Whitehall generated its own information and ideas during the formulation of policy, which were far removed from the economic ideas understood by economists. Consequently, the thesis has not utilised the myriad definitions of economic ideas provided by political scientists or economists and, instead, has sought to determine how economic ideas have been interpreted and politically constructed by actors in UK economic policymaking. The historiography in Chapters Three and Four allowed us to identify several specific orthodox interpretations of economic ideas prevalent to the formulation of macroeconomic policy including internationalism, competitiveness, crowding-out and economic liberalism. When we explore change and continuity in economic ideas during our discussion of the orthodox cycle, it is to these orthodox interpretations that we refer.

Economic ideas are the most important aspect of UK macroeconomic policy orthodoxy, which accounts for their position at the apex of Figure One. The importance of economic ideas lay in how they are used and deployed in the formulation of policy. For example, Chapters Three and Four showed that orthodox interpretations of economic ideas provided individuals with world views, which ensure the selection and continuity of orthodox policy objectives, instruments and outcomes over possible alternatives. Furthermore, these orthodox interpretations allow the construction of crisis and policy narratives. Crisis narratives provide an interpretation of events and emergencies in such a way as to designate them as a crisis. Meanwhile, policy narratives seek to legitimise the implementation of economic policies as the policy solution to crisis. These two types of narratives need not be separated and can be combined in the same narrative.

The orthodox objective of macroeconomic policy is price stability. Orthodox fiscal policy instruments are those of public expenditure reduction, public expenditure restraint and/or tax increases, which are implemented to achieve the orthodox fiscal policy outcomes of the balanced or surplus budget and national debt

reduction. Orthodox monetary policy instruments are those of the Bank Rate and Open Market Operations (OMOs), which are implemented to alter credit conditions through the management of short-term market interest-rates. Furthermore, there exists an orthodox hierarchy between macroeconomic policy instruments. Here, fiscal orthodoxy ensures that the structure of market interest-rates and the cost of credit in the UK economy are not conditioned by government borrowing and an associated loss of confidence, but rather the operational decisions on the Bank Rate and OMOs taken by the Bank of England. Consequently, fiscal orthodoxy plays a supportive role to orthodox monetary policy instruments in the pursuit of the orthodox objective of price stability.

The Orthodox Cycle in UK Macroeconomic Policymaking

The opening chapters of the thesis established a second gap in our knowledge of UK economic policymaking for the need of a superior understanding of when and why UK macroeconomic policy exhibits change and continuity. This need arises from the common deployment in studies of UK economic policy of the model of punctuated equilibrium, which presents a misleading explanation of change and continuity in UK economic policymaking.

The historiography presented in Chapters Three and Four determined a pattern within UK macroeconomic policymaking, which sees the continuity of orthodox macroeconomic policy through a series of distinct phases. The identification of this historical pattern has allowed for the formulation of a new conceptual framework of the orthodox cycle, which seeks to provide a superior understanding of when and why UK macroeconomic policy exhibits change or continuity and is demonstrated in Figure Two. In contrast to the model of punctuated equilibrium, the orthodox cycle recognises significant continuity of orthodox macroeconomic policy and ideas, rather than radical policy and ideational change, in the aftermath of crises. Each of the distinct phases in the orthodox cycle are governed

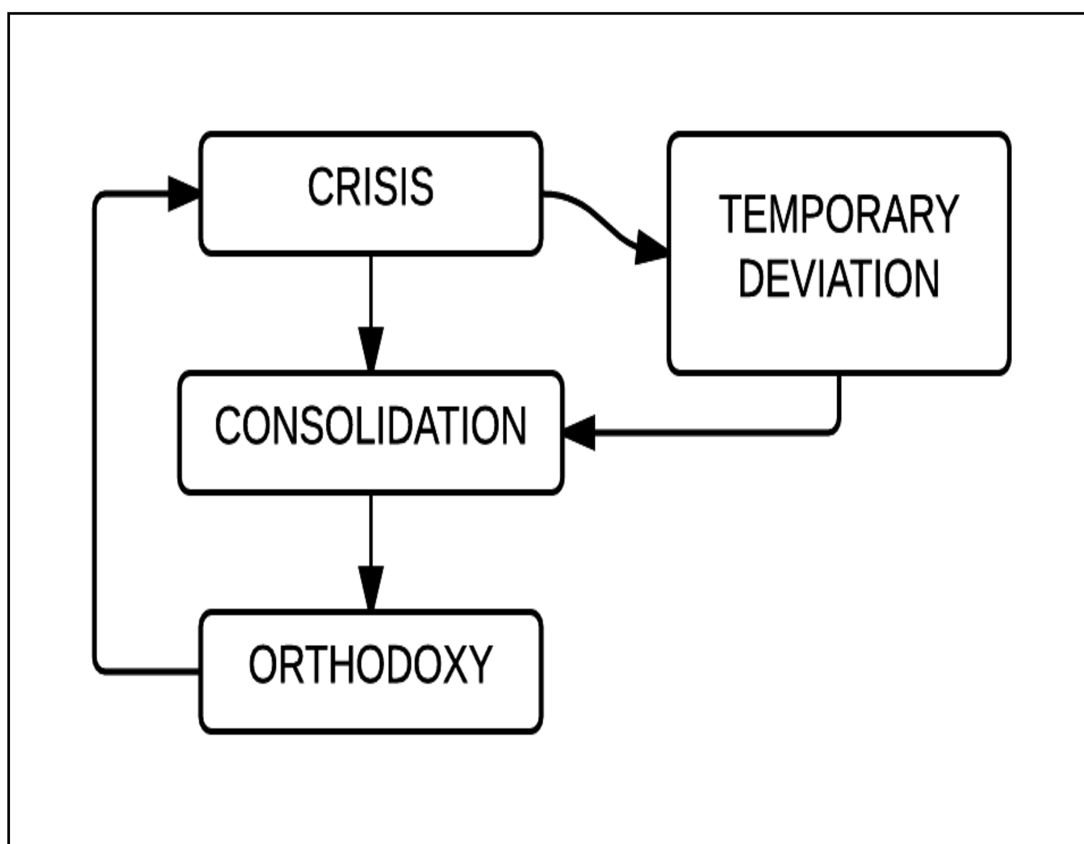
by their own dynamics, which explain when and why continuity or change occurs in macroeconomic policy and ideas. The historical precedence for each of these phases in UK macroeconomic policymaking is available in Figures Three to Six, which also provide examples of the dynamics of each phase referred to in subsequent discussion. There is no fixed timeframe for each phase of the cycle and each phase could last for consecutive months or years. In addition, fiscal and monetary policymaking can operate at different speeds and paths through the phases of the orthodox cycle. Finally, the orthodox cycle operates irrespective of the political party in government.

The orthodox cycle however does not seek to challenge existing explanations of the role of institutions in the formulation of policy, except to note that the return to orthodox macroeconomic policy can be supported in the consolidation and orthodoxy phases by the creation of new institutions and operational changes to the formulation of macroeconomic policy. Consequently, the orthodox cycle does not explain the process by which policy decisions are formulated or implemented via an in-depth analysis of the inner working of institutions. Nor does the orthodox cycle explain how established interests influence the policymaking process and policy outcomes. As a result, the orthodox cycle does not elucidate from where in the policymaking process the return to orthodoxy is generated, or the motivation of institutions and interests in returning macroeconomic policy to orthodoxy. The explanatory potential of the orthodox cycle focuses narrowly on the when and why of change and continuity in macroeconomic policy and ideas.

The research presented in this thesis therefore represents only the first step in an on-going research agenda, which will be addressed in more detail in the concluding chapter. However, at this juncture, it is worthwhile indicating that a future research agenda will include analysis of the role of institutions and interests in the orthodox cycle. Otherwise, the orthodox cycle is open to the same criticism directed at the stages, evidence-based (EBP) and state-centric models of public policymaking, which were identified in Chapter Two. In particular, criticism could be directed at the orthodox cycle pertaining to its ordered view of the policymaking process, which excludes analysis of the number, type and motivations of institutions

and interests involved in making policy. Despite the potential for criticism, the orthodox cycle is significantly different from those models of policymaking previously mentioned even without an examination of the role of institutions and interests. For example, the orthodox cycle accentuates the critical role played by economic ideas and politics – through crisis and policy narratives – in macroeconomic policymaking. Consequently, the orthodox cycle does not present the policymaking process as a technocratic exercise.

Figure Two: The Orthodox Cycle in UK Macroeconomic Policymaking



The first phase in the orthodox cycle is the crisis phase. The crisis phase consists of a series of events and emergencies, which are interpreted and designated as crises by

narratives. Therefore, crises are considered endogenous constructions through politics and the crisis phase is initiated when a narrative or narratives are deployed, which attempt to designate an event or emergency as a crisis. At this juncture, politicians and policymakers have to make a decision pertaining to the formulation and implementation of macroeconomic policies to counteract the crisis phase. The macroeconomic policy or strategy implemented by politicians and policymakers to overcome the crisis phase will determine the subsequent path that is taken in the orthodox cycle. Finally, when the events and emergencies of the crisis phase occur in the financial markets, orthodoxy includes financial interventionism to protect financial institutions and markets from collapse.

The second phase of the orthodox cycle is the temporary deviation phase. The temporary deviation phase is initiated at the moment of implementation of an 'unorthodox' macroeconomic strategy, which consists of the use of 'unorthodox' policy instruments that leads to 'unorthodox' policy outcomes in economic performance. Consequently, the main impact of temporary deviation phase lay in the relationship between policy instruments and policy outcomes. Furthermore, the temporary deviation phase will see a deployment of a policy narrative, which seeks to legitimise the 'unorthodox' macroeconomic policy strategy as the policy solution to the crisis phase.

This phase explains that change in UK macroeconomic policy occurs only temporarily in the aftermath of crises, which do not provide the stimulus for permanent radical change in policy or ideas as explained by punctuated equilibrium. The temporary nature of change in macroeconomic policy and ideas accounts for the position of the temporary deviation phase outside of the linear structure of the orthodox cycle. Furthermore, the position of the temporary deviation phase in the orthodox cycle represents one further element of the pattern identified in UK macroeconomic policymaking in Chapters Three and Four. Specifically, the temporary deviation phase may not occur at all as macroeconomic policymaking directly enters the consolidation phase of the orthodox cycle.

There do remain certain elements of the temporary deviation phase, however, that require further analysis to fulfill the explanatory potential of the orthodox cycle in understanding change and continuity in UK macroeconomic policymaking. For example, historiography in Chapters Three and Four did not explicate the role of ideas in the temporary deviation phase. Thus, it is not yet understood whether the formulation of 'unorthodox' macroeconomic strategies rests on anything more substantial – such as the adoption of 'unorthodox' economic ideas - than expediency in the face of significant events and emergencies that requires policy action. This was certainly the case for the phase of temporary deviation in response to the events and emergencies of the First World War. Further analysis on this point is required to fully explore its explanation of change and continuity in macroeconomic policy, which will be conducted in subsequent case-study on contemporary macroeconomic policymaking after the 1st May 1997.

The third phase in the orthodox cycle is the consolidation phase. Dependent on the macroeconomic strategy implemented to overcome the crisis phase, the consolidation phase occurs either immediately after the crisis phase or after the phase of temporary deviation. The consolidation phase is initiated when a macroeconomic policy strategy is implemented that deploys orthodox policy instruments, which are used to create the economic conditions necessary to secure a later return to orthodox fiscal policy outcomes or the orthodox objective of price stability. The implementation of orthodox policy instruments during the consolidation phase will, at least in part, arise from a resurgence of orthodox economic ideas in the formulation of policy. Furthermore, the consolidation phase can see the creation of new institutions or operational change to the formulation of macroeconomic policy, which support the implementation of orthodox macroeconomic policy instruments. Therefore, new institutions and operational changes during the consolidation phase are not designed to formulate radical macroeconomic policy change, but rather are used to ensure the consolidation of orthodoxy. The consolidation phase will also see the deployment of a policy narrative that legitimises the implementation of orthodox policy instruments as the policy solution to crisis.

This phase of the orthodox cycle represents a consolidation of macroeconomic policy orthodoxy, rather than the return to orthodoxy, for several reasons. First, in terms of economic performance, the consolidation phase will see a continued departure from orthodox objectives and outcomes. The explanatory emphasis of the consolidation phase is to accentuate that orthodox policy instruments are implemented to tackle these economic problems the departure from orthodoxy in economic performance. Second, the implementation of orthodox policy instruments may occur alongside policy instruments, which can be classed as 'unorthodox'. However, if these 'unorthodox' policy instruments are implemented, rather than providing the basis for subsequent radical macroeconomic policy change, they are deployed to assist orthodox macroeconomic policy instruments in creating the economic conditions necessary for a return to orthodox macroeconomic policy outcomes. Furthermore, they are only implemented in macroeconomic policy for a time-limited period during the consolidation phase and do not become permanent features in the macroeconomic policy instruments implemented by the Treasury and the Bank of England.

The fourth phase in the orthodox cycle is the orthodoxy phase, which can be initiated by two factors. First, it may be initiated by a significant event, which serves to institutionalise orthodoxy within the macroeconomic policymaking process even if economic performance has not returned to the orthodox objective of price stability or the orthodox fiscal policy outcome of the balanced budget and national debt reduction. Second, it may be initiated through economic performance, which could include a return to the orthodox policy objective of price stability or the orthodox fiscal policy outcomes of a balanced budget and the reduction of national debt. If monetary and fiscal policymaking resides in the orthodoxy phase at the same time, then the orthodoxy phase will consist of the restoration of the full framework of orthodox macroeconomic policy in policymaking. However, monetary and fiscal policymaking can move through the orthodox cycle at different speeds and it is possible for one to reside in the orthodoxy phase without the other. In such circumstances, the orthodoxy phase will consist of a return to orthodoxy in that

particular realm of policymaking, which would include evidence of orthodox economic ideas in the formulation and implementation of macroeconomic policy.

The orthodoxy phase can also see the creation of institutions or operational changes to the formulation of macroeconomic policy, which support the implementation of orthodox macroeconomic policy. Therefore, as in the consolidation phase, the purpose of these new institutions or operational changes to the formulation of macroeconomic policymaking is not to affect a departure from policy orthodoxy, but rather lead to the continuity of orthodox macroeconomic policy. The orthodoxy phase will also see the deployment of a policy narrative that seeks to legitimise the return to orthodox macroeconomic policy. Finally, if fiscal policy responds to a downturn in growth in the UK economy via the automatic stabilisers then fiscal policymaking is not considered to have left the orthodoxy phase for the reasons discussed in Chapter Four.

Figure Three: The Historical Precedent for the Orthodox Cycle in UK Macroeconomic Policymaking from 1914-1929

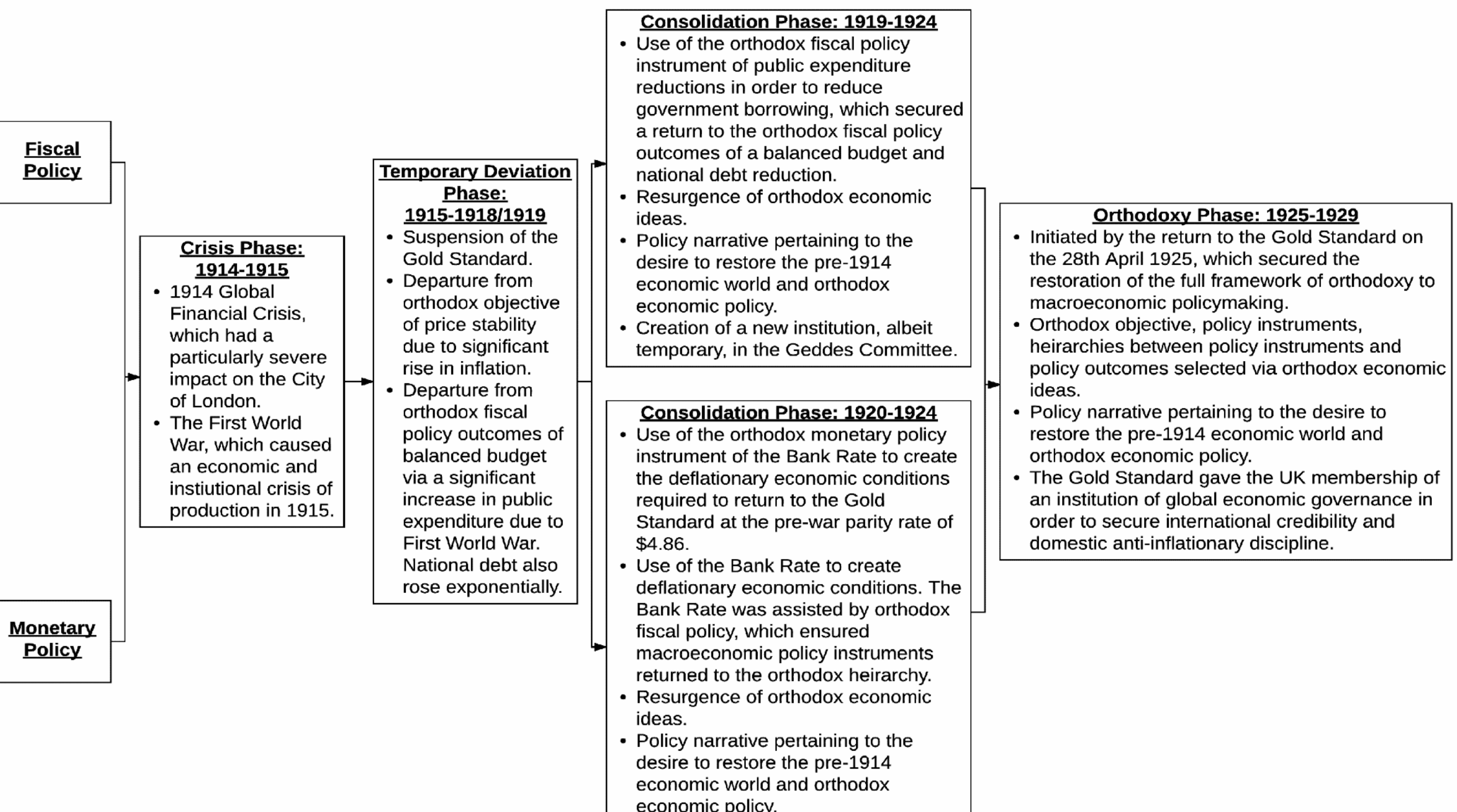


Figure Four: The Historical Precedent for the Orthodox Cycle in UK Macroeconomic Policymaking from 1929 to 1934

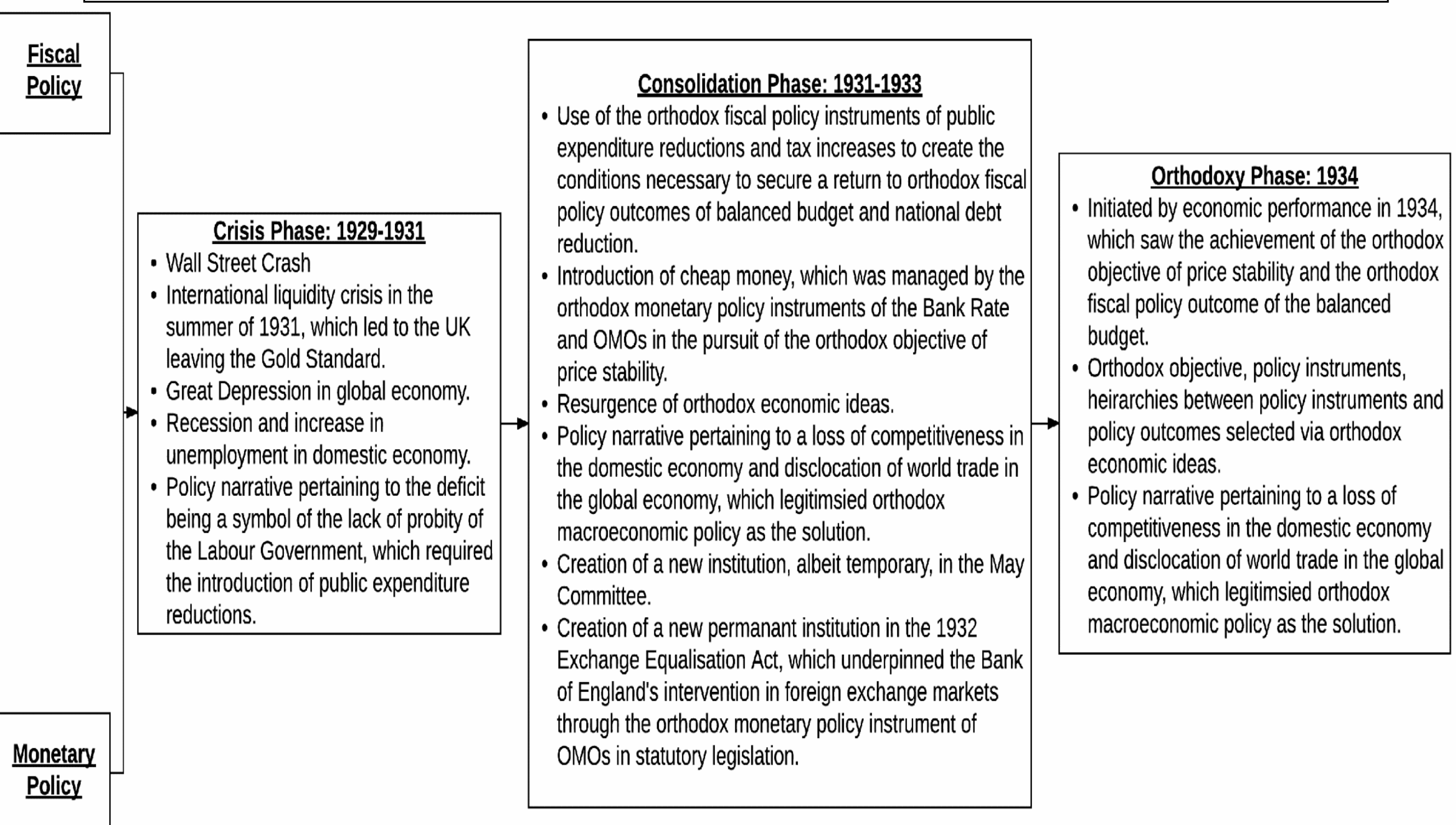


Figure Five: The Historical Precedent for the Orthodox Cycle in UK Macroeconomic Policymaking from 1974 to 1990

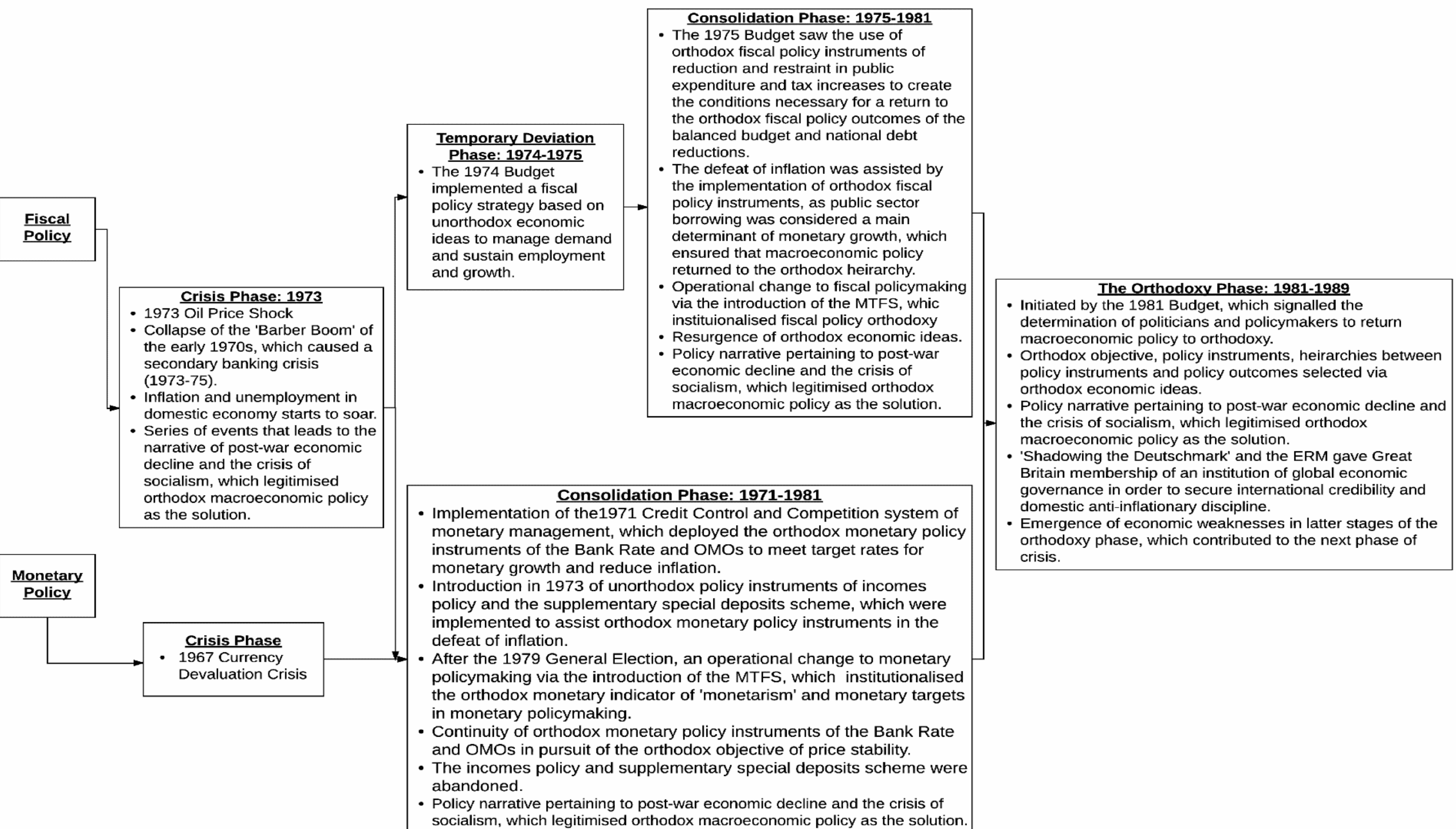
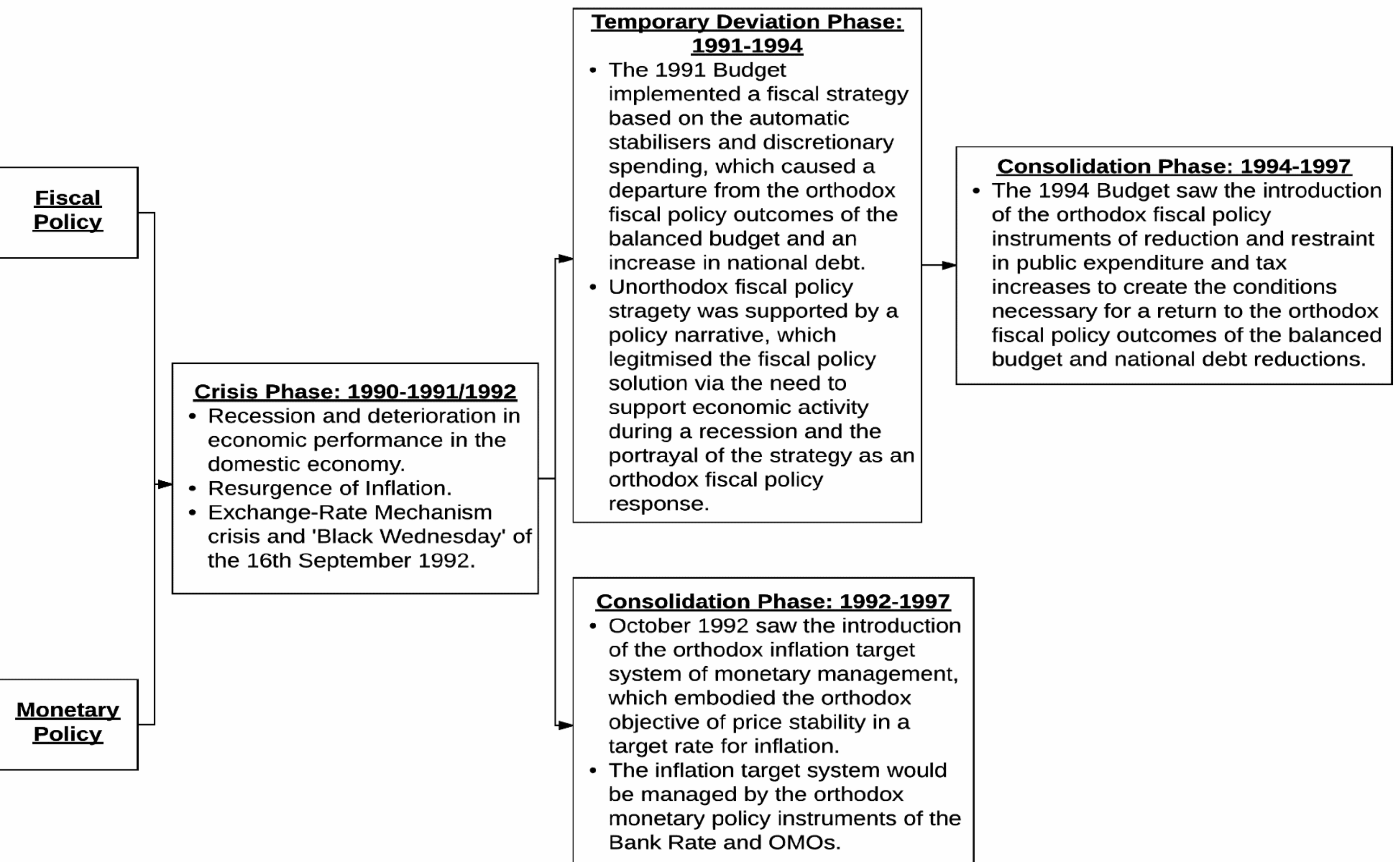


Figure Six: The Historical Precedent for the Orthodox Cycle in UK Macroeconomic Policymaking from 1990 to 1997



Methodology

This thesis has been split into two halves, which both serve a different but related purpose. So far, this chapter has re-stated the contribution of the first half of the thesis provided by literature reviews and historiography of UK macroeconomic policymaking, which established gaps in our existing knowledge and allowed the conceptual framework of the orthodox cycle to emerge. The second half of the thesis will apply the orthodox cycle to UK macroeconomic policymaking via a series of case-studies to see whether it provides a superior understanding and explanation of change and continuity in UK macroeconomic policy than that furnished by punctuated equilibrium. The methodology chapter has been strategically positioned at this juncture for two reasons. First, to avoid ambiguity and to clearly demarcate the unique contributions that both halves of the thesis offer. Second, as a consequence of methodology, which will be discussed in the research design section of this chapter. Consequently, the rest of this chapter will discuss the methodology and methods adopted in the historiography and case-study chapters.

Research Design

The research design of the first half of the thesis took the form of critical literature review and historiography of UK economic policymaking. Historiography is the writing of history based on the examination and analysis of sources, which are synthesised into a narrative. Historiography was selected as an appropriate research design for Chapters Three and Four because Chapter Two highlighted that scholars who have identified continuity in UK economic policy after the Global Financial Crisis have done so only from the perspective of policy immediately preceding the crisis. Thus, the chance to draw wider understanding on the reasons for change and continuity from UK economic policymaking during earlier economic crises had been lost. Consequently, Chapter Three and Four provided historiography of UK

economic policymaking in response to major economic crises in the Twentieth century with particular focus placed on macroeconomic policy.

At its simplest, Venn (2016) contends that historiography is the explaining of past events. However, Venn highlights that the process of providing an 'explanation' is complicated by the fact that history is not governed by covering laws as in natural world of physics. For example, Venn (Ibid) illustrates his point by claiming that historians have shown that the proposition that 'stable prices and full employment cannot exist at the same time' depends entirely upon the definition of full employment. Consequently, Venn (Ibid) concludes that the problem with historical laws is that one counter-example is enough to provide disconfirmation and subsequently historians often content themselves with discovering historical relationships based not on laws and absolute certainty, but rather high degrees of 'possibility' and 'plausibility'. Nevertheless, Venn (Ibid) posits that historiography still plays an important role as a research method because it is still useful to know whether an outcome is certainly, or even just likely, to happen.

Whilst the historiography and case-study chapters present a body of evidence that suggests the orthodox cycle provides a 'possible' and 'plausible' explanation of change and continuity in UK macroeconomic policymaking, the orthodox cycle is claimed as neither a historical law nor theory. Instead, the orthodox cycle is considered a conceptual framework, which provides an analytical tool for understanding and explaining change and continuity in UK macroeconomic policy. One reason why the orthodox cycle is considered a conceptual framework is because of existing limitations in the study – some of which have already been identified in the introduction and earlier in this chapter – that need to be addressed by a future research agenda. For example, historiography in this thesis did not include examination of the UK economic policymaking in the post-war era from 1945-1974. Whilst this period of UK economic history was neglected because of the absence of a major economic crisis during this period, the application of the orthodox cycle to this historical period would test and strengthen its explanation of change and continuity. Similarly, the historical period prior to 1914 was only given brief attention in Chapter Three and a future research agenda would require more systematic analysis

of the change and continuity in UK macroeconomic policy dating back to the 1688 Glorious Revolution and 1694 Bank of England Charter.

The final reason that the orthodox cycle is considered a conceptual framework is a matter of methodology. Given the previous discussion on the lack of certainty in historiography and historical laws, inductive reasoning was selected as the most suitable methodology for historiography. Inductive methodology involves making specific observations on a subject, in this case change and continuity in UK macroeconomic policymaking, which are then developed into broader generalisations. Consequently, inductive methodology begins with specific observations and pattern detection, proceeds to the formulation of tentative hypothesis that can be explored in greater depth and ends with conclusions that are deemed probable on the given evidence. In contrast, deductive methodology starts with a theoretical or hypothetical assertion, which is then tested by the collection of data that allows research to draw a definitive and certain conclusion via confirmation or rejection of theory or hypothesis.

The adoption of an inductive methodology has determined the structure of the thesis in the following manner. The critical literature review in Chapter Two identified a gap in our current knowledge of UK economic policymaking. Inductive methodology then allowed Chapters Three and Four to make the observations of UK macroeconomic policymaking in different historical periods, which led to the two research findings and research question presented in this chapter. Chapters Six to Nine provide further exploration of UK macroeconomic policymaking in the contemporary era and produces a body of evidence that will answer the research question.

The strategic positioning of this methodology is a consequence of the decision to adopt an inductive methodology, which would not have been possible had the methodology chapter been placed earlier in the thesis structure. For example, had the methodology chapter been placed at Chapter Three, prior to any historiography, it would have necessitated the assertion of a theoretical proposition or hypothesis on change and continuity in UK economic policymaking based on the literature review

conducted in Chapter Two, which would then require testing in subsequent chapters. Thus, it would have meant the adoption of a deductive methodology unsuited to the historiography of UK macroeconomic policymaking that Chapter Two demonstrated was necessary to gain a broader understanding of the dynamics of change and continuity. For example, had deductive methodology been adopted, which does not include the process of specific observation and pattern detection of a subject that were integral to the identification of the orthodox cycle in UK macroeconomic policymaking, then the research findings presented in this chapter may not have been identified.

Consequently, the historiography in previous chapters is far from mere background, context or preamble. Indeed, it is of vital importance to answering the research question. First, the historiography allowed the orthodox cycle to emerge, which provides us with an analytical tool for organising our understanding and explanation of change and continuity in UK macroeconomic policymaking distinct from that furnished by punctuated equilibrium. Second, the historiography provided a body of evidence that suggested the orthodox cycle provided a 'plausible' or 'possible' explanation of change and continuity. Third, the historiography allowed the establishment of a research question that enables us to provide further testing of that 'plausible' or 'possible' explanation. Indeed, without the inductive methodology in the historiography the research question would not have been possible, which leads us back to the argument pertaining to the strategic positioning of this chapter. Fourth, the conceptual framework of the orthodox cycle developed in the historiography aided the organisation of empiric research presented in subsequent chapters.

The research design in the second half of the thesis takes the form of multiple case-studies of UK macroeconomic policymaking, which begin with the election of Tony Blair, Prime Minister (1997-2007), and New Labour on the 1st May 1997 and end with the resignation of David Cameron, Prime Minister (2010-2016), on the 13th July 2016.

A case-study research design was selected as appropriate because it provides continuity in research design throughout the thesis. For example, Yin (2014:12,16)

highlights the overlap between historiography and case-study research designs, which both deal with phenomenon and context and rely on many of the same techniques of data collection and data analysis. Thus, Yin (2014:12) posits historiography is the preferred research design when no direct observation, control or access to events is possible and when relevant persons to the case are no longer alive to report on what occurred. Meanwhile, case-study is the preferable research design to study contemporary events.

The case-study research design was also chosen because it is suited to the research question. For example, Yin (2014:51) notes that the selection of a case-study research design is justified when that case is 'critical' to a hypothesis or theoretical proposition; especially, in instances when a hypothesis or theory have specified a clear set of circumstances upon which its propositions are believed to be true. In these circumstances, Yin (Ibid) highlights that case-studies 'can be used to determine whether the propositions are correct or whether some alternative set of explanations might be more relevant'. Although the discussion of methodology has established that the orthodox cycle is a conceptual framework, rather than theory, the same justification for a case-study research design can be applied to concepts. For instance, the conceptual framework of the orthodox cycle has sought to establish the dynamics, through a series of distinct phases in UK macroeconomic policy, upon which it believes change and continuity in macroeconomic policy and economic ideas is probable. Consequently, a case-study research was considered apt for a research question, which seeks to establish whether the orthodox cycle provides a superior understanding and explanation of change and continuity in UK macroeconomic policy than that furnished by punctuated equilibrium.

Meanwhile, the breadth in time covered by the multiple case-studies of UK macroeconomic policymaking was purposefully selected to ensure that the research design was 'longitudinal'. Yin (2014:57) defines a 'longitudinal' research design as the use of single or multiple case-studies to examine and observe the same case at two or more different points in time. Furthermore, Yin (Ibid) declares that a longitudinal research design is vindicated in two circumstances. First, when a case-study will test a concept that specifies how certain conditions and their underlying

processes can change over time. Second, Yin (Ibid) posits that a longitudinal research design is justified when the time period chosen for the case study reflects the anticipated stages at which change could reveal themselves.

The first reason that a 'longitudinal' research design was selected for the second half of the thesis is to ensure the multiple case-study of UK macroeconomic policymaking adopt what Yin (2014:57) describes as 'a before and after logic' and allows examination of the case 'prior to and then after some critical events' in relation to the Global Financial Crisis of 2007-2009. Thus, it was a purposeful decision to design a 'longitudinal' research project that placed the first major economic crisis of the Twenty-First Century near the centre of the time-period covered by the multiple case-studies. Furthermore, the decision to select 'longitudinal' cases ensured uniformity with previous historiography in that it allowed the examination of macroeconomic policymaking and economic ideas during governments, either in the majority or Coalition, of the three major UK political parties: Labour (1997-2010), Conservative-Liberal Coalition (2010-2015) and Conservatives (2015-2016).

The second reason that a 'longitudinal' research design was chosen for the second half of the thesis is that it provides a broad period in UK macroeconomic policymaking (1997-2016) for change in policy and ideas to become apparent. If the case-study research design had not been 'longitudinal' then changes in policy and ideas may not have been as easily observed in the data. Alternatively, it could have meant that temporary changes in policy and ideas were over-emphasised in the data. In either way, the 'longitudinal' research design should alleviate any potential bias in the data in favour of the orthodox cycle or punctuated equilibrium. Similarly, the placing of the Global Financial Crisis of 2007-2009 near the centre of the time-period covered by the multiple case-studies should allow change and continuity in policy and ideas to be evident in the data and ensures that the orthodox cycle and punctuated equilibrium have equal opportunity to understand and explain those developments.

Research Methods

The research methods in the historiography and case-study chapters are both qualitative and quantitative. Despite claims to the contrary, McQueen and Knussen (2002:196) highlight that qualitative and quantitative data methods need not be in direct opposition to one another and can be deployed within the same study. Thus, Matthews and Ross (2010:142) suggest that mixed methods is best thought of as combining the collection, analysis and presentation of qualitative and quantitative data in a manner best for a research project. Similarly, Bryman (2012:628) contends that a mixed methods project should be understood as a research agenda that integrates both qualitative and quantitative research.

Bryman (1988:128) identifies, however, that within research projects that adopt mixed methods, it is rare that each method is given equal weight. Indeed, Bryman (Ibid) suggests that it is more usual for there to be a dominant research method with the results from data analysis in the dominant method buttressed by data from the subordinate method. This is certainly the case in this thesis where the dominant research method has been qualitative. Thus, in the historiography and case-study chapters, data from qualitative methods have then been supported by the selective use of quantitative data from UK institutions such as the *Office of National Statistics* (ONS) and *Office of Budget Responsibility* (OBR). Furthermore, Bryman (1988: 68, 129) provides a line of defence for the deployment of mixed methods that is particularly important for this thesis, namely, that mixed methods has gained support in American policy studies as the appropriate methodological strategy for examining policy change. Moreover, McQueen and Knussen (2002: 22) note that case studies are particularly well suited to use both qualitative and quantitative data.

Data Collection

Yin (2014:105-108) posits that qualitative data is usually derived from sources such as documentation, archival records, interviews, direct observations, participant observations and physical artifacts. Unfortunately, because the topic of our historiography and case-study is UK macroeconomic policymaking, some of these qualitative sources of data collection are unavailable. For example, direct or participant observation of the macroeconomic policymaking process at the Treasury and the Bank of England is not possible. Neither does the macroeconomic policymaking process commonly produce physical artifacts in the manner suggested by Yin. Meanwhile, Burnham and colleagues (2008: 189) note that in the face of access problems to primary documents, political scientists instead often focus on data from elite interviews complimented by secondary and tertiary documents. However, the problem of data accessibility was quite different for this research project than that outlined by Burnham. Indeed, there is readily available a wealth of accessible primary documentary sources on UK macroeconomic policymaking. In contrast, it is the accessibility to elite interviews that is more problematic.

Consequently, a decision was taken not to pursue the collection of data via elite interviews. In the case of the historiography of interwar UK economic policymaking in Chapter Three, this was out of necessity given the lapse of time and inevitable passing of the major participants. Furthermore, whilst several actors involved in UK economic policymaking in Chapter Four are still with us, many are now reaching old-age. This was no more evident than in the sad passing of Denis Healey and Geoffrey Howe within days of one another in October 2015. The accessibility to elite interviews was complicated by the fact that UK civil servants, either retired or still in service, rarely give interviews. Finally, accessibility to elite interviews was further complicated for our case-studies of contemporary UK macroeconomic policymaking by the fact that many of the actors from the 1st May 1997 onwards are still, or were until very recently, involved in active politics. The likelihood of securing interviews with such persons was deemed to be slim.

As noted previously however there is a significant array of primary documentation from both historical and contemporary periods of UK macroeconomic policymaking, which is highly accessible. For example, there is a significant array of primary documentation on UK macroeconomic policymaking, such as Treasury Budget and Pre-Budget Reports, Bank of England Inflation Reports and Budget and Pre-Budget Statements by the Chancellor of the Exchequer. Furthermore, prior to data collection, it was ascertained that primary and secondary data from civil servants at the Treasury, such as oral evidence provided to the Treasury Committee and public speeches, are a matter of public record. Indeed, accessibility to primary documentation has been aided in recent years by the digitisation of archive and government records. Moreover, where digitisation of archives has not taken place, documentation is available through in archives. Here, several trips were taken to access primary documents such as government records at the National Archives, Conservative Party archives at the Bodleian library at Oxford University and the Labour Party archives at the People's History Museum in Manchester. Thus, a decision was taken not to pursue elite interviews with such persons and instead focus on the wealth of primary, secondary and tertiary documents available from historical and contemporary periods. Consequently, this thesis has followed the advice set out by Harrison (2001:106) who states that 'in order to answer a political research question, it may be more appropriate to analyse data which already exists, rather than collect new information'.

Accordingly, the data presented in the historiography and case-study chapters has been collected exclusively from documentary and archival sources. Here, Vromen (2010:262) notes the rich tradition played by documentary and archival analysis within historiography in political science, which has been frequently deployed by sub-disciplines such as public policy, comparative politics and international relations. Thus, Vromen (Ibid) notes the substantial lineage of the 'writing of history based on selective, critical reading of sources that synthesizes particular bits of information into a narrative description or analysis of a subject' Vromen (2010:262) also identifies, however, that reliance upon documentary and archival sources presents potential problem in terms of the selection of sources. For

example, Yin (2014:109) claims that in order to not get lost within the mass of potential documentary evidence on the chosen case-study, it is vital to establish a system of triage available sources according to importance to the inquiry. Such a system, it is suggested by Yin (Ibid), ensures that more time is spent reading and reviewing documents central to the case.

The classification system of documents adopted by this thesis is one identified by Burnham (2008:187-188) as common to historians, which classifies data sources as either 'primary', 'secondary' or 'tertiary'. In this stratum, primary sources are those produced by or part of the event in question. Meanwhile, secondary sources are those related to or produced soon after an event. Finally, tertiary sources are materials written afterwards to reconstruct the event. The type of sources under this classification system, from which data has been collected for the historiography and case-study chapters, is available in Appendix One. A further stratum of time-period was then added to this classification system. For example, primary or secondary sources outside of the time period of the historiography or case-study chapters were rejected for analysis, unless they were of particular importance to the case. In total, the data for the historiography and case-study chapters was collected from 765 primary sources, 257 secondary sources and 276 tertiary sources. Finally, the breakdown of how many primary, secondary and tertiary data sources have been used in the collection of data for each individual chapter of historiography and case-study is available in Appendix Two.

The adoption of this classification system had an advantage in that it allowed data collection to allocate prioritisation given to primary sources. This is particularly important for historiography and case-studies of UK macroeconomic policymaking because government records are the most single important source of information for those interested in policymaking (Lowe, 1997: 240). Furthermore, Lowe (1997: 200-201, 240-241) contends that government records 'allow careful researchers the opportunity to make good gaps in knowledge', 'make a decisive contribution to understanding change over time' and also to understand 'what did not change'.

Data Analysis

Matthews and Ross (2010:282) identify that whilst there are many ways of interpreting and analysing documents are available, the simplest (but perhaps most time consuming) is close reading of the document. Here, a thematic approach to the analysis of data was applied. Grbich (2007:16) describes thematic analysis as 'a process of segmentation, categorization and relinking of aspects of the data prior to final interpretation'. Matthews and Ross (2010: 373-374) outline the process of thematic analysis. First, the raw data from each source is categorized according to several broad themes. The themes applied in data analysis conducted for the historiography and case-study chapters is available in Appendix Three. The raw data from each theme is then arranged alongside each other, which helps to uncover meanings, relationships, similarities and differences to emerge. Here, Matthews and Ross (Ibid) contend that the thematic approach allows analysis to remain in touch with raw data, which allows a constant process of re-appraisal, checking of interpretations and making links between different aspects of data to occur.

The classification system provided a further advantage in that it allowed for the 'triangulation' of data analysis to occur at each level of the primary, secondary and tertiary data (Pierce,2008:90). The triangulation of data is important because the use of documentary sources is not without its pitfalls. For example, Yin (2014: 105-108) points out that documents are not always accurate and can be biased and they are often written for a specific purpose other than that required by the researcher. Similarly, (Pierce, 2008: 81) highlights that all primary sources include some degree of bias, perception and interpretation. In contrast, Gamble (2002: 150) identifies the difficulty in using tertiary sources alone when he noted that it would be 'almost impossible to trace the evolution of policymaking through the use of biographies alone'. Thus, Burnham and his fellow authors (2008: 195) suggest that secondary and tertiary documents are 'most effectively employed in combination… with the analysis of primary documents'.

Conclusion

This chapter has outlined the methodology employed by this thesis and specified the research question, which the following case-study chapters will answer. The chapter began by re-stating the two research findings derived from the historiography of UK macroeconomic policymaking. The chapter then established methodology and methods. For example, the chapter determined that the thesis has adopted an inductive methodology. Furthermore, the chapter has explained that the data collected for the historiography and case-study chapters has been collected exclusively from documentary and archival sources. Here, a classification system was employed, which classed sources according to a primary, secondary or tertiary status. The chapter continued to explain that the data collected from these sources was analysed according to a thematic approach. The following chapter will present a case-study of change and continuity in UK macroeconomic policy from the 2nd May 1997 to the 6th June 2001.

Chapter 6

Change and Continuity in UK Macroeconomic Policymaking during the Blair Government of the 1st May 1997 to the 6th June 2001

Introduction

This chapter consists of a case-study of United Kingdom (UK) macroeconomic policymaking from the 2nd May 1997 to the 6th June 2001, which encompasses the first government of Tony Blair, Prime Minister (1997-2007). The purpose of the case-study is to see whether the orthodox cycle provides a superior understanding and explanation of change and continuity in UK macroeconomic policy than that furnished by punctuated equilibrium. According to model of punctuated equilibrium, radical change in policy, ideas and institutions occur via exogenous and endogenous shocks to the policymaking process. Endogenous shocks that produce radical change include the election of a new government. Therefore, the general election victory of New Labour on the 1st May 1997, after eighteen years of Conservative government, should have provided an endogenous shock to the macroeconomic policymaking process sufficient to provide radical change in policy, ideas and institutions. In contrast, the orthodox cycle is able to explain that, whilst the New Labour government did make significant changes to the institutional and operational framework for macroeconomic policymaking during the 1997-2001 Parliament, rather than engender radical departure in policy and ideas, the election of New Labour led to the continuity of orthodox macroeconomic policy.

This chapter concludes that the orthodox cycle provides a superior understanding and explanation of change and continuity that than furnished by punctuated equilibrium for two reasons. First, the orthodox cycle allows us to locate a significant event, which initiated an orthodoxy phase in UK macroeconomic policymaking. This significant event was the 6th May 1997 announcement by Gordon Brown, Chancellor of the Exchequer (1997-2007), that the Bank of England would be granted operational responsibility for setting interest-rates, which formed part of a new framework for monetary policymaking. Second, the orthodox cycle explains that the new framework for macroeconomic policymaking created after the election of New Labour, rather than leading to radical change in policy and ideas, served to institutionalise orthodox macroeconomic policy in the formulation of policy. Consequently, the 1997-2001 Parliament saw the restoration of the full framework of orthodox macroeconomic policy, which is in accordance with what we should expect when monetary and fiscal policymaking reside in the orthodoxy phase of the orthodox cycle at the same time.

The chapter will be organised in the following manner. The first section of the chapter focuses on both monetary and fiscal policymaking. It will begin by documenting the institutional additions and operational changes to the formulation of monetary policy made on the 6th May and 12th June 1997. The chapter will proceed to demonstrate that the new monetary policy framework, rather than instituting a period of radical change and departure in monetary policy, led to the continuity of orthodox monetary policy. The chapter will then continue to introduce the institutional additions and operational changes made to the formulation of fiscal policy. Again, the chapter will demonstrate the continuity of orthodoxy in fiscal policy after the election of New Labour, rather, than radical change and departure.

The following section of the chapter focuses exclusively on the role of economic ideas. It opens by considering the economic idea of globalisation and its importance to macroeconomic policymaking from the 2nd May 1997. Here, the chapter posits that globalisation is the modern expression of the traditions and discourse associated with the orthodox economic idea of internationalism. The chapter then proceeds to chart the continuity of the orthodox economic ideas of

competitiveness, crowding-out and economic liberalism. During the discussion of the economic ideas of globalisation and crowding-out their critical role in the creation of the new institutional framework for macroeconomic policymaking is highlighted. Furthermore, it is identified that orthodox economic ideas were important in the formulation and implementation of policy in three key areas, which produced continuity of orthodox macroeconomic policy. First, the implementation of a five-year deficit-reduction plan. Second, the assignation of an orthodox hierarchy between macroeconomic policy instruments, which saw fiscal policy play a supportive role to monetary policy. Third, the rejection of discretionary fiscal strategies of demand management and the establishment of a division of responsibility in economic policymaking between macroeconomic and microeconomic policy, which assigned to macroeconomic policy the objective of economic stability. Here, the chapter identifies that economic stability was defined and measured via the orthodox objective of price stability. Finally, the chapter will highlight how the creation of the new macroeconomic policymaking framework was supported by the deployment of a policy narrative.

The Orthodoxy Phase in UK Macroeconomic Policymaking after the 1997 General Election

New Labour inherited on the 2nd May 1997 a macroeconomic policymaking process firmly lodged in the consolidation phase of the orthodox cycle. Chapter Four outlined that the early 1990s saw the reemergence of a crisis phase in macroeconomic policymaking as the UK economy entered recession. Furthermore, speculative pressure on Sterling from financial markets culminated in 'Black Wednesday' of the 16th September 1992 and the ejection of the UK from the European Exchange-Rate Mechanism (ERM). Fiscal policymaking left the crisis phase and entered the temporary deviation phase of the orthodox cycle at the 1991 Budget, which saw the implementation of an 'unorthodox' fiscal policy strategy to overcome crisis that

involved – albeit at a modest level – discretionary public spending. The temporary deviation phase in fiscal policymaking was maintained until the 1994 Budget, when fiscal policymaking entered a phase of consolidation as public spending restraint and tax increases secured a downward trajectory in government borrowing and national debt as a percentage of GDP. Meanwhile, monetary policymaking responded to the crisis phase by immediate entry into the consolidation phase after the UK's ejection from the ERM. This consolidation phase was initiated by the introduction of the inflation target system in October 1992, which embodied the orthodox macroeconomic policy objective of price stability in a target rate for inflation and was implemented via the orthodox monetary policy instruments of the Bank Rate and Open Market Operations (OMOs). This chapter will show that rather than introduce radical change from this policy inheritance, New Labour initiated an orthodoxy phase in macroeconomic policymaking.

The first major public act of Gordon Brown's (1997a) Chancellorship was to announce in a press conference at the Savoy Hotel, London, on the 6th May 1997 that the Treasury would cede operational responsibility for setting interest-rates in the UK economy to the Bank of England. Indeed, Brown only told Edward George, Governor of the Bank of England (1993-2003), of the decision in a morning meeting between the pair prior to the press conference. At this meeting, Brown (1997) presented George with a letter, which established a new operational remit for the formulation of monetary policy. Henceforth, the Bank of England would set interest-rates in the UK economy according to an annual target for inflation of 2.5% RPIX[70], which replaced the '2.5% or below' target set by Kenneth Clarke, Chancellor of the Exchequer (1993-1997), in the 1995 Budget. Furthermore, the letter set out that the objective for monetary policy was still price stability, embodied in the inflation target, and that without prejudice to this objective, monetary policy could support the government's objectives for growth and employment. This new operational remit for monetary policymaking was given statutory underpinning in the 1998 Bank of

[70] RPIX stands for Retail Prices Index excluding mortgage payments.

England Act (2015i:20-80) and was subsequently affirmed in each subsequent Budget Statement delivered by Brown (1997d;1998;1999;2000a;2001).

This was not the only change, however, to the framework for monetary policymaking established on the 6th May 1997. For example, Brown's (1997) letter to George had also signalled the creation of a new institution to reside within the Bank of England called the Monetary Policy Committee (MPC), which would be responsible for operational decisions and the implementation of interest-rate policy. The MPC would comprise of the Governor of the Bank of England, two Deputy-Governors, two Bank of England officials and four external members who would be appointed by the Chancellor of the Exchequer. Decisions pertaining to the Bank Rate would be made by majority vote and in cases of a tie the final decision would be made by the Governor.

The final operational change to the formulation of monetary policy was to make the inflation target both symmetrical and flexible. The new symmetrical and flexible inflation target system was established in a Treasury (1997b) paper released on the 12th June 1997 entitled *Remit for the Monetary Policy Committee*. The inflation target was made symmetrical via the introduction of trigger points 1% either side of the 2.5% RPIX target. Thus, if inflation was to rise above 3.5% or fall below 1.5% RPIX the Governor of the Bank of England would be required to send an open letter to the Chancellor of the Exchequer explaining why, the policy action that would be taken to deal with the departure, the period within which inflation was expected to return to target and how this policy approach would meet the Bank's monetary policy objectives. This letter was to be repeated every three months that inflation remained outside of the 1% range around the inflation target. Meanwhile, the flexible inflation target was based on the recognition that economic shocks may cause the 'actual inflation target' to 'depart from its target' and that 'attempts to keep inflation at the inflation target in these circumstances may cause undesirably volatility in output'(Ibid).

The introduction of a new monetary policymaking framework just five days after the election of New Labour would seem to confirm the model of punctuated

equilibrium and its understanding of change and continuity, which links endogenous shocks to the policymaking process, such as the election of a new government, to subsequent radical institutional and policy change. However, the orthodox cycle explains that an orthodoxy phase in UK macroeconomic policymaking can be initiated through a significant event, which serves to institutionalise orthodox macroeconomic policy within the policymaking process. Here, the chapter provides two reasons pertaining to why the introduction of a new monetary policymaking framework on the 6th May 1997 should be considered a significant event.

The introduction of a new monetary policy framework on the 6th May 1997 can be claimed as a significant event because the announcement that the Bank of England would be granted operational responsibility for national interest-rates had not been signalled whilst New Labour were in opposition. Thus, as noted by Keegan (2004,155,173), the announcement was met with shock within the political establishment, Treasury, Bank of England and economic commentariat. However, of far more fundamental importance in the consideration of the 6th May 1997 as a significant event is that it returned to the Bank of England its traditional historical responsibility within UK macroeconomic policymaking for setting national interest-rates. Ed Balls[71] and Gus O'Donnell[72] (2002:85) claimed that the decision to grant 'Bank of England independence' and 'cede such a significant power as setting national interest rates to an unelected agency was politically and constitutionally innovative'. In reality, the period from 1946-1997, when the Bank of England had been nationalised and operational responsibility for the Bank Rate had been transferred to the Chancellor of the Exchequer and Treasury, was the aberration within UK macroeconomic policymaking. Indeed, prior to 1946, the Bank of England had exercised its traditional responsibility for national interest rates since the 1694 Bank of England Charter (Bank of England,2016). Therefore, Sinclair (2007:296) argued that granting operational independence for the Bank of England

[71] Ed Balls was Chief Economic Adviser to Gordon Brown and HM Treasury (1994-2004),

[72] Gus O'Donnell was Managing Director of HM Treasury Macroeconomic Policy and International Finance Division (1999-2002).

represented a step back towards 1939 or 1914 ‘when policy interest rate decisions were taken by the Governor of the Bank of England, not the Chancellor’.

The new monetary policymaking framework, however, returned to the Bank of England something more fundamental to its history than just its traditional responsibility for the Bank Rate. Specifically, the new monetary policymaking framework allowed the Bank of England to fulfill its orthodox role within macroeconomic policymaking as the guardian of monetary stability, which it had to share with the Treasury after 1946. Thus, in a speech on the 24th February 1998, George (1998a) argued that “new legislation does not fundamentally alter the Bank’s raison d’etre – our core purposes” and that the new monetary policymaking framework merely brought “new clarity to our responsibilities” for monetary stability. The return of the Bank of England to its orthodox role in UK macroeconomic policymaking is further evidenced when we consider that the new monetary policymaking framework was supported by discourse reminiscent of that advanced in favour of the return to the Gold Standard after the First World War. For example, it was claimed that Bank of England operational independence would insulate monetary policy from short-term political manipulation (Bevir,2005:109)[73].

The 6th May 1997 announcement by Gordon Brown was also a significant event because the orthodoxy phase of the orthodox cycle explains that the implementation of orthodox macroeconomic policy can be supported by the creation of institutions or operational changes to the formulation of macroeconomic policy. Consequently, the orthodox cycle explains that, rather than the election of New Labour heralding a period of radical policy change, the introduction of the new monetary policymaking framework led to the continuity of orthodox monetary

[73] The claim that operational independence for the Bank of England would bring an end to the short-term political manipulation of monetary policy was made in public speeches by Brown (1997c:1998f;1999c). Brown also presented this justification for his new monetary policy framework in oral evidence to the Treasury Committee (1997:Ev.22, Q.61,Ev.23,Q.62;1998a:Ev.65,Q.300). Moreover, this view was held by Mervyn King (1999:2), Deputy-Governor of the Bank of England (1993-2003), the Treasury in their 1997 Pre-Budget Report (1997a:11) and Balls and O’Donnell (2002:8,17).

policy. In the first instance, the new monetary policymaking framework ensured the continuity of the inflation target system of domestic monetary management, which had originally been introduced in October 1992 by Norman Lamont and the previous Conservative government. Thus, Sinclair (2007:296) classified the creation of the MPC, not as an example of radical institutional change, but ‘a logical extension of Norman Lamont’s decision to replace the broken anchor of British monetary policy… with a new monetary framework, inflation-targeting’. Furthermore, the MPC further institutionalised the continuity of orthodox monetary policy via its choice of policy instruments. Specifically, the MPC sought to achieve the inflation target and implement monetary policy through the orthodox instruments of the Bank Rate and OMOs, which had been deployed by the Treasury and the Bank of England after the introduction of inflation targeting in October 1992 and under previous monetary frameworks of the Gold Standard and monetarism.

The MPC (1998) paper entitled *The Transmission Mechanism of Monetary Policy* is crucial in understanding the orthodox operation of the Bank Rate after the creation of the MPC. In this paper, the MPC (Ibid) posited that monetary policy worked via aggregate demand, which determined the nominal or money values of goods and services (i.e. the price level). In this endeavour, the Bank Rate was the main monetary policy instrument used by the MPC, which impacted on economic activity and inflation via the ‘transmission mechanism’. Primary among the ‘transmission mechanism’ was the impact of the Bank Rate on market interest-rates[74]. For example, the MPC (Ibid) posited that if the Bank Rate was raised there would be a corresponding rise in market interest-rates, which would make credit more expensive in the UK economy. If the MPC lowered the Bank Rate the impact on market interest-rates and the cost of credit worked in the opposite direction. The cost of credit in the UK economy was claimed to influence aggregate demand by altering the relative attractiveness of saving, consumption and investment. Thus, the MPC contended that, other things being equal, increases in the Bank Rate led to higher market interest-rates, which would increase the cost of credit in the UK

[74] The MPC (1998) also noted that the transmission mechanism of the Bank Rate affected asset prices, expectations and the exchange-rate.

economy and encourage saving over consumption and investment. According to the MPC (Ibid), the corresponding reduction in aggregate demand would then translate into a lower price level (i.e. lower inflation rate).

Meanwhile, the Bank of England (1997c:204-207) had affirmed in its *Quarterly Bulletin* of May 1997 the role played by OMOs in the implementation of monetary policy[75]. Here, the Bank of England (1997c:204) explained that it helped the UK banking system manage its liquidity effectively 'through open market operations conducted on a transparent basis in prime-quality market instruments'. However, this was not the primary aim of the Bank's operations in Sterling money markets, which was 'to steer short-term market interest-rates' (Ibid). It was through the provision of liquidity to the UK banking system, via the orthodox monetary policy instrument of OMOs, that the Bank of England could marry policy instrument with objective, primarily, because the price at which the Bank of England provided liquidity to the banking system through OMOs 'exert[ed] a powerful influence on short-term market rates, steering them to a level consistent with official monetary policy' set by the MPC in the Bank Rate (Ibid). The Bank of England conducted its OMOs through repo (sale and repurchase agreements) and outright purchases of financial instruments such as gilts, Treasury foreign currency debt and eligible bills (Treasury bills, local authority bills and bank bills).

The new monetary policymaking framework also institutionalised the orthodox objective of price stability as the primary objective for monetary policy. Indeed, the formal ordering of objectives for the MPC clearly prioritised price stability over and above concerns for economic growth and employment (Allsopp,2002:2). Table One presents the annual percentage changes for RPIX and demonstrates that the nascent MPC was remarkably successful in achieving the orthodox objective of price stability after the 6th May 1997 in economic performance,

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[75] The role played by OMOs in monetary management, through the provision of liquidity to the banking system, was also affirmed by the Bank of England (1997d;187-197;1997f:256-258;1997h:336-338;1998:11-14;1998b:109-113;1998d:199-201; 1998f:309-310;1999:15-17;1999b:140-141;1999d;249-252;1999e:340-341;2000a: 20-22;2000c;129-131;2000d:228-232;2000e:331,333-338;2001:17-24;2001a:157-163) in successive *Quarterly Bulletins* between August 1997 and June 2001.

which is another indicator of the macroeconomic policymaking entering the orthodoxy phase of the orthodox cycle. Consequently, inflation targeting played the same role in monetary policymaking as had the Gold Standard and monetarism, operating as a monetary framework, which guides policymakers in operational decisions pertaining to the implementation of orthodox monetary policy instruments in pursuit of the orthodox objective of price stability.

Table One: RPIX (Excluding Mortgage Interest) Annual Percentage Change during 1997-2000

Years	**RPIX** (Annual Percentage Change)
1997	2.8%
1998	2.6%
1999	2.3%
2000	2.1%

(**Source:**ONS,2015)

The new monetary policymaking framework further institutionalised the orthodox objective of price stability in monetary policymaking when the inflation target was made symmetrical on the 12th June 1997. For example, the introduction of a '2.5% RPIX or below' target for inflation in the 1995 Budget of Kenneth Clarke had led Ed Balls to fear that monetary policymakers may purposefully provoke deflation as a means to comfortably achieve the inflation target, which would destabilise prices, growth and employment in the UK economy (Keegan,2004:168-170,179). Thus, the Treasury (1997:9) noted in its 1997 Budget Report that the symmetrical nature of the

inflation target meant that deflation or inflation in the price level had to be treated with equal merit. Consequently, monetary policymakers were more likely keep prices stable around the inflation target and thus achieve the orthodox objective of price stability.

Finally, the return of the Bank of England to its orthodox role within UK macroeconomic policymaking was maintained by the decision not to join the first-wave of Economic and Monetary Union (EMU) in Europe on the 1st January 1999, which would have meant the adoption of the Euro. Gordon Brown (1997j) announced this decision in a statement to the House of Commons on the 27th October 1997, which introduced and declared that the UK economy had failed five economic tests that it needed to pass before it was beneficial to join EMU. Those five tests included the issue of sustainable convergence between the UK and single currency economies, whether the UK economy demonstrated sufficient flexibility to cope with economic change, the effect on investment, the impact on the financial services industry and whether it was good for employment. Had New Labour decided to join EMU, however, change would have gone far beyond a new national currency and would have required the new monetary policymaking framework to be dismantled. For example, operational responsibility for setting UK interest-rates would have been transferred on the 1st January 1999 from the Bank of England to the European Central Bank.

The formulation of fiscal policy also saw a series of institutional and operational changes after the 6th May 1997. In his first Budget Statement of the 2nd July 1997, Brown (1997d) introduced two fiscal rules for policymaking. The first was the golden rule, which would ensure that current spending was balanced across the economic cycle and meant that New Labour would only borrow for capital investment. The second was the sustainable investment rule, which meant public debt would be held at the 'prudent and stable level' of 40% GDP. The new fiscal rules were codified in the 1998 Code for Fiscal Stability (HM Treasury,1998c:6,Part 2), which required the government to explicitly state its fiscal policy objectives and operating rules. Furthermore, the Code for Fiscal Stability established five principles for fiscal management, which included transparency, stability, responsibility, fairness

and efficiency. The Code for Fiscal Stability was underpinned by statutory legislation in the 1998 Finance Act.

The election of New Labour also saw the expansion of the Private Finance Initiative (PFI). The PFI had originally been introduced by the Major government in 1992, although it was pursued to a far greater extent under New Labour. The PFI allowed private sector consortiums to bid for contracts tended by government that would allow them to build, maintain and operate public facilities such as hospitals and schools. Typically, after construction, these public services were then leased back to the government for a period of two to three decades, which provided the private sector consortiums with guaranteed revenue payments and a license to provide services from the facilities they had just built (Shaw, 2007:Chp.4). One of the attractions of PFI, according to Alan Milburn (1999), Chief Secretary to the Treasury (1998-1999), was that PFI harnessed "private sector capital in public investment". Thus, Shaw (2007:90) claims that the PFI was an 'accounting trick' in terms of the public finances in that it allowed for substantial public investment without the need for government borrowing, which may have threatened the sustainable investment rule.

Fiscal policymaking also saw the introduction of a new operational system for public expenditure control and planning. In July 1997, Brown launched a Comprehensive Spending Review (CSR), which entailed a zero-based analysis of departmental spending in order to determine the best way to deliver government objectives. Meanwhile, the CSR was complemented by a series of biennial Spending Review's (SR), which were designed to set in place firm spending limits for each government department. The first CSR took a year to complete and was delivered to the House of Commons on the 14th July 1998. Here, Brown (1998e) also announced the introduction of Public Service Agreements (PSA), which were described as a "contract…for the renewal of public services" made between Treasury and government departments. Henceforth, each government department was required to agree to a series of departmental objectives and targets with the Treasury that were to be met in exchange for resources. Thus, Brown (Ibid) declared that public spending

was "conditional on the implementation of essential reforms, money but only in return for modernisation".

In his 1998 CSR Statement, Brown (Ibid) also announced further operational additions to public expenditure planning and control. Notably, that public spending would be split into Total Managed Expenditure (TME)[76], Departmental Expenditure Limits (DEL)[77] and Annual Managed Expenditure (AME)[78]. Henceforth, the Institute of Fiscal Studies (IFS) (2009:9) noted that TME would be established in the preceding Budget Report to each SR. The SR would then allocate TME between DEL and AME for the proceeding three years.

The classification of public spending into TME, DEL and AME, however, was described by the IFS (2009:8) as merely the 'most recent stage in a gradual evolution in the planning of public spending that has been under way since the early 1990s'. Moreover, the IFS (Ibid) added that 'when one compares the current system with its predecessors, it is clear that the new framework does not represent a radical change' and instead 'is a development of previous techniques'. Indeed, the IFS (2009:8-9) noted striking continuities in the new framework for public expenditure control and planning introduced by New Labour with the reforms introduced by the previous Conservative government and Treasury. For example, prior to 1992, the total level of public expenditure had been determined by an annual public expenditure survey, which took the form of bilateral negotiations between Treasury and government department. This system of public expenditure control and planning was reformed in 1992 to enable government to exercise greater 'top-down' control of aggregate public expenditure. Henceforth, each summer the government would set out departmental public spending for the subsequent three years. The cumulative amount of public expenditure was known as the 'control total' and was published in the annual budget. For example, the November 1996 Budget set the control total for the years 1997-98, 1998-99 and 1999-2000.

[76] TME is the total amount that a UK government spends in a financial year.
[77] DEL is the amount of TME that a government department has available to spend in each financial year.
[78] AME is the amount of TME spent on demand-led areas of public expenditure such as welfare, pensions and tax credits.

The orthodox cycle expounds that, as with the new monetary policymaking framework, the introduction of a new framework for fiscal policymaking did not lead to a radical new era in fiscal policy, but, rather, supported the implementation of orthodox fiscal policy. For example, Lee (2009:40,68,70,76-77) noted that the new fiscal policymaking framework gave the Treasury an unprecedented degree of control over the allocation of resources and policy design and strengthened the Treasury in its orthodox role as the guardian of the UK public finances. Consequently, the new macroeconomic policymaking framework served to strengthen both the Treasury and the Bank of England in their traditional responsibilities and orthodox roles. Here, the introduction of SR's and CSR's gave the Treasury greater control over its traditional responsibility in macroeconomic policymaking for public expenditure. Meanwhile, the introduction of PSA's allowed Brown to exercise greater influence in areas of public policymaking, which was normally the preserve of other government departments. Indeed, Keegan (2004:171) posits that the greater influence wielded by the Treasury in public policymaking after the 6th May 1997 was aided by the decision to return to the Bank of England its traditional responsibility for the Bank Rate, which gave Brown more time to 'concentrate on all the other myriad areas of policy' and 'delve into part of ministries that previous Chancellors had never reached (Ibid).

The orthodox cycle explains that when monetary and fiscal policymaking reside in the orthodoxy phase at the same time, the orthodoxy phase will consist of the restoration of the full framework of orthodox macroeconomic policy, which has already been outlined in monetary policymaking. Consequently, the orthodox cycle is also able to explain developments in the UK public finances after the election of New Labour. In a speech on the 20th October 1997, Brown (1997h) declared that at the centre of "our new fiscal framework" was a "five year deficit reduction plan which allows us to meet the golden rule in public finances". Table Two highlights that Brown and the Treasury went far beyond just deficit-reduction and secured the return in the UK public finances of the orthodox fiscal policy outcome of an absolute surplus and national debt reduction. For instance, public sector net borrowing fell from a deficit of 0.7% GDP to a surplus of 1.6% GDP by 2000-2001, a fiscal

tightening of 2.3% GDP. Furthermore, the economic performance of the Current Budget improved from a 0.2% GDP deficit in 1997-1998 to a surplus of 2.3% GDP in 2000-2001, a fiscal tightening of 2.5% GDP. Moreover, the surplus on the primary balance was increased by 1.5% GDP and the stock of public sector national debt saw significant reduction from 39.1% to 29.9% GDP. Indeed, Brown claimed in oral evidence on the 30th March 1998 to the Treasury Committee (1998a:Ev.62,Q.273, Ev.69,Q.320) that New Labour had achieved the "biggest fiscal tightening since 1981".

Table Two: Government Borrowing and National Debt during the 1997-2001 Parliament

Years	**Public Sector Net Borrowing** (% of GDP) *(- = Surplus)*	**Current Budget Deficit** (% of GDP) *(- = Surplus)*	**Primary Balance** (% of GDP) *(+ = Surplus)*	**Public Sector Net Debt** (% of GDP)
1997-98	0.7%	0.2%	+2.1%	39.1%
1998-99	-0.5%	-1.1%	+3%	37.3%
1999-00	-1.5%	-2.1%	+3.6%	34.4%
2000-01	-1.6%	-2.3%	+3.6%	29.9%

(Source:OBR,2016)

Furthermore, the return to orthodox fiscal policy outcomes in the UK public finances was secured through the implementation of the orthodox fiscal policy instrument of public spending restraint. Whilst in opposition, Gordon Brown had committed New

Labour to remaining within the 'control total' established for 1997-1998 and 1998-1999 by the 1996 Budget of the previous Conservative government (Gamble and Kelly,2001:174). Thus, the Treasury (1997:4) identified in its 1997 Budget Report that the 'control total' for public expenditure for 1997-1998 and 1998-1999 remained unchanged, although an extra £1.2billion and £1billion was found for the National Health Service (NHS) and education. Furthermore, the Treasury (1997:12) indicated its support for fiscal orthodoxy when it declared that the deficit-reduction plan 'is intended to ensure sound public finances', which was a 'prudent approach' that 'aims to avoid the mistakes of the past' including the 'large [fiscal] policy errors' of the late 1980s. Subsequently, the 1998 Treasury (1998a:5) *Public Expenditure Statistical Analysis* found that Brown had kept public expenditure in the first two years of the New Labour government at the levels set in 1996 Budget.

The implementation of orthodox fiscal policy instruments during the 1997-2001 Parliament is demonstrated in Table Three, which shows the level of spending restraint both as a % of GDP and in 2014/15 prices. Moreover, the implementation of orthodox fiscal policy instruments was highlighted by the OECD (2000:13-14,62-63) 2000 *Economic Survey of the UK*, which posited that New Labour had secured a balanced budget through a mixture of public spending restraint in some areas, lower public spending in others, undershoots in departmental spending and increased taxation revenue. The deployment of orthodox fiscal policy instruments was also highlighted by the IFS (2001:2,22) in their 2001 *Green Budget*, which found that public spending during 1997-2000 was lower in real terms than under Conservative governments since 1979 and had been driven by reduced expenditure on defence, housing, transport and trade and industry and capital spending on health and law and order that was low by historical standards.

Table Three: Public Expenditure and Taxes during the 1997-2001 Parliament

Years	Total Managed Expenditure (% of GDP)	Total Managed Expenditure (2014/15 Price - £billions)	Public Sector Current Expenditure (% of GDP)	Public Sector Current Expenditure (2014/15 Price - £billions)	Public Sector Net Investment (% of GDP)	Public Sector Current Receipts (% of GDP)	National Account Taxes (% of GDP)
1997-98	36.9%	£481.3	34.3%	£446.2	0.5%	36.2%	33.6%
1998-99	36.2%	£483.0	33.6%	£449.4	0.6%	36.7%	34.1%
1999-00	35.9%	£487.6	33.3%	£452.8	0.6%	37.4%	35%
2000-01	36.1%	£501.8	33.5%	£463.3	0.6%	37.7%	35.2%

Source: (OBR, 2016).

The implementation of orthodox fiscal policy instruments during the 1997-2001 Parliament also included tax increases. Here, New Labour and the Treasury continued the trend begun in the UK public finances during the 1970s, which had seen a broadening of the tax base through new indirect taxes and successive reductions in direct taxation. Therefore, during the 1997-2001 Parliament, the higher rate of income tax was held by New Labour at 40%, the standard rate was lowered from 23% to 22% and a new 10p tax rate was introduced on lower incomes. However, such was the plethora of new indirect taxes implemented after the 2nd May 1997 they became referred to as ‘stealth taxes’ (Stevens,2001:195-196), which included new or higher levels of indirect taxes on stamp duty, fuel duties, tobacco

duties and climate change levy whilst tax relief was reduced and removed on dividend tax credit, mortgage interest, married couples allowance, foreign earnings and company cars. Consequently, Gamble and Kelly (2001:174-175) found that New Labour raised substantial new taxation revenue, which is demonstrated in Table Three, and the overall tax burden increased.

A variety of domestic and global actors began to criticise the efficacy of the fiscal rules during the 1997-2001 Parliament (IFS,1999:13;OECD,2000:13). For instance, the 1999 International Monetary Fund (2000:18) *Article IV Consultation Report* stated that the fiscal rules were ‘not very constraining and leaves considerable scope for future initiatives’. This criticism by the IMF was related to the belief that the fiscal rules would not constrain rises in public expenditure or preclude a future departure from the orthodoxy of the balanced budget. However, the fiscal rules and the 1998 Code for Fiscal Stability did not institutionalise permanent fiscal orthodoxy in the public finances; rather, it institutionalised periodic bouts of fiscal consolidation in the public finances. First, if the golden rule were threatened then a mixture of the orthodox fiscal policy instruments of public spending restraint, public expenditure reductions or tax increases would be required. Second, if the sustainable investment rule was in danger of being breached orthodox fiscal policy instruments would be required to reduce government borrowing and keep national debt below 40% GDP. Indeed, the 1998 Code for Fiscal Stability (HM Treasury,1998c:6,Part 2) allowed the government to ‘temporarily’ depart from the fiscal rules so long as the reasons for departure, when fiscal policymaking would return to the fiscal rules and the objectives and operating rules that would apply over the departure period were stated.

Consequently, an important aspect of the period of fiscal orthodoxy in the UK public finances after the 1997 general election was that it was pursued on a scale that was wholly unnecessary according to Gordon Brown’s own fiscal rules. For example, the 1998 IFS (1998:1) *Green Budget* found that core public spending could have risen by 3% per annum in real terms from 1998-1999 onwards and the golden rule would still have been met in 2001-2002. Therefore, the orthodox cycle explains that the fiscal rules during the 1997-2001 Parliament were superseded by the

restoration of orthodox fiscal policy, which is what we should expect when fiscal policymaking resides in the orthodoxy phase.

In preparation for the 2000 SR, Brown (2000a) announced in his Budget Statement of the 21st March 2000 that current public spending would increase by 2.5% per in real terms and public net investment would double to 1.8% GDP in the three-years from 2001. Furthermore, Brown (Ibid) announced that a significant beneficiary of this extra public expenditure would be the National Health Service (NHS), which would see spending increases worth 6.1% per year in real terms between 2001 and 2004. The 2000 SR then allocated a further £43billion additional public spending to DEL above that set out in the 2000 Budget (HM Treasury,2000c:8-9), which meant that TME and DEL were now forecast to rise from £176.8billion and £340.7billion in 1999-00 to £245.7billion and £439.6billion in 2003-04 respectively. In the 2001 Budget a further £2.33billion was allocated to public spending on health and education (HM Treasury,2001:3).

Despite the increase in TME and DEL announced in the 2000 Budget and 2000 SR, Bevir (2005:114-115) noted that it would only return the level of public expenditure to a percentage of GDP inherited by New Labour at their 1997 general election victory. Thus, Table Three shows that whilst public expenditure did increase in 2000-01 in cash terms, as a percentage of GDP it was still lower than in 1997-1998. Furthermore, despite the increase in public expenditure in 2000-2001 there was no departure from the orthodox fiscal policy outcomes of a surplus budget and national debt reduction, which is demonstrated in Table Two. Consequently, despite the increases in public expenditure announced at the 2000 Budget and 2000 SR, the orthodox cycle explains that Brown and HM Treasury were still implementing restraint in public spending. Indeed, if we accept that the IFS were correct in their aforementioned 1998 *Green Budget* and the fiscal rules would have permitted a 3% rise per annum in core public spending then TME could have stood £27.8billion higher than £501.8billion in 2000-2001.

Consequently, the Treasury's (2000:1,3) 2000 Budget Report claimed that whilst "substantial new resources" had been made available for the public services,

the 2000 Budget 'lock[ed] in the fiscal tightening over the next two years' and New Labour would continue to meet its fiscal rules. The Treasury (2000:25-26) was able to make this claim because it forecast that even with the new resources made available to the public sector, the current budget was destined to generate ever greater surpluses to the end of its forecast period in 2004-05. Furthermore, the Treasury (Ibid) forecast that borrowing would remain in surplus in 2001-02 with only a small deficit of £3billion emerging in 2002-03 and that national debt would continue to reduce as a percentage of GDP. Accordingly, fiscal policymaking remained in the orthodoxy phase of the orthodox cycle throughout the 1997-2001 Parliament.

The Continuity of Orthodox Economic Ideas after the 1997 General Election

The orthodox cycle explains that when monetary and fiscal policymaking reside in the orthodox cycle at the same time, then restoration of the full framework of orthodox macroeconomic policy will include evidence of orthodox economic ideas in the formulation and implementation of macroeconomic policy. It is now a staple of the academic literature that globalisation was central to New Labour political economy and economic policy, which would seem to suggest that the election of New Labour did lead to ideational change[79]. However, in his study of *globalisation and ideology in British politics*, Berry (2011:x,2) states that in order to understand why globalisation became pervasive in UK politics in the late 1990s it is necessary to look closely at extant ideas, traditions and discourse.

[79] Although far from an exhaustive list, Beech (2004:87-89), Berry (2011:Chp.3), Coates (2005:33), Coates and Hay (2002), Coffey and Thornley (2009), Driver and Martell (1998:42-43), Watson and Hay (2003), Lee (2008:20), McGrew (2004) and Wilkinson (2000) all highlight the importance of globalisation to the political economy and economic policymaking of New Labour.

This chapter argues that globalisation resonated in UK politics and economic policymaking because it built substantially upon the discourse and traditions of internationalism. Thus, it is claimed that rather than being an example of radical change in ideas in policymaking engendered by the election of New Labour, as we should expect according to the model of punctuated equilibrium, the economic element of the globalisation idea is merely the modern expression and continuity of the orthodox economic idea of internationalism. Indeed, there is significant similarity between the interpretation and construction – albeit expressed in new language - of the orthodox economic idea of internationalism and the economic element of globalisation in political discourse and policy documents after the 2nd May 1997.

The similarity between the construction of the two economic ideas is clear from two key elements in the interpretation of globalisation by New Labour, the Treasury and Bank of England. The first element in the construction of the economic idea of globalisation similar to internationalism is the portrayal of the UK economy as an integrated part of the global economy. The second element in the construction of globalisation is that UK economic prosperity would be secured not by rejecting globalisation but by deepening the interconnection of the global and domestic economy.

There were two differences in the construction of the economic ideas of globalisation and internationalism in rhetoric and policy documents, neither of which undermine the argument that the economic idea of globalisation is the modern expression of internationalism. For example, the third element in the construction of globalisation was that the role of macroeconomic policy in the global economy was to achieve economic stability. Furthermore, globalisation carried with it certain assumptions about global economic processes that were not readily apparent in internationalism. Thus, the fourth element in the construction of globalisation was that the mobility of capital, factors of production and trade in goods and services in global economy was causing rapid economic change. An example of the way globalisation was constructed in political discourse is available in the first Budget Statement delivered by Brown (1997d) on the 2nd July 1997, which stated that the "impact of the global market in goods and services, and of rapidly advancing

technology, is now being felt in every home and every community in our country. New production, new services, new opportunities challenge us to change; old skills, old jobs, old industries have gone and will never return". Here, Brown (Ibid) contended that globalisation offered a "historic opportunity" of economic prosperity for the "dynamic economies of the future". Furthermore, Brown (Ibid) posited that "the central purpose of this Budget is to ensure that Britain is equipped to rise to the challenge of the new and fast changing global economy", which meant "ensur[ing] stability, investment, work, and opportunity for all"[80]. Consequently, Fairclough (2000:viii) found that globalisation was presented in New Labour discourse as an 'accomplished fact' to which there was 'no alternative' and that change in the structure of the UK and global economy was 'represented as an inevitable movement in the direction of globalisation' instead of a series of economic processes that displayed 'partial and uneven tendencies'.

Furthermore, the orthodox cycle understands that the orthodox economic idea of internationalism and its modern expression of globalisation had a similar impact on the formulation of policy through the continued importance placed on the issue of confidence and credibility in economic policymaking (Clift,2001;Driver and Martell,1998:63,69;Gamble and Kelly,2001:174;Keegan,2004:152-153). This was no more evident than in the notion of constrained discretion, which informed the new institutional framework for macroeconomic policymaking introduced by New Labour and the Treasury from the 6th May 1997 onwards. The notion of constrained discretion was explained by Ed Balls (1998) in his 1997 lecture *Open Macroeconomics in an Open Economy*, which was published in the *Scottish Journal*

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[80] These four elements in the construction of globalisation are available in public speeches by senior figures in New Labour such as Blair (1998; 1998b:1999a;1999b;1999c;2000;2000b;2000c) and Brown (1997b;1997e;1998f; 1998b;1998f;1998h;1998k;1998m;1999a;1999b;1999m). Furthermore, these four elements were articulated in the public speeches of Cabinet members such as Byers (1999c;1999d;2000b) and junior ministers at HM Treasury and the DTI such as Caborn (2000), Darling (1997;1998), Johnson (2001), McCartney (1999) and Timms (2000a). Finally, this construction of globalisation was also expressed in policy documents by the Department of Trade and Industry (1998a) and HM Treasury (1997:c.22) and public speeches by Edward George (1997:3;1998c:3; 1999c:2;2000:2; 2000a:4).

of Political Economy. Here, Balls (1998:122) argued that globalisation meant the 'power of the markets is always and everywhere' and would 'immediately punish any government which strays from the macroeconomic straight and narrow'. Thus, Balls (Ibid) suggested that 'rapid globalisation of the world economy has made credibility more rather than less important', which was the 'elusive elixir of modern macroeconomics' because global markets punish governments 'much more rapidly than thirty or forty years ago'. Meanwhile, Balls (1998:124) argued that globalisation meant governments are 'judged by the market to be pursuing sound monetary and fiscal policies, can attract inflows of investment capital at higher speed'.

As a result, Balls (1998:119-121) contended that globalisation meant the creation of the new institutional framework for macroeconomic policymaking had been guided by four 'post-monetarist' principles. First, the principle of stability through constrained discretion, which meant macroeconomic policymaking was constrained by the acceptance that economic stability and low inflation was the necessary condition for achieving and sustaining high and stable levels of growth and employment. Within that constraint, Balls claimed that credibility allowed the implementation of discretionary economic strategies in response to shocks that threatened economic stability. Moreover, the new institutional framework for macroeconomic policymaking would secure credibility through the three principles of sound, long-term policies, maximum transparency and pre-commitment through the adoption of rules. For example, in his 19th October 1999 *Mais Lecture*, Brown (1999k) suggested that the "discretion necessary for effective economic policy is possible only within an institutional framework that commandsg market credibility" and that "credibility depends upon clearly designed long-term policy objectives, maximum openness and transparency, and clear and accountable divisions of responsibility".

Consequently, the desire to secure credibility in the global economy was an integral impetus behind the creation of a new macroeconomic policymaking

framework[81]. For example, Brown (1997b) claimed in a speech on the 20th May 1997 that granting operational independence for setting the Bank Rate to the Bank of England had "put monetary policy on a credible, long-term footing". Similarly, Brown told the Treasury Committee (1997:Ev.22,Q.61,Ev.23, Q.62) in oral evidence on the 22nd July 1997 that operational independence for the Bank of England was "right for any government that is interested in setting a long-term framework that commands credibility" and the "best guarantee we have of both long-term credibility and confidence in the system". Indeed, Gamble and Kelly (2001:174) argued that the 6th May 1997 announcement pertaining to the Bank of England had been a 'striking example' of the bid for credibility in economic policymaking made by New Labour.

The relationship between credibility and the new monetary policymaking framework was also expressed by Edward George (1998a) in a speech on the 24th February 1998 when he posited that "the overriding purpose of these new arrangements is to improve the credibility of monetary policy". Furthermore, the Bank of England (1997b:3,16,51;1999c:24) *Inflation Report* of the May 1997 and August 1999 also claimed that the new monetary policymaking framework would improve credibility. Finally, it becomes clear from the minutes of MPC meetings that establishing credibility in the new institution was an important factor in the implementation of monetary policy via the Bank Rate made by its members through the 1997-2001 Parliament[82].

The issue of credibility was also important in the operational changes to fiscal policymaking and the implementation of fiscal policy during the 1997-2001 Parliament. For example, in a speech on the 20th May 1997, Brown (1997b) declared he would "take action to enhance the credibility of the public finances", which included inviting the National Audit Office to inspect and make comment upon

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[81] The following speeches made by Brown (1997c;1997j;1998a;1998c;1998d;1998f) and Darling (1998) highlighted that credibility was an important factor in the formation of the new institutional framework for macroeconomic policymaking.

[82] Several minutes of MPC meetings during the 1997-2001 Parliament show that establishing credibility in the MPC was a significant factor in decisions on the Bank Rate made by MPC members (Bank of England,1997g;62;1998a:53,62,69;1998e:56; 1999a;73;2000:69;2000b:76).

Treasury public finance forecasts. Later, in speeches on the 22nd and 28th April 1998, Brown (1998a;1998c) claimed that the introduction of the 1998 Code for Fiscal Stability "guarantee[d] certainty and therefore credibility in decision-making". Meanwhile, Brown (1999f) suggested in a speech on the 2nd July 1999 that the introduction of "clear rules" for fiscal policy had put in place "a long-term fiscal framework for sustainable public finances". Moreover, in a speech on the 17th September 2002, which provided a retrospective on macroeconomic policymaking after the election of New Labour, Gus O'Donnell (2002) claimed that "one of the key principles behind the changes to the fiscal policy framework is exactly the same as that underlying the changes in the monetary policy framework, namely the desire to achieve credibility". Finally, Brown claimed in oral evidence on the 22nd July 1997 to the Treasury Committee (1997:Ev.32,Q.111-112) that he had implemented deficit-reduction because it carried "credibility and gives people confidence", which would not be secured "unless you can show people that you have in terms of the deficit a reduction plan which is not just for a year but a period of years".

The restoration of the full framework of orthodox macroeconomic policy after the election of New Labour also included the orthodox economic idea of competitiveness in the formulation of macroeconomic policy, which was heavily wrapped within the discourse on globalisation (Crafts,2007:273;Owen,2001:209). Competitiveness was interpreted and constructed in public speeches and policy documents in the same manner that it had during earlier periods of the Twentieth century with UK firms and entrepreneurs were identified as operating within a 'global marketplace'[83], which meant their ability to sell and export goods and services was subject to global competition[84]. For instance, in his *Mansion House*

[83] Direct reference to the 'global marketplace' can be found in the Treasury (1997a:5,7) 1997 Pre-Budget Report. Moreover, the 'global marketplace' was articulated by Beckett (1998;1998b). The most important references to the 'global marketplace', in respect to macroeconomic policymaking, are found in the public speeches of Gordon Brown (1997c;1997k;1998a;1998c;1998d;1998f;1998k; 1999b;1999f;1999h2000b;2000c) where it was claimed that the 'global marketplace' necessitated that macroeconomic policy secured economic stability and microeconomic policies secured open, competitive and flexible markets.

[84] The identification that UK firms and entrepreneurs operated in the context of global competition was evident in public speeches by Blair (1997a;2000b) and

speech in the City of London on the 12th June 1997, Brown (1997c) argued that the "global marketplace [is] characterised by ever more fierce competition" and the "new economy" and "country" must be "fully equipped to contribute to and compete within this global marketplace". Thus, it was identified by New Labour that the route to competitiveness in the 'global marketplace' was via greater competition and entrepreneurship in domestic markets[85]. Indeed, Peter Mandelson (1998b), Secretary of State for Trade and Industry (1998), in a speech on the 10th December 1998 stated that "instead of building socialism in one country" New Labour were "seeking competitiveness in the global economy".

The implication of the orthodox economic idea of competitiveness for the formulation of economic policy was to produce clear divisions of responsibility for macroeconomic and microeconomic policy. For example, Brown (1999f) identified in a speech on the 2nd July 1999 that the role of macroeconomic policymaking in "the new global marketplace" was to pursue "policies for monetary and fiscal stability" as "national economies must be found on the rock of stability". Economic stability, it was claimed, aided competitiveness by attracting global investment capital (Bevir,2005:109). Meanwhile, microeconomic policy would promote competitiveness in the global economy by promoting competition within the UK economy (Driver and Martell,1998:68). For example, the 1998 Competition Act

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Brown (1997g; 1998g;1998k;1999d;1999f; 1999g;1999i;1999l;1999m;2000;2000b; 2000c). It was also expressed by a series of Secretaries of State at the DTI. For example, see Beckett (1997; 1997a;1997b;1997c;1998b), Byers (1999;1999a; 1999b;2000;2000b;2000c) and Mandelson (1998;1998a;1998b). Furthermore, it was also articulated by junior ministers at HM Treasury and DTI such as Darling (1998), McCartney (1997;1999), Roche (1999), Smith (2000) and Timms (2000;2000a). Furthermore, the economic idea of competitiveness was also constructed in these terms in policy documents. For instance, see Bank of England (1997:5,25,51;1997c: 5,24,49;1999a:14,20,35;1999c:35), DTI (1998:6-10;1998a; 2001), HM Treasury (1997:5;1997a:33-34) and public speeches by Edward George (1998c:4; 1999c:2;1999d:5).

[85] The following public speeches by Beckett (1997), Brown (1998;1998d;1998f; 1999;1999f;1999g;2000;2000b;2001), Byers (1999d;2000;2000a), Mandelson (1998a) and Timms (1999) all identified that the route to competitiveness came from enhanced competition and entrepreneurialism in the UK economy. Moreover, see the 1997 Pre-Budget Report by HM Treasury (1997a:17) and a DTI (1998a:12) report on the state of competitiveness in the UK economy.

became the dominant source of competition law in the UK economy and sought to end the restrictive practices and market abuses of firms that were deemed anti-competition such as price fixing. The 1998 Competition Act also established the Competition Commission, a non-departmental government body, on the 1st April 1999 with responsibility for regulating competition law and investigating mergers and acquisitions.

The orthodox cycle also facilitates the identification of the return of the orthodox economic idea of crowding-out in both of its conceptions: financial and psychological in the formulation of macroeconomic policy Financial crowding-out was constructed in the same manner as it had been during the Twentieth century, specifically, that government borrowing leads to an increase in market interest-rates, which crowds-out private sector investment and consumption from the market. For example, the financial version of crowding-out was important to Brown in his implementation of a five-year deficit-reduction plan, which was evident when he stated in oral evidence to the Treasury Committee (1997:Ev.33,Q.114) that deficit-reduction would relieve pressure on market interest-rates. This was echoed by Brown in oral evidence to Treasury Committee (1999:Ev.50,Q.278) on the 30th March 1999, which posited that deficit-reduction and subsequent surplus in the Current Budget had helped achieve "lower long-term interest-rates" and "is helping to make it possible for interest rates to come down more generally". Moreover, Alistair Campbell (2011:215), Downing Street Press Secretary (1997-2000) and Director of Communications and Strategy at Number 10 (2000-2003), noted in his diaries that Gordon Brown rejected the pleas of Blair for higher public spending on the NHS in a Cabinet meeting on the 20th January 2000 via the argument that higher public spending would lead to higher inflation, which in turn would cause the Bank of England to increase interest-rates. Finally, the financial version of crowding-out was also evident in Treasury officials. For example, Gus O'Donnell claimed in oral evidence to the Treasury Committee (1999:Ev.35-36,Q.157,159,164) on the 18th March 1999 that expansionary fiscal policy led to higher interest-rates.

Consequently, the orthodox cycle explains that the restoration of the full framework of orthodox macroeconomic policy after the 2nd May 1997 included the

return to the orthodox hierarchy between policy instruments, which saw fiscal policy play a supportive role to monetary policy[86]. In the first instance, Brown and O'Donnell's aforementioned oral evidence to the Treasury Committee argued that fiscal orthodoxy ensured the policy space for market interest-rates and the cost of credit in the UK economy to reflect the operational decisions taken by the MPC and the Bank of England, rather, than fiscal policymakers at the Treasury. Furthermore, orthodox fiscal policy during the 1997-2001 Parliament meant that fiscal policy could support the MPC in achieving the orthodox objective of price stability. For example, in his 1998 Pre-Budget Statement on the 3rd November, Brown (1998l) argued that the cumulative fiscal tightening of 3.75% GDP from 1996-97 to 1998-99 meant fiscal policy had "played its part with interest rate policy in tackling inflationary pressure". Moreover, Joe Grice, Deputy Director of the Macroeconomic Policy and Prospects Division at the Treasury (1997-2000), declared in oral evidence to the Treasury Committee (1998a:Ev.41,Q.145) that "sharp tightening in fiscal policy… has been helpful" to the MPC and Bank of England in "managing interest rates to meet the government's monetary objectives". Finally, O'Donnell (2002) argued in a speech on the 17th September 2002, which offered a retrospective on macroeconomic policymaking since the 2nd May 1997, that "countries with an independent monetary policy tend to rely on interest rates as the main instrument to stabilise demand, with fiscal policy playing a supporting role". O'Donnell (Ibid) continued to argue that "fiscal policymakers know this and set fiscal policy in the knowledge that monetary policy will respond. Thus the system allows fiscal policies to support monetary policy in ensuring macroeconomic stability, rather than conflicting with it".

The primacy of monetary policy over fiscal policy in the implementation of macroeconomic policy was also evident when the MPC took the lead in countering disturbances in the domestic and global economy after May 1997. Indeed, the MPC feared the Bank Rate from 6.5% to 7.5% between the 6th June 1997 and 4th June 1998 (Bank of England, 2016a) as the MPC worried that an "overheating" UK

[86] The supportive role played by fiscal policy to monetary policy was identified in public speeches by Brown (1999c;1999m) and in oral evidence to the Treasury Committee (2000:Ev.32,Q.187,Ev.43,Q.276-279).

economy would lead to a surge in inflation (George,1998e). The MPC then reduced the Bank Rate in successive stages until it fell to 5% on the 10th June 1999, which was the Bank Rate's lowest point "since 1971" and was considered by George (1999d) to be a "relatively aggressive response" to the global growth slowdown emanating from the Asian Financial Crisis of 1997-1998.

Meanwhile, the psychological version of crowding-out was also evident in the creation of the new framework for macroeconomic policymaking after the election of New Labour. Psychological crowding-out had been interpreted and constructed in the Twentieth century as the notion that government borrowing leads to a loss of confidence, which results in higher interest-rates that crowds-out investment and consumption. Whilst the psychological version of crowding-out was not directly expressed in these terms after the election of New Labour it was, nevertheless, clearly identifiable in discourse and played a role in the formation of the new institutional framework for macroeconomic policymaking. For example, in his statement on the 6th May 1997, Brown (1997a) asserted that "it has become increasingly clear that the present arrangements for policymaking are not generating the confidence necessary", which was why the UK had higher long-term interest rates than other countries. The Treasury (1997a:7) echoed this argument in their 1997 Budget Report. The psychological version of crowding-out was also referred to by Brown (1999k) in his 1999 *Mais Lecture* of the 19th October when he stated the importance of credibility in macroeconomic policymaking because "once lost, [it] is hard to regain. The economy then pays the prices in higher long-term interest rates and slower growth".

The restoration of the full framework of orthodox macroeconomic policy included the use of orthodox economic idea of economic liberalism in the formulation of economic policy, which was interpreted and constructed in public speeches and policy documents in the same manner as earlier periods of the Twentieth century. Consequently, it was readily identified that business and entrepreneurs of the private sector, rather than state and government, were the drivers

of economic growth and employment in public speeches by New Labour[87]. Thus, as per previous governments in our historiography, the role of the state under New Labour was to implement microeconomic policy that would secure the 'potential for dynamism and efficiency delivered by the markets' (Faucher-King and Le Gales,2010:6-7). As a result, it was declared by New Labour that the state would not be used to 'pick winners' via economic policies of corporatism and government subsidy, but rather would 'make markets work better' so they operated in the public interest[88]. Here, microeconomic policy would ensure markets operated in the public interest by supplying entrepreneurs with an open, competitive and flexible market system, which would create economic growth and employment[89]. Where New Labour microeconomic policy took a more activist form, such as in the provision of a skills agenda, it was not implemented to intervene in the working of the economy, but rather in order to enhance the efficiency and dynamism of market-exchange and competitive advantage in the global economy.

[87] The claim that business and entrepreneurs were the drivers of economic growth and prosperity was made in several public speeches by Blair (2000a), Brown (1998b;19998k), Byers (1999a;1999b;1999d;2000) and McCartney (1999).

[88] The claim that New Labour microeconomic policy would not 'pick winners' but instead 'make markets work better' so they operated in the public interest was evident in a number of public speeches by Blair (2000) and Brown (1997b;1999f;1999g;2000). Furthermore, it was also expressed in speeches by junior ministers at HM Treasury such as Darling (1997) and Timms (2000c). Finally, it was also articulated by Balls (1998:116) and HM Treasury (1997:16) in the 1997 Budget Report.

[89] The following public speeches and policy documents make it clear that the route to an enterprise economy was considered to lay in open, competitive and flexible markets for product, capital and labour. For example, see Blair (1997;1998a;1999a;2000;2000b; 2000c) and Brown (1998d;1998f;1998j:1; 1998h;1998i;1999;1999g;1999i:1;2000; 2000b). Furthermore, this assertion was made in public speeches by Secretaries of State at the DTI such as Beckett (1997;1997c;1998;1998a;1998b), Byers (1999;1999a;1999c; 2000;2000a;2000b; 2000c) and Mandelson (1998b) and junior ministers at HM Treasury and the DTI including Battle (1998), Darling (1997) and McCartney (1998;1999). Finally, the HM Treasury (1997:16;1998:12;1998b:15-16) 1997 and 1998 Budget Report and 1998 Pre-Budget Report, DTI (1998:1998a;2001) policy documents and public speeches by Edward George (1998c:2;1999c:3) all articulated that the route to an enterprise economy would be achieved by open, competitive and flexible markets for products, capital and labour.

New Labour microeconomic policy saw the implementation of the six microeconomic policies implemented by previous Conservative governments that have been identified by Jessop (2003:5), which included liberalisation, deregulation, privatisation, commodification of the public services, internationalisation of the domestic economy and reduced taxation of firms and corporations[90]. For instance, during the 1997-2001 Parliament, twin announcements in the 1997 Budget and Pre-Budget Statement by Brown (1997d;1997k) reduced corporation tax from 33% to 30% by April 1999. These cuts to corporation tax were complimented by similar reductions in capital gains tax from 40% to 10% and cuts in small company taxation form 23% to 20%, which, it was claimed, would increase investment and stimulate entrepreneurship[91]. As a result, New Labour microeconomic policy conformed to Cerny's (1997:259-260) notion of the competition state, which pursues increased marketisation of domestic economic activities in order to increase their 'competitive advantage' in international and transnational terms. Cerny argued that two further features of the competition state included the reduction of government spending in order to minimise the 'crowding-out' of private investment and microeconomic policies such as deregulation of economic activities.

Orthodox economic ideas led therefore to the establishment of divisions of responsibility between macroeconomic and microeconomic policy in the formulation of economic policy during the 1997-2001 Parliament. These defined roles are important, primarily, because it meant that macroeconomic policy was assigned the objective of economic stability, which required a new institutional framework for macroeconomic policymaking. For example, Brown (2000c) argued in his 8th May 2000 *James Meade Memorial Lecture* that the "global economy" required "a new long-term framework for monetary and fiscal policy that can command new

[90] The following literature also identifies New Labour microeconomic policy as a continuation of the neoliberal microeconomic policy implemented by previous Conservative government includes Crafts (2007), Fairclough (2000), Heffernan (2001), Jenkins (2007), Lee (2007;2008;2009), Marquand (1997), Moran and Alexander (2000), Sinclair (2007) and Taylor (2001).
[91] The claim that reducing corporation tax would increase investment and stimulate entrepreneurship was made in the following public speeches by Brown (1997d; 1997k; 1999;2001) and junior ministers at HM Treasury such as Darling (1997), Primarolo (2001), Roche (1999), Smith (2000) and Timms (2000;2000a).

confidence. Its essence is that long-term, open and transparent decision-making procedures which command credibility provide a better route to stability". Thus, it was consistently highlighted in Treasury documents that the purpose of the new institutional framework for macroeconomic policymaking was to secure economic stability[92]. Meanwhile, microeconomic policy would improve economic performance in areas such as growth, employment, productivity and competitiveness (Driver and Martell,1998:32,69-70;Keegan,2004:206;Owens,2001:209;Stevens,2001:186)[93]. Consequently, the division of responsibility in the formulation of macroeconomic and microeconomic policy was precisely that outlined by Nigel Lawson in his 1984 Mais Lecture, which was discussed in Chapter Four. +

The priority objective for macroeconomic policy after the election of the Blair government was the orthodox objective of price stability. This was the case in macroeconomic policymaking because the macroeconomic objective of economic stability was defined and measured by the orthodox objective of price stability. For example, Gamble and Kelly (2001:173) noted that New Labour would achieve economic stability in its first-term via the 'inflation target'. This was supported in the sixteenth *Mais Lecture* delivered by Edward George (1997a:4) on the 24th June 1997 when he contended that the MPC used 'price stability as an indicator of stability in the economy as a whole', which allowed the MPC to 'aspire to help to moderate the economic cycle rather than aggravate it'. Indeed, Gordon Brown's (1997a) stated in his 6th May 1997 announcement that "price stability… [was] an essential precondition" for New Labour's wider economic objective of "high and sustainable levels of growth and employment"[94]. This argument is further strengthened when we

[92] For example, HM Treasury (1997:6-15;1997a:7-8;1998:2,9,12;1998b:1;1999;5-6; 1999a:2000:1-2;2000a:1; 2001:1) Budget and Pre-Budget reports between June 1997 and March 2001 would all emphasise that the purpose of the new macroeconomic policymaking framework introduced after the 6th May 1997 was to secure economic stability.

[93] These respective roles for macroeconomic and microeconomic policy were highlighted in a number of public speeches by Gordon Brown (1998c;1999b; 1999e;2000c) and Edward George (1997a;1998:2;1998a:2-3,5;1998b:4;1998d:2-3;1998e:6;1999a:3-4;1999c:2;2000c;2001d:2).

[94] Price and economic stability as a 'precondition' and 'necessary' for high and stable levels of growth and employment was repeatedly emphasised in a number of public

reconsider that macroeconomic policy instruments after the 2nd May 1997 were operated according to the orthodox hierarchy, which saw fiscal policy play a supportive role to monetary policy in the pursuit of the orthodox objective of price stability.

Orthodox economic ideas therefore led to the rejection of discretionary fiscal policy to stabilise economic growth and employment through demand management[95]. For example, Brown (1999k) declared in his 1999 *Mais Lecture* of the 19th October that the macroeconomic objective of full employment had to be achieved in a "radically different context" than the post-war era of "integrated capital markets, greater international competition and innovation as the key to competitive advantage". On this same theme, Brown (2000c) asserted in the *James Meade Memorial Lecture* of the 8th May 2000 that "Keynesian fine-tuning" and "fixed monetary targets" had been "designed for sheltered national economies" that no longer existed in the age of "modern, liberalised and global capital markets". Thus, Balls (1998:118) identified two grounds upon which macroeconomic strategies of demand management would be rejected by New Labour. First, it was argued that the new global economy of rapid and volatile capital markets meant that expansionary macroeconomic policy could not 'deliver, let alone sustain, full employment'.

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speeches by Brown (1997f:1;1998g;1998l;1999b;1999f;1999g) after the 6th May 1997. It was also highlighted by Balls (1998:120;2000) and junior ministers at HM Treasury such as Darling (1997;1998). Finally, the notion that price and economic stability was a 'precondition' and 'necessary' for economic growth and employment was also evident in public speeches by George (1998:2;1999a:4; 1999b:2;1999c:2;2000b:3) and the 1997 Pre-Budget Report by the Treasury (1997a:8).

[95] The rejection of discretionary fiscal policy instruments as an instrument of macroeconomic stabilisation through the management of demand was articulated in a number of public speeches by Blair (1999b;2000c) and Brown (1998d;1998f;1999j:1; 1999k;2000c). Furthermore, see Brown's oral evidence to the Treasury Committee (1997:Ev.29,Q.92; 1998a:Ev.62,Q.28). Moreover, the rejection of macroeconomic strategies for stabilisation based on the implementation of discretionary fiscal policy was also evident in policy documents such as the HM Treasury (1997a:16-17) 1997 Pre-Budget Report and in public speeches by Edward George (1998c:3;1998e:6). Finally, the rejection of fiscal strategies of demand management by New Labour has been identified by several scholars such as Bevir (2005:113), Keegan (2004:85,277,310) and Stevens (2001:185-188).

Second, it was claimed that expansionary macroeconomic policy led to economic instability. Particularly, it allowed 'inflation to run out of control', which then had to 'forcibly restrained' by higher interest-rates and public expenditure reductions, which caused a 'long-term price in higher unemployment'. Here, Balls (Ibid) noted his debt of gratitude to Milton Friedman and his demonstration that there was no long run tradeoff between inflation, growth and employment and expansionary macroeconomic policy led to inflation and higher unemployment[96].

Finally, the orthodox cycle also explains that the orthodoxy phase will see the deployment of a policy narrative that seeks to legitimise the return to orthodox macroeconomic policy. Here, the prioritisation of economic stability was supported by a distinctive policy narrative deployed in rhetoric of Gordon Brown after the election of New Labour, which legitimised creation of the new institutional framework for macroeconomic policymaking. A key component of this policy narrative was a particular analysis of Twentieth century UK economic history, which posited that post-war economic decline as the product of periodic bouts of boom and bust in the UK economy[97]. For example, in his first public statement as Chancellor on the 6th May 1997, Brown (1997a) contended that "long-term national economic success" must be "built on the solid rock of prudent and consistent economic management, not the shifting sands of boom and bust". In his first Budget Statement of the 2nd July 1997, Brown (1997c) identified that ending the boom and bust cycle in the UK economy required a new monetary and fiscal policymaking framework based on openness, accountability, discipline and rules. Subsequently, Blair (2000a;2000d) and Brown (1999n;2000d) claimed that the new macroeconomic

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[96] Friedman posited that in the long-run expansionary macroeconomic policies increase inflation and leads to higher unemployment. Hence, employment creation through expansionary macroeconomic policy was only applicable in the short-term. That there was no long-run trade-off between inflation and unemployment was repeated in public speeches by Balls (2001), Brown (1998b:1998c;1998d; 1999e;1999j:1;1999k;2000). Furthermore, see Brown's oral evidence to the Treasury Committee (1998a:Ev.62,Q. 283).

[97] The narrative that UK economic decline was a consequence of period bouts of boom and bust in the UK economy, which required a new institutional framework for macroeconomic policymaking was articulated by Brown (1997a;1997b1997d; 1997f:4-5;1997jk;1999c) in a number of speeches after the election of New Labour.

policymaking framework had brought ‘end to boom and bust’ and would ensure ‘no return to Tory boom and bust’.

Conclusion

This chapter has provided a case-study of UK macroeconomic policymaking from the 2nd May 1997 to the 6th June 2001. The chapter has drawn two conclusions pertaining to why the orthodox cycle provides a superior explanation and understanding of developments in UK macroeconomic policymaking than that furnished by punctuated equilibrium. First, the orthodox cycle located a significant event, which initiated an orthodoxy phase in UK macroeconomic policymaking. This significant event was the 6th May 1997 announcement by Gordon Brown that the Bank of England would be granted operational responsibility for setting interest-rates. Second, the orthodox cycle explained that the new macroeconomic policymaking introduced by New Labour, rather than producing radical change in policy and ideas as expected by the model of punctuated equilibrium, served to institutionalise orthodox macroeconomic policy within the policymaking process.

Consequently, the orthodox cycle explained that macroeconomic policy saw the restoration of the full framework of orthodoxy after the election of New Labour, which is what we should expect to occur when monetary and fiscal policymaking reside in the orthodoxy phase of the orthodox cycle at the same time. For example, the new monetary policymaking framework led to continuity of the inflation target system, which continued to act as a monetary policy framework in the same manner as the Gold Standard and monetarism had previously. Furthermore, the new monetary policymaking framework institutionalised the orthodox objective of price stability as the priority objective for monetary policy. Finally, the MPC managed the inflation target system via implementation of the orthodox monetary policy instruments of the Bank Rate and OMOs.

In terms of fiscal policymaking, the new framework included operational changes to the system of public expenditure control and planning strengthened the Treasury its orthodox role as the guardian of the UK public finances. Meanwhile, the introduction of two new rules for fiscal policy need not have led to the restoration of orthodox fiscal policy. However, the orthodox cycle expounded that the fiscal rules were superseded during the 1997-2001 Parliament by the implementation of a deficit-reduction plan, which returned the UK public finances to fiscal orthodoxy. For example, the UK public finances returned after the election of New Labour to the orthodox outcomes for fiscal policy of an absolute surplus and reduction in national debt, which were achieved by the deployment of orthodox fiscal policy instruments of restraint in public expenditure and increases in indirect taxes.

The orthodox cycle also explained that the restoration of the full framework of orthodox macroeconomic policy included orthodox economic ideas. Here, the orthodox economic idea of internationalism was replaced by globalisation. The adoption of the economic idea of globalisation by New Labour was not classed as a change in economic ideas because the way that globalisation was interpreted and constructed by New Labour, Treasury and the Bank of England demonstrated significant continuity with previous interpretations and constructions of internationalism. The chapter highlighted that orthodox economic ideas were critical in the creation of the new institutional framework for macroeconomic policymaking. Furthermore, orthodox economic ideas were important in a number of macroeconomic policy developments, which is explained by the orthodox cycle as continuity of orthodoxy. First, the implementation of a five-year deficit-reduction plan. Second, the assignation of an orthodox hierarchy between macroeconomic policy instruments, which saw fiscal policy play a supportive role to monetary policy. Third, the rejection of discretionary fiscal policy strategy of demand management and the establishment of a division of responsibility between macroeconomic and microeconomic policy, which assigned to macroeconomic policy the objective of economic stability. Here, the chapter highlighted that economic stability was measured and defined by price stability, which ensured that the orthodox objective of price stability was the overall objective for macroeconomic

policymaking. Finally, the orthodox cycle explained that the prioritisation of economic stability as the objective of macroeconomic policy and the new macroeconomic policymaking framework designed to achieve that objective was legitimised by a distinctive policy narrative deployed by Gordon Brown. The following chapter will present a case-study of change and continuity in UK macroeconomic policy from the 7th June 2001 to the 26th June 2007.

Chapter 7

Change and Continuity in UK Macroeconomic Policymaking during the Blair Governments of the 7th June 2001 to the 26th June 2007

Introduction

This chapter consists of a case-study of United Kingdom (UK) macroeconomic policymaking from the 7th June 2001 to the 26th June 2007, which begins with the 2001 general election victory of New Labour and ends the day before the resignation of Tony Blair as Prime Minister (1997-2007). The purpose of this case-study is to see whether the orthodox cycle provides a superior understanding and explanation of change and continuity in UK macroeconomic policy than that furnished by punctuated equilibrium. Radical change in policy, ideas and institutions in the model of punctuated equilibrium is predicated on endogenous shocks, such as the election of a new government, or exogenous shocks, such as an economic crisis, to the policymaking process. Punctuated equilibrium posits that radical change that occurs in response to these shocks then forms a new policy equilibrium in policymaking, which exists until it is disrupted by the next endogenous or exogenous shock. In the absence of endogenous or exogenous shocks, punctuated equilibrium forecasts that stability ensures continuity in policy, ideas and institutions. If change does occur during a period of stability then punctuated equilibrium expects those changes to result in only superficial or minor adjustment to the existing policy equilibrium.

This chapter draws two conclusions. First, that the orthodox cycle provides a superior understanding and explanation of change and continuity in monetary policymaking after the 2001 general election than that furnished by punctuated equilibrium. However, the reasons for the superiority of the orthodox cycle are more nuanced than the example provided in the preceding chapter. For example, in Chapter Six, the orthodox cycle explained that the endogenous shock of the election of New Labour did not lead to radical policy and ideational change as macroeconomic policymaking entered a phase of orthodoxy on the 6th May 1997. Thus, the superiority of understanding provided by orthodox cycle in this case-study arises from its explanation of continuity in orthodox monetary policy from the 7th June 2001 to the 26th June 2007, rather, than continuity in the new radical policy equilibrium expected by punctuated equilibrium after the election of the Blair government on the 1st May 1997. The second conclusion is that neither the orthodox cycle nor punctuated equilibrium can explain the change in fiscal policy that occurred at the 2002 Budget. In the orthodox cycle, temporary deviation from orthodox policy occurs after a crisis phase, which was absent after the 2001 general election. Also absent from policymaking after the 2001 general election was an exogenous or endogenous shock. Furthermore, change in macroeconomic policy was far greater after the 2002 Budget than the minor or superficial policy adjustments during a period of stability envisaged by punctuated equilibrium.

The chapter will be organised in the following manner. The first section of the chapter focuses on monetary policymaking. It begins by documenting the change to the operational remit of the MPC announced at the 2003 Pre-Budget Statement. The chapter will then explain this operational change did not presage any fundamental alteration in the institutional framework established during the 1997-2001 Parliament, which continued to institutionalise orthodox monetary policy in the policymaking process. Operational changes introduced in 2005 and 2006 to the Sterling Monetary Framework are then discussed. Once again, the orthodox cycle expounds that these operational changes supported the implementation of orthodox monetary policy. Consequently, the orthodox cycle explains that monetary policymaking remained in the orthodoxy phase after the 2001 general election.

The following section of the chapter focuses on fiscal policymaking. This section of the chapter opens by briefly highlighting that the conditions for policy change described by the orthodox cycle and punctuated equilibrium were absent after the 2001 general election. Nevertheless, the chapter explains that the orthodox cycle provides a framework that allows the identification of when the departure from orthodox fiscal policy occurred, which happened at the 2002 Budget. The chapter continues to note that the departure from orthodox fiscal policy provided an increasing stimulus to domestic demand, which threatened two further areas of orthodox macroeconomic policy. First, it threatened the orthodox hierarchy between macroeconomic policy instruments. Second, it threatened the division of responsibility between macroeconomic and microeconomic policy established during the 1997-2001 Parliament. During this discussion, another development not anticipated by the orthodox cycle is highlighted, namely, the growing disjuncture between economic ideas in rhetoric and the formulation and implementation of fiscal policy. However, the chapter advances to note that, despite the stimulus to domestic demand, the departure from orthodox fiscal policy was not motivated by the adoption of economic ideas associated with demand management. This section of the chapter concludes with the provision of two tentative observations that may explain the departure from orthodox fiscal policy and discussion of the requirements for a future research agenda.

The Continuity of Orthodox Monetary Policy after the 2001 General Election

In the two and a half years after the 7th June 2001, Gordon Brown, Chancellor of the Exchequer (1997-2007), regularly affirmed that the operational remit for the MPC continued to be the setting of national interest-rates according to an annual inflation target of 2.5% RPIX and, subject to that, monetary policy could support the government's objective for high and stable levels of growth and employment. This

affirmation was provided by Brown (2002;2002a:1;2003a;2003b:1) at the 2002 and 2003 Budget Statement and a letter entitled *Remit for the Monetary Policy* Committee, which was sent from the Chancellor to the Governor of the Bank of England on the same day. The first change to the monetary policymaking framework after the 2001 general election was delivered by Brown (2003k) in his 2003 Pre-Budget Statement of the 10th December, when he announced that the inflation target in the operational remit for the MPC would adjust from 2.5% RPIX to 2% CPI[98].

This change in the operational remit for the MPC at the 2003 Pre-Budget Statement however did not presage any deeper or more fundamental change to the monetary policymaking framework, introduced during the 1997-2001 Parliament, other than a change in the measure in the inflation target. For example, continuity in the operational remit for the MPC after the 2003 Pre-Budget Statement was demonstrated by the Bank of England's (2004:1) *Inflation Report* of February 2004 – the first published after the 2003 Pre-Budget Statement – which stated that 'the government has set the Bank's Monetary Policy Committee (MPC) a target for the annual inflation rate of the Consumer Prices Index of 2%. Subject to that, the MPC is also required to support the government's objective of maintaining high and stable growth and employment'[99].

Brown (2003k) also affirmed in his 2003 Pre-Budget Statement that the inflation target in the remit for the MPC remained symmetrical after the operational change to 2% CPI inflation target[100]. For example, the Bank of England's (2004:36) *Inflation Report* of February 2004 noted that 'if inflation deviates by more than 1 percentage point from the [inflation] target the Governor is obliged to write an open

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[98] CPI stands for Consumer Prices Index.

[99] The new operational remit for the MPC of an annual inflation target of 2% CPI was affirmed in every subsequent Bank of England (2004:1;2004b:1;2004d:1; 2004f:12005:1;2005b:1;2005d:1;2005f:1;2006a:1;2006c:1;2006e:1; 2006g:1;2007:1 ;2007b:1) *Inflation Report* until end of the Blair Premiership and by Gordon Brown (2003l:1; 20004c:1;2005:1;2006a:1) in annual letters to the Governor of the Bank of England at each Budget Statement entitled *Remit for the MPC.*

[100] The continuity of the symmetrical inflation target and open letter system was affirmed by Brown (2002a:2-3;2003b:2-3;2003l:4;2004c:2-3;2005:2-3;2006a:2-3), before and after the change to the 2% CPI inflation target, in his annual letter to the Governor of the Bank of England, sent at each Budget Statement.

letter to the Chancellor explaining why, and how the MPC plan to bring inflation back to target'. Moreover, Brown affirmed, before and after his 2003 Pre-Budget statement, that the inflation target remained flexible[101]. For example, in his 2002 *Remit for the MPC* letter, dated the 17th April, Brown (2002a:2) that the monetary policymaking framework 'takes into account that any economy at some point can suffer from external events or temporary difficulties, often beyond its control. The framework is based on the recognition that the actual inflation rate will on occasions depart from its target as a result of shocks and disturbances. Attempts to keep inflation at the inflation target in these circumstances may cause undesirable volatility in output'.

Finally, the monetary policy framework and the Bank of England's traditional responsibility over the Bank Rate and orthodox role as guardian of monetary stability were protected on the 9th June 2003. In this statement to the House of Commons of the same day, Brown (2003d) declared that the UK economy had passed only one of the five economic tests required to join European Economic and Monetary Union (EMU) established on the 27th October 1997. If Brown and the Treasury had decided that the UK economy had passed these economic tests, then fundamental change in the monetary policymaking framework would have occurred as responsibility for setting UK national interest-rates passed from the MPC and Bank of England to the European Central Bank.

Consequently, the monetary policymaking framework after the 2001 general election, both before and after change in the operational remit of the MPC at the 2003 Pre-Budget Statement, continued to institutionalise orthodoxy in the formulation of policy. As a result, the orthodox cycle explains that monetary policymaking remained in the orthodoxy phase between the 7th July 2001 and the 26th June 2007. For example, the Bank of England's (2004:1) *Inflation Report* of February 2004 clearly established that the objective of the inflation target system of

[101] Brown (2003b:3;2003l:4;2004c:2;2005:2;2006a:2) affirmed the flexible nature of the inflation target, in the terms explained in this paragraph, in each annual letter entitled *Remit for the MPC* from the 2001 general election to the 26th June 2007.

monetary management was ‘to maintain price stability’[102]. Indeed, Ed Balls[103] and Gus O’Donnell[104] (2002:12) argued that the inflation target represented the best means to achieve price stability as its allowed policymakers to take into account all of the factors that affect inflation. Furthermore, price stability continued to be identified as a ‘precondition’ for the wider economic objectives of high and stable levels of growth and employment by figures in New Labour, Bank of England and HM Treasury[105]. That monetary policymaking remained in the orthodoxy phase is also demonstrated via the MPC’s choice of policy instruments to implement monetary policy and meet the inflation target, which continued to be Bank Rate and Open Market Operations (OMOs). Consequently, inflation-targeting continued to operate as a monetary framework after the 2001 general election, which guided monetary policymakers in operational decisions pertaining to orthodox monetary policy instruments in pursuit of the orthodox objective of price stability.

The continuity of the orthodox instrument of the Bank Rate in the implementation of monetary policy was affirmed in the 2002 Bank of England (2002:4) ‘Red Book’. Here, the Bank of England claimed that it derived its influence over market interest-rates because of its monopoly supply of central bank money (reserves and banknotes) to the banking system, which provided the only form of final settlement available for Sterling payments. The price at which the Bank of England met this demand for central bank money was established by the Bank Rate decided upon by the MPC. As a result, the Bank of England (Ibid) contended that the Bank Rate ‘influence[d] other short-term Sterling wholesale lending and deposit

[102] The objective of the 2% CPI inflation target to ‘maintain price stability’ was affirmed by every subsequent Bank of England (2004:1;2004b:1;2004d:1;2004f:1; 2005:1;2005b:1;2005d:1;2005f:1;2006a:1;2006c:1;2006e:1;2006g:1;2007:1; 2007b: 1) *Inflation Report* between May 2004 and May 2007.

[103] Ed Balls was Chief Economic Adviser to Gordon Brown and HM Treasury (1994-2004) and Economic Secretary to the Treasury (2006-2007).

[104] Gus O’Donnell served as Permanent Secretary for HM Treasury (2002-2005).

[105] Price stability was identified as a ‘precondition’ for high and stable levels of growth and employment by Brown (2002a:3;2003b:3;2003l:4;2004c:3;2005:3; 2006a:3), in his letters to the Governor of the Bank of England entitled *Remit for the MPC,* in public speeches by Edward George (2001d:2;2001e:2;2002a:2;2002b:2; 2002c:2) and by Balls and O’Donnell (2002:4,10,12,44-45).

rates as well as commercial banks' base rates, and hence the structure of rates across the economy as a whole'. Consequently, the 2002 'Red Book' established that the MPC continued to operate monetary policy in the orthodox manner described in Chapter Six, which saw the MPC would achieve its inflation target through the Bank Rate, which was used to manage short-term market interest-rates and credit conditions in the UK economy[106].

The Bank of England met the demand for central bank money and provided liquidity to the banking system through the orthodox monetary policy instrument of OMOs[107]. For example, the Bank of England (2002:4,8-12) explained in the 2002 'Red Book' that it supplied central bank money to the banking system and 'implemented the monetary policy committee's interest rate decisions' through 'open market operations conducted… in high quality credit quality market instruments'. The 2002 'Red Book' (Ibid) established that the majority of the OMOs conducted by the Bank of England were repo (sale and repurchase) agreements with financial institutions in a range of securities often with a two-week maturity. The rate charged on these repo agreements was a rate deemed necessary to bring market interest-rates towards the Bank Rate. Finally, the 2002 'Red Book' (Ibid) noted that Bank of England also conducted outright purchases of eligible securities from the banking system. The range of securities considered eligible for OMOs, either through repo or outright purchase, included gilts, HM government Sterling debt, Treasury bills, Euro-denominated securities and eligible bank bills and local authority bills.

Operational change within the Bank of England's Sterling Money Market Framework (SMMF) did occur after the 2002 'Red Book' through the introduction of a new system of 'voluntary reserve-averaging' to the Sterling money market

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[106] The Bank of England (2006:5) affirmed that the Bank Rate established by the MPC was used as the price to provide central bank money and liquidity to the banking system, which influenced market interest-rates, in its 2006 'Red Book'.

[107] The role of OMOs in monetary management, in the manner described by this paragraph, was affirmed by the Bank of England (2001c:277-282;2001e:383-387; 2002b:19-22;2002d:141-146;2002f:260-261;2002h;368-370;2003a:17-19;2003c: 160-163;2003e:267-270;2003g:403-406;2004a:16-19;2004c:126-130;2004e:277-281;2004g:409-413;2005a:18-22;2005c:135-139;2005e:319-323;2005g:416-423; 2006b:19-23;2006d:138-141;2006f:283-288;2006h:366-372;2007a:161-21;2007c; 201-206) in successive *Quarterly Bulletins* from the Autumn 2001 onwards.

framework. The operational change to ‘voluntary reserve-averaging’ was outlined by Paul Tucker, member of the MPC (2002-2013) and Deputy Governor of the Bank of England (2009-2013), in a speech on the 28th July 2004. In this speech, Tucker (2004) identified that under the operation of the SMMF that was in place prior to ‘voluntary reserve-averaging’, Sterling settlement banks were required to ensure non-negative balances with the Bank of England over a one-day maintenance period, which required settlement banks to borrow from the Bank of England through OMOs. As a result, the Bank of England needed to engage in OMOs with the Settlement Banks at a rate of three to four times per day.

The new system of ‘voluntary reserve-averaging’ was formally introduced at the beginning of 2006 and the operation of the new system was explained in the Bank of England (2006:3-6) 2006 ‘Red Book’. Henceforth, banks and building societies were expected to hold target balances (reserves) with the Bank of England over a monthly maintenance period, which was set at a voluntary level by the financial institution. If the bank/building societies average balance over the monthly maintenance period was within a specified range around the voluntary reserve then their balance with the Bank of England would be remunerated at the Bank Rate. The primary method of supplying banks and building societies with central bank money, which allowed financial institutions to meet their target balances and satisfy its demand for banknotes continued to be OMOs. However, the new system of ‘voluntary reserve-averaging’ also saw the introduction of new standing facilities for deposits and lending at the Bank of England, which could be used on demand by banks and building societies to meet their target balance. Thus, banks and building societies would have a choice between OMOs and the standing facility when seeking to achieve their target balance at the end of the monthly maintenance period. The caveat was that use of the standing facility carried with it a heavy interest-rate penalty when compared with the Bank Rate to encourage banks/building societies to engage in OMOs.

Once again, the orthodox cycle can account for the introduction of ‘voluntary reserve-averaging’ as an operational change to the Bank of England’s SMMF, which supported the implementation of orthodox monetary policy and led to continuity of

orthodoxy in the monetary policymaking process. First, the fundamental purpose of the new system of 'voluntary reserve-averaging' in the SMMF remained the exertion of influence on market interest-rates so that they were brought into line with the Bank Rate set by the MPC. For example, the Bank of England (2006:3,5) 'Red Book' of 2006 asserted that the primary objective of operations in the Sterling money market was 'to ensure that short-term Sterling market interest-rates are consistent with the official Bank Rate' whilst 'meeting the liquidity needs, and so contributing to the stability of, the banking system as a whole'. This was echoed in the Q3 2006 *Quarterly Bulletin* published by the Bank of England (2006f:283), which stated that the Bank's management of its balance sheet was 'related to the implementation of monetary policy through establishing the official bank rate in the money markets'.

Furthermore, the operational change in the SMMF to 'voluntary reserve-averaging' significantly strengthened the role of the orthodox monetary policy instrument of OMOs in monetary management, which ensured the continuity of orthodox monetary policy. For example, as part of the new system of 'voluntary reserve-averaging', the Bank of England (2006b:22) allowed financial institutions to engage in longer-term repo agreements with the Bank in securities at a maturity of three, six, nine and twelve months, which would be charged at fixed interest-rates. Meanwhile, instead of offering OMOs to the financial markets on a daily basis, the Bank of England (Ibid) announced it would only offer OMOs weekly. Consequently, the Bank of England's (Ibid) Spring *Quarterly Bulletin* noted that the operational change to 'voluntary reserve-averaging' would 'increase significantly the amount of funds that the Bank needs to provide via OMOs' so that banks/building societies could avoid use of the standing facility[108].

[108] The Bank of England (2006f:287) also noted in its Q3 2006 *Quarterly Bulletin* that the new system of 'voluntary reserve-averaging' would increase the amount of OMOs conducted by the Bank.

The Departure from Orthodox Fiscal Policy at the 2002 Budget

Policy change in punctuated equilibrium is predicated on endogenous or exogenous shocks to policymaking from politics or the economy, which disturbs policy equilibrium. However, these shocks were absent after the 2001 general election. Indeed, the 2001 and 2005 general election victories by New Labour maintained political stability and ensured the longevity in office of key figures in fiscal policymaking from the 1997-2001 Parliament such as Blair, Brown, Balls and O'Donnell. Meanwhile, whilst sources of economic instability weren't absent in the world economy in the late 1990s and early 2000s, the growth rate of the global economy remained strong and did not provide an exogenous shock to UK economic stability and macroeconomic policymaking after the 2001 general election[109]. For instance, having emerged from recession during 1992, the UK economy proceeded to enjoy sixty-two consecutive quarters of economic growth (Q2 1992 – Q4 2007) under successive Conservative and Labour Chancellors of the Exchequer. This strong economic performance included forty-two consecutive economic quarters of growth after the election of New Labour in Q2 1997 until Q4 2007, forty quarters of which occurred under the Chancellorship of Gordon Brown (ONS,2015a).

The dynamics necessary for the orthodox cycle to explain change in fiscal policymaking at the 2002 Budget, however, were also absent after the 2001 general election. In the orthodox cycle, temporary deviation from orthodox macroeconomic policy is explained as a consequence of a previous crisis phase in macroeconomic policymaking. The crisis phase in the orthodox cycle consists of a series of events and emergencies, which are interpreted and designated by narratives in political discourse as a crisis that require an economic policy response.

[109] Sources of economic instability in the world economy included the 1997-1998 Asian Financial Crisis and the 2000-2002 Dot.Com collapse and Stock Market Crash, which contributed to recession in the United States economy in 2001 and French and German economy in 2001-2002. Despite these sources of economic instability, the lowest global GDP growth rate was 1.975% in 2001 and the annual average GDP growth rate was 3.783% from 1997 to 2007 (World Bank,2016).

At no point however after the 2001 general election was economic instability in the global economy interpreted and designated by narratives as an economic crisis for the UK economy. For example, Edward George, Governor of the Bank of England (1993-2003) declared to the Treasury Committee (2003a:Ev.13,Q.63) on the 24th June 2003 that whilst UK economic growth had slowed in the early 2000s, economic events and emergencies were "primarily a global economy shock' whose "impact [fell] on the global macro economy". In fact, the dominant narrative in political discourse was the opposite from the explanation of the crisis phase in the orthodox cycle. Specifically, a narrative was deployed by Brown to legitimise the macroeconomic policymaking framework introduced after the 1997 general election, which, it was claimed, had helped the UK economy navigate economic instability in the global economy and secure growth and stability in the UK economy. For example, in his 2002 Budget Statement on the 17th April, Brown stated due to the "new monetary and fiscal framework, we have been able to steer a steady course of stability". Furthermore, in his 2002 Pre-Budget Statement of the 27th November, Brown (2002g) claimed the macroeconomic policymaking framework had meant the UK economy had avoided recession unlike Japan, US and Germany and achieved economic growth that was "strongest of the major economies". The absence of a crisis phase or an endogenous or exogenous shock means that neither the orthodox cycle nor punctuated equilibrium can provide an understanding or explanation of the change that occurred in fiscal policymaking from the 2002 Budget onwards.

In the previous chapter, the orthodox cycle expounded that, despite increases in public expenditure and public sector net investment in the 2000 Budget, 2000 Spending Review (SR) and 2001 Budget, public spending continued to be characterised by restraint throughout the 1997-2001 Parliament and fiscal policy remained orthodox. The consequence of this continued restraint in public spending is demonstrated in Table One, which shows that fiscal policy outcomes prevailed in 2001-2002. For example, the Current Budget deficit and Primary Balance all remained in surplus and Public Sector Net Debt was reduced by a further 0.6% GDP from 2000-01. Meanwhile, Public Sector Net Borrowing ran into deficit of just 0.1% GDP, well within the margin of error of an orthodox balanced budget.

Table One also identifies however that 2002-2003 saw the departure from orthodox fiscal policy outcomes. For instance, Public Sector Net Borrowing increased from a deficit of 0.1% GDP in 2001-2002 to peak at 3.4% GDP in 2004-2005. Furthermore, the Current Budget and Primary Balance moved from surplus to deficits involving a fiscal loosening of 2.8% GDP and 3.5% GDP respectively at their peak levels. Finally, whilst deficits in the UK public finances reached their peak in 2004-05 and fell thereafter, once Public Sector Net Borrowing, the Current Budget and Primary Balance are cyclically-adjusted, we can begin to see the scale of the departure from orthodox fiscal policy outcomes from 2002-03 onwards.

Table One: Government Borrowing and National Debt during the Blair governments, 2001-2007

Years	**Public Sector Net Borrowing** (% of GDP) *(+ = Deficit)*	**Cyclically-Adjusted Net Borrowing** (% of GDP) *(+ = Deficit)*	**Current Budget Deficit** (% of GDP) *(- = Surplus / + = Deficit)*	**Cyclically-Adjusted Current Budget Deficit** (% of GDP) *(- = Surplus / + = Deficit)*	**Primary Balance** (% of GDP) *(+= Surplus / - = Deficit)*	**Cyclically-Adjusted Primary Balance** (% of GDP) *(+ = Surplus / - = Deficit)*	**Public Sector Net Debt** (% of GDP)
2001-02	+0.1%	+0.7%	-1.1%	-0.5%	+1.6%	+0.9%	29.3%
2002-03	+2.3%	+2.4%	+1.0%	+1.1%	-0.8%	-0.9%	30.3%
2003-04	+2.6%	+2.9%	+1.4%	+1.7%	-1.1%	-1.4%	31.8%
2004-05	+3.4%	+4.1%	+1.7%	+2.3%	-1.9%	-2.5%	34.3%
2005-06	+3.1%	+3.6%	+1.2%	+1.7%	-1.5%	-2.0%	35.4%
2006-07	+2.6%	+3.1%	+0.6%	+1.2%	-0.9%	-1.4%	36.1%

(**Source:**OBR, 2016)

The Treasury (2002b:4;2003:4) claimed in the 2002 Pre-Budget and 2003 Budget Reports that government borrowing was a consequence of instability in the global economy, which had caused tax revenue to fall. Meanwhile, in oral evidence to the Treasury Committee (2002a;Ev.59,Q.136) on the 12th December 2002, Brown claimed that the fiscal deficit was a consequence of allowing the automatic stabilisers

operate in response to economic instability from the collapse of the Dot.Com boom and stock market crash. Had the automatic stabilisers been the cause of the departure from orthodox fiscal policy outcomes, fiscal policymaking would have remained in the orthodoxy phase. However, Table Two demonstrates that, despite these claims by Brown and the Treasury, the rise in government borrowing being the sole result of the operation of the automatic stabilisers is only tenable in 2002-2003, which saw a dramatic fall in tax receipts. For example, Table Two shows that public sector current receipts and national account taxes had largely recovered to their 2001-2002 level by 2004-2005 and had exceeded that level in 2006-2007. Meanwhile, Table One shows that the UK public finances remained in significant deficit from 2004-2005 onwards. If rising government borrowing from 2002-2003 onwards had been the product of the decision to allow the automatic stabilisers to operate in the face of economic instability in the world economy, then the resurgence of tax revenue by 2004-2005 would have meant the UK public finances returned in that year to the balance of 2001-2002, before the dramatic fall in tax receipts of 2002-2003. That government borrowing remained in substantial deficit after 2004-2005 demonstrates that the departure from orthodox fiscal policy outcomes was not a consequence of the automatic stabilisers.

Chapter Six identified that the fiscal rules established in the 1997 Budget did not institutionalise permanent fiscal orthodoxy in the public finances. Here, Table Two highlights that the most significant factor in the departure from orthodox fiscal policy outcomes was a corresponding departure from the orthodox fiscal policy instrument of public spending restraint. For example, Table Two shows that total managed expenditure (TME) (2014/15 prices) rose by £130.7billion from 2001-2002 to 2006-2007. Furthermore, Table Two allows us to identify that increases in TME (2014/15 prices) was largely a product of increased public sector current expenditure, which increased by £111.2billion from 2001-2002 to 2006-2007. Indeed, such was the rate of expansion in TME and public sector current expenditure that both rose after the 2001 general election significantly above the percentage of GDP inherited by New Labour on the 1st May 1997. Finally, public sector net investment increased by 0.8% GDP after the 2001 general election.

Table Two: Public Expenditure and Taxation during the Blair governments, 2001-2007

Years	**Total Managed Expenditure** (% of GDP)	**Total Managed Expenditure** (£billions) *(2014/15 Prices)*	**Public Sector Current Expenditure** (% of GDP)	**Public Sector Current Expenditure** (£billions) *(2014/15 Prices)*	**Public Sector Net Investment** (% of GDP)	**Public Sector Current Receipts** (% of GDP)	**National Account Taxes** (% of GDP)
2001-02	37.1%	£548.5	34.0%	£502.2	1.2%	37%	34.6%
2002-03	37.9%	£577.1	34.6%	£526.6	1.3%	35.6%	33.2%
2003-04	38.7%	£609.6	35.6%	£650.8	1.2%	36.1%	33.8%
2004-05	40.1%	£644.4	36.5%	£585.9	1.7%	36.7%	34.4%
2005-06	40.1%	£666.4	36.2%	£602.6	1.9%	37.0%	34.5%
2006-07	39.9%	£679.2	36.0%	£613.4	2.0%	37.3%	34.9%

(**Source:**OBR, 2016)

Whilst the orthodox cycle may not have anticipated nor explained this departure from orthodox fiscal policy after the 2001 general election, nevertheless, the orthodox cycle does provide us with an understanding of when the departure from orthodox fiscal policy occurred. Specifically, it enables us to locate the departure from orthodox fiscal policy at the 2002 Budget of the 17th April. Here, Table One shows that the fall in taxation revenue in 2002-2003 conspired to turn previous spending restraint into a deficit in Public Sector Net Borrowing of 2.3% GDP. Consequently, at the 2002 Budget, Brown and the Treasury had a choice in fiscal policymaking. First, they could continue to implement restraint in public spending

and allow the automatic stabilisers to operate, which would have ensured fiscal policymaking remained in the orthodoxy phase. Second, they could increase the growth rate of public expenditure, which would cause a discretionary departure from orthodox fiscal policy outcomes in the UK public finances.

At the 2002 Budget the second course of action was taken. For example, Brown (2002) announced in his 2002 Budget Statement that the public spending envelope for Total Managed Expenditure (TME) would expand in the next three years from £390billion in 2001-02 to £471billion in 2004-05, a rise of £81billion. Furthermore, public sector net investment would increase by 2004-05 to account for 2% GDP. A significant beneficiary of this expansion of public spending would be the National Health Service (NHS), which would see a rise in spending on average of 7.4% in real terms per annum. In order to help pay for this increase in spending on the NHS, Brown (Ibid) introduced a 1% tax increase on National Insurance contributions from employers, employees and the self-employed on earnings above £4615. Thus, the 2002 Budget departed from fiscal orthodoxy not only via the significant expansion of public spending on the public services, but also through the introduction of a specific increase in direct tax for the purposes of public spending, rather, than as a policy instrument to reduce government borrowing.

Subsequently, the Treasury (2002a;5-7) 2002 SR Report projected that TME was expected to rise from £418.4billion in 2002-03 to £511.4billion in 2005-06, which equated to an increase of 4.3% in real terms per annum. In total, the Treasury stated that current public spending (including public sector net investment) was expected to climb by 3.3% in real terms per annum by 2004-05, with 41% of that annual increase spent on health and personal services, 23% on education and 9% on transport. The expansion of public expenditure would be maintained at subsequent Budgets and SR's – albeit at a lower rate of growth in real terms per annum - for the remainder of Tony Blair's period as Prime Minister and Gordon Brown's Chancellorship until the 26th June 2007. For example, Brown (2004b) announced in his 2004 Budget Statement that there would be a further 2.5% real terms per annum increase in current public spending over the next three years and an expansion of

public sector net investment from 2% GDP to 2.5% GDP. Furthermore, the Treasury (2007:5) Budget Report of 2007 announced that public spending would rise on average by 1.9% in real terms per annum for the proceeding three years and public sector net investment would be held at 2.5% GDP. The Treasury's (2007a:12) *Public Expenditure and Statistical Analysis,* published in April 2007, reported that impact of this cumulative expansion in public sector spending had increased total managed expenditure, departmental expenditure limits and annual managed expenditure in the six years between 2001-02 and 2007-08 by £124billion, £82billion and £46.5billion respectively.

The previous chapter identified that a key determinate in macroeconomic policy formulation during the 1997-2001 Parliament was the desire to establish the credibility of New Labour in economic policymaking (Faucher-King & Le Gales,2010:18-19). However, developments in fiscal policymaking from the 2002 Budget onwards ensured that hard-won credibility was lost. Furthermore, the loss of credibility in fiscal policymaking exposes something else unanticipated by the orthodox cycle, namely, the growing disjuncture after the 2001 general election between the orthodox economic ideas deployed in rhetoric and the reality of the departure from orthodox fiscal policy on macroeconomic policymaking.

The growing disjuncture between orthodox economic ideas and the formulation and implementation of fiscal policy was evident in the continued rhetorical appeals made to the orthodox economic idea of globalisation. In similarity with the 1997-2001 Parliament, the orthodox economic idea of globalisation had four elements in its construction in discourse in public speeches and policy documents. First, the mobility of capital, factors of production and trade in goods and services in global economy was causing rapid economic change. Second, the UK economy was cast as an integrated part of this emerging system of global economy. Third, it was argued that UK economic prosperity would be secured not by rejecting globalisation but by deepening the interconnection of the global and domestic economy. Fourth,

the role of macroeconomic policy in the global economy was to secure economic stability[110].

The first element in the construction of the orthodox economic idea of globalisation, for instance, is available in the 2005 Treasury (2005:2) Budget Report, which stated that 'the international economy is becoming increasingly integrated through greater cross-border trade and investment, driven in part by rapid advances in technology. Production processes are becoming increasingly flexible, dispersed across continents'. Similarly, the 2006 Treasury (2006:2) Budget Report highlighted that 'the global economy is undergoing a major transformation, with far-reaching and fundamental changes in technology, production and trading patterns. Faster information and falling transport costs are breaking geographical barriers to economic activity. The boundary between what can and cannot be traded is being steadily eroded'.

The second and third elements of the construction of the orthodox economic idea of globalisation were evident in public speeches by Blair and Brown. For example, in a speech on the 22nd March 2004, Blair (2004) posited that "globalisation is not our enemy but our friend" that "presents us with a choice: embrace it and make it work for us; or try to thwart it". Here, Blair (Ibid) argued that New Labour would embrace globalisation in the modern era as the UK economy had in earlier periods of

[110] These four elements in construction of the orthodox economic idea of globalisation were evident in public speeches by senior figures in New Labour such as Blair (2001;2002;2003;2004:2004b;2005;2005a;2006;2006a), Brown (2001c: 2001d;2001f;2001f;2002c;2002e;2003c;2003e;2003g;2003j;2004i;2004l;2005b; 2005d;2005e;2006b;2006c;2006d;2006e;2007a;20007b) and Balls (2003;2006; 2006a;2006b;2006c;2007b;2007c). Furthermore, this construction of globalisation was evident in public speeches by Cabinet ministers such as Blunkett (2005) and Hewitt (2001;2003a) and junior ministers at the Treasury such as Boateng (2001;2002), Browne (2005;2006), Kelly (2004), Lewis (2005) and Murphy (2007). Moreover, this interpretation of the economic idea of globalisation is available in policy documents by the Bank of England (2005f:5), Department of Trade and Industry (DTI) (2004;2004a) and Treasury (2002a:1-2;2004a:3,Box1:1;2006; 2006a:1-2). Finally, this construction of the orthodox economic idea of globalisation can also be located in the public speeches of Bank of England officials, Treasury officials and MPC members such as Bean (2006), Clementi (2001), George (2001f;2002:2), Gieve (2006;2006a:2), King (2004:1;2005;2005a:3-4;2006:2), Large (2004), Lomax (2005:1), MacPherson (2005) and Plenderlieth (2001).

economic history, when this “island nation built its fortunes on trade: on our willingness to open up to the world” and the “attendant flow of goods, people and ideas”. Meanwhile, Brown identified the City of London as the success story of UK economy, which offered lessons for economic policy in the age of globalisation. For example, in his *Mansion House* speech on the 21st June 2006, Brown (2006c) contended that “the message London’s success sends out to the whole British economy is that we will succeed if like London we think globally”, which meant economic prosperity rested on the acceptance of competition, competitive tax rates, light-touch regulation, flexibility and investment in skills.

The result of the continued appeal in to the economic idea of globalisation was that credibility was still identified in rhetoric as important in the formulation of macroeconomic policymaking[111]. For example, Balls and O’Donnell (2002:33,35,37) claimed that credibility was ‘the elusive elixir of modern macroeconomics’, which rapid globalisation - understood as process of technological change, capital market liberalisation and growth in international trade - had made ‘more rather than less important’. Globalisation had enhanced the need to secure credibility, according to Balls and O’Donnell (Ibid), because it meant ‘markets immediately punish any government which strays from the macroeconomic straight and narrow’. In contrast, governments that are judged by the market to be implementing the correct macroeconomic policies ‘can attract inflows of investment capital at higher speed, greater volume and lower cost’.

The fourth element in the construction of the economic idea of globalisation was affirmed by Balls and O’Donnell’s claim that macroeconomic stability would be achieved in the age of globalisation through the logic of constrained discretion, which Balls originally introduced in 1997. Macroeconomic stability would be achieved, Balls and O’Donnell (2002:27) claimed, through four ‘post-monetarist’

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[111] The importance of confidence and credibility was signposted in a number of Bank of England (2003b:40;2004:11;2006d:33) policy documents and a public speech by Blair (2003b). However, the most important mention of the importance of confidence and credibility were made by Brown (2001a;2003c), Balls (2001:2002a;2003; 2004a;2007), Balls and O’Donnell (2002:8,28,93), Bhundia and O’Donnell (2002) and O’Donnell (2004), which posited that discretion in economic policymaking was only possible within a framework that commands market credibility and public trust.

principles for macroeconomic policymaking. First, the principle of stability through constrained discretion. Here, discretionary macroeconomic policy was constrained by the need to secure credibility, which would be achieved by the second, third and fourth principles of sound, long-term policies, maximum transparency and pre-commitment to rules-based policymaking. Thus, Balls and O'Donnell (2002:x,95) stated that discretion was only possible 'within an institutional framework that commands market credibility and public trust with government constrained to deliver clearly defined long-term policy objectives, maximum openness and transparency and clear and accountable divisions of responsibility with macroeconomic policymaking'.

The fiscal rules introduced at the 1997 Budget were the two most important measurements of credibility in fiscal policymaking. First, the golden rule stipulated that the Current Budget must be balanced across the economic cycle. Second, the sustainable investment that required national debt to be held under 40% GDP. Measurement of the golden rule for fiscal policymaking, however, was complicated by the need to accurately date the economic cycle. Indeed, O'Donnell admitted in oral evidence to the Treasury Committee (2002a:Ev.41,Q.156-157) on the 10th December 2002 that "if we were sailing very close to the wind on the golden rule… then you would find the timing of the cycle mattered a lot". Table Three shows that, under the Treasury's own forecasts, the increase in public expenditure, government borrowing and national debt from the 2002 Budget onwards meant the public finances came close to breaching both fiscal rules.

<u>Table Three: Treasury Forecasts on the Fiscal Rules, 2002-2007 Budget</u>

Treasury Budget Report	**Average Surplus on the Current Budget across the Economic Cycle** (% of GDP)	**Net Debt to GDP Ratio** (% of GDP)
2002 Budget	0.7%	31%
2003 Budget	0.5%	33.8%
2004 Budget	0.1%	36.5%
2005 Budget	0.1%	37.1%
2006 Budget	0.1%	38.4%
2007 Budget	0.1%	38.8%

(Source:HM Treasury,2002;4;2003:5;2004:4;2005:4;2006:4;2007:3-4**)**

There was a growing disjuncture, however, between the rhetorical appeals to globalisation and credibility and the formulation and implementation of fiscal policy after the 2002 Budget. For example, judgement pertaining to whether Brown and the Treasury were meeting the golden rule for fiscal policymaking was complicated by the fact that the timing of the economic cycle was altered on no less than three occasions by Brown and the Treasury after the 2001 general election, which lost "a significant amount of market credibility and confidence" in fiscal policymaking (Lee,2010:21). Furthermore, observers of fiscal policymaking noted the potential cynical motivations behind these changes in the timing of the economic cycle. For example, the 2006 and 2007 IFS (2006:1;2007:1-2) *Green Budgets* highlighted that change in the timing of the economic cycle only started to occur when downward revisions to the public finance forecasts meant the fiscal rules were close to being broken, which threatened 'undermining the credibility of the fiscal framework'.

Furthermore, credibility in the golden rule was eroded as several observers of fiscal policymaking came to believe that the Treasury's forecasts that the fiscal rules would be met in the future was based on over-optimistic projections of future economic growth and taxation revenue. For example, members of the Treasury Committee (2002a:Ev.34,Q.63-65,Ev.50-51,Q.228,Q.230-237;2003:Ev.1,,2,3,6-7,49-51,Q.297-298,Q.300-303,Q.305-308;2006: Ev.21,Q.124) regularly complained to Brown and Treasury officials that projections of future economic growth of 3.5% GDP per annum and tax growth were optimistic. Furthermore, the over-optimistic forecasts for economic growth and tax revenue was noted in written evidence provided to the Treasury Committee (2005:Ev.63-71) by the Confederation of British Industry.

Consequently, the fiscal rules came under increasing criticism after the 2001 general election as their adequacy as a constraint on fiscal policymaking were brought into question by domestic and global actors[112]. For example, the IFS (2003:2) claimed in their 2003 *Green Budget* that Brown and the Treasury were in danger of missing the golden rule for fiscal policy in the next economic cycle, which at that point was due to end in 2005-2006, unless public expenditure was reduced and taxes increased. Indeed, the IFS (Ibid) stated that Brown and the Treasury would not 'avoid such measures for long without undermining the credibility of the fiscal rules'. The IFS (2004:1;2005:1) repeated their call for public expenditure reductions and tax increases to meet the golden rule in the next economic cycle in their *Green Budgets* of 2004 and 2005. Similarly, the IMF (2005:3,7,8,17;2006:17-18) and OECD (2004:12,67,92;2005:14,30-33) argued that fiscal consolidation through public expenditure restraint or reduction and tax increases was necessary. First, to reduce the fiscal deficit and ensure the golden rule was met in the next economic cycle. Second, so that the credibility of fiscal policymaking was not diminished. Finally, the IFS' (2007:1) 2007 *Green Budget* posited that in order to return the Current Budget to balance and halt the rise in Public Sector Net Debt, a cumulative

[112] Criticism of the fiscal rules and the size of government borrowing after the 2001 general election, for example, was made by the IMF (2002a;2003a;2004a;2005a; 2006a) and the IFS (2003:10;2004:9-21).

consolidation in the public finances of 1.6% GDP, consisting of a 0.8% GDP worth of cuts to public spending and a 0.8% GDP rise in the overall tax burden, needed to be implemented. In effect, the IFS argued that the UK public finances required a phase of orthodoxy in fiscal policymaking so the fiscal rules could be met.

The departure from orthodox fiscal policy at the 2002 Budget, however, had a further impact than just damage to the credibility of the fiscal rules. Specifically, rising public expenditure and government borrowing increasingly contributed a stimulus to domestic demand, which exacerbated weaknesses in the composition of economic growth. For example, the 2001 IMF (2002:4) *Article IV Consultation Report* warned that economic growth 'has been sustained primarily by domestic demand… private consumption and public spending, rather than private investment, have been the main driving force' with rising house prices and an over-extension of credit to households and corporations a particular worry. The 2002 IMF (2003:4,7,13,15) *Article IV Consultation Report* re-stated these fears and highlighted that 'domestic demand [was being]… sustained… by fiscal expansion' as economic growth became reliant on public spending and consumption driven by the accumulation of household debt based on a house price boom. The 2002 OECD (2002:10-11) *Economic Survey of the UK* also stated that 'fiscal measures on both the tax and spending side provide for a significant demand stimulus'. Moreover, the 2003 IMF (2004:4,5,12-16) *Article IV Consultation Report* repeated their criticism that economic growth was reliant on the domestic demand generated by expansionary fiscal and monetary policies and increasing accumulation of household debt due to rising house prices. Consequently, the 2005 IMF (2006:4) stated that 'the shallowness of the UK growth slowdown during the last global downturn reflected in part the most aggressive fiscal expansions of any G7 country'.

Furthermore, the persistent departure from orthodox fiscal policy after the 2002 Budget, meant that fiscal policy continued to stimulate domestic demand long after it was necessary from the perspective of macroeconomic stabilisation as global growth levels recovered from 2003 onwards (World Bank,2016). Thus, the 2005 IMF (2006:7) *Article IV Consultation Report* noted that, whilst fiscal policy may have played a counter-cyclical role in 2001-2002 and 2002-2003, fiscal policy played

a pro-cyclical role in the UK economy from 2003-2004 onwards, which led to a growing structural deficit and rising national debt. The pro-cyclical role for fiscal policy was also identified by the IFS (2006:1,7) in their 2006 *Green Budget*, which highlighted that most independent economists thought that the Treasury's belief there was still an output gap in the UK economy was misguided and, in reality, the UK economy was operating at close to full capacity and the fiscal deficit in the public finances was structural, rather than cyclical. The 2004 and 2005 IMF (2005:9-10;2006:3,11) *Article IV Consultation Report* and the 2005 OECD (2005:26) *Economic Survey of the UK* also stated their belief that the UK economy did not have an output gap and was operating at full capacity. Only one individual within the Treasury went on public record to note that rising deficits after the 2002 Budget may be structural. In oral evidence to the Treasury Committee (2004:Ev.31,Q.184) on the 23rd March 2004, Jon Cunliffe, Managing Director of Macroeconomic Policy and International Finance and Second Permanent Secretary at the Treasury (2002-2007), admitted that the fiscal deficit was 40% structural due to a permanent injection of resources into the public services.

The impact of this pro-cyclical fiscal stimulus to aggregate demand economy contributed to a build-up of inflationary pressure in the UK economy. In turn, the build-up of inflationary pressure threatened to reverse the implementation of the orthodox hierarchy between macroeconomic policy instruments, which sees fiscal policy play a supportive role to monetary policy in pursuit of the orthodox objective of price stability. Indeed, it is instructive that after the 2001 general election, as the fiscal deficit rose ever higher, there was no reference in public speeches by Brown and Balls of the orthodox economic idea of crowding-out, which was a key economic idea that allowed actors to determine that the appropriate relationship between macroeconomic policy instruments lay in the orthodox hierarchy. Once again, a disjuncture is apparent between the rhetoric of public speeches and policy documents and the formulation and implementation of fiscal policy from the 2002 Budget onwards. For example, it was articulated in public speeches and policy documents that the fiscal policy continued to play a supportive role to monetary policy in

macroeconomic policymaking[113]. Thus, in oral evidence to the Treasury Committee (2001:Ev.40,Q.269) on the 4th December 2001, Brown stated that this prudent approach to the public finances had allowed the Bank of England to pursue monetary activism in response to instability in the global economy, which had "brought interest rates down" to their lowest rate "for nearly forty years". Indeed, the MPC had lowered the Bank Rate from 5.75% on the 8th February 2001, five months prior to the 2001 general election, to 3.5% on the 10th July 2003 (Bank of England,2016a).

The MPC however had to raise the Bank Rate in successive stages from 3.5% until it reached 5.75% on the 5th July 2007, just eight days after Blair's resignation at a special Labour party conference on the 27th June 2007, in order to contain inflationary pressure in the UK economy (Ibid). Indeed, on the 16th April 2007, Mervyn King, Governor of the Bank of England (2003-2013) was forced to write the first *open letter* to the Chancellor since the introduction of the symmetrical inflation target on the 12th June 1997, when CPI inflation rose above the 3% trigger point to stand at 3.1%. In his open letter, King (2007) stated that half of the rise in CPI inflation from 1.8% in April 2006 to 3.1% in April 2007 was due to increasing domestic energy costs and global food prices. However, the remaining increase in inflation was attributed to the 'rapid growth of money and credit' associated with consumption and 'capacity pressures' in the UK economy (King,2007::2).

Whilst the *open letter* did not blame fiscal policy as a contributory factor in 'capacity pressures' in the UK economy, King had complained about developments in fiscal policymaking on three occasions in 2004. First, in his speech at *Mansion House* in the City of London on the 16th June 2004, King (2004b) stated that the balance of the UK public finances had "tilted more and more towards the spending side" and that return to a "sustainable fiscal position" was "important because the improvement in the fiscal stance in recent years has been a key element in achieving

[113] The orthodox hierarchy between macroeconomic policy instruments, which saw fiscal policy play a supportive role to monetary policy in the pursuit of the orthodox objective of price stability, was articulated in public speeches by Brown (2001g;2003a;2003k), Balls (2007), O'Donnell (2004;2004a) and by the Treasury (2001a:2;2002:1;2002b:2; 2003:4;2003a:17;2004:16;2004a:13-14;2005:15;2005a:14; 2006:17;2006a:13;2007:12) in their Budget and Pre-Budget Reports.

macroeconomic stability". Second, in oral evidence to the Treasury Committee (2004a:Ev.16.Q.69-74) on 24th June 2004, King reiterated on several occasions the importance for the MPC that the fiscal rules were met because if they were not then the MPC's "life will be more difficult" because "inflation expectations will be affected; credibility of the framework will be damaged". Third, in oral evidence to the Treasury Committee (2004b:Ev.26,Q.129) on the 30th November 2004, King declared that meeting the fiscal rules were not "an optional extra, it is an integral part of the overall macroeconomic framework".

The orthodox economic idea of competitiveness also continued to be deployed in policy speeches and policy documents after the 2001 general election and was constructed in public speeches and policy documents in the same manner identified after the election of New Labour on the 1st May 1997. Consequently, it was identified that UK firms and entrepreneurs operated within a 'global marketplace'[114], which meant their ability to sell and export goods and services was subject to global competition[115]. For example, in a speech on the 17th June 2003, Brown (2003e) stated that due to the "new wave of globalisation there is hardly a

[114] Direct reference to the 'global marketplace' can be found in public speeches by Brown (2004k:2004l) and junior ministers at the Treasury such as Boateng (2004) and Browne (2006). Direct reference to the 'global marketplace' can also be found in the Treasury's (2002b:35) 2002 Pre-Budget Report.

[115] The identification that UK firms and entrepreneurs operated within the constraints of global competition was evident in public speeches by Balls (2006c:2007), Blair (2006a), Hewitt (2002b) and junior ministers at the Treasury such as Browne (2005), Kelly (2004), Primarolo (2001) and Timms (2005). The orthodox economic idea of competitiveness was also expressed in public speeches by Bank of England officials such as George (2001f:2002b:3;2002e:2-3) and King (2004:1) and Treasury officials such as Balls, O'Donnell and Grice (2004:7-8) and O'Donnell (2004;2004a). The notion of global competition was also articulated in Bank of England (2001b:37,44,53;2001d:iii.37,61,62,63;2002a:iii,42,54,55;2002c:32,47,54,55,56; 2002e:8,30,59,61;2002g:41,43,66,67,68;2003:33,44,61,62;2003b:35,36,62;2003d: 8,36,38,61;2003f:42,55,56;2004:54-55;2004b:19,20,46,59,60;2004d:59,6;2004f:32-33,53,55;2005:6,16;2005b:iii;2005d:17;2006a:ii,16,17,31;2006c:ii,31,38;2006e:33) policy documents such as their *Inflation Reports*. In the public speeches of Brown (2001c;2001e;2002b;2003;2003i;2004;2004d;2004e;2004f;2004g;2004h;2004i; 2004j;2004k;2005a;2005c:2006b;2006c;2006f;2007;2007a;2007b) it was claimed that the 'global marketplace' and 'global competition' necessitated that macroeconomic policy secured economic stability and microeconomic policies secured open, competitive and flexible markets.

good we produce here in Britain and many services that are not subject to intense global competition… today there is no safe haven, no easy escape for any country from global competition without putting at risk long-term stability, growth and employment". Meanwhile, Blair (2005) told the 2005 Labour Party Conference on the 27th September that "in the era of rapid globalisation, there is no mystery about what works: an open liberal economy, prepared constantly to change to remain competitive…. Competition can't be shut out; it can only be beaten".

Consequently, it was identified that the route to competitiveness in the global economy lay in the extension of greater competition in the UK economy, which would create more dynamic and entrepreneurial domestic markets[116]. For example, in a speech on the 19th November 2002, Blair (2002a) stated that "we must promote effective competition. Competition drives innovation and competitiveness". Similarly, in his 2002 Pre-Budget Statement of the 27th November, Brown identified that "the surest route to British companies becoming global champions is to extend competition and open up new markets at home". Thus, the 2002 Enterprise Act was passed in Parliament, which was aimed at enhancing the competition regime, modernising insolvency laws and 'bringing down the barriers to enterprise and entrepreneurial activity' (HM Treasury,2002:6).

The remainder of the Premiership of Tony Blair after the 2001 general election also saw the continued rhetorical appeal to the orthodox economic idea of economic liberalism, which was interpreted and constructed in the same way as it had been during the 1997-2001 Parliament. Thus, the drivers of economic growth and employment in the UK economy were repeatedly located in public speeches by New Labour as business and entrepreneurs in the private sector[117]. Furthermore, it

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[116] That the route to a more competitive economy lay in the extension of competition and entrepreneurship was identified in Treasury (2001a:36-39;2002:45-47;2002b:39-42;2003:49-54;2003a:48-53;2004:52-53;2004a:40-44;2005:45-47;2005a:39-42;2006:45-48;2006a:41-44;2007:53-55).

[117] Businesses and entrepreneurs in the private sector were located as the drivers of economic growth and employment in public speeches by Brown (2002f;2003h:2004f;2004i;2004j;2004l;2005a;2005d), Cabinet minister such as Hewitt (2002:2002a) and junior ministers at the Treasury such as Browne (2005a) and Smith (2002).

was affirmed after the 2001 general election that microeconomic policy would 'not pick winners' but rather would 'make markets work better' so they worked in the public interest[118]. For example, Balls, O'Donnell and Grice[119] (2004:6-7) posited that 'markets are a powerful means of advancing the public interest… [it is] important to strengthen markets where they work and to tackle market failures where they occur'. Thus, Balls, O'Donnell and Grice (Ibid) identified three parameters for microeconomic policy. First, an enhanced role should be given to markets so they can operate in the public interest. Second, the limits of markets were recognised and in such cases public funding and provision may be more equitable, efficient and responsive solution. Third, ensure that government failure should not replace market failure and government intervention should be targeted at addressing those failures to make markets work in the public interest.

Where markets were deemed to require an enhanced role it was identified in public speeches and policy documents that microeconomic policy should safeguard and extend open, competitive and flexible markets for products, labour and capital, which would allow markets to operate in the public interest through the creation of economic growth and employment[120]. Where microeconomic policy took a more

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[118] It was affirmed that microeconomic policy would 'not pick winners' but, rather, would 'make markets work better' so they worked in the public interest by Balls, O'Donnell and Grice (2004:xi,6-10), Blair (2003c:2004a) and Brown (2002e;2003; 2004h).

[119] Joe Grice served as Director of Macroeconomic Policy and Chief Economist at the Public Services Directorate at the Treasury (2000-2007).

[120] The microeconomic policy should safeguard and extend open, competitive and flexible for products, labour and capital, which would ensure economic growth and employment was identified by key figures in New Labour such as Blair (2001; 2003a;2004:2005a;2005b),Brown (2001d:2001e;2001h;2002d;2002f;2002g;2003; 2003c;2003e;2003f;2003h;2003i;2003j;2004;2004h;2004i;2004l;2005b;2005c: 2005e;2006;2006b;2006c;2006e;2007;2007a;2007b) and Balls (2003;2007a), cabinet members such as Hewitt (2001;2003) and junior ministers at the Treasury such as Boateng (2002), Browne (2005a:2006) and Smith (2002). Finally, the need for open, competitive and flexible markets to secure economic growth and employment was identified by Bank of England officials such as George (2001f:24;2002b:3;2002d:2-3;2002f) and King (2004a:5), Treasury officials such as Balls and O'Donnell (2002:27), Balls, O'Donnell and Grice (2004:8-9,12,Box1:1) and in Treasury (2003:1,2,7,13;2004:1-2,4-6;2005:7;2007:2) and DTI (2001a:2004:14;2004a) policy documents.

activist form in markets it was in areas identified as suffering from a market failure such as education, health and skills. For instance, Balls, O'Donnell and Grice (2004:16-18) noted that the provision of health and education were clear instances where market failures can occur. However, this did not mean that government failure should replace market failure. Consequently, Balls, O'Donnell and Grice (Ibid) contended that public service reform should include the decentralisation of delivery and contestability between providers including the private sector.

Consequently, microeconomic policy after the 2001 general election represented a continuation of the six microeconomic policies identified in Chapter Six as those implemented during the 1997-2001 Parliament, which included liberalisation, deregulation, privatisation, commodification of the public services, internationalisation of the domestic economy and reduced taxation of firms and corporations. For example, in his 2005 Budget Statement of the 16th March, Brown introduced "risk-based" and "light and limited touch" to regulation, which included reducing the number of regulatory bodies from thirty-five to nine and reducing the number of company inspections. This 'risk-based' and 'light-touch' approach to regulation was extended by Brown (2005d;2006c) to the Financial Services Authority regulation of financial markets, which Balls (2006;2006a) claimed was a competitive advantage for the City of London.

There was a growing disjuncture between the appeal to the orthodox economic ideas of competitiveness and economic liberalism in rhetoric and the formulation and implementation of fiscal policy from the 2002 Budget onwards. A clear division of responsibility had been established during the 1997-2001 Parliament between macroeconomic and microeconomic policy, due to the role of orthodox economic ideas, including competitiveness and economic liberalism, in the formulation of economic policymaking. The role of macroeconomic policy within this division of responsibility was to secure economic stability whereas the purpose of microeconomic policy was to improve economic performance in areas such as growth, employment, productivity and competitiveness. After the 2001 general election, this division of responsibility between macroeconomic and microeconomic

policy continued to be asserted in public speeches and policy documents[121]. For example, Treasury Budget and Pre-Budget Reports between 2001 and 2007 affirmed that the objective of macroeconomic policy was to secure economic stability[122].

The growing disjuncture, however, between the orthodox economic idea of competitiveness and economic liberalism and the formulation and implementation of fiscal policy arose from the impact the departure from orthodox fiscal policy had on the stimulation of domestic demand. In turn, this threatened the division of responsibility between macroeconomic and microeconomic policy as the pro-cyclical fiscal policy stimulus contributed to economic growth and employment. This was noted by O'Donnell in his oral evidence to the Treasury Committee (2002a:Ev.34,Q.70-71) on the 10th December 2002 when he stated that the "strong drivers of growth are public spending and public investment". Indeed, Brown acknowledged to the Treasury Committee (2002a:Ev.52,Q.239) in his oral evidence on the 17th December 2002 that the composition of economic growth consisted of a mixture of consumption and public expenditure. Finally, Jon Cunliffe, Managing Director of the Macroeconomic Policy and International Finance Division at the Treasury (2002-2007), stated in oral evidence to the Treasury Committee (2003b:Ev.13,Q.80) on the 16th December 2003 that "large amounts of public sector investment have helped to maintain confidence", which sustained economic growth.

Whilst fiscal policy increasingly contributed to the stimulation of domestic demand there is little evidence in public speeches and policy documents, however, to support the notion that the departure from orthodox fiscal policy outcomes and orthodox fiscal policy instruments at the 2002 Budget arose because of the adoption of economic ideas distinct from those utilised during the 1997-2001 Parliament.

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[121] Public speeches by Blair (2004), Brown (2004a) identified that the role of macroeconomic policy was to secure economic stability and the role of microeconomic policy to improve economic performance. Meanwhile, these roles for macroeconomic and microeconomic policy were also determined by George (2002:2;2002b:2;2002c:2; 2002d:3) and King (2004c:2) at the Bank of England.

[122] That the objective of macroeconomic policy was to secure economic stability is evidenced from Treasury (2001a:1-2;2002:1-2;2002b:2;2003:2;2003a:2;2004:1-2;2004a: 1;2005:1;2005a:1-2;2006:1;2006a:1;2007:1) in their Budget and Pre-Budget Reports.

Indeed, despite the stimulus that fiscal policy provided to domestic demand and economic growth after the 2002 Budget, New Labour and Treasury officials were adamant this was not the product of a return to demand management through discretionary fiscal policy[123]. In a speech on the 20th May 2003, for example, Brown (2003c) contended that the "modern route to economic stability… is based on a shared recognition that the old [fiscal] fine-tuning cannot work, that in liberalised market rigid monetary targets cannot on their own deliver stability and that the discretion necessary for effective economic policy is possible only within a framework that commands public and market credibility". Here, Balls and O'Donnell (2002:30-31) noted their debt of gratitude to Milton Freidman who was 'one of the great US post-war economists'. Specifically, because Freidman disproved the idea of a long-run trade-off between inflation and unemployment[124], which showed that 'expansionary monetary and fiscal policy cannot, in and of itself, deliver, let alone sustain, full employment' and 'excessive macroeconomic expansions – which allow inflation to run out of control and then be forcibly restrained – end up involving a long-term price in higher unemployment'.

The use of discretionary fiscal policy as an instrument to manage demand in the UK economy was also rejected by Treasury officials. For example, in oral evidence to the Treasury Committee (2001:Ev.3,Q.13) O'Donnell stated that the Treasury were 'not a believer in fiscal activism, that you can actually manipulate fiscal policy and fine tune it to manage unexpected events'. Here, O'Donnell returned to this theme in his oral evidence to the Treasury Committee (2002:Ev.34,Q.109-110) on the 23rd April 2002 when he stated that the Treasury "do not go in for fine tuning with fiscal policy" and "do not think fiscal policy can be used for fine tuning". Moreover, in a speech on the 17th September 2002, O'Donnell (2002) stated that the Treasury rejected discretionary fiscal policy because "in

[123] Public speeches by Balls (2001;2004a), Brown (2003c;2003e;2003i) and O'Donnell (2002) made it clear that they still rejected the use of discretionary fiscal policy as a policy instrument to manage demand in the UK economy. Moreover, the use of discretionary fiscal policy was rejected in the book written by Balls and O'Donnell (2002:x).

[124] That there was no long-run trade-off between inflation and unemployment was asserted in several speeches by Brown (2001f;2003) and Balls (2001;2004a).

practice, the long and variable lags involved in implementing fiscal decisions, the difficulty of reversing fiscal measures and the problem of reconciling stabilisation policy objectives with other objectives, have made all governments reluctant to use discretionary policy". Finally, Cunliffe stated in oral evidence to the Treasury Committee (2004:Ev.25,Q.136) that "short-run demand management of the economy is the Bank of England's responsibility", which the MPC achieved via the Bank Rate in accordance with the inflation target.

Consequently, the departure from orthodox fiscal policy at the 2002 Budget was not underpinned by the transition to a new set of economic ideas in favour of demand management nor the reversal in the orthodox hierarchy between macroeconomic policy instruments and the division of responsibility between macroeconomic and microeconomic policy. In this regard, Brown is best claimed as an 'accidental Keynesian' in the early 2000s in that increases in public spending accidentally coincided with a slowdown in global growth, rather, than intended as an strategy of macroeconomic stabilisation (Keegan,2004:299,333). The remainder of the chapter will present two tentative observations that may explain why change in fiscal policy occurred at the 2002 Budget and explain the requirements of a future research agenda.

The first observation is that increased public expenditure and the corresponding departure from orthodox fiscal policy outcomes could be explained as a consequence of the pursuit by New Labour of traditional aims associated with Social Democracy of social justice and redistributionism[125]. Here, Riddell (2004:314) argued that New Labour 'remained recognisably in the Social Democratic tradition' with clear links of 'objectives and policy' such as broadening equality of opportunity and state-financed public services. For example, the 2002 Treasury (2002:10) Budget Report posited that the government would 'deliver world class public services through sustained increases in investment and modernisation to improve

[125] If this was the case then it would confirm that literature, which identifies New Labour public policy within the older traditions and values of the Labour Party and Social Democracy such as social justice and redistributionism. For example, see Beech (2004;2006), Beech and Hickson (2007:265-283), Bevir (2005), Fielding (2003:217; 2004:285) and Toynbee and Walker (2004).

performance', which was a 'vital part of the government's strategy' in 'extending opportunity, tackling poverty and social exclusion and delivering higher living standards for all'. The public service element of the departure from orthodox fiscal policy is further accentuated by previous analysis, which showed that government borrowing was a consequence of rapid increases in public expenditure and not a cyclical response to instability in the global economy and the decision to allow the automatic stabilisers to operate in the UK public finances.

The second observation is that the departure from orthodox fiscal policy was driven by the internal rivalry within New Labour between Tony Blair and Gordon Brown[126]. The troubled relationship between Blair and Brown was founded upon the ascension of Blair to the leadership of the Labour Party in the aftermath of the death of John Smith, Leader of the Labour Party (1992-1994). In order to secure the commitment of Brown not to run in the leadership context, the pair made an agreement at the Granita restaurant in Islington, London in 1994, which saw Brown 'secure an unprecedented control over the design and delivery of domestic economic and social policy' (Lee,2009:36-37). Brown exercised this control through the aforementioned operational changes to fiscal policymaking that saw the introduction of SR's, CSR's and PSA's, which strengthened the power of Brown and the Treasury over public expenditure planning and control and public service delivery. Indeed, when it came to economic policymaking, Brown often used the freedom afforded to him as Chancellor by side-lining Blair from policy decisions, which is confirmed by the diaries of Alistair Campbell (2011:30-31,408,418;2012:544,581), Director of Communications and Strategy at Number.10 (2000-2003) and a monograph written by Derek Scott (2004:9,20,23-25,214), Economic Adviser to Tony Blair (1994-2003).

[126] The troubled political relationship between Tony Blair and Gordon Brown has been well-documented in memoirs and diaries of New Labour's period in office, no more so than by Blair (2010), Campbell (2011;2012), Darling (2011) and Mandelson (2010). The internal political conflict between Blair and Brown has also been noted by many tertiary accounts of New Labour's period in office such as those by Beckett (2007:149), Bower (2005:Chp.6), Rawnsley (2001:31,33,48), Rentoul (2001:382-383,476) and Stevens (2004:83-84,122,332).

In this internal power struggle between Blair and Brown increased levels of public expenditure delivered from the Treasury on public services, such as the NHS and education, aided Brown in his attempts to hasten the departure of Blair as leader of the Labour Party and Prime Minister. Primarily, because higher levels of public expenditure allowed Brown to portray himself, whatever the truth of the matter, as the guardian of the public services and upholder of the traditional aims and values of the Labour Party, which contrasted with Blair's perceived pursuit of the commodification of the public services (Beckett,2007:141). For example, Blair (2010:480-481) noted in his memoir that after the 2001 general election he was intent on 'changing the monolithic nature of the [public] service[s]' via the introduction of foundation hospitals and the academic programme in education, which would advance the boundaries of competition and blur the distinctions between the public and private sector.

The failure of the orthodox cycle to understand and explain the change that occurred in UK macroeconomic policymaking after the 2002 Budget requires remedy via analysis by a future research agenda, which needs to encompass two lines of enquiry. First, a future research agenda would have to include further historiography of UK economic policymaking. Examination of other periods of UK economic history would determine whether 2002-2007 is an outlier in the data on UK fiscal policymaking with no previous historical precedent, or alternatively may determine that a similar period is observable. If such a period in fiscal policymaking was found in a previous historical period this would allow firmer explanations to be drawn as to when and why policy changes occur without the stimulus from a crisis phase in macroeconomic policymaking. In turn, it may require an extra phase of macroeconomic policymaking to be added to the orthodox cycle or the current explanation of change and continuity in the orthodoxy phase may need amendment. Second, the future research agenda would need to include further study of 2002-2007 in fiscal policymaking in order to draw further observations pertaining to why fiscal policy departed from orthodoxy at the 2002 Budget.

Conclusion

This chapter has provided a case-study of UK macroeconomic policymaking from the 7th June 2001 to the 26th June 2007. This chapter has drawn two conclusions pertaining to monetary and fiscal policymaking during this period. First, in terms of monetary policymaking, this chapter has explained that the conceptual framework of the orthodox cycle provides a superior understanding and explanation of change and continuity than that furnished by punctuated equilibrium. However, it should be noted that reason why the orthodox cycle provides a superior understanding and explanation of change and continuity in monetary policymaking than punctuated equilibrium is more nuanced than the previous chapter. Specifically, the superiority of the orthodox cycle arises from the identification of continuity in orthodox monetary policy from the 7th June 2001 to the 26th June 2007, rather, than continuity in the new radical policy equilibrium that should have been formed after the election of New Labour on the 1st May 1997 according to punctuated equilibrium. Thus, the orthodox cycle expounds that operational changes to monetary policymaking after the 2001 general election did not presage and fundamental change in the institutional governance of monetary policymaking, which continued to institutionalise orthodox monetary policy. Indeed, operational changes to the SMMF made by the Bank of England strengthened the role of the orthodox monetary policy instrument of OMOs in domestic monetary management. As a result, the orthodox cycle locates that monetary policy remained in the orthodoxy phase of the orthodox cycle after the 2001 general election.

The second conclusion of this chapter relates to changes that occurred in fiscal policymaking from the 2002 Budget onwards, which neither the orthodox cycle nor the model of punctuated equilibrium provides an explanation. Indeed, the chapter highlighted that the dynamics for policy change in the orthodox cycle, such as a crisis phase, and punctuated equilibrium, such as an endogenous or exogenous shock, were absent after the 2001 general election. Furthermore, change in macroeconomic policy was far greater after the 2002 Budget than the minor or

superficial policy adjustments during a period of stability envisaged by punctuated equilibrium. In mitigation, the chapter demonstrated that the orthodox cycle did allow us to understand when the departure from orthodox fiscal policy occurred, which happened at the 2002 Budget.

There was another aspect of macroeconomic policymaking after the 2002 Budget, which was not explained by the orthodox cycle but has been highlighted in the chapter, namely, that there was a growing disjuncture between the orthodox economic ideas deployed in rhetoric and the formulation and implementation of fiscal policy, which saw departure from orthodoxy. Furthermore, the departure from orthodox fiscal policy provided a pro-cyclical stimulus to domestic demand and economic growth from 2003 onwards, which threatened two other areas of orthodox macroeconomic policy. First, it threatened the orthodox hierarchy between macroeconomic policy instruments. Second, it threatened the divisions of responsibility between macroeconomic and microeconomic policy established during the 1997-2001 Parliament. However, despite the pro-cyclical stimulus to domestic demand and economic growth, the chapter showed that the departure of orthodox fiscal policy was not driven by the adoption of economic ideas in favour of discretionary fiscal policy. At this juncture, the chapter advanced two observations that could explain why fiscal policy departed orthodoxy at the 2002 Budget and explained that a future research agenda should attempt to seek historical parallels for this period in fiscal policymaking and requires further study of 2002-2007 in fiscal policymaking. The next chapter will provide a case-study of UK macroeconomic policymaking from the 27th June 2007 to the 5th May 2010.

Chapter 8

Change and Continuity in UK Macroeconomic Policymaking during the Brown Government of the 27th June 2007 to the 5th May 2010

Introduction

This chapter provides a case-study of United Kingdom (UK) macroeconomic policy during the government of Gordon Brown, Prime Minister (2007-2010), from the 27th June 2007 to the 5th May 2010 and the Global Financial Crisis of 2007-2009. The purpose of this case-study is to see whether the orthodox cycle provides a superior understanding and explanation of change and continuity in UK macroeconomic policy than that furnished by punctuated equilibrium. According to punctuated equilibrium, a significant exogenous shock, such as the Global Financial Crisis, should have disrupted the pre-crisis equilibrium in the policymaking process and produced radical policy, ideational and institutional change. This innovation is them claimed to form a new policy equilibrium that exists until it is disrupted by the next endogenous or exogenous shock.

This chapter concludes that the orthodox cycle provides a superior understanding and explanation of change and continuity than that furnished by punctuated equilibrium for four reasons. First, the orthodox cycle provides exactitude in the initiation of a crisis phase in UK macroeconomic policymaking with the deployment of a 'debt crisis' narrative by David Cameron, Leader of the Conservative Party (2005-2016), on the 16th September 2007. Second, the orthodox cycle explains that the Global Financial Crisis led not to radical monetary policy

change, but rather the continuity of orthodox monetary policy as monetary policymaking entered a consolidation phase of the orthodox cycle on the 8th October 2008. Third, change in fiscal policy and economic ideas did occur in response to the Global Financial Crisis, however, rather than leading to a new policy equilibrium, the orthodox cycle expounds that fiscal policymaking entered a temporary deviation phase at the 2008 Pre-Budget Statement of the 24th November. Fourth, the orthodox cycle explains that fiscal policymaking joined monetary policymaking in the consolidation phase at the 2009 Pre-Budget Statement of the 9th December.

This chapter will be organised in the following manner. The first section of the chapter discusses the crisis phase in UK macroeconomic policymaking. It will begin by providing an overview of the events and emergencies of the Global Financial Crisis of 2007-2009 and the orthodox economic policy response of the Brown government of financial interventionism. The chapter proceeds to discuss the initiation of the crisis phase, which occurred with the deployment of a 'debt crisis' narrative by David Cameron on the 16th September 2007. Here, the chapter also identifies the two narratives deployed by the Brown government to counter the 'debt crisis' narrative.

The second section of the chapter analyses monetary policymaking. This section of the chapter proceeds by identifying institutional and operational continuity in the monetary policymaking framework. The chapter advances to explain that monetary policymaking entered the consolidation phase of the orthodox cycle, which was initiated on the 8th October 2008. Here, the chapter identifies how the orthodox monetary policy instruments of the Bank Rate and OMOs were used to create the economic conditions necessary to secure the later return of inflation to target and price stability. This includes a discussion of how Quantitative Easing (QE) should be understood as an orthodox monetary policy instrument of Open Market Operations (OMOs). The chapter also explains how the orthodox cycle can account for the implementation of 'unorthodox' monetary policy instruments such as the Credit Guarantee Scheme (CGS).

The third section of this chapter explores fiscal policymaking during the Brown government. The outset of this section of the chapter highlights that a temporary deviation phase in fiscal policymaking was initiated at the 2008 Pre-Budget Statement, which involved the implementation of a discretionary fiscal policy strategy to stimulate aggregate demand, support economic growth and create employment. The chapter proceeds to document how the formulation of this discretionary fiscal policy strategy was based on the adoption of 'unorthodox' economic ideas associated with John Maynard Keynes and included the reversal of the orthodox hierarchy between macroeconomic policy instruments.

The fourth section of the chapter also focuses on fiscal policymaking. The beginning of this section documents the internal conflict within the Brown government pertaining to fiscal policymaking. The chapter progresses to identify that consolidation of the public finances had been planned from the very beginning of the temporary deviation phase. Thus, the chapter locates the initiation of the consolidation phase in fiscal policymaking at the 2009 Pre-Budget Statement of the 9th December.

The Crisis Phase in Macroeconomic Policymaking from the 16th September 2007

A series of events in the global financial markets that transpired during the summer of 2007 marked the beginning of a Global Financial Crisis. In August 2007, the French investment bank BNP Paribas announced that it was suspending payments from two of its investment funds, which triggered a systemic loss of confidence in financial markets. This loss of confidence served to close the market for complex credit instruments, such as mortgage-backed securities based on sub-prime mortgages in the United States (US) housing market, which meant that banks could no longer package the mortgages they held on their balance sheets into securities products for distribution to global investors. Consequently, as the foreclosure rate in

the US housing market rose, financial institutions began to report huge quarterly losses. In turn, financial institutions increasingly lost confidence in the safety of lending to one another as uncertainty as to where losses would be reported next pervaded the financial markets. This caused funding costs in the interbank wholesale markets to rise substantially, which was a particular problem for those UK banks, such as Northern Rock, whose business models depended upon the availability of wholesale funding.

The first tremors of the Global Financial Crisis of 2007-2009 came to the attention of the UK public when the precarious financial position of Northern Rock was reported in media, which precipitated the first run on a UK bank over the weekend of the 14th-17th September 2007 since 1866. The problems at Northern Rock emanated from the business model it had adopted upon its demutualisation in 1997, which was reliant on access to short-term borrowing in global wholesale markets (Darling,2007). However, Northern Rock was not the only UK bank to adopt this business model. For example, Mervyn King (2009a:4). Governor of the Bank of England (2003-2013), identified in a speech on the 17th March 2009 that it was now a "distinctive feature of the contemporary British model of banking". The events and emergencies of the Global Financial Crisis led to a substantial economic downturn in the UK economy lasting eight consecutive quarters of economic contraction between Q1 2008 to Q4 2009 (Chamberlin, 2010: 55) and a decline in economic output worth 6% GDP, which the Office of National Statistics (ONS,2014:1) calculate is 'the deepest recession since records began in 1948'. Furthermore, UK unemployment rose from 1.6million in early 2008 to 2.5million by 2010 (Chamberlin,2010: 61).

Volatility and uncertainty in the global financial markets became more acute in September and October 2008. The economic policy response of the Brown government to the Global Financial Crisis was to implement two recapitalisation schemes on the 8th October 2008 and the 19th January 2009, which, at their peak, provided the UK banking system with £1.162trillion worth of finance and guarantees (National Audit Office,2011: 5). Furthermore, the Bank of England provided significant levels of emergency liquidity assistance to the UK banking system. For example, in a written statement delivered to the House of Commons on the 31st

March 2008, Alistair Darling (2008d), Chancellor of the Exchequer (2007-2010), explained that Northern Rock had accessed £26.7billion of liquidity from the Bank of England by the 31st December 2007. Moreover, Darling (2009r) told the House of Commons in a Statement on the 25th November 2009 that the Bank of England had provided emergency liquidity assistance to Halifax Bank of Scotland (HBOS) and Royal Bank of Scotland (RBS) in early October 2008, which peaked at £61.6billion on the 17th October 2008.

Furthermore, the Brown government followed up their nationalisation of Northern Rock, which was announced by Darling (2008a) in a House of Commons Statement on the 17th February 2008, with further nationalisations of other high-street UK banks. For example, on the 28th September 2008, the Brown government executed its second nationalisation of a UK financial institution when the mortgage book and loan assets and liabilities of the building society Bradford & Bingley were brought into government ownership. Moreover, the £500billion bank rescue package introduced on the 8th October had included a £50billion Bank Recapitalisation Fund (BRF), which made capital available to UK banks in exchange for preference and ordinary shares in those institutions. The use of the BRF by UK banks to bolster their available capital led the Brown government to take a majority ownership position of 84.4% in RBS and 43.4% in Lloyds Banking Group. Indeed, Lloyds Banking Group, formed of the merger between Lloyds TSB and HBOS, had only proceeded because, as Darling (2008g) informed the House of Commons in a statement on the 6th October 2008, the Brown government had "amended the competition regime" and waived normal competition rules prohibiting financial institutions from owning a majority of the UK mortgage market.

The orthodox cycle can account for the financial interventionism of the Brown government. Here, the orthodox cycle explains that when the events and emergencies of the crisis phase occur in the financial markets, the crisis phase can include economic policies that provide financial interventionism to protect financial markets from contagion and individual financial institutions from collapse. Indeed, Darling (2011:3) claimed in his memoir that without the recapitalisation scheme of the 8th October 2008, events and emergencies 'would have brought down the global

banking system within hours'. Furthermore, despite the severity of the crisis, the Brown government consistently made it clear that they would not use the nationalised banks to affect a strategic restructuring of the UK financial system, but rather nationalised banks would be operated at 'arms-length' (Cooper,2008;MacPherson;2009) and would be returned to the private sector[127].

The crisis phase of the orthodox cycle consists of a series of events and emergencies, which are interpreted and designated as crises by narratives in political discourse. The orthodox cycle explains that a crisis phase in UK macroeconomic policymaking was initiated on the 16th September 2007, two days after the start of bank run on Northern Rock, by an article written by David Cameron (2007) for the Daily Telegraph. Here, Cameron constructed a 'debt crisis' narrative that interpreted events in the global financial markets and the emergency at Northern Rock as a consequence of the failed economic policymaking of Gordon Brown and New Labour. For example, Cameron (Ibid) stated that Labour governments since the 1st May 1997 had 'presided over a huge expansion of public and private debt… though the current crisis may have had its trigger in the US, over the past decade the gun has been loaded at home. Under Labour our economic growth has been built on a mountain of debt'.

This was merely the first step in the construction of a 'debt crisis' narrative, which the Conservative opposition sustained in political discourse up until the 2010 general election on the 5th May 2010[128]. Increasingly, the focus of the 'debt crisis' narrative was sharpened to accentuate rising public expenditure, government borrowing and national debt since the 1st May 1997 as the cause of economic instability, recession and unemployment in the UK economy. For example, in a speech on the 26th January 2009, George Osborne (2009), Shadow Chancellor of the

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[127] The desire of the Brown government to return the nationalised banks to the private sector was asserted in a number of public speeches by Brown (2008d) and Darling (2008b;2008i;2009;2009a;2009e).

[128] The debt crisis narrative, with its sharpened focus on the role of fiscal policymaking under Brown and the increase in government borrowing and national debt, was deployed by Cameron (2007a;2008;2008a;2009;2009a;2009c;2009e) and Osborne (2008;2008a; 2008b;2008c:cc.504-506;2009c;2009d;2010) in a range of public speeches during 2008-2010.

Exchequer (2005-2010), stated that "this is Labour's debt crisis. The debt crisis is the product of years of debt-fuelled spending which the country could not afford". Similarly, in a speech on the 6th March 2009, Osborne (2009a) posited that "our banking system is not separate from our economy, it is a reflection of it… the unsustainable debts in our banks are a reflection of unsustainable debts in our households, our companies and our government. That is what the man who had Chancellor for ten years to apologise for… year after year Whitehall itself lived beyond its means with persistent budget deficits… building up debts that will take a generation to pay off".

In response to the 'debt crisis', the Brown government deployed two narratives. The first narrative sought to designate and interpret events and emergencies in the UK economy as a 'global banking crisis', which started in the US housing market and was caused by systemic failures in global financial markets and financial regulation in the global economy[129]. For example, in a speech on the 12th January 2009, Brown (2009) contended that recession in the UK economy was "different because it is global and it is financial, it is different because of what has happened round the world to the banks. We are living through the first global financial crisis of this new global age and we have witnessed nothing less than a worldwide failure of the banking system, a failure that as we know began in America". Thus, in a speech at an annual dinner at the Confederation of British Industry (CBI) on the 20th May 2009, Brown (2009l) stated the UK was suffering not "an inflation-led recession… this is not an interest-rate led recession…. This is not a public-debt led recession either… it is led by a banking crisis". The political strategy was to counter the 'debt crisis' narrative and portray events in financial markets and the UK economy as an externally generated product of globalisation (Lee,2009:241).

[129] Brown (2008;2008a;2008c;2008d;2008e;2008f;2008f;2009;2009a;2009b;2009c; 2009g;2009i;2009l) and Darling (2008;2008e;2008k;2009g) regularly argued in public speeches, for example, that events and emergencies in the financial markets and domestic economies were the product of the first crisis of 'globalisation' or the 'global age', which began in the United States (US) housing market and led to systemic failures in the global banking system and global financial regulation. Moreover, the 'global banking crisis' narrative was affirmed by Brown (2010:5,7,10) in his 2010 memoir.

The second narrative deployed to structure interpretations of the crisis was one exclusive to Gordon Brown, which attempted to designate the events and emergencies as a 'crisis of morals and values' that itself was a product of failure in economic ideas[130]. For example, in his Labour Party Conference Speech on the 29th September 2009, Brown (2009r) exclaimed that "what let the world down last autumn was not just bankrupt institutions but a bankrupt ideology. What failed was the Conservative idea that markets always self-correct but never self-destruct. What failed was the right wing fundamentalism that says you leave everything to the market and says that free markets should not just be free but values free…. Markets need what they cannot generate themselves… I say to you today; markets needs morals"[131].

The Consolidation Phase in Monetary Policymaking from 16th June 2008 to the 5th May 2010

The crisis phase in UK macroeconomic policymaking, however, did not lead to radical institutional change in the monetary policymaking framework. For example, in his letter to the Governor of the Bank of England sent on the 11th March 2008 entitled *Remit for the MPC*, Darling (2008c:1-2) affirmed that the objective of the Bank of England remained 'to maintain price stability; and subject to that, support the economic policy of Her Majesty's government including its objectives for growth and employment', which would be measured and achieved via continuation of the

[130] In several public speeches across 2009, Brown (2009g;2009i:2009k:2009s) proclaimed the 'end' or 'death' of the Washington Consensus and repudiated the 'free-market' or 'right-wing' fundamentalism of laissez-faire economic policy, which Brown argued his government had eschewed in its action to nationalise banks and implement a discretionary fiscal policy strategy.

[131] In a number of public speeches, Brown (2008f:2009d;2009e;2009f;2009i) asserted that markets and globalisation should be free but never 'values-free' or 'rule-free'.

operational remit for the MPC of the 2% CPI inflation target[132]. The inflation target in the MPC's operational remit also remained flexible. For example, in the aforementioned letter on the 11th March 2008, Darling (2008c:2) acknowledged that 'the actual inflation rate will on occasions depart from its target as a result of shocks and disturbances. Attempts to keep inflation at the inflation target in these circumstances may cause undesirable volatility in output'[133]. Thus, Darling (2008j) asserted in his 2008 *Mais Lecture* of the 29th October 2008 that the MPC was allowed discretion over the horizon in which it brought inflation back to target in order that "the MPC can support, in line with its statutory requirements, the government's wider economic objectives". Finally, the inflation target also remained symmetrical via the maintenance of trigger points at 1% and 3% CPI inflation that, if breached, required the Governor of the Bank of England to send an open letter to the Chancellor of the Exchequer explaining why CPI had departed from target and the action the MPC would take to return inflation to target[134].

The consolidation phase in the orthodox cycle in UK macroeconomic policymaking is initiated when a macroeconomic policy strategy is implemented that utilises orthodox policy instruments to create the conditions in economic performance necessary to secure a later return to the orthodox objective of price stability. The preservation of the operational remit for the MPC during the Brown government is important to our subsequent discussion for two reasons. First, the

[132] Darling (2009h:1-2;2010b:1-2) affirmed the operational remit for the MPC and price stability objective in further letters entitled *Remit for the MPC* sent to the Governor of the Bank of England on the 22nd April 2009 and 24th March 2010. Moreover, this operational remit for the MPC and Bank of England was affirmed in each Bank of England (2007d:1;2007e:1;2008a:1;2008c:1;2008e:1;2008g:1;2009a:1; 2009e:1;2009g:1;2009i:1;2010:1) *Inflation Report* published during the Brown government.

[133] Flexibility in the inflation target was affirmed by Darling (2009h:2;2010b:3) in subsequent letters to the Governor of the Bank of England entitled *Remit for the MPC* sent on the 22nd April 2009 and 24th March 2010. The flexible inflation target system was also noted in *open letters* and public speeches delivered by King (2008:3;2008a:3;2008b :3;2008c:7;2008d:2) during 2008.

[134] The symmetrical inflation target was affirmed by Darling (2008c:2-3;2009h:2-3;2010b:2-3) in each of his *Remit for the MPC* letters sent to the Governor of the Bank of England during his period as Chancellor of the Exchequer.

inflation target system continued to operate as a monetary framework, which guided policymakers in operational decisions pertaining to monetary policy instruments in pursuit of the orthodox objective of price stability. Second, the flexible inflation target allowed the MPC and Bank of England to ignore the departure of CPI inflation from target, which rose above the 3% trigger point in the symmetrical inflation target in six of the twelve economic quarters during the Brown government (ONS,2016b). Instead, the flexible inflation target allowed monetary policymaking to enter the consolidation phase of the orthodox cycle as monetary policy instruments were deployed to provide support to economic growth via nominal spending and nominal demand. In turn, support to economic activity by the MPC and Bank of England served to counter the 'downside' risk and 'downward' pressure on inflation from the Global Financial Crisis and domestic recession and aim to return inflation to target and price stability at the end of a two-year forecast period[135].

The latest phase of consolidation in monetary policymaking was initiated by the MPC on the 8th October 2008, when the MPC cut Bank Rate from 5% to 4.5% as part of an internationally coordinated action by Central Banks across the global economy. The cut in Bank Rate on the 8th October, however, was only the first in several further reductions of the Bank Rate from 4.5% on the 8th October 2008 to the then historic low of 0.5% on the 5th March 2009 (Bank of England,2016a)[136]. The minutes of the MPC meetings from October 2008 to March 2009 justified cuts to Bank Rate because dislocation in global financial markets and synchronised downturn in the world economy had caused tight credit conditions and declining economic activity, which meant CPI inflation was likely to fall well below the

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[135] The 'downside' risk and 'downward' pressure on UK prices caused by turmoil in the global financial markets and tightened credit conditions and declining economic activity, was highlighted by the Bank of England (2008a:8,10,39,41-42,46;2008c:8,39,40,43,47;2008e:5,8,38,39,41;2008g:7,8,36;2009a:5,7,8,38,39,40, 42;2009e:10,45,46;2009g:8,41,46) in its *Inflation Reports* from February 2008 to August 2009 and by Mervyn King (2008b:4;2008d:2-3;2009b:2;2010:2) in his open letters to the Chancellor of the Exchequer.

[136] The MPC cut the Bank Rate to 3% on the 6th November 2008, 2% on the 8th December 2008, 1.5% on the 8th January 2009 and 1% on the 5th February 2009 (Bank of England,2016a).

inflation target in the medium term[137]. Thus, King (2008d:3) explicated in his *open letter* of the 15th December 2008 that, despite CPI inflation being above target at 3.9% in Q3 2008, the emergence of ‘a substantial risk… that inflation will undershoot the target in the medium term’ meant the ‘the MPC have lowered Bank Rate very significantly at each of its past three meetings’. Furthermore, the minutes of the MPC meeting on the 4th and 5th February noted that cuts to Bank Rate had been implemented in order ‘to restore nominal spending growth to levels that were more consistent with returning to the 2% target, thus helping to reduce the length and depth of the recession’ (Bank of England,2009b:7).

The MPC’s reaction to the Global Financial Crisis therefore was to operate the Bank Rate in the orthodox manner described in Chapter Six. For example, the Bank of England (2009a:44) February 2009 *Inflation Report* provided an explanation of the transmission mechanisms through which the Bank Rate influenced economic activity and inflation. Primary among the transmission mechanisms was the impact the Bank Rate had on the short-term market interest-rates that banks and other financial companies charged one another for lending and services. These short term market interest-rates in wholesale markets then altered the amount of broad money and credit that banks and building societies made available to the economy and the interest-rates charged to households and companies on loans and deposits. The Bank of England specified three further transmission mechanisms for the Bank Rate including confidence about future policy, inflation expectations and the exchange-rate. Cumulatively, the Bank of England (Ibid) declared that these transmission mechanisms ‘influence[d] the spending of households and companies… the incentive to save or spend, and the levels of money and credit’. The associated increase in economic activity would support the UK price level and counter the threat that inflation would fall below target.

[137] The fear that tight credit conditions and declining economic activity would cause CPI inflation to fall below target was noted as the justification to cut the Bank Rate in MPC meetings in November 2008, December 2008, January 2009, February 2009 and March 2009 (Bank of England,2008i:6-7;2008j:6-7;2009:6-8;2009b:7;2009c:6-7).

The minutes of the MPC meeting held on the 7th and 8th January 2009, however, noted there was ‘impairment in the monetary transmission mechanism associated with dysfunctional credit markets’ (Bank of England,2009:7). Indeed, the Bank of England (2009a:44) *Inflation Report* in February 2009 declared that severe disruption in financial markets had ‘blunted the impact of reductions in the Bank Rate’, particularly, but not exclusively, in the willingness of banks to extend new credit. Thus, the minutes of the MPC meetings held on the 4th and 5th February 2009 concluded that it was ‘unlikely that the inflation target could be met solely by cutting Bank Rate. The short-term market interest rates that Bank Rate sought to influence could not go far, if at all, below zero’ (Bank of England,2009b:7).

The orthodox cycle explains that orthodox monetary policy instruments during the consolidation phase can be assisted, for a time-limited basis, in creating the economic conditions necessary for the return of orthodox policy outcomes and objectives by policy instruments that could be considered as ‘unorthodox’. In the context of the impaired transmission mechanism of the Bank Rate due to dysfunctional domestic credit markets, the orthodox cycle expounds that such an ‘unorthodox’ monetary policy was introduced by Darling (2008h) on the 8th October 2008 in the £250billion Credit Guarantee Scheme (CGS), which was funded and operated by the Treasury and aimed to restore bank lending in the UK economy. For example, in his statement on the 8th October 2008, Darling (Ibid) explained that the CGS would ‘ensure that the banking system has the funds necessary to maintain lending… so that banks can go about their business of lending to people and business’. Moreover, in his Statement to the House of Commons on the 13th October 2008, Darling (2008i) explained that the CGS would underwrite new debt issues by banks that were used as collateral in interbank lending. Therefore, the CGS provided a government guarantee of interbank lending, which Darling (Ibid) argued was ‘an essential part of banks resuming lending’. The CGS was closed on the 28th February 2010 and the final guarantee under the scheme expired on the 26th October 2012.

A further development in monetary policy was announced on the 19th January 2009 in a Statement to the House of Commons by Darling (2009), which introduced

the Asset Purchase Facility (APF). In this Statement, Darling (Ibid) declared that the APF, funded by the issuance of Treasury bills, but managed by the Bank of England, would "initially" buy £50billion of assets in credit markets, such as "corporate bonds, commercial papers and syndicated loans" from "banks, financial institutions and financial markets". The purpose of the APF, according to Darling (Ibid), was to "accelerate a resumption of lending" and "increase the amount of funding available to companies". Furthermore, Darling (Ibid) added that the MPC "will keep under review whether this facility could be used as an additional way for meeting the inflation target". Just sixteen days later, in the meeting of the MPC held over the 4th and 5th February 2009, the MPC agreed that the Governor should write to Darling to request permission to extend the parameters of the APF of the purchase government securities financed by the creation of Central Bank money (Bank of England,2009b:8-9).

Darling (2009b) provided this authorisation in a Statement in the House of Commons on the 5th March 2009, which extended the APF to £150billion, £100billion of which would purchase UK government debt and £50billion would purchase assets in credit markets. The first purchases of gilts, financed by the creation of Central Bank money, began on the 11th March 2009 (Bank of England,2009f:70,82). The purchases of private sector assets via the creation of central bank money became termed as quantitative easing (QE), which was claimed an 'unconventional' monetary policy by Darling, King and several Bank of England officials and members of the MPC[138].

The remainder of this section of the chapter will argue that, far from being an 'unconventional' monetary policy, QE is an OMO, which is an orthodox monetary policy instrument. Thus, the consolidation phase of the orthodox cycle can account for QE as an orthodox monetary policy instrument used to create the conditions in economic performance necessary to secure a later return to the orthodox objective of

[138] QE was claimed as an 'unconventional' monetary policy in Bank of England (2009j:258) policy documents and public speeches by Bank of England officials and MPC members such as Blanchflower (2009:15), Dale (2009:2,8), King (2009:7), Fisher (2009:6) and Posen (2009:2). Meanwhile, QE was claimed as an 'unorthodox' monetary policy by Bean (2010:2).

price stability. In a paper for the *Bank of International Settlements*, Borio and Disytat (2009:1-2) identified that monetary policy had generally converged among member countries on what they termed as 'interest rates policy', which consists of the two key features identified in Chapters Three, Four, Five, Six and Seven. The first feature of 'interest rates policy' is the use of the central bank interest-rate, which sets the desired level of short-term market interest-rates in the economy. The second feature is the use of open or liquidity management operations, which uses the 'balance sheet policy' of the central bank exclusively to make the central bank interest-rate effective. Here, Borio and Disytat (2009:1) noted that the 'unconventional' nature of the monetary policies implemented by central banks after 2008 came from 'balance sheet policy' in that central banks had used their balance sheets to 'directly affect market prices and condition beyond a short-term, typically overnight, interest rate'. However, the authors (Ibid) highlighted that the use of 'balance sheet policy' by central banks were 'not really unconventional in their essence'.

Indeed, several Bank of England officials and Members of the MPC have questioned in public speeches whether QE is indeed an 'unconventional' monetary policy. For example, in a speech on the 27th March 2009, Spencer Dale (2009), Chief Economist at the Bank of England and Member of the MPC (2008-2014), posited that "the purchase (and sale) of assets by central banks is nothing new; central banks have always implemented monetary policy by changing the size and composition of their balance sheets". Moreover, Tim Besley (2009:2), Member of the MPC (2006-2009), noted in a speech on the 2nd July 2009 that QE was the "natural way to conduct monetary policy when nominal interest rates hit their effective lower bound" and was a "natural extension of standard open market operations that are used to implement Bank Rate". Similarly, David Miles (2009:5), Member of the MPC (2009-2015), contended in a speech on the 30th September 2009 that QE "is a piece of jargon for what is in many way a fairly standard central bank operation, namely the purchases of assets from the private sector in exchange for money". Finally, the minutes of the MPC meeting during the 4th and 5th March 2009, it was noted that QE was 'a natural extension of the committee's usual monetary policy operations' (Bank of England,2009c:8).

The claim that QE is an orthodox monetary policy is strengthened when we consider the long-standing role of OMOs within the Bank of England's Sterling Monetary Framework (SMF), which was outlined in the 2008 'Red Book' and has been discussed in Chapters Three, Four, Six and Seven. Here, the Bank of England (2008:2) posited that the 'framework for its operation in the Sterling Money markets is designed to implement the interest rate decisions of the… MPC while meeting the liquidity needs, and so contributing to the stability of, the banking system as a whole'. The Bank of England (2008:3) explained that there were three main elements to the SMF. First, banks and building societies hold target balances (reserves) at the Bank of England over a monthly maintenance period that is remunerated at Bank Rate if the target balance is met, which was a continuation of the system of 'voluntary reserves-averaging' discussed in Chapter Seven. Second, standing facilities are available on demand to enable banks/building societies to meet their target balance but carry a penalty rate of 0.25% on Bank Rate if used on the final day of the maintenance period and 1% on Bank Rate at all other times. Third, OMOs provide the banking system with the central bank money necessary for banks and building societies to achieve their target balances.

The primary objective of the SMF stated by the Bank of England (2008:2,4) in the 2008 'Red Book' was to 'ensure that short-term Sterling market interest-rates are consistent with the official Bank Rate', with particular reference to overnight market interest-rates. The Bank of England (Ibid) posited that it could implement monetary policy because it was 'the sole issuer of Sterling central bank money', consisting of banknotes and reserves, which allowed the Bank of England to 'establish itself as the rate-setter by being the marginal supplier and taker of funds at its chosen rate(s)'. The Bank of England (2008:5) explained that 'the role of OMOs in the operational framework is to provide… the necessary central bank money to the banking system… and thus avoid forcing reserve scheme banks into the standing facilities with a consequence potential impact on market interest rates'. The OMOs conducted by the Bank of England (2008:3) as part of the SMF consisted of short and long-term repo (sale and repurchase agreements) and outright purchases of eligible

assets from the banking system[139]. Thus, the Bank of England (2009a:46) *Inflation Report* of February 2009 highlighted that QE 'continued to exploit the bank's position as monopoly supplier of reserves', the difference being that whilst the Bank Rate focused on 'reducing the price of… reserves', QE focused on expanding the quantity of reserves and using the proceeds to purchase a range of financial assets.

The paper provided by Borio and Disytat (2009:1) also stated that Central Bank 'balance-sheet- policy was 'unconventional' because of the 'specific market segment chosen as the focus of central bank operations'. This sentiment was also expressed by Dale (2009:8), in a speech on the 27th March 2009, when he stated that what was different about QE from previous monetary policies "is the range of assets being purchased by the Bank and the scale of those purchases'. However, in a speech on the 20th January 2009, King (2009) claimed that "conventional approach to such unconventional measures" is to buy "government securities or gilts" whereas the unconventional approach to unconventional measures was the purchase of assets in credit markets. Thus, the orthodoxy of QE is further demonstrated by the long-standing use of gilt purchases by the Bank of England in the SMF. Indeed, by the end of January 2010, the Bank of England (2010a:16) stated in its *Quarterly Bulletin* of Q1 2010 that of the £200billion of asset purchases conducted via QE, £198.3billion of the purchases had been of gilts. Within that £198.3billion figure, the Bank of England had purchased £88.6billion worth gilts with a 3-10year maturity, £84.8billion worth of gilts with a 10-25year maturity and £24.8billion worth of gilts with a maturity over 25years.

It was only on the 14th March 2005, for example, that the Bank of England (2005c:22) announced that, whilst it would still conduct repo agreements for Treasury bills, it would no longer conduct outright purchases. Indeed, the Bank of England (2006h:364) noted that repo agreements in gilts had formed the largest component of OMOs within the SMF since their introduction in May 1997. Thus, whilst outright purchases of gilts and Treasury bills had always formed only a small

[139] The role of OMOs in monetary management, in the manner described by this paragraph, was affirmed by the Bank of England (2008b:17-24;2008d:137-142; 2008f:264-269;2008h:373-378;2009d:19-22;2009f:83-85;2009h:171-173;2009j:269-270;2010a:18-19 in successive *Quarterly Bulletins* during the Brown government.

percentage of OMOs conducted by the Bank of England, such purchases had formed part of the SMF only four years before the introduction of QE (Ibid).

Indeed, the introduction of QE on the 5th March 2009 did not even signal the re-introduction of outright purchases of UK government debt by the Bank of England to the SMF, which had actually occurred in January 2008 when the Bank of England announced that it would add to its OMOs the outright purchase of UK government bonds. This was affirmed in the Bank of England (2008:8,10,20,21,23) 'Red Book' of 2008, which stated that the 'bonds purchased… compromise conventional gilts' via 'open market operations' at maturities of a maximum of twenty-one years and a minimum of three years in order to provide long-term financing to the UK banking system. The first purchase of £400million of gilts was conducted by the Bank of England (2008b:2) on the 28th January 2008 and every month thereafter – excluding December – until the introduction of QE.

The Bank of England (2008d:142) added further to its range of OMO's dealing in gilts with the introduction of the Special Liquidity Scheme (SLS) on the 21st April 2008, which made £50billion of Treasury bills, for an initial six month period, available to the banking system for swap with illiquid mortgage-backed securities. The aim of the SLS, according to the Bank of England (Ibid), was to 'improve the liquidity position of the banking system and increase confidence in the financial markets'. The SLS was extended to £200billion by Darling (2008h) on the 8th October 2008, which formed part of the £500billion recapitalisation scheme announced on the same day.

The Bank of England (2008h:380) then introduced in October 2008 as part of its OMO operations the Discount Window Facility (DWF), which provided a permanent institution within the SMF to provide liquidity insurance to banks in the event of extreme economic stress. Specifically, the DWF allowed banks to borrow government securities with a maturity of thirty days, in exchange for a commercial fee, against a wide range of collateral. The DWF was then extended on the 19th January 2009 to allow banks to borrow government securities with a maturity of three hundred and sixty-four days to provide longer-term liquidity to the financial

markets. Thus, Paul Fisher (2009a:9), Executive Director of Markets at the Bank of England and Member of the MPC (2009-2014), noted in a speech on the 19th November 2009 that the DWF drew upon many of the features of the SLS because it allowed banks to borrow gilts from the Bank of England.

The orthodox nature of QE is further evidenced in that it provided a complement to the orthodox monetary policy instrument of the Bank Rate, rather than abrogation, whilst the transmission mechanism of monetary policy was impaired. One of the aims of QE, as explained in a number of policy documents and public speeches by Bank of England officials and MPC members, was to increase the money supply in the UK economy[140]. For example, the minutes of the MPC meeting held on the 4th and 5th February 2009 noted that the impact of QE on the money supply would be direct via an increase in the money stock of investors and institutions who sold assets and indirect through an expansion of credit from the banking system (Bank of England,2009b:8)[141]. Thus, in a speech on the 20th January 2009, King (2009:7) highlighted that asset purchases, which included the purchase of gilts would "increase the supply of broad money and credit". Accordingly, in a speech on the 12th June 2009, Fisher (2009:6) noted that 'instead of easing monetary conditions by cutting the Bank Rate" and thus affecting the price of money, QE allowed the Bank of England to "ease conditions by increasing the quantity of money in the economy directly" through the creation of Central Bank reserves.

The complement provided by QE to the Bank Rate is also evidenced in the similarity between the transmission mechanisms of the two monetary policies. For example, Fisher (20096-7) identified in his speech on the 12th June 2009 four separate transmission mechanisms of QE, which were claimed as "not much more complex than that for a change in the Bank Rate". First, QE would increase demand

[140] The aim of QE being to increase the money supply in the UK economy was expressed in a number of Bank of England (2009a:46;2009e:5,16;2009f:69) *Inflation Reports* and *Quarterly Bulletins*. Moreover, it was highlighted in a number of public speeches by Bank of England officials and MPC members such as Bean (2010:4), Blanchflower (2009:13-15), Dale (2009:13-15;2010:2) and King (2009:7;2009b:3).
[141] The Bank of England (2009a:46;2009e:16) *Inflation Reports* of February and May 2009 also noted that QE would ease credit conditions and increase lending by the banking system.

for those assets not purchased by the Bank of England. Second, expanding the banking systems reserves at the Bank of England, which were credited when assets were purchased, would support bank lending. Third, an expanding money supply would give people confidence. Fourth, the provision of liquidity in key markets would improve market function[142]. Indeed, Mervyn King asserted in oral evidence to the Treasury Committee (2010:Ev.4,Q.14) on the 23rd February 2010 that the way QE worked was "through a very traditional transmission mechanism, not dissimilar to the way changes in the Bank Rate work, by leading to changes in asset prices, in the spreads on particular instruments in the economy which can lower the costs of finance to companies and households, through a range of channels".

The orthodox nature of the monetary policy instrument of QE was also evident in that it could be deployed within the existing monetary policy framework. For example, in his Statement of the 5th March 2009, which authorised the purchase of gilts via the creation of central bank money, Darling (2009b) stated that QE did not "affect the objectives of the Government's monetary policy framework. The objective of the Monetary Policy Committee continues to be to maintain price stability, and subject to that, support the Government's economic policy, including its objectives for growth and employment". Thus, a paper authored by members of the Bank of England's Monetary Analysis Division (Benford,2009:90) stated that whilst the 'introduction of asset purchases has shifted the focus of monetary policy' to the quantity of money in the UK economy, rather than its price, 'the objectives have not changed' and 'asset purchases provide an additional tool to help the committee meet those objectives'. For instance, the Bank of England (2009f:69) *Quarterly Bulletin* published in Q2 2009 identified that through an increase in the money supply, it was hoped that QE would stimulate nominal spending and demand in the UK economy and lead to a higher rate of economic growth, which, in turn, would increase prices and allow the MPC to meet the inflation target.

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[142] These four transmission mechanisms of QE were also identified by the Bank of England (2009e:16) *Inflation Report* of May 2009 and the minutes of the MPC meetings held on the 4th and 5th March 2009 (Bank of England,2009c;8-9).

The Temporary Deviation Phase in Fiscal Policymaking from the 24th November 2008 to the 8th December 2009

The temporary deviation phase is initiated at the moment of implementation of an 'unorthodox' macroeconomic strategy, which consists of the use of 'unorthodox' policy instruments that lead to 'unorthodox' policy outcomes in economic performance. However, this phase explains that change in UK macroeconomic policy occurs only temporarily in the aftermath of crises, which do not provide the stimulus for permanent radical change in policy or ideas as understood by punctuated equilibrium. Thus, the orthodox cycle can account for developments in fiscal policymaking via the temporary deviation phase of the orthodox cycle, which was initiated at the 2008 Pre-Budget Statement of the 24th November.

The Treasury (2008:1-2,4) Pre-Budget Report of the 24th November 2008, for example, announced the implementation of 'discretionary fiscal policy to support the economy through these difficult times', which was 'designed as a timely response to the UK economy entering recession'. The discretionary strategy announced at the 2008 Pre-Budget Report included both spending and revenue measures such as a temporary reduction in Value Added Tax (VAT) rates from 17.5% to 15% from the 1st December 2008 to the 31st December 2009, £3billion of capital investment brought forward from 2010-2011 to 2008-2009 and a range of measures to provide tax relief and credit support to businesses. The Treasury (2008:14,20) calculated that the total discretionary fiscal policy support to the UK economy provided in the 2008 Pre-Budget amounted to 1.7% GDP in 2008-2009 and 2009-2010. The discretionary fiscal policy strategy was maintained at the 2009 Budget via a reduction on stamp duty on all homes worth £175,000 or above, provision of capital allowances for business investment and £600million allocated to house-building (HM Treasury,2009:1). Furthermore, Darling (2009g) announced in his 2009 Budget Statement of the 22nd April a £300million car scrappage scheme, which saw government contribute £1000 to the purchase cost of a new vehicle registered after the 16th May 2009.

The discretionary fiscal policy strategy therefore consisted of purposeful increases in public expenditure and tax reductions. For example, Table One shows that total managed expenditure (TME) rose to 45.2% GDP by 2009-2010, 10.4% of GDP higher than the 34.8% of GDP inherited by New Labour in 1997-1998 (OBR,2016a). Similarly, Table One highlights that public sector current expenditure rose to 39.8% of GDP, a level 7.5% of GDP higher than the 32.3% of GDP inherited by New Labour in 1997-1998 (Ibid). Meanwhile, in 2015-2016 prices, TME and public sector current expenditure rose by £95.7billion and £46billion respectively during the three years of the Brown government. Moreover, public sector net investment rose by 1.4% of GDP. Finally, the fall in 1.3% GDP in Public Sector Current Receipts and 1.5% GDP in National Account Taxes was a consequence the tax component of the discretionary fiscal policy stimulus and the impact of declining tax revenue due to recession and low economic activity.

Table One: Public Expenditure and Taxation during the Brown Government, 2007-2010

Year	**Total Managed Expenditure** (% of GDP)	**Total Managed Expenditure** (2015/16 Prices) *(Billions)*	**Public Sector Current Expenditure** (% of GDP)	**Public Sector Current Expenditure** (2015/16 Prices) *(Billions)*	**Public Sector Net Investment** (% of GDP)	**Public Sector Current Receipts** (% of GDP)	**National Account Taxes** (% of GDP)
2007-2008	39%	£658.3	35.2%	£618.0	2%	36.4%	34%
2008-2009	42.6%	£727.0	37.3%	£637.6	3.3%	35.8%	33.2%
2009-2010	45.2%	£754	39.8%	£664.0	3.4%	35.1%	32.5%

Source: (OBR,2016a).

The discretionary fiscal policy strategy therefore also contributed to a significant increase in government borrowing and national debt. For example, Table Two shows that the 'unorthodox' fiscal strategy implemented by the Brown government exacerbated the departure from orthodox fiscal policy outcomes of the balanced or surplus budget and national debt reduction, which the previous chapter explained occurred in 2002-2003. Furthermore, Table Two shows that the combination of existing government borrowing, discretionary fiscal policy and automatic stabilisers in the public finances served to increase Public Sector Net Borrowing to 10.1% GDP, which amounted to an increase of 7.5% GDP from 2007-2008. Meanwhile, the Current Budget deficit rose to 6.7% GDP and the Primary Balance deficit stood at 8.6% GDP in 2009-2010. Finally, Public Sector Net Debt increased significantly by 28.6% GDP during the Brown government, which was due to a combination of the discretionary fiscal policy strategy, the automatic stabilisers and the liabilities of the nationalised banks being brought into the UK public finances.

Table Two: Government Borrowing and National Debt during the Brown Government, 2007-2010

Years	Public Sector Net Borrowing (% of GDP) *(+ = Deficit)*	Cyclically-Adjusted Net Borrowing (% of GDP) *(+ = Deficit)*	Current Budget Deficit (% of GDP) *(+ = Deficit)*	Cyclically-Adjusted Current Budget Deficit (% of GDP) *(+ = Deficit)*	Primary Balance (% of GDP) *(- = Deficit)*	Cyclically-Adjusted Primary Balance (% of GDP) *(- = Deficit)*	Public Sector Net Debt (% of GDP)
2007-2008	+2.6%	+3.7%	+0.6%	+1.7%	-1.1%	-2.2%	35.8%
2008-2009	+6.7%	+6.6%	+3.4%	+3.4%	-5%	-5%	50.6%
2009-2010	+10.1%	+8.0%	+6.7%	+4.7%	-8.6%	-6.5%	64.4%

Source: (OBR,2016a).

Gordon Brown also pursued a vigorous global diplomatic agenda to create an international political coalition in favour of discretionary fiscal policy strategy to support economic activity and economic growth in the world economy. Here, Brown's actions were based on his belief that the efficacy of domestic discretionary fiscal policy strategies was increased if pursued in cooperation with other nation-states in the global economy[143]. This diplomatic agenda reached the apex of success at the G20 Summit held in London on the 2nd April 2009. The Leaders' Statement

[143] Brown (2008d;2008f;2008h;2009a;2009j) expressed on a number of occasions his belief that discretionary fiscal policy was best pursued as part of a global economic strategy.

published after the London G20 (2009:1-2) Summit posited that in response to 'a global crisis [that] requires a global situation' the G20 countries had agreed to 'an unprecedented and concerted fiscal expansion' worth $5trillion, which would 'save or create millions of jobs' and 'raise output' in the global economy 'by 4 per cent'.

The orthodox cycle can also account for developments in politics as the temporary deviation phase expects to see the deployment of a policy narrative in discourse, which seeks to legitimise the 'unorthodox' macroeconomic policy strategy as the policy solution to the crisis phase. The Brown government sought to legitimise the implementation of an 'unorthodox' fiscal policy strategy through a 'growth' narrative, which appealed to the need to support economic activity and employment during a downturn[144]. For example, in a speech to the CBI on the 24th November 2008, the same day as the 2008 Pre-Budget Statement, Brown (2008h) stated that "we have seen in previous recession how a failure to take action at the start of the downturn has increased both the length and depth of a recession. It was a mistake made in the recession of the 80s and 90s". Consequently, Brown (Ibid) posited that "doing too little too late would mean more damage and more deterioration, the loss of vital successful businesses. And it would mean a weaker economy, lower growth, eventually greater fiscal problems and in that event, higher interest rates and higher taxes". In particular, the 'growth' narrative often referred to the "mistakes of the 1930s", such as in the speech made by Brown (2009n) on the 5th September 2009, which argued that the lessons of that decade taught us that "public investment and spending" played "a key role in supporting demand and protecting jobs".

In his study of the *representation of the economic crisis in contemporary Britain*, however, Pirie (2012) highlights that a primary narrative, which focused on the precariousness of the state's fiscal position and the profligacy of past and present Labour governments with the public finances became the dominant interpretation of

[144] The 'growth' narrative argued that discretionary fiscal policy stimulus was necessary to stimulate economic activity, growth and employment was expressed by Brown (2008b;2008c;2008d;2008e;2008f;2008g;2008h;2009;2009a;2009b;2009e; 2009f;2009g;2009j;2009k;2009n;2009o;2009p;2009s;2009u;2010b),Darling (2008k; 2008l;2009c;2009d;2009f;2009g;2009i;2009j;2009l;2009m;2009n;2009o;2009q; 2010a) and Mandelson (2009;2009b).

the crisis in the UK media by the end of 2008. Here, Pirie (2012:354) blames the emergence of this narrative in the media, at least in part, in the 'failure of the Labour party to advance any coherent crisis narrative of its own'. For example, this chapter has highlighted two separate crisis narratives deployed by the Brown government alongside a 'growth' narrative to legitimise the 'unorthodox' discretionary fiscal policy strategy.

In contrast to the numerous narratives deployed by the Brown government, the Conservative opposition led by Cameron and Osborne continued to deploy a focused and relentless 'debt crisis' narrative. This narrative not only sought to interpret events and emergencies in global financial markets and designate them as a crisis of government debt, but also sought simultaneously to de-legitimise the discretionary fiscal policy strategy of the Brown government and legitimise cuts to public expenditure as the solution to that crisis. For example, in his reply to Darling's 2008 Pre-Budget Statement, Osborne (2008c:c.504) stated that the "Chancellor is borrowing more on the nation's credit card than all previous Governments put together… like the gambler who cannot give up, he still thinks that he can borrow his way out of debt". Moreover, in his speech on the 19th March 2009, Cameron (2009b) stated that "our overriding objective will need to change from sharing the proceeds of growth, to paying down our debt. To achieve this, we need clear plans for controlling public spending". Thus, in a speech on the 26th April 2009, Cameron (2009d) argued that the "alternative to dealing with the debt crisis now is mounting debt" and "everybody knows that Labour's debt crisis means public spending cuts". Here, Cameron (Ibid) added that the economy needed to replace "Labour's spendaholic government with a new government of thrift". Similarly, in a speech on the 8th April 2009, Osborne (2009b) declared that "the politics of prosperity is giving way to the politics of austerity".

Chapter Five identified that certain elements of the temporary deviation phase required further analysis to fulfil the potential of the orthodox cycle in explaining change and continuity in UK macroeconomic policymaking. One of the elements that needed further explication was the role of ideas in the temporary deviation phase. For example, it was highlighted that it was not yet understood whether the formulation of

'unorthodox' macroeconomic strategies rested on anything more substantial – such as the adoption of 'unorthodox' economic ideas – than expediency in the face of significant events and emergencies that required policy action. Here, analysis of economic ideas during the Brown government demonstrated that the formulation of the discretionary fiscal policy strategy during the temporary deviation phase was based on the adoption of the 'unorthodox' economic ideas of John Maynard Keynes (Lee.2010:29;Osborne,2008d). For example, in their account of the Brown government, which was based on anonymous interviews with Cabinet ministers, civil servants and political advisors at No.10, Seldon and Lodge (2011:192,363) identified that the economic ideas of Keynes were an important influence on Gordon Brown's thinking during the Global Financial Crisis. In particular, Seldon and Lodge (2011:192) claimed that Keynes provided Brown, who had 'long believed in the efficacy of public spending', with a 'contemporary relevance' for the deployment of fiscal policy in that 'it would help bring Britain out of recession more quickly'.

The impact of 'Keynes' on the formulation of the discretionary fiscal policy strategy during the temporary deviation was evident in numerous public speeches delivered by Brown, Darling and Peter Mandelson, First Secretary of State (2009-2010), which made direct reference to 'Keynes'[145]. For example, in his speech at Bloomberg on the 13th October 2009, Brown (2009s) declared that "in the 1920s and 1930s, politicians in Britain made fatal mistakes", which included the rejection of "Keynes" who had recommended inter-war governments should take policy action "to move us quickly out of recession". Here, Brown (Ibid) highlighted that Keynes' economic ideas were rejected because "the economic orthodoxy was to suggest that the measures that were being proposed [such as schemes of public-works financed by government borrowing] would lead to inflation, extravagancy and bankruptcy" [146].

[145] Brown (2008a;2008d;2009b;2009l;2009s;2009t;2009u), Darling (2008i:2009c; 2009i;2009q;2010) and Mandelson (2009) made direct reference to Keynes and his economic ideas on several occasions in public speeches.

[146] Brown (2008a;2008c;2008d;2008h;2009b;2009h;2009s;2010b) claimed in several public speeches that the Global Financial Crisis had demonstrated the need to leave behind economic policy 'orthodoxy' or 'orthodoxies' of the past and adoption of new economic ideas and new policy solutions. Furthermore, Brown (2010:xix) argued

Furthermore, in an interview with the Daily Telegraph (Hennessy,2008) on the 18th October 2008, Darling asserted that Keynes was 'the greatest economist of the last century' and that 'much of what Keynes wrote still makes a lot of sense'. In his memoir, Darling (2011:177) affirmed that by the end of 2008 he had been 'hugely influenced by Keynes' thinking'.

Specific ideas advanced by Keynes and articulated by key members in the Brown government can be identified, which were used to formulate the discretionary fiscal policy strategy. For example, in his book on the Global Financial Crisis, Brown (2010:10-11,12,142) echoed Keynes' critique of neoclassical economic theory, which can be found in footnote twenty-two of Chapter Three, and claimed that orthodox economic theory of perfect information and optimal and self-regulation markets were 'irrelevant to the conditions we faced' because the crisis had showed that 'economic players are not always rational, markets are not self-correcting, that employment does not automatically recovery, and that a wholly deregulated, passive model of capitalism… cannot cope with the extreme fluctuations and shocks…. We saw in the banking crisis'. Consequently, Brown (2010:142) identified that it was necessary for government to support economic activity and employment through policies to secure a 'higher level of aggregate demand'. Thus, Brown expressed the ideas expressed by Keynes (1936/2007) in his *General Theory of Demand, Money and* Interest, which posited that economic growth and employment was dependent on the level of aggregate demand in an economy and when threatened with economic downturn government should seek to inject demand into an economy in order to stimulate economic activity and employment.

Alistair Darling also expressed several economic ideas, which were developed by Keynes in support of his *General Theory*. One such economic idea was the 'paradox of thrift', which argued that increased saving by households and business would not lead to increased lending and investment as bank expanded their deposits, but rather would exacerbate a downturn in the economy via a reduction in

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that nationalisation of banks and discretionary fiscal policy strategy were examples of the reversal of "decades of orthodoxy".

consumption and investment, which would lead to lower total saving in the economy (Keynes,1936/2007). For example, in a speech on the 12th February 2010, Darling (2010) stated that "when times are difficult, families will rightly tighten their belts. Governments must behave differently. At a time of low private sector activity, continued government spending provides vital demand. Pull away that support too soon… you hurt growth, reduce the tax take, push up benefit spending, and eventually make borrowing worse. That is the key lesson from the 1930s and what Keynes called the paradox of thrift"[147]. Darling (2011:177) also noted in his memoir the importance of the 'multiplier effect', which claimed that initial impact of government spending on economic activity would multiply through increased consumption and investment in the economy (Kahn,1931/1972; Keynes,1933/1972), in his fiscal policy decisions as Chancellor.

A further economic idea of Keynes used by the Brown government to formulate the discretionary fiscal policy strategy was that of liquidity traps, which claims that when interest-rates fall towards the zero lower-bound monetary policy will be ineffective in stimulating an economy (Sutch,2014:8-13). Indeed, in his book on the Global Financial Crisis, Brown (2010:75) claimed that Keynes' work on liquidity traps and the experience of the Japanese economy in the 1990s and 2000s had taught him 'hard lessons' that 'once recession takes hold, it cannot easily be reversed by monetary policy alone'. Thus, in a speech on the 14th November 2008, Brown (2008d) contended that "as Keynes recognised in the 1930s when he talked about the problems of not being able to see the effective response that he expected from interest rates, you have got to look at other means too", which included "a fiscal response". More explicitly, in a speech on the 24th November 2008, Brown (2008h) posited that "the orthodoxy of the last few decades has been that monetary policy is the only effective instrument for economic management", however, in the context of

[147] Darling (2009p;2011:175-177) also articulated the 'paradox of thrift' in a speech on the 21st October 2009 and in his memoir.

the impairment of the monetary policy transmission mechanism, "it would be a mistake to rely entirely on it to pull the economy out of downturn"[148].

As a result, the temporary deviation phase in fiscal policymaking saw a reversal in the orthodox hierarchy between macroeconomic policy instruments as monetary policy played a supportive role to fiscal policy, rather than vice versa, in the stimulation of economic activity and employment in the UK economy. This argument is strengthened when we consider our previous discussion of monetary policy during the consolidation phase, which saw orthodox monetary policy instruments used to provide stimulus to nominal spending and nominal demand. Consequently, David Blanchflower (2009a:8), Member of the MPC (2006-2009), stated in a speech on the 25th February 2009 that "when monetary policy becomes ineffective because financial markets have become dysfunctional, it is left to fiscal policy to provide an effective stimulus to the economy' and the formulation and implementation of macroeconomic policy was "largely returning to the ideas attributed to Keynes".

The Consolidation Phase in Fiscal Policymaking from the 9th December 2009 to the 2010 General Election

Despite the articulation of a 'growth' narrative by the Brown government, memoirs published by Darling (2011:11,217,224,253,262-263,266) and Mandelson (2010:450,463-465,467,476-478,483-484,489-499) commented upon the internal division within the Labour Party. On one side stood Gordon Brown and Ed Balls, Secretary of State for Children, Schools and Families (2007-2010), who favoured an 'investment/growth' electoral strategy at the 2010 general election. On the other were Darling and Mandelson who thought such a strategy would only work if the

[148] Brown (2009b;2009n) and Darling (2008k;2008l;2009q) noted in several public speeches that fiscal policy was necessary to stimulate the UK economy due to the impairment of the transmission mechanism of monetary policy on several occasions.

Brown government had established prior that they would reduce public spending and the deficit once economic recovery had been established. Thus, Darling (2011:180-181,218) highlighted in his memoir that he believed it has been necessary to 'show a plan to cut borrowing and reduce debt as we moved out of recession' not just for reasons of electoral strategy, but, also, to maintain the confidence of the financial markets and because 'it was one of many preconditions for a return to growth'.

An important aspect of the 'growth' narrative therefore was the acceptance that discretionary fiscal policy stimulus was only 'temporary' and once economic recovery was secured consolidation would take place in the UK public finances to reduce the fiscal deficit[149]. For example, prior to the implementation of discretionary fiscal policy at the 2008 Pre-Budget, Darling (2008f) stated in his speech to the Labour Party Conference on the 22nd September 2008 that, whilst it would have been irresponsible not to have taken policy action to limit economic downturn, it was "equally irresponsible, once recovery is assured, not to take tough action so we can live within our means", which would include "get[ting] borrowing down, spending will have to be tighter in the years ahead". Thus, Mandelson (2009a) stated in a speech to Progress on the 14th September 2009 that the Brown government must not "allow ourselves to be painted as a party that is oblivious to economic conditions" and that it was their "duty… to pass on sound finances… there will be pressures on spending once we are safely through the recession". Consequently, Mandelson (2010a) stated in a speech on the 6th January 2010 that "deficit-reduction is a three-sided triangle: spending reductions, tax increases and economic growth".

Indeed, the temporary nature of the discretionary fiscal policy stimulus had been evident from its very initiation at the 2008 Pre-Budget Report. For example, Darling (2008k) announced in his 2008 Pre-Budget Statement that henceforth fiscal policy would be conducted according to a temporary operating rule, which had two

[149] That discretionary fiscal stimulus was only a 'temporary' policy and once economic recovery was secured it was necessary to implement consolidation in the UK public finances to reduce government borrowing was identified by Brown (2008d;2008h; 2009b;2009l;2009m;2009n;2009p;2009s;2009t;2009u;2010b), Darling (2008j;2009l; 2009m;2009p;2010) and junior ministers at the Treasury such as Myners (2010) and Pearson (2010) in public speeches.

elements. First, to improve the position of cyclically-adjusted Current Budget each year until reaches balance once economic recovery had been secured. Second, to ensure that debt as a percentage of GDP fell once global shocks had dissipated from the economy. Consequently, the Treasury (2008:1) Pre-Budget Report stated that discretionary fiscal stimulus would be followed by fiscal consolidation in 2010-2011 when 'the economy is expected to be recovering and able to support a reduction in borrowing'. Furthermore, several policies of consolidation were introduced at the 2008 Pre-Budget Report, which included an increase in the higher rate of tax from 40% to 45% to take effect from April 2011, increases in National Insurance Contributions (NIC) by 0.5% from April 2011 and restriction on tax allowances on incomes over £100,000 from April 2010 (HM Treasury,2008:1). Policies of consolidation were also introduced at the 2009 Budget (HM Treasury,2009:1), which included an increase on tax on incomes over £150,000 from April 2010 to 50%, immediate increases in fuel duties and changes in tax relief on pension contributions over £150,000 from April 2011. Consequently, the Treasury (2009:17,19) 2009 Budget Report stated that 'once the economy emerges from the downturn', fiscal consolidation would begin in 2010-2011 and would achieve an average reduction in the cyclically-adjusted current balance of 0.8% GDP in each year from 2010-2011 to 2013-2014.

The consolidation phase of the orthodox cycle is initiated when a macroeconomic strategy is implemented that deploys orthodox policy instruments, which are used to create the conditions in economic performance necessary to secure a later return to orthodox fiscal policy outcomes. Thus, the orthodox cycle explains that fiscal policymaking left the temporary deviation phase at the Pre-Budget Statement on the 9th December 2009 when a consolidation phase in fiscal policymaking was initiated. The Treasury (2009a:13,20) 2009 Pre-Budget Report stated that 'government action has been successful in averting the more severe downturn risks to the economy' and the government 'judges that a gradual transition for fiscal policy, from supporting activity in the recession to supporting the conditions for growth in the recovery is appropriate'. According to the Treasury (2009a:31) in the 2009 Pre-Budget Report, supporting the conditions for economic

growth meant 'delivering a sustained fiscal consolidation' in the public finances, which would 'ensure sound public finances, creating space for continued support to the economy during the early stages of recovery'. Thus, the Treasury (Ibid) asserted that 'actions to reduce borrowing and to support growth are mutually reinforcing: sound public finances are necessary for sustainable economic growth'.

It was at the 2009 Pre-Budget that the Brown government also announced its intention to introduce a Fiscal Responsibility Bill to the House of Commons, which was subsequently passed into legislation in the Fiscal Responsibility Act on the 10th February 2010 (HM Treasury,2009a:5,37-38). The Fiscal Responsibility Act enshrined plans for fiscal consolidation in statutory legislation and required the government to halve Public Sector Net Borrowing by 2013-2014, reduce borrowing as a percentage of GDP each and every year from 2010-2011 and ensure that Public Sector Net Debt falls as a percentage of GDP in 2015-2016. In a speech on the 12th February 2010, Darling (2010) claimed that the plan to halve government borrowing within four years was "the most ambitious deficit reduction plan of any G7 country". Furthermore, Brown (2010b) contended in a speech on the 10th March 2010 that the Fiscal Responsibility Act was the "first time in British history, the government has made a tough legally binding commitment to reduce the deficit: a contract between the government and the British people".

Despite the claim by the Brown government that the UK economy should be supported by fiscal stimulus until the economic recovery was secure[150], the Institute of Fiscal Studies (IFS) (2010;43-44,54) noted in their 2010 *Green Budget* that the decision not to implement further discretionary fiscal policy in the 2009 Pre-Budget meant that the Brown government and Treasury had withdrawn fiscal stimulus in the UK economy by the start of 2010. Indeed, the IFS (Ibid) highlighted that withdrawal of stimulus would lead to a fiscal 'tightening' in the public finances worth 0.6% GDP in 2010-2011 and 1.6% GDP once the public finances had been cyclically-adjusted.

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[150] Brown (2009n;2009o;2009p;2009q;2009s;2009t;2009u;2010a;2010b), Darling (2009p:2010) and Mandelson (2009b;2009c;2010b) regularly warned, in public speeches, of the economic danger of withdrawing fiscal support from the economy by introducing public spending cuts in 2010, which would reduce economic activity and lead to higher unemployment.

Thus, the IFS (2010:44) declared that 'out of the 19 countries of the G20… the UK and Argentina are the only two not planning to implement a discretionary fiscal stimulus' in 2010.

The IFS' (2010:54) *Green Budget* of 2010 also identified that the public finance forecasts in the 2009 Pre-Budget Report, which envisaged a reduction in the Current Budget deficit to 2.9% GDP by 2014-2015 in order to meet the fiscal targets in the Fiscal Responsibility Act, meant the Brown government would have to implement a four year fiscal consolidation period worth 5.9% GDP in the public finances. If the Brown government were to keep to the forecasts presented in the 2009 Pre-Budget Report, the IFS (2010:54,56) highlighted that it would 'require deep cuts' in Departmental Expenditure Limits (DEL) worth 10.9% in the four years from 2010-2011 to 2014-2015, which would 'reverse almost all of the increases in DEL as a share of national income seen since Labour took office'.

Consolidation in fiscal policymaking was maintained at the 2010 Budget on the 24th March, which the Treasury (2010:1) Budget Report explained was 'fiscally neutral' and confirmed 'the government's plans to more than halve the deficit over four years, maintaining a credible path of fiscal consolidation'. The 2010 Budget announced further policies of consolidation including £11billion worth of 'savings' in public expenditure, reduction in public sector net investment to 1.25% GDP by 2013-2014, public spending restraint with real term per annum increases in public sector current expenditure capped at 0.8% and above inflation increases in fuel, alcohol and tobacco duties. In an interview with the British Broadcasting Corporation (2010) on the 25th March 2010, just one day after his Budget Statement, Darling (2010a) admitted that in order to meet the fiscal plans laid out in the 2010 Budget, public spending cuts would have to be "tougher and deeper" than those implemented by the Thatcher governments.

Consequently, a paper published by the IFS (2010a) in the build up to the 2010 general election found that the fiscal plans of the three major British political parties, Labour, Conservatives and Liberal Democrats, were very similar with the difference between them not in overall objectives; the three political parties aiming

for fiscal consolidation of the same size, but rather in composition and timing. First, the Labour and Liberal Democrats favoured tax increases to share a greater burden in fiscal consolidation than public spending cuts. Second, the Labour and Liberal Democrats wished to spread fiscal consolidation over a longer time period. However, even on this issue, the IFS (2010a:35) concluded that ‘the Conservatives want to start earlier and proceed more quickly, but not sufficiently so that this would make a dramatic difference to the outlook for government borrowing or debt’.

Conclusion

This chapter has provided a case-study of UK macroeconomic policy during the government of Gordon Brown, Prime Minister (2007-2010), from the 27th June 2007 to the 5th May 2010 and the Global Financial Crisis of 2007-2009. This chapter has drawn four conclusions pertaining to why the orthodox cycle provides a superior explanation and understanding of developments in UK macroeconomic policymaking than that furnished by punctuated equilibrium. First, the orthodox cycle provides exactitude in the initiation of a crisis phase in UK macroeconomic policymaking on the 16th September 2007, which occurred when David Cameron deployed a narrative that sought to interpret events in the global financial markets and the emergency of the bank run on Northern Rock as a ‘debt crisis’. Indeed, Cameron and the Conservative opposition continued to apply this ‘debt crisis’ narrative up until the 2010 general election, which was opposed by two counter-narratives deployed by the Brown government. Finally, the orthodox cycle could account for the economic policies of financial interventionism implemented by the Brown government, which is the orthodox approach to crises that consist of events and emergencies in financial markets.

The second conclusion drawn is that the orthodox cycle explains that the Global Financial Crisis led not to radical and permanent monetary policy change, but rather the continuity of orthodox monetary policy as monetary policymaking entered

a consolidation phase of the orthodox cycle on the 8th October 2008. Specifically, the orthodox cycle expounds that orthodox monetary policy instruments of the Bank Rate and OMOs were used to create the conditions in economic performance necessary to return to the orthodox objective of price stability. This argument included the identification of QE as an OMO and thus a continuation of orthodox monetary policy. Furthermore, continuity in the monetary policymaking framework was highlighted as important to the consolidation phase because it meant inflation targeting endured as a guide policymaker's operational decisions in terms of policy instruments and policy objectives. Finally, the orthodox cycle could account for the introduction of 'unorthodox' monetary policy instruments such as the CGS, which, in the context of impairment in the transmission mechanism of the Bank Rate, was used to create the conditions in economic performance necessary to return to the orthodox objective of price stability.

The third conclusion drawn is that the orthodox cycle reveals that change in fiscal policy and economic ideas did occur in response to the Global Financial Crisis. However, rather than innovation leading to a new policy equilibrium, the orthodox cycle expounds that fiscal policymaking entered a temporary deviation phase at the 2008 Pre-Budget Statement of the 24th November. The temporary deviation phase consisted of a discretionary fiscal policy strategy involving 'unorthodox' fiscal policy instruments and outcomes. Furthermore, the discretionary fiscal policy strategy was formulated due to the adoption of 'unorthodox' economic ideas of John Maynard Keynes, which allowed the chapter to go some way towards addressing the areas identified in Chapter Five that required further analysis to fulfil the potential of the orthodox cycle in explaining change and continuity in UK macroeconomic policymaking. Finally, the Brown government sought to legitimise the discretionary fiscal policy strategy via the articulation of a 'growth' narrative, which was opposed by Cameron and the Conservative opposition by the policy element of the 'debt crisis' narrative.

The fourth conclusion is that the orthodox cycle understands fiscal policymaking joined monetary policymaking in the consolidation phase at the 2009 Pre-Budget on the 9th December. Here, the chapter noted the internal conflict

surrounding fiscal policymaking within the Brown government and how future consolidation of the public finances had always been a component part of the discretionary fiscal policy strategy implemented at the 2008 Pre-Budget. The consolidation phase was then initiated at the 2009 Pre-Budget, which withdrew fiscal stimulus from the UK economy and set in place plans for government borrowing and national debt that, if enacted, would have led to deep cuts in public expenditure and tax increases.

Chapter 9

Change and Continuity in UK Macroeconomic Policymaking during the Cameron-Clegg and Cameron Governments of the 12th May 2010 to the 13th July 2016

Introduction

This chapter provides a case-study of UK macroeconomic policy during the David Cameron, Prime Minister (2010-2016), and Nick Clegg, Deputy Prime Minister (2010-2015) coalition government of the 12th May 2010 to the 7th May 2015 and the Cameron government from the 8th May 2015 to the 13th July 2016. The purpose of the case-study is to see whether the orthodox cycle provides a superior understanding and explanation of change and continuity in UK macroeconomic policy than that furnished by punctuated equilibrium. The stimuli for radical policy, ideational and institutional change in the model of punctuated equilibrium arises from exogenous or endogenous shocks to the policymaking process, examples of which are both available in this period in UK politics and economic policymaking. For instance, according to punctuated equilibrium, the formation of the coalition government between the Conservatives and Liberal Democrats on the 11th May 2010, the first since the National government of 1931-1945, should have provided an endogenous shock to policymaking, which resulted in radical policy, ideational and institutional change. Meanwhile, UK economic performance had only returned to positive economic growth in two successive economic quarters (Q4 2009-Q1 2010) after the exogenous shock of the Global Financial Crisis of 2007-2009, which should also

have led to radical policy, ideational and institutional change that forms a new equilibrium in policymaking.

This chapter concludes that the orthodox cycle provides a superior understanding and explanation of change and continuity than that furnished by punctuated equilibrium for two reasons. First, the orthodox cycle explains that the Global Financial Crisis and the formation of the Cameron-Clegg government led not to radical monetary policy change, but rather the continuity of orthodox monetary policy as monetary policymaking remained in the consolidation phase of the orthodox cycle Second, the orthodox cycle expounds that the Global Financial Crisis and formation of the Cameron-Clegg government led not to radical fiscal policy change, but rather the continuity of orthodox fiscal policy as George Osborne, Chancellor of the Exchequer (2010-2016), and the Treasury initiated the orthodoxy phase of the orthodox cycle at the 'Emergency' Budget of the 22nd June 2010.

The chapter will be organised in the following manner. The first section of the chapter focuses on monetary policymaking. The chapter opens with the identification of continuity in the monetary policymaking framework originally introduced by the Blair government on the 6th May and 12th June 1997. The chapter then identifies the role of the Bank Rate in monetary policymaking. The chapter proceeds with an exploration of the various 'unorthodox' credit easing policies implemented by the Cameron-Clegg government. Finally, this section of the chapter analyses the role of Open Market Operations (OMOs) and operational changes implemented by the Bank of England to the Sterling Monetary Framework (SMF). Cumulatively, the chapter demonstrates that the Coalition and Conservative governments between the 11th May 2010 and the 13th July 2016 ensured that monetary policymaking remained in the consolidation phase of the orthodox cycle.

The second section of this chapter focuses on fiscal policymaking. The chapter proceeds with a discussion of the 'Emergency' Budget of the 22nd June 2010, which initiated in fiscal policymaking the orthodoxy phase of the orthodox cycle. Here, the chapter advances four reasons why the 'Emergency' Budget should be considered a significant event in fiscal policymaking. The chapter then progresses to

identify how this orthodoxy phase included the implementation of orthodox fiscal policy instruments in pursuit of orthodox fiscal policy outcomes, which had not been achieved by the time David Cameron resigned as Prime Minister. Finally, this section of the chapter closes with an exploration of the policy narrative deployed by the Cameron-Clegg and Cameron governments to legitimise the implementation of orthodox fiscal policy.

The third section of this chapter focuses exclusively on the role of economic ideas in the formulation of macroeconomic policymaking. In particular, the chapter identifies the importance of the orthodox economic ideas of globalisation, crowding-out, competitiveness and economic liberalism. During each discussion, the importance of orthodox economic ideas in the continuity of orthodox macroeconomic policy, rather, than radical policy change after the 12th May 2010 is highlighted in three specific areas. First, the implementation of deficit-reduction and restoration of orthodox fiscal policy. Second, the restoration of the orthodox hierarchy between macroeconomic policy instruments and the provision of monetary stimulus to the UK economy. Third, the return to the same division of responsibility between macroeconomic and microeconomic policy, which had been assigned economic by Nigel Lawson in his 1984 *Mais Lecture* and by New Labour governments after their election in May 1997.

The Continuation of the Consolidation Phase in Monetary Policymaking from the 11th May Onwards

The formation of the Coalition government between the Conservative and Liberal Democrats did not bring any immediate changes to the monetary policymaking framework introduced by the Blair government in May and June 1997. For example, the Bank of England (2010b:1) *Inflation Report* of May 2010, published on the 12th May, stated that the objective of monetary policy was to 'maintain price stability' whilst the operational remit for the Monetary Policy Committee (MPC) remained 'a

target for the annual inflation rate of the Consumer Prices Index of 2%. Subject to that, the MPC is also required to support the government's objective of maintaining high and stable growth and employment'. This objective for monetary policy and operational remit for the MPC was affirmed, up until the 2013 Budget of the 20th March, by Osborne and the Bank of England[151].

The inflation target in the operational remit was also affirmed as symmetrical and flexible. For example, in his *Remit for the MPC* letter published on the 23rd March 2011, Osborne (2011c:2) maintained that if 'inflation moves away from the target by more than percentage point in either direction' then the Governor of the Bank of England is expected to write an open letter setting out why inflation has moved away from target, the policy action to deal with it, the period within which inflation is expected to return to target and how this approach meets the Governments monetary policy objective. Furthermore, Osborne (Ibid) declared that 'the framework is based on the recognition that the actual inflation rate will on occasions depart from its target as a result of shocks and disturbances. Attempts to keep inflation at the inflation target in these circumstances may cause undesirable volatility in output'[152].

In his 2013 Budget Statement on the 20th March, however, Osborne (2013) announced three results of an internal Treasury review into the monetary policy framework. First, a 'new' remit for monetary policymaking was introduced. Second, the Bank of England was requested to provide an assessment of the merits of intermediate thresholds in monetary policymaking. Third, it was suggested to the MPC that they "may wish to issue explicit forward guidance" (Ibid). Subsequently, on the 7th August 2013, Mark Carney (2013), Governor of the Bank of England (2013-Present), wrote to the Chancellor of the Exchequer to announce the introduction of Forward Guidance to the framework for monetary policymaking.

[151] The price stability objective for monetary policy, which was embodied by in the 2% CPI inflation target for the MPC was affirmed in Osborne's (2011c:1,2,3; 2012c:1,2,3) *Remit for the MPC* letters at each Budget Statement and Bank of England (2010b:1;2010e:1;2010g:1;2011:1;2011b:1;2011d:1;2011f:1;2012:1; 2012b: 1;2012d:1;2012f:1;2013b:1) *Inflation Reports*.

[152] The symmetrical and flexible inflation target was affirmed by Osborne (2012c:2) in his *Remit for the MPC* letter published on the 21st March 2012.

Forward Guidance was explained by the Bank of England (2013a) in a document entitled *Monetary Policy Trade-Offs and Forward Guidance*, which established the future path for monetary policy through the pledge not to alter the present expansionary monetary policy stance until the unemployment rate fell below an intermediate threshold of 7%. When unemployment did fall below this intermediate threshold it would signal a re-evaluation of the economic situation and the formulation of monetary policy by the MPC. Furthermore, Carney (2013) explained in a letter to Osborne on the 7th August 2013 that Forward Guidance included three 'knockouts', which meant the intermediate threshold of the 7% unemployment rate would cease to operate in the formulation of monetary policy. First, was the price stability 'knockout', which related to the MPC's judgement that inflation would depart from target at the end of a two-year forecast period. Second, was the financial stability 'knockout', which would see a withdrawal of monetary policy stimulus if it posed a significant threat to financial stability. Third, was the expectations 'knockout', which arose if economic actors thought the MPC were willing to tolerate persistent departure of inflation from target in the future.

The introduction of a 'new' remit for the MPC and Forward Guidance would seem to herald a significant operational change to the remit for monetary policymaking conducted by the MPC. However, the orthodox cycle understands the introduction of Forward Guidance as an example of an operational change to the formulation of macroeconomic policy, which supported the implementation of orthodox macroeconomic policy instruments during the consolidation phase. Indeed, the 'new' remit and Forward Guidance should properly be understood as a clarification of the existing flexible inflation target introduced by Brown and the Treasury on the 12th June 1997.

In his *Remit for the MPC* letter published on the 20th March 2013, for example, Osborne (2013a:1) stated that the flexible inflation target meant that 'short-term trade-offs… [must] be made between inflation and output variability in setting monetary policy. It therefore allows for a balanced approach to the objectives set out in the remit, while retaining the primacy of price stability and the inflation target'. Thus, Osborne's (Ibid) letter established that the 'new' remit 'clarified the

government's expectation of the Committee in terms of the judgements it must make in setting and communicating policy in such exceptional circumstances'. Here, Osborne (2013a:2-3) explained that the new expectation of the MPC was in 'forming and communicating' its policy decisions so that it would 'promote an understanding of the trade-offs inherent in setting monetary policy to meet a forward-looking inflation target while giving due consideration to output volatility'. This included the requirement of the MPC to communicate more efficiently the four areas established under the symmetrical inflation target as well as the 'trade-offs that has been made with regard to inflation and output variability in determining the scale and duration of any expected deviation of inflation from target'[153]. Thus, in his *Remit for the MPC* letter published at the 2014 Budget on the 19th March, Osborne (2014a) argued that 'forward guidance has provided clarification about the factors affecting policy decisions, and reassurances that the recovery will not be threatened by a premature withdrawal of monetary stimulus'.

Similarly, Mark Carney also identified in his oral evidence to the Treasury Committee (2013:Ev.11,Q.66) hearing on his appointment as Governor of the Bank of England on the 7th February 2013 that Forward Guidance was an update to the existing flexible inflation target system. Here, Carney (Ibid) acknowledged that changes to the operational remit for monetary policymaking were "being discussed under a flexible inflation target regime, so it has to be consistent with that regime and ultimately bounded by the medium-term [inflation target] objective". Moreover, Carney told the Treasury Committee (2013:Ev.12,Q.71) that the "best framework remains flexible inflation targeting… Properly operated, properly understood… using the full power of that framework and the tools under that framework is going to be the best contribution, not just to price stability but to full employment in this country". Thus, Carney expressed to the Treasury Committee

[153] Carney (2013), Osborne (2013d) and the Treasury (2013a:4) affirmed that the 'new' remit required the MPC to provide more clarity in the trade-offs between returning inflation to target and output when faced with large and persistent economic shocks in an exchange of letters and the policy document entitled *Review of the Monetary Policy Framework*, which was published at the 2013 Budget.

(2013:Ev.10,Q.64,Ev.35-36) that “monetary policy guidance can be useful in providing additional information” and communicative stimulus to the UK economy.

In the context of the introduction of the ‘new’ remit and Forward Guidance the Bank of England defended its past conduct in policymaking in several policy documents. For example, the Bank of England (2013d:8) stated in their May 2013 *Inflation Report* that the MPC ‘has always recognised such short-run trade-offs. In particular, under its remit, the Committee has flexibility to temper the speed at which it seeks to return inflation to target in order to limit the volatility in output, subject to meeting the inflation target in the medium-term’. Similarly, in the Bank of England’s (2013a:5) *Monetary Policy Trade-Offs and Forward Guidance* document it was acknowledged that, since 2007, the MPC had ‘been faced with the need to balance the risk of achieving an insufficiently rapid restoration in activity against the risk that continued elevated inflation results in medium-term inflation expectations becoming less well anchored to the target’. Furthermore, the Bank of England (2013a:6) stated that the ‘MPC has in the past provided broad guidance on its reaction function via its inflation reports, the minutes of its monthly meetings, evidence to the Treasury Committee, and speeches by individual committee members’.

Consequently, Osborne admitted in oral evidence to the Treasury Committee (2013a:Ev.49,Q.359) on the 26th March 2013 that the ‘new’ remit “was catching up with the practise that the MPC had themselves developed”. This was also identified by the Treasury Committee (2013a;48) report on the 2013 Budget, which stated that ‘the changes to the monetary policy remit by the Government could be seen merely as formalising the MPC’s existing practice. If that is the case, there will be little change to how the MPC operates’. Thus, Chris Giles (2014), Economics Editor at the Financial Times, described the introduction of Forward Guidance as ‘dressing old policy in the governor’s new clothes’.

The requirement of the MPC to communicate the trade-off between output and returning inflation to target therefore did not lead to any changes in the objectives for monetary policy nor the operational remit of the MPC. For example, Osborne (2013) confirmed in his 2013 Budget Statement the “primacy of price

stability and the inflation target in Britain's monetary policy framework" would "apply at all times". Furthermore, the Treasury (2013a:4) *Review of the Monetary Policy Framework* stated that the 'new' remit and Forward Guidance was 'consistent with the Bank of England Act 1998, which sets the statutory objectives for the MPC to maintain price stability, and subject to that, to support the economic policy of the government'[154]. As a result, Osborne and the Bank of England regularly affirmed after the 2013 Budget, during the Cameron-Clegg and Cameron government, that the objectives for monetary policy remained the orthodox objective of price stability, which was embodied in the 2% CPI inflation target[155] that remained both symmetrical[156] and flexible[157].

The consolidation phase of the orthodox cycle consists of the implementation of orthodox policy instruments, which are used to create the economic conditions necessary to secure a later return to orthodox fiscal policy outcomes or the orthodox objective of price stability. Thus, the demonstration of continuity in the monetary policy framework is important for the two reasons identified in Chapter Eight. First, it ensured that the inflation target system continued to operate as a framework that guided the implementation of monetary policy instruments in pursuit of the objective of price stability. Second, the flexible nature of the inflation target system, strengthened under the 'new' remit and Forward Guidance, meant that the MPC and

[154] The Bank of England (2013a:5-8), Carney (2013:2;2013a:9) and Osborne (2013d:1-2) all affirmed that Forward Guidance was consistent with the existing operational remit for the MPC in policy documents and public speeches in August 2013.

[155] The affirmation of the price stability objective for monetary policy and the operational remit of an annual inflation target of 2% CPI for the MPC was evident during the remainder of the Cameron-Clegg and Cameron government in Bank of England (2013d:1;2013f:1;2013h:1;2014a;1,8;2014c:1;2014e;1;2014g:1;2015a:1; 2015c:1;2015e:1;2015g:1;2016b:1;2016f:1) *Inflation Reports* and Osborne's (2013a:1,3;2014a: 1,3;2015a:1,3;2015b:1,3;2016a:1,3) *Remit for the MPC Letters*.

[156] The inflation target was affirmed as flexible during the remainder of the Cameron-Clegg and Cameron government by Osborne's (2013a:4;2014a:4; 2015a:1,4;2015b:1,4;2016:1,4) *Remit for the MPC* letters and Carney's (2015:3;2015a:3;2015b:3; 2015c:3;2016:3;2016a:4) *open letters*.

[157] The inflation target was affirmed as flexible during the remainder of the Coalition government was indicated by Osborne's (2013a:1,3;2014a:3-4;2015a:3-4;2015b:3-4;2016:3-4) *Remit for the MPC* letters and Carney's (2015:3;2015a;3;2015b:3; 2015c:3; 2016:3;2016a:4) *open letters*.

Bank of England could maintain monetary policy stimulus to the UK economy, despite the oscillation of CPI inflation performance during the Cameron-Clegg and Cameron governments and its repeated departure from the symmetrical inflation target. For example, CPI inflation stayed above the 2% CPI inflation target from Q2 2010 to Q4 2013, which included above 3% CPI inflation until Q3 2012. Meanwhile, CPI inflation fell below the 2% CPI inflation target in Q1 2014 and fell below 1% CPI inflation from Q4 2014 to Q2 2016, which saw an average quarterly CPI inflation rate of just 0.25% CPI (ONS,2016b).

During both of these periods of departure of CPI inflation from target, the implementation of monetary policy stimulus was justified by the judgement that spare capacity and unemployment in the UK economy placed significant downward pressure on inflation[158]. For example, in his *open letter* published on the 12th February 2015, Carney (2015) communicated that because inflation was below target whilst the economy was operating with spare capacity and unemployment meant there was no 'immediate trade-off between returning inflation to target and supporting economic activity. In fact, to return inflation to the target it is necessary to eliminate the remaining degree of economic slack'[159]. Thus, even though unemployment fell below the 7% intermediate threshold in Q1 2014 to 6.8%, the MPC decided not to raise the Bank Rate (ONS,2016c). Consequently, the continued provision of monetary policy stimulus to the UK economy, designed to counter-act the downward pressure on inflation from spare capacity and unemployment and create the economic conditions required to return inflation to target and the orthodox

[158] King (2010a:2;2010c:2;2010e:1-2;2011:2;2011a:2;2011c:2;2011e:2;2012a:2) explained in his *open letters* that the rise of CPI inflation above target from Q2 2010 to Q3 2012 was 'temporary' and spare capacity in the UK economy placed significant downward pressure on prices and threatened to bring inflation significantly below target in the medium-term. When CPI inflation did fall significantly below inflation target after Q1 2014 then Carney's (2015:1-3;2015a:1-3;2015b:1-2;2015c:2; 2016:2;2016a:2) *open letters* and Bank of England (2014a:5,8-9;2014c:7-8,29;2014e: 8,16) *Inflation Reports* posited that spare capacity and unemployment subdued inflationary pressure in domestic costs such as wage.

[159] Carney (2015a:3-4;2015b:3;2015c:3;2016:3;2016a:5) repeated the claim that there was no tradeoff between returning inflation to target and the use of expansionary monetary policy stimulus to support economic growth and eliminate spare capacity in his *open letters* from the early 2015 onwards.

objective of price stability, meant monetary policymaking remained in the consolidation phase of the orthodox cycle.

One of the policy instruments implemented by the MPC to create the economic conditions necessary to secure a return to orthodox objective of price stability was the orthodox monetary policy instrument of the Bank Rate. Here, the MPC maintained the Bank Rate at the then historic low of 0.5% through the Cameron-Clegg and Cameron government (Bank of England,2016a). Consequently, the MPC continued to operate the Bank Rate according to the orthodox manner. This is affirmed when we consider the transmission mechanism of the Bank Rate as explained by McLeay (2014:2,4,5,7-8) and his fellow authors, all officials within the Bank of England Monetary Analysis Directorate. In their paper, it was explained that the Bank of England was the monopoly supplier of central bank money (banknotes and reserves), which is required by the banking system to meet withdrawals of money by their customers, settle Sterling transactions with other banks and meet liquidity regulations. Here, the Bank Rate sets the interest-rate paid on reserves held by commercial banks with the Bank of England. Therefore, the Bank Rate establishes the rate at which banks can obtain money from the Bank of England, which influences a range of short-term market interest-rates, particularly, the rate at which banks lend to one another in the wholesale funding markets. Thus, McLeay (2014:5) and his colleagues declared that a lower Bank Rate influences credit conditions in the economy through a reduction in loan rates, which increases 'how much household and companies want to borrow' and, in turn, the volume of lending, investment and consumption that contributed to the overall inflation rate in the economy[160].

The transmission mechanism of the Bank Rate, however, continued to be impaired as credit conditions in the UK economy, particularly for small and medium sized enterprises (SMEs), deteriorated after the formation of the Cameron-Clegg government on the 12th May 2010. For example, the Bank of England's (2016d:9) *Credit Conditions Review*, published before the resignation of David Cameron on the

[160] This transmission mechanism for the Bank Rate was also affirmed by the Bank of England (2013:3) in their 2013 'Red Book'.

13th July 2016, noted that the annual growth rate of lending to SMEs only entered positive territory for the first time since 2008 in July 2015. The orthodox cycle explains that orthodox monetary policy instruments during the consolidation phase can be assisted, for a time-limited basis, in creating the economic conditions necessary for the return of orthodox policy outcomes and objective by policy instruments that could be considered as 'unorthodox'. The Cameron-Clegg government implemented several such 'unorthodox' credit easing policies, the purpose of which were to support economic growth via the alleviation of deleterious credit conditions for households and businesses and the restoration of bank lending to businesses and households.

The first 'unorthodox' policy instrument implemented by the Coalition government (2011) was 'Project Merlin' on the 9th February 2011, which was an agreement between government and five major UK banks to commit £190billion of gross lending, £76billion of which would be lent to SMEs. Osborne (2011p) then announced, in his 2011 Autumn Statement of the 29th November, the introduction of two further credit easing policies in the £20billion National Loan Guarantee Scheme (NGLS) and a £21billion Funding for Lending Scheme (FLS), which were both implemented to lower the cost of bank loans and ease credit conditions in the UK economy. The NLGS launched on the 20th March 2012 and was delivered by the Debt Management Office at the Treasury. The NGLS offered government guarantee on unsecured borrowing by banks, enabling them to borrow funding in the wholesale markets at a cheaper rate and deliver low-cost bank loans to the UK economy. Meanwhile, the FLS was introduced on the 13th June 2012, extended in 2013, 2014 and 2015 and will remain in operation until January 2018. In similarity with the NGLS, the FLS provided government funding to banks and building societies for an extended period at below market rates in an attempt to encourage the banking system to ease credit conditions and supply more credit to households and businesses.

Monetary policymaking also saw the continuation of quantitative easing (QE) after the formation of the Cameron-Clegg government, which was still claimed by

some at the Bank of England as an ‘unconventional’ monetary policy[161]. Indeed, by November 2012, Osborne had authorised the Bank of England to increase the purchase of assets from the private sector from £200billion to £375billion. Chapter Eight argued that QE was an example of the orthodox monetary policy instrument of OMOs, which had been implemented to create the economic conditions, via an increase the money supply, that would allow the MPC to return inflation to target and the orthodox objective of price stability[162]. This chapter provides further evidence to support this analysis.

The argument that QE is an example of the orthodox monetary policy instrument of OMOs is further evidenced by the reply of “absolutely” by Mervyn King, Governor of the Bank of England (2003-2013) in oral evidence to the Treasury Committee (2011:Ev.6,Q.46) hearing on QE on the 25th October 2011, to the question of whether the Bank of England were purchasing gilts from the open market. Thus, in a speech on the 28th March 2012, David Miles (2012:5-6), Member of the MPC (2009-2015), stated that “QE is in some ways very similar to the Bank of England’s normal policy operation. The Bank of England, like most central banks, routinely buys and sells government debt in the secondary market as part of its normal operations – the only thing that distinguishes QE from these normal operations is its scale and the length of time for which the assets are likely to be held”. Consequently, the orthodox nature of QE is further evident after the formation of the Cameron-Clegg government because of the £375billion of asset purchases, £374.9billion had been of gilts (Bank of England,2016e:2).

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[161] QE was described as an ‘unconventional’ monetary policy by the Bank of England officials Bean (2010a22;2011:11;2013:2;2014:2) and Fisher (2010:2). Furthermore, QE was claimed as an ‘extraordinary’ monetary policy by King (2010d:3).

[162] That the purpose of QE was to bring about an increase in the money supply was affirmed by King (2010b:5;2010d:3;2011d:2;2012:2;2012b:1) in public speeches and his *Extension of Asset Purchase Facility* letters and by the Bank of England (2013:10-11) and Mcleay (2014:14) in policy documents. Furthermore, this aim for QE was affirmed by Osborne (2011c:2;2011o:1;2012a:1;2012b;1; 2012c:2;2012f:1;2013a:3;2014a:2) in his *Remit for the MPC* letters, *Extension of Asset Purchase Facility* letters and replies to the Governor of the Bank of England’s *open letters*.

Two respected economic commentators in UK national newspapers also noted that QE, rather than being an 'unconventional' monetary policy instrument, was in fact an OMO. For example, in an article in the Daily Telegraph on the 15th January 2012, Roger Bootle (2012) wrote that QE was not 'as esoteric as you might imagine. It is quite simply the policy of open market operations… and it is an extension of conventional monetary policy'. Similarly, in an article in the Financial Times, Samuel Britain (2013) highlighted that QE was an example of what 'old-fashioned textbooks' called 'open-market operations'. Here, Brittan (Ibid) added that 'it is a pity that the central banks decided to use the ugly term quantitative easing for what they are doing. If they had called them extended open-market operations, or something similar, they would have had less explaining to do'. Furthermore, the economist Ann Pettifor (2013:5) identified the historical genealogy of 'central bank monetary operations such as quantitative easing', which 'have been regular practice since the establishment of the Bank of England in 1694'.

Finally, the claim that QE is an orthodox monetary policy instrument is supported by operational changes to the Bank of England's Sterling Monetary Framework (SMF) after its introduction in March 2009. The operational change to the SMF was outlined in the Bank of England (2013:9-11) 'Red Book' of 2013 and saw the replacement of the 'voluntary reserve-averaging' system, which was discussed in Chapters Seven and Eight, with the 'floor' system in which reserve accounts held by banks and building societies at the Bank of England became 'effectively Sterling current accounts' that could be varied freely to meet liquidity needs. Furthermore, under the 'floor' system, all reserves were remunerated at Bank Rate by the Bank of England, rather than under the previous 'voluntary reserves-averaging', which had only seen the reserves that were at target at the end of a monthly maintenance period remunerated at Bank Rate. However, despite the operational change to the 'floor' system, the two purposes of the SMF remained to implement the MPC's decisions pertaining to the Bank Rate in order to meet the inflation target, which was achieved by the remuneration of reserve balances at Bank Rate as described earlier in the chapter, and the supply of liquidity to the banking system. Meanwhile, the Bank of England provided reserves and liquidity to the

banking system in the 'floor' system via QE because asset purchases were financed by the creation of Bank of England reserves; long-term repo OMOs, including the Discount Window Facility discussed in Chapter Eight, and the operational standing facilities[163]. Thus, the orthodox cycle can explain the introduction of the 'floor system' as an operational change to the formulation of monetary policy within the SMF, which supported the implementation of orthodox macroeconomic policy instruments.

The Orthodoxy Phase in Fiscal Policymaking from the 'Emergency' Budget on the 22nd July Onwards

The orthodox cycle explains that the orthodoxy phase in macroeconomic policymaking can be initiated by two factors. One of those factors is a significant event, which serves to institutionalise orthodoxy within the macroeconomic policymaking process even if economic performance has not returned to the orthodox objective of price stability or the orthodox fiscal policy outcome of the balanced budget and national debt reduction. The significant event that initiated an orthodoxy phase in fiscal policymaking after the formation of the Cameron-Clegg government was the 'Emergency' Budget of the 22nd June 2010. In his Budget Statement, Osborne (2010f) stated that "this budget is needed to deal with our country's debt. This budget gives confidence to our economy. This is the unavoidable budget". Similarly, the June 2010 Treasury (2010a:1) Budget Report argued that 'the most

[163] The 'floor' system in the SMF and the provision of reserves through QE, long-term repo OMOs and the operational standing facilities was affirmed by the Bank of England (2014:9-13;2015:9-13) in their 2014 and 2015 'Red Book'. Furthermore, the use of OMOs, primarily QE and Long-term Repo's, was affirmed in each Bank of England (2010d:86-91;2010f:160;2010h;246-249;2011a:8-11,12-13;2011c:88-91; 2011e;188-190,192-193;2011g:282-283,286-288;2012a:12-14;2012c:102-103,106-107;2012e:188-189,192-194;2012g:296-299;2013c:15-18;2013e:163-166;2013g: 264-267;2013i:389-391;2014b:84-87;2014d:213-215;2014f:326-328;2014h:389-391;2015b:82-83;2015d;194-196;2015f:304-306;2015h:378-380;2016c:59-61) *Quarterly Bulletin* during the Coalition and Conservative government.

urgent task facing this country is to implement an accelerated plan to reduce the deficit', which was 'unavoidable'.

The orthodox cycle also expounds that if monetary or fiscal policymaking reside in the orthodoxy phase without the other, which this chapter explains occurred in macroeconomic policymaking after the formation of the Cameron-Clegg government, then the orthodoxy phase will consist of a restoration of orthodoxy in that particular realm of policy. Consequently, the orthodox cycle can account for the restoration of orthodox fiscal policy from the 'Emergency' Budget of June 2010 onwards. For example, Osborne (2010f) told the House of Commons in his Budget Statement that the Cameron-Clegg government and Treasury would reduce Public Sector Net Borrowing from £149billion (10.1% GDP) in 2010-2011 to £20billion (1.1% GDP) in 2015-2016 and Public Sector Net Debt would peak at 70.3% GDP in 2013-2014 before falling thereafter to 67.4% GDP in 2015-2016. Moreover, Osborne (Ibid) announced in his 'Emergency' Budget Statement extra fiscal tightening amounted to £40billion above the plans announced by the Brown government. Here, the Office of Budget Responsibility (OBR) (2010:78) found that of the extra £40billion in fiscal consolidation announced at the 2010 'Emergency' Budget, £32billion would be implemented via cuts to public spending by 2014-2015. Furthermore, the Treasury (2010a:2) 'Emergency' Budget Report found that total consolidation in the public finances, including both that planned by the Brown and Cameron-Clegg government, amounted to £113billion by 2014-2015 and £128billion by 2015-2016.

The June 2010 'Emergency' Budget also explained that fiscal consolidation would be achieved by the implementation of orthodox fiscal policy instruments. For example, Osborne (2010f) explained in his Budget Statement that the bulk of deficit-reduction would come from lower spending rather than higher taxes, which would include average real cuts in Departmental Expenditure Limits (DEL) of 25% over the next four years. Meanwhile, the Treasury (2010a:2) Budget Report calculated that, by 2015-2016, £99billion of deficit-reductions would come from public spending reductions and £29billion from tax increases. Further orthodox fiscal policy instruments implemented in Osborne's (2010f) 'Emergency' Budget Statement in

June 2010 included immediate cuts in public spending amounting to £6.2billion and an increase of Value Added Tax from 17.5% to 20% effective from the 4th January 2011. Moreover, the Treasury (2010a:2) Budget Report identified the implementation of orthodox fiscal policy instruments including £11billion of welfare savings, a two year public sector pay freeze on incomes over £21,000 from 2011-2012 and the indexation of benefits, tax credit and public service pensions with CPI, rather than RPI, from April 2011.

There are four specific reasons why the 'Emergency' Budget of June 2010 should be considered a significant event in fiscal policymaking that initiated an orthodoxy phase. First, relates to the feverish political climate after the 'hung' result at the 2010 general election, the ensuing negotiations to form a coalition government and the changing position of the Liberal Democrats on fiscal policy. Indeed, the central factor that brought the Conservative and Liberal Democrats together in the Cameron-Clegg government was the desire to reduce the fiscal deficit (D'Ancona,2013:223;Young,2012:33). Consequently, deficit-reduction was at the heart of the preliminary Coalition government (2010:1) and the formal coalition government (2010a:7,15) agreement, published on the 12th May and 20th May 2010.

Whilst the 2010 general election manifesto of the Conservative party (2010:4-5) had made clear that a future Conservative government would seek to eliminate the structural deficit over a Parliament via the implementation of orthodox fiscal policy instruments policies, the Liberal Democrats position on deficit-reduction, as highlighted in Chapter Eight, was more similar to that established by the Brown government. However, during the negotiations that took place after the 'hung' election result on the 6th May 2010, there was an 'alacrity' with which the Conservative and Liberal Democrat negotiators 'agreed on the pressing matter of fiscal policy' (Ganesh,2012:299). Thus, in a speech on the 18th May 2011, Clegg (2011a) asserted that the Liberal Democrats "didn't just sign up to the [deficit-reduction] plan – we co-wrote it, we believe in it, and we take responsibility for seeing it through… sound public finances are the key to macroeconomic stability… balancing the books now is the only way to avoid subjecting our children to years of high debt, higher interest rates, fewer jobs".

David Laws, who was part of the Liberal Democrat coalition negotiation team and served as Chief Economic Secretary at the Treasury for just seventeen days in May 2010 until an expenses scandal forced his resignation, identified three reasons why the Liberal Democrats changed their position on deficit-reduction prior to the 2010 general election and during the coalition negotiations. First, was the prospect of a 'hung' parliament, which Laws (2010:68,108-111.113) claimed made the Liberal Democrats 'increasingly concerned that the financial markets would react badly if a strong government could not be established, which had the votes and market credibility to deal with the deficit' and that a future coalition government would 'almost certainly need to take credible, early, action of some kind, to reduce the future scale of the deficit'. Second, was the potential adverse reaction from the financial markets, which Laws (2010:43,82-83,93) highlights meant the Liberal Democrats 'main intention [during coalition negotiations] was to send out the clearest possible signal that we would support tough action to steady the financial markets. A financial market panic would not just be disastrous for the country, but would be the worst possible backdrop against which to make difficult decisions' and precluded the formation of a 'traffic light' coalition with Labour, Scottish National party, Plaid Cymru and Green party. The third reason was the increasingly perilous economic situation in Greece, which Laws (2010:43,109) declared 'certainly began to influence our thinking in the final couple of weeks before the general election' and was key to the Liberal Democrat adoption of the Conservative position on deficit-reduction because it 'showed what could happen when market lose confidence in a government ability to control its deficit and service its debt'. Thus, Laws (2010:111) claimed that whilst the Liberal Democrats knew they 'could negotiate with the Conservatives, and that if we wanted to we could probably succeed in watering down the £6billion in various ways… we thought that the signaling of these limited cuts was important'[164].

[164] These reasons behind the Liberal Democrat conversion to the Conservative position on deficit-reduction prior the 2010 general election and during the coalition negotiations has been affirmed by accounts of the coalition negotiations by Boulton and Jones (2010:136,143,151,152,167, 180-182), Ganesh (2012:298) and Wilson (2010:182-183).

The second reason why the 'Emergency' Budget of June 2010 should be considered a significant event in fiscal policymaking that initiated an orthodoxy phase is the considerable institutional support for deficit-reduction and restoration of orthodox fiscal policy within the Treasury and Bank of England. For example, according to Seldon and Lodge (2011:97) whose work included anonymous interviews with Treasury officials, the Treasury began to reconnect in 2008 with notions of 'sound finance' and increasingly took the view that deficit-reduction needed to be clearly demonstrated in the future strategy for fiscal policymaking and became skeptical about the efficacy of fiscal policy as an instrument of Keynesian demand management. Specifically, Seldon and Lodge (2011:252-253) identified Nicholas MacPherson, Permanent Secretary at the Treasury (2005-2016), and Tom Scholar, Second Permanent Secretary at the Treasury (2009-2013), as having lost faith in Keynes as the Treasury came to believe that Gordon Brown was 'dangerously influenced by a misguided reading of Keynes' and was 'wedded to an out-of-date economic orthodoxy which said salvation would come from still further stimulus'. Here, Seldon and Lodge (2011:198,363) claim that the Treasury were concerned that the size of the fiscal deficit would cause an adverse reaction against UK government debt in bond markets and that the Treasury were successful in halting the implementation of further discretionary fiscal policy in the 2009 November Pre-Budget, which, if correct, would make the Treasury key initiators of the consolidation phase in fiscal policymaking located in the previous chapter.

Consequently, in a speech on the 16th January 2013, MacPherson (2013) stated that the Treasury's core purpose in macroeconomic policymaking remained public spending control and that 'Gladstone's economic principles of sound money and free trade have endured in the Treasury for one hundred and fifty years… at a time of austerity Gladstone's focus on candle-ends lives on". Indeed, in a speech on the 17th January 2014, MacPherson (2014) articulated a 'Treasury view for our time', which, despite his protestation that 'Treasury orthodoxy has come a long way since the Treasury view of the 1920s', shared many similarities with the orthodox macroeconomic policy identified in this thesis. For example, MacPherson (Ibid) claimed the modern day 'Treasury view' consisted of a belief that economic

'prosperity rests on free-trade'; that 'markets work' and create efficient allocation of product, capital and labour; that the provision of 'sound money' is an 'abiding Treasury obsession' and 'the provision of price stability is 'tantamount to a moral issue'; that fiscal policy should not be used as a policy instrument to manage demand; the role of fiscal policy in macroeconomic stabilisation should be limited to the operation of the automatic stabilisers and fiscal policy should provide support to monetary policy 'from a position of strength, when public debt is low or non-existent'; that governments find it difficult to raise taxation revenue beyond a certain point regardless of the mixture and levels of tax; that spending control is the central purpose of the Treasury; that supply-side policy is another long-standing Treasury obsession', which should focus on producing entrepreneurship in flexible and competitive markets. Here, MacPherson (Ibid) claimed the Treasury's focus on supply-side policy was not surprising 'if you take the classical economist's view that in the long run the nation's income is determined by the supply of labour and capital and the productivity of each'.

The most consistent supporter of deficit-reduction within the Bank of England was Mervyn King, who had made his policy preference for deficit-reduction in the public finance clear both prior to and after the 2010 general election[165]. For example, in his *Mansion House* speech on the 17th June 2009, King (2009c:5) stated that it was "necessary to produce a clear plan to show how prospective deficits will be reduced during the next Parliament" and "so returning to a gradually declining path for the ratio of national debt to national income". Importantly, in a press conference on the 12th May 2010, the day that the Cameron-Clegg government was officially formed, King asserted that "the most important thing now is for the new government to deal with the challenge of the fiscal deficit. It is the single most pressing problem facing the United Kingdom… it is very important that measures are taken straight away to demonstrate the seriousness and the credibility of the

[165] King (2009a:5;2009b:2;2011b:2,3) made clear his belief that deficit-reduction was necessary in several public speeches and in oral evidence to the Treasury Select Committee (2010:Ev.2,3,5,6) on the 23rd February 2010. Furthermore, Bank of England officials and MPC members such as Bean (2010a:41;2012:6;), McCafferty (2013:3;2013a:2), Sentence (2010:9) and Weale (2011:14) also expressed their support for deficit-reduction.

commitment to dealing with the deficit… it doesn't make sense to run the risk of an adverse market reaction" (Bank of England,2010c:3-5). Therefore, in his unauthorised biography of George Osborne, Ganesh (2012:300,309) claims that it was a 'widely known view of the Treasury and Bank of England that in-year cuts [in 2010] were necessary to keep the markets at bay' and that the 'Treasury saw this as an historic opportunity to turn the public finances around'.

The Treasury's and Bank of England's support for deficit-reduction was also evident during the coalition negotiations between the Conservative and Liberal Democrats. For instance, Laws (2010:95,110,113) and Boulton and Jones (2010:178-180) highlight that Gus O'Donnell, Cabinet Secretary and Head of the Civil Service (2005-2011), sought to 'steer' the negotiation meetings between the Conservative and Liberal Democrats with interjections on the uncertainty in financial markets and economic situation in Greece. Furthermore, O'Donnell offered to provide a 'brief' to the negotiators on the 'dire' economic situation, which was rejected by the Conservative and Liberal Democrats negotiating teams; the 'brief' would have been provided by Mervyn King and Nicholas Macpherson.

The third reason the 'Emergency' Budget of June 2010 should be considered a significant event in fiscal policy is the scale of fiscal consolidation it introduced, even though the fiscal targets announced in the 'Emergency' Budget of June 2010 were subsequently missed, served to provide a forceful communication of the restoration to the UK electorate and institutionalised orthodox fiscal policy in the policymaking process. For example, the Institute of Fiscal Studies (IFS) (2010b:2) stated in their post-Budget press conference on the 23rd June 2010 that 'we are looking at the longest, deepest sustained period of cuts to public services spending at least since World War II". The fourth reason is that the 'Emergency' Budget was implemented in a fervent academic debate pertaining to the relative merits of 'stimulus vs austerity' fiscal policy strategies, which started in 2008 and continued unabated throughout the Cameron-Clegg and Cameron government. For example, prior to the 2010 general election, economists had engaged in this debate via the letters pages of UK national newspapers. This began on the 14th February 2010 with a letter (2010) sent by twenty economists to the Sunday Times, which argued that

deficit-reduction should begin in 2010-2011, the majority arising from the implementation of cuts to government spending. This drew a response in two separate letters (2010a;2010b) by sixty and nine economists respectively, published by the Financial Times on the 18th February 2010, which claimed that the implementation of deficit-reduction in 2010-2011 would stall the nascent economic recovery.

The 'Emergency' Budget of June 2010 also saw the introduction of two new fiscal rules, which the orthodox cycle can account for as an operational change to fiscal policymaking that supported the implementation of orthodox fiscal policy instruments. The fiscal rules introduced by Osborne (2010f) in his 'Emergency' Budget Statement included a target for balance in the cyclically-adjusted Current Budget by the end of a rolling five-year forecast period and a supplementary debt rule that would see Public Sector Net Debt falling as a percentage of GDP by 2015-2016. However, Osborne (Ibid) announced in his 2010 Budget Statement that the target for balance in the cyclically-adjusted Current Budget would be achieved one year early in 2014-2015 when the Current Budget was forecast to be in surplus of 0.3% GDP. Consequently, Osborne (Ibid) exclaimed that his fiscal rules "set the course" for a "balanced budget and falling national debt by the end of this Parliament". The formation of the Cameron-Clegg government also saw the creation of the OBR, which Osborne (2010) asserted in a speech on the 17th May 2010 would provide a "truly independent audit of the public finances" and establish credibility in fiscal policymaking and the public finances[166]. The OBR was underpinned in statutory legislation in the 2011 OBR Act, which established the main duty of the institution to examine and report on the sustainability of the public finances and to provide judgement on whether the government's fiscal policy is consistent with a better than 50% chance of meeting its fiscal rules.

The fiscal rules were then supplemented by a further operational change to fiscal policymaking at the 2014 Budget with the introduction of a 'welfare cap',

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[166] For example, Alexander (2012b), Greening (2011:c.749;2011a:c.1308) and the Treasury (2010b15;2013:27) claimed that the OBR enhanced the credibility of fiscal policymaking and the public finances in public speeches and policy documents.

which established a ceiling, set by the Treasury over a rolling five-year forecast period, to contain expenditure on welfare (HM Treasury,2014a:7). Some sections of welfare spending, such as jobseekers allowance, were excluded from the 'welfare cap' to allow the automatic stabilisers to operate. The 'welfare cap' was the first of subsequent amendments to the formulation of fiscal policymaking, which the orthodox cycle can explain as operational changes that supported the implementation of orthodox fiscal policy. For instance, the fiscal rules were changed again at the 2014 Autumn Statement as the target for balance in the cyclically-adjusted Current Budget was brought forward to the end of a rolling three-year forecast.

Osborne subsequently replaced his target for balance in the cyclically-adjusted Current Budget at the 'summer' Budget of the 8th July 2015, after the election of the Cameron government at the 2015 general election, with a new target for 'absolute surplus' in the public finances. The 'absolute surplus' target aimed for a surplus in Public Sector Net Borrowing in 'normal times' and each subsequent year thereafter by 2019-2020, which would return the public finances to orthodoxy. The 'absolute surplus' target would apply in all circumstances except when economic growth fell below 1% in the most recent four-quarter period, was currently below 1% or was forecast to fall below 1%, which was judged to be indicative of a significant negative shock to the UK economy (HM Treausry,2015b:7).

Osborne and the Treasury attempted to meet these fiscal rules and targets via the implementation of orthodox fiscal policy instruments of public expenditure cuts, public spending restraint and tax increases. On top of the orthodox policies of fiscal consolidation announced in the 'Emergency' Budget of June 2010, sources of deficit-reduction included cuts to welfare spending and welfare reform, which included the politically controversial decision in the 2010 Spending Review (SR) to remove child benefit from households paying the top rate of tax and the introduction of the aforementioned 'welfare cap' (HM Treasury,2010b:16,28;2011:6;2012a:6,8;2013b:8;2013c:33-35); extra cuts to DEL (HM Treausry,2012a:6;2013:5-6;2013b:5;2013c:26); underspending by government departments (HM Treasury,2013:24;2013c:28;2014:2; 2015:19); 'efficiency' savings in public spending (HM Treasury,2013b:8;2014b:7); reform to public sector pay and pensions,

such as the aforementioned pay freeze for public service employees (HM Treasury,2010b:16,37;2011:6;2013:3) and measures to limit tax avoidance and evasion (HM Treasury,2010b:30;2013:5). Thus, in the 2015 Budget Report, the Treasury (2015:19) confirmed that the Cameron-Clegg government had implemented £83billion worth of discretionary reductions in public expenditure throughout the 2010-2015 Parliament and £106billion of £121billion of total discretionary consolidation planned in the public finances would be implemented by 2015-2016. The IFS (2015:1) *Green Budget* of 2015 forecast that the ratio of public spending cuts to tax rises in the fiscal consolidation in the public finances implemented between 2010-2011 and 2015-2016 stood at 82:18.

The implementation of orthodox fiscal policy instruments is evident in Table Three, which presents data from the public finances under both the Coalition and Conservative government of David Cameron. For example, Table One shows the discretionary reductions in public expenditure implemented during the Cameron-Clegg government during the 2010-2015 parliament ensured restraint in TME in 2015/2016 prices, which secured a tightening of 4.8% GDP. Similarly, Table One highlights that restraint in Public Sector Current Expenditure produced a tightening of 3.9% GDP. Meanwhile, Public Sector Net Investment decreased steadily by 0.9% GDP by 2015-2016 bringing it in line with its 2004-2005 to 2006-2007 level (OBR,2016b). Finally, Public Sector Current Receipts and National Account Taxes fell after 2011-2012, the consequence of persistent economic dislocation in domestic, regional and global markets that impacted upon economic activity and the low level of deficit-reduction implemented through tax increases. This trend was excacerbated by reductions in direct taxes, such as lowering the top rate of tax from 50% to 45% in the 2012 Budget and successive reductions from the 2010 'Emergency' Budget onwards in corporation tax from 28% to 20% in March 2016.

Table One: Public Expenditure and Taxation during the Cameron-Clegg Government and Cameron Government, 2010-2016

Year	Total Managed Expenditure (% of GDP)	Total Managed Expenditure (2015/16 Prices) *(£billions)*	Public Sector Current Expenditure (% of GDP)	Public Sector Current Expenditure (2015/16 Prices) *(£billions)*	Public Sector Net Investment (% of GDP)	Public Sector Current Receipts (% of GDP)	National Account Taxes (% of GDP)
2010-2011	44.9%	£763.7	40%	£681.8	2.7%	36.3%	33.7%
2011-2012	43.8%	£754.3	39.5%	£681.4	2.1%	36.7%	34%
2012-2013	43.2%	£755.0	38.8%	£677.8	2.3%	36%	33.2%
2013-2014	41.8%	£747.9	37.9%	£677.2	1.8%	35.9%	33.1%
2014-2015	40.7%	£747.3	36.7%	£674	1.9%	35.7%	32.9%
2015-2016	40.1%	£753.0	36.1%	£679.5	1.8%	36.1%	33.4%

Source: (OBR,2016b).

Table Two demonstrates, however, that Osborne and the Treasury failed to meet the supplementary debt rule with Public Sector Net Debt continuing to rise throughout the Cameron-Clegg and Cameron government. Whilst the target for balance in the cyclically-adjusted Current Budget at the end of a 'rolling' five-year, and latterly three-year, forecast period makes it difficult to say that the target was 'missed'. What Table Two does illustrate is that the cyclically-adjusted Current Budget was still not in balance when Osborne superseded the rule with the aim for an 'absolute surplus' in the public finances. Indeed, on the OBR's (2016b) most recent fiscal forecasts, the cyclically-adjusted Current Budget was not projected to return to surplus until 2018-2019.

Osborne (2015e) also announced in his 2015 Autumn Statement on the 1st November that welfare spending would exceed the 'welfare cap' in the 2015-2020 Parliament. Then, in the context of the leave vote in the European Referendum held in the UK on the 23rd June 2016, Osborne announced in a speech to the Manchester Chamber of Commerce on the 1st July 2016 that he would abandon the target for an 'absolute surplus' in the UK public finances claiming that "we must provide fiscal credibility, continuing to be tough on the deficit while being realistic about achieving a surplus by the end of the decade" (BBC News,2016). Thus, by the end of Osborne's Chancellorship, none of his fiscal target remained in operation. Whilst Osborne and the Treasury may have missed all of their fiscal targets, Table Two demonstrates the significant level of consolidation in the public finances implemented by the Cameron-Clegg government, which is evident in the columns for Public Sector Net Borrowing, the Current Budget and Primary Balance. For example, the Cameron-Clegg and Cameron government implemented fiscal tightening worth 4.6% GDP in Public Sector Net Borrowing, 3.7% GDP in the Current Budget and 3.9% in the Primary Balance.

Table Two: Government Borrowing and National Debt during the Cameron-Clegg and Cameron Government, 2010-2016

Years	**Public Sector Net Borrowing** (% of GDP) *(+ = Deficit)*	**Cyclically-Adjusted Net Borrowing** (% of GDP) *(+ = Deficit)*	**Current Budget Deficit** (% of GDP) *(+ = Deficit)*	**Cyclically-Adjusted Current Budget Deficit** (% of GDP) *(+ = Deficit)*	**Primary Balance** (% of GDP) *(- = Deficit*	**Cyclically-Adjusted Primary Balance** (% of GDP) *(- = Deficit)*	**Public Sector Net Debt** (% of GDP)
2010-2011	+8.6%	+6.6%	+5.9%	+3.8%	-6.3%	-4.3%	71.2%
2011-2012	+7.1%	+5.2%	+5.0%	+3.1%	-4.7%	-2.8%	74.9%
2012-2013	+7.3%	+5.3%	+5.0%	+3.0%	-5.3%	-3.3%	78.5%
2013-2014	+5.9%	+4.3%	+4.1%	+2.5%	-4.0%	-2.4%	80.9%
2014-2015	+5%	+4.2%	+3.1%	+2.4%	-3.3%	-2.6%	83.2%
2015-2016	+4%	+3.7%	+2.2%	+1.9%	-2.4%	-2.1%	83.7%

Source: (OBR,2016b).

The orthodoxy phase of the orthodox cycle will also see the deployment of a policy narrative that seeks to legitimise the return to orthodox macroeconomic policy. Here, the Cameron-Clegg and Cameron government maintained the narrative that had been originally deployed by the Conservative party whilst in opposition, which sought to legitimise the implementation of orthodox fiscal policy as the policy solution to a

‘debt crisis’ caused by the overspending of previous Labour governments[167]. For example, in his speech on the 28th May 2010, Cameron (2010) argued that “as a country we have become indebted on an unprecedented scale. Our huge deficit and rapidly growing public debt are the clearest manifestations of our economic mistakes”. In more explicit terms, Cameron (2011b) told the Conservative Party conference on the 5th October 2011 that “we’re in a debt crisis. It was caused by too much borrowing, by individuals, businesses, banks, and most of all, governments… the only way out of a debt crisis is to deal with your debts. That’s why households are paying down their credit and store card bills. It means banks getting their books in order. And it means governments – all over the world – cutting spending and living within their means”. The ‘debt crisis’ narrative was also deployed by Liberal Democrats within the Cameron-Clegg government. For instance, in his speech to the Liberal Democrat Autumn Conference on the 20th September, Clegg (2010a) argued that “we are gripped by a crisis, and it’s the worst kind: it’s invisible. You can’t see the debts mounting up” to which the only solution was “balancing the budget. I did not come into politics to make spending cuts. But it is the only choice if we want to steer Britain out of the economic mess Labour made”[168].

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[167] A number of scholars have identified that the Cameron-Clegg government deployed a ‘debt crisis’ narrative to legitimise the implementation of ‘austerity’. For example, see Afoko and Vockins (2013), Crines (2013), D’Ancona (2013:225), Hay (2011:24), Kavanagh and Cowley (2010:83), McCarron and Purcell (2013:3), O’Hara (2014:1), Schmidt and Thatcher (2013) and Stanley (2014:9,17).

[168] The ‘debt crisis’ narrative, which sought to legitimise the implementation of deficit-reduction and orthodox fiscal policy instruments as the solution to the overspending of previous Labour governments and avoidance of a sovereign debt crisis, was deployed consistently during the Cameron-Clegg and Cameron governments in public speeches by figures such as Cable (2010:2011b:cc.330-331), Cameron (2010a:2011c:c.327;2012a; 2013a:2013d), Clegg (2010;2012), Hague (2010;2012), Hoban (2010:2012:c.746) and Osborne (2010b;2010c:2010d:2010e; 2010f;2010g;2010h:2011d;2011g;2011i;2011k; 2011l;2011m;2012;2012e;2013e; 2013f;2015d).

Continuity of Orthodox Economic Ideas during the Cameron-Clegg Government and Cameron Government

The orthodox cycle explains that the resurgence of orthodox economic ideas in the formulation of policy will lead to the implementation of orthodox policy instruments during the consolidation phase. Furthermore, the orthodox cycle expounds that the restoration of orthodox macroeconomic policy during orthodoxy phase, in circumstances when monetary or fiscal policymaking enter this phase of the cycle without the other, will include evidence of orthodox economic ideas in the formulation of policy in that particular realm of policymaking. Consequently, the orthodox cycle can account for the continuity of orthodox economic ideas in macroeconomic policymaking after the 12th May 2010. For example, the formulation of macroeconomic policy saw the return of the orthodox economic idea of globalisation, which was constructed in public speeches and policy documents in the same manner as it had been after the election of the Blair government on the 1st May 1997.

The first element in the construction of the economic idea of globalisation during the Cameron-Clegg and Cameron government was the portrayal of the UK economy as an integrated part of the global economy. For example, in his speech on the 28th May 2010, Cameron (2010) argued that "in the modern, global economy, our fortunes are intertwined with the fortunes of others". Furthermore, Cameron (2013b) claimed in his speech on the 10th June 2013 that the UK's economic interests, cultural ties, history, businesses, location and instincts had created an "open, trading nation" who "depends for its living on international ties and global trade". The second element in the construction of globalisation, closely related to the first, is that UK economic prosperity would be secured not by rejecting globalisation but by deepening the interconnection of the global and domestic economy. For instance, in his speech on the 17th May 2012, Cameron (2012a) asserted that the global economy was creating a "world that is ever more connected and ever more competitive", which leads to "new countries demanding our products, fuelling new jobs at home. If

we make the most of this, there is a huge opportunity to secure a great fortune for our country". Thus, Osborne (2011e) used a statement to the International Monetary and Finance Committee at the International Monetary Fund on the 16th April 2011 to "urge countries to design policies that support globalisation and… highlight the risks of trade restrictions in response to supply shocks". Finally, such an interpretation of globalisation was also expressed by other members of the Cameron-Clegg government such as William Hague (2011a), Secretary of State for Foreign Affairs and the Commonwealth (2010-2015), who stated in a speech on the 21st November 2011 that "our future prosperity requires us to look further afield and to seize the many opportunities that the global economy presents for an outward-looking and highly-developed economy like our own".

The third element in the construction of the orthodox economic idea of globalisation under the Cameron-Clegg and Cameron government was that the mobility of capital, factors of production and trade in goods and services in the global economy was causing rapid economic change. For example, in their 2012 Autumn Statement Report, the Treasury (2012a:7) stated that 'the UK economy is facing rapid global change. The growth of emerging economies, such as China, India and Brazil is creating new challenges for the UK, but also new opportunities'. Moreover, Cameron (2013d) told the Conservative party conference on the 2nd October 2013 that "all these global companies that employ lots of people – they can set up anywhere in the world… and these companies base their decisions on some simple things like the tax rates in each country". The fourth element in the construction of the orthodox economic idea of globalisation posits that role of macroeconomic policy in the global economy was the achievement of economic stability. For instance, the Treasury (2014b:7) Autumn Statement Report in 2014 noted that the persistent existence of the 'structural deficit confirms the government's view that the UK is not immune from the problems being experienced in the Eurozone and other parts of the global economy'.

The fourth element in the construction of globalisation, however, is most evident in the impact of the orthodox economic idea of globalisation had on the formulation of fiscal policy in the Cameron-Clegg and Conservative governments,

which accentuated the importance of confidence and credibility in policymaking. Thus, deficit-reduction via the implementation of orthodox fiscal policy instruments was deemed necessary to regain confidence and credibility in global financial markets, which in turn would secure economic stability[169]. For example, in his speech on the 17th May 2010, Osborne (2010) posited that an 'Emergency' Budget and £6.2billion of reductions of spending cuts was necessary to demonstrate the "determination to act quickly in the short-term in order to establish credibility for the longer term" and was necessary to "restore confidence in our economy". According to Osborne (Ibid), this would avoid an adverse reaction against UK government debt by investors in global financial markets that could spark a 'sovereign debt crisis' and higher market interest-rates in the UK economy. Osborne (2010h) echoed this theme in his 4th October 2010 Conservative party conference speech that "we secured for our nation a breathing space in the face of a European debt crisis by immediate reductions to this year's spending programmes… within fifty days we had restored confidence at home and abroad in Britain's ability to pay its way in the world with a bold emergency budget…. there is no panic, no daily dread of the bond market, no paralysing fear that our credit rating could be lost, no immediate danger of a deathly spiral of higher interest rates… our victory is the absence of war". Subsequently, it was repeatedly claimed that deficit-reduction in the UK public finances had achieved

[169] The importance of confidence and credibility in policymaking was repeatedly affirmed by key members of the Cameron-Clegg government, such as Alexander (2011:c.68;2011a;2011b:c.151;2011e:2012:c.702;2012b;2012e), Cable (2011:c.1146; 2011a: 2011b:c.331), Cameron (2012c;2013a), Clegg (2011;2011a), Hague (2011) and Osborne (2010a:2; 2010i;2011j: 2) and junior ministers at the Treasury such as Greening (2011a) and Javid (2013). Here, deficit-reduction was identified as necessary to restore confidence and credibility in fiscal policymaking, which would secure economic stability and avert a 'sovereign debt crisis' and associated rising market interest-rates in the UK economy. This relationship between deficit-reduction, credibility and economic stability was also affirmed by the Treasury (2010a:11) and MacPherson (2011) in a public speech. Finally, it was affirmed by Dave Ramsden, Chief Economic Advisor at the Treasury (2010-Present), in an interview with *Civil Service Quarterly* (Lambert,2013).

economic stability and allowed the UK economy to become a 'safe haven' for global investment[170].

In an article in the *European Journal of Economic Thought*, Bridel (2014) highlighted what he considered the unexpected return of the 1929 'Treasury view' to the debate between academic economists in the period 2008-2009. Equating the 1929 'Treasury view' with the economic idea of crowding-out, Bridel (2014:9) claims that 'the (un-)expected return of a simplified version of the Treasury View has (fortunately) nothing to do with decision-making processes in economic policy… [and] is purely an academic dispute linked to modelling preferences'. However, Bridel is wrong, or, at least, he is wrong in the context of macroeconomic policymaking after the formation of the Cameron-Clegg government on the 12th May 2010 (Lee,2011:66), which saw the return of the orthodox economic idea in both of its conceptions: financial and psychological in the formulation of macroeconomic policy

The financial conception of the orthodox economic idea of crowding-out continued to be interpreted and constructed in the same manner as it had during the Twentieth century and in the 1997-2001 Parliament by the Blair government. Thus, it was explained in public speeches and policy documents that government borrowing led to an increase in market interest-rates, which crowds-out private sector investment and consumption from the market[171]. Indeed, Osborne (2010b) stated in a speech on the 19th May 2010, a week after the formation of the Cameron-Clegg government, that "at the heart of the [coalition] agreement… is a firm commitment to

[170] The claim that deficit-reduction had restored economic stability and allowed the UK economy to become a 'safe haven' for global investors was made by Alexander (2012a:2012b), Hague (2012), Hoban (2012:c.746), Osborne (2011i;2011k; 2012d:2012j) and the Treasury (2011:5;2012:1,12,21;2012a:11,2013:9).

[171] The financial conception of the orthodox economic idea of crowding-out was articulated by important members of the Cameron- Clegg government such as Alexander (2010:c.194-195,200;2010a:cc.778-779;2010b:c.780;2011d:c.163;2012e), Cable (2011a), Cameron (2010a;2010b;2011;2012:c.740;2012a;2013a;2013e), Clegg (2011;2011a) and Osborne (2010g;2010j:2011:2011n;2011p;2012j:c.874) and junior ministers at the Treasury such as Guake (2010), Hoban (2010a:c.786-787), Javid (2013:c.237W) and Smith (2012;c.679).

tackle Britain's debt and create the space for a private sector recovery", which was necessary because "over the past decade, over half of all jobs created were associated in some way with public spending". Thus, in his 2010 'Emergency' Budget Statement on the 22nd June, Osborne (2010f) exclaimed that it was the Cameron-Clegg governments intention to create "an economy where the state does not take almost half of all our national incomes, crowding out private endeavour" and that the implementation of £6.2billion of cuts to public spending represented "urgent action to keep our interest rates lower for longer. To boost confidence in the economy and protect jobs. To show the world that we can live within our means".

The interpretation and construction of the financial version of the orthodox economic idea of crowding-out was vividly evident in the rejection of the Cameron-Clegg government of calls for a 'Plan B', which would have involved increasing government borrowing to fund infrastructure projects to boost economic growth and employment. For example, in a Statement to the House of Commons on the global economy on the 11th August 2011, Osborne (2011i) declared that the Cameron-Clegg government had "an unwavering commitment to fiscal responsibility and deficit reduction" because "more spending now, paid for by more government borrowing and higher debt, would lead directly to rising interest rates and falling international confidence that would kill off the recovery not support it". Similarly, Osborne (2011k) claimed in a speech on that 6th September 2011 that "abandoning the plan we have set out would put Britain back into the firing line, lead to soaring interest rates and cripple any hope of a sustainable recovery".

The psychological version of the orthodox economic idea of crowding-out was also interpreted as it had been during the Twentieth century. Thus, it was articulated in public speeches that a loss of confidence in domestic and global markets would result in rising market interest-rates, which would crowd-out private sector investment and consumption in the UK economy[172]. Indeed, this construction of the psychological version of crowding-out was evident in the 2010 Conservative

[172] The psychological version of the orthodox economic idea of crowding-out was expressed by important members of the Cameron-Clegg government such as Cameron (2010a;2010c;2011;2011b;2013a), Hague (2010) and Osborne (2011k:2012h:c.127).

party (2010:7) general election manifesto, which stated that 'the absence of a credible plan to deal with our record budget deficit, the largest of any major economy, is creating uncertainty over Britain's credit rating and interest rates… this instability undermines confidence and jeopardises investment. It could tip Britain back into recession'. Consequently, in a speech on the 17th August 2010, Osborne (2010g) argued that "the actions we took in the Budget [of June 2010] have removed the biggest downside risk to the recovery in a loss of confidence and a sharp rise in market interest rates… economic stability now depends on a credible plan to restore the public finances to a sustainable path. To fail to do that would mean higher market interest rates and higher debt interest payments". Similarly, in a speech on the 27th January 2012, Osborne (2012) claimed that a loss of fiscal credibility would lead to higher market interest rates that, in turn, would "make recovery all but impossible".

The financial and psychological version of the orthodox economic idea of crowding-out, however, was not solely expressed by Cameron and Osborne, but also was articulated by Liberal Democrats within the coalition government, the Treasury and Mervyn King at the Bank of England. For example, Danny Alexander (2011f), Chief Secretary at the Treasury (2010-2015), posited in a speech on the 24th October 2011 that "large and growing deficits merely lead to higher inflation, higher taxes and higher interest rates". Furthermore, in a speech on the 20th April 2012, Alexander (2012a) claimed that deficit-reduction was responsible for "record low market interest rates to the benefit of businesses and households". Similarily, the Treasury (2010a:9) Budget Report of June 2010 contended that the deficit-reduction plan 'should provide businesses with confidence they need to plan and invest, supporting the necessary recovery in business investment' and 'provide the conditions for sustainable growth in the private sector'. This would occur, according to the Treasury (2010a:11), because deficit-reduction 'will underpin private sector confidence and reduce competition for funds for private sector investment' and 'failure to address rising Public Sector Net Debt in the UK risks pushing up long-term interest-rates, which would affect not just the government, but also families and businesses through higher costs of loans and mortgages'. Crowding-out was also articulated by the Treasury (2012:13;2013c:38) in their 2012 Budget Report, which

posited that 'lower government spending will release resources from the public sector for use by the private sector', and in their 2013 Autumn Statement Report, which claimed that 'high levels of debt damage growth through a number of channels, including by increasing levels of taxation, by crowding-out private investment and by increasing uncertainty'. Finally, King (2010b), in his *Mansion House* speech on the 16th June 2010, posited that deficit-reduction was necessary because "it is not sensible to risk a damaging rise in long-term interest rates that would make investment and the cost of mortgages more expensive".

The impact of the orthodox economic idea of crowding-out on the formulation of macroeconomic policy during the Cameron-Clegg and Cameron government was to return the relationship between policy instruments to the orthodox hierarchy, which sees fiscal policy play a supportive role to monetary policy. In the first instance, the orthodox hierarchy involves the use of orthodox fiscal policy instruments to create the policy space for interest-rates and credit conditions in the UK economy to reflect the policy decisions of the MPC and Bank of England. For example, in his reply to an *open letter* from the Governor of the Bank of England on the 15th February 2011, Osborne (2011a:1) argued that deficit-reduction 'provide[s] the MPC with the space it needs to target low inflation' and failure to implement fiscal consolidation in the public finances 'would make the MPC's job harder by putting further upwards pressure on inflation, and would risk promoting an offsetting monetary tightening'[173]. Thus, in his *Remit for the MPC* letter published on the 19th March 2014, Osborne (2014a:1) explained that 'monetary policy is a key element of the government's macroeconomic strategy, supported by a credible commitment to necessary fiscal consolidation'.

Deficit-reduction also allowed fiscal policy to support the MPC in the achievement of the orthodox objective of price stability. For example, in his reply to an *open letter* on the 18th May 2010, just six days after the formation of the

[173] Osborne (2011f:1;2011j:2;2012e) contended that deficit-reduction created the space for the MPC to target low inflation and stepping back from fiscal consolidation in the public finances would prompt an offsetting monetary tightening in two further replies to *open letters* and a public speech on the 14th June 2012.

Cameron-Clegg government, Osborne (2010a:2) asserted that fiscal credibility, through the implementation of deficit-reduction and a new fiscal framework for policymaking, would 'support the recovery and the goal of price stability'. Furthermore, Cameron (2010) declared in his 28th May 2010 speech that "getting the deficit down and keeping it down will help to restrain inflationary pressures, allow interest rates to remain lower for longer and create the space for private investment". Specifically, according to members of the Cameron-Clegg government, deficit-reduction supported monetary policy by delivering the credibility in macroeconomic policy that allowed the MPC and Bank of England to provide monetary stimulus to the UK economy, which would allow economic recovery to be based on private sector investment and entrepreneurship[174]. In turn, as explained earlier in the chapter, monetary stimulus would create the economic conditions that would allow inflation to return to target and the orthodox objective of price stability.

In his reply to an *open letter* on the 14th February 2012, for example, Osborne (2012b:2) explained that 'the government's absolute commitment to reducing our record budget deficit and getting the public finances back on a sustainable path allows monetary policy to stay looser for longer, providing a monetary stimulus to the economy at a time of fiscal consolidation'. Similarly, the Treasury (2013c:12) Autumn Statement Report of 2013 argued that 'fiscal credibility has helped keep UK market interest rates low by historical standards and facilitated an activist monetary policy'. This was echoed by Dave Ramsden, Chief Economic Advisor at the Treasury (2010-Present), in an interview with *Civil Service Quarterly* when he stated that 'fiscal credibility… means that the monetary authority can concentrate on

[174] Important members of the Cameron-Clegg and Cameron governments such as Alexander (2010:c.198;2011d;2012:c.702;2012b:2012c;2012d), Cameron (2012b: 2013a) and Osborne (2010f;2011h;c.148;2011k;2011m;2011n;2012e;2012g;2013b; 2014c;2015a;2015c) repeatedly affirmed that deficit-reduction provided the credibility in macroeconomic policy that allowed the MPC and Bank of England to provide monetary stimulus to the UK economy. In turn, it was claimed this would enable economic recovery to be based on private sector investment and entrepreneurship. The relationship between deficit-reduction, credibility and monetary stimulus was affirmed by the Treasury (2011:22,27;2015:2,9;2015a:9) and junior ministers at the Treasury such as Greening (2011;c.746).

supporting the economy rather than worrying about whether there is going to be a loss of confidence' (Lambert,2013).

It was through the orthodox economic idea of crowding-out that the Cameron-Clegg and Cameron government were adherents of the notion of expansionary fiscal consolidation, which posited that public expenditure cuts and deficit-reduction would lead to economic growth in countries with a high debt-to-GDP ratio. Indeed, it was regularly asserted by members of the Cameron-Clegg government in public speeches that deficit-reduction would secure the economic recovery and lead to the resurgence of economic growth in the UK economy[175]. For example, in a speech on the 19th May 2010, Osborne (2010b) stated that "we must tackle our record deficit – because otherwise there will be no recovery at all. It will be undermined by rising interest rates, falling confidence and the fear of higher taxes". Similarly, in his speech on the 28th May 2010, Cameron (2010) argued that "the British state is borrowing one pound for every four it spends. Our budget deficit is set to overtake Greece. If we don't deal with this, there will be no growth, there will no recovery. It will be undercut by rising interest rates, rising inflation, falling confidence and the prospect of higher taxes", which meant that "dealing with the deficit is not an alternative to economic growth – the two go hand-in-hand". Thus, in his 'Emergency' Budget Statement on the 22nd June 2010, Osborne (2010f) declared that "the crisis in the Eurozone shows that unless we deal with our debts there will be no growth. And these forecasts demonstrate that a credible plan to cut our budget deficit goes hand in hand with a steady and sustained economic recovery, with low inflation and falling unemployment".

Once the UK economic recovery began to strengthen from the Autumn of 2014 onwards, Osborne displayed increasing hubris in the claim that economic growth proved vindication of the notion of expansionary fiscal consolidation. For

[175] The assertion that deficit-reduction secured the economic recovery and promoted economic growth in the UK economy was made by Alexander (2010c;2011c;2011f;2012;2012a;2012b), Cameron (2010b:2011;2011d;2012a; 2012b), Cameron and Clegg (2012). Clegg (2011b;2012) and Osborne (2010h). Expansionary fiscal consolidation was also expressed in policy documents by the Treasury (2010a:1;2010b:1,14-15).

instance, in a speech on the 9th September 2013, Osborne (2013e) declared that "those in favour of a Plan B have lost the argument" because "the pace of fiscal consolidation has not changed, government spending cuts have continued as planned, and yet growth has accelerated and many of the leading economic indicators show activity rising than at any time since the 1990s". Osborne (2014b) returned to this theme in a speech on the 11th April 2014 when he argued that "pessimistic predictions that fiscal consolidation was incompatible with economic recovery have been proved comprehensively wrong by events. Cutting deficits and controlling spending has not choked off recovery but has instead laid the foundations for sustainable growth". Finally, in a speech on the 14th January 2015, Osborne (2015a) declared that the return of economic growth in the UK economy meant "the argument about the past is settled".

The formation of the Cameron-Clegg government also saw the return of the orthodox economic idea of competitiveness, which was constructed in public speeches and policy documents in the same manner as it had in the Twentieth century and continued to be wrapped within the discourse on globalisation as it had during the Blair government elected on the 1st May 1997. For example, in a speech on the 15th June 2011, Osborne (2011g) asserted that UK business were "all exposed to fierce competition" from the global economy. Moreover, Cameron (2013b) posited in a speech on the 10th June 2013 that the global economy was characterised by "competition that is more intense than ever before, involving more countries than ever before, who are more ambitious and determined than ever before. That is why I call it a global race". Thus, the UK economy and its firms and entrepreneurs were identified as being part of a 'global marketplace' or global race' in which the ability to sell and export goods and services was subject to global competition[176].

The impact of the orthodox economic idea of competitiveness on the formulation of policy during the Cameron-Clegg and Cameron government was to

[176] Cameron (2010b:2012c;2012d;2013;2013e;2014), the Treasury (2010a:3,25; 2012a:5,7;2013:1,3,9,33,45,48;2013c:7,11,42,48,57;2014:9,18,33;2014b:20; 2015a: 17) and Osborne (2012i;2013;2013b;2013c;2014) all asserted that the UK firms and entrepreneurs operated in a 'global marketplace' or 'global race', which was characterised by ever greater competition between businesses for sales and exports.

assign macroeconomic and microeconomic policy to the divisions of responsibility established as explained by Nigel Lawson in his 1984 *Mais Lecture* and during the Blair government during the 1997-2001 Parliament. Here, it was the role of microeconomic policy to create competitive domestic markets that would enhance the competitiveness of UK business in global markets. For example, in their 2012 Autumn Statement Report, the Treasury (2012a:7,39) posited that 'to enable the UK to compete in this global race… the government is delivering an ambitious programme of structural reforms" and "redoubling its efforts to promote exports and encourage foreign direct investment". Thus, in a speech on the 19th June 2013, Cameron (2013c) contended that coalition government were delivering "structural reforms to increase our competitiveness so our young people can get into work and succeed in the global race".

Structural reform would enhance the competitiveness of the UK economy in global markets, according to David Cameron (2013b;2013e), by reducing the size of the state. For instance, in his 2012 Conservative party conference speech on the 10th October 2012, Cameron (2012b) asserted that the nations that failed in the 'global race' would be those who were "fat, sclerotic, over-regulated, spending money on unaffordable welfare systems, huge pensions bills, unreformed public services". Thus, Cameron (Ibid) argued that it was necessary to ensure the "private sector [is] bigger and the public sector [is] smaller… our opponents call it Tory cuts, slashing the state. No: it's the best way to create the sustainable jobs people need". One of the microeconomic policies identified by Osborne (2010f;2015a) and the Treasury (2012:32) as particularly important in improving the competitiveness and growth potential of the UK economy was reduction in direct taxation, in particular, corporation tax and the cut in the higher rate of income tax from 50% to 45% at the 2012 Budget. Finally, the orthodox economic idea of competitiveness was used to reject the implementation of discretionary fiscal policy strategies. For instance, in a speech on the 11th November 2013, Cameron (2013e) claimed that the route to competitiveness did not lay in "spending and borrowing more on an ever bigger state in an attempt to somehow insulate ourselves from global competition".

The final orthodox idea that was important to the formulation of economic policy after the formation of the Cameron-Clegg government was that of economic liberalism, which was interpreted and constructed in the same manner as it had during the Twentieth century and in the 1997-2001 Parliament by the Blair government. Similar to previous discussion of the orthodox economic idea of competitiveness, economic liberalism identified that business and entrepreneurs of the private sector, rather than state and government, were the drivers of economic growth and employment[177]. For instance, in his 2010 'Emergency' Budget Statement, Osborne (2010f) declared that it was his "deeply held belief that a genuine and long-lasting economic recovery must have its foundations in the private sector. That is where the jobs will come from – and we will do absolutely everything to support their creation". Osborne (2011b) echoed this sentiment in a speech on the 5th March 2011 in which he stated that "It's people who create growth. It's the strivers, the entrepreneurs, the engineers, the innovators, the savers, who create growth". Here, Osborne (2012) identified the UK, in a speech on the 27th January 2012, as a "liberal Anglo-Saxon economy" that was "even more open to trade and investment than the US… we must continue to preserve this openness against those who seek to undermine open markets and free enterprise".

The impact of the orthodox economic idea of economic liberalism on the formulation of economic policy during the Cameron-Clegg and Cameron government was the same as the orthodox economic idea of competitiveness in that it led to the establishment of a division of responsibility between macroeconomic and microeconomic policy. Therefore, in the forward to the joint Treasury and Department of Business, Innovation and Skills (BIS) (2010:3-4) paper entitled *The Path to Strong, Sustainable and Balanced Growth*, Osborne and Vince Cable, Secretary of State for Business, Innovation and Skills (2010-2015) stated that, whilst government did not create economic growth, what it 'can do is provide the

[177] The identification of entrepreneurs and businesses in the private sector as the drivers of economic growth and employment was made by important members of the Cameron-Clegg government such as Alexander (2014), Cameron (2011;2011a:c.287;2011b), Osborne (2010g;2013f), junior ministers at the Treasury, such as Guake (2010) and Hoban (2010;2011;c.1033), the BIS (2010:3,5;2010a), Treasury (2010a2-3,25;2010b:25) and a joint paper by the Treasury and BIS (2011).

conditions for success to promote a new economic dynamism – harnessing our economic strengths, removing barriers which prevent markets from supporting enterprise, and putting the private sector first when making decisions on tax, regulation and spending' and 'create the best environment for the private sector to succeed'. Thus, the Treasury and BIS (2010:5) stated the Cameron-Clegg governments desire to 'build a broad-based economy rooted in higher levels of business investment, open and competitive markets and greater exports', which required the economic stability delivered through deficit-reduction and the implementation of orthodox fiscal policy instruments, monetary activism to ensure the private sector had access to finance and microeconomic policy to provide open, free, competitive and dynamic markets that would promote inward investment and private sector growth.

Conclusion

This chapter has provided a case-study of UK macroeconomic policy during the Cameron-Clegg and Cameron governments from the 12th May 2015 to the 13th July 2016. The chapter has drawn two conclusions pertaining to why the orthodox cycle provides a superior explanation and understanding of developments in UK macroeconomic policymaking than that furnished by punctuated equilibrium. First, the orthodox cycle explains that the Global Financial Crisis and the formation of the Cameron-Clegg government between the Conservative and Liberal Democrats did not lead to radical monetary policy change, but rather led to the continuity of orthodox monetary policy as monetary policymaking remained in the consolidation phase of the orthodox cycle. For example, the orthodox cycle explains that the MPC and Bank of England continued to use orthodox monetary policy instruments to create the economic conditions necessary to return inflation to target and the orthodox objective of price stability. Here, continuity in the monetary policymaking framework allowed the MPC and Bank of England to provide monetary stimulus to

the UK economy to counteract the ‘downward’ pressure to inflation exerted by spare capacity and unemployment.

The chapter also demonstrated that the orthodox cycle can account for the implementation of ‘unorthodox’ credit easing policies, which were used to assist the Bank Rate during a period when the transmission mechanism of the Bank Rate was impaired. Furthermore, the chapter provided further evidence pertaining to why we should consider QE an example of OMOs, which the orthodox cycle explains as an orthodox monetary policy instrument. Finally, changes within the Bank of England’s SMF is explained by the orthodox cycle as an operational change to the formulation of monetary policy that supported the implementation of orthodox macroeconomic policy instruments.

The second conclusion pertaining to why the orthodox cycle provides a superior explanation and understanding of developments in UK macroeconomic policymaking than that furnished by punctuated equilibrium relates to fiscal policymaking. Specifically, the chapter identified the ‘Emergency’ Budget of the 22nd June 2010 as a significant event in fiscal policymaking, which initiated the orthodoxy phase of the orthodox cycle even though the economic performance of the public finances had not returned to orthodox policy outcomes. In particular, four reasons were given as to why the ‘Emergency’ Budget should be considered a significant event. First, relates to the feverish political climate after the ‘hung’ result at the 2010 general election, the ensuing negotiations to form a coalition government and the changing position of the Liberal Democrats on fiscal policy. Second, is the considerable institutional support for deficit-reduction and the restoration to orthodox fiscal policy within the Treasury and Bank of England. Third, is the scale of fiscal consolidation the ‘Emergency’ Budget introduced, which provided a forceful communication of the restoration and institutionalisation of orthodox fiscal policy to the UK electorate. Fourth, is that the ‘Emergency’ Budget was implemented in a fervent political climate pertaining to the relative merits of ‘stimulus vs austerity’ fiscal policy strategies, which started in 2008 and continued unabated throughout the Cameron-Clegg and Cameron government. The onset of the orthodoxy phase means the orthodox cycle can account for the continuity of orthodox fiscal policy, which

saw orthodox fiscal policy instruments implemented in the pursuit of the return to orthodox fiscal policy outcomes in the public finances. Furthermore, orthodox cycle can explain the myraid of operational changes to the formulation of fiscal policymaking introduced during the Cameron-Clegg and Cameron government by Osborne and the Treasury as operational changes to the formulation of policy that supported the implementation of orthodox fiscal policy.

Finally, the chapter also discussed the role of economic ideas in the formulation of macroeconomic policy during the Cameron-Clegg and Cameron government. Once again, the orthodox cycle can explain the continuity of orthodox economic ideas. First, during the consolidation phase, the orthodox cycle explains that the implementation of orthodox policy instruments is supported by the resurgence of orthodox economic ideas in the formulation of policy. Second, the orthodox cycle expounds that the restoration of orthodox macroeconomic policy during orthodoxy phase, in circumstances when monetary or fiscal policymaking enter this phase of the cycle without the other, will include evidence of orthodox economic ideas in the formulation of policy in that particular realm of policymaking. Specifically, continuity in orthodox economic ideas were integral to several developments in macroeconomic policy after the 12th May 2010, which served to produce continuity of orthodox macroeconomic policy, rather, than radical policy change after the 12th May 2010. First, the implementation deficit-reduction and restoration of orthodox fiscal policy. Second, the return to an orthodox hierarchy between macroeconomic policy instruments and the continued provision of monetary stimulus to the UK economy. Third, the return to the same division of responsibility between macroeconomic and microeconomic policy, which had been assigned by New Labour governments after their election in May 1997.

Chapter 10

Conclusion

This thesis has argued that the model of punctuated equilibrium provides a flawed understanding and explanation of when and why policies and ideas exhibit change and continuity in UK macroeconomic policymaking. To this end, the thesis has challenged the common view that exogenous and endogenous shocks, such as economic crises or changes in government, to UK macroeconomic policymaking leads to radical change in policy and economic ideas. In providing this challenge, Chapters Two, Three and Four identified two gaps in our current knowledge of UK economic policymaking. The first gap pertained to the need for greater specificity in our understanding and definition of orthodox UK macroeconomic policy. The second gap related to the need for a superior understanding of when and why UK macroeconomic policy and economic ideas exhibits change and continuity.

The original contribution provided by this thesis to our existing comprehension of UK economic policymaking has arisen from the two research findings that it has generated. The first research finding supplied by this thesis is greater precision in our understanding and definition of orthodox macroeconomic policy, which was delineated in Chapter Five. However, the second half of the thesis did make one amendment to the new understanding and definition of orthodox macroeconomic policy, which requires identification in the conclusion. Specifically, Chapter Six identified that after the election of the Blair government on the 1st May 1997 the orthodox economic idea of internationalism was replaced by the economic element of the idea of globalisation. This thesis has demonstrated the continuity between the economic element of globalisation and the orthodox economic idea of

internationalism in two areas. First, the similarity in the interpretation and construction of the orthodox economic idea of internationalism and globalisation as evidenced in public speeches and policy documents. Second, the orthodox economic idea of internationalism and globalisation had the same impact on the formulation of macroeconomic policy, namely, to accentuate the need to maintain confidence and credibility in policymaking. Therefore, this thesis has argued that the economic idea of globalisation is the modern expression of the orthodox economic idea of internationalism. The final version of the new understanding and definition of orthodox macroeconomic policy, updated to include the orthodox economic idea of globalisation, but changed in no other respect from that presented in Chapter Five and discussed in the case-study chapters is available in Figure One.

The second research finding delivered by this thesis is the identification of the orthodox cycle in UK macroeconomic policymaking, which utilises the new understanding and definition of orthodox macroeconomic policy and explains the continuity of orthodox macroeconomic policy and ideas via a series of distinct phases. This is in stark contrast to punctuated equilibrium, which conceives of radical policy and ideational change as a discontinuous process arising from aforementioned exogenous and endogenous shocks. Whilst the orthodox cycle explains the continuity of orthodox macroeconomic policy and ideas, it does not argue that change never occurs. Rather, the orthodox cycle understands that deviation from orthodox policy and ideas occurs only for a temporary phase in macroeconomic policymaking. Furthermore, the orthodox cycle has explicated that institutional additions and operational changes to macroeconomic policymaking are regularly introduced. However, these institutional additions and operational changes are not implemented to produce radical change in policy. Instead, they are designed to support the implementation and return to orthodox macroeconomic policy in the aftermath of a crisis. It is these institutional additions and operational changes to macroeconomic policymaking, such as the introduction of 'monetarism', that are often confused by scholars with radical policy change.

This thesis has identified the explanatory value of the orthodox cycle in UK macroeconomic policymaking as a conceptual framework to understand change and

continuity in policy and ideas in several different historical and contemporary periods, which has included November 1918 to December 1934, April 1975 to April 1997 and May 1997 to July 2016. The orthodox cycle in UK macroeconomic policymaking from the 2nd May 1997 onwards is illustrated in Figure Two. This thesis concludes, notwithstanding the need for a future research agenda, that the orthodox cycle provides a superior understanding and explanation of continuity and change in UK macroeconomic policy than that furnished by punctuated equilibrium.

Figure One: UK Orthodox Macroeconomic Policy

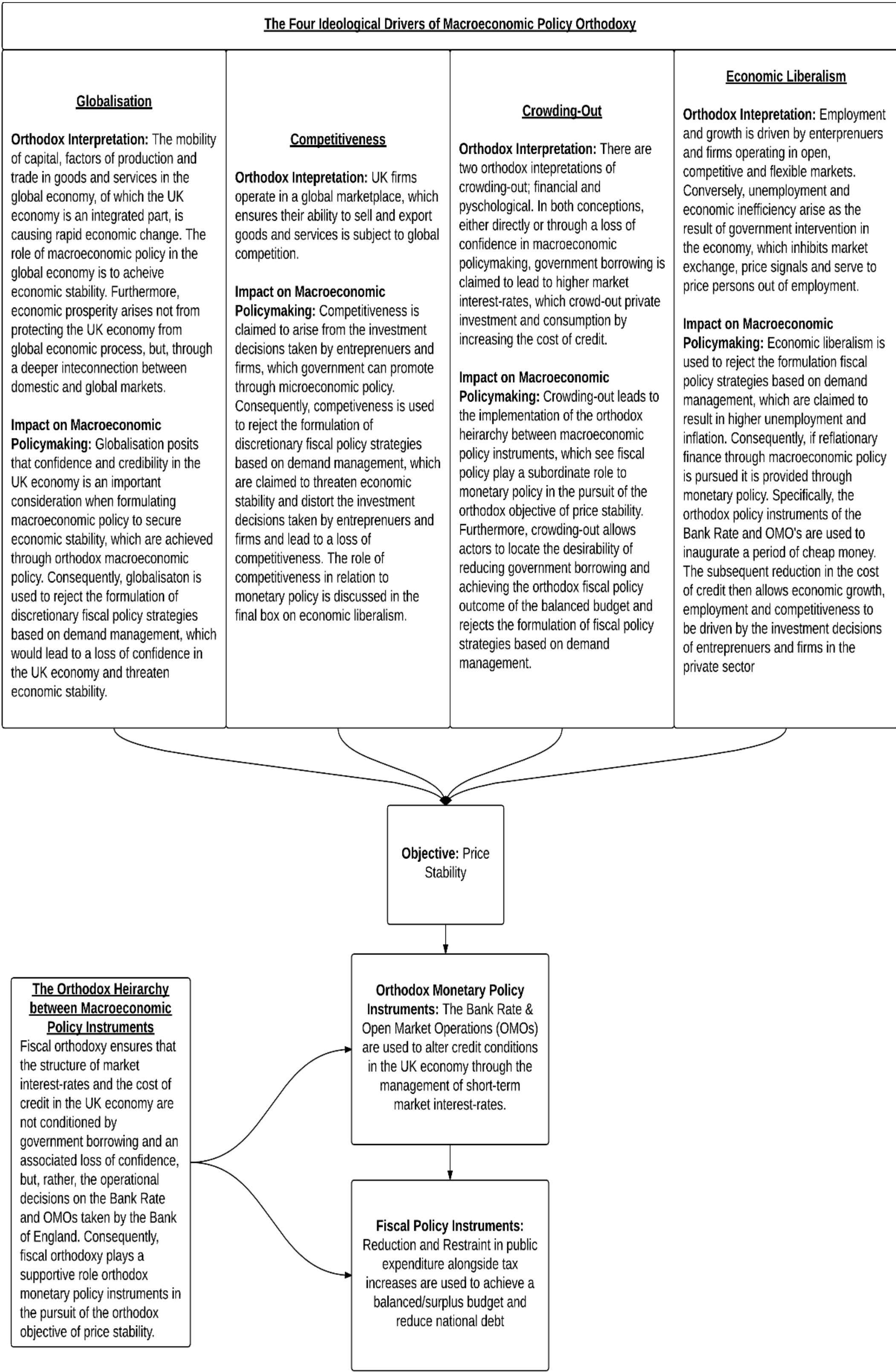
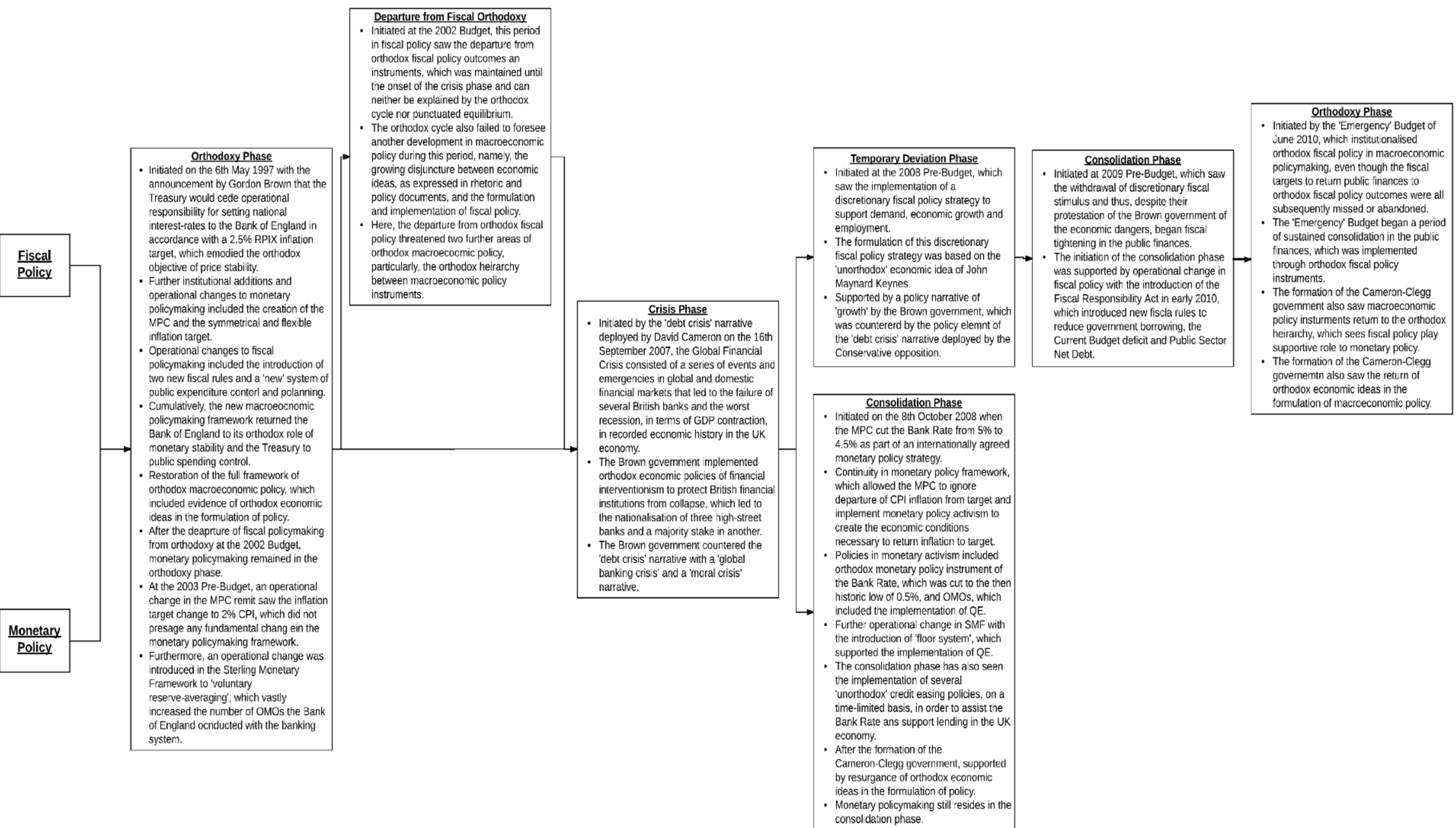


Figure Two: The Orthodox Cycle in UK Macroeconomic Policymaking from 2nd May 1997 to 13th July 2016



Future Research Agenda

At various junctures of this thesis it has been highlighted that the analysis presented is only the first stage in a future research agenda. The first stage of this future research agenda requires the application of the orthodox cycle and its understanding and explanation of when and why UK macroeconomic policy and ideas exhibit continuity and change to alternative historical periods. For example, whilst the post-war period was neglected for historiography in the first half of the thesis because of the absence of major economic crises prior to 1973, the application of the orthodox cycle to this historical period in UK macroeconomic policymaking would provide a significant test of the orthodox cycle's explanatory potential. Furthermore, the applicability of the orthodox cycle to explain continuity and change prior to 1914 was only given cursory attention in Chapter Three and a future research agenda requires detailed and systematic analysis of UK macroeconomic policymaking dating back to the 1688 Glorious Revolution and the 1694 Bank of England Charter. Moreover, this stage of the future research agenda would need to address the 2002-2007 period in fiscal policymaking because, as Chapter Seven highlighted, neither the orthodox cycle nor punctuated equilibrium could explain the departure from orthodox fiscal policy from the 2002 Budget onwards. Finally, this stage of the future research agenda could include a study of contemporary developments in UK macroeconomic policymaking. In particular, the signalled 'reset' of fiscal policy indicated by Phillip Hammond, the replacement of George Osborne as Chancellor of the Exchequer, in response to the 'shock' of the leave vote in the European Union referendum of the 23rd July 2016 and eventual 'Brexit' when Article 50 of the Lisbon Treaty is triggered by the new government of Theresa May.

The second stage of the future research agenda requires extending the explanatory potential of the orthodox cycle. This involves questioning the process by which macroeconomic policy is formulated and how established interests influence policy outcomes. To be precise, this stage of the research agenda would seek to establish where the return to orthodoxy is generated in the policymaking process and UK politics and the motivation of institutions and established interests in returning

macroeconomic policy to orthodoxy. During the collection and analysis of data for Chapters Three and Four, several observations on the point pertaining to established interests were made. However, these observations remain tentative without the further inquiry conducted during this stage of the future research agenda.

This stage of the future research agenda is particularly necessary because, as the orthodox cycle is currently constituted, it is open to the same criticisms directed at the stage, evidence-based (EBP) and state-centric models of public policymaking, which were identified in Chapter Two. Specifically, the orthodox cycle could be criticised for failing to include analysis of the number, type and motivations of institutions and interests involved in making macroeconomic policy. Whilst the potential for these criticisms of the orthodox cycle are valid, the orthodox cycle does not present a technocratic exposition of the policymaking process as it is presented in those aforementioned models. For example, the orthodox cycle gives a significant role in policymaking to ideas, particularly in the formulation of policy, and politics through the deployment of crisis and policy narratives.

The third stage of the future research agenda requires the incorporation of microeconomic policy, which has only been discussed in this thesis in relation to its impact on the formulation and implementation of macroeconomic policy into the orthodox cycle. Here, an inductive methodology would be applied to the study of UK microeconomic policy to see if any patterns are detectable in policymaking and if an 'orthodoxy' can be discerned. The results of this stage of the future research agenda can then be cross-referenced with the orthodox cycle, which would allow us to establish if the orthodox cycle has any explanatory value for microeconomic policymaking. Alternatively, this stage of the future research agenda could determine that the orthodox cycle needs amendment to include the research findings from the study of UK microeconomic policy or that the orthodox cycle can only explain change and continuity in UK macroeconomic policymaking. Once again, during the collection and analysis of data for Chapters Three and Four tentative observations on 'orthodox' microeconomic policy that would require further analysis were made.

Appendix 1

This Appendix provides specification of the sources used for data collection according to the primary, secondary and tertiary classification system in the historiography and case-study chapters.

Primary Sources

Primary sources are those produced by or part of the event (UK macroeconomic policymaking) in question.

- HM Treasury documents such as Budget and Pre-Budget Reports.
- Bank of England documents such as Inflation Reports and Quarterly Bulletins.
- Cabinet documents such as Cabinet Papers and Cabinet Memorandum.
- Public speeches by figures such as the Prime Minister, Chancellor of the Exchequer, HM Treasury and Bank of England officials and MPC members.
- Minutes of MPC meetings.
- Public Papers such as letters written between the Chancellor of the Exchequer and Governor of the Bank of England.
- Quantitative data produced by institutions such as the OBR and ONS.

Secondary Sources

Secondary sources are those related to or produced soon after the event.

- Reports by government committee such as the Treasury Select Committee.
- Reports by non-governmental institutions such as the IFS, IMF and OECD.

- Oral evidence to government committees by figures such as the Chancellor of the Exchequer and Bank of England officials.
- Hansard: Parliamentary Debates.
- Public speeches by Cabinet members other than the Chancellor of the Exchequer and Junior ministers at HM Treasury and other government departments.
- Policy documents by government departments other than HM Treasury.
- General election manifestos.
- Newspaper articles and internet blogs

Tertiary Sources

Tertiary sources are materials written afterwards to reconstruct the event.

- Autobiographies, biographies, memoirs and diaries.
- Monographs
- Academic Journal Articles

Appendix 2

This appendix provides the number of different primary, secondary and tertiary sources used in the collection of data in the historiography and case-study chapters.

Chapter Three

- Primary Sources = 13
- Secondary Sources = 16
- Tertiary Sources = 110

In this chapter, although not reflected in the numbers above, primary data was collected from tertiary sources. During the 1970s and 1980s, several scholars took advantage of the release of new primary documentation released under the thirty-year rule to produce detailed monographs and journal articles on interwar UK economic policymaking. Whilst Chapter Three includes data collected from independent archival trips, extensive use was made of the monographs and journal articles who had already consulted detailed examination of these public records. Where primary data has been collected from tertiary sources the author has been appropriately cited.

Chapter Four

- Primary Sources = 75
- Secondary Sources = 42
- Tertiary Sources = 75

Chapter Six

- Primary Sources = 157
- Secondary Sources = 56
- Tertiary Sources = 35

Chapter Seven

- Primary Sources = 182
- Secondary Sources = 58
- Tertiary Sources = 27

Chapter Eight

- Primary Sources = 127
- Secondary Sources = 38
- Tertiary Sources = 10

Chapter Nine

- Primary Sources = 211
- Secondary Sources = 47
- Tertiary Sources = 19

Appendix 3

This appendix provides the broad themes for each historiography and case-study under which data was categorised and analysed.

Chapter Three

The broad themes used for the categorisation in Chapter Three were…

1. Macroeconomic Policy Objectives, 1918-1928.
2. Fiscal Policy Instruments, 1918-1928.
3. Monetary Policy Instruments, 1918-1928.
4. Relationship between Policy Instruments, 1918-1928.
5. Economic Ideas, 1918-1928.
6. Policy Narratives, 1918-1928.
7. Events and Emergencies (Political and Economic), 1918-1928.
8. Macroeconomic Policy Performance, 1918-1928.
9. Institutional Additions and Operational Changes to the conduct of Macroeconomic Policymaking, 1918-1928.

And…

10. Macroeconomic Policy Objectives, 1929-1939.
11. Fiscal Policy Instruments, 1929-1939.
12. Monetary Policy Instruments, 1929-1939.
13. Relationship between Policy Instruments, 1929-1939.
14. Economic Ideas, 1929-1939.
15. Policy Narratives, 1929-1939.
16. Events and Emergencies (Political and Economic), 1929-1939.

17. Macroeconomic Policy Performance, 1929-1939.
18. Institutional Additions and Operational Changes to the conduct of Macroeconomic Policymaking, 1929-1939.

Chapter Four

The broad themes used for the categorisation in Chapter Four were…

1. Macroeconomic Policy Objectives, 1975-1979.
2. Fiscal Policy Instruments, 1974-1979.
3. Monetary Policy Instruments, 1971-1979.
4. Relationship between Policy Instruments, 1975-1979.
5. Economic Ideas, 1975-1979.
6. Policy Narrative, 1975-1979.
7. Events and Emergencies (Political and Economic), 1973-1979.
8. Macroeconomic Policy Performance, 1975-1979.
9. Institutional Additions and Operational Changes to the Conduct of Macroeconomic Policymaking, 1975-1979.

And…

10. Macroeconomic Policy Objectives, 1979-1990.
11. Fiscal Policy Instruments, 1979-1990.
12. Monetary Policy Instruments, 1979-1990.
13. Relationship between Policy Instruments, 1979-1990.
14. Economic Ideas, 1979-1990.
15. Policy Narrative, 1979-1990.
16. Events and Emergencies (Political and Economic), 1979-1990.

17. Macroeconomic Policy Performance, 1979-1990.
18. Institutional Additions and Operational Changes to the Conduct of Macroeconomic Policymaking, 1979-1990.

And…

19. Macroeconomic Policy Objectives, 1990-1997.
20. Fiscal Policy Instruments, 1990-1997.
21. Monetary Policy Instruments, 1990-1997.
22. Relationship between Policy Instruments, 1990-1997.
23. Economic Ideas, 1990-1997.
24. Policy Narrative, 1990-1997.
25. Events and Emergencies (Political and Economic), 1990-1997.
26. Macroeconomic Policy Performance, 1990-1997.
27. Institutional Additions and Operational Changes to the Conduct of Macroeconomic Policymaking, 1990-1997.

Chapters Six and Seven

The themes used for the categorisation in Chapter Six and Seven…

1. Macroeconomic Policy Objectives, 1997-2007.
2. Fiscal Policy Instruments, 1997-2007.
3. Monetary Policy Instruments, 1997-2007.
4. Relationship between Policy Instruments, 1997-2007.
5. Economic Ideas, 1997-2007.
6. Policy Narrative, 1997-2007.

7. Events and Emergencies (Political and Economic), 1997-2007.
8. Macroeconomic Policy Performance, 1997-2007.
9. Institutional Additions and Operational Changes to the Conduct of Macroeconomic Policymaking, 1997-2007.

Chapter Eight

1. Macroeconomic Policy Objectives, 2007-2010.
2. Fiscal Policy Instruments, 2007-2010.
3. Monetary Policy Instruments, 2007-2010.
4. Relationship between Policy Instruments, 2007-2010.
5. Economic Ideas, 2007-2010.
6. Policy Narrative, 2007-2010.
7. Events and Emergencies (Political and Economic), 2007-2010.
8. Macroeconomic Policy Performance, 2007-2010.
9. Institutional Additions and Operational Changes to the Conduct of Macroeconomic Policymaking, 2007-2010

Chapter Nine

1. Macroeconomic Policy Objectives, 2010-2016.
2. Fiscal Policy Instruments, 2010-2016.
3. Monetary Policy Instruments, 2010-2016.
4. Relationship between Policy Instruments, 2010-2016.
5. Economic Ideas, 2010-2016.

6. Policy Narrative, 2010-2016.
7. Events and Emergencies (Political and Economic), 2010-2016.
8. Macroeconomic Policy Performance, 2010-2016.
9. Institutional Additions and Operational Changes to the Conduct of Macroeconomic Policymaking, 2010-2016.

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