

# 1

## *The End and the New Beginning of History*

Everything has been globalized except our consent. . . . Democracy alone has been confined to the nation state. It stands at the national border, suitcase in hand, without a passport.

GEORGE MONTBIOT  
*The Age of Consent*, 2003

The great ideological struggle between the Soviet and Western models of society, which in essence constitutes the history of the 20th century, reached new levels of intensity only a generation ago, with fierce ideological debates raging on campuses and in election campaigns. In Vietnam and other parts of Asia, as well as in Latin America and Africa, the struggle took place on battlefields.

That “history” ended in the early 1990s, as announced ahead of time by Francis Fukuyama in his celebrated and prescient article published several months before the fall of the Berlin Wall.<sup>1</sup> Since then a new beginning of history has unfolded in the form of a wide-ranging and increasingly passionate debate about globalization.<sup>2</sup> This book is about the globalization debate. It is about the politics and the economics of globalization and the significance of democratic consent in the 21st century. The debate is ideological, in the classical 20th century sense, as illustrated by the arguments and passions unleashed by the war in Iraq or the meetings of the World Trade Organization (WTO). The “end of history” did take place in the early 1990s only to give place to a “new history.” Humanity has not exhausted the great ideological debates; they are only changing in nature. The beginning of the 21st century is being shaped by a great ideological debate about the nation-state and global governance, about the

1. Fukuyama’s article “The End of History” was first published in the summer 1989 issue of *The National Interest*. Fukuyama (1992) expands on the original article.

2. Ralf Dahrendorf, in his collected essays entitled *Der Wiederbeginn der Geschichte*, uses the same metaphor about a new beginning of history (Dahrendorf 2004).

legitimacy of the use of power, and about public policy at the local, regional, national, and supranational levels, all against a backdrop of huge inequalities in wealth, income, and power that divide the world.

This global debate has two broad dimensions related to economics and security. The economic discussions focus on financial volatility, world trade, the pace and quality of global growth, the distribution of income, the need to fight global poverty, and related health and environmental issues.<sup>3</sup> These discussions draw on economic theory and the analysis of economic institutions. Mainstream economists often use the concept of public goods at the global level to analyze the challenges facing public policy.<sup>4</sup> More generally, many of the books and articles dealing with the economic aspects of globalization focus on capital markets or trade and on the role of the International Monetary Fund (IMF), World Bank, and WTO.

The other major dimension of the global debate is conducted in essentially political terms, focusing on security, the fight against terrorism, the projection of US power worldwide, the role of the United Nations, and new versions of global balance-of-power analysis. Here, authors draw on political theory and history as well as international relations theory.<sup>5</sup> The “modern” political debate on international relations and global governance goes back to ancient Greece and Rome, with classical roots in the works of philosophers such as Thucydides (*History of the Peloponnesian War*) and Marcus Aurelius (*Meditations*), and that of great philosophers such as Dante, Hobbes, Grotius, Rousseau, Montesquieu, Kant, and Hegel, to name some of those who have been influential beyond their times. Karl Marx and Marxist theories of imperialism remain influential among writers such as Eric Hobsbawm, David Harvey, and Samir

3. See, for example, Eatwell and Taylor (2000); Rodrik (1997); Stiglitz (2001, 2003); Kenen (1994, 2001); Kuczynski and Williamson (2003); Fischer (1998, 2001, 2002, 2003); Bhagwati (2004); Wolf (2004); Stern (2002); Woods (2000, 2001); Ocampo (2000); and the Global Economic Prospects Series published by the World Bank, which contains quantitative analysis of economic globalization. For a thorough introduction to the globalization debate, see Held and McGrew (2002a, 2002b, 2003).

4. A very useful collection of essays looking at the challenge in terms of global public goods can be found in Kaul, Grunberg, and Stern (1999). See also the more recent UNDP volume entitled *Providing Global Public Goods*, edited by Inge Kaul et al. (2003).

5. A few examples are Gilpin (2001); Russett (1997); Rosenau (1992); Alger (1998); Childers (1997); Childers and Urquhart (1994); and Keohane (2002). Brzezinski (2004) focuses on the fundamental “choice” the United States faces in its foreign and security policy, but in the process offers an overall political analysis of globalization.

Amin.<sup>6</sup> The political part of the globalization debate thus has roots in human thought that are much more ancient than the modern economics of global public goods or international capital markets.

Anthony Giddens (1998) was quite correct when he wrote in his influential book *The Third Way: The Renewal of Social Democracy*: “The term globalization has come from nowhere to be everywhere in a period of just a decade. . . .” Indeed, it is not possible to look at the politics or the economics of the emerging world of the 21st century without making globalization a central feature of the analysis. The debate about the nature of globalization, its direction, whom it benefits, the survival of the nation-state, the “right” to intervene across borders, and other related matters has replaced the old “capitalism versus socialism” debate. The intensity of the debate and the passions around it will increase with every subsequent event that challenges us to find solutions appropriate to the realities of the 21st century, whether it is another financial crisis, an epidemic, or further acts of terror.

A point of departure for what is to follow is that it is useful to look at the economics and the politics of globalization together, as part of the overall discussion of the international system.<sup>7</sup> Too often, economic problems and proposed solutions are discussed without a real political context. Making progress on the globalization debate with viable proposals for change can benefit from an analysis linking the economic and political dimensions and focusing on the legitimacy of political and institutional power. This linkage is essential because without greater legitimacy at the supranational level, progress in solving global problems will be very difficult. Ideas for reform emerging from the economic debate face obstacles of an intrinsically political nature. Proposals for change in the

6. Hobsbawm (2000); Harvey (2003); and Amin (1996, 2004). In their much-publicized book *Empire* (2001), Michael Hardt and Antonio Negri use Marxist analysis and argue that as the sovereignty of nation-states erodes, a new global sovereignty, “Empire,” emerges from the coalescence of “a series of national and supranational organisms united under a single logic of rule” with no clear international hierarchy.

7. Authors who linked political and economic aspects and tried to give an integrated overview include, for example, Kennedy (1993); Woods (2001); Rischard (2002); Held and Koenig-Archibugi (2003); Strauss-Kahn (2000); Cohen (2003); and Rasmussen (2003). Bhagwati (2004) and Wolf (2004) also include political aspects in their recent spiritedly argued defenses of globalization, although they remain books focused on the economics of globalization. Singer (2004) discusses globalization as a philosopher from the point of view of ethics, linking political and economic aspects. Kozlu (1999) and Ulagay (2001) provide Turkish perspectives on globalization.

economic domain cannot succeed unless they include political willingness to take steps toward greater legitimacy in the exercise of power. Concern for economic efficiency and practicality must be part of the analysis and certainly must shape the proposals for change, but the globalization debate is really about fundamental worldviews, about ideology. Conversely, the debate about security issues should take into account the economic and financial implications of the options discussed. Some of the excessive emphasis on the purely military aspects of power that prevails in some of the neoconservative thinking in the United States neglects the economic implications of the proposed security policies.

The fall of the Iron Curtain has indeed marked an important turning point and has “ended” a certain period of history, a period that has shaped the lives of all of us who experienced the 20th century. In that sense, Fukuyama’s message was powerful, correct, and prescient, since his original article appeared before the fall of the Berlin Wall. The 15 years that followed that momentous event have not led us, however, to reach a relatively safe haven. After a dramatic turn, history continues to take us into uncharted waters with tremendous dangers and promises.

## **A Brief History of Legitimacy**

### *From Divine Right to the Common Will*

More than ever, the exercise of power requires legitimacy. The ideological triumph of liberal democracy as the model of human political organization means that everywhere the exercise of power requires the consent of those that are governed. This need for legitimacy based on consent is widely acknowledged with regard to power exercised within national borders, but the same need has emerged in international affairs. The worldwide debate over American policies and actions in Iraq has been largely concerned with their legitimacy. Among those opposing the war, practically nobody had any sympathy for Saddam Hussein. During the Vietnam War, leftists in the streets of Europe and America had carried portraits of Ho Chi Minh; there were no portraits of Saddam in the massive antiwar protests ranging from London to Rome in 2003. Most protesters would not have hesitated one second if they had been given the choice between American democracy and Middle Eastern dictatorship. The protests were not directed at the American socioeconomic model, as they had been in the 1960s, but rather at what was perceived as the illegitimate use of power projected beyond borders without some form of

international sanction. In a very different context, protests against the IMF in the streets of Buenos Aires, São Paulo, Prague, and Washington have also been directed fundamentally at what people perceive, rightly or wrongly, as an illegitimate use of power; in this case financial power.

Looking at history, even the most repressive political regimes have needed some degree of legitimacy. Viotti and Kauppi (1999) define legitimacy as the implication of the existence of right: that is when a government is said to have, or to have been granted, a right to govern based on such criteria as its popular acceptance, the legal or constitutional processes that brought it to or maintain it in a position of authority, the divine right of kings, or charismatic leadership that commands a following and thus contributes to the government's popular acceptance. Plainly, legitimacy is an accepted entitlement or sanction to rule. All governments depend on some combination of coercion and consent. Without consent, it is very difficult to exercise power; as Jean-Jacques Rousseau put it in *The Social Contract*: "The strongest is never strong enough to be always the master unless he turns might into right and obedience into duty."

Throughout post-Roman history, political legitimacy was linked to and derived from the religious realm.<sup>8</sup> Medieval kings in Europe were religious leaders or claimed to rule in the name of the divine. Unity of the church was one of the main pillars of Charlemagne's power. The Russian tsars assumed the role of supreme heads of Orthodox Christianity, claiming the status of protector of Orthodox Christians everywhere. The blueprint for Thai state-builders was Angkor, the great Cambodian kingdom that had been at its height from the 11th to the 13th centuries. From Angkor came ideas adapted originally from Indian Brahmanical thought, particularly such concepts of society as a divinely ordained hierarchy and of *devaraj*—the ruler as an immensely potent incarnation of a Hindu deity. In the Islamic world, the *Khalif* was both supreme religious leader and head of state. He did not have a divine character, but his exercise of power derived its legitimacy from his claim to enforce divine law.

8. In ancient Greece and Rome, the "link to God" was more tenuous. In Greece, the ruling aristocracy derived its legitimacy from lineages, tribes, and kinship vaguely related to Greek gods. The Roman Republic was essentially a secular state. It had no constitution but functioned as a system of agreed-upon procedures developed by tradition and administered by annually elected officials answerable to the Senate. The system deteriorated by the 2nd century and Augustus transformed it into a *principate* in which legitimacy was essentially derived from the emperor's leadership and military might. It is well known, of course, that in many ways the "classical age" was a precursor of modern times.

This “link to God” was the accepted foundation of legitimacy in most parts of the world up to the French and American Revolutions. There was, of course, debate as to how this mandate should function in practice. As early as in the first half of the 14th century, Dante Alighieri argued for a kind of “secularism” in proposing a world empire where the “authority of the Empire by no means depends on the church.” The church and the universal empire were to be coordinate powers, each autonomous and supreme in its respective realms. The empire was to be guided by reason and philosophy, the church by faith and theology.<sup>9</sup> But Dante’s emperor still was to derive his legitimacy from God—what Dante emphasized was that this link should be direct and not intermediated by the church or the Pope. It was only much later in the 18th century that the thinkers of the Enlightenment such as Montesquieu and Rousseau started to delink legitimacy from the religious realm and propose that the “common will of men” exercising human reason become the source of legitimacy.<sup>10</sup> The radical break with the past was symbolized in its most extreme form during the French Revolution by the cult of “Goddess Reason” (*Déesse Raison*), which was not an attempt to suppress all religion, but an early effort to establish the purely secular nature of the state. In most other countries the break with the past and with the religious basis of sovereignty was not as radical as what happened in France during the revolution. Nonetheless, the French Revolution was a watershed that deeply influenced developments in the 19th and 20th centuries in Europe and throughout the world.

It is important in this context to stress that the development of “secular and democratic legitimacy” was made possible by the emergence in Europe during the 17th century of the clearly territorially defined Westphalian nation-state. During the Middle Ages, the realms of power of the Pope, the Holy Roman Emperor, feudal lords, free cities, etc. overlapped a great deal. With the end of the Thirty Years’ War and the peace agreement at Westphalia in 1648, Europe entered the age of the territorially based, sovereign nation-states. The protestant reformation had a lot to do with this since it made “Christian Unity” impossible and irreversibly

9. Dante’s *De Monarchia* was placed on the church’s list of banned books and not removed from it until the 20th century.

10. “Law in general is human reason, inasmuch as it governs all the inhabitants of the earth; the political and civil laws of each nation ought to be only the particular cases in which human reason is applied” (Montesquieu in *The Spirit of Laws*). “Only the general will can direct the forces of the state according to the purpose for which it was instituted, which is the common good” (Rousseau in *The Social Contract*).

undermined any hope for supranational universal authority exercised by the church. Economic forces such as the development of industry and other economic activities not associated with land ownership also contributed to undermining feudalism and allowing the establishment of centralized state power, as emphasized by Marx. Once the nation-state was established, the foundation was also laid for modern democratic legitimacy based on the “will of the people” living in that nation-state, although one and a half centuries separate the Peace of Westphalia from the French and American Revolutions.

One has to be careful not to generalize too quickly from European experience and history to the entire world. Nonetheless, the ideas of the European Enlightenment enabled both the French and the American Revolutions. European ideas spread throughout the world, with colonization and postcolonial emulation of the European nation-state. Most of the new countries that emerged from decolonization tried to establish themselves “as if” they were European nation-states, admittedly with very mixed success. The idea that legitimate power had to be based on the explicit consent of citizens in a territorially defined nation-state made steady progress throughout the 19th and 20th centuries.

It is telling that in the 20th century, most repressive regimes had to keep up the pretense of elections in order to proclaim some form of legitimacy. Even in kingdoms where the sovereign’s authority still derived from the religious realm, the right to exercise power had to be linked to some form of parliamentary elections to reinforce the legitimacy of these regimes. In many countries, constitutional monarchy replaced absolute monarchy and even the most totalitarian dictatorship kept the appearance of a constitution endorsed by an election. In authoritarian secular regimes or in kingdoms, some of these elections were “won” by 99 percent of the vote and nobody was really fooled; but such was the need for at least a pretense of legitimacy that even the worst tyrants could not give up an attempt to legitimize themselves through elections! It is interesting to note in this context that authoritarian regimes deriving at least part of their legitimacy from the spiritual realm have often found it easier to allow some parliamentary opposition, whereas authoritarian regimes that could not claim any religion-linked legitimacy have tended to engineer completely overwhelming electoral majorities.<sup>11</sup>

11. In the Soviet Union up until 1987, elections usually were held with unopposed candidates, selected by the local office of the Communist Party, receiving 99 percent of the votes. Although engineered for complete victory, elections sometimes helped citizens to

With the fall of the Berlin Wall and the collapse of communist ideology as a serious contender in the clash of ideas, the liberal democratic view of legitimacy based on free and competitive elections in the context of a nation-state has become almost universally accepted, although still not always practiced. At the core of liberal democracy is universal suffrage, which is a necessary condition for legitimacy. There are other necessary conditions, however. Legitimacy also requires a competitive political context within which the right to vote is exercised. In the Soviet and fascist systems, elections had also been held, but these elections did not take place in a free “public space” of debate. They did not involve political parties competing against each other. Legitimacy, as understood in the liberal democracies, requires not only citizens who vote, but also a process of political competition and free debate, with elections taking place in that context. This process can vary according to different constitutions and national circumstances. In democracies, the “one citizen, one vote” principle does not translate into a “the majority can do whatever it wants” situation; it is qualified and augmented by fundamental rights of the individual and of minorities, as well as by requirements for supermajorities and/or “federalist” rules often giving subnational entities special weight in the way votes translate into majorities. Despite all these qualifications, the one citizen, one vote principle is nonetheless at the core of democratic legitimacy, reflecting the essential belief that legitimacy is conferred on governments and political decisions by the sum of individual citizens exercising their right to vote. We would not call a country a democracy today if a one person, one vote electoral process were not central to its political constitution, although this basic principle can be qualified, weakened, and augmented according to various complementary rules. It took humanity roughly two centuries to reach consensus on what is an acceptable process giving rise to legitimacy of governance in a nation-state. European countries have gone furthest in codifying this

---

make their concerns public: They used furnished paper ballots to write their requests for public services! Both Mussolini and Hitler secured absolute control by intimidation and violence, yet still held elections. Mussolini abolished universal suffrage in 1928 and restricted parliamentary elections to official candidates of the fascist Grand Council. After the 1933 elections, Hitler arrested or excluded 81 communist deputies and bribed the nationalist and the center party to get the enabling bill passed that gave him unlimited power. A month later all political parties were declared illegal. In North Korea, the constitution provides for the Supreme People’s Assembly, the highest organ of state power, to be elected every five years by universal suffrage. The Communist Party fields a single list of candidates who run without opposition.



consensus within the framework of the Organization for Security and Cooperation in Europe (OSCE)<sup>12</sup> and the Copenhagen Criteria,<sup>13</sup> but there is worldwide agreement on the basic concept, and even in Africa, Asia, and the Middle East, some form of democracy is increasingly becoming the only “legitimate” political model, which means that sooner rather than later the remaining authoritarian regimes will democratize or collapse. In that sense, the history of the 19th and 20th centuries has ended.

*The Social-Liberal Synthesis:  
Ideological Foundations of Legitimacy*

Before going further, I would like to argue that the success of the liberal democratic model of national governance is not just the victory of a particular model of political governance, but also reflects a much deeper ideological convergence on economic and social affairs. The history of political legitimacy is not just the history of the evolution of political constitutions and of laws regulating electoral processes. While due competitive political processes and appropriate legal arrangements, together, are necessary conditions for the sense of legitimacy that exists in well functioning democracies, there is more to legitimacy than process. If there exist, within a given society, fundamentally irreconcilable views, let us call them ideologies, on what good “outcomes” are, due democratic process is unlikely to be able to confer a widely perceived legitimacy. For Fukuyama’s “end of history” to take place, the world needed an end to fundamental ideological combat.

In the Western Europe of the first half of the 20th century, for example, the gap between the ideologies of the Left and Right was so large that democratic elections failed to provide the elected majorities with a legitimacy respected by all. When there is insufficient common ideological ground regarding economic and social matters, the votes of the “others”

12. The OSCE is the largest regional security organization in the world with 55 participating states from Europe, Central Asia, and North America. It is active in early warning, conflict prevention, crisis management, and postconflict rehabilitation. The OSCE deals with a wide range of security-related issues including arms control, preventive diplomacy, confidence and security building measures, human rights, democratization, election monitoring, and economic and environmental security. All OSCE participating states have equal status, and decisions are based on consensus.

13. The Copenhagen Criteria, accepted by the European Union in a summit meeting on the process of enlargement, require that a candidate country must have achieved “stability of institutions guaranteeing democracy, the rule of law, human rights and respect for and protection of minorities” before negotiations toward full EU membership can begin. See <http://europa.eu.int/comm/enlargement/intro/criteria.htm>.

tend to be rejected and the functioning of democracy is endangered. Take the electoral victory of the *Front Populaire* in France in 1936. Important elements of the French Right did not at all accept the legitimacy of the outcome. This rejection explains in no small measure the nature of the Vichy regime and the degree of collaboration that was possible between elements of the French Right and Nazi Germany.<sup>14</sup> It is worth adding that Hitler would never have come to power in Germany had the traditional German Right not feared an “illegitimate” electoral victory of the Left. Similarly and more generally from the 1920s into the 1960s, the communist Left in Europe never really accepted the legitimacy of elected non-communist governments because the competing worldviews of the Marxist Left and the rest of the political spectrum were just too far apart. For communists in the postwar period, noncommunist electoral victories were due to the uneven distribution of wealth and economic power and did not establish democratic legitimacy. Process alone cannot ensure a strong degree of legitimacy. For electoral outcomes to be accepted by both winners and losers, there is also need for a set of widely shared basic values that translate into agreement on the overall socioeconomic model that constitutes the framework within which political competition takes place.

In contrast to the examples referred to above, the American and German elections in the years 2000 and 2002 illustrate the existence and importance today of such common ideological ground. Albert Gore, the democratic candidate who lost the 2000 presidential election, actually got a majority of the popular vote. Nonetheless, the electoral rules as interpreted by the US Supreme Court gave the victory to George Bush. Democrats and Republicans certainly hold very different views on a multitude of issues. There is sufficient shared ideological ground in the United States, however, to make one side accept the other’s victory, even when the results are very close and open to interpretation. The same can be said for today’s Germany. In September 2002, the difference in the number of votes between Social Democrats and Christian Democrats was less than 8,000 votes out of a total of 48 million.<sup>15</sup> One may imagine what would

14. The Vichy Regime was the nominal French government between 1940 and 1944. The regime was only quasi-sovereign over the unoccupied zone, which comprised two-fifths of the country to the southeast. The Vichy regime was established by Henri-Philippe Petain as head of state, who suspended the Constitution of the Third Republic of 1875 and the Parliament and transferred all powers to himself. *Liberté, Egalité, Fraternité* (Freedom, Equality, Brotherhood), the French national motto, was replaced by *Travail, Famille, Patrie* (Labor, Family and Country).

have happened in Germany, France, or Italy in the 1950s if the communists had evenly split the national vote with the Gaullists or the Christian Democrats. Whatever the supreme courts or the supreme electoral commissions would have decided about such close outcomes, the loser would have challenged the legitimacy of the winner. The fact that this does not happen in Western democracies today is due not to the electoral rules as such, but to the fact that there is an underlying and agreed-upon socio-economic framework or common ideological ground shared by the overwhelming majority of the population.

With the fall of the Berlin Wall in 1989, the common ideological ground that already existed in Western Europe, North America, and Japan acquired a more global nature. It may be appropriate to call this common ideological ground the “social-liberal synthesis,” a synthesis that has gained ground throughout the 20th century and that has become universally dominant since the Soviet version of Marxism lost its claim to be a credible alternative model of society. “Liberal” is used here in the European sense and denotes a belief in markets, individual enterprise, and democracy. “Social” refers to the traditions and values of equity, solidarity, and belief in the contribution an activist public policy can make to society that has characterized the political Left. In the United States the labels are different, but the basic substance of the common ideological ground that has emerged in the second half of the 20th century is similar to what emerged in Europe, although it is fair to say that the American center is to the right of the European center. It is because of the ideological strength of the social-liberal synthesis that modern democracy can function so well at the level of the nation-state in the developed nations. In this sense, too, Fukuyama was right in proclaiming the end of history. It is useful to briefly recall how “history ended,” and how the social-liberal synthesis emerged from decades of competition between the political Right and Left.

From the middle of the 19th century to the last decade of the 20th century, two powerful socioeconomic ideologies competed for preeminence and power throughout most of the world and within a very large number of individual nation-states. As Stiglitz (2001) puts it: “For almost

15. The Social Democrats (alone) and the Christian Democratic Union/Christian Social Union each received 38.5 percent of the total, with the Social Democrats ahead by only 8,000 votes. The Social Democrats’ coalition partner, the Green Party, got 8.6 percent, and the Christian Democrats’ partner, the Free Democrats (FDP), got 7.4 percent.

a hundred years, two theories had competed for the hearts and minds of people struggling to break free of poverty—one focusing on markets, and the other on government. Both of these ‘modern’ ideologies had their roots in the Enlightenment and in the French and American Revolutions. They were secular, focused on progress through the application of reason and science, and aimed at happiness and prosperity for all through economic progress here on earth—not in an afterlife. There was fundamental disagreement, however, on the means toward those ends.”

On the Right, there was, for want of a better word, “capitalism,” politically liberal or not, with a system of belief in private ownership, private entrepreneurship, and markets. On the Left there was Marxism, with rejection of private property of the means of production perceived as the source of exploitation and inequity, and the trust it placed in central planning as the best mechanism to allocate resources. It is easy, today, to forget how big the difference was between these two worldviews, particularly in the period from the 1920s to the 1970s. In the early postwar years, Oscar Lange, one of the most famous Marxist economists who also taught at the University of Chicago, proclaimed in an article entitled “The Computer and the Market” that contrary to what he himself thought in the 1930s, a socialist economy did not need markets, even for final products, because computers would allow “perfect” planning to allocate resources in a centralized fashion.<sup>16</sup> This view that computerized planning could solve all resource allocation problems was abandoned by most socialists in the 1970s. Nonetheless, the Left continued to believe that planning was essential to steer investment in the right direction. Leftist views were also influential in the theoretical economics literature, particularly in centers such as Cambridge, England, with many mathematical growth theorists stressing the incapacity of capital markets to steer economies on to their optimal growth paths.<sup>17</sup>

On the other end of the political spectrum, conservative economists in the tradition of Friedrich A. von Hayek, Ludwig von Mises, or Milton Friedman, to name three of the best known leaders of conservative thought, argued that markets, including stock markets and foreign exchange markets, would work perfectly, if only governments could

16. Oscar Lange, reprinted in Feinstein (1967). Computers could “mimic” the market and find optimal resource allocations without there being the need for “actual” markets.

17. See, for example, the works of M. Morishima and L. Pasinetti as well as other economists close to the “Cambridge School” of capital theory.

refrain from interfering with them. Monetary policy should not try to react to output or inflation indicators, but be set on automatic pilot, and stable growth would ensue. Central banks should not intervene in foreign exchange markets. “Stabilizing speculation” would ensure the smooth functioning of these markets.<sup>18</sup> Free markets and entrepreneurs seeking profit would ensure growth, and the fruits of growth would inevitably “trickle down” even to the poorest segments of the population. The clash between these two broad worldviews, ranging from conceptual debate to armed struggle, lasted for decades and shaped the history of the 20th century.

There is, of course, more to the history of the last two centuries than the clash between the “pure” versions of capitalism and socialism. Within the capitalist system there was a fierce struggle between the politically liberal variant and the fascist regimes of the 1930s, which ended with the decisive Allied victory in 1945. The rise of fascism itself was part of the overall dynamic referred to above. Fascism gained its initial strength from the fear of Marxism in countries such as Italy, Germany, and Spain and can only be understood within the overall context of the “clash of titans” that was the struggle between the Marxist Left and the capitalist Right.<sup>19</sup> It is also true that the United States, internally, was not much affected by Marxism and, therefore, Americans never fully experienced in their own political process this ideological competition the way Europe and other continents did. Americans experienced the ideological battle differently as citizens of the country that was leading one camp, with the United States in the 1950s becoming the leader of the capitalist world and one of the two key actors in the global ideological battle.

This is not the place for a detailed narrative of this struggle, which shaped modern history. It will be sufficient to remember here just how fierce the struggle was, how many millions died in the Spanish and other ideology-driven civil wars, and in wars in Korea, Vietnam, and elsewhere, and how close the world came to complete nuclear destruction during the

18. The development of “rational expectations” models in mathematical economics gave further support to ideas in the von Hayek-Friedman tradition. See, for example, V.V. Chari (1998) on Robert Lucas’ contribution to modern macroeconomics.

19. “If we [National Socialists] were not, already today there would be no more bourgeoisie alive in Germany. . . . And when people cast in our teeth our intolerance, we proudly acknowledge it—yes, we have formed the inexorable decision to destroy Marxism in Germany down to its last root.” Adolf Hitler’s Speech to the Düsseldorf Industrial Club in 1932. Quoted in Fritz Thyssen (1941).

Cuban missile crisis.<sup>20</sup> In the course of this great struggle, both ideologies and systems evolved, influenced by each other and reacting to challenge. The United States, Western Europe, and Japan emerged victorious from their competition with the Soviet model, but only after capitalism adopted many “socialist” features that transformed the nature of the advanced market economies radically from what could be observed at the beginning of the 20th century. The average share of government in the GDP of today’s industrialized countries was below 11 percent during the late 19th century and around 13 percent before World War I; today the average share is around 45 percent. It stands above 50 percent in Europe and close to 33 percent in the United States.<sup>21</sup> Government expenditures had to rise to fund what is modern governance under the social-liberal synthesis. This model of governance emerged over the course of the 20th century with the banning of child labor, the commitment to publicly funded universal education, the growth of progressive taxation, the development of social safety mechanisms such as unemployment insurance and publicly funded healthcare, the commitment to take care of old people, the increasing effectiveness of monetary and fiscal policies that counteract business cycles, and the strengthening of environmental policies and regulations that protect public welfare.

Germany, an industrial latecomer (and where pure economic liberalism never really became a dominant force), was perhaps the first in providing social protection for the working class against economic insecurity. Germany’s first chancellor, Otto von Bismarck, was the first statesman ever to devise a comprehensive social insurance scheme in the late 19th century. A pragmatic leader, Bismarck was driven by the political motive of competition with the socialists: a positive advancement of the welfare of the masses to forestall the rise of socialism. Conservative industrialists, such as Friedrich Harkort, Alfred Krupp, and Baron Carl Ferdinand von Stumm, were also strong supporters of compulsory social insurance, with

20. The world came within a hairbreadth of massive nuclear strikes and counterstrikes that would have caused the deaths of hundreds of millions of people and led to an aftermath of economic chaos and radiology-induced illness affecting the globe. The Cuban missile crisis is the utmost example of the world coming to the brink of nuclear war. The crisis was a major confrontation between the United States and the Soviet Union over the deployment of Soviet IRBMs in Cuba in 1962. An American naval blockade and high alert status ensued until the crisis was defused by the removal of the Soviet missiles and an American pledge to dismantle IRBMs in Turkey and to never invade Cuba.

21. See Tanzi and Schuknecht (2000) for a comprehensive overview of the expansion of the public economy. For an earlier analysis, see Cameron (1978).

similar motives. The significance of social insurance as an investment in national productivity therefore was first emphasized in Germany, but at the beginning of the 20th century the idea was gaining acceptance in other industrialized countries. Later, both Churchill and Roosevelt advocated comprehensive social insurance. In the United States, some members of Congress unsuccessfully attempted to establish unemployment payments during the 1893–94 recession as well as in 1914 and 1921. It was only in 1932 that the “Emergency Relief Act of 1932” was passed into law, supplementing local relief efforts. In 1933, Roosevelt set up the Civil Works Administration out of concern that direct relief would lead to loss of dignity among the poor. The program faced widespread opposition from the business community and was abolished the next year. In 1935, a Social Security Act was passed that included direct relief and provisions for unemployment insurance. The same year, 20 million people in the United States were already receiving relief.

In England, national health and unemployment insurance were introduced in 1911. The social insurance principle was advanced with the experience of Bismarck in mind (Bismarck had faced stiff resistance to a solely tax-based welfare system) in order not to alienate the voter base of the liberal government. Lloyd George was able to win over the opposition by offering a tripartite financing scheme from workers, employers, and taxpayers. In 1925, the Widows’, Orphan’s, and Old Age Contributory Pensions Act was passed. More than a decade later, William Beveridge, often considered the founder of the modern British welfare state, was asked by the government to prepare a report on how Britain should be rebuilt after the Second World War. Beveridge’s report, published in 1942, recommended that the government find ways to fight the five “giant evils” of want, disease, ignorance, squalor, and idleness. Government took action by passing the Butler Act in 1944 that reformed schooling and declared commitment to full employment the same year. The Family Allowance Act was passed in 1945. Clement Attlee and the Labour Party, after defeating Winston Churchill’s Conservative Party in General Elections in 1945, passed the National Insurance Act (1946), which was followed by the National Health Act (1948) providing free medical treatment for all. In Germany, the postwar economy was rebuilt as a “social market economy” by Ludwig Erhard and the Christian Democrats partly out of Christian Social convictions, and partly to take the wind out of the sails of the rival Social Democrats. In France, important social welfare legislation was passed in 1936 after the first electoral victory of the Left

and was further developed during the postwar period, including by Gaullist governments to forestall and counter the Left. In the postwar period, Sweden and the other Scandinavian countries developed the social-welfare state even beyond the standards reached in the rest of Europe.

What triumphed at the end of the 20th century was not, therefore, the capitalist model of the beginning of the century. It was the synthesis that evolved between capitalism and socialism, based on private property and competitive markets as drivers of productivity growth and resource allocation, and a very large redistributive and regulatory role played by a strong state that “governs” the market mechanisms and funds public goods. Moreover, inside the private sector there is a lot of “planning” going on at the level of corporations, many of which exceed many small countries in size, whereas within the government, market principles are partially applied to improve efficiency and resource allocation. This is what can be called the social-liberal synthesis.<sup>22</sup>

Under the umbrella of this synthesis there is still a lively debate on details and on degree between the political Right and Left. It would be wrong to argue that the distinction between Left and Right has disappeared. Should the tax-to-GDP ratio be 2 percent higher or 2 percent lower? How long should unemployment benefits be available once a worker loses her job? To what extent is it possible to fine-tune fiscal and monetary policies to reduce the business cycle? How tightly should utilities be regulated? These are the questions that one finds in the domestic

22. Note that actual developments have been contrary to the pronouncements of purists of the Left and Right. Both von Mises and von Hayek, for example, argued that “the market economy . . . and the socialist economy preclude one another. There is no such thing as a mixture of the two systems. . . .” (von Mises, 1949); and “Both competition and central direction become poor and inefficient if they are incomplete. . . . a mixture of the two . . . will be worse than if either system had been consistently relied upon” (von Hayek, 1944, as quoted in Hodgson, 1999). For the diametrically opposite view which I believe to be correct, see, for example, Jean-Paul Fitoussi (2002, 2004), who argues that market allocation becomes acceptable only when it is tempered and circumscribed by the democratic political process intruding into the allocation process. The same point had already been developed by Ruggie (1982), who used the term “embedded liberalism” to describe what I call the “social-liberal” synthesis to stress the contribution of the socialist political family to this synthesis. Ruggie already in 1982 described how Western countries learned to reconcile the efficiency of markets with the values of social community to survive and thrive. On the political aspects of this synthesis, see the interesting collection of texts brought together by Canto-Sperber (2003). I would like to stress, however, that in this book the term “social-liberal” is used in a much broader sense than by Canto-Sperber. It encompasses all who agree like Fitoussi that socioeconomic outcomes must be determined by both markets and government action within a democratic political framework.



political debate. They are important questions and the political cleavages still remain. Within the broad framework of the social-liberal synthesis, the Left and the Right will continue to compete. American liberals are different from American conservatives. European socialists have different overall policy preferences from those of European conservatives. Tony Blair's "Third Way" Labor Party remains to the left of the post-Margaret Thatcher conservatives, just as the German Social Democrats' *Neue Mitte* remains to the left of the Christian Democrats' views. But within most nation-states' borders the basic socioeconomic "system" is no longer in question. There is agreement on seeing the government and markets as complements rather than substitutes. Conservatives may emphasize "means-testing" and time duration limits to social insurance expenditures, but the center-right does not propose to forego the social part of the social-liberal synthesis altogether; and the New Left, arguing for an enabling and ensuring state, accepts markets as the basic organizing framework for economic activity. People are no longer willing to die for the sake of nationalizing the means of production or for the sake of privatizing what is left in the hands of the state. Chancellor Schroeder has been able to govern with an 8,000 vote majority and George Bush with a minority of the popular vote because the basic socioeconomic system in their countries is not at stake. The man who used to have a high-ranking job in the KGB is president in Moscow, overseeing socioeconomic policies that are not very different in their ideological content from what we find in Berlin, Paris, Tokyo, or Madrid. Brazilian president Luiz Inácio "Lula" da Silva, who devoted his life to the struggle for socialism and whom the "markets" feared for decades, is presiding, so far successfully, over social-liberal synthesis policies. Before him, as Bhagwati (2004) points out, Fernando Henrique Cardoso, who had invented the "dependency thesis" warning against international trade in a world of unequal power, became president and implemented social-liberal reform policies that increased Brazil's integration into the world economy.<sup>23</sup> Prime Minister Recep Tayyip Erdogan in Turkey, coming from the tradition of political Islam, which has been distrustful of global integration, is implementing socioeconomic policies close to what one sees in non-Muslim emerging-market economies. A page of ideological history, indeed, has been turned.

23. Fernando H. Cardoso and Faletto Enzo's *Dependency and Development in Latin America* is one of the most important pieces of dependency literature. The book was first published in 1969 in Spanish and was published in English in 1979.

## The New Beginning of History

History has not ended, however. As much as there is broad agreement on the basic socioeconomic model within which political competition takes place and policies get formulated at the level of the nation-state, fundamental disagreement and dissent exist and persist when it comes to decision making beyond the nation-state on issues that transcend national borders. There is nothing resembling the social-liberal synthesis at the international level. And yet an increasing number of problems are transnational or global in nature. These problems range from sectors such as health and the environment to the disruptions caused by excessive financial volatility and the moral challenge of extreme poverty, and extend from the threat from terror and weapons of mass destruction to the issues related to the abuse of basic human rights or the need to regulate new techniques of genetic engineering.<sup>24</sup> Thinking about these problems in relation, for example, to fine-tuning the domestic income tax in any single economy reminds one of an observation by Paul Krugman about the hierarchy of issues in a human being's personal life. Krugman (1997) shares with us his belief that the three most important things in a person's life are his or her career, health, and love. All three may be tremendously important, but generally difficult to change. Improvement often requires radical and sustained measures involving high upfront costs. So she or he, contemplating change on a Sunday morning, shrinks from courageous action and decides to improve the basement instead! And life for those who are unhappy but do not take action continues with dissatisfaction and a feeling of alienation at work, habits that will lead to a heart attack, and a marriage with little passion!

Something similar tends to happen in politics. The war in Iraq probably cost the US taxpayer close to \$150 billion by the summer of 2004, and it cost the world economy as a whole substantial additional amounts. A crisis involving war with North Korea or a major problem with Iran could cost multiples of these amounts. Allowing a power vacuum to develop in Afghanistan, and failing to prevent the growth of a deadly terrorist network from that base, cost the United States and the world more than can easily be expressed in terms of hundreds of billions of dollars. And with each of these costs there was substantial loss of human life. Or take the examples of AIDS and Severe Acute Respiratory Syndrome

24. See Fukuyama (2002) for a broad analysis of the new challenges posed by genetics.

(SARS). For all its horror, AIDS is not easily transmittable. SARS is easily transmitted, but thankfully has a short incubation period so that it could be contained relatively easily by isolating infected persons. Suppose, on the contrary, that the incubation period of SARS had been two months rather than two weeks. SARS would have spread all over the world in a much more devastating fashion, with destructive effects on trade, tourism, and industry. The failure to rapidly report the outbreak would have cost large numbers of human lives and probably hundreds of billions of dollars in economic losses. The next disease that arises may have such features and may well constitute a much more formidable threat. Similar interdependence exists in the economic and financial sphere. Policy mistakes in one of the important countries or in a group of countries can slow down the whole world economy, creating unemployment and hardship beyond the area where the initial mistake was made. And yet, there is no framework in place, that is perceived as legitimate, to deal with these global issues. As expressed in the quote at the beginning of this chapter, democratic consent stops at the border of the nation-state.

Having an international political system in place to prevent or at least reduce the likelihood of crisis and the ensuing costs would improve the welfare of all, much more than what any individual nation can achieve by fine-tuning the income tax. It seems clear that the degree of interdependence that exists in the world of the 21st century greatly increases the scale of the damage that failure in one part of the system can inflict on all. Conversely, the benefits that can be generated by early preventive action can be immense. And yet it is extremely difficult to take preventive action. In so many fields, preventive action must be international in nature to be timely and effective. To be accepted, it must be legitimate, and it must command adherence and respect. Unfortunately the current international institutional architecture lacks the required degree of legitimacy. It is essentially a leftover of the postwar world of the 1940s and cannot, without major reforms, help us manage the 21st century.

The new beginning of history will be driven by the debate on how to achieve this effectiveness and legitimacy in global governance. The world is in need of an extension of the social-liberal synthesis into the global sphere. Those who gathered at the World Social Forum in Porto Alegre, Brazil, in 2003 with a sense of moral outrage at the undemocratic and inequitable dimensions of the globalization process must turn their energies to finding ways of governing globalization for the benefit of the great majority, rather than trying to reject or deny an irreversible process. On

the other hand, the increasingly global business and financial elites that dominate the world economy and influence political decisions must realize that the dangers of insufficient redistribution, regulation, and policy coordination are likely to lead to storms and floods where everyone will drown. How can happiness and security be ensured if hundreds of millions of people continue to live in abject poverty in an interdependent world where suffering and luxury form a dramatic contrast on television screens every night?<sup>25</sup> That contrast can lead some people to rationalize the most inhumane actions. How can devastating terrorism be prevented if people all over the world do not cooperate in a worldwide effort to secure peace that is perceived as fair and legitimate? Must it take a catastrophe even greater than September 11 in New York or March 11 in Madrid for humankind to really come together and face this danger? What use is it to build fences around wealth and privilege if a disease bred by poverty can travel by air, killing rich and poor alike? Has the time not come to devote some real effort and imagination to solving the big problems that threaten us rather than engaging in a continuation of the politics of the past circumscribed by irrational habits and imprisoned in a conceptual framework that is no longer relevant? History continues. If we want to survive and prosper, must we not do more than just try to fix our basement? It is appropriate to end this chapter with a quote from Oscar Wilde who defined progress as the realization of utopia:

“A map of the world that does not include utopia is not worth even glancing at for it leaves out the one country at which humanity is always landing. And when humanity lands there, it looks out, and seeing a better country, sets sail.”<sup>26</sup>

We must indeed face the challenges of the new century by setting sail for new ideas, mindful of the dangers inherent in ideology, but understanding that new realities require new conceptual designs and new practical solutions.

25. Daniel Cohen (2004) makes the point that in many ways, the defining characteristic of today's globalization when compared with the globalization of the 19th century is how “visible” the contrasts are—how easily the gaps in power and wealth can be *perceived*. Brzezinski (2004, 42–43) agrees: “The contemporary world disorder stems more broadly from a new reality. The world is now awakened to the inequality in the human condition. . . . spreading literacy and especially the impact of modern communications have produced an unprecedented level of political consciousness among the masses.”

26. The passage is from Oscar Wilde's essay “The Soul of Man under Socialism” (1891).