

**IMPOSING THE NEOLIBERAL ORDER.
FOUR HISTORICAL CONFIGURATIONS
(US, Europe, Japan, and Korea)
Preliminary draft**

Gérard DUMÉNIL and Dominique LÉVY
MODEM-CNRS and CEPREMAP-CNRS

Version: September 5, 2001.

Address all mail to : CEPREMAP-ENS, 48 bd Jourdan, 75014 Paris, France.
Tel : 33 1 43 13 62 62, Fax : 33 1 43 13 62 59
E-mail : dominique.levy@cepremap.cnrs.fr, gerard.dumenil@u-paris10.fr
Web Site : <http://www.cepremap.cnrs.fr/~levy/>

RÉSUMÉ

IMPOSER L'ORDRE NÉOLIBÉRAL QUATRE CONFIGURATIONS HISTORIQUES (États Unis, Europe, Japon, Corée)

Il faut voir dans l'apparition du néolibéralisme au début des années 1980 un acte politique, de la part d'une classe dirigeante de propriétaires capitalistes, dont la domination s'était trouvée sensiblement limitée depuis la Seconde Guerre mondiale, et dont les revenus avaient été considérablement diminués pendant la crise structurelle des années 1970. Aux États-Unis et en Europe, ce nouvel ordre social fut mis en place dans les conditions qu'avait créées la crise structurelle, faisant suite à la baisse du taux de profit. Le premier choc fut la montée des taux d'intérêt en 1979 ; le second, la transformation des structures de financement des sociétés et du gouvernement d'entreprise, et la libéralisation de la mobilité internationale des capitaux. Le cadre institutionnel propre à l'Europe (intervention étatique, rôle du crédit dans le financement de l'accumulation...) était déjà sensiblement différent de celui prévalant aux États-Unis, et les coûts du néolibéralisme furent plus élevés en Europe. Le néolibéralisme fut imposé à des économies comme celles du Japon et de la Corée, où les conditions de la crise structurelle atlantique n'existaient pas, et dont les cadres institutionnels étaient tout à fait particuliers (intervention encore plus étendue de l'État, rôle des crédits bancaires et relations banque-entreprise spécifiques). Ces pays firent front avec assez de succès au choc des taux d'intérêt au début des années 1980, mais furent affectés par la transformation des structures financières. Cependant, le Japon et la Corée furent touchés dans des circonstances distinctes, notamment en ce qui concerne les tendances sous-jacentes de la technique et de la répartition. Le Japon stagne dans une crise durable, alors que la Corée s'est rétablie rapidement. Mais beaucoup est encore à venir.

ABSTRACT

IMPOSING THE NEOLIBERAL ORDER. FOUR HISTORICAL CONFIGURATIONS (US, Europe, Japan, and Korea)

The emergence of neoliberalism in the early 1980s must be interpreted as a political move of the ruling class of capitalist owners, whose dominance had been subjected to significant limitation since World War II, and whose income had been considerably diminished by the rise of inflation during the structural crisis of the 1970s. This new social order was implemented in the US and Europe, under the conditions created by the structural crisis, following the decline of the profit rate. The first shock was the rise of interest rates in 1979 ; the second, the transformation of the patterns of financing of corporations and corporate governance, and the liberalization of the international mobility of capital. The institutional framework prevailing in Europe (state intervention, role of credits in the financing of accumulation...) was already different from that characteristic of the US, and the costs of neoliberalism were larger in Europe. Neoliberalism was imposed to economies like Japan and Korea, where the conditions of the Atlantic structural crisis did not prevail, and whose institutional frameworks were quite specific (even larger state intervention, roles of bank loans and specific bank-enterprise relations). They faced rather successfully the interest rate shock of the early 1980s, but were considerably upset and hurt by the transformations of financial structures. Still, Japan and Korea were affected in circumstances largely distinct, notably with respect to the underlying tendencies of technical change and distribution. Japan stagnates in a lasting crisis, whereas Korea recovered rapidly. But there is obviously more to come.

MOTS CLEFS : Néolibéralisme, finance, tendance, changement technique, crise, instabilité financière, États Unis, Europe, Japon, Corée.

KEYWORDS : Neoliberalism, finance, tendency, technical change, crisis, financial instability, United States, Europe, Japan, Korea.

J.E.L. Nomenclature : E00, E3.

This paper is a preliminary draft. References to the existing literature will be added in a future version.

Introduction

A major change occurred within the main capitalist countries at the end of the 1970s, and the contrast is sharp between the rules prevailing during the first decades after World War II and the last two decades. The emphasis is often placed, in the literature, on globalization, and there is no denying the fact that the internationalization of capital—a long trend in the history of capitalism—reached new degrees, and is presently manifested under new forms. One must, however, be careful in the reference to globalization since the notion is used to camouflage the true nature of the transformation which marked the transition between the 1970s and 1980s, *the imposition by ruling classes of a new social order: neoliberalism*. The globalization of markets is only one of its components, and is presently used as a tool to spread the new neoliberal order to the entire planet.

During the 1970s, the major capitalist countries excluding Japan, entered into a structural crisis. This crisis followed a period of decline of the profit rate, resulting from the gradual deterioration of the performances of technical change (declining growth rates of labor productivity and falling productivity of capital). Besides these poor technical achievements, this crisis was marked by the slowdown of accumulation and growth, a wave of unemployment, large macroeconomic instability (overheatings and recessions), and soaring inflation. The traditional Keynesian policies were first implemented, but only attenuated the effects of the crisis.

The assertion of neoliberalism must be interpreted as a political move. The dominance of owners had been considerably weakened by the social order established, domestically and internationally, after the Great Depression and World War II (the expression of the “New Deal coalition” in the US), with a large intervention of the state, and the *managerial* features of capitalism seemed rather well established in the 1960s. The crisis (the fall of profit rates) and the rise of inflation (which devalues securities) pushed the real income of the holders of securities to the floor, or even transformed their gains into losses, and diminished their wealth. A gradual but very powerful reaction developed, culminating in the change in monetary policy, in particular the rise of interest rates, the *1979 coup*, initiated in the US by the president of the Federal Reserve at the end of the Carter administration, accompanied by a set of deregulations and reregulations, the assault on the worker movement, etc. The emblematic figures of neoliberalism were Margaret Thatcher in the UK and Ronald Reagan in the US. This new order proved immediately very profitable to ruling classes, even at the trough of the crisis, *i.e.*, during the 1980s. Interest rates were extremely high, dividends abundantly distributed in spite of low profits, and the stock market soared. The cost was huge for other classes: prolongation of unemployment, in particular in Europe, stagnating wages and attacks again the welfare state, overindebtedness, crisis of the Third World debt, etc.

Gradually the new neoliberal order was spread throughout the planet. Rapidly, the model reached Europe, and the resistance to the dismantling of social protection resulted

in the hybrid combination characteristic of the “social-neoliberalism” à la Blair or Jospin. Japan was hit by neoliberalism in the mid-1980s (despite its large efficiency, an object of great concern in the US). In Asia and Latin America, the debt / financial crises of the 1980s and 1990s provided the economic pressure for the imposition of the neoliberal order.

The “conditions” in which neoliberalism was imposed to the various countries and the actual transformations differ considerably. Two basic components must be emphasized :

1. The institutional frameworks characteristic of these various countries were not the same.¹ The state played a central role, even in the US, but to degrees and through mechanisms significantly different from those prevailing in Europe or Asia. The organization of the financial sector and its relationship to the nonfinancial economy were specific. The reliance on bank loans in the financing of firms was largely unequal. Countries like Europe and, even to a larger extent Japan and Korea, relied heavily on bank loans, with low real interest rates, a pattern of financing very favorable to accumulation. The labor market was not functioning along the same rules, and social protection also varied in degrees and mechanisms. These features, and others, have often been discussed.
2. Crucial to the impact of neoliberalism were also the long-term trends of technology and distribution, as well as the occurrence (its forms, timing...) of the structural crisis. As recalled above, the rise of neoliberalism followed, in the US and Europe, from the deterioration of the conditions of technical change and the ensuing crisis (in its real and financial components). The situation was significantly different in Asia. The structural crisis cannot be blamed on neoliberalism in the US ; neoliberalism prolonged the crisis in Europe ; its responsibility is even larger in Asia, though in combination with other factors whose importance is difficult to assess.

This paper does not purport to provide a comprehensive analysis but suggests a possible framework of analysis and hypotheses for future research. The approach is limited to basic stylized facts, which, we believe, may contribute to the discussion of the international extension of neoliberalism. It must be understood as an attempt to refute the neoliberal creed : (1) the US is the leading neoliberal country ; (2) its growth is rapid, faster than in other advanced capitalist countries ; therefore (3) neoliberalism means investment (capital accumulation) and growth ; (4) the crises of the 1990s are the result of still limited or imperfect implementation of neoliberalism ; (5) other countries must emulate the US. Major questions are pending. Why European and Japanese growth rates were inferior to those prevailing in the US during the 1990s? Why was Europe more and durably hurt in terms of unemployment? Why Japan was still considered at the end of the 1980s a threat to US world supremacy, and suddenly fell into a lasting depression in the 1990s? Why was the booming Korean economy suddenly destabilized? What were the comparative roles of inherent weaknesses and international factors? Would a stricter adherence to neoliberalism remedy or increase the risk of instability? Etc.

The paper divides into three sections. Section 1 is devoted to the conditions which led to the structural crisis of the 1970 in the US and Europe, the major features of the crisis, the neoliberal revolution, and a discussion of the different impacts of neoliberalism in the US and Europe. The second section compares these trends and developments as observed in these countries to Japan : trends, institutional frameworks, neoliberal reforms, and the crisis of the 1990s. The third section is an attempt to introduce Korea into this broad fresco.

1. As we have shown in various studies, what we denote here as “institutional frameworks” refers to specific configurations of relations of production and class hegemonies and compromises.

1 - The Atlantic bloc under US hegemony

Section 1.1 documents the similar profiles of technological and distributional changes in the US and Europe, in particular the decline and subsequent recovery of the profit rate. Section 1.2 discusses the unequal burdens financial costs placed on accumulation in each area. Section 1.3 imputes these differences, and the relative US advantage, to the distinct patterns of financing of accumulation. Section 1.4 recalls some of the basic features of the financial crisis in the US caused by neoliberal policies, and how the US economy was able to surmount them. Section 1.5 restates the major conclusions.

1.1 Technology and distribution : Decline and recovery

The historical profiles of technical change have been strikingly similar in the US and Europe since the 1960s. Both units experienced comparatively large growth rates of labor productivity in the first decades after World War II and the well-known productivity slowdown beginning in the late 1960s or the mid-1970s. Beginning in the 1960s, both units of analysis experienced a decline of the productivity of capital (the ratio of output to the stock of fixed capital) up to the mid-1980s.

A similar parallelism is observed concerning distribution. In these countries, the growth rate of the cost of one hour of labor diminished gradually from the 1970 onward. In spite of this moderation, the profit rate plunged during the 1980s as shown in figure 1. Then, a recovery was observed, even larger in Europe than the US, back to the levels of the 1960s. This upward trend reflects simultaneously the rise of the productivity of capital and the larger growth rate of labor productivity in comparison to the growth rate of the labor cost (*i.e.*, a rise of the share of profits).

The decline of the profit rate had important consequences on growth. As shown in figure 2, the rate of accumulation (the growth rate of the stock of fixed capital) diminished considerably into the 1980s. It now fluctuates at levels significantly below those reached in the 1960s, even in the US. (The growth rates reached in 1999, in this latter country, levels corresponding to the average rates of the 1960s, but below the peaks of the 1960s, and it is already clear that this point will remain a peak.) The US grew more rapidly than Europe from the mid-1980 onward.

<i>Rate of accumulation (yearly average, %)</i>				
	<i>60s</i>	<i>70s</i>	<i>80s</i>	<i>90s</i>
Europe	5.3	3.6	2.2	2.3
USA	3.6	3.5	2.7	2.4

The financial groups which directed the neoliberal revolution claim that they are at the origin of this new course, having provided the stimulus for the improvement of profitability records, in particular : (1) imposing wage moderation, labor discipline and flexibility ; (2) opening the planet to the expansion of capital ; (3) stimulating top management by astounding financial inducements ; (4) imposing high norms of profitability ; (5) helping to the promotion of a new pattern of financial relations and fusions. There is nothing

Figure 1 Profit rate (%): Europe (----) and the United States (—)



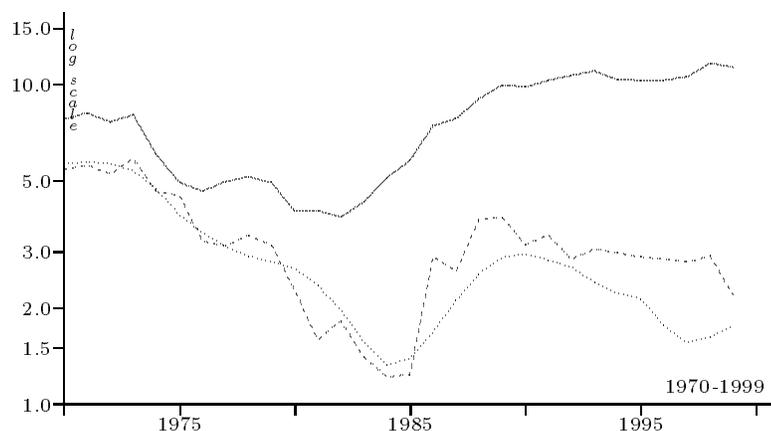
Europe refers here to three countries: France, Germany, and United Kingdom. The unit of analysis is the *private economy*. The profit rate relates a broad estimate of profits (production minus the cost of labor) to the stock of fixed capital. Both variables are net of depreciation. Therefore, taxes, interest and dividends paid are still included within profits.

Figure 2 Rate of accumulation (%): Europe (----) and the United States (—)



The unit of analysis is as above. The rate of accumulation is the growth rate of the stock of fixed capital. Both variables are net of depreciation. The series have been slightly smoothed in order to abstract from short-term fluctuations.

Figure 3 Rate of profit before the payment of interest and dividends (—), rate of retained profits (after these payments) (-----), and accumulation rate (.....) (%): France, nonfinancial corporations



The *accumulation rate* is the growth rate of the stock of fixed capital, net of depreciation. Profits, in both definitions of the profit rates, are divided by net worth. This figure uses a logarithmic scale on the vertical axis, and the distance between the curves is, thus, proportional to the ratios among the various rates. The burden of interest and dividends payments is measured by the distance between the two series (-----) and (—).

Figure 4 Ratio of the net debt to tangible assets (%): France (---) and US (—), nonfinancial corporations



The net debt is the total debt minus monetary and financial assets; tangible assets are the sum of the fixed capital stock and inventories.

obvious in these respects. These new trends are, to a large extent, technical and managerial achievements, and it would be necessary to discuss here what could have been the potential alternatives to neoliberalism. A refutation of these neoliberal claims trespasses the limits of the present study.

1.2 Accumulation and the burden of financial costs

A first puzzle is the divorce between the recovery of profit rates as in figure 1 and the comparatively sluggish rates of accumulation, as in figure 2, in particular in Europe. A more detailed analysis shows its relationship to the distribution of profits as interest and dividends. Real interest rates were about zero during the 1970s as a result of inflation and rather stable nominal rates. First, as recalled in the introduction, real interest rates suddenly soared to about 5%, and despite recurrent declines when the economy enters into a recession, they tend now to fluctuate around such levels (figure 9). Second, as profit rates recovered, larger fractions of profits were paid out as dividends (from about 30% in the 1970s to 60% in the 1990s). These flows are important, since investment is actually very dependent on the profits retained by firms.

Figure 3 illustrates these relationships between various measures of profit rates and accumulation for French nonfinancial corporations. The first series (—) shows a first measure of profit rates: the ratio of profits after all taxes, but *prior* to the payment of interest and dividends, to the net worth of corporations (total assets minus debt). The recovery of the profit rate appears strikingly in this measure. The second series (-----) is the same profit rate but *after* interest payment and the distribution of dividends. It also accounts for the devaluation of debts by inflation.² In this new measure, the benefit of the recovery vanishes. The third series (.....) is the rate of accumulation (the growth rate of the stock of fixed capital net of depreciation). Its profile is very similar to that of the rate of retained profits. Thus, it appears that the potential benefits of the underlying recovery of the profit rate have been largely offset by the transfer of profits to financial institutions and individuals. (The financial costs of enterprises are the incomes of other agents.)

The same analysis can be made for the US with converging results, although the burden of financial costs is less dramatic.

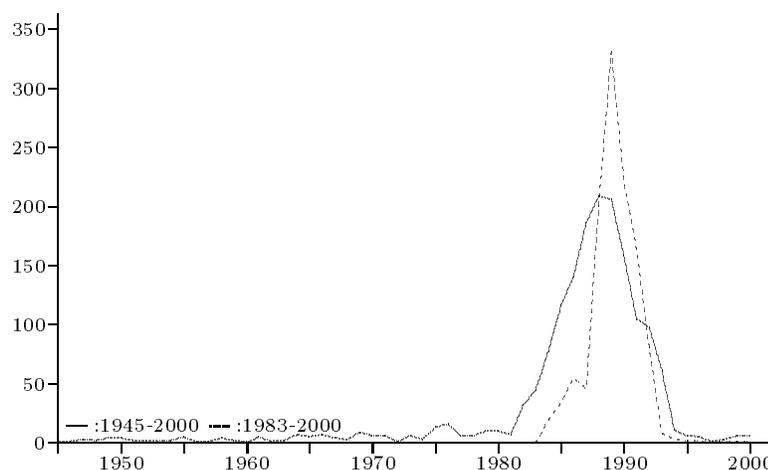
1.3 Growth and unemployment: Crisis in Europe

Both in terms of growth and unemployment the structural crisis of the 1970s hurt less severely the US economy than the European economy. Two factors combined their effects:

1. The *1979 coup* affected more the European economy, in particular a country like France, because enterprises were financing their investment on borrowings. Between 1970 and 1985, new loans contributed to nearly 60% of the total needs of French corporations to finance their expansion. (The issuance of new shares was nearly negligible, and the remaining

2. Borrowers repay amounts representing a purchasing power diminished by inflation. This is at the origin of a transfer of wealth from lenders to borrowers which compensate to some extent for the payment of interest. The direction of the overall flow can be reversed if the real interest is negative. Enterprises are simultaneously borrowers and lenders (and holders of financial assets also devalued by inflation). Their net debt is at issue.

Figure 5 FDIC-insured commercial and Savings banks (—) and Savings and loans associations (-----) that were closed or received FDIC assistance : US



FDIC : Federal Deposit Insurance Corporation

40% were self-financed.) French corporations were, and are still, more in debt than US corporations. This is demonstrated in figure 4, which shows the ratio of the net debt (total debt minus monetary and financial assets) to tangible assets of nonfinancial corporations in France and in the US. These observations explain why the burden of high interest rates was quite larger in France than in the US. French corporations attempted to get out of debt, in particular during the 1990s (rates of self-financing were above 100%, *i.e.*, total debts were diminishing), but with limited success. This situation sharply contrasts with that observed in the US, where corporations reduced the burden of their net debt to very small amounts. This is a crucial factor of the diverging performances concerning accumulation and growth, and one factor in the explanation of the more severe and lasting unemployment in France. Countries where loans played traditionally important roles in the financing of accumulation were, and are still, severely hurt by neoliberalism.

2. The large unemployment rates observed in Europe in comparison to the US also reflect the comparative rates of growth of labor productivity or of the *capital/labor ratio*, significantly larger in Europe than in the US. A same accumulation of capital generates less and less employment due to technical change in both area, but to degrees significantly larger in Europe than in the US. This factor adds to the above. It cannot, however, be imputed to the rise of neoliberalism.

1.4 Financial crisis at the center

The process of deregulation and reregulation characteristic of neoliberalism, accompanied by the rise of interest rates and its devastating effects on fractions of the US economy and the Third World created the conditions of a major financial crisis in the US : the multiplication of bankruptcies within the banking system and the *Savings and loans associations* crisis in the early 1980s (figure 5).

Two types of phenomena explain the absence of financial panics :

1. The state intervened strongly to bail out the financial system, in particular by injecting large amounts of money into the institutions in charge of the insurance of deposits.
2. The dollar is the world currency and enjoys what is often denoted as a position of *seigniorage*. This is apparent in the large external deficits which developed in the US from the early 1980s onward. Such imbalance of external accounts would have provoked a rush on any money, with the exception of the dollar. In sharp contrast, European countries are consistently subject to a strict external constraint.

1.5 The neoliberal shock in the US and Europe

The followings must be emphasized :

1. The new neoliberal order was imposed in the US and Europe in the wake of a decline of the profitability of capital, in a situation of structural crisis.
2. It is difficult to date these events with precision, but everywhere the crisis was long and considerably affected the various economies and societies, with real as well as monetary and financial components.
3. The underlying factors of the crisis were as severe in the US than in Europe, but the neoliberal shock hurt less the US than Europe. This was basically due to the distinct patterns of accumulation, notably the unequal reliance on borrowings in the financing of firms. The hegemonic position of the dollar also contributed to the ability of the US to take advantage of the new social order.
4. In spite of these differences, the new trends of technical change and distribution, favorable to capital, are of comparable size in Europe and in the US. The permanence of unemployment in Europe is due to slower accumulation and more rapid substitution of capital for labor in Europe.

2 - Decadence of the Japanese model ?

Section 2.1 is devoted to the challenge that the rapid growth of Japan represented for the US economy, further increased by the fact that these performances were obtained within a significantly different institutional framework. Section 2.2 compares the Japanese and US economies with respect to technical change and profitability. Although the outstanding results obtained by Japan prior to 1975 were significantly eroded after this date, this deterioration was not interpreted in terms of crisis, up to the 1990s. Section 2.3 documents financial aspect of these evolutions. Since the *1979 coup* and up to the 1990s, real interest rates are high and the transfer in favor of nonfinancial corporations has been considerably diminished. The impact of neoliberalism is also evident in the ephemeral transformation of the pattern of financing in the late 1980 which introduced to the crisis. Section 2.4 summarizes these elements.

2.1 The Japanese challenge

In the 1970s and 1980s, the Japanese economy was doing so well, in particular in comparison to the US economy (notably at the beginning of the 1980s), that it was perceived as a rival, a threat to US dominance. Many analysts had already declared the demotion of the US economy, and the future obviously belonged to the Japanese model. Indeed, the performances of Japan had been, and were still, outstanding concerning growth, labor productivity, international trade... This assessment did not survive, however, the end of the 1980s, when Japan entered a severe and lasting crisis.

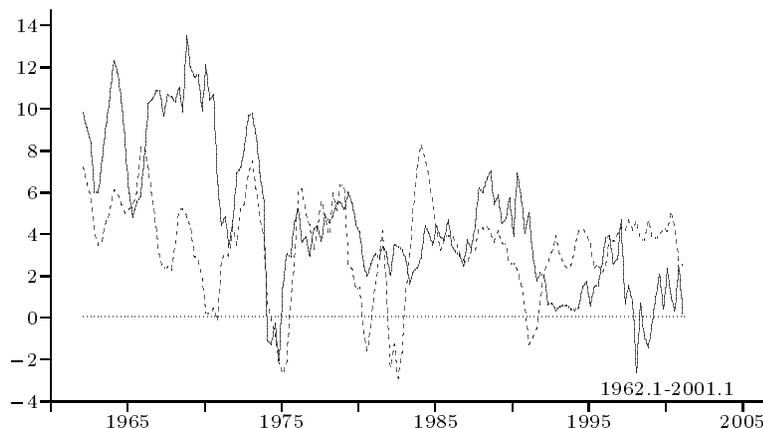
At the end of World War II the Japanese technology was comparatively backward (considerably less mechanized). In 1950, the capital-labor ratio was equal to 3.2 thousands dollars per worker in this country, to be compared with 25.7 in the US. At a quite extraordinary rhythm, Japan caught up with US technology, at least within some sectors of the economy (such as Manufacturing industries). A large surplus of the balance of trade appeared during the first half of the 1980s (about 2.5% of GDP) and was maintained throughout the 1990s to the present.

During the 1960s Japan grew at truly amazing rates, and growth remained strong after the recession of 1974-1975 although less dramatically superior to the growth of the US economy than previously. This is shown in figure 6, which compares, for the two countries, the growth rates of GDP for each quarter vis-à-vis the same quarter one year earlier (thus, yearly growth rates are considered). Typical of the US is the fall into the 1980 and 1982 recessions and the surge in 1983. At the end of the 1980s, the two economies were growing substantially, although the Japanese rates were larger, before and just after 1990. Then, the US plunged into the recession of 1990-1991, and the growth rate of Japan began its gradual decline. Finally, the contrast is large between the courses of the two economies during the 1990s. As the US recovered strongly (up to the recession of 2000), Japan stagnated close to 0, with the exception of the short-lived recovery of 1996. This picture is fully confirmed by an examination of the capacity utilization rate of Manufacturing industries which declined in Japan by about 10% of its value between the 1980s and 1990s. Note that such a decline is usually characteristic of "short" recessions, and not maintained during a decade. This is an important indicator of the specific character of the crisis of the 1990s in Japan.

<i>Rate of growth (yearly average, %)</i>			
	62/74	75/92	93/2000
Japan	8.2	3.8	1.3
USA	4.1	2.3	3.8

The spectacular performances of the Japanese economy were obtained within an institutional, policy, and political context quite different from that prevailing in the US. It has been often described: a large involvement of the state (including a large public sector), a quite specific financial system tightly connected to industry, a very limited role of the stock and capital markets, an also specific management of labor relations, etc. To even larger degrees than in Europe, the fact that such performances were achieved in a context so different from the US, added to the potential threat for the dominant economy. Since the crisis of the dollar in 1973, the Japanese economy was under attack, for example the (now flexible) exchange rate was largely manipulated and a constant pressure was placed

Figure 6 Yearly growth rate of output for each quarter (%): Japan (—) and US (-----)



The variable is the growth rate of each quarter in comparison to the same quarter one year earlier.

by the US concerning international trade. From the first years of the emergence of neoliberalism, and despite the prosperity of Japan during the 1980s, new trends became evident within the Japanese economy, and the crisis of the 1990s is now hastily interpreted, within neoliberal circles, as the demonstration of the superiority of the neoliberal model—a very questionable assertion.

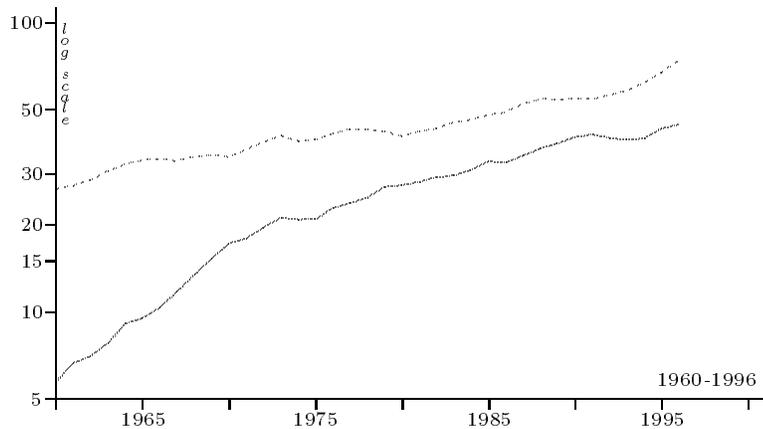
2.2 Technology and profitability

The catching-up of Japan with the US concerning labor productivity is well known. It is dramatically illustrated in figure 7 for Manufacturing industries.³ One can notice that, as the series for Japan moved gradually closer to that of the US, Japan also experienced the famous *productivity slowdown*, although the growth rates of labor productivity remained larger up to the 1990s. During this last decade the performances of Japan were affected, in addition to the effects of technical change *per se*, by the decline of the capacity utilization rate. The productivity of labor as measured in figure 7 is the gross product per *worker*. In this measure, the growth rate of labor productivity appears larger in the US during the last years of the series because of the rise of the number of hours worked by each worker.

Figure 8 shows the movement of the productivity of capital in Japan and the US, also within Manufacturing industries. Productivity is defined as the ratio of gross output to the gross stock of fixed capital in current yens or dollars. To our knowledge, it is not possible to compare consistently the productivity of capital in these two countries using other definitions (such as variables net of capital depreciation), and even in the definition used here the series cannot be prolonged to recent years. The two profiles appear strikingly

3. This is where the comparison is the most relevant, since the two countries basically compete within international markets concerning the output of their Manufacturing industries. The heterogeneity between Manufacturing industries and the rest of the economy is particularly large in Japan.

Figure 7 Labor productivity (\$ 1990): Manufacturing industries in Japan (—) and in the US (-----)



Labor productivity is gross output in volume per worker. Because of the use of purchasing power parity indexes the levels can be compared to some extent.

Figure 8 Productivity of capital: Manufacturing industries in Japan (—) and in the US (-----)



The productivity of capital is the ratio of gross output to the gross stock of fixed capital in current yens or dollars.

similar, concerning levels and trends. Again, the sharper decline in Japan from 1990 onward is partly the effect of the decline of the capacity utilization rate.⁴

The combination of figures 7 and 8 reveals that the rise of labor productivity in Japan and the US—the *technical catching-up*—was achieved at the cost of a sharp increase in the amount of fixed capital (mechanization). We denote such a trajectory a *pattern à la Marx*, referring to Marx’s analysis of historical tendencies in Volume III of *Capital*. These features of technical change are characteristic of both countries in spite of their differences. There is nothing exceptional in this profile of technical change in Japan, except the rapidity of the growth of labor productivity, in particular up to 1975. More research will be needed to determine the causes and consequences of the trends of the productivity of capital during the 1990s, a prolongation of earlier trends in Japan, which have been inverted for the total US and European economies. These observations do not question, in any respect, the performances of the Japanese economy prior to the implementation of neoliberalism.

Due to the limitation of data, in particular the absence of a series for net capital, it is not possible to determine a profit rate for Japan directly comparable with the one shown for the US in figure 1. One can surmise from the observation of the above variables and others, that the profit rate in Japan, in particular within the Manufacturing industries, displays a downward trend, with a sharp decline in the early 1970s, then a relative stabilization up to 1990, and finally a new decline—simultaneously a factor and an effect of the crisis.

The fall of the profit rate in Japan around 1970 was followed, as in the US and Europe, with distinct timing and profiles, by a large decline of rates of accumulation and growth (figure 6). This break in the growth of the Japanese economy was not interpreted as a structural crisis because of: (1) the absence of recessions in the early 1980s; (2) the still significant values of these growth rates; (3) the absence of unemployment. Japan actually confronted rather successfully this decline of its profit rate up to 1990.

2.3 Financial disruption

The analysis of the transformations of the US and European economies which are the expression of the spreading of the new neoliberal order has clearly demonstrated the importance of financial mechanisms: the transfer of profits to capitalist owners (interest and dividends) and the corresponding impact on accumulation, and the change in the pattern of financing of corporations.

Like the US and Europe, Japan had to confront the rise of real interest rates. Figure 9 shows the variations of real interest rates in Japan and the US. The similarity of the profiles is striking. In both countries, real interest rates were very small or even negative before the *1979 coup*, and rose sharply. Although interest rates are manipulated along the phases of the business cycle, they tend to remain high. Japan is no exception in this respect, with the proviso that the “recession” appears now ten years long (abstracting from the ephemeral and partial recovery). Real short-term interest rates declined gradually from

4. These observations for the US economy might appear contradictory with the rise of the productivity of capital for the total economy since the mid-1980s, mentioned in section 1.1. Actually, the data for the US Manufacturing industries, consistent with those used in figure 1, show that the productivity of capital for Manufacturing industries displays a profile identical to that in figure 8, declining and then horizontal from 1982 to 1999. There is large difference between the profiles observed for the total economy and Manufacturing industries.

Figure 9 Real long-term interest rates (%) : Japan (—) and the United States (-----)



Real rates are equal to nominal rates minus the inflation rate (the GNP deflator of the country).

the early 1990s onward, but real long-term interest rates remained high during the first half of the 1990s, a factor which contributed to the aggravation of the crisis. The fall of interest rates, after 1995, has not been reversed, but real rates tend to rise again due to deflation.

Like in the US and Europe, the rise of real interest rates had consequences on profit rates. It is possible to provide a measure of this effect, using a data set for nonfinancial corporations based on *enterprise* accounting.⁵ Figure 10 shows two measures of the profit rate for Japanese corporations: (1) prior to the payment of interest and dividends (the net flows) and to the correction for the devaluation of debts by inflation (accounting for a transfer of wealth from lenders to borrowers potentially compensating for the payment of interest); (2) considering these flows. The discrepancy between the two series can be interpreted as an indicator of the burden placed on the profitability of corporations by the distribution of profits.

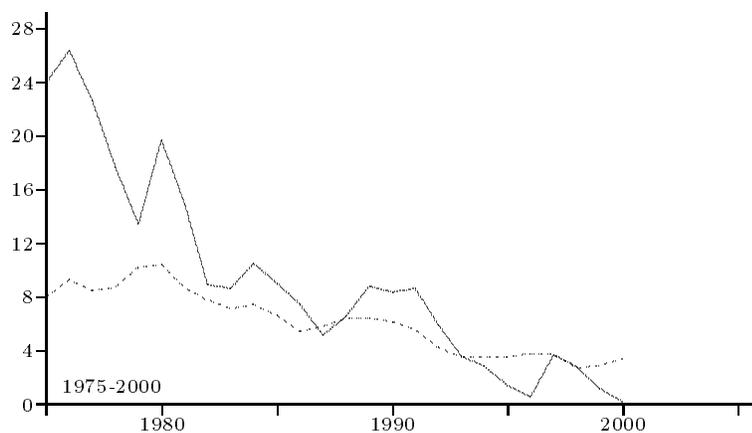
Figure 10 documents the effect of the *1979 coup*:

1. Prior to the early 1980s, low interest rates and large inflation rates resulted in negative real interest rates and were at the origin of a transfer in favor of nonfinancial corporations.
2. The rise of real interest rates at the end of the 1970s considerably reduced this dramatic transfer.
3. One can also notice, that up to 1993, the transfer remained favorable to nonfinancial corporations. This suggests that these corporations were not actually paying on their entire stock of debt the positive real rates displayed in figure 9, but lower rates, signaling favorable conditions of financing from the banking system or the state.

Thus, very favorable conditions were transformed into still favorable conditions, as neoliberalism added to the decline of the profit rate in Japan, like in the US and Europe. Because of the distinct nature of the relationship between the financial sector and

5. A problem is that fixed capital is measured at historical cost, instead of replacement cost as within national accounting frameworks.

Figure 10 Profit rates prior (-----) and after (—) the payment of interest and dividends, and the correction for the devaluation of debt by inflation (%): Japanese nonfinancial corporations



Profits are after all taxes, and the capital stock is the net worth of corporations. A correction is made for the depreciation of the net debt by inflation. The real interest rate (the apparent real rate of interest) was often negative, in particular during the late 1970s, and this explains why profit rates after the payment of interest and correction were often larger than the one prior to this payment.

Figure 11 Sources of external financing for Japanese nonfinancial corporations (%): ratio of new bank loans (—) and of the issuance of shares, bonds, and commercial paper (-----) to the stock of monetary and financial assets



nonfinancial corporations, and the intervention of the state, the consequences of this deterioration on accumulation rates were less severe in Japan than could have been expected. The astounding rates of accumulation characteristic of the 1960s belonged to the past, in relation to the decline of the profit rate and to the flows of bank loans, and this movement was considerably increased by the rise of real interest rates and the transformations of borrowing conditions, although growth rates remained larger in Japan up to the beginning of the 1990s.

The consequences of the attempt to graft the new patterns of corporate governance on the Japanese economy can also be observed. Figure 11 plots two series, the ratios to the stock of monetary and financial assets⁶ of: (1) new bank loans; and (2) the issuance of securities (stocks, bonds, and commercial paper) on the capital market. The following remarks can be made:

1. Up to the mid-1980s, one can observe the traditional reliance on loans from the banking system. In the 1960s, the flow of new loans represented about 3% of total financial assets, while the issuance of securities on the capital market only represented 0.5%. The decline of the rate for loans during the 1970s was the expression of the diminished rates of accumulation.
2. The issuance of shares, bonds, and commercial paper peaked during the second half of the 1980s, just prior to the crisis, signaling a new ephemeral reliance on the capital market — the irruption of neoliberal financial patterns in Japan. This movement was contemporaneous of the so-called “bubble” of the stock market — not coincidentally.
3. The series can also be interpreted as indicators of the size of the call to external financing (adding the two series): (1) large prior to 1975; (2) intermediary between 1975 and 1985; (3) rising during the movement toward the capital market from 1985 to 1989; (4) finally the general collapse of the two sources during the crisis. Note that the large growth rates in Japan around 1990 (figure 6), which coincided with the bubble (in the stock market and real-estate), was the first strong expansion financed along neoliberal lines: It disrupted the Japanese economy.
4. Because of the collapse after 1990, it is not possible to assess the possible survival of this new pattern of financing beyond the peak of 1990.

From other sources and studies, one can derive the consequences of the shock produced on nonfinancial corporations and on financial institutions by the combination of large real interest rates up to the crisis and the redirection of the financing of corporations in the wake of the bursting of a bubble that the new course had itself inflated. The effects of the accumulation of bad debts have often been described. The disruption of monetary and financial mechanisms reached such degrees that the traditional tools of monetary and deficit policies proved inefficient to stabilize the economy, as had been the case during the 1930s in the US and other countries.

6. It would have been more appropriate to relate these flows to the stock of fixed capital at replacement cost, but the series is not available.

2.4 The neoliberal shock in Japan

Japan accomplished, during the decades following World War II, an amazing process of catching-up with major capitalist countries: building a Manufacturing sector capable of competing with US industries, and reaching considerable levels of output as a result of exceptionally large growth rates. This was performed within a quite specific social framework.

After a sharp decline of its profitability during the second half of the 1970s, Japan had nearly stabilized its profit rate. The rise of real interest rates (in the early 1980s) did not upset the institutional configuration characteristic of Japan, with its tight connection between financial institutions and nonfinancial corporations. This configuration was destabilized during the second half of the 1980s, the second neoliberal coup on the Japanese economy with degenerated into speculation. This second blow was fatal and introduced to a lasting crisis.

There is an important difference between the first and second neoliberal coup. The first one, the rise of real interest rates in the early 1980s affected the Japanese economy in its former institutional framework, from outside, so to say. Large real interest rates were alien to this framework. On the one hand, it allowed Japan to protect itself, for example by pursuing a policy of differential interest rates in favor of industry; on the other, it represented a threat for the survival of the system. The second coup, the opening to national and international capital markets, modified this institutional framework from the inside. Combined with the rise of real interest rates, it radically upset the existing patterns of financing. It paved the way for the emergence of a new potentially very profitable financial sector, obviously open to international financial investment!

One can surmise that the crisis will have effects on technical change, similar to those observed in the US and Europe. The new tendencies, in particular the rise of the productivity of capital, in the US and Europe, followed lasting episodes of crisis, real and financial. The same will probably be true of Japan. The resistance of the Japanese economy to the imposition of the neoliberal order appears so large, that it is unclear, however, whether the recovery from the crisis will mean a new step forward in the gradual extension of neoliberalism to the planet, or suggest the contours of a more significant alternative.

3 - Korea: prosperity and crisis

Section 3.1 illustrates the outstanding performances of the Korean economy, concerning growth and technical change, and the evolution of foreign exchanges. No declining performances are apparent as is the case in Japan. Section 3.2 interprets the crisis of 1997 as the outcome of a “scissor effect”, stagnating profits and rising financial costs, multiplied by the extreme volatility of international capital flows. Section 3.3 summarizes these observations.

3.1 Growth, technical progress, and foreign trade

The performances of the Korean economy since the 1970s have been outstanding. As shown in figure 12, the growth rates of total output (GDP) fluctuated around 8% up to the 1997 crisis, and industrial production at rates even larger. Only one recession was observed in 1980. The rest of the time, the lowest annual growth rates remained above 5%, and thus superior to US and Japanese growth rates during the 1970s and 1980s. The growth rates prevailing during the decade preceding the crisis are lower than those attained during the previous decade, but only slightly. The last three years before the crisis were marked by a decline of growth rates, but fluctuations of this amplitude were usual.⁷ The capacity utilization rate within Manufacturing industries remained normal prior to the crisis. Indeed, the 1997-1998 recession was deep, but the economy shot up again in 1999, in particular within Manufacturing industries, before a new limited decline.

	<i>Rate of growth (yearly average, %)</i>		
	<i>70s</i>	<i>80s</i>	<i>90s</i>
Korea, GDP	7.5	8.7	6.2
Korea, Industrial production	15.9	11.4	8.5
Japan, GDP	4.5	4.1	1.4

The results obtained concerning technical change were also outstanding. Figure 13 shows the rise of labor productivity in Korea, as well as in Japan for comparison, for Manufacturing industries (actually “industries” in Korea). The growth rate of labor productivity appears strikingly strong, even in comparison to Japan and, obviously, the US. The years preceding the two recessions were not marked by any significant slowdown of the growth rate of labor productivity.

Unfortunately, due to the limited availability of data, it is not possible to discuss here, the profile of the productivity of capital and of the profit rate. It is sometimes contended that the share of profits was diminishing prior to the 1997 crisis. This is true of the total economy, but not for Manufacturing industries. It is, therefore, difficult to consider this inflection as a significant factor of the crisis.

Figure 14 documents the growth of foreign trade, exports and imports, expressed in constant dollars. The growth of exchanges was steady since the late 1970s and exchanges represented, up to the 1997 crisis, about 25% of GDP. The growth rate was slightly reduced during the two years preceding the crisis. (This slowdown disappears when exports are measured in constant won.) As figure 14 shows, the Korean economy was periodically subject to similar slowdowns without significant damages. A small deficit was manifested during these two years, but nothing dramatic is apparent. It is remarkable to notice, as is well known, that during the last decade before the crisis, exchange rates between the dollar and the yen manifested very sharp fluctuations. Such movements could have triggered a recession in a situation of macro instability, but no lasting deterioration of the capability to export of Korea was apparent.

7. It is sometimes contended that the recession began in 1995. First, the term *recession* is inappropriate. What is at issue is a limited decline of the growth rate. Second, as stated in the text, such fluctuations were observed in the Korean economy since 1971, with a surprising regularity. Only twice they introduced to actual recessions.

Figure 12 Growth rates of GDP (—) and industrial production (-----) (%) : Korea
 Growth rates of GDP (---) (%) : Japan

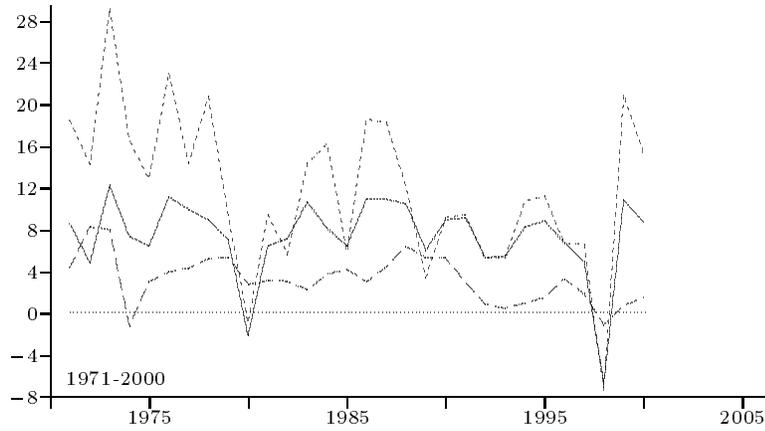
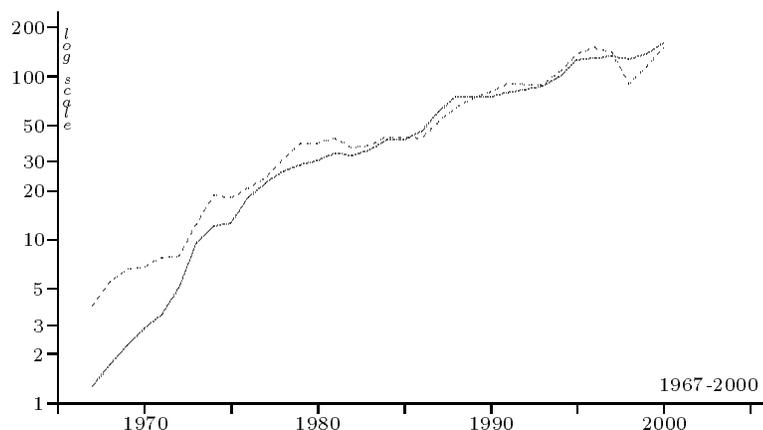


Figure 13 Labor productivity (\$ 1990 per worker, as in figure 7) : Industries in Korea (—) and Manufacturing industries in Japan (-----)



Labor productivity is value added per worker.

Figure 14 Exports (—) and imports (-----) (Billion \$ 1996) : Korea



3.2 Interest rates, corporate profitability, and foreign capital

The rise of interest rates within the major capitalist countries from 1979 onward did not destabilize the Korean economy. Before the opening to international finance, a large gap was maintained between domestic and international rates in Korea. As shown in figure 12, a recession occurred, however, in 1980, in a context considerably different from that of the 1997 crisis. The year 1980 was one of the last within a period of very large inflation rates and the economy was protected against financial turbulences (the variation of interest rates and capital flows) from outside. The economy operated in the framework, which has been often described, of large intervention of the state and specific relationships between the financial and nonfinancial sectors of the economy.

Enterprises simultaneously pay financial costs, such as interest, and received financial incomes, such as interest or dividends. They pay more than they receive, and we denote the net flow as *net financial costs*. Figure 15 shows the variation of the operating surplus of nonfinancial corporations and of their net financial costs (paid from this operating surplus), both series in constant wons. The following observations can be made:

1. The operating surplus of nonfinancial corporations grew steadily and rapidly since the recovery from the 1980 recession, though less rapidly than before. Beginning in 1996, the operating surplus stagnated. We will not discuss here the causes of this break, which can be interpreted as a manifestation of various inflections often mentioned in the literature, notably the rise of wages, the diminished growth of exports, the variations of the prices of exports, rising real-estate prices, etc. Further research would be required to assess their relative importance.
2. From the 1980 recession onward up to 1995, this growth was paralleled by that of net financial costs. However, the growth rate of net financial costs began to increase in 1996 and up to 1999. This movement is obviously linked to the new conditions of financing of corporations, rising real interest rates and short-term indebtedness, with the large international opening which has been often described.

Figure 15 Operating surplus (—) and net financial costs (-----) (Billions of wons of 1995) : Korean nonfinancial corporations



Figure 16 Ratio of net financial costs to the operating surplus: Korean nonfinancial corporations



3. Thus, between 1995 and 1997, Korean nonfinancial corporations were taken into a fatal “scissor effect”—a crucial element in the occurrence of the crisis. It is in this context of accelerated weight of indebtedness and sagging of profits that the first effects of the deteriorating situation were felt (in particular the failure of a number of *chaebols*). This figure shows very clearly the twofold nature of the deterioration, and this explains why the available analyses emphasize one or the other aspects of the crisis, or sometimes both: a combination of overinvestment (related to the stagnating profits prior to the net financial costs) and financial fragility, here manifested in the soaring net financial costs. (A more sophisticated description of the changes which occurred in the balance sheets of nonfinancial corporations would obviously be required to document the various aspects of these transformations⁸.)

Figure 16 shows the ratio of net financial costs to the operating surplus, another view of the same movements. The scissor effect is apparent in the rise of the ratio in 1995, 1996, and 1997, and the peak above 1 during the crisis in 1998, which means that net financial costs were larger than the operating surplus. Note that this ratio remained very high in 1999 (81%).

It is interesting to notice that the 1980 recession was accompanied by a similar growth of net financial costs, though the amplitude of the movement was less accentuated. The ratio also began to rise prior to the recession, peaked during the recession year, 1980, and remained high during the following years. An important difference is that operating surplus was rising.

3.3 The neoliberal shock in Korea

The “liberalization” of the Korean economy was gradual as in Japan. It affected banking activities, capital markets (first the stock market and later the bond market), etc. Not surprisingly, it resulted in a stock market and real-estate bubble, as in Japan (in the same years). The effect of the rise of real interest rates was superseded up to the mid-1990s, but finally felt in an economy, which like the Japanese economy (and to a lesser extent, the European economy), relied considerably on borrowings in the financing of its activity. The flows of international capital provided a volatile basis for the pursuit of this movement, in the new institutional context.

The argument that the crisis can be imputed to the incompleteness of the transition to neoliberalism is cynical, since the crisis can be, before all, imputed to the implementation of neoliberalism within a social framework, which had proven its efficiency, and was alien to the neoliberal order. Its effects were differed because of the gradual character of the transition, but finally felt. There is some truth, however, in this argument, if it means that neoliberalism is incompatible with the reliance on borrowings to finance growth. The cost of implementing it in economies where borrowings were crucial had always devastating consequences: in Europe as well as in Asia. The specific characters of the relationship between the lender and the borrower—the possible relaxation of the capital constraint—may add to the distance between a *self-financing* economy such as the US where the gains of the owners are the alpha and the omega, and a credit economy such as was the Korean economy, just like the free international mobility of capital can transform the management of an economy into a nightmare.

8. Independent of the availability of data, these evolutions are difficult to assess. For example, the rise of real-estate prices biased the balance-sheet ratios of corporations.

Conclusion : Neoliberalism, the Atlantic bloc, and Asia

The implementation of neoliberalism led to two successive distinct, though related shocks :

1. The first shock was the sharp rise of real interest rates at the beginning of the 1980s, following the rise of nominal rates in 1979 in the US. This shock was potentially more devastating in countries where the financing of firms was based on borrowings, in particular bank loans—as was not the case in the US.
2. The second shock was the transformation of the pattern of financing, and the opening to capital markets and international financial flows.

Due to specific institutional configurations (in particular state intervention, relationship between banks and nonfinancial corporations), countries like Japan and Korea supported the first shock successfully and delayed the second. This was not the case in a country like France which was directly hurt by large interest rates and a rapid transformation of the financing of its corporations (toward a self-financing economy). French corporations are, however, still fighting to get out of debt. The second shock reached Japan and Korea during the late 1980s and the 1990s, and the final issue is still unclear. It is hard to tell what pattern of financing will emerge in Japan when the crisis of the 1990s will be superseded. Korean corporations are still largely in debt despite the vigorous recovery which followed the 1997 crisis, and the alignment remains to be performed.

The emergence of neoliberalism must be analyzed as a class reaction to a structural crisis in the US and Europe. It is possible, though unclear, that Japan would have reached similar structural crisis conditions in the 1990s, independently of the rise of neoliberalism. It is also unclear what type of institutional adjustment and policy reaction a country like Japan could have implemented, if it had not been caught into the neoliberal global maelstrom. These structural crisis conditions were certainly not characteristic of Korea. Overall, seen from Asia, the conditions (the structural crisis and class struggle) which led to the introduction of neoliberalism in the Atlantic bloc appear anecdotal.

The consideration of Asian countries strengthens the argument that neoliberalism was not the unavoidable product of the deterioration of fundamental economic conditions. The US and European crises of the 1970s provided capitalist owners the opportunity to consolidate their dominance, under US hegemony, at home and throughout the planet.

Main sources

- OECD (Europe, USA, Japan, Korea) :
 1. National Accounts (II).
 2. Economic Outlook.
 3. International Sectoral Data Base (ISDB).
 4. Flows and Stocks of Fixed Capital.

- KOREA :
 1. Korea National Statistical Office, National Accounts (GDP, exports, imports, productivity index, industrial production) : <http://www.nso.go.kr/eng/>
 2. The Bank of Korea, Flow of Funds : http://www.bok.or.kr/index_e.html

- JAPAN :
 1. Economic and Social Research Institute (ESRI), National Accounts : <http://www.esri.cao.go.jp/en/sna/menu.html>
 2. Bank of Japan, Flow of Funds Accounts Based on 68SNA : http://www.boj.or.jp/en/siryo/siryo_f.htm
 3. Ministry of Finance, Financial Statements Statistics of Corporations by Industry : <http://www.mof.go.jp/english/ssc/historical.htm>

- USA :
 1. Bureau of Economic Analysis, National Accounts : <http://www.bea.doc.gov/bea/dn1.htm>
 2. Federal Reserve, Flow of Funds : <http://www.federalreserve.gov/releases/z1/current/data.htm>

- FRANCE :
 1. INSEE, National Accounts : http://www.insee.fr/fr/indicateur/cnat_annu/cnat_annu.htm
 2. Banque de France, Flow of Funds (Les comptes nationaux financiers) : <http://www.banque-france.fr/fr/stat/main.htm>

Contents

Introduction	1
1 - The Atlantic bloc under US hegemony	3
1.1 Technology and distribution: Decline and recovery	3
1.2 Accumulation and the burden of financial costs	6
1.3 Growth and unemployment: Crisis in Europe	6
1.4 Financial crisis at the center	7
1.5 The neoliberal shock in the US and Europe	8
2 - Decadence of the Japanese model?	8
2.1 The Japanese challenge	9
2.2 Technology and profitability	10
2.3 Financial disruption	12
2.4 The neoliberal shock in Japan	16
3 - Korea: prosperity and crisis	16
3.1 Growth, technical progress, and foreign trade	17
3.2 Interest rates, corporate profitability, and foreign capital	18
3.3 The neoliberal shock in Korea	21
Conclusion: Neoliberalism, the Atlantic bloc, and Asia	22
Main sources	23