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## Forward Thinking

# Thatcherism and the origins of the 2007 crisis

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**Abstract** The crisis of 2007 affected banks, financial institutions and retailers at a macro-economic level as well as individuals and families at a micro-economic level. Following the acceptance of a crisis the politics of blame began, with politicians, the media academics and the public assessing who (or what) generated the crisis and what could be done to alleviate it. Three broad narratives of blame have hitherto been purported; the first views the crisis as an international crisis, or whose roots stem from the United States, the second suggests that the policies of New Labour generated the crisis and the third traces the origins of the crisis back to Britain's withdrawal from the ERM in 1992. In this article I present a fourth account which sees the crisis as stemming from the 1980s and the policies of Thatcherism. Specifically I argue that the 'Right to Buy' scheme and the Big Bang deregulation of 1986 shifted the labour-capital relationship decisively in favour of capital paving the way for the crisis of 2007. Through doing so I question contemporary policies introduced to try and alleviate the crisis, asking if they will create a new growth model or simply entrench/recreate the model developed in the 1980s.

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## Introduction

The existing literature on and debates around the origins of the 2007 crisis broadly fit into three categories. The first views the crisis as an international crisis (French and Thrift, 2009), or at least ones whose roots can be traced to the United States (Duca *et al.*, 2010), and one which policy makers in Britain only had a little or indirect effect upon. The second suggests the crisis evolved from the accession of New Labour (Goodhart, 2008; Hodson and Mabbett, 2008) in particular Gordon Brown's time as Chancellor, and the promising of the ending of boom and bust (Kavanagh and Cowley, 2010, pp. 19–23). The third argument offers a slightly longer-term approach, whereby the financial crisis is seen as stemming from the ERM crisis of 1992 (Martin and Milas, 2013). In this article I contend that the financial crisis has a



longer history than either 1997 or 1992. In doing so I suggest that British policy makers were directly responsible for laying the foundations of the crisis in the 1980s – though the trigger event(s) can be linked to the role of investments in US sub-prime mortgages, the lack of liquidity within the UK banks in August 2007, or the ballooning of government debt following the bank bailouts/ nationalisations of 2007/ 2008 depending upon the accepted definition/narrative of the crisis (Hay, 2011; Blyth, 2013). I do not contend that Thatcherism was responsible for these events, which occurred in the 2000s, but that the reforms of the Thatcher government set the political and economic scene in such a manner that once such problems emerged/ became prominent a crisis (however defined) was the logical conclusion of events. In this article I trace the foundations of the 2007 crisis back to the reforms of the 1980s and suggest that the origins of the current crisis can be seen as stemming from the Thatcher government's response to the previous crisis, that of the 1970s and early 1980s – a crisis in which the trade unions were heavily blamed for high inflation rates, high levels of industrial unrest and stagnant economic growth. By looking at the financial crisis in such a light new questions emerge both from a historical perspective for example, reassessing the legacy of Thatcher's economic policy, and a policy-making perspective for example, if the banking sector is left unreformed in the wake of the current crisis, one for which they have been heavily blamed, then can we expect a similar crisis in the not too distant future? Alternatively can we speak of a sustainable crisis resolution before changes are made to the banking sector?

Before I directly address the Thatcher government's economic policies and record I wish to partly deconstruct the argument of those who support the view that the crisis is a global phenomenon. While I do not disagree that the crisis has impacted many countries – though predominantly those classified as 'westernised' – this negates two important aspects; first that the position of Britain in the global economy was a product of specific economic policies such as the 'Big Bang' reforms of the 1980s and second that the position of Britain in the crisis was in some respects unique, and the pattern of economic 'recovery', has been different to the 'recoveries' in the Eurozone or the United States.

## **The 2007 Crisis as a Crisis of Growth**

Following the 2007 crisis there has developed a number of competing rhetoric's and narratives each which aim to define, understand and/or conceptualise the crisis. Hay (2011) highlights two distinct crises the first being the US sub-prime crisis and the second a crisis of British growth. Although the two are related they are not the same phenomenon as Hay (2011, p. 14) notes;

Though it is tempting to see the UK's longest and deepest recession since the 1930s as a product of contagion – the consequence of financial interdependence

more than anything ... is both profoundly wrong and profoundly dangerous. It is wrong because this is just as much a crisis (if crisis it is at all) of the Anglo-liberal growth model as it is a specifically American crisis; it is dangerous because it may lead us to overlook the endogenous frailty at the heart of the Anglo-liberal growth model that has been exposed.

In another article Hay (2013, p. 24) also distinguishes between a 'debt crisis' and a 'growth crisis' arguing that although the former has become the dominant discourse promoted by elites (politicians and the media) it is in fact a second order crisis which stems from the growth crisis. Hay further argues that blame attribution alongside political considerations has led to a misdiagnosis, whereby the crisis of growth has been mislabelled a crisis of debt.

Krippner (2011) in exploring the crisis in the United States notes that the crisis stemmed from policy makers actions in the 1970s. Tracing the American economy from the 1970s and 1980s into the 2000s she argues that the problems of the crisis stemmed from a financialisation of the economy. Defining the 'central thesis' of her argument she notes;

the turn to finance allowed the state to avoid a series of economic, social and political dilemmas that confronted policy makers ... paradoxically preparing the ground for our own era of financial manias, panics and crashes some three decades later. (Krippner, 2011, p. 2)

According to Krippner the problems were exaggerated not only through this shift in the balance of the economy but through a belief that financial markets were, and could be, efficient. Such a philosophy can be said to have occurred in Britain. Important within this shift was a belief in the virtues of the free market and neo-liberal ideologies. Crouch (2009, p. 388) points to notions of 'privatised Keynesianism' which developed out of the inflationary pressure felt by states in the 1970s. The privatised Keynesianism was based on an increasingly extended investment chains and the opening up of these trade chains to riskier trades and traders. According to Crouch (2011, p. 99) 'banks constructed bundles of very varied risk, in which quite safe loans were mixed up with unsecured mortgages in unspecified proportions'. This is linked to the short-termism of investors buying such bundles of risk, Crouch continues 'but the traders buying them showed no interest in examining the bundles, as they were geared solely to the set of beliefs about sets of beliefs about sets of beliefs in an almost infinite regress that was setting prices in the secondary markets.' This form of privatised Keynesianism was based on the confidence of markets to perform efficiently, and a mood of 'excessive optimism' on the part of traders, 'a confidence proved to be justified – that governments would not let the system fail and would therefore move in to compensate them for any losses they made through excessive trading' (Crouch, 2011, p. 101). This system prioritised the role of capital over labour within the



economy; it emphasised the role of the market and the traders working within such a framework.

While it would be wrong to suggest that such changes caused a the crisis, it would be equally misinformed to suggest that the blame lies solely in the global financial system or the culprits for the crisis lay in the United States when the crisis has trajectories unique to Britain. I argue that in order to fully understand the crisis of 2007 the unique positioning of Britain's economy in 2007 – something that directly stems from the macroeconomic policies of the 1980s and 1990s – must also be explored and understood. Here I wish to explore the nature of the British crisis – the crisis in the British growth model. In doing so I follow Hay's (2011, 2013) assertion and argue that this – rather than systemic problems of debts – is the most pressing crisis facing Britain. Although this crisis came to prominence in 2008 (as a result of changes that affected Britain but also most of the westernised world) I argue that this crisis has deeper foundations, and that these foundations were laid by the politics of the Thatcher governments in their responses to the Keynesians crisis of the 1970s.

In this article I demonstrate how events and policies that changed the political economy in the 1980s can be seen as laying the foundations for the current crisis. Policies such as the 'Right to Buy' scheme and the 'Big Bang' deregulation of the financial sector, while distinctive in their own right, are important in assessing these shifts in policy making. Both generated growing inequalities, helped prioritise capital and the owners of capital over labour and organised labour and significantly helped to shift the drivers of British economic growth. Further, by assessing these policies and drawing parallels with policies aimed at promoting Britain's recovery from the financial crisis I ask, 'are we simply repeating the mistakes of the past?' and 'how new or novel are the proposed means of recovering from the crisis?' The answers to these questions link into wider debates surrounding the sustainability of present policies aimed at generating an economic recovery.

## **Thatcher and the 'Crisis Resolution' of the 1980s**

Thatcher and the Conservative Party won the 1979 general election amidst perceptions of mounting industrial unrest, excessive union militancy and power and an 'oversized' state (King, 1975). British economic growth in the 1970s was beset by the problem of stagflation – a problem with roots in the 1960s – and talk of a 'British economic decline' was rife (Artis and Cobham, 1991; Will, 2009). Equally the trade unions were perceived and portrayed as being overtly political in their actions and a threat to wider democratic principles. Two elections, February 1974 and 1979, it was argued, were lost by incumbent governments because of excessive or unnecessary industrial unrest (Butler and Kavanagh, 1980; Gilmour, 1992, pp. 76–77). Such problems formed the basis for the construction of a crisis narrative, and enabled

politicians and the media to blame the trade unions and pursue an anti-union agenda (Hay, 1996; Sandbrook, 2010).

Thatcherism was, I contend, a set of deliberate policies aimed at weakening the power of labour in the production process. Thatcher used and amended the narratives of crisis which emerged in the 1970s to promote the role of capital over labour in the economy. Thatcher herself was heavily involved in this process, and stressed the importance of reigning in trade union powers (*The Sun*, 1979, 2; Dorey, 1995). In 1982, Ferdinand Mount, one of Thatcher's policy advisors, wrote of the goal of reducing the trade union power and envisioned a trade union movement 'much reduced in size' (Duffin, 2013). Over the course of the 1980s and 1990s 'the core institutions of collective regulation were systematically dismantled' (Howell, 2007, p. 164).

The weakening of the trade union movement was central to Thatcher's macro-economic policy objectives; the rebalancing of the economy and the shift away from Keynesianism towards monetarism and shifting attention from unemployment to inflation statistics. If trade union powers could be reduced, so the narrative went, then economic factors such as unemployment would become increasingly less significant and could be replaced as key indicators by measurements such as inflation.

Here I do not wish to surround myself with debates about the 1970s. Instead I suggest that the rhetoric and policies of the Thatcher government weakened labour and promoted the role and importance of capital in the economy policies which although successful in creating economic growth in the short term generated a very unsustainable economy and laid the foundations for the crisis of 2007. In doing so I shall explore two particular policies of the Thatcher government: the 'Right to Buy' scheme and the 'Big Bang' deregulation of the financial industry in 1986.

## **'Right to Buy' Scheme (Housing Act 1980) and the Creation of a Housing Bubble**

Housing policy was central to Thatcher's electoral success in 1979 and 1983. The Conservatives were able to offer new and pragmatic policies, based around twin goals of 'reducing public expenditure and encouraging growth in home ownership'. The central pillar of this strategy was the selling off of Britain's housing stock through the 'Right to Buy' scheme (Monk and Kleinamn, 1990, p. 121).

The 'Right to Buy' scheme was introduced in 1980. It gave those living in social housing the chance to purchase their houses from the government at a reduced rate of between 33 and 60 per cent and has continued post-Thatcher (albeit with reduced financial incentives offered to tenants) (Garrett, 1994, p. 110; Jones and Murie, 2006). The scheme was further extended through the 1984 Housing act which shortened the period of occupancy before a tenant could buy their house and increased the maximum discount offered by councils. Between 1980 and 1987 over a million homes – '6 per cent of Britain's housing stock' – were sold (Norris, 1990, p. 68).



Over 1.3 million people brought their homes under the scheme between 1980 and 1990, and a further 2.5 million between 1990 and 2009 (Pawson and Wilcox, 2011, p. 122). This combined with restrictions on 'local authority use of their capital receipts to build new houses, in combination with the operation of the [right to buy] ... resulted in a substantial reduction in, and a residualisation of local authority housing available for rent' led to significant increases in house prices (Ford and Burrows, 1999, p. 307) as demand for housing (especially in the more prosperous South East and London regions) outstripped supply.

Such rises in house prices resulted in the unequal growth of property ownership. In 1988,

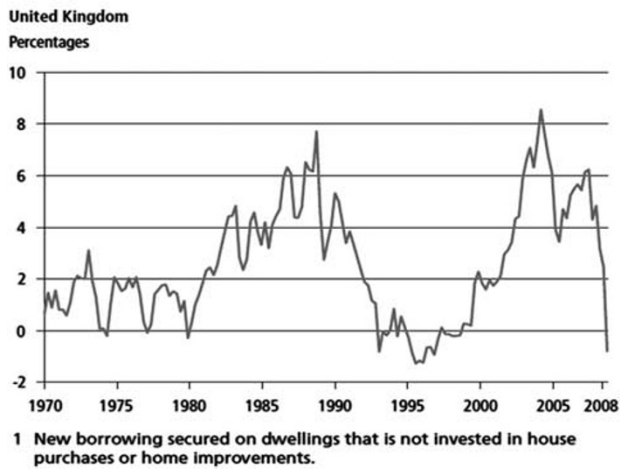
58 percent of young people in the low-to-middle income group owned a home and 14 percent rented privately. By 2008, those figures had flipped to 29 percent [owning] and 41 percent [renting privately]. This change took place in spite of a dramatic loosening of credit. (Plunkett, 2011, p. 11)

Changes to council, or public, housing impacted upon the private rental sector and promoted inequalities in society. During the 1980s the groups of people renting was largely confined to 'low income, non-family households in furnished ready-access accommodation and mainly elderly households in unfurnished accommodation, where long-term tenancies were concentrated.' The tax system further discouraged people who could afford to buy from renting (Crook and Kemp, 1996, p. 51).

The extension of home ownership presented some people with assets which, if refinanced, could provide an alternative from of income. This is important for those who experienced an 'income shock', for example those made unemployed and have little or no other liquid assets to sustain themselves with (Hurst and Stafford, 2004). However those who suffered an 'income shock' were not the only ones who could refinance, houses could be used to obtain credit which in turn could be used to finance consumption. As Figure 1 demonstrates the amount of money taken from houses and used for consumption and investment rose during 1980s and, despite a fall in the early 1990s, the upward trend continued from 1995. By 2007 the figure was significantly higher than 1980. The number of new mortgages issued further experienced two boom periods. The first in 1981–1987 and the second 1995–2003. At its peak in 2004 the number of new mortgages issued (140 000) was double the 1979 figure (Barrow, 2012). In addition to this the value of these new mortgages grew at a faster rate than wages, again increasing exposure to debt. As Ambrose (2012, original emphasis) notes;

Had the volume of mortgage lending moved up from 1980 in line with earnings, and had these practices not been adopted, total outstanding mortgage debt would have been about £200bn by 2007. In fact it was over £1000bn – i.e. £1trillion. *The enormous sum of about £800bn had been invested, or one would argue miss-invested, over this period in stimulating house prices.*

**Housing equity withdrawal<sup>1</sup> as a proportion of post-tax income**

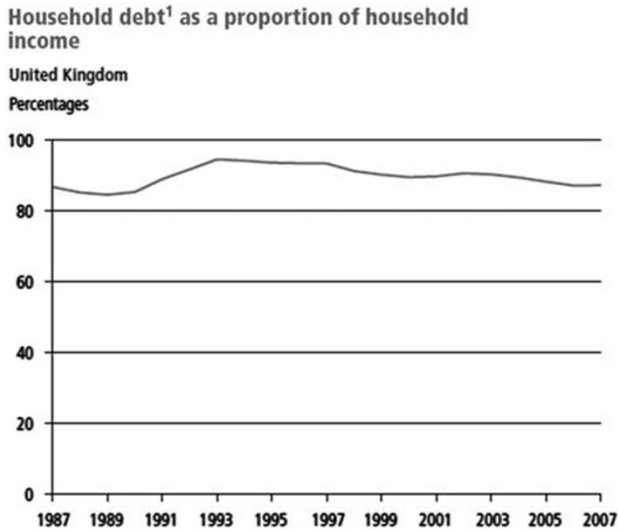


**Figure 1:** Housing equity withdrawal as a proportion of post-tax income.  
*Source:* Office for National Statistics (2009, p. 88).

Along with the extension of credit cards and other loans (both secured and unsecured) the rise in mortgages (and the value of mortgages) outstripped rises in wages. Britons (and the wider economy) became increasingly reliant upon debt. Despite a 330 per cent rise in household income the proportion of ‘total household disposable income was relatively steady over the period 1987 to 2007’, (see Figure 2). This demonstrates a consumer bubble, as debts have risen in line with household income. This implies that the rise in household income is being used to fuel consumption rather than saving.

While some view Britain’s consumer society as a long-term phenomena (Hilton, 2003) – a point I do not reject – I maintain that the 1980s saw a distinct shift in this consumer nature as profits gained from house-price fluctuations could be used to fuel consumers demand. Figure 1 not only demonstrated two clear periods of increasingly equity withdrawal, one from the mid1990s through into the early 2000s, but also one previously between 1980 and 1987. This demonstrates a longer-term trend towards house prices and perceptions of future price changes. Although the effects of the mid-1980s borrowing were relatively short lived (certainly compared to the increases from 1995), house prices (and house price rises) gained an increasing significance in the wider economy and were now linked to credit, debt and consumption.

The housing bubble crash in the early 1990s did not signal an end to the Thatcherite consensus on home ownership or mortgages. The Right to Buy scheme was amended five times between 1990 and 2004 (Jones and Murie, 2006, p. 38)



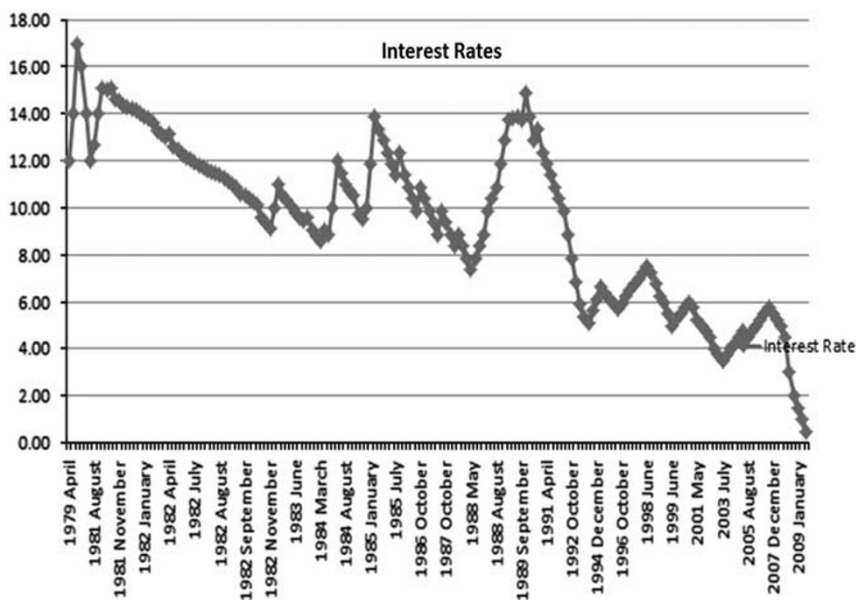
**Figure 2:** Household debt as a proportion of household income.<sup>1</sup> Includes secured and unsecured debt.  
*Source:* Office for National Statistics (2009).

helping fuel another housing bubble, between the mid 1990s and 2006. House prices, aided by historically low rates of inflation, outstripped inflation (Nationwide, 2013), (see Figure 3). This increased levels of mortgage debt, while simultaneously increasing people's dependency upon high house prices as property was their main source of wealth.

Changes in house prices were facilitated by declining interest rates (as interest rates represent the cost of borrowing money and the relative ease at which people can obtain and repay mortgages). Interest rates follow a similar pattern to equity withdrawal, whereby trends which started in the 1980s, following a short reversal, were exaggerated in the 2000s. Interest rates peaked at 17 per cent in November 1979, before steadily falling to 8.8 per cent in 1988. Despite increasing again before the end of the decade the long-term trend was downwards and by the mid-2000s (February 2003–November 2006) they averaged just over 4.3 per cent. (Bank of England, 2013), see Figure 3. These historically low interest rates along with increased consumerism encouraged and enabled house owners to re-mortgage their properties and release money from their homes.

This rise in credit was further exaggerated by new entrants in the credit market. Throughout the 1980s credit became available to a wider variety of people, in particular those on lower incomes. This in part occurred because of the cheapening of credit (Aoki *et al*, 2002; Figure 3). Buoyed by rising housing prices, people were able, and encouraged, to borrow more, as the value of people's assets were continually





**Figure 3:** Interest rates 1979–2009.  
 Source: Bank of England (2013).

increasing albeit at an unequal rate. Increases in housing wealth ‘contributed significantly to the consumer boom of the 1980s’ (Attanasio and Weber, 1994; Muellbauer and Murphy, 1997, p. 1701; see also Figure 1 and Figure 4). Money ‘released’ from housing or house price increases could further be invested, speculatively, either in property or the increasingly deregulated stock market. Notions of making ‘a quick buck’ were facilitated by the expansion of credit. Such opportunities were popularised in film – Gordon Gekko in the 1987 film *Wall Street* famously said ‘Greed – for lack of a better word – is good. Greed is right. Greed works’. Speaking following the dot.com bubble burst in 2001 Alan Greenspan (Quoted by, Folbre, 2009, pp. 1–2) spoke of ‘“an infectious greed” within the business community. It is not, he explained, “that humans have become any more greedy than in generations past. It is that the avenues to express greed had grown enormously”’.

The expansion of credit was not equal, for those on middle-to-low incomes the burden of mortgage repayments rose rather than fell during this period (Plunkett, 2011, p. 11). However there was a greater willingness, from within the banking sector, to help fund house purchases particularly at the ‘bottom end of the market’ (Boddy, 1989, p. 94), thus exposing banks and later building societies to riskier assets.

Such linkages were sustainable only in so far as house prices continued to increase. If house prices fell (as they did post 2007) people would quickly find themselves



**Figure 4:** Wealth of a selection of the British public 1970–1989.

\*Data for 1980 unavailable.

Source: Alvaredo *et al* (2013).

unable to repay their debt. Mortgage indebtedness was such that by the timing of the 1992 election, following an economic downturn, many new property owners in the South East were left in a ‘housing trap where the size of their mortgages was greater than the value of their homes. [Although] the incentives for people to sell their homes had increased, their ability to do so decreased.’ (Garrett, 1994, p. 108)

Thatcher’s reforms to the housing market, along with changes in the interest rates (which were set by governments until 1997), artificially inflated house prices. Those that did own their own home were able to use it as an asset, in a deregulated credit market, to fuel consumption. House prices rose steadily in the 1980s, though were increasingly connected to the debt and consumer bubble, once house prices began to fall wider economic problems were likely to occur.

## ‘Big Bang’ Deregulation

The Thatcher government was committed to deregulating the financial services industry and promote both competition within a deregulated economy and London’s position as a ‘major world financial centre’ (Boddy, 1989, p. 92). In 1979, the incoming Thatcher government lifted exchange controls, meaning British firms could buy foreign securities (Poser, 1988, p. 320). The government’s commitment to deregulating the financial services market was further demonstrated in 1980 when the government removed the ‘corset’ – ‘a device by which the Bank of England imposed limits on bank lending’. In 1986 the Stock Exchange was excluded from the ‘operation of the Restrictive Trade Practises Act’ (Thatcher, 1993, p. 125, p. 311). Deregulation further increased the capacity of new financial service providers to enter

markets such as the mortgages market, and in doing so gave these institutions greater powers to set their own commercial interest rates (Boddy, 1989, pp. 94–95). Such policies promoted the role of capital and granted increased powers to capital (*vis-à-vis* labour) in the economy.

The notion of a ‘Big Bang’ emerged following the passage of two pieces of legislation; the Financial Services Act and the Building Societies Act in 1986 (Barnard, 1987). This ‘Big Bang’ was described by Galletly and Ritchie (1986, p. 12) as ‘a revolution ... daily procedures which have lasted for two generations are being swept away almost overnight.’ The date of this ‘revolution’ was the 27 October 1986. It was part of the process of creating ‘popular capitalism’, what Norris (1990, p. 64) describes as ‘a new share-owning, property-owning, self-reliant Conservative working class’, further aided by the large scale-privatisation projects of Thatcher’s second term (Young, 1990, pp. 498–499).

The ‘Big Bang’ became synonymous with deregulation, and the deregulation of the British financial sector. Poser (1988, p. 319) identifies four key components of the ‘Big Bang’;

- (1) The abolition of fixed commission rates charged by members to their customers, and their replacement by negotiated rates.
- (2) The elimination of the ‘single capacity’ system, which prevented stock exchange members from acting both as brokers – that is, agents – for customers and dealers – that is, principals – for their own accounts.
- (3) The introduction of a new system for trading securities on the stock exchange.
- (4) The lifting of restrictions on exchange membership, which enable major British and foreign financial institutions to become member firms of the London Stock Exchange.

The Building Societies Act ‘ease[d] restrictions on building societies in terms of use of funds, allowing for unsecured loans and finance for land and property development’ (Boddy, 1989, p. 93). This was important as it changed the nature of, and institutions involved in, the mortgage market. Previously building societies were the major funders of loans for house purchases. Under the new act however institutions were able to diversify their portfolio this enabled building societies to hold riskier assets (Boddy, 1989, p. 100). This in turn made the investments of building societies (and later banks) riskier. Banks seeking increased profit margins increased their operations and offered mortgages to new and riskier entrants into the housing markets for the first time. This increased their exposure to the risks of mortgage defaults.

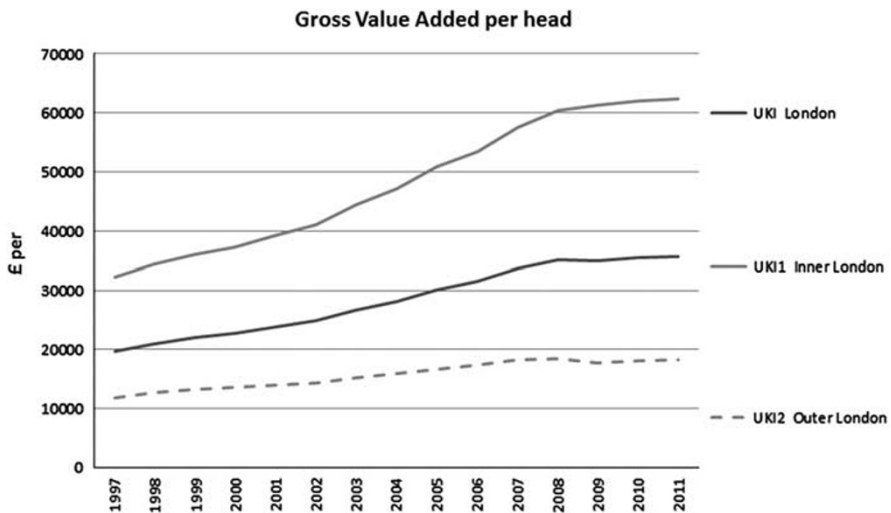
The ‘Big Bang’ had three key economic implications. First it signified and entrenched the importance of the City of London in Britain’s economy, second it offered large deregulation of the banking sector increasing its exposure to risk and third it helped integrate Britain’s economy into the neo-liberal global order.

The City of London and its success was crucial for the Thatcher government that sought to privatise industries and shift the focus of the economy away from labour in



favour of capital. Thatcher, speaking at the Lord Mayor's banquet in 1981 defined the City of London as 'a precious national asset [and warned that any] government that fails to recognise this fails to understand our national interest' (Green, 2004, p. 172). Throughout the Thatcher governments the centrality of the City of London became evident. Economic changes meant that traditional staple industries were declining in importance and increasingly Britain and her policy makers became increasingly dependent upon the City of London and finance to maintain national income and tax receipts. Britain's economic fortunes for the first time became linked with non-tangible goods, and facilitated the rise of the service sector. This led to a widely imbalanced economy with an over-reliance upon one geographical region and a particular economic sector. Pay rates in London far outstripped those in the rest of the country (Thrift and Leyshon, 1992, p. 290). As Figure 5 demonstrates the gross value per head in London rose dramatically over the period 1997–2013, and has even increased to record levels since the onset of the financial crisis. As one (albeit London) newspaper suggested 'London has never been this important to the UK economy' (Heath, 2013).

Legislative changes further helped generate notions and realisations of 'international' financial markets. Following the 'Big Bang' and loosening of restrictions on capital transfers, Britain became more intertwined in the global economy. This was part of the drive towards competitiveness the Thatcher governments pursued. In practice this meant an acceptance of a neo-liberal world order and moving away from the tripartite or corporatist state of the post-war period – a move made easier by the high profile defeats of the trade union movement in Britain and elsewhere in Europe



**Figure 5:** Gross value added per head, London 1997–2013.

Source: Office for National Statistics (2011).

(Overbeek, 1993, pp. 16–17). The ‘Big Bang’ positioned the City of London, and by extension the whole of the UK economy, firmly in the neo-liberal world economy. Along with a move towards internationalisation, the ‘Big Bang’ formed part of the government’s policies of deregulating and increased competition in the banking industry (Ennew, *et al*, 1990, p. 80). The acts were ‘crucial’ in allowing the ‘city to adapt to the highly competitive international markets’ which it operated in (Thatcher, 1993, pp. 311–312). This along with greater interconnectedness made Britain more susceptible to a global economic downturn.

The Big Bang further aided the stock market, which was becoming central to Britain’s economic fortunes. Already buoyed by newly privatised industries which were being sold by government at a discounted rate

the abolition of minimum commissions changed the economics of brokerage and market-making, making joint-provision of these functions and foreign entry inevitable. Although the total number of institutions did not increase, there was a marked rise in the number of individual members of the Stock Exchange. (Bank of England, 2010)

This further helped increase the performance of the stock market on a short-term basis. The ‘Big Bang’ ‘was assisted by and in turn further stimulated the booming bull market’. The number of equity market-makers (previously ‘dealers’) increased from 13 in 1986 to 34 just a year later (Davis, 1996, p. 433).

Such deregulation and increased competition led to banks becoming

more aggressive in the marketing and positioning of their off-balance sheet products and services. Many banks entered the securities business by acquiring stock broking and jobbing firms. Non-banking financial institutions, such as insurers, retailers and building societies, challenged the banks on their traditional balance sheet activity. (Matthews *et al*, 2007)

and, thus, increasing their exposure to risk – one key problem of the recent financial crisis. Banks and building societies, far from being passive in such regulations were

active participants, encouraged by the UK’s lax national financial regulatory regime, its low interest rates, and an insatiable quest on the part of the banks and demutualised building societies to become global players, to borrow in global money markets in order to create ever larger volumes of profitable mortgage lending.

## **Impact of Thatcher’s ‘Resolution’: The Crisis of 2007**

Thatcherism sought to fundamentally alter the nature of the British economy. The economy during the 1980s was reconfigured; weakening the power(s) of labour and



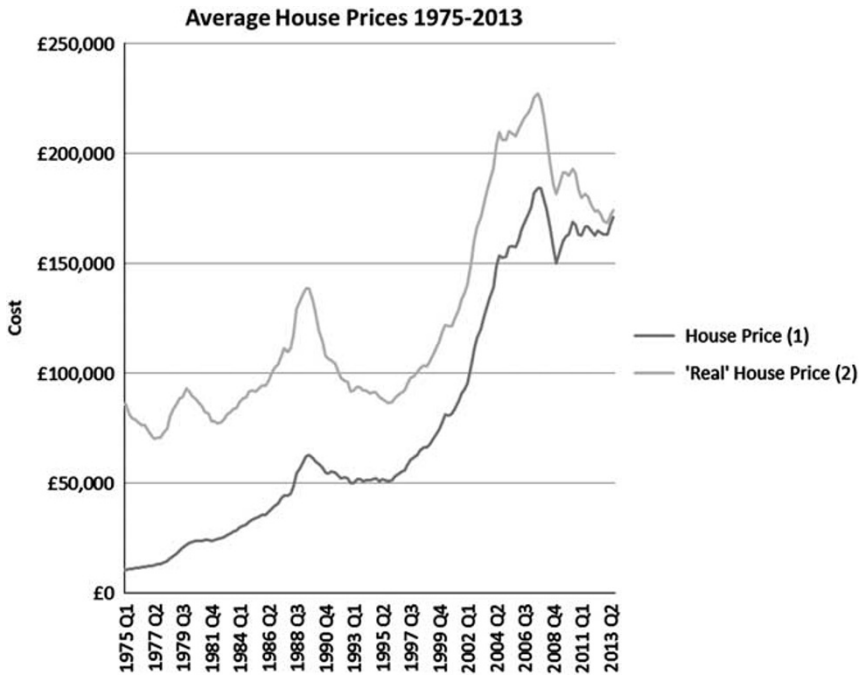
enhancing the power(s) (and owners) of capital. Gamble (2009, p. 161) notes ‘the financial growth model which underpinned the recovery from the 1970s stagflation depended on giving maximum freedom to finance to drive the pursuit of profit in all sectors of the economy’.

Such reforms led to further problems in the economy. Underlying problems developed out of the response to the crisis of the 1970s which created an inherently unstable economy. Thatcher was undoubtedly successful in weakening the powers of labour, and especially the trade unions in the 1980s while increasing the powers of capital (and the owners of capital). Capital gained power relative to labour, and the British growth model became reliant upon non-tangible goods, such as financial products. The sale of council houses helped create and inflate a housing bubble, which, alongside an easing of credit restrictions (for example, lower interest rates) and a greater willingness from consumers to use credit as a means of sustaining consumption led to a highly volatile market.

Much of the rise in share and home ownership was fuelled by short term debt and often borrowed against the assets being purchased (for example, against the home in the case of mortgages). This proved problematic as this debt binge inflated both stock and housing prices ‘far beyond their long term sustainable levels, and [made] banks seem more stable and profitable than the really [were]’ (Reinhart and Rogoff, 2009, p. xxv). Debt was used to purchase – and secured upon – an asset whose price had been inflated. This had cyclical connotations, as rises in house prices and stock market prices led to an increase in expectations, which in turned enabled a boom in consumer spending, as money could be increasingly obtained from asset purchases such as houses, or (expected) price rises (Allen and Gale, 1999, p. 13).

The process of, and drive towards, consumerism is important. Advocates of consumerism claimed it legitimised capitalism and the Thatcher governments’ wider political programme. The rise in consumption can also be linked to the rise in debt, as consumption became increasingly financed by debt. Debt could be obtained based on future predictions of economic income/prosperity. Equity withdrawal rose, on the back of rising house prices, and fuelled by short term bubbles and governmental policy, expectations of future economic successes became increasingly optimistic (Peachy, 2013; see also Figure 1). From 1980 to 1989 house prices rose at an annual average rate of over 12 per cent (see Figure 6). Figure 6 demonstrates two clear periods of house price growth, one between 1978 and 1988 encouraged by the Thatcherite policy of right to buy, and a second from 1996. Credit became easier to obtain on the back of rising asset prices, and credit cards and loans became accessible to a greater proportion of the population. Importantly this credit was obtained based on future projections, rather than guaranteed income – if the house prices fell, leaving people with ‘negative equity’, they would struggle to repay their loans (as was the case with many US-subprime mortgages in the 2000s).

Equally the institutions offering credit were less insulated than they once were; banks and building societies became more interconnected to the wider economy, and



**Figure 6:** Average house prices 1 = nominal house prices, not seasonally adjusted. 2 = House prices adjusted for inflation (RPI).  
 Source: Nationwide (2013).

financial services were increasingly connected to house prices and stock market variations. At the same time as the British economy was becoming increasingly reliant upon banks and financial institutions these institutions themselves were issuing and exposing themselves to riskier loans and debts. Furthermore changes both in Britain and abroad made the financial markets more susceptible to global pressures and shocks, which would inevitably be passed on to consumers of credit.

The interconnectedness of the financial sector and its weakness is possibly best demonstrated in the case of Northern Rock. Northern Rock became a victim of the crisis not because of its lending practises but because of the interconnectedness of the globalised economy, and the decisions of other banks. A rise in the LIBOR rate, in early September, along with an announcement, 13 September 2007, that Northern Rock sought (and received) emergency funding from the Bank of England led to the first run on a British bank for 150 years (*BBC News*, 2008). The problem faced by Northern Rock was of increases in interest rates, which occurred because of the actions of other financial institutions, and meant that Northern Rock was no longer



able to rely upon the short-term loans market to ‘roll over’ or renew its debt (as this relied upon a liquid housing market) (Hay, 2011).

Banking reforms had led Britain during the period 1980–2007 to become increasingly globalised (Miles, 2006). Such changes were not natural or predetermined shifts, but represented clear policy goals of the Thatcher – and later New Labour – administrations. In particular the economies of Britain and the United States became increasingly connected. A number of US financial firms (Merrill Lynch, Goldman Sachs, JP Morgan, Credit Suisse and First Boston) took advantage of the ‘Big Bang’ deregulation to establish themselves in London. This linked the fortunes of the British and American markets. Such was the foreign investment that by the turn of the century London had become ‘dominated by overseas institutions’ (Hamnett, 2003, p. 36). This interconnectedness ensured that British banks were no longer solely susceptible to risks within the domestic economy but were now exposed to the risks taken by American banks too. Eichengreen *et al* (2012) demonstrate how banks became interconnected before 2007. The interconnectedness of banks was not a product of the crisis – be it a global crisis or a British one – but stemmed from the policies of American but also British policy makers in the 1980s. Both the Thatcher and Regan administrations committed themselves to global neo-liberalism and pursued the creation of a new growth model away from the Keynesianism one that was established after the Second World War (King and Wood, 1999).

These policies stemmed from the narrative and responses of the Thatcher government to the trade union crisis in the 1970s. The ‘Thatcher revolution’ and its subsequent acceptance in a post-Thatcherite settlement further fuelled a debt crisis, raised house prices, generated and extended inequalities in society, helped inflate a stock market bubble, promoted what Strange (1997) labels ‘casino capitalism’ and led to an increased dependence upon banks. Banks became increasingly interdependent, but also riskier as they were now dependent upon a wider range of creditors, including those less likely to be able to repay loans (Thrift and Leyshon, 1988). Domestically there also existed a greater reliance upon debtors; mortgages were linked to the stock exchange and pensions to international financial transactions. In turn this meant an increased reliance upon banks and the stock market and helped to generate notions of ‘too big to fail’ which would come to characterise the state’s involvement in the crisis in 2007.

## **Crisis Management in the Wake of the 2007 Crisis: Repeating the Mistakes of the Past?**

The previous section has demonstrated how the Thatcherite reforms paved the way for the crisis of 2007. Many other authors (see for example Gamble, 2009; Hay, 2011; Blyth, 2013) have debated the effects of the crisis, and I do not wish to repeat these arguments here. Instead I wish to; using the evidence presented above, ask how



likely is a sustainable recovery given current government economic policy or if such policies are simply repeating the mistakes of the past.

The fall in house prices since the onset of the financial crisis in 2007 has left many people facing the problem of negative equity. Akin to this is the growing number of people unable to afford to join the lowest rungs of the property market or save enough to put down a deposit on a house. In order to try and overcome the latter of these problems the government has introduced a new help to buy scheme easing the flow of credit. Furthermore, despite levelling blame at the banking sector the government (along with its New Labour predecessor) has failed to move away from the existing growth model or economic paradigm. The model of banking which became prevalent in the 1980s (especially after the reforms of 1986) has been largely defended. These two policies appear extremely reminiscent of the 1980s and need to be examined in order to ascertain how sustainable the post financial crisis recovery/new growth model actually is.

Despite the banking sector initially being blamed for the financial crisis, the problem has since been rebranded as one of national debt by politicians pursuing austerity policies. In this discourse the City of London's political and economic importance is demonstrated as far from being 'reformed' or marginalised, it has been incorporated into debates surrounding Britain's economic recovery (Sibun, 2010; *BBC News*, 2011). The regulatory structures of the banking system have been largely maintained throughout the crisis. The financial system – what Hay (2011) defines as the Anglo-American growth model – has not undergone widespread structural change. Since the 1980s the banking sector has become important not only with the British economy but also within the political sphere (Hindmoor & McConnell, 2013, p. 553). Linked to this is the narrative of 'too big to fail' which was used to defend the bailouts of banks and financial institutions. This narrative argued that if no government support came forward Britain would face widespread economic problems which would ultimately be more costly than bailing out the institutions in the first instance.

The problem of this logic was noted by Mervyn King, who in 2009 (Quoted by Goldstein and Veron, 2011) said that 'if some banks are thought to be too big to fail, then ... they are too big .... Privately owned and managed institutions that are too big to fail sit oddly with a market economy.' However such lessons may not have been heeded by policymakers. As Crouch (2011) notes politicians see the rebuilding of the deregulated model as advantageous. Crouch (2011, p. 123) asks;

how long can one expect the boundaries erected between safe mass banks and risky investment banks to last, when those boundaries are preventing bankers and politicians from reaping the benefits they came to understand in the 1990s and 2000s?

Furthermore in the wake of an EU challenge the coalition government has sought to defend bankers' bonuses – despite such bonuses as being increasingly scrutinised,



and blamed for the recklessness they encouraged following the bailouts of 2007/2008 payments (Jones & Schomberg, 2013) (*BBC News*, 2013a).

Similar parallels can be drawing in the housing market, following the government's Help to Buy Scheme warnings have come from both economists and politicians alike (*BBC News*, 2013b). According to the Office for National Statistics (2013) house prices in August 2013 reached their highest level, 'surpass[ing] its previous peak in January 2008 (185.5) by 0.3 per cent'. House prices rose 7.7 per cent year on year in November 2013, and 11.7 per cent by the same measure in July 2014. This growth however has been unequal with most of the price increases coming in London and the South East. The growth rate in London as of July 2014 was 19.1 per cent four times that of Northern Ireland (4.5 per cent) and almost four times that of Yorkshire and the Humber (5 per cent). There have also been concerns over an overheating housing market leading the Bank of England to refocus 'the Funding for Lending scheme (FLS) on business, not mortgage borrowers' (*BBC News*, 2013c, 2014). As in the 1980s housing reforms stem from a primarily conservative desire for private property ownership and the extension of property rights, adopted by the coalition government.

In both cases (housing and bank regulation) the government's plans may, as in the 1980s, create a largely unsustainable bubble in house (or asset) prices while further encouraging a consumer bubble built upon debt and (optimistic) future predictions of price increases. To do so would be to repeat the mistakes of the 1980s, risking further economic problems, and to ignore the lessons of the recent financial crisis. In short, to achieve a sustainable recovery a differential approach, what others have labelled a 'new paradigm' (Hodson and Mabbett, 2008; Hay, 2011), one which notes the lessons of the 1980s, is required.

## Conclusions

The Thatcherite reforms while 'alleviating' the crisis of the 1970s and 1980s paved the way for a new crisis. The reforms increased the power of capital (or the owners of capital) over labour. Capital, banks and the wider financial sector became increasingly deregulated and the government undertook a deliberate policy to weaken labour's ability to cause, or generate, a crisis akin to the one for which they were blamed in the 1970s. Building societies and banks took on increasingly riskier assets, helped facilitate an expansion of the mortgage market and became increasingly interconnected. Both house and share prices ballooned, aided by an expansion of credit to fuel speculative bubbles and historically low interest rates.

Such changes failed to prevent future crises from occurring, and in many ways the Thatcher reforms laid the foundations for the next crisis, that of 2007. The visible effects of the 1980s may only have occurred, on a macro-economic scale, in 2007 but the seeds were laid much earlier. The relationship between capital and labour, and the

desire of the Thatcher governments (and their successors) to promote capital is pivotal to understanding the crisis that unfolded in the late 2000s. While it may be argued such changes were unforeseen, or accidental, the policies and the policy drives implemented by the Thatcher governments represented a clear determination to alter the labour/capital relationship in Britain and are important in relation to the crisis of 2007.

I have demonstrated how the financial crisis of 2007 has its foundations in the 1980s. By examining two specific policies, the 'Right to Buy' housing scheme and the 'Big Bang' deregulation of the financial services industry I have traced significant changes in recent British economic history and demonstrated that the continued acceptance of the Thatcherite reforms led to banks becoming increasingly important and powerful in the economy. Such changes I contend should be viewed as a response to the crisis of the 1970s and 1980s and helped set the stage for the financial crisis of 2007.

More research is required to assess the impact of the governments' current economic plans, not least because of the short time frame between the latest extensions of the housing scheme. Whilst this article cannot provide a definitive account of the coalition's policies on housing or banking (or the coalition's wider macro-economic policies/management) evidence presented here suggests that the resolution of the previous crisis led to an unbalanced and unstable economy and if the policies of the 1980s are repeated on a macro-economic scale then the mistakes of the 1980s may again repeat themselves. This article suggests that the responses to the financial crisis pose striking similarities to the crisis resolution of the 1980s, in particular policies of inflating the housing market is once again returning to the forefront of government policy. Such policies through creating and financing both a housing and consumer bubble laid the foundations for the financial crash of 2007. The same growth model that caused the crisis in 2007 has not been radically altered; instead the coalition government seems content to re-impose much of the flawed economics, such as the reliance on property bubbles and capital and the owners of capital to create and sustain economic growth.

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