

What is the Relation of Neoliberalism and the Liberal Script?

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The term “neoliberalism” is rarely used by economists. I propose to use “extractive and inclusive institutions” instead to describe economic and political systems. Extractive economic institutions such as monopolies and cartels are a threat to inclusive political institutions. If, instead, institutions keep access to markets and private property open and allow people to develop their talents, economic liberalism can underpin democracy and social rights.



Here are my five cents on “neoliberalism” – or a worm’s eye view of an economist who studies markets at the micro level. One difficulty I have is that the term ‘neoliberalism’ is rarely used by economists, on the right or on the left. Thus, it is not an analytical category. Rather, research and political discussions center around different aspects of capitalism or the market economy:

- redistribution and taxation (as evidenced currently where the advice to not lower the tax rates to adjust to inflation by the Council of Economic advisors (SVR) has led to a prompt reply of former conservative members of the council), or
- the speed of the green transformation of the economy, the use of subsidies or incentives for companies, the scope of emissions trading and the price for carbon, or
- the minimum wage (its effects on social welfare and unemployment), or
- the redistributive and incentive effects of the Bürgergeld in comparison to Hartz IV.

Historically, it is evident that free markets, private property etc. were integral parts of liberalism, a movement that was emancipatory against the

backdrop of feudalism. In this sense, *capitalism and the Liberal Script are mutually constitutive*. The freedom to engage in exchange that is beneficial for both sides is central to a liberal order. This does not hold true for all goods (private property can be restricted) but for many goods. Life in a kibbutz or cloister with almost no private property appears as distinct from what we consider a liberal order. (However, it is part of a liberal order that people can decide to live in a cloister or a kibbutz, that such institutions are created and maintained.)

What is it that has turned liberalism into “neoliberalism” and rendered the project of economic liberalism questionable? While free markets and the free exchange of goods are part of the Liberal Script, many different versions of capitalism exist.

Is private property the defining element, potentially endangering social rights, and democracy? I think it is a mistake to focus on private property. Instead, I propose to look at the type of institutions that govern economic exchange with private property. One way to do this is by using Daron Acemoglu’s terms of **extractive and inclusive institutions** (mainly laid out in his book with James Robinson “Why nations fail”, 2012). Focusing on this distinction instead of on the institution of private property has more explanatory power for country differences in welfare, equality, etc.

Inclusive economic institutions create inclusive markets which give people the freedom to do what they want to and use their talents, providing a level playing field. Institutions that distribute power broadly in society are necessarily pluralistic. Having people found businesses, take on jobs in which they are productive, with high levels of education and innovations, are important for economic well-being.

There is a strong **synergy between economic and political institutions**. In this sense, extractive economic institutions such as monopolies, cartels, regulatory capture (i.e., no independence of regulatory agencies) are hallmarks of neoliberalism, and they are a threat to inclusive political institutions. A feedback loop exists. An elite that controls political institutions often also controls economic institutions to extract resources from society. Even if a new group of people grabs power, it has an incentive to continue extracting resources using the economic institutions (monopolies etc.) in place. Combinations of inclusive and extractive institutions tend to be

unstable. E.g., when economic institutions are inclusive and pluralistic, groups that become rich due to economic growth will destabilize the existing elites and try to replace them. Conversely, if political institutions are open and pluralistic, extractive economic institutions are likely to be regulated to give people access to the wealth created.

Summing up, if the economic institutions are extractive, a tension exists between the economic sphere on the one hand and democracy and social rights on the other. In contrast, a competitive market order and private property go along with democracy and social rights when the economic institutions are inclusive.

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