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An Agenda for a Democratic Economy

*David Cayla*¹

The art of governance requires managers to take “good” decisions that align with accepted standards. Today, the standard neoliberal management is to evaluate the costs and benefits of each option to show that the selected one is objectively “good”—with benefits outweighing costs. This approach is prevalent in any decision-making structure where someone chooses on behalf of others, be it a company, public administration, or non-profit organization.

This norm is fundamental to contemporary capitalism, but it is grounded in another institution: the market. According to the neoliberal doctrine, the market’s primary function is not as an exchange platform but as a valuation and price-creating device (Cayla 2023a).

In its idealized vision, a market is a place where numerous and autonomous exchanges generate prices and incentives that push each agent to behave in accordance with the global needs of the economy. But there are situations where the smoothness of the market process cannot work. In such moments, the norm of the market price disappears and is replaced with other ways of valuation. For instance, in 2022, the European union experienced a deep energy crisis. On the spot market, the price of electricity increased to more than €1000 by MWh, a level that was judged unbearable by political authorities. Direct subsidies, specific taxes and a global reform of the electricity market were decided to overcome the market prices.

This example shows that besides the market mechanism, social, strategic, or diplomatic issues must be considered in economic policies. The environmental protection, for example, is typically a question that appears to challenge the neoliberal standard. Can we switch toward an ecological transition by giving carbon emissions a price? Nobel Prize-winning economist William Nordhaus believes so, explaining that a relatively small price per ton of CO₂ emissions (from \$25 in 2015 to \$160 in 2050) would suffice to limit global warming to +2.5°C, the best cost-benefit trade-off (Nordhaus 2013, 228).

Most climate experts and engineers do not share Nordhaus’ optimism. First, they believe that there can be no cost-benefit valuation of global warming, as costs are hazardous and the economic value of ecosystems cannot be estimated; second, fossil fuels are difficult to substitute with other energy sources, and there is no guarantee that an increase in their prices would suffice to reduce their demand to zero by 2050; finally, they argue that a single carbon price for countries with different levels of development would be unfair and unbearable for the poorest populations.

In other words, for philosophical, technical, and equity reasons, the market process may not be able to reduce our carbon emissions. Therefore, other non-market tools may be necessary to cope

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with global warming. This leaves us with important questions: what other complementary coordination mechanisms can be used to change economic behaviors? What would be their efficiency? How can they complete with the market mechanisms?

Precise answers to these questions exceed the scope of this article. However, I intend to explain, in the following sections, what neoliberalism is about, how it was historically implemented, why it is already in crisis, and what can be done to create non-market institutions that could solve some coordination issues that the market mechanism cannot resolve.

The Neoliberal Agenda

The Walter Lippmann Colloquium held in Paris at the end of August 1938 is generally regarded as the founding moment of the neoliberal doctrine (Foucault 2008; Reinhoudt and Audier 2018). The participants, among them Friedrich Hayek, Ludwig von Mises, Wilhelm Röpke, and many others, were convinced of the necessity to refound liberalism in order to respond to the threat of “planning,” embodied with communism and fascism.

Two main ideas were at the heart of this meeting. The first one was that liberalism had to turn away from a “dogmatic *laissez-faire* attitude” (Hayek [1944] 2001, 37), the Manchestarian vision of liberalism. As Louis Rougier stated in the opening speech of the colloquium:

Being liberal is not, like the “Manchesterian,” letting cars drive in all directions, following their whim, from which traffic jams and endless accidents would result; it is not, like the “planner,” fixing for each car its hour of exit and its itinerary; it is imposing rules of the road, all while recognizing that [this set of rules] is not necessarily the same at the time of rapid means of transportation as during the time of the stagecoach. (Reinhoudt and Audier 2018, 99)

This shift in perspective on *laissez-faire* stemmed from a revised understanding of the market. Contradictory to the traditional conception of Adam Smith, the participants of the colloquium believed that the market should not be considered as a “natural” institution, the product of the human willingness to exchange with others, but as being embedded into a broader legal and cultural framework. The artificiality, and therefore fragility, of the market was the core idea of German neoliberalism² and the reason why they emphasized the concept of “economic constitution” (Böhm, Eucken, and Grossmann-Doerth 1989, 23–25). Participants like Röpke and Alexander Rüstow, but also Rougier and Lippmann, were strongly defending this position.

The second idea emphasized by the colloquium participants was that the market is an indispensable institution for economic rationality, since only a competitive market could set a price system that would perfectly reflect the needs and the means of a society. This idea was put forward by Mises ([1920] 1990 and [1922] 1951) to contest the idea that socialism had any economic rationality. It was then used by Hayek to explain how the market price conveys relevant information (Hayek 1945). The centrality of the price mechanism is put forward in the concluding remarks of the colloquium that aimed to propose “The Agenda of Liberalism,” of which it constitutes its first point:

Economic liberalism recognizes as a fundamental premise that only the pricing mechanism functioning in free markets allows for obtaining an organization of production likely to

² For an in-depth analysis of German neoliberalism, also known as “ordoliberalism,” see Gerber 1994.

make the best use of the means of production and to lead to the maximum satisfaction of the wants of men. (Reinhoudt and Audier 2018, 177)

The Neoliberal doctrine was later developed in discussions held in the Mont Pelerin Society after its foundation by Hayek and Albert Hunold in 1947.³ Since the market was not a natural institution, what kind of institutional framework should be implemented to assure its good functioning as a price generator? How should the state intervene in that regard? Neoliberals insist on the importance of discriminating between “conformable” and “non-conformable” actions regarding the intervention of the states (Foucault 2008, 137–138). Basically, conformable actions help the market to achieve its task of valuation, while non-conformable interventions denature the market and alter its ability to generate relevant prices. The state should therefore organize its self-limitation through a legal framework enforcing the “rule of law,” as opposed to the “rule of men,” which is based on arbitrary economic interventions.

The conformable actions can be grouped into four main categories according to the objectives they aim to achieve.

- Actions that strengthen the competitive dimension of the market (anti-trust policies).
- Actions needed to preserve social order (minimum income, subsidies for disabled people, etc.).
- Actions to ensure free trade and a fair international order through economic exchanges.
- Actions to preserve money and price stability.

The neoliberal normativity can be visualized with the figure below.

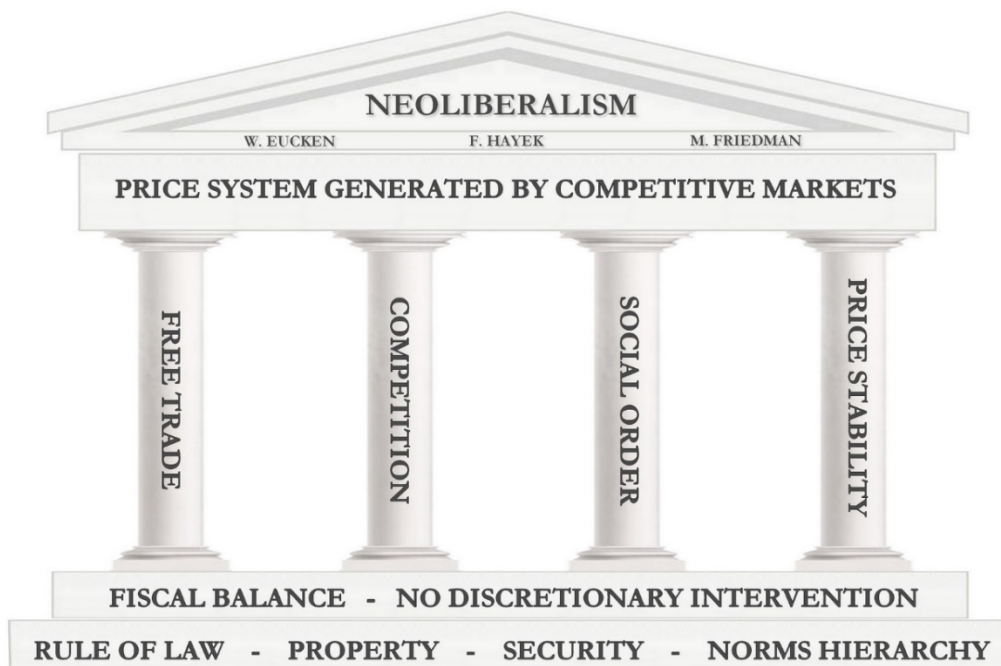


Figure 1. The Temple of Neoliberalism (from Cayla 2021, 110)

³ As Mirowski (2013, 29) explains, the term “neoliberal” was widely used by the participants of the MPS in the 1950s; Milton Friedman himself judged that “neo-liberalism offers a real hope of a better future” (Friedman 1951).

Neoliberalism in Practice

The neoliberal agenda, as it was conceived in the late 1930s, could not be put into practice before the 1970s. The warfare economy, the necessity of rebuilding Europe with the help of the Marshall plan, and the fact that most governments were rather comfortable with the idea of controlling the prices of the means of production (energy, raw materials, labor, interest rates . . .) explain why neoliberalism did not become the standard doctrine, although a limited neoliberal experience was tried in postwar Germany (Cayla 2023a, 55–59).

It is only with the collapse of the Bretton Woods system, the oil crisis, and the return of high inflation that the neoliberal ideas came back into the public debate (helped in this by two well-timed economics Nobel Prize awards in 1974 and 1976).

The neoliberal revolution took place in three main phases.

The first phase concerned the international monetary system and the banking and financial sector. After the end of the gold exchange standard in 1971, competition between currencies led each country to export its inflation through investor-friendly policies. This period of “ad hoc globalization” supported by the City and Wall Street ended with the establishment of common rules and the creation of a globalized financial market from 1986 onwards, at the initiative of French leaders (Abdelal 2007).

The Single European Act of 1986 contributed to the globalization and standardization of finance, but also initiated a second phase of liberalization that concerned labor and public utilities. The dismantling of public monopolies and the disappearance of internal borders in Europe, under the supervision of the European Court of Justice, reinforced the competitive regulation of the European single market. It was then extended to other countries through the negotiation of free trade agreements.

The last phase of the neoliberal revolution concerned agriculture. After the Marrakech Agreement (1994), developed countries had to reform their agricultural subsidy systems and open their markets to more agricultural products. Regulation of agricultural commodity prices was gradually abandoned in favor of a world price regulation.

By 1999, with the adoption of the single currency in Europe and the repealed of the Glass–Steagall legislation by the Clinton administration, the neoliberal agenda in the financial sector was rather complete. That same year, the liberalization of public utilities and the intensification of competition were also underway, as were agricultural reforms.

After the 1992 Earth Summit and the adoption of the Kyoto Protocol in 1997, the challenges raised by climate change were integrated into the neoliberal agenda. The idea was “to use harmonized prices, fees, or taxes as a method of coordinating policies among countries” (Nordhaus 2008, 149) either with a carbon tax or with the creation of a market for emissions allowances. The latter was finally established in Europe in 2005. Although they produce almost the same economic outcome, from a neoliberal perspective, the advantage of a cap and trade mechanism is that prices are not the result of political decisions but generated directly by the market forces.

The Failures of the Neoliberal Doctrine

The coordination of economic behaviors through market prices became more difficult after 2008.

The first sector where this standard collapsed is banking and finance. The subprime crisis of 2007–2008 is the consequence of the disappearance of liquidity for many financial assets backed by the U.S. mortgage system. Lacking buyers, the market froze and became unable to generate prices and valuations. To solve this problem, Secretary of the Treasury Henri Paulson, and then the Federal Reserve, adopted purchases programs for mortgage-backed financial assets, restoring prices and hence valuations. In the years that followed, the Federal Reserve continued to purchase government bonds in its quantitative easing programs. In so doing, it kept long-term interest rates low. In other words, a public institution, the central bank, tightly controlled the price of capital (Cayla 2023a).

In fact, central bank policies after 2008 were totally at odds with the neoliberal agenda. But this is not the only symptom of the failure of neoliberal doctrine. The development of the digital sector has raised other problems. Not only do the tech giants behave like monopolies, but the very fact of seeking to implement an anti-trust policy in a context of increasing returns is costly (Williamson 1968). This is why the idea of regulating the digital economy through prices derived from competitive forces has had to be abandoned. More fundamentally, it appears that digital platforms tend to replace the functions of markets. They organize the meeting between supply and demand and generate prices (Cayla 2022, 552). Reinforcing competition in a situation where markets are replaced by algorithms makes little sense.

The liberalization of public services has led to other dysfunctions. Competition in electricity markets has caused major crises in California (2000–2001) and, more recently, in the European Union (Cayla 2023b). In the United Kingdom, the partial renationalization of the rail network, decided in 2021, shows that neoliberalism is running out of steam even within Conservative administrations.

At last, free trade and other neoliberal policies were contested for their social consequences. As Dani Rodrik (2017 and 2021) explains, economists tend to underestimate the social consequences of international trade. Not only is free trade being widely contested, but the 2016 election of Donald Trump, the vote for Brexit in the United Kingdom, and the rise of populist protests in Europe shows that the social order pillar of the neoliberal doctrine is also under a decisive pressure (Cayla 2019 and 2021).

Four Principles for a Democratic Economy

The market's strength as an institutional device lies in its ability to “naturalize” the price system and place it beyond the political sphere. This makes prices acceptable to all parties, allowing for efficient resource allocation and economic coordination. However, managing scarce resources and preserving social welfare may require setting up other forms of economic coordination, as long as they are granted with a high level of legitimacy.

Taking Account of Planetary Limits

Many problems, such as the scarcity of natural resources or environmental issues, cannot be solved solely by price signals. Today, about 80% of our energy consumption comes from fossil fuels. To

reduce this proportion to a maximum of 10–20% in less than thirty years, we need not only to develop alternative energy sources, but also to change most of our industrial equipment and vehicles in a very short space of time. The depth of this kind of economic transition is similar to the transition to a war economy.

During World War II, the Roosevelt administration took decisive steps to rapidly reorganize the American economy. It realized that it was necessary to go beyond the logic of the market in order to spare the poorest and the middle class from too great an effort. For this reason, Roosevelt created two important institutions: the National Defense Advisory Commission, whose purpose was to advise the government on military purchases but also to maintain price stability and protect households; and the Office of Price Administration and Civilian Supply, which had control over most retail food prices.

As in a war economy, organizing a shift to a sustainable economy will require a rapid and profound reorientation calling for mechanisms more effective than price signals alone. It will also be necessary to reintroduce political aims into the value calculation process. Furthermore, governments will have to invest massively in technological research to find new sources of decarbonized energy, much like the United States did to build the first atomic bomb.

Re-Embedding the Market

The market is an indispensable space in any developed society for everyone to be able to conduct business and trade freely. However, the market logic can also destabilize a society, as Karl Polanyi ([1944] 2001) explained, and can lead to a dysfunctional market society.

To avoid such an outcome, it is necessary to allow the market to determine the value of commodities, which are the part of wealth that has been produced for the purpose of being sold. However, resources such as labor force, natural resources, public utilities, etc., should be allocated and valued on non-market bases. These resources are not commodities either because they were not produced at all (natural resources are extracted and not produced) or because they were produced for other purposes (labor force, public utilities, etc.).

Rethinking Public Action

The state is a sovereign institution that allows a collectivity to decide on and attain collective objectives. As such, it must manage resources that are not commodities in a democratically decided manner. But a state can also develop a long-run strategy that implies controlling the price and allocation procedures of some strategic commodities (this is the case in a war economy) or protecting certain values or principles, for instance to preserve cultural traits or artistic diversity. Lastly, the state can organize the coordination and the functioning of markets in line with the neoliberal principles.

Strengthening Democracy

Democracy presupposes the preservation of the primacy of politics over economics. But the nature and functioning of democracies may vary from country to another. For instance, every democracy needs to find procedures to solve legitimacy conflicts when different democratic institutions take different decisions. Should the local or the federal government prevail when they disagree? There cannot be any general answer to this question. However, what matters is that markets must be re-embedded in society at a level where a public debate can be organized and at the level which has the strongest legitimacy.

The weak point with globalization is that the market evolves at an international level where there are no democratic institutions, and the places where debates can be organized are too limited to control the market forces. The question that most economists do not see is that free trade is less a social and economic question than a democratic issue. The matter is less that the globalization increases inequality, but that it escamotages democracy. In other words, democracy can only be strengthened if the place and institutions where political debates occur have the ability to control their economic borders. A process of de-globalization is the key to organizing the economy along democratic lines.

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