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Capitalism and Post-Keynesian Economics: Some Critical Observations.

Introduction

No positive economic doctrine has been able until now to escape from the trap of being valid only under very specific conditions, so special as not to be replicated even minimally in actual historical experience. Consider the two fundamental approaches of the 19th century: the Marxian and the Neoclassical one. They both attempt to tell a story about the long-term behaviour of the system. The former tries to identify objective laws of motion, the latter some kind of immanent behaviour to be taken as a normative reference for a real system. They both fail encountering similar analytical problems. In particular the long-term validity of both approaches depends heavily on the homogeneous nature of the economy they depict.¹ Marx's long term theory of capitalist accumulation is not free from the scourge of homogeneity either (see Appendix). Indeed I believe that there are in Marx two distinct and non-compatible macroeconomic theories. The first, of a Ricardian nature, is to be found in Volume One of *Capital* and culminates in the well known chapter (25) on the Reserve Army of Labour. Its essential elements are reproduced in *Wage Price and Profit*, a fact that has some importance. *Wage Price and Profit* is Marx's speech at the founding meeting of the First International. It can, therefore, be viewed as expressing his core thoughts when economic statements had to be stripped down to their essential points. The second approach is contained in Volume Two of *Capital*, largely put together by Engels, which gave rise to the most far reaching set of economic debates within the Second International. The centrepiece of Volume Two are the famous schemes of reproduction leading to the discussion of disproportionalities, of the non-continuous character of trade cycles – whereas the cycle outlined in chapter 25 of Volume One and in *Wage Price and Profit* is continuous and, without a rising organic composition of capital, would generate a

¹ As a result of a set of theorems by Debreu, Sonnenschein and Mantel we now know that a microeconomic text book ought to be closed and shelved at the very first attempt to present a general many agents-multi goods barter equilibrium, let alone a supply and demand diagram. In other words, it is impossible to establish that net demand functions are systematically related to prices in an inverse manner. The issue was intuitively understood by Hicks already in 1939 in *Value and Capital*, otherwise he would not have stated that the prerequisite for attaining his flex-price temporary equilibrium is the dominance of the substitution over the income effect. Debreu-Sonnenschein and Mantel showed that the income effect may indeed prevail so that the fundamental microeconomic price adjustment story comes to an end as soon as it is stated. This point has been lucidly made by **Bernard Guerrien** in his *Concurrence, flexibilité et stabilité*, Paris: Economica, 1989, and by **Steve Keen** in *Debunking Economics*, Sydney: Pluto Press, 2001. In the case of Ricardo and Marx the homogeneous nature of the system stems from the attempt to extend the clear-cut results obtained in a corn economy to a more complex system still operating under competition.

limit cycle à la Goodwin – of breakdowns in the accumulation process. In concrete terms non-continuity means that once a breakdown occurs we do not know how the system can get out of it. Like strategists we could map out all sorts of scenarios - and to do that we would need concrete knowledge about politics, classes and history, something which to day is alien to economists of virtually all persuasions - but we cannot claim to have a reliable theory of long term growth and cycle.

In other words, if one is a Neoclassical economist and follows the Blanchard-Fischer approach to macroeconomics, he/she must, as a matter of faith, take the Ramsey parable to be true. That is, our colleague would have to dogmatically assert that a society based on production and money and profits behaves, in the end, like a farmer whose problem is to decide how many eggs to eat and how many to leave for further hatching in relation to a precisely expected level of consumption (in terms of utility) – for herself/himself or for the children – at a precise date in the future. If, by contrast, our friend is a Classical economist he/she would have to believe that whatever amount of corn is left unconsumed will be automatically invested. Alternatively he or she could state that whenever the amount of surplus value rises the rate of accumulation and the rate of profit will rise as well, unless the organic composition increases more than proportionately. Yet once we move away from Ramsey's farmer or from the Ricardian corn model, or from Marx's competitive uniform organic composition of capital model, we simply do not know and cannot know what will happen overtime unless the system is already in a steady state. Even in the simplest of all possible cases - a two sector fixed coefficients model – we are no longer able to determine how and whether the economy as a whole manages to traverse from one state to the next².

2. Kalecki in context: The Second International, the Comintern, and the issue of accumulation and crisis

The participants in the debate of the Second International understood very well, also in practical terms, the issue of heterogeneity and its implications for discontinuity³. They never assumed that machines could become, unlike corn, consumption goods ipso facto. They came very close to grasp the fact that if, for any reason, more corn is saved – say because the ratio of unpaid labour time has risen in the corn sector as well as in the sector producing tractors for itself and for the corn sector – it will not lead, per se, to a higher rate of capital accumulation for the system as a whole. It may, indeed, cause a fall in accumulation through the formation of unused capacity in the corn sector which will spread to the capital goods sector via a reduction in the demand for tractors. Furthermore it was quite clear to the participants, even if they belonged to different tendencies, that the creation of a complex capital goods sector

² See Joseph Halevi and Peter Kriesler “Marx or Hicks? Structural proportions and crisis: the transition from the First to the Third Volume of *Capital*”, in **Marxian economics : a reappraisal : essays on volume III of "Capital" / edited by Riccardo Bellofiore**. Publisher New York : St. Martin's Press, 1998, Vol 2.

³ Still unsurpassed is the discussion of that debate by Paul Sweezy in his celebrated *Theory of Capitalist Development*, New York : Monthly Review Press, 1968; originally published in 1942. The best collection of most of the original texts is due to Lucio Colletti and Claudio Napoleoni (eds.), *Il futuro del capitalismo: crollo o sviluppo? (The Future of Capitalism: Breakdown or Growth?)*, Bari: Laterza, 1970.

was linked to the emergence of large scale industries and signalled a new stage in the expansion of the forces of production. However given the scientific culture of the period, especially in Germany and Russia, they tended to search for absolute or definitive conditions for breakdowns or sustainability, eschewing history altogether. Even the question of monopolies and cartels was seen in those absolute terms condensed in the well known Hilferding-Schumpeter position according to which cartels generate stability once the fight over markets has subsided⁴.

To my mind the works of Michal Kalecki and, over the years, of the editors of *Monthly Review* (Paul Sweezy, Paul Baran, Harry Magdoff) bring to the fore what was absent in the debates of the Second International. This is done by putting the issue of capacity utilisation at the centre of capitalism's contradictions something that the people of the Second International failed to recognise. The question is not so much that of acknowledging that the economy does not automatically attain full employment and therefore that something must be done about it. In the Kalecki-MR approach the main concern is to identify the forces governing the capitalist system prior to, and independently of, policy considerations. This aspect will be seen more clearly in the third section of the paper. Here I will give some examples concerning Kalecki's analysis during the interwar years⁵.

In the interwar period, certainly until the first half of the 1930s, two positions dominated within the European Socialist parties and within the Third International. One was that cartels produced stability, a position rather common among the Socialdemocracies⁶. Another, officially endorsed by the Comintern until the Dimitrov-Togliatti-Thorez Front Populaire strategy, viewed in the very depth of crisis its solution. Kalecki challenged both. In relation to the Socialdemocratic position he argued that, concretely, capitalism is made of two components: a cartelised sector displaying constant profit margins and a competitive one where profit margins fluctuate with prices thereby rising in a boom and falling in a recession. Cartels compete not through prices but via the building up of productive capacity so that during a boom they engage in an investment race leading to excess capacity thus contributing to the demise of the boom itself. Given the stability of profit margins, the slowdown in demand relatively to capacity will be met by a reduction in output and employment engendering yet more unused capacity. The

⁴ Joseph Schumpeter, "The Instability of Capitalism", *The Economic Journal*, Vol. 38, No. 151. (Sep., 1928), pp. 361-386.

⁵ A more elaborate discussion of the consistency in which Kalecki modified some of his views in the post 1945 period is in Joseph Halevi, "Kalecki and Modern Capitalism", *Monthly Review*, June 1992.

⁶ German Socialdemocracy never abandoned that view and this is why it is technocratic but not Keynesian. The advent to power of the SPD in 1969 opened the way to the deflationary role taken by the Bundesbank. It is strange that so many post-keynesians from Kaldor to Cornwall were so taken by the German system of industrial relations precisely when the Bundesrepublik used that system in order to enforce a massive change in the distribution of income away from wages and embark onto a neomercantilist policy of net surpluses which brought no Kaldorian cumulative causation to the rest of Europe. Notice that Kaldor believed that export oriented growth would generate a wider cumulative causation because the exporting countries would need imports linked to their exports. Now it is true that whenever South Korean or Taiwanese exports accelerated, Japanese exports expanded as well. But this was due to a precise hierarchical relation governed by Japan's monopoly capital. Hardly any industry or service in East Asia can do without Japanese industrial inputs. There is no magical cumulative causation in this.

formation of unemployment in the cartelised sector causes a fall in the demand for consumption goods, whose industries are viewed as belonging to the competitive segment of the economy. Hence their prices and in their profit margins will fall as well. It follows that the output of the competitive sector will not decline as much as that in the cartelised industries. Contrary to the Socialdemocratic and the Hilferding-Schumpeter positions, the economy with a cartelised segment will show greater fluctuations than a competitive system⁷.

Instead of embodying a rationalism making it the forerunner of a planned society, a cartel based economy displays great difficulties in breaking out of the impasse of the crisis. It is at this point that we can bring in Kalecki's critique of the Comintern position, expressed at the time by Eugene Varga in February 1932 in an article in the *Internationale Presse Korrespondenz*. For Varga the fall in wages caused by the depression would reduce the cost of production thereby lifting the rate of surplus value⁸. Kalecki argued instead that if prices fell as much as wages did, nothing would really change, if, by contrast, money wages fell more than prices the likely result would be the accumulation of unsold inventories in the consumption goods sector. Finally, if the fall in total profit was caused by a fall in output greater than the fall in prices – as was the case in the industrial sectors at the onset of the Great Depression – the value of output per unit of capital would decline actually lowering the rate of profit⁹. Quite appropriately Kalecki never attached policy considerations to his analysis but did outline the scenario that he considered most likely. Given the inability of highly concentrated economies to sort themselves out only a war time boom could do the trick.

The idea that the capitalist economy requires, in Kalecki's words, a "financial trick" to break out of a tendentially static position, is maintained during the post 1945 period. Here too, however, not much significance is assigned to full employment policies. The high level of employment is rather ascribed to the prerogatives of the capitalist groups among which armament expenditures figure prominently. The question for Kalecki becomes whether the system can be subjected to a crucial reform¹⁰. This will be discussed in a subsequent section.

⁷ See Michal Kalecki, "The Influence of Cartelization on the Business Cycle", in **Collected works of Michal Kalecki / edited by Jerzy Osiatynski ; translated by Chester Adam Kisiel**. *Publisher* Oxford : Clarendon, 1990-1997, Vol. 1 (Part 2). Originally published in 1932 in the Polish Journal *Socialist Review*.

⁸ As if history did not matter, this is exactly what the late David Gordon has maintained regarding the possible exit of the US economy from the crisis of the 1970s. The same approach has been taken recently by Duménil and Lévy in their study on the long run behaviour of the rate of profit. See Appendix.

⁹ Michal Kalecki, "Is a 'Capitalist' Overcoming of the Crisis Possible?" in **Collected works of Michal Kalecki / edited by Jerzy Osiatynski ; translated by Chester Adam Kisiel**. *Publisher* Oxford : Clarendon, 1990-1997, Vol. 1 (Part 2). It should be noticed that Kalecki's advantage over Varga lies in that he always thinks on monetary terms and prices are money prices not labour values (i.e. real prices) as implicitly postulated by Varga.

¹⁰ Michal Kalecki, Tadeusz Kowalik, "Observations on the 'Crucial Reform'" in **Collected works of Michal Kalecki**. Volume 2. Capitalism: Economic dynamics. Kalecki, Michal, Edited by Jerzy Osiatynski. Translated by Chester Adam Kisiel Oxford; New York; Toronto and Melbourne: Oxford University Press, Clarendon Press. p 467-76. 1991. Previously Published: 1971.

2 Is there a Post Keynesian Dialectical Conception of Capitalism? NO!

Post Keynesians are great believers in economic policies regardless of the evolution of power relations operating in contemporary capitalism. In other words many of present day Post-Keynesians would suggest and propose what they deem to be rational policies (for full employment) without studying first the 'laws of motion' of the economy; ie. the tendencies, the social and class configurations, the coagulation and the direction of capitalist interests etc.

The best way to approach the question is to look at the founder of both theoretical and applied Post-Keynesianism: Nicholas Kaldor. But which Kaldor?

There is a pre-war Kaldor less convinced of the self propelling capacity of capitalism. This shows up in his beautiful December 1938 *Economic Journal* paper called "Stability and Full Employment". Except for Maurice Dobb, who has alerted me to its importance through one of his papers, few have appreciated it¹¹. The economy has the two traditional Marxian sectors, but both have unused capacity. The transition from one short period to the next depends upon the speed at which relative rates of utilisation grow/contract during a given short period. Perfectly consistent with Kalecki when the latter argues that in socialist economy a fall in investment need not lead to unemployment but simply to an expansion of employment in the consumption goods sector relative to that of the capital goods sector (see the next section). Kaldor '38 paper is better than Harrod's famous 1939 one since it does not entail cycles along trend lines. In Kaldor '38 the structure is compatible with the Kaleckian emphasis on sectors and effective demand. It even goes beyond that since it moves towards an issue, which has been part of both American institutionalism and German-Russian Marxism: the relation between oligopolistic power and the heavy industry sectors.

I think that it is the best paper on disproportionality cum effective demand crisis. It forcefully introduces the notion that in a developed industrialised economy the stock of capital - at, and even before, full capacity - can employ the whole of the labour force. A developed capitalist economy has a developed capital goods sector, which can potentially generate a rate of accumulation higher than that allowed by the full utilisation of machinery and of labour. Knocking out old equipment via technical progress will not solve the problem unless by chance the reduced employment capacity of the new equipment turns out to be in the aggregate equal to the number of people released by scrapping older equipment. In general therefore unused capacity will make its appearance and with it the recession in the demand for investment good. Kaldor does consider the possibility of changing the distribution of income not by automatic means, such as price flexibility, but rather through direct state intervention. The 1938 paper is very close to the well known Kalecki 1968 *Economic Journal* essay where, for a certain level of capital stock and a certain level of the degree of monopoly, the economy can fall into the trap of chronic unused capacity even in the presence of significant technical progress. In the Kalecki paper the degree of monopoly is represented by the share of profits over

¹¹ I think it is one of Kaldor's least cited essays.

national income. In Kaldor's 1938 essay the degree of monopoly emerges as a structural relation between the investment and the consumption goods sectors. When this connection is understood both papers tell the same story: left to its own devices the capitalist economy is likely to get stuck in a state of stagnation since¹²:

As investment activity continues at a high level, excess capacity of equipment is bound to make its appearance. [new paragraph] Once redundant capacity appears, it will be almost impossible to maintain activity undiminished, unless State investment activity is extended so wide as to replace private investment.

The structural picture disappears altogether in Kaldor the Post-Keynesian, but not from Kalecki and Sweezy¹³. In the first 1956 paper the economy is assumed at full employment, investment is given exogenously and the saving ratio always adjusts, via income distribution, to keep the system at full employment¹⁴. Methodologically the problem with Kaldor is that he often tried to obtain general trends from particular situations. In 1938 he believed that the industrial system was stuck, in 1956 he thought capitalism could naturally expand on a full employment path. This aspect emerges very well in his two-part paper on economic growth and inflation published in *Economica* in 1959. He says openly that unemployment in the history of capitalism was small stuff, hovering around 5%, with only the Great Depression being an exception. To quote him in full¹⁵:

[I]n the history of advanced capitalist societies periods of severe unemployment were exceptional and not the rule; a part from periods of acute depression, unemployment did not appear to exceed a few per cent. on the average since the second half of the nineteenth century (In the forty years, 1881-1920, in the U.K. it averaged less than 5 per cent., including both boom and depression years). As the actual level of employment averaged 95% per cent. of the full employment level,

¹² Nicholas Kaldor. "Stability and Full Employment", *The Economic Journal*, Vol. 48, no. 192 (December, 1938), p. 653.

¹³ From a non Marxian, but quite structural, perspective - although couched in Cassellian terms - a good antidote to Kaldor's 1956 is the paper by Masao Fukuoka, "Full Employment with Constant Coefficients of Production", *Quarterly Journal of Economics*, Vol. 69, no. 1 (February, 1955).

¹⁴ The first 1956 paper by Kaldor is the well known "Alternative Theories of Distribution", *Review of Economic Studies*, Vol. 23, No. 2, 1956, pp. 83-100. There also a second essay based on a lecture given at Beijing University where, like the *Economica* 1959 articles, the political economy of the theory presented in the *RES* 1956 paper is fully spelled out. Here he even tried to make his approach intelligible in terms of the labour theory of value given the location of the lecture. Unlike Kalecki and Sweezy Kaldor does not see the exogenous determination of investment as a critical factor in the instability of capitalism's economic forces. If, he argues, capitalists attempt to fix the level of investment and of profits at 50% of the working time bestowed on production, but the cost of the social reproduction of the working class - the value of variable capital - is 60% of the amount of time spent on production, then profits will be brought down to 40%. Yet, if the socially necessary amount of time for the reproduction of the working class is 40% and capitalists still fix the share of profits at 50%, the remaining 10% will be absorbed by the rise in wages above the requirements of social reproduction. Nicholas Kaldor. "Capitalist Evolution in the Light of Keynesian Economics", in **Essays on economic stability and growth/Nicholas Kaldor**, London: Duckworth, 1960, pp. 243-58.

¹⁵ The set of quotations is taken from Nicholas Kaldor, "Economic Growth and the Problem of Inflation", in **Essays on economic policy I/Nicholas Kaldor**, New York: Holmes & Meier, 1980, pp.169-70. Originally published in *Economica* August 1959.

this is unlikely to have been a mere coincidence; it strongly suggest that forces must have been at work which operated on the relationship between effective demand and supply, or between the propensity to invest and to save, in such a way as to yield an equilibrium level of employment that was fairly close, if not equal to, the full employment level.

The Keynesian explanation of the historical tendency of the capitalist system to approach full employment is to be found in the fact that:

[I]n a competitive society (I ought to say a *fairly* competitive society – I do not mean perfect competition) variations in the strength of demand cause variations in the level of prices in relation to costs; these variations in turn have a powerful influence on the community's propensity to save or to consume, and thereby adjust the level of effective demand so as to make it coincide with the available supply, as determined by the resources available.

The inescapable conclusion of Kaldor's reasoning is:

The very fact that prices rise or fall under the influence of demand creates an automatic tendency towards full employment, at any rate within certain boundaries.

Thus capitalism naturally tends to full employment (which must be interpreted as a statement about the essentially crisis free nature of capitalism), provided the income distribution adjustment is allowed to work itself out. In the short run some kind of Keynesian policies will be needed but the system will be essentially governed by price flexibility relatively to wage costs. If wages increase too much prices will rise cutting them back to the level where the predetermined level of investment is compatible with a full employment distribution of income between wages and profits. By contrast if accumulation of the single product output were to rise too fast prices would fall relatively to wages raising the share of wages to the position required to attain full employment¹⁶. In this context the issue of inflation acquires relevance because if wage earners do not allow their wages to be cut by price increases when they grow too fast, the natural function of prices in adjusting the distribution of income in relation to full employment would be derailed.

Already during Kaldor's times there were people who were arguing that there was no automaticity in the high levels of employment attained by capitalism: Sweezy, Kalecki, and to some extent also Galbraith. Even before the seminal Baran-Sweezy book *Monopoly Capital* there existed publications pointing to the US dependence upon armament expenditure¹⁷. Moreover others like Triffin were pointing at the

¹⁶ The story no longer works if many sectors or many firms are considered. G.C. Harcourt, "A critique of Mr Kaldor's model of income distribution and economic growth", *Australian Economic Papers*, Vol. 2, no.1, June 1963, pp. 20-36; Joseph Halevi, "*Capital and Growth* : Its Relevance as a Critique of Neoclassical and Classical Economic Theories", *Indian Journal of Applied Economics - Special Issue in the Respectful Memory of John Hicks*, Vol. 7, No. 4, October-December, pp. 79-98.

¹⁷ **The U.S. economy in the 1950s/ Harold Vatter**, New York: Norton, 1963.

strange nature of the international financial system based on the dollar standard arguing that it could not last for long. Thus from the point of view of explaining the behaviour of capitalism Kaldor's post 1956 approach is irrelevant. Harrod was more aware of the situation with his book on the dollar crisis.

There is finally a third Kaldor appearing during the 1970s and culminating in his Italian Mattioli lectures published only a few years ago¹⁸. It is clear from the texts that he realised that his beloved Socialdemocratic corporatist paradigm was vanishing but he did not probe deeply into the reasons of the end of the long boom. The social transformations of capitalism never appear since he constantly refused to treat the capitalist economy as a power system. In fact he never refers to oligopolies as a systemic force. He sees full employment growth to be perturbed by three forces: a growth in wages higher than productivity which fuels inflation, an asymmetry between raw material prices and finished products fuelling both inflation and recession, and the irrational force of monetarist policies. But even in the post 1975 period where he seemed to pay more attention to the issue of intersectoral balances, he remained faithful to his 1956 growth and distribution views which, in my opinion, have been dictated entirely by his Socialdemocratic beliefs. In fact, if the conflict between the producers of raw materials and of manufactured commodities could be regulated by means a buffer-stock based international currency and if wages could be disciplined relative to productivity, the smoothness of the adjustment process would be guaranteed.¹⁹ Kaldor can be considered as the most systematic theoriser of what John Cornwall called *democratic capitalism*. A more extreme version of this approach is that represented by Sidney Weintraub for whom the fixity of the mark up was a 'fact' so that wage increases above the rate of growth of productivity could only cause inflation²⁰.

3 Kalecki and Sweezy : a different conception

For the post war period Michal Kalecki and Paul Sweezy provided us with a substantially different picture of capitalist's dynamics, indeed much closer to the 1938 paper by Kaldor²¹. The level of profits is determined by the level of investment, which, for any given distribution of income, will determine the level of output and employment. Hence, in Kalecki's words:²²

¹⁸ **Causes of growth and stagnation in the world economy / Nicholas Kaldor.** *Publisher* New York : Cambridge University Press, 1996.

¹⁹ In the end this is the view held by most Post-Keynesians also by those who take a Kaleckian perspective on mark-up pricing: **Economic breakdown & recovery : theory and policy / John Cornwall ; with a foreword by David Colander.** *Publisher* Armonk, N.Y. : M.E. Sharpe, c1994

²⁰ **General theory of the price level, output, income distribution, and economic growth / Sidney Weintraub.** *Publisher* Philadelphia : Chilton Co., Book Division, 1959.

²¹ Michal Kalecki "Observations on the Theory of Growth", *Economic Journal*, March 1962. Paul Sweezy, "A Crucial Difference Between Capitalism and Socialism", in **Past and Present/ Paul Sweezy.** *Publisher* New York : Monthly Review Press 1953. Reprinted in **Marx and Modern Economics/David Hrowitz ed.** *Publisher* New York: Monthly Review Press 1968.

²² Michal Kalecki "Observations on the Theory of Growth", pp.139-140.

When investment reaches its top level during the boom the following situation arises. Profits and national income, whose changes are directly related to those of investment, cease to grow as well, but capital equipment continues to expand because net investment is positive. The increase in productive capacity is thus not matched by the rise in effective demand. As a result investment declines, and this causes in turn a fall in profits and national income.

By contrast in a non capitalist framework it is possible to conceive a situation where the downward cumulative causation is avoided because:

The changes in the national income would not be tied to those of investment, but would follow the changes in productive capacity. If investment remained constant while the stock of fixed capital expanded prices would be reduced or wages raised. In this way the demand for consumption goods would increase in accordance with the expansion of the stock of capital.

This is, in Kalecki's contribution, the historically specific nature of the relation between profits and production in advanced capitalism. Kalecki viewed capitalism as a historically contradictory system. Economically because - to approximately cite him - the tragedy of investment is that it generates the crisis because it is useful. As expenditure it adds to profits and as new fixed capital it adds to capacity which clashes with profitability unless demand is propped up. The propping up of demand has to be consistent with profits. But if the propping up of demand turns out to be successful, full employment will weaken capitalists' power who, therefore, will retreat from full employment and revert back to sound finance policies. According to Kalecki during the 1950s and 1960s capitalism implemented a crucial reform through a financial trick based on budgetary policies and related armament spending. However the crucial reform was by no means a permanent situation because it was based upon a persistent arms race and actual wars.

A similar view had been developed much earlier by Paul Sweezy in the essay published in the *Present as History*. Sweezy used Marx's characterization of the accumulation process in terms of two sectors to show that upon the completion of industrialization an economy necessarily attains a stage of maturity. Under these conditions the endogenous capacity for the further expansion of investment will weaken since there is plenty of capital stock around²³. Can a solution to stagnation be found within the institutional framework of capitalism? The answer given by Sweezy constitutes a critique of Kaldor's Post-Keynesian theory of distribution before it even appeared. It is indeed a critique of *democratic capitalism* and of the possibility of a lasting crucial reform.

²³ Like Kaldor in 1938, Sweezy rejects the view that the solution can be found in an ever expanding creation of new economy industries: "For example, new industries generally produce an effect akin to that of industrialization, and if they are sufficiently numerous and important they may keep the system going at or near full capacity. But in each case the effects are bound to wear off sooner or later. The tendency to collapse is always there in an industrialized capitalist society." (Sweezy, in David Horowitz ed. *Marx and Modern Economics*, New York: Monthly Review Press, pp. 320-1).

In terms of our two-department schema, the result would be that the gap in total demand created by the disappearance of expansion demand in Department I would be made up by an increase in consumption demand on the one hand and an increase in expansion demand in Department II on the other (Sweezy in Horowitz, p. 320).

The hypothetical adjustment envisaged by Sweezy is exactly Kaldor's 1956 for whom "... a fall in investment, and thus in total demand, causes a fall in prices (relatively to the wage level) and thereby generates a compensating rise in real consumption. Assuming flexible prices (or rather flexible profit margins), the system is thus stable at full employment"²⁴. Yet this is precisely the mechanism rejected by both Kalecki and Sweezy. In the words of the latter:

But it is certainly impossible today to maintain that the capitalist price system works this way. [...] In other words, there is no reason to suppose that the approach of the end of the period industrialization would set in motion a mechanism accelerating the growth of consumption at the expense of accumulation and thus taking up the slack which the disappearance of expansion demand in Department I would otherwise cause (Sweezy, *ibid.*).

In defence of Kaldor, but not of Weintraub who keeps the markup steady and blames inflation on workers' appetite, one could argue that the stability of full employment is arrived at by assuming that investment is at full employment in the first place. But in the *Economica* 1959 paper on growth and inflation the mechanism works also in the neighbourhood of full employment and, importantly, the economy is brought to gravitate around it by endogenous forces impacting upon the average saving ratio. Thus contrary to Kaldor's claims it is savings that end up determining investment.

It can be useful at this point to inquire about how can investment be fixed at full employment remembering that profits are determined by the level of investment and, if capitalists do not consume, they are equal to it. If full employment requires a long term decline of the ratio of the capital to the consumption goods sector it would entail a fall in the share of profits. This will run against capitalists' perception of a stable investment environment: It will therefore be as difficult to reduce investment to its full employment level as much as it is difficult to systematically raise it in developing economies. The stability and, possibly, the upward movement of the value of profits over the value of output is one of the main features of the capitalist enterprise as it also influences the financial evaluation of the companies. Thus if investment is to be adjusted downward it will be done not in relation to full employment requirements but in relation to market realities at the ruling share of profits. The problem cannot be solved by State intervention either, unless the said intervention sterilises itself. Assume that the state intervenes in order to guarantee the adjustment described by Sweezy. It purchases the machines at a given price, as not to upset capitalists' expectations about returns, and sets up new plants in the consumption goods sectors. This step would most likely be seen as encroaching upon the sphere of private capital in production, as well as reducing

²⁴ Nicholas Kaldor, "Alternative Theories of Distribution", *Review of Economic Studies*, Volume 23, No. 2, 1955-56, p. 95.

the mark up in the consumption goods sector at the expense of private profit margins. The reasonable solution can only be that suggested by James Meade when analysing the relation between machines and a growth rate exceeding the full employment one²⁵:

In the latter case, it will, of course, be very difficult to prevent a general slump in economic activity; for it will be difficult with existing machinery idle or used below capacity to maintain the incentives to invest in new additional machinery on a scale necessary to make use of all the savings (..) forthcoming from the national income if it is maintained at its full employment level. The economy will thus be prone to lapse into a stagnant state in which neither machinery nor men are fully employed.

Thus, unless one believes in the virtues of price flexibility in relation to wage costs, it is up to the government to avoid stagnation:

For example, the government may have a public-works policy whereby it borrows the excess savings to spend on the excess supply of machines in order to hold them off the private market. The remainder of the output of new machines would no longer be in excess of the amount needed to match the growing labour force.

The rate of accumulation and the level of profits would be thus safeguarded by mopping up unwanted capital equipment. But for how long can this financial arrangement continue? Pretty soon corporations will realise that they are producing unwanted machinery stored up by the government which is also compelled to increase its debt relatively to total output. Thus in the course of time capitalists' consensus towards this sort of policies will breakdown. We are once more back to Sweezy's observation according to which when industrialization is completed its fruits tend to be dissipated in unemployment and stagnation.

Some contemporary Post-Keynesians following up from the Kaldor-Weintraub tradition claim that it is possible to ensure a stable investment environment at full employment by means of traditional government expenditure and with wage controls addressing the issue of inflation²⁶. But if we think in terms of stages of development and thereby view the advanced capitalist world as possessing a level of productive capacity which, if fully utilised, can employ the whole – and even more – of the able bodied population, the structural problem at full capacity is not inflation but the immanent tendency towards over accumulation. Inflation can, in this context, be seen as the corporate resistance to the decline in profits which would be indeed required to maintain full employment.

This is in fact how Kalecki viewed the role of the class struggle in the short run. If capitalists' power is very strong, corporations will transfer higher wages onto

²⁵ **A neo-classical theory of economic growth/ James Meade.** *Publisher* London: George Allen and Unwin, 1962, pp. 47-48 footnote.

²⁶ Philip Arestis, Malcolm Sawyer, *Keynesian Economic Policies for the New Millennium.* [Journal Article] *Economic Journal*. Vol. 108 (446). p 181-95. January 1998.

prices. Thus in France in 1936-38 to the political power of the labour movement expressed by the *Front Populaire* did not correspond an equal economic power since the increase in wages had been reabsorbed by an equal increase in prices²⁷. In the post war period, due to the crucial reform, which brought about a high level of employment, workers can wage an offensive struggle by breaking through the inflationary resistance of capitalists. Under oligopolistic conditions unused capacity is the norm. If the function determining the mark up is unchangeable any variation in costs will be reflected in price changes. But this function may depend on international competition as well as on trade union's activity. Since oligopolies extend well beyond national boundaries, the real break to tendentially rising mark-ups can come mainly from the trade unions. If successful, wage struggles increase the level of employment by increasing the rate of capacity utilisation, without a major impact on the level of profits. Only their distribution will change substantially towards the consumption goods sector. Of course at full capacity the functions determining the mark up cease to operate. Yet for Kalecki this is a very remote possibility under capitalism²⁸.

If Trade Unions manage to break through capitalists' inflationary barrier up to the level of full capacity, the issue will not be that of inflation but that of directing the allocation of the surplus. The more industrially developed is the system the more the very essence of the capitalist economy will be called into question. To quote Sweezy again:

As near as anything can be, profit is the be-all and end-all of capitalist society. It follows that when the economic functioning of capitalism calls for a drastic and steady decline in profit and/or a use of profit which runs directly counter to the will of the capitalists, the system is caught in a very real contradiction.

Capitalism may be temporarily rescued from the contradiction by new industries; it may seek with more or less success an escape through imperialism and militarism; it may even undertake, again with more or less and certainly against the growing resistance of the capitalists themselves, to modify the functioning of the system through taxation and government spending. But one thing is certain: as long as it remains capitalism, it can never abolish the contradiction (Sweezy in Horowitz, p. 324).

4 Some conclusions

Kalecki thought that the 'crucial reform' implemented by post war capitalism would last longer than it did, although in the late 1960s *Monthly Review's* articles were pointing to a systematic reappearance of the tendency towards stagnation, to day well recognised²⁹. Unlike Kaldor and Cornwall conceptions

²⁷ Michal Kalecki, "The Lessons of the Blum Experiment", *The Economic Journal*, Vol. 48, No. 189. (Mar., 1938), pp. 26-41.

²⁸ Michal Kalecki, "Class Struggle and Distribution of National Income", *Kyklos*, Vol. 24, No.1, 1971, pp. 1-9.

of *democratic capitalism* the ‘crucial reform’ had little to do with the virtues of Socialdemocracy. It was rather based on the connection between government expenditure which ensured a high level of employment and the rise of wages along with productivity which allowed workers’ incomes to rise. One of the reasons why Kalecki viewed the crucial reform as unsatisfactory is that it was linked to imperialism and to a monopolistic control of the means of communications by big business³⁰. These elements explain why he was sympathetic to the 1968-69 students’ movement in Western Europe. He considered the students as a factor that would break the rules of the game and would rekindle the challenge to capitalist power in the advanced countries.

It follows that, even without going into the issue of financial instability which comes on top of the structural aspects discussed earlier, those who want to advocate Post-Keynesian policies to day, would have to assess whether a new crucial reform is possible. Prior to this they will have to make their views clear in relation to the way they see the evolution of capitalism from, say, 1945 to 1971. Do they see it in Kaldor-Cornwall terms or in Kalecki-Sweezy-Magdoff terms? If they see it in Kaldor-Cornwall eyes than all that is needed to restore Socialdemocratic capitalism is a ‘tax and spend’ policy with an eye on wages to prevent inflation, and with some budget deficits to push the system along coupled with the implementation of Paul Davidson’s proposal for a new international monetary system.

The Kaldor-Cornwall approach is based on the idea of a benevolent state and on the related absence of imperialism as a crucial feature of present day capitalism³¹. In essence, however, the neo-liberal characteristics of the capitalist states never faded. The history of the welfare state is turning out to be just an episode dictated by the Great Fear – to borrow a term used for the conditions leading to the French Revolution – raised by anti imperialist national liberation movements, the existence of the USSR and of the People’s republic of China and, in the United States, by the radicalism of the workers during the Depression.

The excellent historical scholarship which has been coming out of the United States in the last two decades confirms and enriches the Kalecki-*Monthly Review* analysis according to which imperialism and military expenditures

²⁹ **The dynamics of U.S. capitalism: corporate structure, inflation, credit, gold, and the dollar [compiled] by Paul M. Sweezy and Harry Magdoff.** Publisher New York [Monthly Review Press, 1972]. See also Harold G. Vatter,; John F Walker, Gar Alperovitz, *The Onset and Persistence of Secular Stagnation in the U.S. Economy: 1910-1990*, *Journal of Economic Issues*. Vol. 29 (2). p 591-600. June 1995

³⁰ In the post-war period Kalecki treated imperialism in a Kautsky rather than in a Leninist sense. He did not considered interimperialist wars to be possible any longer.

³¹ Moreover this approach trivializes the notion of democracy which many authors found at odds with the expansion of capitalism. See **Democratic theory : essays in retrieval / C. B. Macpherson.** Publisher Oxford : Clarendon Press, 1973; **Democracy against capitalism : renewing historical materialism / Ellen Meiksins Wood.** Publisher Cambridge : Cambridge University Press, 1995.

were the pillars of post 1945 capitalism³². This is particularly true for the post war history of Japan and of East and South-East Asia which have constituted the truly new geographical frontiers of 'successful' capitalist expansion. It is remarkable how in this area there is very little Post-Keynesian scholarship³³. Surely this must be linked to the neglect of historical analysis. But also on Europe there are major misgivings. The Kaldorian based infatuation with neocorporatist regimes of industrial relations misses their historically specific nature and fails to explain why they weakened so much, especially in relation to Germany. Moreover the identification of French indicative planning with Keynesian policies, also a Kaldor generated myth, is positively misleading and historically wrong. It misses the unifying role played by financial capital, and therefore sound finance policies, in the consolidation, strengthening and grip on power of France's capitalist classes so well epitomised by the role of Jacques Rueff from the *Front Populaire* to the de Gaulle regime³⁴.

The issue of the State and its class characteristics seems therefore to be the weakest link in the post-Kaldorian literature. This factor leads to the mythology of the actual possibility, under present day capitalism, of a return to full employment and to an endless (post) Keynesian welfare state. The narrowness of this view has been recently highlighted by Harry Magdoff with the following words³⁵:

If the belief isn't engraved at the conscious level, it is well preserved at the unconscious. Reform proposals by progressives tend to seek ways to reestablish a Keynesian "harmony," when what we should be working for are changes that challenge capitalism and the ideology of the market system. The educators among us have a huge educating job ahead; to explain why challenging capitalism at every opportunity is in the best interest of the working classes of the world.

³² **Altered states : the United States and Japan since the occupation / Michael Schaller.** Publisher New York : Oxford University Press, 1997; **The Pacific alliance : United States foreign economic policy and Japanese trade recovery, 1947-1955 / William S. Borden.** Publisher Madison, Wis. : University of Wisconsin Press, 1984

³³ See however: Peter Kriesler, Joseph Halevi, "Asia, Japan and the Internationalization of Effective Demand", *Economies et Societes. Vol. 30 (2-3). p 301-20. Feb.-March 1996*; Joseph Halevi, Peter Kriesler, "History, Politics and Effective Demand in Asia" in Joseph Halevi and Jean-Marc Fontaine eds, *Restoring demand in the world economy: Trade, finance and technology*, Cheltenham, U.K. and Northampton, Mass.: Elgar; pp. 77-92. 1998.

³⁴ Alain Parguez., "The Roots of Austerity in France", *Restoring demand in the world economy: Trade, finance and technology.* Joseph Halevi, Jean-Marc Fontaine, eds., Cheltenham, U.K. and Northampton, Mass.: Elgar; distributed by American International Distribution Corporation, Williston, Vt. p 182-96. 1998.

³⁵ Harry Magdoff., "The same old state", *Monthly Review*, Jan 1998 v49 n8 p. 1-10

APPENDIX

I believe that Marx was the most scientific of all the economists who wanted to tell a long run story – that he thought to be historically accurate - of how the system evolves. *Das Kapital* Volume One transforms – via Ricardo – class relations into a set of economic laws of motion. Behind every economic category there is a specific class: behind profits there is the capitalist class and behind wages there is the working class. The power relations between these two classes are contained in the process of value formation since part of the labour time bestowed in production is surrendered free as surplus value to the owners of capital.

Marx's theory of accumulation of Volume One variety aims at telling a scientifically objective story about historical tendencies of accumulation combining the short run with the long run. The short run side of it is the famous cyclical process of growth based on the Reserve Army of Labour. Here the classical inverse relations between the wage rate and the rate of profit does wonders as the fall in accumulation resulting from a dwindling Reserve Army brings down the rate of profit. The typical capitalist is deemed to operate under competition which means that the capitalist is forced by the very process of competition "to constantly expand his capital, but expand it he cannot except by means of progressive accumulation"(Capital, Volume One page 555). It is indeed competition which compels the capitalist firm to invest every single penny left over after deducting wage payments. Notice that this logic requires that prior savings finance investment exactly like in Ricardo's theory. The competitive drive, in which Kaldor the Post Keynesian believed so much, prevents the capitalist from developing a mark up policy both for the defence of monetary profits and of accumulation strategies. When, at the founding meeting of the First International in London, citizen Weston (the first Kaleckian ante litteram) tried to argue that indeed capitalists do have power over prices, Marx strongly criticized him arguing that prices are unambiguously set by the labour theory of value, and wages by the relative pace of accumulation. The pace of accumulation determines the variation in the rate of employment relatively to the available work-force and this will determine whether the wage rate will rise or not relatively to the rate of profit. The crisis becomes therefore the positive solution to the profit squeeze induced by a too high rate of accumulation which engendered a rise in wages relatively to the rate of profit. Capitalists defend themselves not through prices but by means of technical innovations (assumed to be capital augmenting) and those who can't will go bust. The low level of accumulation coupled with technological restructuring will generate unemployment to which we must add the unemployed coming from the firms who went bust. At last the Reserve Army of Labour is endogenously replenished! Unemployment will rise, the wage rate will fall so that rate of profit will rise as a consequence. Since the rate of profit governs the rate of accumulation we immediately know that the share and the rate of investment will rise and with it the growth rate. The crisis is indeed the solution to the impasse of a previously too high rate of accumulation since it allows accumulation to recover on an expanded technical basis. This process could go on indefinitely were it not for long run rise of the organic composition of capital brought about by the very restructuring undertaken at each turning point of the cycle.

Marx viewed the above theory not in terms of a model but as actually explaining reality. It all depends on savings (profits) preceding investment under conditions of classical competition. If it were possible to ascertain that these two conditions were met during the period that Marx studied we could argue that Marx's trade cycle represented a specifically identifiable phase in the history of capitalism: that of competitive accumulation. But we can't ascertain anything of this sort. We can only speculate without even being able to draw upon circumstantial evidence. Certainly, in relation to competition we would be hard put to argue for a relatively long phase of price competitive processes. In the first decade of the 20th century one German historian, Hermann Levy³⁶, perhaps the father of the monopoly capital version of industrialisation, actually maintained that competition is nothing but a brief transition period between phases of monopolistic dominance. Furthermore present day historical studies on the Gold Standard and British imperialism show in a rather convincing manner that Britain was steadily building within its empire a monopolistic zone for the commerce of its manufactured products³⁷. List himself viewed the act which led Ricardo to rationalise competitive trade between Portugal and Britain as an expression of non competitive relations. In Marx's economics the idea of competition is as important as the notion of labour value based exploitation. It is competition that compels capitalists to strive to make profits (savings) and to invest them. It is competition that enables capitalism to expand endogenously following precisely defined laws. Without competition capitalists may become so in spite of themselves, for reasons not uniquely related to the endogenous forces of accumulation. Hence the capitalist system may be built from above rather than from endogenous economic impulses.³⁸

From a conceptual point of view the creation of internal savings can happen only if the society is small and based on consumption so that savings are made in order to obtain greater consumption in a precisely known future. Normally a Ramsey saver is considered to be a single family unit of farmers deciding how much corn to eat and how much to set aside for the next harvest and therefore for future consumption. In a small society every family of farmers knows exactly what the others produce and knows that the labouring activities are geared mainly to self consumption. Here savings will take a Ramsey form. These kind of savings do not involve any money. But the Ricardo-Marx savings are supposed to involve money in a context of capitalist production where producers do not know each other nor do they really care about what specific commodities are being produced. Yet Marx's Ricardian based theory of cyclical accumulation works best when it is in a money-less system and especially when such a system is formed by one

³⁶ **Monopoly and competition : a study in English industrial organisation / Hermann Levy.**
Publisher London : Macmillan, 1911.

³⁷ **Money and empire : the international gold standard, 1890-1914 / Marcello de Cecco.**
Publisher Oxford : B. Blackwell, c1974.

³⁸ **Capitalism from above and capitalism from below : an essay in comparative political economy / Terence J. Byres.** *Publisher* Houndmills, Basingstoke, Hampshire : Macmillan Press ; New York : St. Martin's Press, 1996.

Capitalists in spite of themselves : elite conflict and economic transitions in early modern Europe / Richard Lachmann. *Publisher* New York : Oxford University Press, 2000.

multipurpose commodity, corn. The Marx-Ricardo capitalists behave in an opposite but comparable way to the Ramsey savers as they attempt to withhold from consumption the largest possible amount of corn (profit = saving) in order to plough it back (invest) into production. Marx's laws of motion tell us that, under free competition, capitalists operate under a tight restriction which prevents them from always raising the share of corn withheld from consumption. Whenever the rate of ploughing back exceeds the rate at which capitalists can find workers to undertake the job, wages will rise engendering the profit and investment squeeze outlined earlier.

The emergence of the Ricardo-Marx mechanism of savings and investment as just the dual of Ramsey's intertemporal consumption decision, highlights the essentially non monetary single-sector nature of the basic approach to accumulation put forward by the Classical economists. It was Marx himself who unwittingly criticised his own views few pages before he presented them in chapter 25 of Volume One of *Capital*. In chapter 15 of Volume One, the famous chapter on machinery, he attacked the theory of compensation according to which workers displaced by innovations would be reabsorbed elsewhere in the economy. In response Marx constructed an example of carpet weavers replaced by mechanical looms. He then argued that once fired the carpet makers would no longer face the capitalists as labour costs, but only as defective consumers since the loss of their wages would reduce the demand for commodities. It is not difficult to see that Marx could make this point because he treated wages in money terms and considered consumption goods in relation to their specifically sectoral characteristics as use values not fitted for accumulation. Now in terms of effective demand for consumption goods, the decline in wage rates due to the rise of the Reserve Army of Labour has the same implications derived from the firing of carpet weavers. But in chapter 25 Marx, in building his macroeconomic theory of cyclical growth – which he calls *the law of capitalist accumulation* – relied on the Ricardian approach of a single sector corn economy, although couched in terms of the labour theory of value, where corn savings precede and determine corn investment. It is because of this special case that Marx could map out a set of laws on growth, cycles and crisis.

The political economy of class relations emerging from Marx's approach is quite stringent: workers' lives will be subjected to ever growing cycles until the falling rate of profit catches up with the cyclical process thereby unleashing a structural crisis. Thus workers have very little reason to stand by the system of exploitation and accumulation. Nowadays very few people would maintain that the falling rate of profit theory is valid in historical time given its logical problems and given that it was conceived on the basis of a competitive process. Yet some authors continue to use the profit squeeze approach in order to explain the breakdown of the long boom while the ensuing unemployment is seen as the essential aspect of the recovery in the rate of profit and in accumulation³⁹. To state this causal linkage those neo-post-Marxist authors have to treat the economy as a single homogeneous whole and have to exclude by assumption the negative impact of unemployment on the demand for

³⁹ **Capitalism since 1945 / Philip Armstrong, Andrew Glyn, John Harrison.** *Publisher* Oxford, UK ; Cambridge, Mass. : Basil Blackwell, 1991; **The economics of the profit rate : competition, crises, and historical tendencies in capitalism / Gérard Duménil and Dominique Lévy.** *Publisher* Aldershot, Hants, England ; Brookfield, Vt. : Edward Elgar, 1993.

commodities as well as the negative consequences, in terms of profits, of such an event for the investment sectors servicing the affected consumption goods industries. Moreover, as pointed out in splendid critique of Duménil and Lévy by Carlo Benetti and Jean Cartelier⁴⁰, the insurmountable problems encountered in the construction of such an aggregate approach are similar to those found in traditional theory whenever it attempts to generalise its concepts to the system as a whole.

In Marx's own framework where the dynamic process is regulated by competition between capitals, involving heavy fluctuations in prices, the business cycle cum technical change, highlighted the permanent subaltern position of wage labour. But to day this position is not acceptable. Structural linkages are far more complex than thought during classical times so that the competitive process, even if it exists, is one of many other processes taking place alongside it. As a consequence to argue that a fall in wages is an indication of the restoration of accumulation and profitability is profoundly misleading.

⁴⁰ **Benetti, Carlo; Cartelier, Jean.** “Une dynamique économique sans théorie?” (With English summary.). [Journal Article] *Recherches Economiques de Louvain*. Vol. 61 (3). p 289-300. 1995.