

Beyond living with capitalism: the Labour Party, macroeconomics, and political economy since 1994

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In 1994 Dan Corry wrote an article in *Renewal* on the shape of Labour's macroeconomic policy (Corry, 1994). After almost twenty years it is striking how relevant much of the article still feels. The original piece was entitled 'Living with capitalism' but today's Labour economic policy appears to have moved beyond simply living with capitalism and is setting out an active agenda of how to change and shape it.

Labour's macroeconomic policy has moved through several distinct stages over the past two decades and the very definition of what exactly constitutes a 'macroeconomic policy' has been contested. In the early 1990s traditional macroeconomic policy (defined as the use of fiscal and monetary policy to impact upon macroeconomic variables such as growth, inflation and unemployment) was downplayed in favour of an agenda of supply-side reforms. In the mid-1990s a brief flirtation occurred with a more rounded approach to 'political economy', as opposed to simple macroeconomics, focused on the concept of a stakeholder economy. But this eventually gave way to a macroeconomic framework of 'constrained discretion' for policy-makers (Bank of England independence and fiscal rules) and a renewed focus on straightforward supply-side reforms. The notion of fundamentally changing the UK's national business model was quietly dropped.

From the late 1990s until the crisis of 2008 macroeconomics seemed oddly absent from British politics, in as much as when it entered political discourse it was usually reduced to seemingly endless lists of achievements (the longest period of consecutive growth since the 1800s, etc.). The crisis of 2008 saw both the return of macroeconomic policy to political debate and the return of active demand-side policies to prevent a slide into depression. In the years since the last general election a new economic agenda has been fleshed out. Labour retains a strong macroeconomic focus but is now going well beyond what are thought of as the traditional levers of macroeconomic policy and into the realm of political economy. This new agenda does not take the shape of the British economy as a given but as something which active government can influence.

1992-1997

Macroeconomics

Dan Corry wrote his original article at a time when Labour's macroeconomic policy, and indeed its entire approach to questions of political economy, was in flux. Labour had

failed to win the general election of 1992, to the great surprise of many, and had committed itself to supporting the European Exchange Rate Mechanism (ERM) which the UK had been forced from in September 1992, just months after that election. By 1994, though, the UK economy was on the road to recovery.

Corry identified four broad schools of macroeconomic thought. ‘Supply Siders’ essentially thought that no macro could have a major beneficial impact on the economy and the proper role of macro policy was simply to ensure stability in variables such as the exchange rate, public spending and interest rates to minimise uncertainty. ‘Active Macro’ proponents agreed that stability was essential but saw a role for macro policy in achieving this by fine-tuning the business cycle. ‘Strong Keynesians’ went a step further and argued that active macro policies had significant and lasting impacts on the real economy. This often led to a focus on managing aggregate demand in the economy and a frustration with the seeming over-emphasis sometimes placed on the supply side of the economy. Finally, ‘Supportive Keynesians’ took a more nuanced view. They thought that active macro policy should be the servant of supply-side policies, but this meant more than simply ensuring stability. In particular, they often emphasised the need for a low exchange rate and low interest rates as preconditions for growth (Corry, 1994).

As Corry noted, by 1987 Labour was still arguing for a broadly Keynesian position, with the manifesto pledging £3 billion of borrowing for capital investment to drive down unemployment. ‘However, by 1992, to many people’s horror, the policy had shifted markedly. A macro dimension seemed to have been given up as Labour went overboard on supply-side issues’ (Corry, 1994, 52). Signing up to the ERM, which severely limited the room for manoeuvre on both fiscal and monetary policy by pegging sterling to the Deutschemark, was seen by many as a continuation of this supply-side fixation.

Looking back twenty years later, Ed Balls argued that this had been a mistake. Labour in 1993, he stated, had neither an alternative to the ‘strait-jacket’ of the ERM nor a ‘credible approach’ to tax and spending. His suggested alternative was to argue for Bank of England independence (a radical idea at this stage) (Balls, 2012).

Ed Balls, from the mid-1990s onwards, became one of the key figures in shaping Labour’s approach to macroeconomics. His own background (PPE at Oxford, time at Harvard studying with Lawrence Summers and Robert Reich, and a stint as an economics leader writer at the *Financial Times*) made him one of the most technically accomplished macroeconomists in British politics. He was in tune with the latest macroeconomic academic thinking and his approach came to dominate Labour’s position.

In technical economic terms the overall macroeconomic approach was one of ‘constrained discretion’. The use of targets and rules to voluntarily constrain its own room for manoeuvre would buy a Labour government credibility with both markets and voters. This credibility could be put to work by using an active macro policy when needed to support the economy. In terms of Corry’s four schools of thoughts this could be seen as ‘Active Macro’, the proper roles of fiscal and monetary policy being to maintain stability by ironing out fluctuations in the business cycle. Crucially, and in tune with the latest economic thinking, the primary tool of stabilisation policy was seen as monetary policy. This was both easier to change (and hence more responsive) and could be placed outside of direct political control. When in the 1990s the Labour Party pledged to end ‘boom and bust’ it was monetary policy they were talking about. By

placing the ability to change interest rates outside of political control the role of the political cycle in setting them could be minimised. An independent central bank was seen as more likely to raise rates as the economy over-heated, while politicians might fret about making voters' mortgages more costly.

Political economy

Alongside the traditional debate on macroeconomic policy, the mid-1990s also saw a renewal of interest in what could be termed 'political economy'. As macroeconomics as a discipline became more 'rigorous', more mathematical and more model-based (Skidelsky, 2009), there was a revival of interest in political science departments in what came to be called 'Varieties of Capitalism' (Hall and Soskice, 2001). This debate went beyond the role of macroeconomic levers in stabilising demand and considered the roles of corporate governance, financial systems, industrial relations and firm relationships in explaining economic performance. The Labour manifesto of 1992 had contained a great deal that broadly fit into such an agenda (Thompson, 2006).

In the UK this was popularised by Will Hutton's *The State We're In* (Hutton, 1995) with its arguments for a more German model of capitalism that took greater account of the different stakeholders in the economy (workers, consumers and management, not just shareholders). Labour flirted with this agenda, most notably in Tony Blair's Singapore speech of 1996. For a while the 'stakeholder economy' was seen as Labour's 'big idea' but the term meant very different things to different actors in the debate. As Andrew Gamble and Gavin Kelly noted in 1996, Labour's practical policy agenda on stakeholder economics was always very limited (Gamble and Kelly, 1996).

Three factors perhaps explain why the dalliance with a stakeholder economy never really moved beyond the rhetorical phase. First, and despite praise from Will Hutton and many others, the German economic model appeared to be in serious trouble by the mid to late 1990s. A costly reunification with East Germany led to a large loss of competitiveness and by the early 2000s Germany was regularly described as 'the sick man of Europe'.

Second, the close ties between New Labour and Clinton's New Democrats during this period almost certainly played a large role. The strong US economic performance and the close links between economic policy advisors such as Summers and Balls led to the US becoming the 'go to' place for economic policy ideas rather than Europe.

Finally, by 1997 the UK economy was growing at a decent pace. The exit from the ERM had led to lower interest rates and a weaker sterling, both of which boosted the recovery. The entry of China and the former Eastern bloc into the global economy greatly increased the global labour supply and put downward pressure on inflation. The UK's economic model appeared to be performing well by the late 1990s and there was seen to be less need to change it – especially given that the formerly heralded post-war winners of West Germany and Japan (both more stakeholder based) were suffering.

The Labour Government elected in 1997 had come a long way from 1992. Macro policy was now in line with the latest New Keynesian academic thinking and wider questions of political economy were downplayed. The incoming government had certainly learned to live with capitalism and with British capitalism in particular.

1997-2007

One academic observer has recently noted that the 1997 to 2010 period saw ‘a government in which the influence of mainstream economics has never been greater.’ Amongst its first acts were Bank of England independence and new fiscal rules whilst

in terms of microeconomic policy, the ethos was generally light touch regulation, but with intervention where there was perceived to be a clear market imperfection ... There was a clear aim to reduce poverty, but again this was done through the tax and benefit system, rather than trying to directly influence market outcomes. (An exception was the introduction of the minimum wage, but that had a lot of support amongst mainstream economists). (Wren-Lewis, 2013)

This certainly seems to be a fair summary of the overall macro approach between 1997 and 2007. The best explanation of the overall macro strategy in this period came from Ed Balls in 2004. He argued that Bank independence, the symmetrical inflation target, and the fiscal rules (only borrowing to invest over the cycle and aiming to get government/debt GDP below 40 per cent) had established ‘a modern, pro-stability but post-monetarist macroeconomic framework that responded to the challenge of the global economy’ (Balls, 2004). The downplaying of political economy apparent before 1997 continued, as did the fundamental acceptance of the British model of capitalism, with its powerful finance sector, its shareholder-dominated corporate structure and its model of property price related business cycles. While the government made many strides forward in improving public services and their funding, in the introduction and expansion of tax credits, in the reduction in poverty (especially child poverty), and in introducing the minimum wage, the economic model was not fundamentally challenged. As one current Shadow Cabinet member has written:

But too many of the tenets of neo-liberalism – the powerlessness of national governments in the face of globalisation, the dependence on under-regulated markets and growing inequality – were accepted, willingly or otherwise. (Wood, 2011)

The successes

In terms of traditional macroeconomic outcomes, the last Labour government was generally successful. As one major study has concluded:

the UK’s performance was good after 1997. The growth of GDP per capita – 1.42 per cent a year between 1997 and 2010 – was better than in any other ‘G6’ country ... The UK’s high GDP per capita growth was driven by strong growth in productivity (GDP per hour), which was second only to the US, and good performance in the jobs market (which was better than in the US). The UK’s relative economic performance appears even stronger in the years prior to 2008 before the Great Recession engulfed the developed world. (Corry, Valero and Van Reenen, 2011)

These macroeconomic successes are undeniable. As the authors note, the employment rate was consistently high, productivity growth strong, and GDP per capita growth (perhaps the best traditional measure of macro success) superb.

The problems

But is this the whole story? (1) The authors of the above cited study conclude that the major failure of the last government was on financial regulation. There is a comforting tale to be told that the last government got most things right and with a bit of tougher financial regulation things can carry on as normal. In reality the picture is a lot more complex and whilst the government's macroeconomic achievements (measured in the standard way) were strong, if one looks at a wider picture then important questions must be asked.

While the UK's performance 1997-2007 was stronger than other major economies, its relative performance in 2008-2010 was not. Can the reasons for the relative under-performance in 2008-2010 be found in the decade before the crisis?

As Wren-Lewis has argued, the policies favoured by the last government were generally those outlined by mainstream economists. It is perhaps no surprise then that the measures of success were also those of mainstream economists – primarily GDP per capita growth.

One charge that can fairly be levelled against the last government is that it was not bothered by where this growth came from, nor did it question sufficiently how sustainable this growth was (2). Perhaps the strongest statement of this case has been made by the Centre for Research on Socio-Cultural Change (CRESC) at Manchester Business School. In an important paper in 2011 they argued that UK's entire national business model was fundamentally broken: growth had become reliant on finance and property, heavily concentrated in the South East, and was increasingly driven by households engaging in mortgage equity withdrawal and a build-up of household debt. This had begun under Thatcher in the 1980s with the hollowing out of manufacturing but essentially been continued under Labour (Froud et al., 2011).

Whilst this case can be overstated, there is undoubtedly some truth to it, hence the focus from politicians of all parties from 2008 onwards on the need to 'rebalance' the UK economy. If the economy needs rebalancing, then it is clearly the case that it became 'unbalanced' before the crisis.

There is now widespread acceptance that financial regulation in 2008 was too weak. The extent of the problem posed by the financial sector, however, remains contested. The Bank of England's Andrew Haldane has argued that what appeared to be a 'productivity miracle' in financial services in the 1990s and 2000s was actually a 'mirage'. Excessive risk taking that was not perceived at the time was reported as rising productivity (Haldane, 2010). If this is true, then it takes away the option of simply saying 'the last government got most things right except financial regulation'. Presumably tougher financial regulation would have meant less excessive risk taking and hence a smaller contribution to growth from financial services and a smaller contribution to the Exchequer from the sector as a whole – all this would have implied either less public spending, more taxation, or greater borrowing. In other words, accepting that financial regulation was too weak opens up wider questions.

The role of the financial sector also goes to the heart of questions of macroeconomic performance between 1997 and 2007. Measured conventionally by GDP per capita growth, it was certainly strong, but such measures focus on flows and neglect stocks (3). If one looks at the wider picture, including what happened to bank, firm and household balance sheets over time, then 1997-2007 looks different. Whilst growth in each individual year was fine, over the decade a large amount of household debt was built up and bank balance sheets became over-extended (Barwell and Burrows, 2011).

Business investment (at least from 2004 onwards) was also weaker than expected and from the mid-2000s firms began to build up a large surplus of cash rather than reinvesting in growth. The government perceived the firm as something of a 'black box' and few questions were raised at the time about why corporate behaviour appeared to be changing and why businesses preferred to hold cash over engaging in capital expenditure (Barwick, Corry and Kenway, 2012). This may again be tied back to the banking system which, over the period 1997-2007, lent £1.3 trillion pounds to the UK based, non-bank private sector. 85 per cent of this lending went into either property or the financial system (Weldon, 2013). The share of national income provided by financial services rose from around 5 per cent in 1997 to 8 per cent in 2007 which directly fed into regional imbalances given the financial service sector's heavy concentration in the South East (TUC, 2012). However, the clearest sign that something was going wrong in the economy before 2008 comes from the labour market. While many hail high employment rates as a sign of success (and they certainly are an important benchmark for macro policy), something odd was happening in pay-setting.

Between 2003 and 2008, the UK grew by around 11 per cent but real median wages (the wages paid to those in the middle after adjusting for inflation) stagnated. The gains from growth increasingly went to those at the top. This development received little comment at the time with the tax credit system, the wider welfare state, and easy access to credit all providing relief for squeezed households (Resolution Foundation, 2012).

Taken together the picture of an unbalanced UK economy in 2007 was reasonably clear. Growth was too concentrated in too few sectors and too few places, tax revenues were too reliant upon those sectors, and the gains from growth were not filtering (by the end of the period) down to those in the middle and below. The light touch approach could at times be seen as part of a grand bargain – the Labour government would allow the financial sector (and the related property sector) to 'get on with it' as long as that generated the tax revenues which could help finance the social security system. Labour was living with British capitalism and using the proceeds of its unbalanced growth to correct the worst excesses.

Recent economic work has suggested that the rise in inequality, rather than simply being a social justice issue, may have contributed to the crisis. A 2010 IMF paper argued that the decline in the bargaining power of labour seen in the 1980s allowed the large rise in inequality of the 1980s and 1990s. This has, in the authors' model, two impacts. First, it creates a demand for credit from those lower down the income scale to sustain their standard of living. Second, and just as important, it creates a supply of credit to meet that demand. Those at the top of the income scale accumulate wealth, as they are more likely to save rather than spend additional income. In effect they build up

financial assets, increasing the size of the financial sector and then boosting the availability of credit. As inequality rises, so too does the size of the financial sector and the amount of personal debt in the economy. This leaves the economy more vulnerable to financial crisis and makes recovery from recession harder as households have debt to service. In many ways this model fits with the UK picture in the years before 2008 (Kumhof and Ranciere, 2010).

Labour's focus on traditional macroeconomic policy and its neglect of wider political economy can be at least partially held responsible for this. The focus on GDP per capita, the employment rate and productivity, and the general sense that much of macroeconomics had been outsourced to the Bank of England, meant that many of these concerns were downplayed. The decline of sectors such as manufacturing was seen as an inevitable result of globalisation, the growth of the financial sector was something to champion rather than worry about, and there was complacency about the sources of growth. To raise these worries, or to talk about issues such as industrial policy, was regarded as rather old fashioned.

2008-2010 – the crisis, active macro and the rebirth of industrial policy

Whatever the cause of the crash, Labour's response (in terms of macroeconomic policy) was strong. The problem of a lack of bank capital was quickly identified and acted upon and the financial system stabilised (although not reformed). Capital spending was brought forward, VAT was cut and the automatic stabilisers (higher social security spending and lower tax revenues) allowed to operate fully. Interestingly, there seemed to be some frustration among policy-makers at the comparatively slower reaction of the Bank of England (Darling, 2011).

This was a straight-forward, almost text-book, macroeconomic response to a severe recession. The government recognised quickly that the immediate problem was a lack of demand in the economy and sought to rectify this. The strongest criticism that can be made about the macroeconomic policy response was that the initial fiscal stimulus was too small.

Alongside the traditional macroeconomic policy response, though, came something less expected: the rebirth of industrial activism. 2008 saw the rebirth of industrial policy in the UK after being out of favour for three decades, as the Business Department pioneered industrial councils, targeted support for sectors, and a closer working relationship with firms. It seemed that policy-makers had grasped that the unbalanced nature of the UK's economy was a problem and saw a role for active government in reversing these trends. On Peter Mandelson's own account, he had come to learn these lessons whilst working as EU Trade Commissioner and observing how industrial policy had successfully functioned overseas (Mandelson, 2010). By a strange irony, 2008 to 2010 perhaps witnessed the return of an interest in a 'Varieties of Capitalism' approach at the top of the party. The 2010 election campaign was the first to be dominated by macroeconomics in a generation, even if much of the debate appeared to be a form of 'shadow boxing' over the wisdom of £6 billion of in-year cuts in 2010/11 rather than about wider questions.

After 2010

Since the 2010 election the UK's economic performance has been poor. Real wages have fallen substantially, which, coupled with changes to the tax and benefit system, have created an unprecedented squeeze on living standards. Growth has regularly been below forecast and deficit reduction targets missed. The UK has underperformed its international peers and had the second worst growth in the G7. Labour policy has been formulated against the backdrop of the successes and failures of both its own time in office and in reaction to the Coalition.

Whilst precise details are lacking, Labour's agenda can be seen as having two distinct elements: firstly a macroeconomic critique of the current Government's policies and secondly a more forward-looking agenda of reform often termed 'responsible capitalism'. The second agenda appears to fall more in the domain of political economy than macroeconomics, although in macro policy terms it could be thought of as an ambitious agenda of supply-side reforms.

Macro policy

Labour's macroeconomic policy since 2010 has focused heavily on fiscal policy, the lack of demand in the economy and the self-defeating nature of the Coalition's austerity programme. It is possible to argue that this does not represent a large shift from the period of 1997-2007 – the previous Labour government was committed to using macro policy to stabilise the business cycle, and when the economy is clearly beset by a lack of aggregate demand there is a strong case for expansionary fiscal policy.

In reality, however, it appears that Labour have moved from what Dan Corry termed 'Active Macro' to the schools he called 'Strong Keynesian' and 'Supportive Keynesian'. The key text for understanding Labour's macro approach remains Ed Balls' 'Bloomberg speech' of 2010. What is notable about that speech is not the straightforward critique of austerity (which claimed far more supporters in the summer of 2010 than it does currently), but the emphasis on the long-term damage that a shortage of demand risked doing to the UK economy (Balls, 2010). Macro policy was no longer seen as just about stabilising the business cycle but also as having important long-term consequences, consequences that had been downplayed in the fifteen years before.

Partially this shift can be explained by a changing economic environment. 2010 was not 1994 and the outlook was much weaker. But equally important was a shift in mainstream New Keynesian macroeconomic thought. Prominent macroeconomists such as Brad DeLong and Lawrence Summers now argued for a greater role for discretionary fiscal policy than they had in the past and placed more emphasis on the long-term scarring effects of low demand on unemployment than they previously had (DeLong and Summers, 2012). The New Keynesian academic consensus shifted during the 'great recession' and Labour's macroeconomic thinking moved with it.

Perhaps related to this is Labour's new found emphasis on capital spending (Balls, 2013b). If one is going to use macro policy (and fiscal policy especially) as a tool to stabilise the economy and if one considers that macro policy has important long-term effects, then capital spending is the natural policy tool. Capital spending not only boosts

output in the short run, but also leaves the economy with better infrastructure and housing in the future, with a potential impact on longer term productivity growth.

Responsible capitalism

Whilst most opponents of the Government have been united in opposing its stance on fiscal policy and supporting some form of stimulus, there appeared for a while to be little agreement beyond this. In macroeconomic policy terms there has been a debate between those who favour a fiscal stimulus to boost demand and restore growth and those who think this is a necessary but not sufficient step.

The debate has been neatly summarised by Gavin Kelly and Nick Pearce as being between those who 'think the fundamentals of the UK economy are sound' and those who believe that there are 'core weaknesses in the UK economy which were graphically exposed when the financial crisis struck, many of which are long standing'. Whilst accepting the strong record on GDP per capita growth, the resilience of the labour market, and the existence of strong parts of the service sector, Kelly and Pearce identify a 'long tail of pedestrian, low-skill sectors', the problems of wage growth pre-2008, the weakness of a tax base dependent upon finance and property, and the sectoral and geographic imbalances that have grown up over thirty years as shortcomings of British capitalism. Tackling these problems, they argue, requires a shift away from macroeconomics and back towards political economy (Kelly and Pearce, 2012, 94-5).

It is this agenda which Labour calls 'responsible capitalism.' In more boring economic parlance this is better thought of as an agenda of supply-side reform:

The 1980s supply-side revolution from the right has run its course; what Britain needs is a supply-side revolution from the left, to build a stronger and fairer economy. We will need different kinds of banks and stronger competition in the banking industry; corporate governance reforms to incentivise good ownership models and longer-term business strategies; ensuring that companies see the continuing upskilling of their workforce as an obligation and not simply a luxury; and the courage to challenge vested interests in the economy that charge excessive prices for energy or train fares and squeeze families' living standards. (Wood, 2012)

Building on the work of US academic Jacob Hacker (Hacker, 2011; see also the interview with Hacker in this issue), Labour have argued for policies sometimes termed 'predistribution', aiming to change market outcomes rather than simply using the state to compensate those who lose out. This approach ran through Ed Miliband's recent speech on social security, which argued that Labour would tackle the social security bill through focusing on its causes rather than simply reducing payment levels. The focus was on tackling low pay, reforming precarious employment, and building more homes to bring down the housing benefit bill (Miliband, 2013b).

Equally, Peter Mandelson's enthusiasm for industrial policy has been continued with Labour placing an active industrial policy at the heart of its economic policy, rather than as just another tool of stabilisation policy in a crisis:

To be successful, active government policy must be for life, not just for a crisis or dependent on the personality and drive of whoever leads the Business Department. It must be about shaping the future, not just reacting to events. It must be less about sporadic and unpredictable intervention, and more about fostering stable institutions within a certain policy environment. (Umunna, 2012)

The emphasis in Labour's medium-term, post-crisis, agenda has been firmly placed on economic reform and the need to look at variables such as training systems, corporate governance, financial systems and the role of government in providing direction as a way to change the economy's performance *and* shape. The composition of growth is once again seen as important as the level of growth. In other words, Labour appears to be firmly back into the realm of political economy, at least as a medium-term agenda, even if the short-term is likely to remain dominated by traditional macroeconomic concerns around growth.

As Ed Balls has argued:

I worry that as a country, if we allow our debate to be solely focused on the rate of economic growth this year and the level of the budget deficit, we risk taking our eye off the long-term goal that we must also focus on – how we make our economy stronger, more balanced and better able to attract new investment and compete in world markets over the next 20 years and not only in the next two years. (Balls, 2013a)

The bar for success in such an agenda is not simply GDP per capita but median income growth, something Ed Miliband has acknowledged in his calls for a recovery built from the middle out and an 'economy that works for working people' (Miliband, 2013a).

Making such an agenda work is an ambitious programme and one that depends upon changing the shape of the UK economy rather than simply pulling traditional levers. Whilst there is much that can be done through the existing minimum wage, the extension of the living wage, pushing up employment, and (crucially) extending collective bargaining coverage to support living standards, in the longer term the challenge is creating more higher skill, higher waged jobs in the first place (Lansley and Reed, 2013; Wren, 2013).

While it is possible to see the two strands in Labour economic policy as being quite separate – macro policy for the short-term, political economy for the longer term – in reality, they are intrinsically linked. In many ways the responsible capitalism agenda can be thought of as part of macroeconomic policy. First, as Rachel Reeves has argued, ensuring fiscal stability is tied to economic rebalancing:

it is clear that a fairer and more balanced economy would mean
– a more reliable and resilient tax base
– as well as fairer outcomes and more resilient families and communities
so as well as delivering a stronger economy and a fairer society, a more responsible capitalism will also help us deliver long-term fiscal sustainability. (Reeves, 2012)

Second, the UK has faced a very serious fall in productivity since the financial crisis. There has been an active debate among economists as to whether the UK's primary problem has been a lack of demand or a problem on the supply side. The answer appears to be a bit of both – the UK faces a serious shortage of demand but it also faces issues on the supply side. These include problems in the banking system, under-investment by firms, problems with skills, and a national business model that can lead to too many low waged, low skilled jobs. To get sustainable macroeconomic outcomes actually requires action on the demand side *and* the supply side. Otherwise, the risk is that the UK goes down the road to being a demand-constrained, lower waged, lower skilled economy (TUC, 2013).

Why is Labour seemingly embracing a more wide-ranging economic agenda today than before 1997? Given the UK's poor economic performance since 2008 it is perhaps unsurprising that Labour has adopted a far more radical approach to economic reform than in the 1990s. While the mid to late 1990s were a period of decent growth, the 2010s seem unlikely to be. Similarly, the unprecedented squeeze on living standards creates the political space to ask bigger questions. It also appears that many in the party leadership have learned not just from the successes of the previous government, but also its failures. Finally, the relative strength of other economies which utilise a different model of capitalism – notably Germany and the Nordics at present – makes such models appear more viable and more attractive than was the case twenty years ago.

Conclusion

Over the past twenty years Labour in opposition and government learned to live with capitalism, specifically its British variant. For much of the period in government Labour ran a macroeconomic policy in keeping with the latest economic thinking while questions of political economy were downplayed. In opposition the party is once again placing an important long and short run emphasis on the role of macroeconomic policy to stabilise demand but also critiquing Britain's economic model. Labour appears to have moved beyond learning to live with capitalism and is now talking about steps actively to reform it. Exactly what steps it would take to achieve this are still unclear but the responsible capitalism agenda may have enough specifics – median wage growth, tackling vested interests, corporate governance and banking reform, active industrial policy – to avoid the fate of the talk of a stakeholder economy in the mid-1990s. It can be more than a rhetorical device.

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Notes

1. For reasons of length, this article necessarily focuses more on the reasons for caution regarding economic performance 1997-2007, but it should not be forgotten that there were important successes not just in terms of macro outcomes but also in public service provision.
2. A charge rejected by Corry, Valero and Van Reenen who argue at length that the UK was not in an unsustainable bubble in 2008. However, as their analysis is focused on traditional macroeconomic measures, they may have over-looked other factors.
3. GDP is a measure of national output (or income) in any given year – it focuses on the flow of production of good and services (or of income through wages and profits) in that year. It does not take account of the build-up of stocks over time.