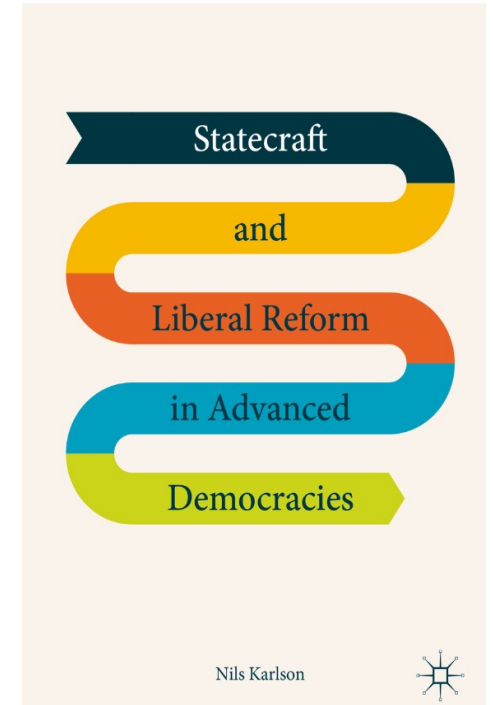


Statecraft and Classical Liberal Reforms



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The Puzzle ...

- Great need of liberalization (in the European sense) and welfare-enhancing reform in most countries
- Many “big bills left on the sidewalk” (Mancur Olson 1996)
- But **how** can reform be promoted?
- Is it possible to formulate a general theory of *Modern Statecraft*?

Statecraft

- *The art of governing an advanced democracy and welfare state well*
- *Implementation of welfare-enhancing institutional change = reforms*
- *Most often equivalent to liberal statecraft, i.e., policies that increase liberty and make society more free*

A very strong *status quo-bias*

1. Special interest and public-goods traps
2. Negativity biases and ideational traps
3. Public opinion and preference falsification

Especially difficult in advanced democracies and welfare states

Sweden in the 1970s and -80s

The Swedish Model



- Extensive transfer systems
- Large public sector and bureaucracy
- Public production of welfare services
- Labor market regulations
- Progressive income taxes, high capital taxes, and a very high tax burden

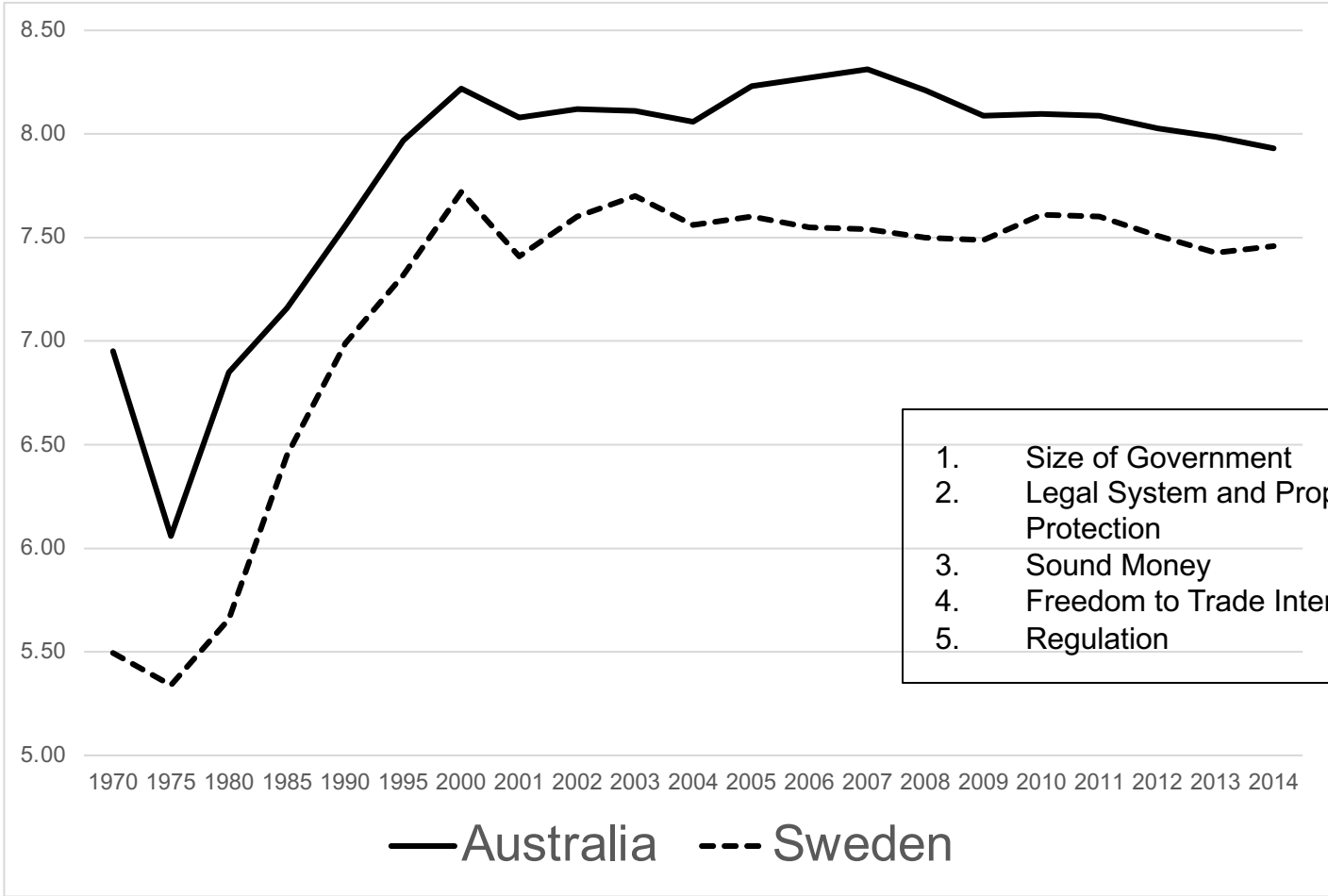
Australia in the 1970s and -80s

Australian settlement

1. White Australia
2. Industry protection
3. Wage arbitration
4. State paternalism
5. Imperial benevolence



Economic Freedom (Fraser index)



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The Australian economy

A wonder down under

Are Australia's economic batteries running low?

Mar 18th 2004 | SYDNEY

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FOR a dozen years Australia's economy has kept going like the Energizer bunny. It is now in its 13th year of expansion: in the past 12, GDP growth has averaged almost 4% a year. But could 13 prove to be an unlucky number?

Australia is basking in some of its best economic numbers for decades. The unemployment rate has fallen from almost 11% in 1992 to below 6% now. Inflation remains well behaved at 2.4%. The country's stunning performance has been due largely to prudent monetary and fiscal policies and to structural reforms. Lower trade barriers, more flexible labour practices and deregulated product markets have boosted productivity and made the economy better able to adjust to shocks. The rate of labour-productivity growth has risen from an annual average of 1.6% in the 1980s to 2.7% over the past ten years—even faster



The Nordic countries

The next supermodel

Politicians from both right and left could learn from the Nordic countries

Feb 2nd 2013 | From the print edition

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Swedish reforms 1985-2010

1985 Deregulation of credit market

1989 Deregulation of foreign exchange market

1990 Start of deregulation of energy, postal, telephone, railway, airline markets

1991 Agricultural reform

1991 Tax reform, lowering marginal income and capital gains tax rates.

1991 Start of sales of state-owned companies

1992 School voucher system, floating exchange rate

1994 Choice in child care, elderly care, etc

1995 New budgetary process, required surplus over cycle

1995 Less generous social insurance and welfare systems

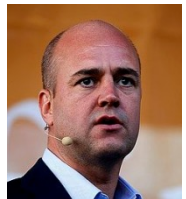
1995 EU membership

1997 Independent central bank and inflation targeting

1998 Pension reform, balanced

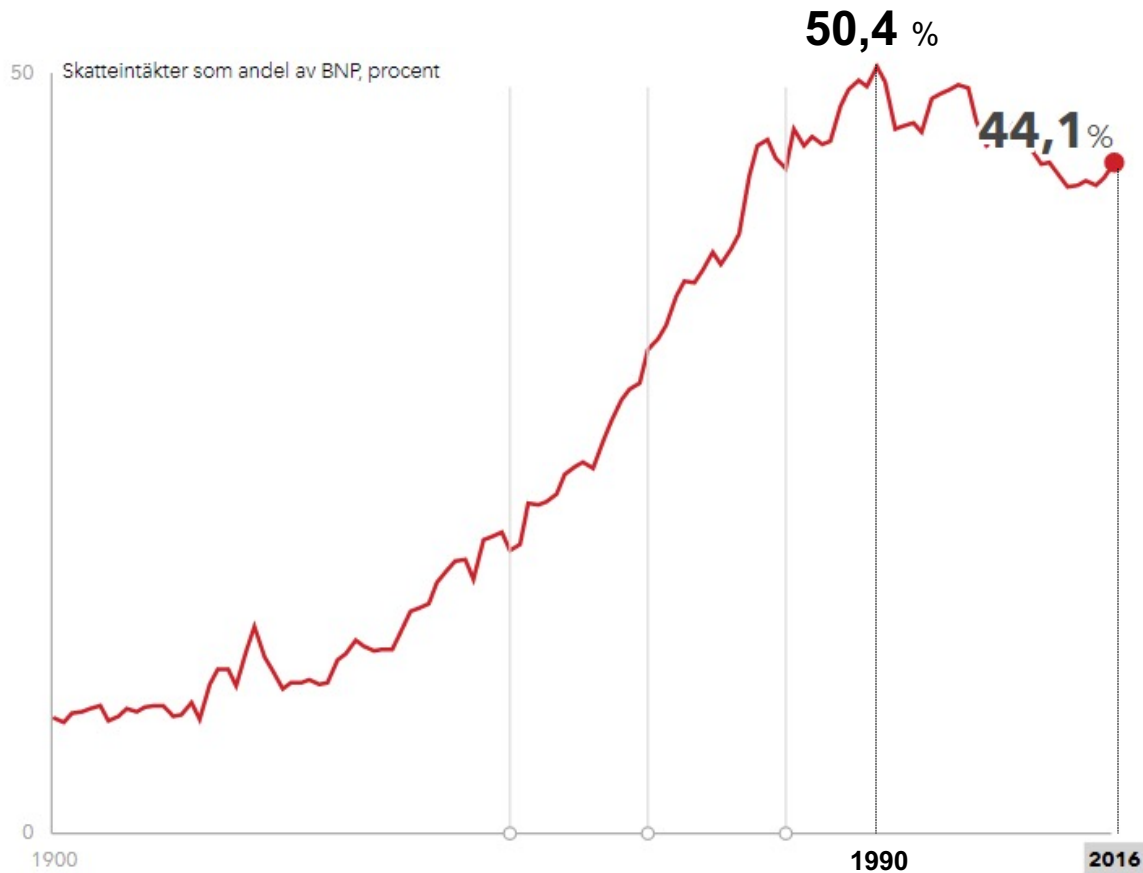
2000 Industrial relations reform
2004 Tax reform, inheritance and gift taxes abolished

2006-10 Wealth tax abolished, social insurance reforms, labour market reforms, earned income tax credits, tax deductions for household services etc.



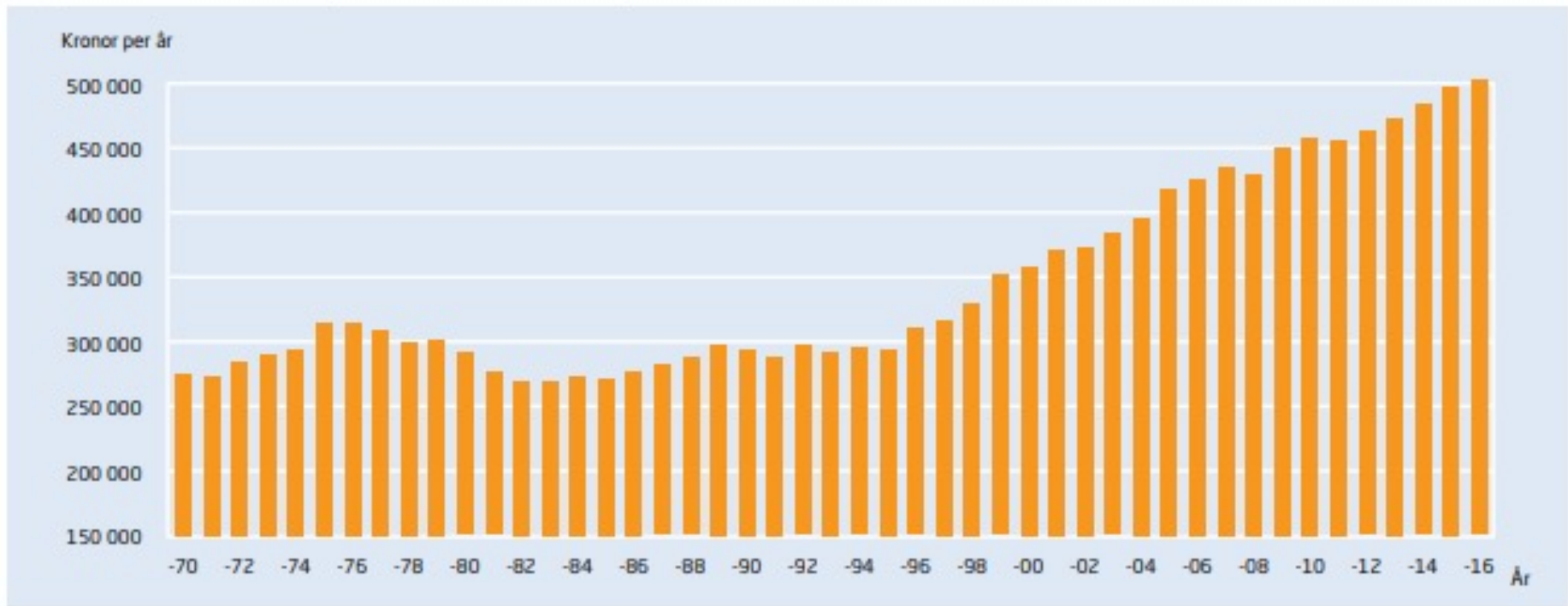
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Taxes as share of GDP in Sweden



Källa: 1900-1949: Rodriguez, E (1981); "Den svenska skattehistorien". 1950-1964: Data om skatteintäkter från Rodriguez (1981), data om BNP från SCB. 1965-1980: Data om skatteintäkter från OECD, data om BNP från SCB. 1980- : SCB.

Real wages, white collar (2016 prices)



Källa: Svenskt Näringsliv

Australian Reforms 1983-2007



1983 Floating of the Australian dollar, abolishing of capital controls

1985 Deregulation financial markets

1985 Tax reform, lowering marginal taxes, abolishing double taxation

1988 Tariff reform starts

1990 Competition, micro-economic reforms, privatizations, deregulation

1990 Firm-level bargaining

1990 Pension reform

1992 Liberalized foreign bank entry, foreign investments eased

1992 Pension reform, superannuation



1993 Industrial Relations Reform, enterprise bargaining

1996 Central bank independence and inflation targeting formalized

1996 Industrial relations reform, Workplace Relations Act

1996 Public sector reforms, competitive tendering, contracting out

1997 Welfare reform, work-for-the-dole scheme

1998 Privatization of employment service

1999 Tax reform, general sales tax

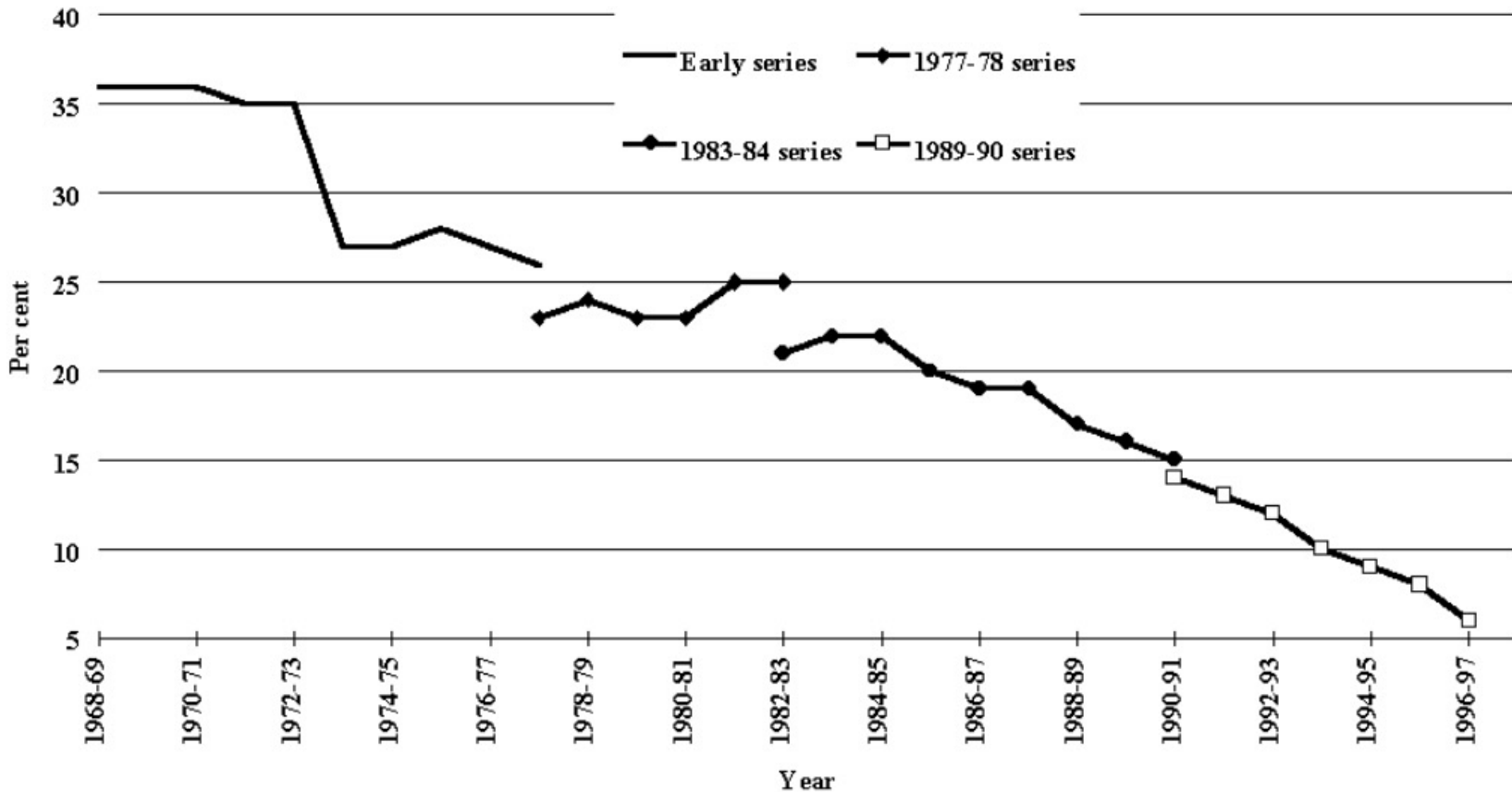
2002 Fiscal consolidation completed

2005-7 Industrial relations reform
WorkChoices



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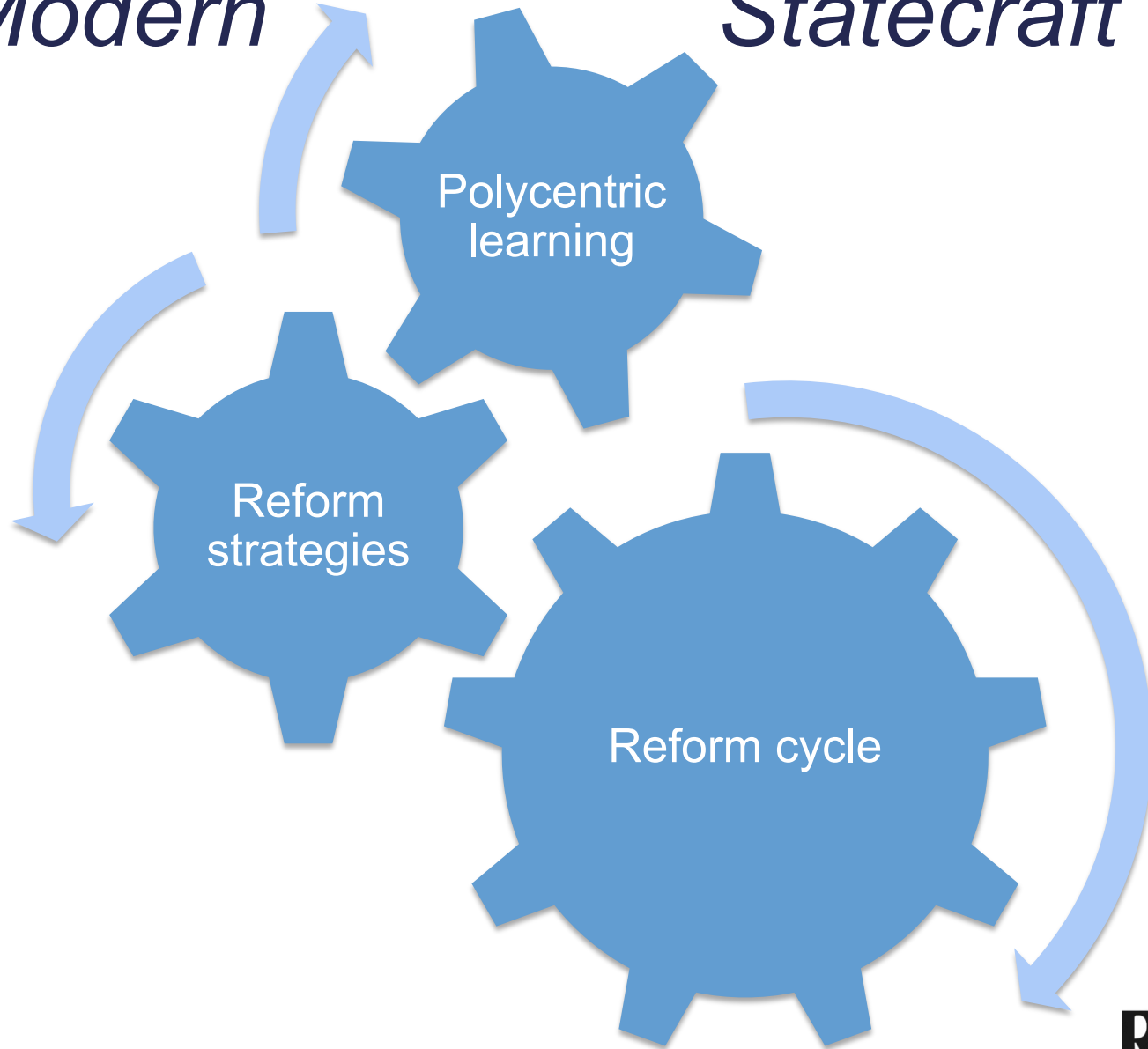
Effective rate of “assistance” to manufacturing in Australia



Source: Industry Commission, Assistance to agriculture and manufacturing industry, Information Paper, March 1995

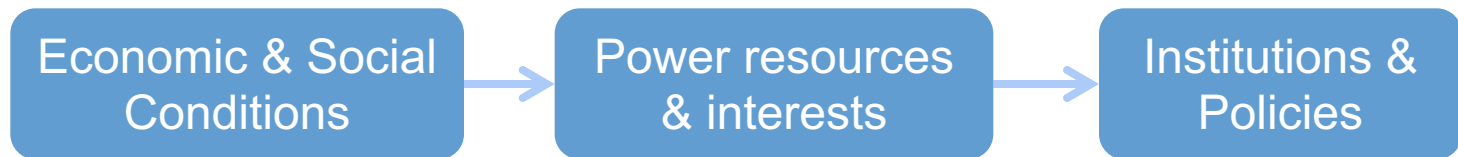
Modern

Statecraft

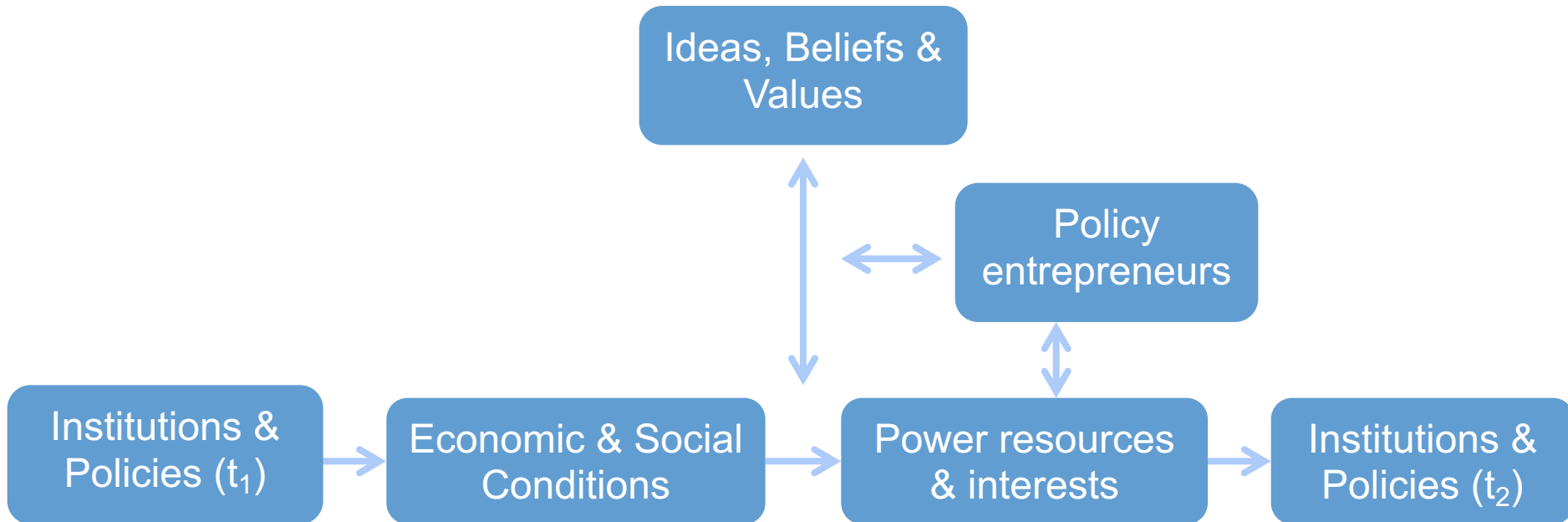


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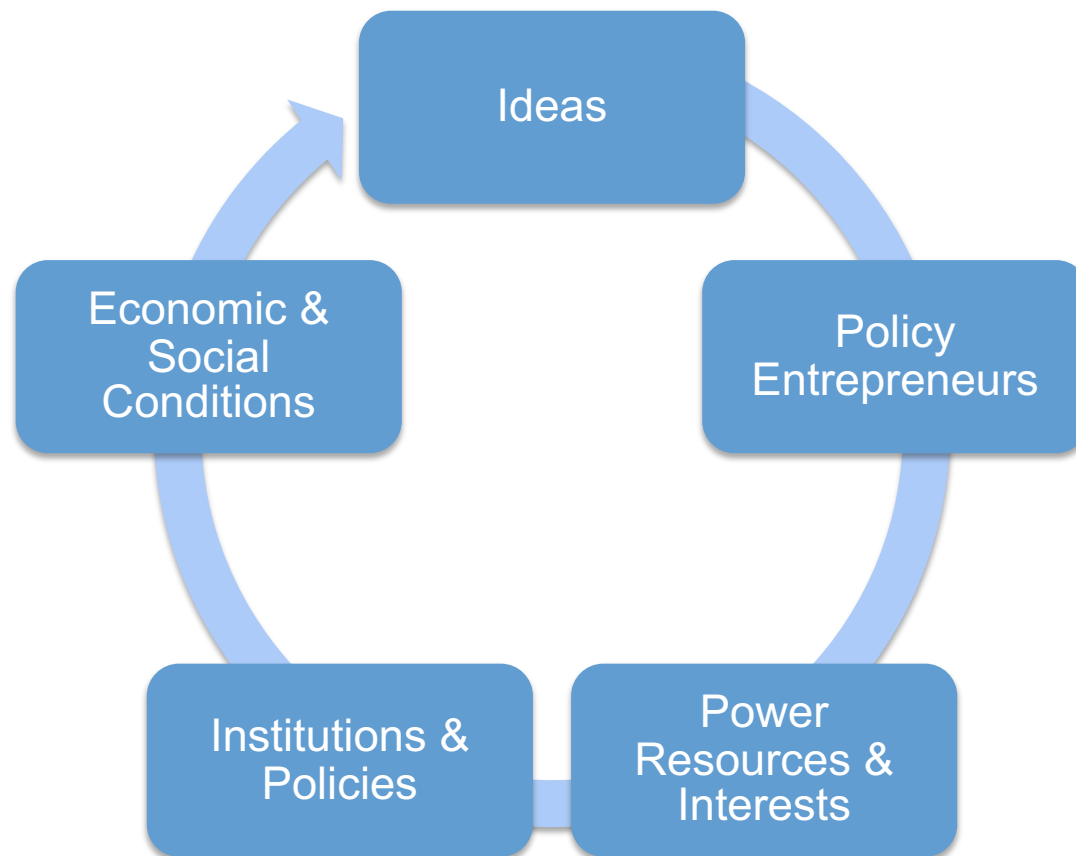
Explaining institutional change



Explaining institutional change



A Synthesis: *The Reform Cycle*



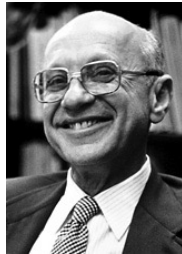
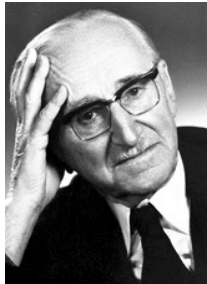
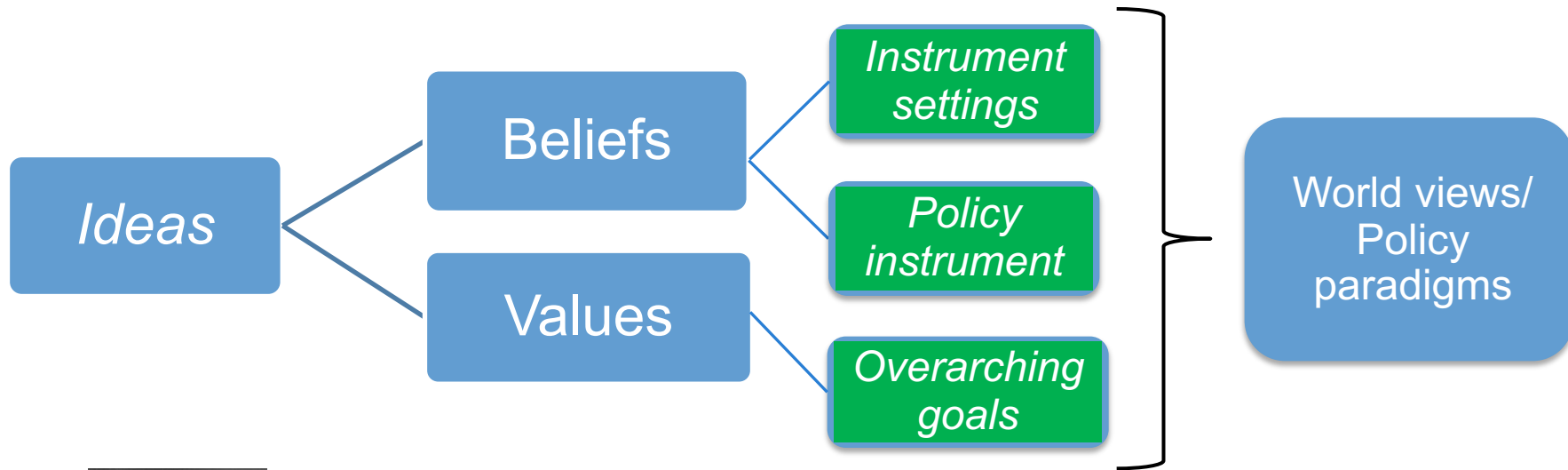
Policy entrepreneurs

- ***Develop and articulate ideas***, new facts, new perspectives, values, worldviews to analyze changing economic and social conditions
- Form ***advocacy policy coalitions***
- ***Activate power resources*** and interests
- Influence public opinion, decision makers, bureaucrats etc.
- Use different ***reform strategies***

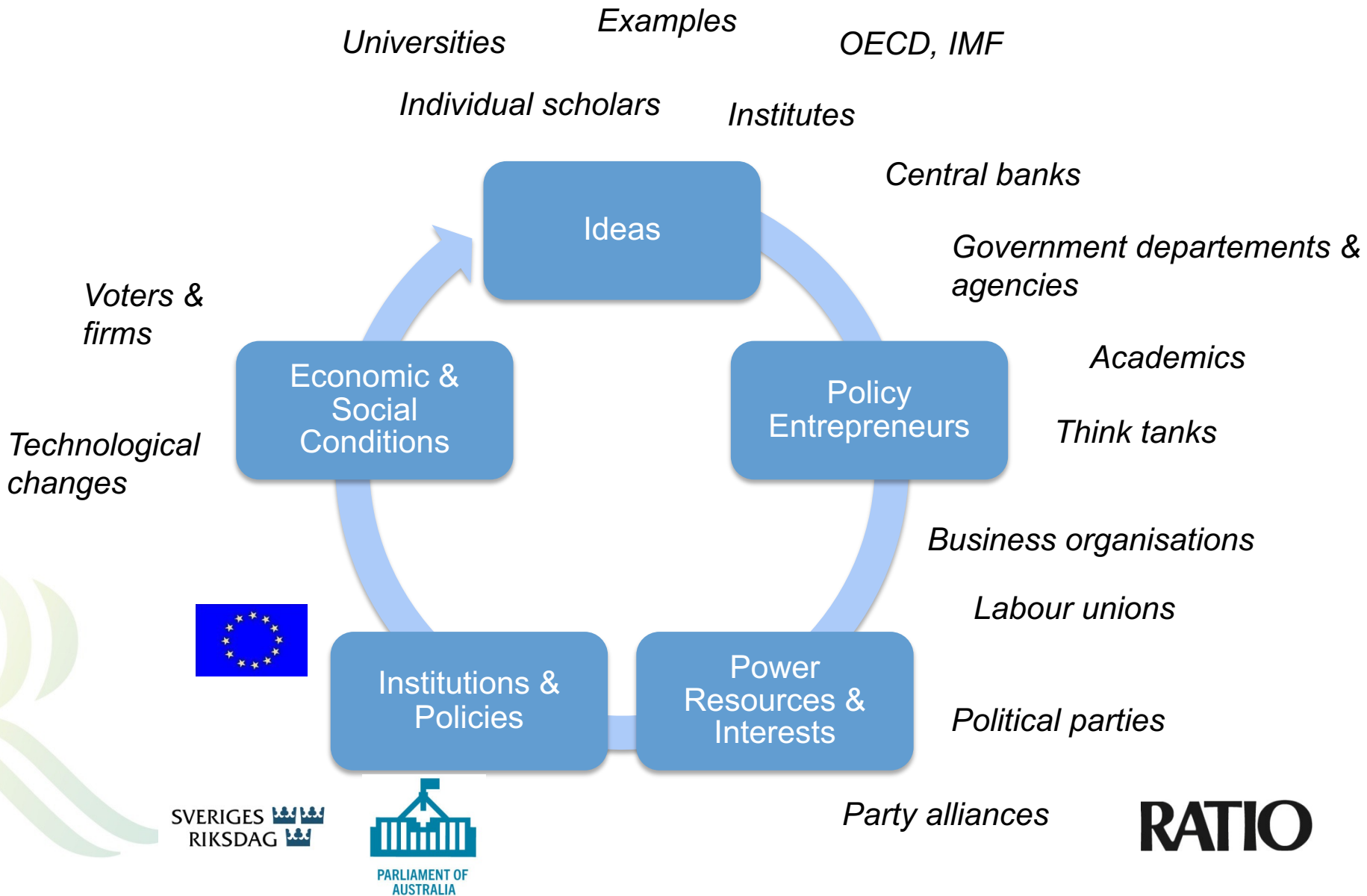


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Most important were *ideas*

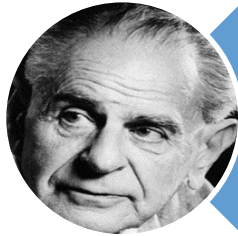


The Reform Cycle





Reform strategies



Popperian
strategies



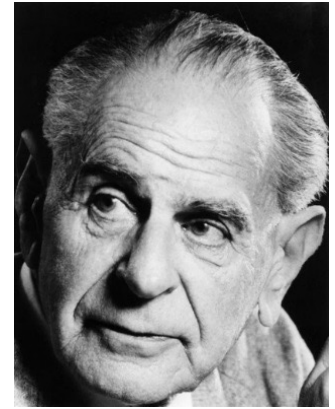
Kuhnian
strategies



Machiavellian
strategies



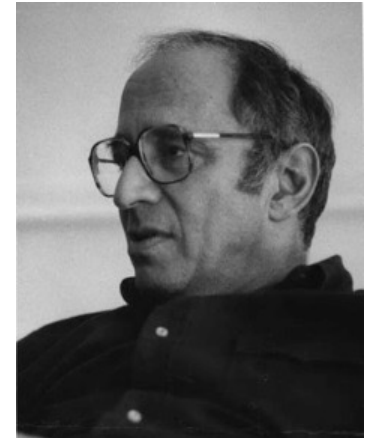
Popperian strategies



1. Use *scientific results*, empirical research and experiments!
2. *Rational argumentation* and open public discussions.
3. Incremental, rather than large-scale institutional changes
4. Do not rely on firm beliefs about how the world works or on strong normative ideals

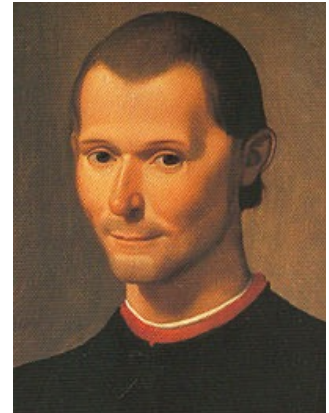
Kuhnian strategies

1. Use windows of opportunities, focusing events, crises or critical junctures!
2. Focus on policy failures, really striking facts and figures, and examples
3. Use *narratives* and rhetoric to *frame* and redefine discussions and agendas
4. *Paradigmatic shifts* are long-term projects – easier to change beliefs than values and preferences



Machiavellian strategies

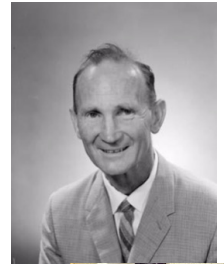
1. *Obfuscate* and lower the visibility through *masking*, indexing, delaying consequences etc!
2. *Split* the opposition and play off one group against another, compensate some and not others
3. Do not show your real intention, spread the blame for hardship on others
4. Beware that your competitors and partners use similar strategies



Example:

The Australian tariff cuts

- Alf Rattigan, long term chair of the *Tariff Board* became an anti-protectionism policy entrepreneur
- Supported by the *Crossroad group* and other academic policy entrepreneurs
- Implemented by the Labor government through successive corporatist *Accords* with ACTU, circumventing the cabinet and ministries
- Pro-consumer perspective, simultaneous changes in taxes, pensions etc.
- All reform strategies used



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Example

The Swedish tax reform 1991

- Initiated by the Liberal Party – and heavily criticized by the Social Democrats
- Later implemented by the same parties – everyone else opposed the reform
- Very ambitious – lowering marginal income and capital gains taxes, broadening the tax base etc.
- Economists at Ministry of Finance key policy entrepreneurs
- Many simultaneous changes made it hard determine winners and losers
- All reform strategies used, but *Machiavellian* dominated



Example

The Swedish wage-earners funds

- Attempt to massively socialize private industry by Social Democrats & LO 1975 -
- Leading CEO Curt Nicolin made chairman of *Confederation of Swedish Enterprise* 1976-1984 – *strong idea focus*
- Massive *pro-market* campaigns, cultivation of non-socialist parties and academics
- *New policy entrepreneurs*: think tanks and publishing houses, private radio station etc.
- *Mobilization* of members and large-scale demonstrations 1983
- Wage-earners funds finally abolished 1992
- Combined *Popperian* and *Kuhnian* strategies



Example

Australian attempts to shift the policy paradigm 1991-1993

- “Fightback” proposal by Liberal Party leader John Hewson, radical market-liberal reform agenda and the GTS
- Keating’s “New Australian Policy” with a new narrative, multiculturalism, pro-Asia, cutting ties with British Crown
- Both failed due to bad reform strategies
- Too radical for middle class voters



Results of the case studies

- The *reform cycle* fits the empirical evidence very well in both Sweden and Australia – ideas and policy entrepreneurs crucial
- All three *reform strategies* also important, not the least Machiavellian strategies. But idea-based Kuhnian strategies perhaps most important

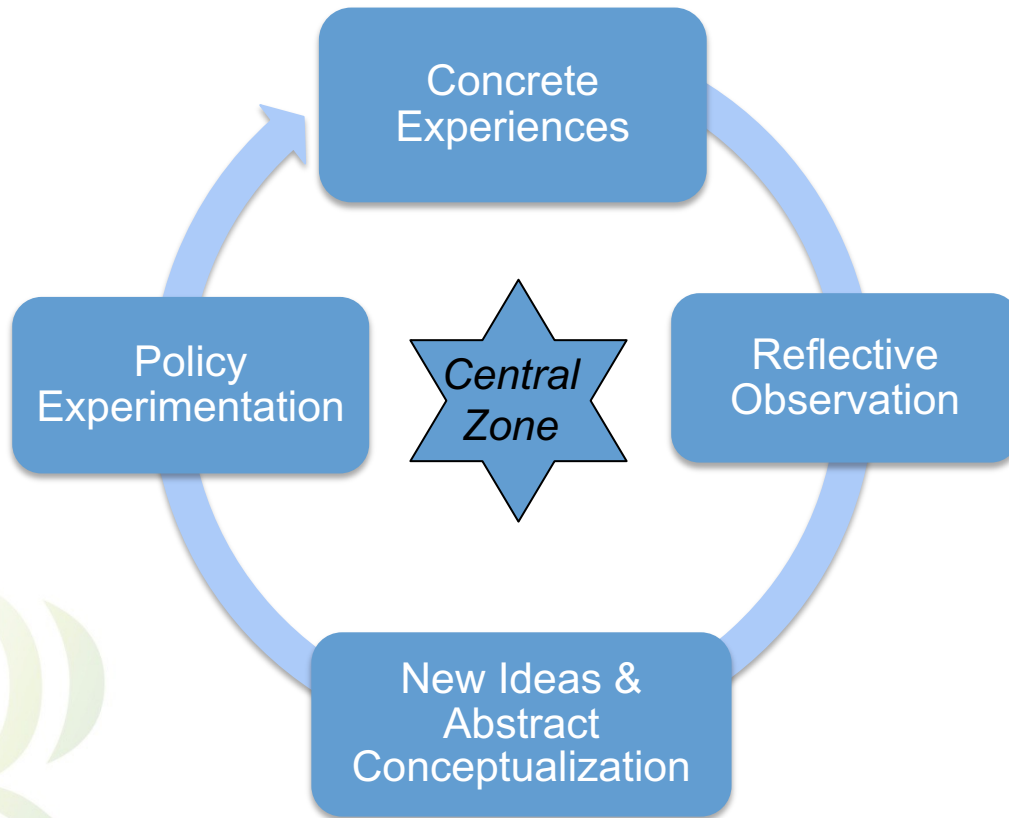
Modern statecraft requires a combination of knowing *what* and knowing *how*

Remaining puzzles

1. Why not welfare-decreasing, illiberal institutional changes instead?
2. How was the collective-action problem involved in liberal reforms solved?



Polycentric experiential learning important



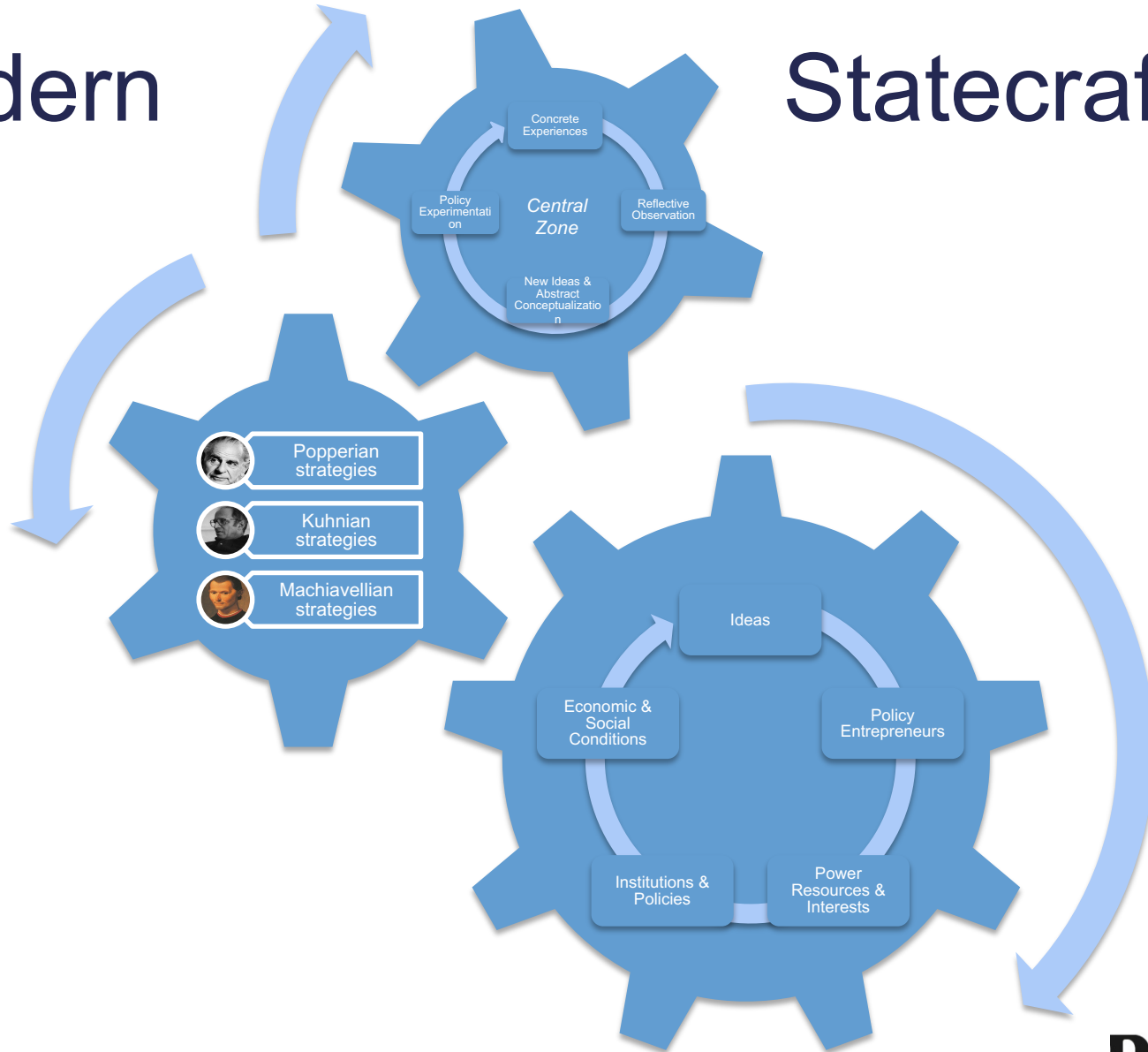
- *Many policy ideas were developed in the reform process itself*
- Took place in the *central zone* – many actors involved
- Largely top down
- Hard-won reforms were often kept by opponents
- Analytical skills where crucial in this

Modern statecraft

- The art of governing well by implementing welfare-enhancing, liberal reforms
- Requires both analytical and political skills
- Takes place within the reform cycle, where Popperian, Kuhnian, and Machiavellian reform strategies are used
- Requires a polycentric effort of experiential leaning, in the central zone of a country

Modern

Statecraft



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Summary

To promote classical liberal reforms

1. Analyse the *economic and social conditions*
2. Conquer the *idea arena*
3. Promote *policy entrepreneurs*
4. Form *advocacy coalitions*
5. Invest *power resources*
6. Use all *reform strategies*



It is a *long-run* project, but with great potential!