Editorial

Philip Arestis*

Cambridge Centre for Economic and Public Policy,
Department of Land Economy,
University of Cambridge,
19 Silver Street, Cambridge CB3 9EP, UK
and
Department of Applied Economics V,
Faculty of Economics and Business,
University of the Basque Country,
Avenida Lehendakari Agirre, 83, 48015 Bilbao, Spain
E-mail: pa267@cam.ac.uk
*Corresponding author

Özlem Onaran

Department of Economics and Statistics,
Middlesex University,
The Burroughs, London NW4 4BT, UK
E-mail: O.Onaran@mdx.ac.uk

The onset of the great recession calls for a serious search of an alternative paradigm to the one that had helped to contribute to it, along with new economic policies. We organised a conference on the subject under the same title as the current issue: economic policy-in search of an alternative paradigm. Eight of the papers presented at that conference, held at the Middlesex University on the 3rd of December 2010, comprise this special issue.

Nigel F.B. Allington, John S.L. McCombie and Maureen Pike begin with their contribution entitled 'The failure of the new macroeconomic consensus: from non-ergodicity to the efficient markets hypothesis and back again'. The 1990s saw the rise what many economists saw as a consensus in macroeconomics, with macroeconomic theory strongly related to, and affecting, policy. This led to low inflation and sustained growth. Based on the rational expectations hypothesis, asset markets were seen as efficient and the proliferation of financial instruments under 'light regulation' were seen as the most efficient means of allocating risk, given agents' diverse preferences for it. This paper considers the failure of efficient markets hypothesis and presents a brief overview of the anatomy of the crises, its implications for the new economics and the appropriate policy response.

Philip Arestis and Malcolm Sawyer follow in their 'A new paradigm for macroeconomic policies'. A set of broad policies designed to secure full employment of labour with due regard paid to sustainable growth is put forward. These policies are based on the proposition that they arise out of and can only be understood by reference to a theoretical framework of the ways in which the economy operates and works. The background to this framework is that the analysis is of a monetary production economy in which finance and credit play a significant role. It relates to an economy, which has degrees of instability and prone to crisis. Inflation is a non-monetary phenomenon with a complex of causes including conflicts of the distribution of income. A set of policies follows, which are the focus of the contribution.

Yiannis Kitromilides turns attention to 'Deficit reduction policies, market credibility and market failure'. This contribution is concerned with two questions. First, is there any justification for the recent subordination of public policy making to market sentiment? Second, are markets 'rational' in the way they define policy 'credibility', or is there a 'market failure'? An example of market failure is when there is 'synchronised' fiscal austerity in a number of interconnected economies: if only one country adopts fiscal austerity measures the markets may consider this a 'credible' policy of deficit reduction; if a number of indebted countries adopt simultaneously fiscal austerity measures the markets may no longer consider fiscal austerity as a 'credible' deficit reduction policy. Ultimately, the adoption of deficit reduction policies in order to 'appease' the financial markets may in fact be counterproductive.

'From wage suppression to sovereign debt crisis in Western Europe: who pays for the costs of the crisis?' is the theme of Özlem Onaran's contribution, who argues that the crisis laid bare the historical divergences within Europe, and transformed the global recession into a European crisis. The focus is on the diverging outcomes of the crisis and policy response in Europe, with careful attention on the distribution of the costs of the crisis and labour market outcomes. What we are going through is a crisis of extreme inequality in distribution, which unfolded as a financial crisis, and was tamed via major banking rescue packages and fiscal stimuli. The hegemonic narrative is now re-labelling the crisis as a 'fiscal crisis'. However, the push for public debt reduction as the major target of macroeconomic policy is the biggest threat to a continuous recovery.

'The institutional dimension of the new economic policy' is pursued by Jesus Ferreiro and Felipe Serrano. In a world of rational expectations, aggregate demand is not so relevant and it also downgrades the relevance of institutions in the economic analysis and policy. Only when the assumption of rational expectations is relaxed would it be possible to introduce institutions and policies in the analysis. Once the existence of fundamental uncertainty is recognised, both the importance of aggregate demand and the role of institutions in the economy are radically revised. Institutions must be required and designed to reach a full employment level of economic activity. A well-designed institutional framework is a necessary condition to warrant the existence of that outcome and to help to implement macroeconomic policies that allow reaching and maintaining this objective.

In the contribution that follows, entitled 'Peripheral Europe's debt and German wages: the role of wage policy in the Euro area', Engelbert Stockhammer argues that German wage suppression is at the root of the crisis of the euro system. The culprit is not the Greek debt crisis. It is rather the German export surpluses that are a critical part of the story. Germany has pursued a policy of aggressive wage restraint resulting in large current account surpluses. Contrary to popular prejudice, German gains in competitiveness (since EMU) have not been founded on superior technological performance, but on more effective wage suppression. The paper argues that the Greek sovereign debt crisis has laid bare fundamental flaws of the architecture of the Euro system. Consequently, an urgent rewriting of the Euro area rule book is desperately needed.

In ‘A critical assessment of the financialisation process and its impact on the US labour force during the great recession’, Aurelie Charles and Giuseppe Fontana analyse two main features of the financialisation period: the replacement of the ‘originate and hold’ banking model with the ‘originate and distribute’ banking model, and the securitisation process of structured finance products. The first part of the paper looks at the potential role of these shattering changes together with inadequate governance arrangements and relaxed supervision by regulatory authorities in causing the current financial crisis and great recession. In the second part, the paper discusses some not well-known effects of the great recession in the USA, namely gender and ethnic stratification of the US labour force. It concludes that the great recession has been neither race nor gender neutral.

Finally, John Weeks in ‘Countercyclical policy for Africa: institutional and economic feasibility’, analyses the feasibility of countercyclical policy in developing countries with a focus on the sub-Saharan region. First, a general analytical framework for designing such policies is presented. Then, an assessment of the availability of policy instruments in Africa for countercyclical intervention is provided. It is concluded that for most of these countries the institutions for effective monetary policy do not exist. On the basis of this, the paper proposes a fiscal stimulus tailored to the conditions and constrains of these countries. Within these constraints, for a majority of the countries the fiscal expansion could be financed domestically, while other countries governments would require external funding. For about a fifth of the countries would a stimulus not be appropriate.

We would very much like to thank the authors for their contributions. We would also wish to thank the editors of the journal, and their staff, who have been extremely supportive throughout the life of this project.