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Neoliberalism, Institutional Change and the Welfare State: The Case of Britain and France

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Abstract
Neoliberal turn in economic policy involved an attack on the welfare state in some countries but not in others. This article provides an institutionalist explanation of the causes of this variation through a comparative analysis of the transformation of British and French economic policy from the end of the Second World War through the end of the 1980s. The author shows that in both nations the transition to neoliberalism accompanied the economic crisis that took place in the 1970s. However, consistent with the differences in the way the two countries came to diagnose the nature of their respective crises; the policy manifestations of neoliberalism remained different in each. In Britain, where the crisis was diagnosed as one of Keynesianism, neoliberalism emerged as a radical anti-Keynesian movement that sought to dismantle major Keynesian institutions and policies. In this context, the welfare state, a fundamental Keynesian institution, was identified as a part of the 'problem,' and became subject to the neoliberal 'solution.' On the other hand, in France, where the crisis was perceived to reside in the declining competitiveness of the dirigiste policies, the neoliberal reorganization of the economy focused on industrial policy. The welfare state was not associated with the problems of dirigisme, and remained largely resilient. Through this analysis, the author attempts to develop a general theory of the relationship between neoliberalism and national policies and provide insights into the process through which paradigmatic ideas such as neoliberalism translate into concrete policy preferences in different national contexts. Data for this study come from a combination of content analysis of major government documents concerning the economy and social policy, political party election manifestos, opinion papers, OECD statistics and secondary literature.

Key words: economic policy • globalization • institutional change • neoliberalism • welfare state

INTRODUCTION

In the period following the Second World War, providing welfare to citizens became a fundamental feature of western statehood. Social expenditures increased rapidly; and traditional relief systems that provided assistance only to the most needy of populations were transformed into comprehensive systems of universal benefits through the welfare state (Quadagno, 1987). Writing in the 1950s, T.H. Marshall saw the development of social welfare programs as comprising an inevitable step in the natural progression of states' relations to their citizens (Marshall, 1950). This view soon became the conventional thinking about the welfare state. The development of the welfare state was taken for granted, so much so that 'it seemed only a matter of time before less developed nations would modernize sufficiently to develop the economic surplus and bureaucratic capacity that would allow them to initiate similar programs' (Quadagno 1987: 110). It is by this logic that the relative lateness and shortage of welfare programs in the United States – a country with both the economic resources and the bureaucratic apparatus – was perceived as an anomaly, something that needed to be researched and explained as a part of the 'American exception' (Jenkings and Brents, 1989; Skocpol, 1989; Mechanic and Rochefort, 1996; Alesina and Glaeser, 2004).

Confidence in the continuous expansion of the welfare state was reversed in the last quarter of the 20th century when, in response to the changes in the international economic environment that are generally referred to as globalization, many western nations began to reorganize their economies along neoliberal ideas. Common wisdom now suggests that in the new international context that favors market solutions to economic problems, the principles of welfare capitalism cannot be sustained. Judging by the prevalence of this view, one might expect to see indisputable evidence of welfare retrenchment across the advanced capitalist world. However, this is not the case. The turn to neoliberalism in economic management has led to different policy adjustments across nations. In some countries, this involved an attack on the welfare state, while in others it did not. The goal of this article is to investigate the causes of this variation, thereby developing a general theory of the relationship between neoliberalism and the constitution of national policies.

There is now a voluminous literature on domestic institutions and comparative politics, which convincingly argues that the emphasis on 'globalization' or 'neoliberalism' as a whole remains underspecified and indeterminate in explaining the specific and different forms of change that took place in state structures and policies over the past two decades (Hall, 1986, 2001; Block, 1990; Weiss, 1998, 2003; Campbell and Pedersen, 2001; Fligstein, 2001; Hall and Soskice, 2001; Hay, 2001; Blyth, 2002; Fourcade-Gourinchas and Babb, 2002; Swank, 2003). Contributors to this literature have long maintained that nations are endowed with distinctive institutions and policy cultures which allow them to pursue diverse strategies in the face of common challenges. It is true that the sea of changes that took place in the international economic environment during the 1970s and the early 1980s affected virtually all countries. Most nations faced high inflation and slowed growth. They had to deal with the disruptive macroeconomic effects of two oil shocks, adjust to the regime of floating exchange rates, and search for ways to sustain their competitiveness in the face of increasing economic integration. As such, the international economic environment constituted an external, objective reality for individual countries, which, in many cases, undermined their traditional economic policies and constrained what their governments were able to do. This provided a particularly favorable context for neoliberal ideas to penetrate into the realm of economic policymaking as potential 'solutions' to the challenges and problems that lay ahead. Contrary to the common view, however, neoliberalism has not translated into a similar set of policy preferences in all nations. To explain which policy arenas were altered, and which ones remained resilient, and why the welfare state came under attack in one nation while it remained intact in another, it is necessary to develop a better notion of institutional change than that offered by the 'globalization' view. After all, as Blyth notes, 'while exogenous changes may help to explain why a particular institutional order becomes unstable, such infusions of instability do not in themselves explain how the new or modified order takes the form it does' (2002: 8).

In this article, I develop an institutionalist approach that places the emphasis on the domestic processes in which neoliberal policies were constituted. I develop this approach by comparing Britain's and France's turns to neoliberalism at the end of the 1970s. I show that in both nations the economic crisis of the 1970s played a critical role in forwarding the neoliberal transition. However, depending on the differences in the way the two countries came to diagnose the nature of their respective problems and needs, the policy implications of the neoliberal turn remained quite different in each. In Britain, where the crisis was identified as one of Keynesianism, neoliberalism emerged as a solution to the failures of Keynesian policies and institutions. In this context, the welfare state, seen as a fundamental Keynesian institution, was diagnosed as part of the 'problem' and became subject to the neoliberal 'solution.' On the other hand, in France, where the crisis was perceived to reside in the declining competitiveness of the *dirigiste* policies, the neoliberal reorganization of the economy focused on industrial policy. The welfare state, which was not associated with the problems of *dirigisme*, remained largely resilient.

METHODOLOGY AND BACKGROUND

Data for this study come from a combination of content analysis of major government documents concerning the economy and social policies; political-party election manifestos; opinion papers; SourceOECD statistics, and secondary literature.

Several factors motivated the selection of Britain and France as comparative cases. Both are Western European countries with the same level of development; both became subject to international pressures and experienced economic problems throughout the 1970s and both turned to neoliberalism at the end of the 1970s. Given these similarities, they could be expected to have converged on an identical model of neoliberal adjustment. However, this was not the case. Despite the similarities of background and circumstances, the policy implications of the neoliberal turn remained different in each of them. While British neoliberalism involved an attack on the welfare state, French neoliberalism remained compatible with it. Such is the interesting divergence that prompts the institutional analysis extended here.

A few words must also be said as to why this study takes the period between the end of the Second World War through the end of the 1980s as its timeframe. In his article on political time and the temporality of crisis, Colin Hay starts with a quote from Debray: 'Time is to politics what space is to geometry' (Debray, 1973, quoted in Hay, 2001). The purpose of this quote is to highlight the temporality of institutional change. It suggests a conception of political time as the strategic terrain in reference to which events can be attributed a meaning. In institutional analyses, the temporality of institutional change is generally indicated in a three-stage model: 1) time of institutional stability; 2) time of critical juncture that triggers institutional change; and 3) time of institutional change (Steinmo et al., 1992; Hall, 1993; Hay, 2001; Blyth, 2002). Following this model, the present article takes the period starting from the end of the Second World War through the end of the 1980s as the strategic historical terrain upon which the shift to neoliberalism can be meaningfully studied. In this model, the period prior to 1970s comprises the time of institutional stability; the developments that took place in the 1970s form the critical juncture that prompted policy change; and the decade following this, the 1980s, remains the time of institutional change when policymakers actively analyzed the problems, interpreted the nature of the crisis, and designed new policies. It should be noted, however, that while the article focuses mainly on the 1980s as a period of active policy change, it also seeks to offer insights into the contemporary politics of the welfare state in Western Europe, particularly in Britain and France. Let me further explain.

The Changing Context of Economic Policy: International Pressures and Institutional Crisis

In institutional theory, there exists a conviction that major institutional change takes place at times of 'crisis,' when there is a mismatch between the challenges faced by a given institutional domain and its traditional way of solving problems (Steinmo et al., 1992; Hall, 1993; Hay, 2001; Blyth, 2002). These crisis periods constitute a 'punctuated equilibrium.' They witness experimentation with different forms of policy and competition among different ideas to restructure the institutional domain. The 1970s constituted such a period for most European countries.

From the end of the Second World War until the 1970s, the international economy had operated within a system whose primary rules were defined by the Bretton Woods agreement. Through a system of convertible currencies, fixed-but-adjustable exchange rates, and capital controls, the Bretton Woods System sustained a form of 'embedded' liberal order which allowed states to combine their national objectives with a commitment to free trade (Block, 1977; Ruggie, 1982; Ikenberry, 1992). In this permissive environment, almost all European countries developed comprehensive welfare states.

Throughout the postwar period, welfare states were seen as constituting an essential element of successful economic policymaking – they were a part of the 'solution' to social and economic problems. Not only did they dampen the adverse effects of the market by providing the society with security against risks that might result from greater openness, but in Keynesian economies they served as 'a powerful counter-cyclical tool, producing deficits during recessionary periods and surpluses during boom times' (Pierson, 1994: 2–3).

In the 1970s, the international economic environment was drastically altered. In 1971, President Nixon declared the US decision to let the dollar float, which practically preordained the demise of the Bretton Woods System – the system that formed the backbone of postwar embedded liberalism. The difficulties in re-establishing the stability of the exchange rate that arose after the collapse of Bretton Woods System were compounded in 1973 by an economic crisis caused by OPEC's decision to increase the price of oil. As Scharpf and Schmidt note, oil-dependent advanced countries now had to deal with the 'macroeconomic challenges of "stagflation", the simultaneous effect of cost-push inflation and demand-gap unemployment' (2000: 4). Starting from the 1980s, economic globalization, characterized by increasing economic integration in trade and finance among nations, became another structural constraint for nations. In the European context, its effect was particularly pronounced due to the emergence of the European Union. The process of integration toward a common market and monetary union through a set of rules and objectives with regard to trade and monetary affairs applied pressure on the member countries.

These developments presented challenges to traditional ways of managing the economy in many nations. Policies and institutions associated with the postwar embedded liberalism, which once 'worked' increasingly, seemed to 'fail' (Campbell and Pedersen, 2001; Blyth, 2002; Fourcade-Gourinchas and Babb, 2002). In this context, many countries began to organize their economic policies along neoliberal ideas that emphasize market solutions and monetary discipline. By the 1990s, neoliberalism had been institutionalized as an overarching policy framework in many advanced capitalist nations.

Globalization, Neoliberalism and National Economic Policy

In the current literature on globalization, many interpret 'neoliberalism' to represent the unrestrained power of the markets over the nation-states. We are told that governments all over the world abandon their distinctive institutions, policies and norms, and embark on a set of common strategies in order to adapt to the various pressures imposed upon them by the global markets. As such, the standard globalization view suggests two propositions. One of these concerns the question of *diminishing state power* – how much political autonomy states have actually lost, to what extent their policy choices are restricted (Weiss, 2003: 3). To this question, some scholars answer in the extreme, proclaiming the end of the nation-state and the commencement of a global era (Ohmae, 1990, 1995; Horsman and Marshall, 1994; Camilleri and Falk, 1992, Albrow, 1996; Falk, 1997). Others, while agreeing that the changes that have taken place are by all means substantial, perceive such changes as representing not quite the end of the nation-state, but rather the end of a certain form of statehood pertaining to the postwar period. According to these more moderate accounts, which Weiss terms the 'constraints school' (Reich, 1991; Castells, 1996; Cerny, 1996; Strange, 1996; Cox, 1997, 2001):

> managing the national economy to promote growth, industrial upgrading, and employment – whether by maintaining or raising taxation and spending levels, coordinating an investment strategy, encouraging industrial upgrading, or supporting technological innovation, and so on – are seen to be increasingly beyond the capacities of territorially-centered states. (Weiss, 2003: 3)

The second proposition of the globalization view concerns the *generality* of the trends abovementioned – in other words, the end of cross-national variations in economic management. As Weiss points out, in the globalization literature, arguments about the retreat of the state often go hand in hand with claims about the 'erosion of national capitalisms' (2003: 3). The so called 'convergence view' suggests that *all* nations are moving towards a liberal model whereby the state's role in the economy is limited only to the basic functions of providing rule of law and security (Weiss, 2003).

The 'constraints' and 'convergence' views of the relationship between the international context and states' economic conduct is shared both by the proponents of globalization and by its critics. Both groups agree that the forces of capitalism, which are increasingly international in character, make it more difficult for governments to exercise interventionist and expansionary policies, while at the same time they favor market-oriented policies. Both view the rise of neoliberalism as a shift toward a single model of capitalism away from the most basic political and economic settlements of the postwar-embedded liberalism, including 'the labor market accords, industrial relations systems, redistributive tax structures, and the social welfare programs' (Campbell and Pedersen, 2001: 4). The difference between them remains in the normative realm – in the way they view the potential social outcomes of this process (Fligstein, 2001).

Proponents of globalization see the rise of neoliberal policies as natural and desirable, given the failure of embedded-liberalism institutions and policies to generate efficient outcomes for countries (Friedman and Friedman, 1980;

Radelet and Sachs, 1997). The 'failure' of embedded liberalism, as well as the 'solutions' to it, constitutes an 'obvious, objective' reality for neoclassical economists: policies that favor active state intervention in the markets, including the mechanisms for social welfare, remain inefficient and must be discarded. Understood in these terms, the neoliberal turn marks a shift from a model of economic management that was 'not working' to a model that will 'work.'

Critics of globalization also see these economic forces as determining action (of states, policymakers, etc.). In addition, they think that international economic pressures render postwar models of economic management unsustainable. Unlike neoclassical economists, however, they do not think that the 'unsustainability' of these policies is due to inefficiencies inherent in them. Rather, they argue that it is the unleashed forces of the markets that limit states' freedom to exercise such policies by shifting the power away from the state and society toward capital (Stallings, 1992; Stiglitz, 2002). In such views, neoliberalism represents ideas, policies and institutions (such as the IMF, WTO or the Washington Consensus) that inform hegemonic modes of globalization (Holzmeyer, 2003), and the rise of a 'new and more virulent phase of capitalism' (Fligstein, 2001).

Scholars engaging in institutional and comparative analyses have systematically shown that arguments about 'constraints' and 'convergence' are much exaggerated (Weiss, 1998, 2003; Campbell and Pedersen, 2001; Fligstein, 2001; Hall and Soskice, 2001; Blyth, 2002; Fourcade-Gourinchas and Babb, 2002). Against all the talk about the dismantling of postwar institutions and narrowing of policy alternatives, a growing body of evidence demonstrates that many of the institutions, policies and powers in question have remained surprisingly resilient in many nations (Garret and Lange, 1991; Pierson, 1994; Rodrik, 1998). Certainly, there have been significant adjustments as well. However, the form and degree of those adjustments have not been uniform across nations.

Globalization accounts ignore the fact that throughout the postwar period, states have varied drastically in the way they have managed their economies – in their goals of policymaking, as well as the techniques and instruments they have used. The size, structure, and the role of the welfare state in economic policy, for instance, did not remain the same across nations, nor did the values and ideas about inequality, family and gender that surround it. Given this, it is rather naïve to assume that countries with quite different institutional histories would interact with the changing international context all in the same way, and that they would converge on the same model. The international economic environment has influenced national policies, but not 'ordered' them. Rather than convergence, what we observe is different politics of adjustment due to variations in domestic structures and processes.

A further problem is the tendency to describe the pressures and the challenges presented by the international context and implementation of neoliberalism in objective/material terms. This remains problematic since policy-making necessarily involves subjective and normative judgments as well as hard facts. The process that involves the diagnosis of the 'problem' that any given institutional domain faces, and its possible 'solution,' is a dynamic, subjective process whereby agents interpret and negotiate what the so-called 'objective' challenges really mean, what their causes are, and what must be done about them. As Blyth argues:

> … structural theories of institutional supply are indeterminate as to subsequent institutional form. Theoretically, no exogenous factor can in and of itself explain the specific forms that institutional change takes. While destabilization of existing institutions can be exogenously driven, moving from such a position to a new stable institutional order must be seen as an *endogenous process*. Specifically, how agents redesign and rebuild institutional orders *and the conditions under which these activities take place* need to be analyzed. (Blyth, 2002: 8)

Along these lines, comparative and institutionalist scholars have emphasized different mediating factors to explain differential adjustment. Weiss predicted that different paths to adjustment would take place along 'nations' varied state capacities for domestic adjustment' (Weiss, 1998); the contributors to the Keohane and Milner's edited volume *Internationalization and Domestic Politics*, emphasized the 'strength of political institutions' as a major source of variation (1996); Steinmo et al. offered an historical-institutionalist account emphasizing the significance of 'policy legacies' (1992); Fourcade-Gourinchas and Babb found the differences to take place around 'institutionalized patterns of state-society relations' (2002); Schmidt highlighted the much-neglected factor of 'discourse' (2001, 2003); and Hall and Soskice's acclaimed perspective pointed out the 'structures of coordination among firms' as a comparative frame of reference (2001).

What emerges from these institutional studies is a whole different view of the relationship between the international context and policy change à la neoliberalism. Neoliberalism turns out to be 'less a coherent totality, as is often assumed, than a loose conglomeration of institutions, ideas and policy prescriptions from which actors pick and choose, depending on prevailing political, economic, social, historical, and institutional conditions' (Campbell and Pedersen, 2001: 3). According to this view, it is untenable to define neoliberalism with a de-contextualized, general statement about its purported tenets, policy content and mechanisms. As Holzmeyer notes,

> … analysts who claim to do so set themselves up to fail in grounding their definitions and in comprehending variations in neoliberal policy-making and restructuring, including issues of cultural translation, negotiation, path-dependence, policy justification, and political framing. Recognizing neoliberalism's variations, contradictions and lack of uniformity across contexts is, in turn, an important aspect of its deconstruction as a monolithic, objective entity (in a descriptive or prescriptive sense) – of recognizing the contextual, social and historical constitution and consequences of neoliberal and other economic policies. (Holzmeyer, 2003)

The Problem: Neoliberalism and the Welfare State

This article joins the existing comparative/institutional literature in its attempt to unpack the concept of neoliberalism and survey its multifaceted manifestations in different national settings. By way of problematizing the assumed link between neoliberalism and welfare retrenchment, it endeavors to offer yet another explanation of how neoliberal variation is possible.

The typical view in the globalization literature regarding the welfare state has been one of retrenchment. It is suggested that in the context of economic integration and openness, governments have to give up their welfare programs to sustain their competitiveness (Strange, 1995, 1996, 1997; Rhodes, 1996; Scholte, 1997; Schwartz, 2001). Historical evidence, however, counters the logic of this argument. As Cameron (1978), Rodrik (1997, 1998), and Garrett (1998a, 1998b) have shown repeatedly, throughout history, economic openness per higher levels of trade has led to more welfare effort on the part of governments, not less. As Polanyi elaborated some 60 years ago, in order to protect their citizens from the risks associated with international trade and finance, governments extended generous welfare programs, rather than rolling back the welfare state (Polanyi, 1944). According to some students of contemporary welfare state transformation, present circumstances hardly present a counter-trend. These scholars find the effect of globalization on the welfare state to be rather exaggerated, if not insignificant (Pierson, 1994; Wade, 1996; Garrett, 1998b; Levy, 2000; Fligstein 2001; Atkinson, 2002).

Beyond these arguments of systematic 'retrenchment' and 'resilience,' there is an ever-growing consensus, which the author of this article joins, that the effects of globalization and neoliberalism on welfare states have been cross-nationally varied (Scharpf and Schmidt, 2000; Huber and Stephens, 2001a, 2001b; Pierson, 2001; Schmidt, 2001, 2003; Blyth, 2002; Swank, 2003). Where the consensus ends is in the question of how to explain this variation. This question has been fervently pursued from various perspectives. In an essay on the state of the art of welfare state studies, Pierson proclaims, 'understanding the causes and consequences of welfare state variation has become a major preoccupation of research on the comparative politics of affluent democracies' (2000). Understandably so, as the welfare state lies at the heart of important social issues including income and gender inequality, aging, health, education, and labor force participation. In that respect, questions about the welfare state make up perhaps the most contested and sensitive aspect of neoliberal transformation.

To highlight some of the perspectives on the welfare variation: Swank attributes divergent welfare state trajectories to the differences in the political institutions and programmatic structures of social democratic, corporatist, and liberal welfare states (2003); Blyth argues that the constitutive role of ideas matters in shaping the specific trajectory of the welfare state (2002); Schmidt points to the significance of the legitimating policy discourse in determining the outcome of welfare reform (2001, 2003); Huber and Stephens find nations' distinct production regimes to be a crucial cause of variation (2001a, 2001b).

Each of these perspectives contributes to the explanation of the cross-national variation in welfare restructuring in important ways. None of them explains it in its entirety. Even when taken together, they do not provide a convincing explanation of the question of how and why states made the decisions they did about their welfare states to begin with. Historical institutionalist analyses that focus on the differences in the welfare institutions, programmatic structures or welfare regimes may show us how countries differed in the particular ways they went about adjusting or transforming their welfare states once they decided to undertake adjustment; or approaches that focus on discourse may show us how the ways in which governments communicated their decisions about welfare adjustment to the public actually affected the failure or success of adjustment as well as the particular form it has taken. However, we still need to explain why and how each government has arrived at its decision of retrenching or retaining its welfare state. For this, I suggest, we need to find out how governments understood their problems, and what needed to be done about them, and more specifically, whether they saw the welfare state as one of the problems to be dealt with, or not. This, I argue, can be done with an institutionalist approach that assigns more emphasis to the role of agency, subjective interpretation and past experience in formulation of policy preferences. Along these lines, Hall's analysis of policy change as a form of social learning offers a good starting point.

Policy Change as Social Learning

In his article entitled 'Policy Paradigms, Social Learning and the State,' Peter Hall portrays economic policymaking as a process that takes place in a realm of ideas and principles that are institutionalized in the form of policy paradigms (Hall, 1993).[1] Policy paradigms operate like 'local knowledge' (Fligstein, 2001). They create a common and coherent understanding among policymakers as to what constitutes good policymaking and specify the policy instruments and mechanisms to be used. As Hall elaborates:

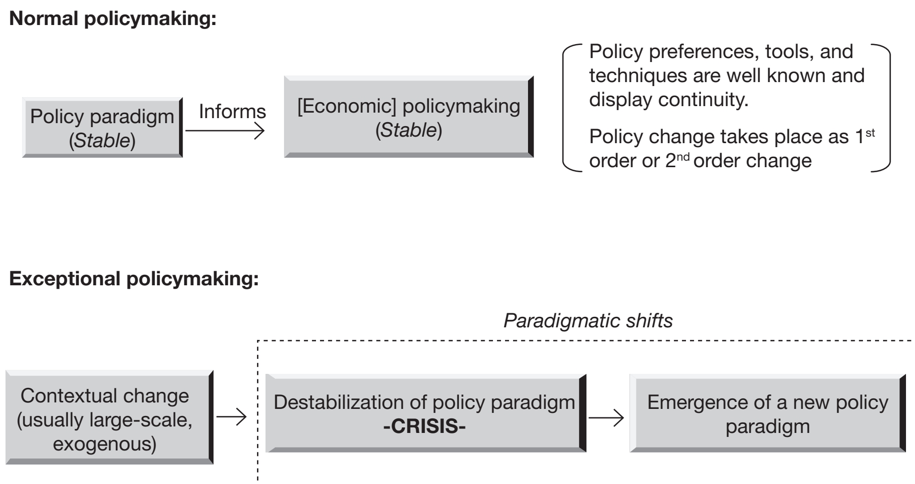
> Policy makers customarily work within a framework of ideas and standards that specifies not only the goals of policy and the kind of instruments that can be used to attain them, but also the very nature of the problems they are meant to be addressing. Like a *Gestalt* this framework is embedded in the terminology through which policymakers communicate about their work, and it is influential precisely because so much of it is taken for granted and unamenable to scrutiny as a whole. (Hall, 1993: 279)

According to Hall, policy change takes place in the form of 'social learning.' Policymakers deliberately adjust the goals or techniques of the policy in the light of past experience and new information. In other words, policy learning as 'social learning' is shaped by external changes on the one hand, and 'policy legacies' on the other.

Along these lines, Hall differentiates between periods of normal policymaking and exceptional policymaking. In normal times, policymaking remains a rather stable process. Policy learning usually takes the form of what Hall calls a 'first-order' or a 'second-order' change. It involves revisions or modifications in the settings, instruments or techniques of policy, rather than a change in the main ideas and goals that direct policy. Exceptional policymaking, on the other hand, refers to unstable times when the effectiveness of the paradigm becomes scrutinized due to certain developments, usually of an exogenous nature, with which the paradigm fails to offer an effective way to deal. Such periods, when there is a mismatch between the challenges a policy field faces and its traditional way of solving problems, constitute what is called a 'punctuated equilibrium,' in other words: a 'crisis.' As Hay elaborates, 'the very parameters that previously circumscribed policy options are cast asunder and replaced, and the realm of politically possible, feasible and desirable is correspondingly reconfigured' (Hay, 2001: 197). These periods witness experimentation with different methods and ideas. Policy learning remains oriented to building a new institutional equilibrium around a new paradigm.

Hall's model of policy change offers useful insights into the rise of neoliberal ideas in economic policymaking. In its emphasis on the possibility for post-crisis change to occur on different levels, it also offers a sound alternative to the convergence arguments in the globalization literature. Nonetheless, in its current form it remains a 'generic and abstracted conception of the policy learning process over time, into which specific events can be slotted' (Hay, 2001: 198).

Figure 1 Hall's model of policy learning



It does not theorize the relationship between ideational shifts,[2] on the one hand, and transformation/reconstitution of policy preferences on the other. While it might help us to understand why nations turned to neoliberal ideas in managing their economies at the end of the 1970s, it does not explain why this turn has translated into the specific forms of organization and policy outcomes that it has in these nations. In other words, the link between neoliberalism as 'a bundle of ideas promoting market solutions to economic problems' and neoliberalism as 'a set of policies' is missing, and without it, we are not able to explain where and why the particular form of 'learning' takes place.

I contend that the 'missing-link' problem in Hall's framework can be solved by problematizing the nature of the institutional crisis that prompted nations to turn to neoliberal ideas (Hay, 2001; Blyth, 2002). Nations have formulated different policies, I argue, because they experienced different sorts of crises. Here, I use the term 'crisis' in an objective and subjective sense. As I have stated before, the globalization literature tends to describe the problems and challenges posed by the new economic conditions in exclusively objective terms, as if the nature of the economic crisis were an obvious, universal reality, as were the solutions to it. It is important to realize, however, especially for comparative purposes, that the process through which countries decided what their crisis was *really* about remained a highly subjective process – one that depended on each nation's policymakers' interpretation of the new conditions vis-à-vis the historical patterns of policymaking.

In this sense, as Hay suggests, the concept of 'crisis' must be understood to imply two conditions. It implies the existence of a set of problems, constraints, chaos and uncertainty facing the field of policymaking. It also suggests, however, a point of 'decisive intervention' (Hay, 2001: 203). In other words, the crisis can be thought of as a two-step process. The first step (A: the objective terrain) involves the destabilization of the policy field by various pressures, usually of an exogenous nature. These pressures might manifest themselves in national statistics in the form of slowed growth rates, high inflation, rising unemployment, exchange rate instabilities, or budget deficits. They not only challenge the field but also constrain what governments are able to accomplish. Policymakers find their room to maneuver significantly diminished and experience limitations in using their traditional methods to deal with them. The second process (B: the subjective terrain) involves the diagnosis of what these objective problems really mean. Actors who are relevant to the policymaking process, such as technocrats, bureaucrats, or politicians offer various perspectives as to what constitutes the crisis in an attempt to influence the direction of the policy change that is to occur. While some actors insist on interpreting and acting on the problems through the existing paradigm, others offer new perspectives that often challenge its main premises. As problems seem more severe and traditional tools seem less apt, challengers gain more power intellectually and politically.

The battle between different actors and views over the construction of the crisis as a certain type remains central to the process of policy change. Indeed, as Blyth argues 'it is not until the agents argue over, diagnose, proselytize and impose on others their notion of what a crisis actually is that collective action to resolve the uncertainty facing them takes any meaningful institutional form' (Blyth, 2002: 9).

In a recent article, Block and Somers reflect on the factors that influence the course of ideational change: 'Fundamental ideational regime changes are rare,' they argue,

> To convert one ideational regime to another, the challenger must meet three difficult requirements. The new theory must, by means of its own logic, be able to demonstrate why the currently dominant ideas can only fail to solve society's problems. It must be able to explain how intelligent people could have been so misled. And it must be able to provide an alternative view of social reality by means of a more compelling public narrative. (Block and Somers, 2006: 271)

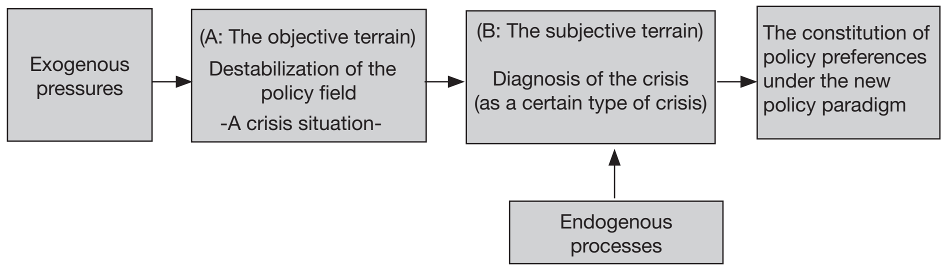
According to Block and Somers, ideas that meet these three requirements enjoy a 'comparative advantage', in effect an 'epistemic privilege' over available others in the battle to determine the direction of change. It is along such ideas that the crisis and its solutions tend to be constructed.

Block and Somers's perspective not only helps us to understand how neoliberalism was able to replace the existing policy paradigms in many nations, but also allows us to explain why its specific ideational baggage and policy prescriptions would differ across nations. As my analysis of the British and French cases will illustrate, in each nation the neoliberal re-embedding of economic policies took place around ideas and policies that effectively constructed the crisis of and solutions to the traditional framework in that nation.

In a word, then, in order to begin to understand the relationship between paradigmatic shifts, such as the turn to neoliberal ideas in economic policymaking on the one hand, and the constitution of policy preferences on the other, we first need to analyze what constituted the 'crisis'. Nations have devised different strategies and developed different policies (in the welfare arena, as well as others) because they were trying to deal with different types of crises in the objective and subjective sense of the word.

The institutionalist perspective developed here by no means offers a full account of neoliberal variation regarding the welfare policy. However, it has merits that go beyond the perspectives that are based on the 'three institutionalisms.' Three of these merits must be noted in particular. First, this approach induces a relational thinking. It attempts to explain the trajectory of the welfare reform by addressing a bigger question, namely the question of 'why some policies were up for grabs while others were not at the time when the neoliberal turn was taking place in economic policy.' In that sense, it allows us not only to explain welfare outcomes of the neoliberal turn,

Figure 2 Crisis and institutional change



but also to develop useful insights about the direction of change in other policy realms as well. Moreover, its emphasis on agency and subjective interpretation combined with its historical approach to the development of economic policy over time enables us to transcend some of the problems inherent in solely *agentic* or path-dependent accounts. Last, but not the least, this approach forms an analytically sound bridge between neoliberalism – *the independent variable*, understood as ‘a heuristic and policy paradigm in political-economic discussions defined by market-oriented political-economic policies and reforms’ (Holzemeyer, 2003), and neoliberalism – *the dependent variable*, understood as a set of policies.

The study of the British and French cases in the next section attempts to show precisely how the interplay of the objective and subjective bases of the crisis determined the form that neoliberalism took in each country, and how it affected the course of welfare reform.

BRITISH TURN TO NEOLIBERALISM

From the perspective of the model of policy change that has been developed so far, the transformation of British economic policy from the end of the Second World War through the end of the 1980s can be divided into three periods:

1) 1945–70: the period of 25 years after the war when economic policy was shaped by a highly coherent system of ideas known as Keynesianism – the period of paradigmatic stability.
2) 1970–9: when Britain’s failure in dealing with the challenges posed by the changing world economic structure decreased the legitimacy of Keynesianism as a viable framework – the period of paradigmatic crisis.
3) 1979–90: when Keynesianism was abandoned in favor of a neoliberal framework with the election of Margaret Thatcher – the period of paradigmatic shift.

In an attempt to explain the implications of this paradigmatic shift for the welfare state, I first analyze the interplay of Keynesianism and the welfare state throughout the postwar period and then discuss how the relationship between the two became re-ordered in transition to neoliberalism after the crisis of the 1970s.

1945–70: The Postwar Institutionalization of the Keynesian Paradigm

When the Second World War ended, economic policymaking in Britain was oriented to three goals: achieving full employment, sustaining exchange rate stability, and providing social welfare to citizens. In the turn to Keynesian ideas in economic policy, these goals played an important role. As a paradigm that assigned major responsibility to governments in maintaining economic stability and growth, Keynesianism offered exactly what was needed at a time when the British government was in search of a framework that would direct and legitimate its active intervention in the economy.

The functioning of the British economy along Keynesian ideas took place by means of two major policy instruments: aggregate-demand management and incomes policy. The level of aggregate demand in the economy was adjusted through manipulation of government expenditures and/or level of taxation. When the economy was growing, and there were strong inflationary pressures and a deficit in the balance of trade, the government would raise tax rates and/or cut government expenditures in an attempt to produce a budget surplus; and when the economy was experiencing recession, the reverse policy would be followed in order to stimulate aggregate demand.

Aggregate-demand management was a successful technique for stimulating employment. However, it did not prove to be quite as effective in dealing with the rising rates of inflation. In the inflationary context of the 1960s, incomes policy was initiated as a supplementary Keynesian tool aimed precisely at dealing with inflationary pressures in the economy. Incomes policy involved controlling the rate of inflation through voluntary or compulsory controls on the growth of wages. The effective use of this policy required amicable relations between the government and trade unions. With the initiation of this policy, British Keynesianism came to embrace collective bargaining as a major policy practice; and keeping strong relations with the trade unions remained a serious concern for the stability of the Keynesian paradigm as well as the stability of the British economy throughout the postwar years.

Postwar Development of the British Welfare State

Britain's welfare state developed steadily under the auspices of Keynesianism. The first major step toward the development of a comprehensive welfare state took place in 1942 with the Beveridge Report. This report proposed a system of social protection that would provide comprehensive and universal welfare benefits for citizens. The Attlee government that entered office in 1945 was committed to achieving these goals and, backed by the Keynesian economic rationale, brought in such legislation as the National Insurance Act, the National

Health Service Act, and the National Assistance Act that broadly carried out Beveridge's ideals of a comprehensive welfare system (Myles, 1984; Hill, 1993).

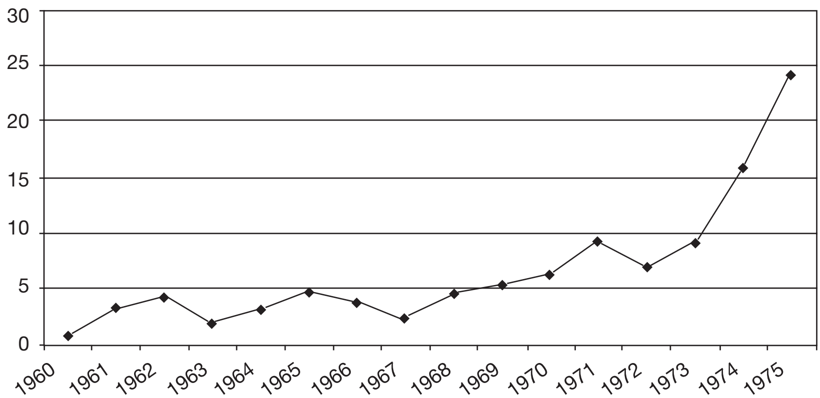
Throughout the 1940s, the British welfare state was upheld as a model to the world. A decade later however, the level of social spending on social security (as a percentage of GDP) in many other European countries surpassed Britain's. These countries were West Germany, Austria, and Belgium by 1950; France and Denmark by 1952; Italy by 1954; Sweden by 1955; and the Netherlands by 1957.[3] Despite its relative stinginess in terms of the aggregate amount that was allocated to social spending, Britain's welfare state expanded steadily and remained a major economic and political institution throughout the postwar era. The share of social expenditure in GDP increased to 23.7 percent in 1981 from 13.9 percent in 1960 (OECD, 1985). Underlying this consistent expansion was the Keynesian consensus, shared both by the Labour Party and by the Conservatives, that welfare spending constituted a useful economic regulator, which could be used to stimulate the economy during times of recession (Marwick, 1968; Janowitz, 1976; Hall, 1986; Quadagno, 1987; Pierson, 1994).

1970–9: Economic Downturn and the Breakdown of the Keynesian Consensus

The world-scale economic developments that took place in the 1970s affected Britain adversely, leading to exchange rate stabilities and stagflation in the country's economy. Britain's reaction to the challenging economic environment of the 1970s took place in two phases. Until 1976, during the four-year Conservative administration, and the next two years following it under a Labour government, Britain responded to economic challenges with traditional techniques, promoting a rather 'orthodox Keynesianism' (Hay, 2001: 210). These policies, however, did not remain effective in solving Britain's economic problems. Edward Heath's Conservative government's (1970–4) attempts to solve the problem of inflation by resorting to incomes policy failed terribly, ending in militant action and massive strikes by unions and coal miners. The general election that took place in February resulted in Labour's victory, marginally so, however, leading to a minority government.

By March 1974, when the Labour government headed by Harold Wilson came to office, the world's oil producers had raised fourfold the price of oil; inflation had increased to 16 percent (from 9.2 percent in 1973); the balance of payments, which had been in surplus in the previous years, had moved into deficit; and recession was at the door (Hall, 1986; Cairncross, 1992; Britton, 1994; Harmon, 1997). In addition, as Britton points out, 'the circumstances in which the Labour Party came to power further reduced their freedom of action' (Britton, 1994: 18). Militant action by the unions seemed to have played an important role in its electoral success. Therefore, being on good terms with the unions remained a major priority for the new government, inhibiting its actions in the field of economic policy (Britton, 1994). Within these circumstances, economic policy during Labour's first year in office was seen largely as a process

Figure 3 Rate of inflation in the UK (1960–75)



Source: National Statistics: [www.statistics.gov.uk].

of 'wage negotiation' with union leaders (Britton, 1994: 19). It remained limited to dealing with short-term exigencies to avoid further political crisis.

The second general election of 1974 also resulted in a Labour victory, giving it a working majority in parliament. For the next few years that followed, economic policy was governed by a consistent Keynesian approach that had evolved in the Treasury and the Bank over the previous 30 years (Britton, 1994). During this period, the diagnosis of the 'crisis' remained in entirely Keynesian terms. Thinking that the 'crisis' was of a temporary nature, not related to the fundamentals of the British economic policy, the government went ahead and exercised expansionary policies, increasing social spending and public sector wages (Harmon, 1997). Far from offsetting the economic problems, however, these policies aggravated Britain's economic problems. The effect of these expansionary policies was particularly visible on the rate of inflation. The rate of inflation in 1975 reached 24.2 percent (OECD, 1990). In this context, controversy over economic policy began to focus on the issue of how inflation was to be brought under control.

In the mid-1970s, the pressures upon the government for policy change intensified. These pressures were multifaceted, as Harmon argues, 'occurring at the structural level from the financial markets, at the bilateral level from the US and Germany and at the multilateral level from the IMF' (Harmon, 1997: 158). At the domestic level, the sources of pressure were even more complex. Labour's inability to deal effectively with economic problems, particularly with high inflation, created major discontent among all segments of the society. In this context, Keynesianism came under increased challenge from a variety of groups, including the City of London, a new array of libertarian think tanks, and some very prominent financial journalists such as Nigel Lawson, Sam Brittan and Peter Jay (Cairncross, 1992; Britton, 1994; Fourcade-Gourinchas and Babb, 2002). Of particular visibility were the criticisms by the City and the financial press, which vigorously endorsed a monetarist view of the economy as articulated by Milton Friedman in the 1960s. Their position did not find an easy welcome on the side of the government and economic policy institutions, however. As Britton explains, 'the monetarists were winning over the press, the city and the Conservative Party, but they had as yet scarcely a toehold either in the Treasury or the Bank' (Britton, 1994: 24). There was, in Grant's words, 'too much intellectual and personal capital invested in Keynesianism' (2002: 32).

Between 1976 and 1979, faced with a deteriorating economy, IMF pressures, and diminishing electoral popularity, the Labour government now headed by James Callaghan had to accept making certain modifications in its economic policy (Hay, 2001). This period marked the end of orthodox-Keynesianism in Britain. After this point, the Labour government began to rely on a mixture of monetary and Keynesian tools for economic management, switching to what is generally described as a 'hybrid, monetarily-constrained Keynesianism' (Hay, 2001: 210); 'frustrated Keynesianism' (Grant, 2002: 31); or 'cautious Keynesianism' (Britton, 1994: 33). As Britton explains:

> The cautious Keynesians both ministers and officials remained in power for a few years yet and the approach to economic policy which they supported was not altogether abandoned. But their intellectual position was much weakened by the events of 1976 and quite different ideas about the aims and instruments of policy were becoming influential even in the Treasury and the Bank. (1994: 33)

The speech by the Prime Minister Callaghan to the 1976 party conference reflected the shift:

> We used to think that you could spend your way out of a recession, and increase employment by cutting taxes and boosting government spending. I tell you in all candour that that option no longer exists, and that in so far as it ever did exist, it only worked by injecting a bigger dose of inflation into the economy, followed by a higher level of unemployment as the next step.

The turn to hybrid-Keynesianism in economic management was still far from constituting a paradigmatic shift, however. The Labour government of 1976–9 had not abandoned its Keynesian view of the economy altogether; it had only begun to pay increasing attention to the growth of the monetary aggregates (Hall, 1993). Indeed, as Hay notes, this period was marked by a 'clear gulf between the instruments of economic management deployed by the British state, which were increasingly monetarist in inspiration, and the governing paradigm and (attendant political goals), which continued to be broadly Keynesian and welfarist' (2001: 209).

As Britton explains:

> The aims of macroeconomic policy and its basis in an understanding of the way economy works, were particularly unclear in the final phase of the Labour government. The immediate need to follow the lead given by the IMF had receded during the 1977. There could however be no explicit going back to traditional Keynesian policies of reflation as

> exemplified by the later Heath years; the experience of 1976 was still very recent and very chastening. On the other hand, ministers and top officials at the Treasury and the Bank were not intellectually converted to the approach of the monetarists. They now treated it with far more respect than they would have done a year or two previously, but with the detached respect of non-believers. It was a period of intellectual confusion, or perhaps of transition. (Britton, 1994: 39)

The strategy of hybrid Keynesianism did not prove to be successful. Britain's economic condition continued to deteriorate between 1976 and 1979, so much so that the country, which had been among the richest OECD countries in the 1950s, ranked among the poorest OECD countries by the end of the 1970s. The government's insistence on resorting to incomes policy to control inflation in the context of worsening economic conditions aggravated union unrest, leading to the massive strikes and work stoppages known as the 'Winter of Discontent' in 1978.

These developments intensified growing public reaction against Labour's Keynesian economic policies, and created an electoral shift in favor of the Conservatives. In the 1979 elections, 43.9 percent of the electorate voted for Thatcher, who wanted to change the workings of the economy in a radical fashion (Butler and Kavanagh, 1980).

Post-1979: Shift from Keynesianism to Neoliberalism and the British Welfare State

With the election of Margaret Thatcher, the economic policy embarked on a complete change of direction (Lawson, 1992), and the paradigmatic shift from Keynesianism to a neoliberal framework was completed (Hall, 1986, 1993).

British neoliberalism under Thatcher had two underpinnings. One of these was embracing a monetarist approach to the economy, which had been promoted for some time by the City of London, financial journalists and influential economists following Milton Friedman, as the 'right' way of thinking. This meant that limiting inflation rather than commitment to full unemployment would be the priority of economic policy, and Keynesian techniques of aggregate demand management, particularly using fiscal policy instruments, would be abandoned.

There was more to Thatcherism than just monetarism, however (Middleton, 2000). The Conservative Party under Thatcher saw the economic problems that Britain experienced in the 1970s as symptomatic of a more fundamental crisis, which could not be handled by changing the economic instruments only. In their view, Britain had a 'state' crisis. The reasons behind the transformation of what had once been the greatest economic power in the world into a struggling economy lay in the particular vision of the 'state,' and its relationship to the economy and society that was embodied in the Keynesian worldview. In this respect, Britain's turn to neoliberalism was not simply about switching to monetary instruments; there was a strong Hayekian sub-text to it, which meant transforming the state-economy-society relationship in a radical manner (Fourcade-Gourinchas and Babb, 2002).

Three issues were particularly emphasized as major elements of the crisis of the Keynesian state: one, the state's excessive intervention in the economy had undermined the markets. Two, the authority of the state vis-à-vis the unions had been undermined. Three, through its welfare programs, the state had turned a 'do-it-yourself' nation into a 'give-it-to-me' nation (Schmidt, 2001: 257). The turn to neoliberalism was intended to reverse these policies.

The formal objectives of the Conservative government were initially laid out in its manifesto. Here, Conservatives criticized the Keynesian management of the economy in the following way:

> The state takes too much of the nation's income; its share must be steadily reduced. When it spends and borrows too much, taxes, interest rates, prices and unemployment rise so that in the long term there is less wealth with which to improve our standard of living and our social services. (1979 Conservative Party General Election Manifesto)

This was a direct echo of the views of Hayekian scholars such as Bacon and Eltis, who argued that Britain's economic problems were due to the 'excessive burdens imposed by the state on the taxpayer and the consequent pre-emption of scarce resources to meet welfare and other needs that lay outside the operation of market forces' (in Cairncross, 1992: 30). According to this view, government intervention in the market through taxation, welfare measures and restraints on business activity had led to wages that were too high, unemployment and lack of initiative. As a remedy, the Conservatives sought 'the reduction of waste, bureaucracy and over-government' in economic management (1979 Conservative Party General Election Manifesto).

Such a diagnosis of the crisis tells much about the form of institutional change that Conservatives hoped to undertake in the transition to neoliberalism. In Britain, neoliberalism was meant to provide a radical break with the past, a complete political redefinition of the desired form of state and society (Fourcade-Gourinchas and Babb, 2002; Schmidt, 2002).

The postwar expansion of the welfare state in Britain was an integral part of the Keynesian paradigm. The repudiation of Keynesianism in the context of a perceived 'state crisis' articulated in Friedmanite and Hayekian ideas posed a direct challenge to Britain's postwar welfare policy. It represented the collapse of the consensus on which the welfare state had been created. The Conservative manifesto criticized the Keynesian welfare state on the grounds of developing a kind of 'dependency' relationship between the state and society over the years, posing a threat to personal freedom, weakening incentives and penalizing success. The difference in the social conditions of those who were hardworking and successful and those who were lazy and unemployed was natural, and it was not the state's responsibility to compensate for this difference.

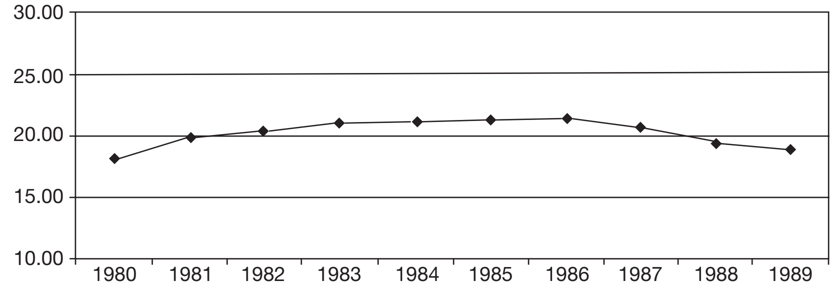
British welfare reform was comprised of four objectives: decreasing the size of the social security budget; eliminating the 'why work?' problem by restoring incentives so that 'hard work pays, success is rewarded and genuine new jobs are created in an expanding economy' (1979 Conservative Party General Election Manifesto); restructuring the social security system in a way that provides support to those who are in 'real' need; and finally, simplification of the social welfare system by way of reducing state's involvement in social protection while at the same time encouraging market mechanisms (e.g. privatization of social security) in the attainment of the welfare goals (MacGregor, 1985).

Policy implementation was achieved in all these areas, to varying degrees. Throughout the 1980s, the British government remained committed to cutting back the size of the welfare state. Britain had fallen behind other European countries in social spending throughout the entire postwar era, except for the 1940s. In 1979, when the Thatcher government took office, social security expenditure in the UK as a proportion of GDP was around 18 percent, as opposed to 21 percent in France (OECD). In terms of its capacity for de-commodification,[4] as well, the British welfare system remained behind all other European nations (with the exception of Ireland). The de-commodification index in Britain circa 1980 was 23.4, as opposed to 27.5 in France, 27.7 in Germany and 39.1 in Sweden (Esping-Andersen, 1990). Despite this, in the first white paper published in 1979, her first year as Prime Minister, Margaret Thatcher argued that public expenditure was at the heart of Britain's economic difficulties. Since the British welfare system is demand-led, the level of spending could not be decreased by imposing cash limits in the budget (MacGregor, 1985). As the number of the entitled population increased, the volume of provision would increase also. Changes that aimed at reduction in the size of welfare expenditures would have to be made either by cutting the level of benefits or by altering the rules governing the entitlement to benefit (MacGregor, 1985). Both methods were employed by the government. *Due to the rise in the number of dependents* – the overall increase in the total number of dependents is estimated to have been around 60 percent during Thatcher's first term in office, between 1979 and 1983 (MacGregor, 1985); the increase in the number of claimants of unemployment benefits only, between 1980 and 1987, is estimated to have been around 200 percent – the decrease in total welfare expenditure fell behind the aspirations of the Thatcher government. *Despite such a substantial rise in the number of dependents*, however, social expenditure decreased in most areas between 1980 and 1990. The cutbacks became particularly more pronounced in the second half of the 1980s.

Unemployment benefits became a particular target in Britain. The government argued that the generosity of unemployment benefits was creating a 'why work?' problem and that if unemployment benefits were reduced, people would actually work. In line with this logic, spending on unemployment was reduced by more than 50 percent over a period of 10 years.

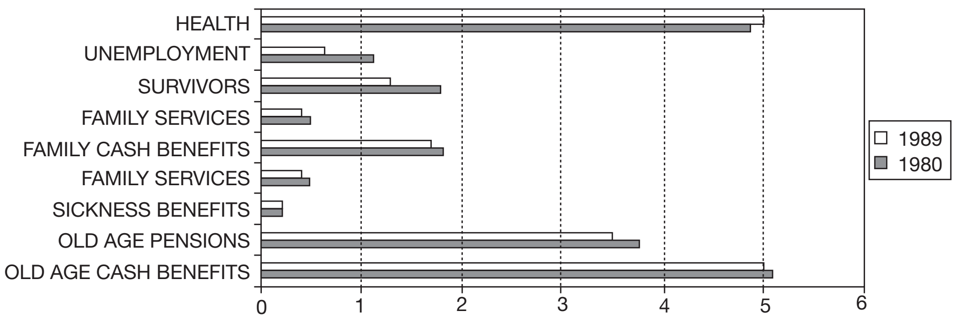
The Conservatives also reduced the level of universal entitlements and increased the importance of means-tested benefits. Universal programs were defined as ill-targeted and wasteful. Maternity and death grants were abolished;

Figure 4 Social spending as a % of GDP during Thatcher's term (UK: 1980–90)



Sources: OECD; Huber et al. (2004).

Figure 5 Social spending by Type (UK: 1980 versus 1989)

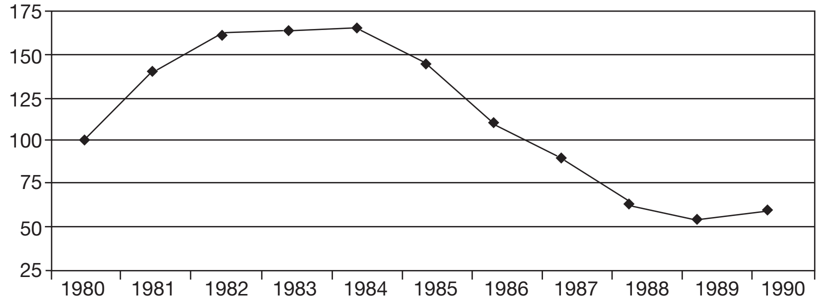


Source: OECD.

child benefits were cut back to a 30-year low in the mid-1980s; and old-age pensions were curtailed. In 1982, the index of the Basic State Pension was changed from earnings to prices, and in 1986, the Social Security Act halved the benefit levels under the State-Earning-Related-Pension Schemes (SERPS) by basing entitlements on whole employment-career earnings rather than the best 20 years (Daguerre and Taylor-Gooby, 2002). Among universal benefits, only the health system remained resilient. The reason for this was political calculation. The government figured that given the popularity of health benefits among the middle class, a major source of electoral support for Thatcher, retrenchment in this realm would be particularly difficult and would be harmful to the Conservatives' electoral support.

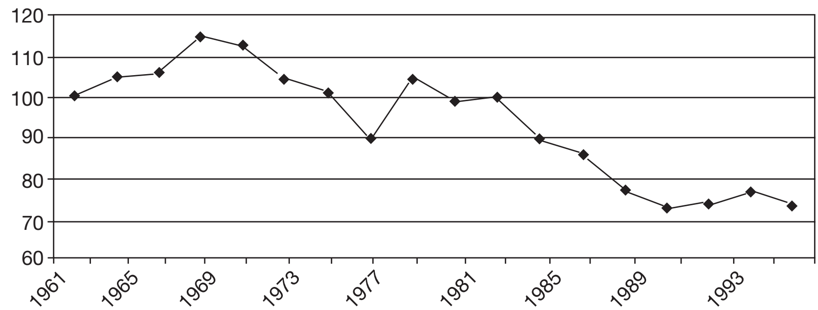
Another development was the attempt at privatization of social security. Alone among the biggest industrialized nations, Britain took the most aggressive steps to shift responsibility for retirement income from government to individuals. The 1986 Social Security Act sought to promote personal pensions by extending the right to individuals to opt out of the pension scheme (Daguerre and Taylor-

Figure 6 Social spending per poor (UK: 1970–90)



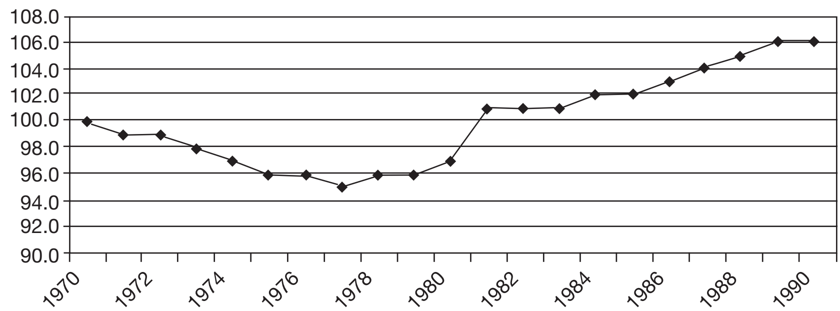
Sources: Author's own calculations. Data on social spending from: Huber et al (2004). For poverty rates: National Statistics website [www.statistics.gov.uk].

Figure 7 Evolution of social wage (UK: 1970–95)



Source: Huber et al. (2004).

Figure 8 Inequality in workers earnings (UK: 1970–90)



Source: Huber et al. (2004).

Gooby, 2002). Workers were encouraged through a combination of tax breaks and educational campaigns to invest a portion of their payroll taxes in a private investment account or a company-sponsored investment program (Daguerre and Taylor-Gooby, 2002).

The extent of these changes in the welfare system can be better understood when situated in the context of the country's rising social inequality and insecurity. As Clayton and Pontusson have persuasively argued, a nation's real welfare effort can be judged to the extent that it meets societal welfare needs (1998). After all, the whole point of welfare systems remains to improve the conditions of the people in need. In the British context, throughout the 1980s, the conditions in question substantially worsened. Poverty and inequality increased severely for wage earners throughout the 1980s. Social wage, a widely accepted measure of social-welfare policy extensiveness measured in terms of 'the percentage of former income that a median-income worker if she or he stops working' (Kenworthy, 1999: 1126), decreased substantially.

In sum, the rise of neoliberalism in Britain attended a period of crisis. Objectively, the crisis manifested itself in the form of a slower growth rate, balance of payments deficit, high inflation and high unemployment early in the 1970s. While these problems were initially interpreted as transitory in nature by the Labour party, public's decreasing approval of government policies in dealing with these problems, mounting unrest on the part of the labor unions, and external pressures emanating from the IMF, Germany, and the US created the conditions for a major change in economic policy.

As I have discussed in length earlier in the article, major changes in policy ideas and practices occur around actors' subjective interpretations of the existing problems. Throughout the 1970s, the field of economic policy in Britain witnessed a period of transition, remaining subject to different views as to what constituted the crisis and what must comprise the solutions. The resort to monetarist techniques to fight with inflation signaled the dissolution of the orthodox Keynesian view. After 1979, with the election of Thatcher, the direction of change in economic policy became clear. The Conservative government under Thatcher interpreted Britain's problems as outcomes of a 'state crisis'. From this perspective, which found its theoretical articulations in the works of Hayek and Friedman, at the source of Britain's problems lay the diminished authority of the state toward certain groups, such as trade unions, and the role it had come to play as a kind of a 'nanny state,' extending extensive welfare to society. Policy reform took shape along these lines. The welfare state was deemed part of the 'problem'.

THE NEOLIBERAL TURN IN FRANCE

The tale of French economic policymaking from 1945 through the end of the 1980s centers on institutionalization, crisis and the demise of *dirigisme* – a policy framework oriented to achieving rapid modernization through active state intervention in the economy. The time frame within which such a transformation took place can be divided into three parts.

1) 1945–74: a 30-year period that was highly successful, known as *les trente glorieuses,* when the French economy enjoyed high growth rates and became the biggest economy in Europe under the *dirigiste* paradigm – the period of paradigmatic stability.
2) 1974–83: a period of 10 years when, faced with the destabilizing effects of two oil crises, of the demise of the Bretton Woods system, and of the inroads made by European integration on the economy, subsequent French governments came to accept the limits of *dirigisme* and began experimenting with different policy ideas and tools – the period of paradigmatic crisis.
3) Post-1983: when French economic policymaking moved away from *dirigisme* in the direction of a neoliberal framework – the period of programmatic change à la neoliberalism.

In order to get a better grip on the course of French welfare policy, one must analyze the interplay of *dirigisme* and the welfare state throughout the postwar period and how the relation between these two became re-ordered in transition to neoliberalism at the end of the 1970s.

Postwar Institutionalization of the Dirigiste Paradigm

At the heart of French *dirigisme* lay the objective of accelerating the pace of economic modernization by channeling resources to key industrial sectors (Hall, 1986; Cole, 1998; Levy, 1999, 2000). This objective was put into operation through three major policy practices: one was the system of national planning, through which the state specified its formal role in economic management, the goals of economic policy, and the ways in which to achieve them. Second was the nationalization of industrial sectors that were considered crucial for the country's development and national independence, such as nuclear power, high-speed trains and digital telephone switches. In order to enhance these key sectors, the state undertook *grands projets* that combined subsidies and technology transfers. And third, was the provision of benefits to industry, to the private as well as the public sectors, in the form of protection from foreign competition through aggressive devaluations in currency and cheap loans through the subsidized credit system. *Dirigisme* functioned quite effectively in the first 30 years following the Second World War. Until the mid-1970s, France remained one of the most prosperous countries in Europe.

Postwar Development of the French Welfare State

The postwar expansion of the welfare state in France was not closely linked with the country's postwar development paradigm. Indeed, as Levy notes, 'for much of the postwar period the French welfare state operated in the shadow of the *dirigiste* model of economic development' (2000: 308). From the perspective of *dirigiste* policymakers, whose primary concern was to make French industry competitive, the welfare state represented a waste of financial resources, which instead should have been allocated to productive investment (Levy, 2000). What prompted the development of the welfare state in France was rather the internal political dynamics of the country. The size and structure of the welfare state changed in conjunction with the changes in the French political context. Among such contexts, De Gaulle's presidency between 1959 and 1969 provided a particularly favorable milieu for the postwar expansion of the welfare state. As Levy notes:

> De Gaulle saw the state as the agent of modernization and the general will, overriding parochial, self-serving traditional elites in order to restore France to greatness. An enlightened, interventionist state was essential to economic and political recovery. It was also essential for transcending class conflict: the French working class would be wooed away from leftist politics and political unionism by a more elaborate and better financed welfare system as well as expanded opportunities for the upward social mobility. (Levy, 2000: 318)

Welfare spending increased by 70 percent under de Gaulle, and its expansion continued during the presidency of Pompidou who also adhered to Gaullist ideas and policies. Its share in GDP, which was 13.4 percent[5] in 1960, reached in 29.5 percent in 1981 (OECD, 1985)

1974–83: Destabilization of the French Economy

Starting from the mid-1970s, the contextual factors that remained favorable to *dirigisme* began to shift. The oil shocks of 1973 and 1979 put Europe into a prolonged recession, ending the rapid growth that France enjoyed during the postwar period. Exercising aggressive devaluations, which had made an inflationary growth strategy feasible during the postwar years, became risky in the post-Bretton Woods environment. In addition, the Treaty of Rome became fully active, forcing France to reduce its barriers to its trade partners and face intense competition. As Cole notes, 'these developments highlighted the external constraints weighing upon the French economy, and the limited room for maneuvering of its governments in initiating policies' (Cole, 1998: 212). French policymakers during this time, like their counterparts in Britain and other European countries, had to figure out ways to reconcile economic objectives with the realities of the new international environment.

Throughout the postwar years, French firms had often been sheltered from foreign competition by tariffs and subsidies, and they had tended to be oriented toward producing more rather than producing more competitively (Hall, 1986). The elimination of tariffs among European partners now raised the question of whether French industry was strong enough to face such competition, and it led to the fear that French companies might lose their share of the domestic and international markets. The shortcomings of *dirigisme* became increasingly apparent in this context. It was clear to many that the French economy would have to adjust itself. The nature of such adjustment would change course several times throughout the 1970s and early 1980s, depending on each subsequent administration's interpretation of what really constituted the crisis.

1976–81: Rolling Back the Frontiers of the State

Faced by a declining industrial production and increasing unemployment, in 1976, President Giscard d'Estaing appointed Raymond Barre – an economist who was known for his liberal views on the economy, as the Prime Minister and charged him with ending industrial stagnation, the foreign trade deficit, and inflation. Barre understood France's economic problems to be related to the extensive role played by the state in the management of the economy, particularly in the management of the industrial sector. As a remedy, his government started an array of market-friendly reforms that included decreasing the aid that was extended to national champions, lowering of subsidies, dismantling price controls, and reducing restraints on the business sector (Levy, 1999). These reforms did not include welfare retrenchment, however. Indeed, during Barre's term social spending increased drastically. The reason for this is that the Barre government's interpretation of the crisis did not center on the welfare state, but rather it focused on the industrial policy.

Barre's economic strategy, known as 'industrial redeployment,' signified France's first move toward neoliberalism in economic policymaking. However, it floundered. This was in part due to the aggravating effects of the OPEC oil shocks, and, in part, as Cole notes, 'because of the belief that there was an alternative economic strategy, a belief not confined to the ranks of the left-wing opposition' (Cole, 1998: 215). Neither the public nor the French political system was ready for a paradigmatic shift. The 1981 elections were marked by the Socialists' victory. Giscard was replaced by François Mitterrand who promised to bring the state back in, and Pierre Mauroy became prime minister.

1981–3: Bringing the State Back In

In a marked contrast with Barre's understanding of the crisis, the socialist government argued that the problem was not that there was too much state but rather there was too little of it (Levy, 1999). Government officials argued that 'what France needed now was a "real industrial policy," that it was time for the state to move to center-stage in restructuring France's economy' (Levy, 1999: 43–4). Repudiating many of the policies of its predecessor, the Mitterrand government nationalized some 38 banks, increased aid to industrial firms, raised taxes, and expanded social benefits (Hall, 1990, Levy, 1999). Like in his predecessor's term, the expansion of the welfare state continued during Mitterrand's presidency.

Mitterrand's expansionary policies led to a massive balance-of-payments crisis. The exchange rate, which had been pegged to the German mark since 1979, came under severe pressure, and France was forced to devalue the franc three times. These developments formed a threat to France's position in the European Monetary System, which was a major concern for the Mitterrand government. The year 1983, when the economic crisis reached its peak, proved to be the turning point for French economic policy. In an attempt to remain within the EMS, the government changed the direction of its policy and began to implement an austerity program. Its traditional inflationary growth strategy was abandoned in favor of a neoliberal point of view that emphasized the virtues of 'competitive disinflation' (Levy 1999: 52).

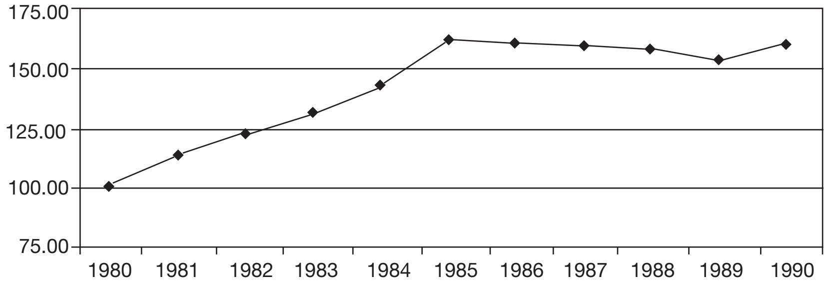
Post-1983: The Shift from Dirigisme to Neoliberalism and the Welfare State

The neoliberal turn in France that attended the crisis of *dirigisme* from the perspective of policymakers occurred in two ways. First, its method of enabling rapid growth through inflationary means became impossible in the new international context. Second, the competitiveness of French industry came under scrutiny. The massive production sites, which had formerly been credited for France's rapid growth, were now seen as a part of the problem. In this context, tying up resources in traditional *dirigiste* projects at the expense of emerging priorities and increasing inflation appeared increasingly problematic (Levy, 1999).

Unlike in Britain, the definition of the crisis and the proposed solutions did not really focus on welfare policy and social expenditures but on the state's interventionist industrial policy. In other words, in the French case, the welfare state was not depicted as a 'problem.' The neoliberal reform that was undertaken by the Mitterrand government involved dismantling many of the key instruments of *dirigisme,* such as competitive devaluations, interventionist industrial policy, nationalization of public sector enterprises, and subsidized credits. These policies were undertaken in the name of modernizing the France and making her apt to face the challenges of the new global context (Fourcade-Gourinchas and Babb, 2002). The array of changes, however, did not include the withering away of the welfare state. Public expenditures in many areas have not decreased but increased since 1983. Indeed, as Levy argues, 'France's welfare state has emerged from the shadows of *dirigisme*' (Levy, 2000: 309). The *dirigiste* paradigm had remained as a break on social spending throughout the postwar years; its dismantling triggered a reverse trend – a relentless expansion in social spending. Social spending rose from 23.5 percent of GDP in 1980 to 26.7 percent in 1990. By 1995, France became the heaviest social spender in Europe, outside Scandinavia (Levy, 2000). This period also saw a reduction in inequality and an increase in social wage.

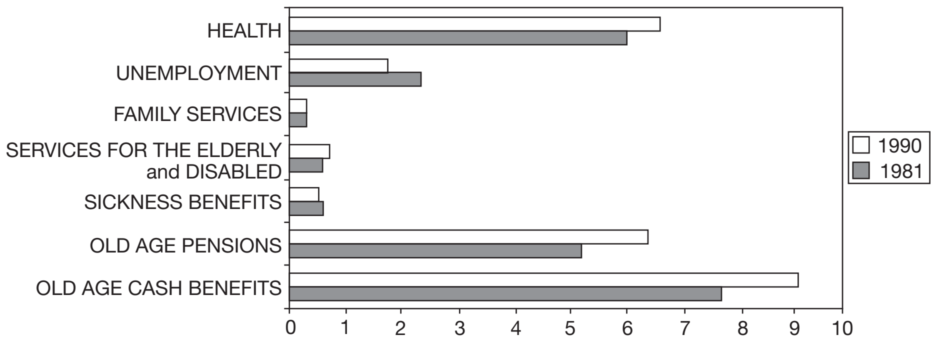
In sum, the crisis in France manifested itself in such objective indicators as slower economic growth, high inflation, high unemployment, balance of

Figure 9 Social spending as a percent of GDP (FR: 1980–90)



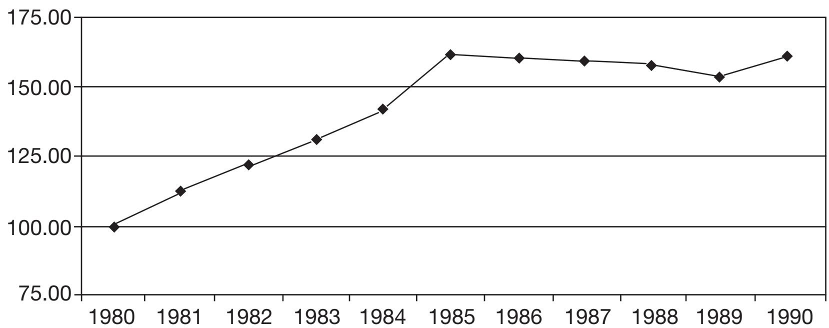
Sources: OECD; Huber et al. (2004).

Figure 10 Social spending by type (Fr: 1980 versus 1990)



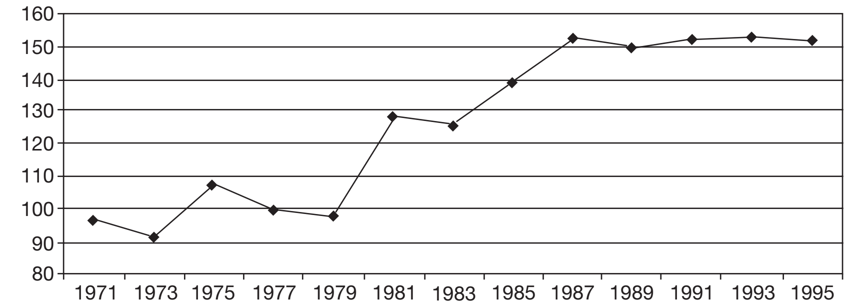
Source: OECD.

Figure 11 Social spending per poor (Fr: 1980–90)



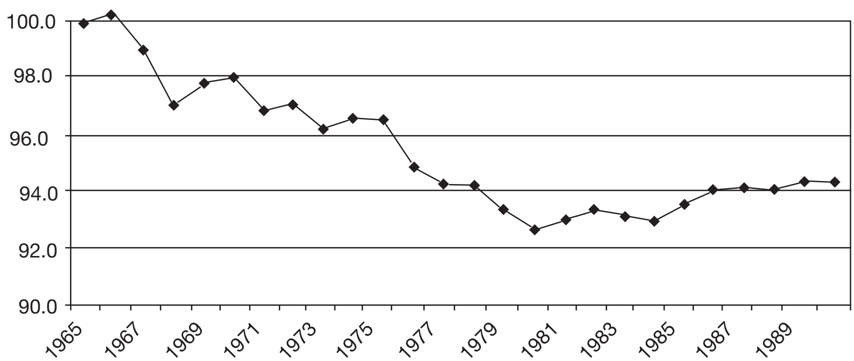
Sources: Author's own calculations. Data on social spending: Huber et al. (2004). Poverty rates: INSEE (Institut National de la Statistique et des Études Économiques).

Figure 12 Evolution of social wage (Fr: 1970–95)



Source: Huber et al. (2004).

Figure 13 Inequality in workers earnings (Fr: 1965–90)



Source: Huber et al. (2004).

payments deficit and exchange rate instabilities. Moreover, France's commitment to stay in the EMS made it impossible for her to devalue the franc and forced her to sustain a low level of inflation. In this context, maintaining an inflationary *dirigiste* growth strategy became increasingly difficult. On the subjective realm, France's decreasing rate of productivity cast the desirability of such strategy into a doubtful light in the first place. Once a model of rapid economic growth, *dirigisme* began to be seen as a model of growth that was not enabling France to grow any further, wasting her funds, and leading to high inflation. In the French case, the construction of the crisis took place around and problematized issues such as the high degree of nationalization of and regulation in the economy, which remained central to the *dirigiste* model. The welfare state was not among these issues.

Levy explains this paradox in the following way:

> Welfare policy played a critical role in France's move away from dirigisme. In a logic first articulated by Karl Polanyi, the extension of market forces was softened, made politically

> acceptable through the expansion of social protections for those most affected by liberalization (Polanyi, 1944). On the one hand, beginning in 1983, state authorities made a market imposing liberalization from above. Austerity, privatization, deregulation and labor market flexibility all heightened the vulnerability of French workers. On the other hand, successive governments especially those on the left, expanded the welfare state in number of ways so as to cushion the blow to the working class. (Levy, 2000: 326)

CROSS-EXAMINATION AND CONCLUSION: VARIETIES OF NEOLIBERALISM AND WELFARE REFORM

Peter Hall argues that one of the prominent challenges facing contemporary comparative researchers is 'to identify the cross-national patterns in processes of adjustment and to explain why each is taken' (2001: 235). In studying the constitution of national welfare policies in the context of a worldwide neoliberal turn, this article has attempted to do just that. The objective here is to cast doubt on those accounts, which, typical of the globalization literature, suggest a unidirectional relationship between neoliberalism and welfare retrenchment through an alternative approach that takes the nation-state seriously as a unit of analysis. In doing so, the article has also attempted to offer significant insights into the process of policy formulation and more specifically into the process through which programmatic and paradigmatic ideas such as Keynesianism and neoliberalism translate into concrete policy preferences.

The neoliberal turn in economic policy has had different implications for the welfare states around the world. In order to explain the variation, this article has analyzed the trajectories of the French welfare system, which is seen as perhaps the most 'immovable object' among Western European welfare regimes (Pierson, 1998; Palier, 2001), and that of the British, where the agenda for reform has remained comparatively far more substantial. Beginning in the early 1980s, both Britain and France began to organize their economies along neoliberal ideas. In both countries, the turn to neoliberalism attended a period of crisis. For both, the crisis was rooted in the constraints that were inflicted upon them by the changing world economic structure. Namely, both countries experienced severe inflation, slowing productivity growth that arose from two oil shocks, and exchange-rate instabilities stemming from the demise of the Bretton Woods system. Despite these similarities in the objective nature of the problems they experienced, the neoliberal reorganization of the economy remained quite different in Britain and France. This article argues that the reason for this is that these nations came to understand and construct their crises in a different way and thus had different expectations from the neoliberal turn.

In Britain, neoliberalism emerged as a solution to the crisis of the Keynesian policies. The crisis of Keynesianism, as articulated by Thatcher, was not limited to the inefficiency of its key policy instruments such as aggregate demand management and incomes policy institutions in dealing with the objective problems and challenges, such as stagflation. It was defined largely as a 'state

Table 1 Cross-examination

	Britain	France
Similarities: • Level of development • Regional context • External events • Timing of the economic crisis	Both are developed Western European nations. Throughout the 1970s, both experienced the constraints and economic difficulties stemming from the demise of the Bretton Woods system and oil shocks.	
Differences: • Postwar economic paradigm	Keynesianism	*Dirigisme*
• The role of the welfare state in the postwar paradigmatic development	Central to the Keynesian paradigm	Marginal to *dirigisme*
• Objective economic problems	Stagflation and exchange rate volatilities	Slow growth, unemployment and exchange rate volatilities
• External anchor	IMF, Germany and the US	European Monetary System
• Interpretation of the Crisis	1970–6 Crisis is seen as originating in the changing world structure and temporary in nature. Keynesianism is intact. 1976–9 The crisis is narrowly defined in terms of the ineptitude of Keynesian instruments in dealing with objective problems particularly with high inflation. 1979–90 With the election of Thatcher, the problems were interpreted in a Hayekian and Friedmanite framework as stemming from a 'state crisis': Britain's problems were believed to be rooted in the diminished authority of the state toward certain groups, such as trade unions, and the role it had come to play as a kind of a 'nanny state,' extending extensive welfare to society.	1976–81 Under Raymond Barre's term as a Prime Minister, the crisis was interpreted as an outcome of the extensive role played by the state in the management of the economy. The policy of 'industrial redeployment' was developed as a counter strategy. Neither the public nor the French political system was ready for a paradigmatic shift, however, and the strategy of 'industrial redeployment' floundered. 1981–3 The Mitterrand government interpreted the crisis not as a problem of too much state intervention in the economy but rather too little of it. Moving the state to the center of the stage, it was believed, would solve the crisis. Post-1983 The crisis was accepted to be one of *dirigisme*. *Dirigisme* began to be seen as unsustainable because of its inflationary outcomes; and criticized for not granting France the competitiveness and rapid growth it deserves.
• Consequences for the welfare system	The welfare system was seen as one of the key problems of Keynesianism that needed to be dealt with, and came under attack.	The welfare system remained marginal to the discussion of the crisis of *dirigisme.* Rather, it was seen as useful in compensating the location that might arise from the dismantling of *dirigisme*.

crisis.' More precisely, Keynesianism was found guilty of diminishing the state's authority vis-à-vis certain groups, such as labor unions, and turning it into a welfare agency whose only effect was to create a dependency culture – *the subjective basis*.

In France, the crisis was one of *dirigisme*. The expansionary policies that had been exercised to enhance the industrial sector became unsustainable in an environment that was characterized by high inflation and budget deficits – *the objective basis*. Moreover, such policies did not seem to be able to make French industry competitive in the new world economy. In other words, the 'problem,' as the French saw it, was the declining competitiveness of French industry, which was caused by the inapplicability of *dirigiste* techniques in the new economic order – *the subjective basis*.

These differences between the two countries led to a different form of neoliberal reorganization in each. In Britain, neoliberalism emerged as a radical political movement that was determined to alter the character of the state's relationship to the economy and society as it had come to exist in the postwar era (Fourcade-Gourinchas and Babb, 2002). The main goal here was to limit state intervention in the economy so as to run the economy along market principles. Contrary to the mainstream view of the matter, neoliberalism in Britain was not a movement that rendered the British state weak. Quite the opposite, it aimed at restoring the authority of the state against unions and a certain segment of society – namely, the welfare clientele. As such, British neoliberalism led to a form of state that Peter Evans describes as 'lean and mean' (Evans, 1997). The neoliberal turn in France, on the other hand, was less radical and more limited in scope. It mostly aimed at restoring France's economic competitiveness by discarding the particular form of industrial policy that had developed under the auspices of *dirigisme.*

The differences between the French and British versions of neoliberalism are crucial to understanding their choices about the welfare state. In Britain, the development of the welfare state was tightly linked to the country's postwar Keynesian economic framework. When the Conservative government diagnosed Keynesianism as the source of the country's major economic and social problems, the welfare state came under the focus of the neoliberal reform. In France, the welfare state was not perceived as linked to the crisis of *dirigisme*. Instead, the postwar development of the welfare state in France had taken place independently of *dirigisme*. Thus, when *dirigisme* was rejected for reasons that were mostly related to France's decreasing industrial competitiveness, the welfare state did not become the focus of the neoliberal reorganization.

This article concludes that the mainstream understanding of the relationship between neoliberalism and the welfare state – that the rise of neoliberalism leads to welfare retrenchment – is indeed mistaken. As the British and French cases show, countries reorganized their economies along their identification of what constituted the crisis. Neoliberalism did not lead to the demise of the welfare state in France because it was not identified as a 'problem' that demanded a neoliberal 'solution.' It did lead to an attack on the welfare state in Britain, however, because there the welfare state was identified as one of the elements that had generated the crisis.

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NOTES

1 Hall's model of social learning builds on Thomas Kuhn's (1962) notion of paradigm shift, which Kuhn develops in his book *The Structure of Scientific Revolutions.*
2 Not all ideational changes constitute a paradigmatic shift. Hall's distinction among levels of policy change is important in terms of understanding the rise of neoliberal ideas in economic policy in different nations. Neoliberal ideas were not institutionalized as a paradigm in all nations. In some nations, as we will see in the French case, they rather served as 'programmatic ideas,' – that is, as policy prescriptions 'that facilitate action among elites by specifying how to solve particular policy problems' (Campbell, 1998: 385).
3 'Welfare State,' Microsoft® Encarta® Online Encyclopedia 2005, [http://au.encarta.msn.com].
4 'Decommodification,' in Esping-Andersen's words, is the degree to which individuals 'can uphold a socially acceptable standard of living independently of market participation' (1990: 37).
5 Excluding education.

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