The Demise of the "Left-Right" Split

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THE LONG-HELD VIEWS OF SOCIAL philosophers, economists and policy-makers have been challenged in three episodes during this volatile century—the Great Depression of the 1930s, stagflation during the 1970s, and global economic integration currently under way. In each case, the tension between the "left" and the "right" has been over the desirable "size" of government. Whereas those on the left argued that prosperity required government to play a significant role in the economy, the right countered that government was wasteful and actually stood in the way of creating prosperity. But this left-right split misses too much that is important, and the events of the past decade have made this very clear. Serious thinking about the government's place in the economy requires that the debate become two-dimensional.

The Pendulum Swings to the Left...

In the four decades following the Great Depression, all western countries experienced a significant expansion in the scope of government. They witnessed a surge in the number of spending programmes and also an increase in their generosity. In addition, government extended its reach significantly through the increase in the number of state-owned corporations, and in the growth of regulations and regulatory bodies. This growth of government was in pursuit of two distinct goals: a more efficient allocation of the economy's resources, and a more equitable distribution of income. Put more crudely, these goals correspond, respectively, to the maximisation of the total size of the pie and a more equitable distribution of that pie. Regulations and state-owned corporations were aimed at achieving the first goal; social programmes were aimed at the second.

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Influenced by the experiences of the Depression, the pendulum of government swung slowly but surely in one direction. The view that government was necessary for "hands-on" management of the economy reached its bizarre peak in the 1970s when US President Richard Nixon—a Republican, accustomed to eschewing the government's role in the economy—imposed wage-and-price controls in an effort to end the OPEC-initiated inflation.

...and Then Back to the Right

Disillusioned with big government, Margaret Thatcher and Ronald Reagan ushered in a new era; the pendulum stopped and then began to reverse direction. Thatcher dismantled the "nanny state", confronted the unions head-on, and began privatising state-owned companies. Ronald Reagan pursued the same agenda in the United States. Though his view of the need to defeat the Soviet Union (combined with a simplistic view of supply-side economics), led to a massive increase in public borrowing, he was still able to convey the message—not without some irony—of the undesirability of big government.

Though it took some time for governments to overcome the inertia that accompanied public spending, most western countries had embarked on credible paths of fiscal consolidation by the early 1990s. Some of this was achieved through tax increases, but the lion's share of the adjustment was accomplished by expenditure reductions. The current fiscal outlook is indeed remarkable when contrasted with the situation of the early 1980s. Nearly all of the EU members have brought their deficits below the Maastricht threshold of 3% of GDP, the US appears to be on course for a balanced budget early in the next century, and Canada—now the OECD's fiscal favourite—will achieve a budget surplus sometime this year. The pendulum has swung considerably since Thatcher and Reagan first arrived on the scene almost 20 years ago.

A Change in the Debate

During the first swing of the pendulum, the debate about the government's role in the economy was mostly one-dimensional: How "big" should government be? Arguments centred around how much governments should tax and spend. Whereas the left tended to focus on the equity issue at the expense of the efficiency issue, the right did exactly the opposite. So the left promoted big government because they saw it as the only way to achieve their pet goal of equity. The right advocated small government as the only way to achieve their pet goal of efficiency. So, while the left and right appeared to be confronting each other head-on in this debate, they were actually arguing past each other to a considerable extent.

This is not surprising in light of the economic conditions of the time. Fast-growing economies in the post-war period provided the illusion that public funds were not particularly scarce. It appeared that society could have "more government" without having less of something else. In such a setting, the question of what the government *ought* to be doing, and *why* it should be doing it, was not particularly pressing. In short, little attention was paid to distinguishing the separate equity and efficiency aspects of government intervention.

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During the second swing of the pendulum, however, making such a distinction was unavoidable. It was simply not possible to cut billions of dollars of public expenditure without sparking a debate about whether the axe should fall on programme X or Y. And within such debates, policy-makers were naturally led to examine the underlying motivation for these programmes: were they to promote equity or efficiency? The debate about government's role in the economy had become two-dimensional.

There Are No Longer Wings...

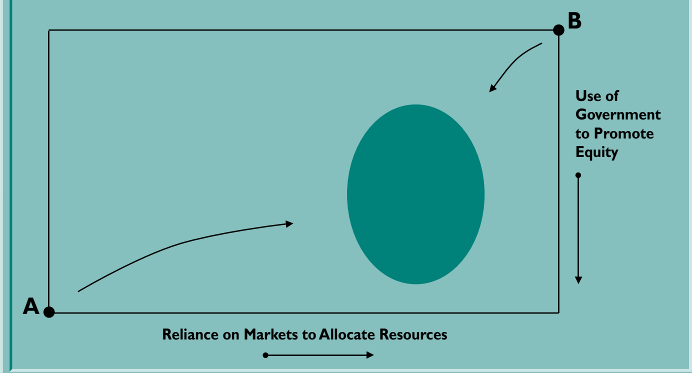
The past two decades have thus witnessed a fundamental change in the debate over government's role in the economy. We no longer argue—or we certainly should not—whether "big" government is better or worse than "small" government. Unless we know what the government is doing, "big" and "small" are meaningless. The meaningful debate is now about more fundamental issues. How can government policy be used to improve the allocation of resources, and thus increase the total size of the pie? What government policies can be pursued to promote more equity in how that pie is distributed? And to what degree are these two goals interdependent?

The left-right split is no longer useful (if it ever really was). What label do we use for Tony Blair, who cuts benefits to single mothers by stressing the negative effects on the willingness to work? Somehow, "left wing" seems to be missing something important. Similarly, it is the current Liberal government in Canada—not their "right-wing" Conservative predecessors—who implemented significant spending cuts and wrestled the deficit to the ground. Such apparent contradictions can only be resolved by thinking about both dimensions of the government's place in the economy.

This is not to suggest that there is less disagreement now than before—only that the source of the disagreement is now clearer. Whereas the old one-dimensional controversies were often two sides arguing past each other, clarifying the two dimensions permits a much sharper debate.

The accompanying figure shows one's views of government along these two dimensions. The horizontal axis measures one's commitment to using markets to allocate resources; a move to the right means that government plays a smaller role in determining the eventual size of the pie. The vertical axis measures one's commitment to using a tax-and-transfer system to redistribute income; a move downward means that government plays a larger role in redistributing that pie. Somewhere close to point *A* is someone from the extreme "left", with little devotion to markets and considerable commitment to promoting equity. Someone from the exteme "right" resides near point *B*; they have little interest in the redistribution of income and uphold a considerable commitment to free markets.

The Two Dimensions of Government



...But There is Still a Centre

So what has become of the schism between the left and right? Placing their beliefs within two dimensions, it becomes clear that the last decade has seen a notable change in positions.

If there is one thing that the leading thinkers of the left have learned over the past decade, it is that markets are tremendous vehicles for motivating individuals, allocating resources, and generating wealth. They have begun to realise that they can maintain their goal of active redistribution only if they are careful about the policies they use.

The right has had to acknowledge that markets do occasionally fail in terms of the allocation of resources. Problems of incomplete information, market power, and public goods provide, at least in principle, a role for intelligent and prudent government intervention.

Finally, extreme views regarding the distribution of income are now commonly believed to be both unrealistic and undesirable. It is utopian to argue—as the left used to—that the lion's share of inequalities should be removed by policy; it would require so much distortionary intervention that the potential pool of wealth would collapse. On the other hand, even the extreme right can see that some income redistribution is desirable. Not only is it quite obviously the decent thing to do, but wealthy individuals, especially, know that their fortunate position would be put seriously at risk by the social unrest that often accompanies extremes in income distribution.

All of this suggests that those from both the left and the right are moving toward the shaded region in the figure. There is a broad consensus that markets are very useful, but that they sometimes fail, and that carefully designed government policy can increase the total size of the pie. There is also a consensus that using government policy to alter the distribution of that pie is important, but sufficient attention must be paid to maintaining healthy incentives for work and investment.

The sensible debates are no longer about "big" versus "small" government. They are about such things as: Do we have better ways of achieving our distributional goals than using extreme tools like minimum wages and rent controls? Can the management of public pension funds be entrusted to private firms? Should anti-trust policy be more-or-less ignored in an era of global markets? Is post-secondary education best financed by students or tax-payers? Can a voucher system applied to health care address the difficult issue of adverse selection? In all of these debates, attention must be paid to both equity and efficiency issues—the two dimensions of government's place in the economy. ◆