

## Critical Realist GPE

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## Neo-Gramscian GPE

- **Quite successful in some IR/Politics departments**
- **However, what tends to be lacking is economic theory proper → limited potential for wider impact**
- **Systematic methodology is also partially absent**
  - for instance, Robert Cox's famous "Essay on Method" fails to mention any social scientific method

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## The roots of the estrangement of economics from the social sciences

Neoclassical economics has become insulated from the social sciences because of the inherent logic of its geo-historical development:

1. *Ontologically*, the positivism of classical economics grounded both the capitalist conception of man and the notion of 'invisible hand' leading to the automatic harmony of atomist market-actors.
2. *Rhetorically*, the mathematical conceptions of neoclassical economics, revolving around the concept of equilibrium, simultaneously imply the quality of being 'scientific' and reinforce (1).

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## Classical orthodoxy

- **David Hume:** empiricism, ontological atomism, the idea of self-correcting market
- **Adam Smith:** the concept of division of labour, the metaphor of 'invisible hand' (advocating free international trade)
- **David Ricardo:** used drastically simplifying assumptions, systematic thought experiments and rigorous deductive logic in constructing arguments
  - steps towards neoclassical reasoning;
  - theoretically, Ricardo also developed the notion of 'comparative advantage'

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## Neo-classical fundamentalism

- In the late 19th century, new notions emerged, such as:
  - marginal utility and marginal costs
  - elasticity of supply and demand curves
  - and the general equilibrium analysis
- Newtonian physics provided the model of science
  - the basic tool: differential calculus
  - the 19th century developments in probability theory were also utilised
- Many of the breakthroughs were made in France and Germany, but this form of reasoning became hegemonic in the US in the course of the 20th century, consolidating its leading and disciplinary role in the aftermath of World War II and at the outset of the Cold War
- Once the conceptual basis was established, neoclassical economists could focus on studying the mathematical properties of different systems of price-determination
  - research excellence was defined in terms of increasing sophistication of mathematical and statistical tools, i.e. in terms of technical methods

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## The real effects of the neoclassical methodology (supported by abundant funding and *Pax Americana*)

1. In contrast to the classical political economy, this kind of closed system modelling implies the total separation of economy from the rest of society.
2. The practical real-world problems of the classical economists fade into the background and economics develops as something akin to a branch of mathematics.
  - **High theorists:** If the world does not accord with the predictions of the theory, the problem does not lie in theory but in the world that fails to meet the requirements of the rigorous theory. Therefore the conclusion is usually that, instead of revising the orthodox theory and perhaps also its methodological underpinnings, the world must be changed to accord better with its prescriptions.
3. Over time, for those economists focussing on the technical methods only, the conceptual foundations of their narrow and specific approach started to appear increasingly self-evident and universalisable.
  - Keynes' 'general theory' → IS-LM apparatus
  - the imperialism of economics (e.g. Gary Becker)

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## The implicit scientific or critical realism of heterodox economics

- Orthodoxy contested → heterodoxy
- Marx as a "proto-critical realist"
  - the bulk of classical political economy 'confines itself systematically in a pedantic way, and proclaiming for everlasting truths, the trite ideas held by the most complacent bourgeoisie with regard to their own world; to them the best of all possible worlds'
  - the main problem of Marxist economics: the labour theory of value
  - perhaps Marx was in fact more Aristotelian than critical realist...
- Keynes was a kind of Marshallian, but introduced or developed a number of new notions, at times coming close to Marx
  - in the real world, future is open, and therefore uncertainty prevails
  - also, the fallacy of composition is prevalent → macroanalysis must be primary
  - and a number of theoretical innovations
- The basic methodological point of Keynes is line with realism: assumptions must be realistic and empirically corroborated
- Also many other key figures of the 20th century economics agreed with Marx and Keynes: Schumpeter, Kalecki, Robinson, Galbraith and others criticised orthodoxy by claiming that its models are irrelevant in understanding the way real economies work
  - orthodoxy is thus dangerously misleading if applied in policy

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## Critical realism as a framework for reintegrating economics and GPE

- GPE presupposes various theories of heterodox economics & GPE itself is based on realist tenets → potential for reintegration
- The framework of CR:
  - realist conception of causality
  - open systems; action (efficient cause), structure (material cause) and power (transformative capacity → causality)
  - epistemological relativism
  - the process of iconic modelling
  - geo-historical qualitative evidence is ontologically primary, but also quantitative evidence indispensable
  - "contrastive demi-regs"

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## Towards reintegration

- Various hypotheses and explanatory claims can be respecified in critical realist terms, and then systematically assessed in terms of ontological, theoretical and empirical plausibility
- Orthodox economic theories, heterodox economic theories and contentions of GPE often make references to the same area of reality and purport to explain overlapping outcomes (although they are usually specified in somewhat different ways, there is overlap that suffices for systematic comparison)
  - this is not only to enrich GPE but also to introduce concepts such as structure and power to economic theory

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## A key example: explaining financial crises

- How to explain financial crises such as the so called Asian crisis of 1997 ☒?
- There have been nearly 200 financial crises since the late 1970s
- Relevant contrastive demographics → indicative of transformative power of finance

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### Daily forex trading volume and its ratio to central bank reserves

Year	Forex volume per day	Average annual growth	Global official forex reserves	Ratio of reserves/forex
1977	18.3		265.8	14.52
1980	82.5	65.2	386.6	4.52
1983	119	13.0	339.7	2.85
1986	270	31.4	456.0	1.69
1989	620	31.9	722.3	1.17
1992	880	12.4	910.8	1.04
1995	1249	12.0	1148.8	0.92
1998	1490	6.0	1636.1	1.10
2001	1200	-7.5	2021.5	1.68

All forex and reserves figures in billions US dollars

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### Volatility in currency markets

	(Standard deviation of monthly changes)				
	1960-69	1970-79	1980-85	1986-89	1990-94
United States	0.2	1.1	1.8	2.1	1.5
Japan	0.3	1.9	2.4	2.4	2.4
Germany	0.7	1.9	2.4	2.4	2.4
France	1	1.2	1.1	0.8	0.7
Italy	0.3	1.7	0.7	0.6	1.9
United Kingdom	1	1.5	2	1.8	2
Canada	0.2	1.1	0.9	1	1.1
Australia	0.6	2	2.3	3	2.2
Austria	0.4	0.7	0.7	0.5	0.6
Belgium	0.3	0.8	1.1	0.8	0.9
Denmark	0.4	1.1	1	0.8	1
Finland	2.1	1	0.9	0.6	2.1
Greece	0.2	1.6	2.9	0.9	0.8
Iceland	4.4	3.7	3.4	1.6	1.1
Ireland	0.5	0.7	1.4	1.2	1.4
Netherlands	0.3	0.8	0.9	0.7	0.8
New Zealand	1.3	1.6	2.4	3	1.4
Norway	0.4	1	0.9	1.4	0.7
Portugal	0.4	1.9	1.7	0.8	0.9
Spain	1.2	2	1.4	1.1	1.5
Sweden	0.9	1.1	1.7	0.5	2
Switzerland	2.4	1.6	1.5	1.2	1.5
Turkey	0.3	6.7	3.8	2.7	6.7
Average	0.773913	1.678261	1.708696	1.386967	1.634783
Average of G7 (excl. Italy) + Australia + Switzerland	0.65	1.6376	1.8	1.8376	1.726

Source: OECD 1995

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## Global markets of bonds and equities

Cross-border transactions in bonds and equities (as percentage of GDP) \*

	1975	1980	1985	1990	1991	1992	1993	1994	1995	1996	1997	1998
United States	4	9	35	89	96	107	129	131	135	159	213	230
Japan	2	8	62	119	92	72	78	60	65	79	96	91
Germany	5	7	33	57	55	85	170	158	172	200	257	334
France	n.a.	5	21	54	79	122	187	197	187	258	314	415
Italy	1	1	4	27	60	92	192	207	253	470	677	640
Canada	3	9	27	65	83	114	153	206	187	251	355	351

\*Gross Purchases and sales of securities between residents and non-residents.

n.a. indicates data not available.

Source: BIS 1999b: Table VL5, 118.

## Explaining financial crises

- Distinction between triggers and generative structures
  - triggers can be extrinsic to the financial system, while the structures and powers generating these kinds of crises are characteristically intrinsic to "developed" systems of finance
  - the constitutive and regulative rules of financial practices are also legal → regulation matters, and the line between inside and outside of finance is graded, fuzzy and contingent
- Key concepts: openness – uncertainty – institutional arrangements
- Structure as an outcome of the past process: the financial multiplication process tends to result in a structure that has the power to generate crises
  - rearticulation of some of the basic ideas of Keynes, Minsky, Kindleberger and others

## Why did global finance re-emerge? Power of financial actors

- Rules of action: expectations are formed in terms of orthodox economic theories – this becomes also a prescription how things should be
- Resources: financial multiplication has increased the transformative capacity of financial actors using their available resources to bring about desired changes (e.g. attacks against a currency)
- Also direct lobbying – collective associations pursuing common interests and views
  - pushing for reforms that ensure continuous extraction of further resources into the financial system
- These, however, do not suffice to explain the re-emergence of global finance, although they certainly co-explain some of the subsequent developments

## Explaining further layers of global finance: structural power and hegemony

- Historical re-emergence of *haute finance* in the 1960s and 1970s
  - at first, problems of competitiveness combined with hegemonic aspirations of particular states (US, UK)
  - then transnational hegemony of economic orthodoxy
- Eurodollar markets, offshore centres, tax havens → structural power as 'exit options' for capital (both productive and financial)
- As a consequence, a panopticon system has emerged: credit rating, exit options, social allocation of short-term (speculative) capital and related media practices make governments accountable to short-term investors rather parliaments → OECD governments have become increasingly susceptible to the arguments of economic orthodoxy and, also, accessible to the financial lobbyists
- States and international organizations are, however, always involved in any process of development of transnational financial markets
  - the US and the IMF were pushing for the Asian tigers to liberalise their financial markets in the early 1990s, also as part of the geo-economic strategies of the US state

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## Explanation, criticism and transformative praxis

- A deeper understanding and explanation of the conditions and generative structures of financial crises is also critical
- A critical condition-- 'T is an inferior account'
- An explanatory condition – 'T can be explained'
- T in this case could be an orthodox economic theory as applied to finance
  - T assumes that financial markets are determined by developments elsewhere, and financial markets and other markets are in a simultaneous equilibrium or getting 'there + 'invisible hand'
- The point now becomes to change those structures that presuppose T → normative argument for transformation
- Communicative action primary, but peaceful strategic action may also become necessary
- A direction has to be established: concrete utopias
  - political possibilities, success and viability always contextual and contingent

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## Conclusion

- In the case of explaining the late 20th century financial crises, the construction of an explanatory model began with a rearticulation of Keynesian theories, respecified in critical realist terms
- Then it moved to explaining the emergence of the powers and structures that account for the possibility of these kinds of financial crises
- At first: power-analysis focusses on financial actors (first and second dimension in Lukes' categorisation)
- But deeper structural analysis – leading also back to past actions of states and international organisations, in accordance with the transformational model of social activity – is necessary as well; here we can also draw on many neo-Gramscian studies
- In this kind of explanation, (heterodox) economics and GPE become fully integrated, as part of the wider scheme of wholistic social scientific explanation

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