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The economics of New Labour: policy and performance

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This paper reviews the foundations of New Labour's economic policies and the performance of the economy since 1997. It argues that New Labour's policies have evolved from Thatcherism and that it has largely embraced the tenets of neo-liberalism. New Labour has rejected most aspects of Keynesianism and its policies have eschewed the use of active demand management policies. But it has been the high levels of demand—in particular consumption expenditure—that have driven economic growth in the UK and which have ensured that (as yet) New Labour has not faced the problems of dealing with a major economic downturn.

Key words: New Labour, Economic policy
JEL classifications: B20, E60

1. Introduction

The election of the Labour Government on 1 May 1997 was heralded as a watershed in British politics. It was seen by many as a major shift from Conservative rule and the various hues of Thatcherism that had dominated economic and social policy since 1979. But it was also seen as a shift from traditional Labour policies—including the use of active economic and social policies and large-scale state intervention—hence the prefix 'New' as an ever-present reminder of the change in direction (New Labour has a taste for prefixes). In the early stages of the New Labour project, the term 'The Third Way' was frequently used to describe the blending of Thatcherite neo-liberalism with new forms of moderate government intervention to curb the impact of free market policies on the disadvantaged. One of the Third Way's main architects described it is as 'a political approach that sought to reconcile economic competitiveness with social protection and with an attack upon poverty' (Giddens, 2007). But the Third Way was a concept embraced mainly by Tony Blair, New Labour's leader (until June 2007), and those close to him. It was frequently dismissed as vapid and vacuous and the term soon disappeared from the policy discourse within the New Labour Government. Nevertheless, the spirit of the Third Way lived on in the economic policy agenda of Gordon Brown, Blair's main rival as the Chancellor of the Exchequer, and his heir as Prime Minister. Despite the frequent allusions to 'evidence-based policy' (or the frequent refrain amongst civil servants of the need for 'policy-based

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evidence'), the theoretical and empirical basis for New Labour's economics was, and remains, narrow and shallow. The economic policy agenda was set by Brown and his advisor Ed Balls; a combination that provided the Conservative opposition with material for cheap laughs.[1] Economic policy was thus Brownian rather than Blairite, and there is no evidence of the 'big tent' approach that was supposed to epitomise New Labour policy making at the end of 2007 when Brown had succeeded Blair.

The purpose of this introduction is to set the scene for the other papers in this special issue that consider specific aspects of the New Labour record in office. It is organised as follows: Section 2 discusses the New Labour economic framework and its rejection of Keynesianism; Section 3 evaluates the stabilisation policy of New Labour. Section 4 briefly considers the economic record; Section 5 considers some of the divisions that persist in the UK economy; Section 6 considers some of the factors other than policy that have been influencing the UK economy, such as increasing global economic integration; Section 7 concludes.

2. The economic framework

The rise and persistence of mass unemployment during the Great Depression in the interwar period led to a significant re-evaluation of economic policy and the role of the state. Keynes's General Theory (1936) showed the fallacy of the classical dichotomy that had underpinned the laissez faire approach to economic policy, which had done much to deepen and sustain the depression. The dichotomy was based on two distinct and separate concepts: Say's law, which stated that supply would create its own demand; and the quantity theory of money, which stated that increases in the money supply would simply increase prices. With Say's law ensuring that the economy would tend to full employment, unless impeded by market imperfections such as trade unions, additional money would be inflationary (although how money was transmitted into prices was something of a mystery). The implications for policy were that government should confine itself to controlling the growth in the money supply, and ensure that market forces and the price mechanism worked freely. Keynes showed the inadequacies of the classical dichotomy by demonstrating that the market could not be relied upon to ensure that all resources were employed because there could be insufficiency of aggregate demand. He also showed that the usual classical solution to unemployment, cutting wages, would be likely to fail, as a cut in money wages would not necessarily lead to a reduction in real wages. Moreover, if real wages were forced down the fall in consumption expenditure by workers would reduce aggregate demand and increase unemployment.

Keynesian economics largely replaced classical economics during the golden age of Capitalism—a period from the 1950s until the early 1970s characterised by rapid economic growth and full employment—although there is some debate as to the extent to which the acceptance of Keynesian economics led to the implementation of Keynesian policies (Kitson, 2004). Nevertheless, as discussed by Wilkinson, the crises of the 1970s—when both unemployment and inflation escalated—led to increasing criticisms of Keynesianism in both the academic and policy communities. The swing back to classical economics was completed with the election of the Thatcher regime in 1979. Thatcherism revived the classical dichotomy and its policy recommendations almost in their original

[1] Balls was credited for Brown's reference to 'post neoclassical endogenous growth theory', leading to Michael Heseltine's response that 'It's not Brown's. It's Balls.'

form: unemployment is largely the fault of trade unions or of lazy workers and inflation is the fault or irresponsible monetary authorities printing too much money. And New Labour has embraced this framework but with some nuances and shifts of emphasis.

2.1 The rejection of Keynesianism

Any vestiges of Keynesianism were discarded by the Thatcher regime as it lurched backwards to embrace classical economics and its belief in the absence of a long-run trade off between inflation and unemployment. This policy shift was emphatically outlined in 1984 by the then Chancellor, Nigel Lawson:

> The conventional post-War wisdom was that unemployment was a consequence of inadequate economic growth, and economic growth was to be secured by macro-economic policy—the fiscal stimulus of an enlarged Budget deficit, with monetary policy (to the extent that it could be said to exist at all) on the whole passively following fiscal policy. Inflation, by contrast, was increasingly seen as a matter to be dealt with by micro-economic policy—the panoply of controls and subsidies associated with the era of incomes policy. The conclusion on which the present Government's economic policy is based is that there is indeed a proper distinction between the objectives of macro-economic and micro-economic policy, and a need to be concerned with both of them. But the proper role of each is precisely the opposite of that assigned to it by the conventional post-War wisdom. It is the conquest of inflation, and not the pursuit of growth and employment, which is, or should be, the objective of macro-economic policy. And it is the creation of conditions conducive to growth and employment, and not the suppression of price rises, which is, or should be, the objective of micro-economic policy. (Lawson, 1984, p. 2)

This transformation of macroeconomics has been embraced by Gordon Brown, the controller of New Labour's economic policy, who accepted much of the Conservative economic thinking, including the belief in the neutrality of money:

> Because there is no long-term trade off between inflation and unemployment, demand management alone cannot deliver high and stable levels of employment ... A few decades ago many economists believed that tolerating higher inflation would allow higher long-term growth and employment ... Milton Friedman argued in his 1968 American Economic Association presidential lecture that the long-term effect of trying to buy less unemployment with more inflation is simply to ratchet up both ... Friedman was right in this part of his diagnosis: we have to reject short-termist dashes for growth. But the experience of these years also points to the solution ... Because there is no long-term trade off between inflation and unemployment, delivering full employment requires a focus on not just one but on all the levers of economic policy. (Brown, 2001, p. C32)

2.2 The new Say's law

In traditional monetarist models, the emphasis on the supply side focused on removing market imperfections, including state regulations that impeded the competitive process, especially in the labour market. In New Labour's post-monetarist approach the emphasis is on improving productivity through creating a 'knowledge based economy' (Department of Trade and Industry, 1998; HM Treasury, 2002, 2005) and 'employability' (HM Treasury 2003A). Thus we have seen New Labour evolving from Thatcherism with an added focus on education, innovation and the commercialisation of science. As Rutledge (2007) shows in his discussion of energy policy, New Labour has tended to adopt a fundamentalist view of the efficiency of competitive markets.

New Labour, and Gordon Brown in particular, have embraced neoclassical endogenous growth theory (Department of Trade and Industry, 1998; HM Treasury, 2000), which in many ways is a modern day version of Say's law (Kitson, 2005). There are many alternative forms of endogenous growth theory (see Temple, 1999) but in the early models the key idea was the rebuttal of the notion of diminishing returns to capital. More recent models have restored the notion of diminishing returns to factor inputs, but have stressed the importance of externalities or spill-overs, which generate growth and which are therefore *endogenous*. Endogenous growth models suggest that if you identify and target the key areas of an economy then long-term growth can be improved—and the key areas are usually linked to knowledge, including education, skills and research and development (R&D).

The limitations of endogenous growth models are both empirical and theoretical. As yet, they have little empirical support, although this may reflect the long lag before growth is increased. Theoretically, most endogenous growth models retain many of the restrictive assumptions associated with neoclassical economics:[1] the economy is assumed to be operating at full employment and thus there is no role for demand; capital and labour are considered to be substitutes; and there is no role for institutions, history or social and political systems. Also, such models ignore the inter-relatedness of many forms of investments—the case that it is not just about 'ideas' but having the physical and human capital and effective institutions to exploit and diffuse such ideas.

An alternative approach to endogenous growth, which incorporate the role of demand, are the cumulative causation models associated with Myrdal (1957), Kaldor (1972) and others. In such models, a high level of demand allows countries (or more specifically, the firms and industries within them) to rapidly adopt the latest technology and to exploit economies of scale and scope, improving competitiveness and trade performance. This in turn boosts demand, creating a virtuous growth cycle, which is strengthened as firms respond to rising demand by increasing investment in plant, products, processes and people. Conversely, low levels of demand limit the exploitation of economies of scale and scope, which lowers competitiveness leading to deteriorating trade performance and a further constraint on demand, thus creating a vicious cycle of decline.

2.3 The five drivers

Turning abstract theory into useful policy is always problematic. In terms of economic growth, New Labour has tried to resolve this problem by identifying skills, enterprise, innovation, competition and investment as 'drivers' of economic growth (Balls *et al.*, 2004; HM Treasury, 2000, 2001A, 2001B, 2003B, 2004, 2006). There are various limitations to the 'drivers' approach. First, although it is derived from a broadly neoclassical framework—no role is given for demand—it is unclear which neoclassical model is being deployed. It seems as if different models are being used for different drivers (Kitson *et al.*, 2004). Second, it is unclear what is driving the drivers—for instance, many economists would agree that a lack of investment can lower long-term growth but there would be much argument about what causes low investment. Third, some of the drivers are more an article of neo-liberal faith than the result of realistic theoretical and empirical consideration. For instance, we do not know what sort of education works best—improved primary education or more rocket scientists? As far as innovation is concerned, much policy uses a narrow notion that science and technology will generate increase economic growth. According to the Treasury (2000) innovation is principally as a result of R&D spending, which generates new ideas and adds to the overall stock of knowledge. This simplistic notion fails to capture

[1] Neoclassical economics embraces the classical dichotomy and the efficiency of markets. It is also based on assumptions of utility maximisation and rationality and is dependent on mathematical models to explain economic phenomena.

the complexities of innovation systems, especially how useful knowledge is generated, enriched and diffused. There is an excessive focus on high-technology industries—such as information technology, biotechnology and nanotechnology. These activities are currently a relatively small part of the national economy and tend to be concentrated in the south and east of England. Furthermore, the notion that such activities are independent development blocks that will generate economic growth ignores the important inter-sectoral linkages that feed the products of 'new' industries into 'old' industries, generating innovation there and generalising the benefits of knowledge advance. When analysing the surge in economic growth in the USA during the latter part of the 1990s, Solow identified wholesale trade, retail trade and financial services (the users rather than the generators of new technology) as the key sectors driving economic growth (Solow, 2001).

The driver that is most difficult to get a handle on is *entrepreneurship*. Apparently the UK is deficient in entrepreneurship (and its relation in big business—'intrapreneurship') in part reflecting a reluctance to take risks (unlike in the USA), which leads to a failure to innovate and promote economic growth. But there is no agreed definition of what entrepreneurship is and whether it is lacking in the UK. And the risk-taking American entrepreneur, who recognises failure as a 'learning experience' without stigma, and who presses on regardless, is easier to find in the minds and rhetoric of many commentators (including British politicians) than in reality. The Treasury's notion that 'fear of failure' is encumbering the entrepreneurship process is also far from clear. As Fawcett and Cameron (2005, p. 15) observe it could also be the case that the 'fear of failure would ensure that only high-return, high-productivity investments took place, eliminating the tail of under-performing investments without affecting profitable opportunities'.

The most extensive empirical study of entrepreneurship is the Global Entrepreneurship Monitor (GEM) (available at http://www.london.edu/gem.html), which defines enterprise as 'any attempt at new business or new venture creation, such as self employment, a new business organisation, or the expansion of an existing business by individuals, teams of individuals or existing businesses.' (Harding, 2003, p. 11). GEM also provides an indicator of intrapreneuship by measuring product, managerial and production changes in firms. Based on these definitions (and there are many alternatives), the UK comes out as a middle ranking economy. France and Netherlands, which have higher gross domestic product (GDP) than the UK, also have much lower levels of entrepreneurship and intrapreneurship, whereas the highly entrepreneurial countries include Chile and Venezuela. The data show that there is no correlation between high levels of economic growth and entrepreneurship (as measured by GEM data) and this may not be the only reason why the UK should not become more like Chile!

3. New Keynesian macroeconomics

New Labour's growth agenda has been complemented by the adoption of New Keynesian macroeconomics as the foundation of its short-term stabilisation policy. It should be emphasised that for many Keynesians, 'New Keynesian' is a misnomer as it is a framework that largely embraces the usual neoclassical assumptions, including an equilibrium rate of unemployment and rational expectations with its 'Keynesianism' being reduced to the presence of short-term stickiness of prices.

The 'non-accelerating inflation rate of unemployment' (NAIRU), the New Keynesian version of the equilibrium rate of unemployment, has been embedded in New Labour economic policy. In the monetarist natural rate model, embraced by the Thatcherites, unemployment is explained as being voluntary or due to 'labour market rigidities' such as trade unions. In the NAIRU model, unemployment is explained by a range of factors (depending on the specification of the specific model), and unemployment may be involuntary. This may explain some of the contrasts in labour market policies between New Labour and their predecessors. Whereas the latter were concerned with reducing the power of trade unions and treating many of the unemployed as lazy or feckless, New Labour at least recognised that many of the unemployed did not choose to be out of work. But, New Labour largely ignored other features of the NAIRU model—most importantly that the so-called equilibrium rate of unemployment follows the actual rate of unemployment. The notion of hysteresis suggests that shocks to an economy may have persistent effects through loss of capacity, loss of skills or changes in wage-bargaining behaviour. Such a notion suggests that money many not be neutral and changes in aggregated demand may have impacts on aggregate supply including employment. It is a fortunate feature of New Labour's term in office that the economy has not suffered a major adverse shock, which may have led it to reappraise its attachment to the classical dichotomy.

3.1 Monetary policy

With New Keynesian macroeconomics, the role of demand management is largely restricted to providing low and stable inflation. With New Labour's monetary framework, announced soon after it came to power, there is one target (inflation) and one instrument (the interest rate). Importantly, as the Bank of England is independent (of politicians) and its decisions are made by professional mainstream economists, it is credited with having 'credibility' with global capital markets. According to Gordon Brown, New Labour's economics is 'post-monetarist' (Brown, 2001) (it seems to be post everything). The current target for the bank of England (of 2%) is expressed in terms of an annual rate of inflation based on the consumer price index (CPI)—with a range of plus or minus 1 percentage point [from 1997 to December 2003 the target was 2.5% for RPIX (retail price index minus mortgage interest payments) inflation]. Angeriz and Arestis (2007) show that although the Bank of England has consistently achieved its inflation target since 1996 (only in March 2007 when CPI inflation was 3.1% was it out of the target range) it has tended to have a deflationary bias with actual inflation being systematically below the central target. Furthermore, as both Angeriz and Arestis (2007) and Wilkinson (2007) show, much of the success in achieving low and stable inflation can be explained by low import prices. Although an overvalued exchange rate has helped keep import prices low—at the same time as harming the competitiveness of exports—this has not been primarily due to monetary policy. The main driver has been increased globalisation and economic growth in South East Asia and Eastern Europe.

Two additional points concerning the new monetary framework should be stressed. First it is not that 'new'. As Angeriz and Arestis (2007) note, the policy of inflation targeting was adopted in October 1992 following the UK's forced withdrawal from the Exchange Rate Mechanism (ERM) and so, in effect, the changes in 1997 were a modification to an existing policy. In fact, plans for making the Bank of England independent were outlined by Nigel Lawson in 1988 (Lawson, 1992, Annex 3) although Thatcher was 'wholly unreceptive' to the idea (Lawson, 1992, p. 870). Second, as Angeriz and Arestis observe, price stability may not be enough, as history shows that there are repeated examples of periods of inflation stability that are followed by major economic and financial crises. This is particularly prescient, as the observation was made before the Northern Rock banking crisis which has severely undermined the credibility of the Bank of England.

3.2 Fiscal policy

Rules and prudence have been the foundations of New Labour's fiscal policy (Balls and O'Donnell, 2002). The 'golden rule' states that over the economic cycle, the government will borrow only to invest and not to fund current spending. The government's other fiscal rule is the sustainable investment rule, which requires it to keep debt at a 'prudent level' that is set at below 40% of GDP. Although New Labour's policies have largely been a continuation of Thatcherism, the golden rule, with its role for automatic stabilisers has a resonance of Keynesianism—but only just, as the rules-based approach limits the use of discretionary demand management.

As Sawyer (2007) observes there has been significant debate regarding the extent to which New Labour has stuck to its own rules. Much of the debate concerns the alleged sophistry involved in estimating the timing of the business cycle. According to the Institute for Fiscal Studies (IFS) 'without the extra two years that the Chancellor added to the beginning of the cycle in 2005, Treasury forecasts would now show him breaking the rule by £5½ billion' (IFS, 2007, p. 2). Labour's commitment to the previous Tory government's spending plans (limits that the Tories did not intend to keep) meant that fiscal policy was tight during the first few years of New Labour although it has been subsequently loosened. Whilst New Labour was tightening fiscal policy, the economy was being driven by a consumption-led boom combined with high investment spending and export demand. Consumer expenditure was being driven by house price inflation, easily available credit and a 'spend, spend, spend' mentality. This is a process that is no longer restrained by periodic balance of payments crises - now consumption is persistently exceeding production, generating structural balance of payments deficits. The fiscal surpluses generated in the late 1990s have done much to allow the golden rule to be achieved, or seem to be achieved. Another device used to meet the rule has been the Private Finance Initiative (PFI), which provides financial support for 'Public–Private Partnerships' (PPPs) between government and the private sector. As Sawyer (2007) observes, the impact of PFI is to increase public expenditure over the life of a project whilst also leading to an underestimation of public liabilities.

4. The economic record: how NICE?

As discussed by both Sawyer (2007) and Wilkinson (2007), under New Labour the UK economy has grown continually, inflation has been low and stable and unemployment has fallen. According to the Governor of the Bank of England, Mervyn King (2003) the economic record was such that the 1990s was a NICE decade (a period of 'non-inflationary continuous expansion'). There are, however, a number of important caveats to this rosy picture that need to be considered. First, the growth of the UK economy can be traced back to the early 1990s, starting under the previous Tory government following the expulsion from the ERM that enabled a loosening of monetary policy and a more competitive exchange rate. Second, the UK economy has been expanding during a period of rapid global economic growth, although there is some evidence that the UK has improved its relative performance compared to some of the other industrialised countries (Organisation for Economic Cooperation and Development, 2007). Third, economic growth has been sustained by high levels of consumption, which have been driven by easily available credit, which in turn has led to high levels of private debt and insolvency. At the macroeconomic level the growth of consumption has outstripped the growth of domestic production and has been sustained by import growth and persistent balance of payments deficits. Fourth, productivity in the UK still lags behind many of the other main industrialised countries. In policy circles in the UK there is an excessive focus on the productivity gap with the USA and the myopic view that US-type policies are the way to improve economic performance. Yet, based on output per hour worked, the UK has a bigger productivity gap with France than with the USA—but there is little call for francophile-type policies

5. A fractured economy?

Despite continued economic growth, both immediately before, and during New Labour's term of office, a numbers of fractures in the economy have persisted or deepened. These include continued structural change and the decline of manufacturing; a significant North–South divide; and the continuation of inequality and significant levels of poverty.

5.1 Decline of manufacturing and the growth of a service economy

As discussed by Coutts *et al.* (2007), deindustrialisation and the decline of manufacturing has been one of the main structural changes under New Labour. Manufacturing output only increased by 2.3% during the period from 1997 to 2006. With continued productivity growth this has resulted in a significant loss of jobs in this part of the economy. The process of deindustrialisation has been taking place in most of the advanced countries—reflecting economic maturity as there is a high income elasticity of demand for services, and increasing competition from low-cost suppliers of manufactured goods in South East Asia and Eastern Europe. The extent of deindustrialisation, however, has been greater in the UK compared to most advanced countries and, as Coutts *et al.* (2007) note, the pace of change has accelerated under New Labour. The deindustrialisation process has harmed the UK's trade performance and widened the regional prosperity divide.

5.2 The regional divide

The most pronounced impacts of the decline in manufacturing have been felt in the traditionally industrialised northern regions of the UK. As Coutts *et al.* (2007) observe, the deindustrialsation process and the growth of a service-based economy has exacerbated a long-run shortfall of jobs in the North and has contributed to a shift in population between the regions of the UK. They do note, however, that there has been some improvement in employment in the North since 2000. Such an improvement, however, masks different trends in individual regions within the north and should also be considered in the context of the wide regional disparities in employment that emerged in the early 1980s—disparities that widened for most of the subsequent two decades. Much of the regional jobs gap is masked by a statistical artifact as many of those without jobs are now not recorded as unemployed but as claiming incapacity benefits. As Fothergill and Wilson (2007) show, the incapacity claimant count in the North East, North West, Scotland and Wales is nearly double that in the South. Furthermore they show that the government's goal of reducing the number claiming incapacity benefit by one million within 10 years is likely to be unattainable. Theodore (2007) argues that despite the significant regional variations in joblessness, New Labour has remained wedded to supply side explanations and has ignored the role of the demand for labour. Whilst aggregate demand has sustained growth for the UK as a whole, it has been primarily service-sector driven with differential spatial impacts throughout the UK—with London and the South East overheating and with slow growth in the North. What is needed is a combination of initiatives that raise the demand for labour in distressed regions with labour market programmes that improve the supply of labour.

5.3 An unequal society

One of the major contrasts between New Labour and the Tory government it succeeded was the explicit commitment of the former to reduce poverty and social exclusion. The evidence indicates that there has been some moderate falls in child poverty and poverty amongst other selected groups but, as Angeriz and Chakravarty (2007) show, poverty reduction has been unevenly distributed between groups of households and amongst the poor. In many respects, where poverty has been reduced it reflects the underlying economic conditions, as the Joseph Rowntree Foundation (2005) observed:

> The improvements have taken place during steady economic growth. In some ways that makes it easier to achieve improvements, for instance in employment rates. But in others it makes it harder: reducing relative poverty while general living standards are rising fast is harder than doing so when they are stagnating, particularly if benefit levels remain price-linked.

Although poverty has been reduced for some groups, there has been no significant change in inequality (Hills and Stewart, 2005). But it should be stressed that reducing inequality was not, and is not, a New Labour goal. The incomes of top earners have accelerated rapidly and New Labour has no intention of stopping the rich getting richer; as Peter Mandelson said, New Labour are 'totally relaxed about people getting filthy rich'. At the other end of the income distribution, the incomes of the working poor have been cushioned by the national minimum wage and tax-benefit changes. When the minimum wage was proposed it was controversial, because orthodox economics suggested it would lead to either unemployment or inflation, or both. According to the latest analysis there is little evidence that the minimum wage 'had any significant negative impact on employment, profits or prices' (Low Pay Commission, 2007, p. xii). It should be added that the fact that the minimum wage is not *now* controversial may reflect the low level at which it is set. And, of course, policies aimed at helping the working poor do nothing for those without jobs. As Haugh and Kitson (2007) discuss, New Labour has encouraged the development of the social economy as a means of tackling social exclusion and poverty. However, as they argue, if this is to be effective the government must carry through its commitment to provide a constructive partnership with the social economy and resist the temptation to use it as a means of privatising the welfare state.

6. Explaining the economic performance

New Labour has been keen to attribute the growth and stability of the UK economy since 1997 to its management of the economy and its reform of the institutions of policy (Brown, 2001). But there are other factors—that are not simply policy-induced—that have had important impacts on the UK economy such as the growth of aggregate demand and the impact of globalisation and new technology.

6.1 The importance of demand

New Labour rejected Keynesian economics—but it is Keynesianism that can explain the growth in the UK economy since 1997. Growth has been driven by a high level of demand, which started in the early 1990s with the UK's withdrawal from the ERM. Since then, high levels of consumption—the largest component of aggregate demand—have driven economic growth. Historically, consumption-led growth has hit the buffers due to either the balance of payments constraint or the inflation constraint. But various aspects of globalisation have either relaxed such constraints or delayed the time when they will bite. And a high level of demand has beneficial impacts on many aspects of the economy. It has reduced unemployment and increased employment—and according to Brown *et al.* (2007) the quality of jobs has increased under New Labour not because of its supply-side labour market policies but because the demand for labour has increased. Similarly the slight revival in employment in some of the Northern regions has been due to the impact of aggregate demand slowly filtering from the overheating South East and has little to do with the success of supply-side policies.

6.2 Global and technical change

Globalisation has been frequently used to suggest that the power of the state has been reduced or that Keynesian economic policies are now redundant. Globalisation has been frequently mentioned—but it is often vaguely defined and conveniently used to justify laissez faire policies. But there are some aspects of globalisation and recent technological change that have had a major impact on economic performance. First, import prices have damped inflation. As Gordon Brown commented: 'globalisation is cutting the prices of basic goods from electronics to clothes, putting what were luxury goods into the hands of ordinary households' (Brown, 2006). Second, global capital markets are now willing to fund long-term and structural balance of payments deficits. In the 1950s, 1960s and 1970s, a small balance of payments deficit could cause economic and political crises. Now, with highly integrated global financial markets using a range of financial instruments, the UK (and the USA) can seemingly maintain a persistent long-term balance of payments deficit. The deficit can be financed through the selling of UK assets—including companies, properties and land—although it is uncertain how long such a deficit can be financed. Third, technical change, in particular the increased use of information and communication technology has raised potential economic growth. Although, as the evidence of the USA has shown, it is the use of technology and not its production that has the largest impact on economic growth.

7. Conclusions

New Labour's economics refined and developed the Thatcherism that preceded it. It embraced neo-liberal economics and accepted the notion that government demand management would not work. And it has washed its hands of rising inequality. The paradox is that while New Labour dismissed the role of demand, it was the expansion of demand that has led to increased economic growth, falling unemployment and raising job quality since 1997. But the expansion of demand was not largely due to the deliberate acts of government policy—although fiscal policy was relaxed after 2000. Demand has been driven by a consumption binge that has been NICE while it lasted—but the hangover may be worse.

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